

TE Connectivity Ltd. (TEL)

\$85.35 (As of 03/02/20)

Price Target (6-12 Months): **\$90.00**

Long Term: 6-12 Months

Zacks Recommendation:

Neutral

(Since: 01/02/20)

Prior Recommendation: Underperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

2-Buy

Zacks Style Scores:

VGM:C

Value: C

Growth: C

Momentum: B

Summary

TE Connectivity is currently benefiting from solid momentum of its industrial solutions in the areas of aerospace, defense, marine and medical applications. Further, growing adoption of sensors in industrial and auto applications is a tailwind. Additionally, the company's expanding content in engineered solutions is a positive. We believe proper execution of TE Connectivity's strategic plans especially cost reduction initiatives in order to generate strong cash flow, is likely to continue aiding it in winning shareholders' confidence. Notably, the stock has outperformed the industry over a year. However, slowdown in the global auto-production is hurting its Transportation segment. Further, inventory destocking is an overhang for the company's Communications segment. Also, supply chain adjustments remain headwinds.

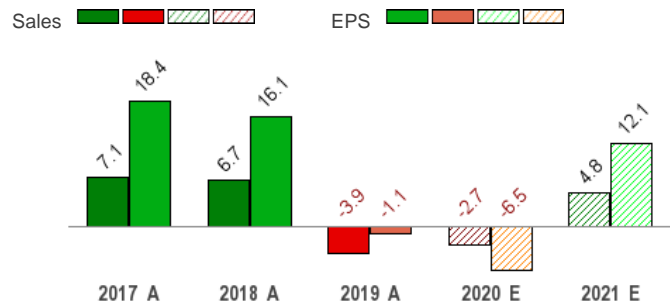
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$101.00 - \$78.83
20 Day Average Volume (sh)	1,735,535
Market Cap	\$28.5 B
YTD Price Change	-11.0%
Beta	1.17
Dividend / Div Yld	\$1.84 / 2.2%
Industry	Electronics - Miscellaneous Components
Zacks Industry Rank	Bottom 31% (175 out of 255)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	6.1%
Last Sales Surprise	1.7%
EPS F1 Est- 4 week change	0.0%
Expected Report Date	04/22/2020
Earnings ESP	0.8%
P/E TTM	15.6
P/E F1	16.5
PEG F1	1.6
P/S TTM	2.2

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	3,316 E	3,414 E	3,521 E	3,498 E	13,721 E
2020	3,168 A	3,217 E	3,346 E	3,363 E	13,089 E
2019	3,347 A	3,412 A	3,389 A	3,300 A	13,448 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$1.34 E	\$1.42 E	\$1.52 E	\$1.50 E	\$5.82 E
2020	\$1.21 A	\$1.25 E	\$1.36 E	\$1.37 E	\$5.19 E
2019	\$1.29 A	\$1.42 A	\$1.50 A	\$1.33 A	\$5.55 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 03/02/2020. The reports text is as of 03/03/2020.

Overview

TE Connectivity based in Schaffhausen, Switzerland, manufactures and designs products that connect and protect the flow of power and data inside millions of products used by consumers and industries. The company partners with customers in a broad array of industries ranging from consumer electronics, energy, and healthcare to automotive, aerospace and communication networks.

TE Connectivity reports under the following three segments –

Transportation Solutions (58.2% of total fiscal 2019 revenues): The segment caters to the needs of automotive, commercial transportation and sensors end markets. It offers sensor solutions and automotive connectivity solutions and products. Its electronic components comprising, connectors, wire and cable, circuit protection devices, heat shrink tubing and molded parts. It also provides application tooling and custom-engineered solutions for the aerospace, defense and marine markets.

