

TransDigm Group Inc. (TDG)

\$498.79 (As of 08/14/20)

Price Target (6-12 Months): **\$529.00**

Long Term: 6-12 Months

Zacks Recommendation:
Neutral

(Since: 07/06/20)

Prior Recommendation: Underperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

3-Hold

Zacks Style Scores:

VGM:D

Value: D

Growth: C

Momentum: C

Summary

TransDigm's third-quarter fiscal 2020 earnings and revenues surpassed the respective Zacks Consensus Estimate. However, results were unimpressive on a year-over-year basis, following the setback that the commercial aerospace market suffered courtesy of the coronavirus impacts. Nevertheless, the company has been enjoying significant growth opportunities in the defense space on account of the expansionary budgetary policy adopted by the U.S. administration and other developing nations in the past couple of years. Moreover, in a year's time, its shares have outperformed the industry. However, the company expects its near-term operational results to consistently suffer as the COVID-19 pandemic will continue to adversely impact customer demand for all market channels, with commercial OEM and commercial aftermarket being the most affected.

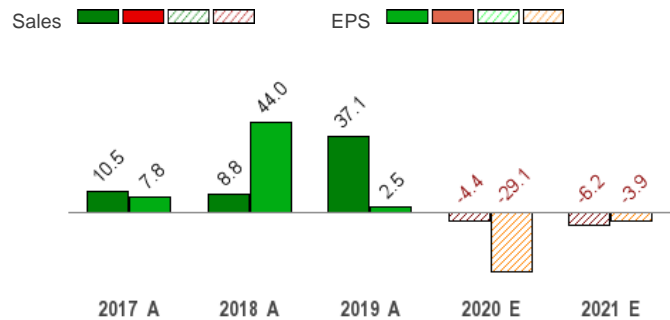
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$673.51 - \$200.06
20 Day Average Volume (sh)	401,604
Market Cap	\$27.0 B
YTD Price Change	-10.9%
Beta	1.42
Dividend / Div Yld	\$0.00 / 0.0%
Industry	Aerospace - Defense Equipment
Zacks Industry Rank	Bottom 15% (214 out of 252)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	55.6%
Last Sales Surprise	1.5%
EPS F1 Est- 4 week change	6.0%
Expected Report Date	NA
Earnings ESP	0.6%
P/E TTM	29.0
P/E F1	38.5
PEG F1	3.3
P/S TTM	4.9

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	1,029 E	1,085 E	1,138 E	1,227 E	4,682 E
2020	1,465 A	1,443 A	1,022 A	1,102 E	4,993 E
2019	993 A	1,196 A	1,658 A	1,541 A	5,223 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$1.75 E	\$2.59 E	\$2.73 E	\$3.51 E	\$12.45 E
2020	\$4.93 A	\$5.10 A	\$1.54 A	\$1.87 E	\$12.95 E
2019	\$3.85 A	\$4.21 A	\$4.95 A	\$5.62 A	\$18.27 A

*Quarterly figures may not add up to annual.

The data in the charts and tables, including the Zacks Consensus EPS and Sales estimates, is as of 08/14/2020. The reports text is as of 08/17/2020.

Overview

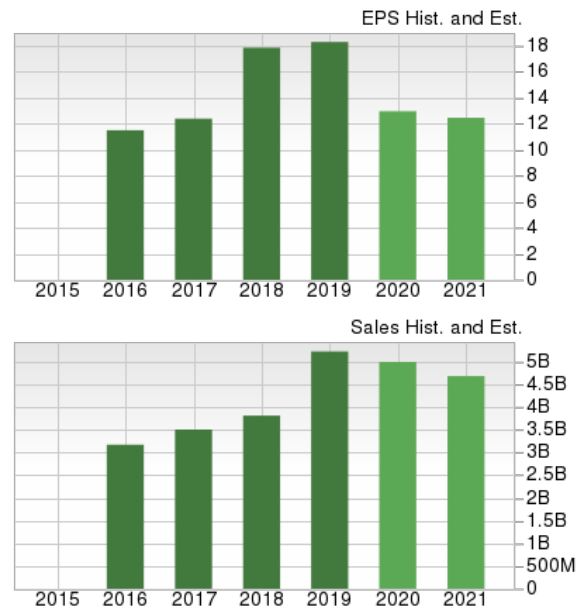
Incepted in 1993, TransDigm is a leading global designer, producer and supplier of highly engineered aerospace components that are used in commercial and military aircraft. The company, through its well-diversified business, offers a broad range of products to its customers. TransDigm currently has four reportable segments:

Airframe: This segment produces systems and components like engineered latching and locking devices, security components and systems, aircraft audio systems, specialized lavatory components, seat belts and safety restraints, engineered interior surfaces and related components, military personnel parachutes and cargo delivery systems. These are used in non-power airframe applications utilizing airframe and cabin structure technologies. It contributed 44.6% to the company's total sales in fiscal 2019.

Power & Control: This segment develops products like mechanical/electro-mechanical actuators and controls, ignition systems and engine technology, specialized pumps and valves, power conditioning devices, specialized AC/DC electric motors and generators, and lifting devices and cargo loading and handling systems. These are used in controlling power of the aircraft utilizing electronic, fluid, power and mechanical motion control technologies. It contributed 52.4% to the company's total sales in fiscal 2019.

Non-aviation: This segment's products include seat belts and safety restraints for ground transportation applications, mechanical/electro-mechanical actuators and controls for space applications, and refueling systems for heavy equipment used in mining, construction and other industries. It contributed 3% to the company's total sales in fiscal 2019.

Esterline: Esterline Technologies became a reportable segment of TransDigm, post its acquisition in March 2019. Notably, Esterline includes a collection of approximately 20 reporting units that primarily develop, produce and market products for the aerospace and defense industry. However, the company is yet to include this segment in its core business.



Reasons To Buy:

- ▲ TransDigm's products holds a significant position in the U.S. defense aerospace market. To this end it is imperative to mention that the company has been enjoying significant growth opportunities in the defense space on account of the expansionary budgetary policy adopted by the U.S. administration as well as other developing nations in past couple of years. For instance, the U.S. fiscal 2021 defense budget includes a massive spending plan of \$57 billion for aircraft. This should enable Boeing and other military aircraft producers to acquire significant defense contracts from the Pentagon, which in turn, should benefit equipment suppliers like Transdigm. Backed by the higher-than-expected defense sales growth in fiscal 2019, management continue to project its fiscal 2020 defense revenues to grow in the mid-single-digit figure compared with the previous year.
- ▲ While TransDigm suffered a setback in the commercial aerospace market, courtesy of the COVID-19 pandemic, the company took the opportunity to explore new business opportunities by working on developing highly engineered solutions for emerging needs such as antiviral, antimicrobial technology, air purification and touchless technologies. This in turn should expand the company's footprint across the board. Moreover, to tackle the reduced demand and uncertainty resulting from the pandemic, TransDigm decided to reduce its total workforce by 30%, which is in addition to its earlier announced mitigation efforts in response to the 737 MAX production rate changes. Such initiatives are expected to boost TransDigm's growth prospects in the long term.
- ▲ Transdigm had a long-term debt of \$19,410 million as of Jun 30, 2020, which moved up from \$17,993 million as of Mar 31, 2020. The company's current debt stands at \$629 million as of Jun 30, 2020, flat sequentially. As of Jun 30, 2020, its cash equivalents were \$4,549 million, which increased sequentially from \$2,668 million. So its cash balance is lower than its long-term debt, but lies much above its current debt value. This indicates a strong solvency position, for the company at least in the near term.

Improved cash balance reflects a solid solvency position for TransDigm. Expansionary defense budget will aid its defense business.

Moreover, the company's current ratio of 4.1, improved sequentially from 3.1. Also, this ratio being more than 1 suggests that the company has the ability to pay off its debt obligation in the near term. Such impressive financial ratio must have enabled the company to outperform its industry in the past year. Evidently, in a year's time shares of the company have declined 7.2% compared with its industry's 35% plunge.

Reasons To Sell:

- ▼ The coronavirus pandemic hit the commercial aerospace market the most along with the aftermarket industry. To this end, it is imperative to mention that TransDigm's results for the third quarter of fiscal 2020 were adversely impacted, led by the COVID-19 effects. Notably, its fiscal third quarter commercial OEM sales decreased 41.6% year over year and commercial aftermarket sales declined 52.1%. While the pandemic was the primary growth inhibitor for commercial OEM sales, 737 Max production stoppage also resulted in its decline. The company expects its operational results to suffer in the remainder of fiscal 2020, under the assumption that the COVID-19 pandemic will continue to adversely impact customer demand in all market channels, with commercial OEM and commercial aftermarket being the most affected due to the pandemic's impact on air travel worldwide.
- ▼ Although the company has outperformed its industry in the past year, a comparative analysis of its historical P/E ratio reflects a relatively gloomy picture that might be a cause for investors' concern. The stock currently has a trailing 12-month P/E ratio of 31.06. This level compares unfavorably with what the stock saw in the past 12 months and is near the higher end of its one-year range of 35.26. The ratio is also higher than the industry's average of 16.68.
- ▼ Global revenue passenger miles are still at unprecedented lows, as a result of the pandemic. Per International Air Transport Association's (IATA) latest forecast a 63% decrease in revenue passenger miles is expected in calendar year 2020 from 2019. On the other hand, the outlook for business jets remains unpredictable as business jet flights are rebounding, thanks to personal and leisure travel as opposed to business travel. The sustainability of this trend is thus difficult to foresee. So, the future of the industry is mired in uncertainty, thereby offering no chance for TransDigm's commercial business to make any rebound, at least in the next few months.

Adverse impacts of coronavirus has been hurting TransDigm's operating results. Unfavorable outlook for commercial aerospace market raises concern for the stock

Last Earnings Report

TransDigm Q3 Earnings Beat Estimates, Sales Fall Y/Y

TransDigm Group reported third-quarter fiscal 2020 adjusted earnings of \$1.54 per share, which surpassed the Zacks Consensus Estimate of 99 cents by 55.6%. However, the bottom line decreased 66.9% from \$4.65 reported in the year-ago quarter.

Barring one-time items, the company reported GAAP loss of 9 cents per share against earnings of \$2.27 in the year-ago quarter.

The year-over-year deterioration can be attributed to a decline in net sales, along with COVID-19 restructuring costs, higher interest expense and a higher tax rate due to discrete one-time tax charges being taken during the quarter.

Sales

Net sales amounted to \$1,022 million, reflecting a decline of 32.8% from \$1,521 million in the prior-year quarter. The reported figure however outpaced the Zacks Consensus Estimate of \$1,007 million by 1.5%. Meanwhile, organic sales declined 9.6%.

Operating Results

The company incurred net loss of \$5 million from continuing operations in the quarter against income of \$128 million in the comparable quarter a year ago.

The effective tax rate was 113.5% compared with 30% in the comparable period in fiscal 2019. The deterioration was due to the unfavorable economic impact of the COVID-19 pandemic on the company's net interest deduction limitation and a discrete cumulative adjustment associated with excess tax benefits from share-based payments.

Financial Position

TransDigm ended the third quarter of fiscal 2020 with cash and cash equivalents of \$4,549 million, up from \$1,467 million as of Sep 30, 2019. At the end of the reported quarter, the company's long-term debt was \$19.41 billion, up from \$16.47 billion as of Sep 30, 2019.

Cash from operating activities amounted to \$991 million as of Jun 27, 2020 compared with \$768 million as of Jun 29, 2019.

Fiscal 2020 Outlook

Given the considerable uncertainty around the extent and duration of business disruptions related to the COVID-19 pandemic and how it will impact operations, TransDigm kept its previously provided fiscal 2020 guidance suspended.

Quarter Ending 06/2020

Report Date	Aug 04, 2020
Sales Surprise	1.51%
EPS Surprise	55.56%
Quarterly EPS	1.54
Annual EPS (TTM)	17.19

Valuation

TransDigm Group's shares are down 10.9% in the year to date period and 7.2% over the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Aerospace sector are down 39.3% and 30.8% in the year to date period, respectively. Over the past year, the Zacks sub-industry is down 35% and the Zacks Aerospace sector witnessed a 31.1% decline.

The S&P 500 index is up 4.5% in the year to date period and 15.4% in the past year.

The stock is currently trading at 13.4X forward 12-month earnings, which compares to 21.9X for the Zacks sub-industry, 21.7X for the Zacks sector and 22.9X for the S&P 500 index.

Over the past five years, the stock has traded as high as 20.9X and as low as 8.3X, with a 5-year median of 15X. Our Neutral recommendation indicates that the stock will perform in line with the market. Our \$529 price target reflects 14.2X forward 12-month earnings.

The table below shows summary valuation data for TDG

Valuation Multiples - TDG					
		Stock	Sub-Industry	Sector	S&P 500
P/E F12M	Current	13.38	21.86	21.65	22.87
	5-Year High	20.91	22.54	21.65	22.87
	5-Year Low	8.25	14.52	14.17	15.25
	5-Year Median	15.04	17.76	17.29	17.58
P/S F12M	Current	5.73	1.46	1.73	3.7
	5-Year High	5.75	1.46	1.73	3.7
	5-Year Low	2.07	0.79	0.92	2.53
	5-Year Median	4.1	1.05	1.18	3.05
EV/EBITDA TTM	Current	17.55	9.82	16.77	17.4
	5-Year High	20.26	12.18	16.81	17.42
	5-Year Low	10.22	5.99	7.39	11.01
	5-Year Median	16.61	8.9	10.6	14.56

As of 08/14/2020

Industry Analysis Zacks Industry Rank: Bottom 15% (214 out of 252)



Top Peers

Company (Ticker)	Rec	Rank
Air Industries Group (AIRI)	Neutral	3
Aerojet Rocketdyne Holdings, Inc. (AJRD)	Neutral	3
Hexcel Corporation (HXL)	Neutral	4
Kratos Defense Security Solutions, Inc. (KTOS)	Neutral	3
Leidos Holdings, Inc. (LDOS)	Neutral	3
Teledyne Technologies Incorporated (TDY)	Neutral	2
Astronics Corporation (ATRO)	Underperform	4
Heico Corporation (HEI)	Underperform	4

Industry Comparison Industry: Aerospace - Defense Equipment				Industry Peers		
	TDG	X Industry	S&P 500	HEI	HXL	TDY
Zacks Recommendation (Long Term)	Neutral	-	-	Underperform	Neutral	Neutral
Zacks Rank (Short Term)	3	-	-	4	4	2
VGM Score	D	-	-	C	B	D
Market Cap	27.04 B	1.96 B	23.68 B	14.36 B	3.52 B	12.25 B
# of Analysts	4	4	14	4	5	1
Dividend Yield	0.00%	0.00%	1.68%	0.15%	0.00%	0.00%
Value Score	D	-	-	D	B	D
Cash/Price	0.18	0.15	0.07	0.03	0.08	0.03
EV/EBITDA	18.92	8.43	13.36	27.17	7.98	20.98
PEG Ratio	3.25	7.64	2.99	8.10	7.17	NA
Price/Book (P/B)	NA	2.45	3.22	7.60	2.45	4.25
Price/Cash Flow (P/CF)	19.61	8.03	12.82	35.88	7.98	23.94
P/E (F1)	38.52	28.08	22.06	51.36	40.42	34.07
Price/Sales (P/S)	4.94	1.36	2.51	7.01	1.71	3.87
Earnings Yield	2.60%	2.77%	4.30%	1.95%	2.46%	2.94%
Debt/Equity	-4.64	0.39	0.77	0.39	0.88	0.30
Cash Flow (\$/share)	25.44	2.26	6.94	2.97	5.29	13.88
Growth Score	C	-	-	A	B	C
Hist. EPS Growth (3-5 yrs)	17.48%	10.59%	10.41%	23.92%	8.21%	19.33%
Proj. EPS Growth (F1/F0)	-29.13%	-17.58%	-6.32%	-9.78%	-70.51%	-7.23%
Curr. Cash Flow Growth	24.18%	12.73%	5.20%	23.18%	12.73%	14.47%
Hist. Cash Flow Growth (3-5 yrs)	15.48%	5.32%	8.55%	20.26%	9.27%	11.00%
Current Ratio	4.10	2.71	1.33	4.39	3.86	1.97
Debt/Capital	NA%	33.12%	44.59%	33.12%	46.81%	23.05%
Net Margin	14.24%	4.46%	10.13%	17.78%	9.48%	12.59%
Return on Equity	-25.74%	8.92%	14.51%	20.70%	14.73%	14.45%
Sales/Assets	0.32	0.73	0.51	0.66	0.64	0.69
Proj. Sales Growth (F1/F0)	-7.34%	0.00%	-1.43%	-17.14%	-31.45%	-2.56%
Momentum Score	C	-	-	D	D	F
Daily Price Chg	0.74%	0.49%	0.12%	0.58%	1.39%	0.17%
1 Week Price Chg	10.15%	6.88%	2.30%	4.44%	9.28%	5.66%
4 Week Price Chg	15.60%	5.61%	4.41%	10.22%	-5.38%	2.86%
12 Week Price Chg	32.89%	14.46%	13.66%	14.46%	35.65%	-2.08%
52 Week Price Chg	-3.38%	-19.36%	5.80%	-24.54%	-47.57%	12.68%
20 Day Average Volume	401,604	146,629	1,984,154	304,569	818,707	209,802
(F1) EPS Est 1 week change	0.00%	0.00%	0.00%	-3.49%	-3.33%	0.00%
(F1) EPS Est 4 week change	6.01%	1.75%	2.08%	4.90%	-24.35%	4.46%
(F1) EPS Est 12 week change	6.01%	-0.34%	2.66%	-0.34%	-17.36%	4.46%
(Q1) EPS Est Mthly Chg	16.53%	0.00%	0.94%	-17.50%	-28.26%	0.00%

Zacks Stock Rating System

We offer two rating systems that take into account investors' holding horizons: Zacks Rank and Zacks Recommendation. Each provides valuable insights into the future profitability of the stock and can be used separately or in combination with each other depending on your investment style.

Zacks Recommendation

The Zacks Recommendation aims to predict performance over the next 6 to 12 months. The foundation for the quantitatively determined Zacks Recommendation is trends in the company's estimate revisions and earnings outlook. The Zacks Recommendation is broken down into 3 Levels; Outperform, Neutral and Underperform. Unlike many Wall Street firms, we have an excellent balance between the number of Outperform and Neutral recommendations. Our team of 70 analysts are fully versed in the benefits of earnings estimate revisions and how that is harnessed through the Zacks quantitative rating system. But we have given our analysts the ability to override the Zacks Recommendation for the 1200 stocks that they follow. The reason for the analyst over-rides is that there are often factors such as valuation, industry conditions and management effectiveness that a trained investment professional can spot better than a quantitative model.

Zacks Rank

The Zacks Rank is our short-term rating system that is most effective over the one- to three-month holding horizon. The underlying driver for the quantitatively-determined Zacks Rank is the same as the Zacks Recommendation, and reflects trends in earnings estimate revisions.

Zacks Style Scores

The Zacks Style Score is as a complementary indicator to the Zacks rating system, giving investors a way to focus on the highest rated stocks that best fit their own stock picking preferences.

Academic research has proven that stocks with the best Value, Growth and Momentum characteristics outperform the market. The Zacks Style Scores rate stocks on each of these individual styles and assigns a rating of A, B, C, D and F. We also produce the VGM Score (V for Value, G for Growth and M for Momentum), which combines the weighted average of the individual Style Scores into one score. This is perfectly suited for those who want their stocks to have the best scores across the board.

Value Score	D
Growth Score	C
Momentum Score	C
VGM Score	D

As an investor, you want to buy stocks with the highest probability of success. That means buying stocks with a Zacks Recommendation of Outperform, which also has a Style Score of an A or a B.

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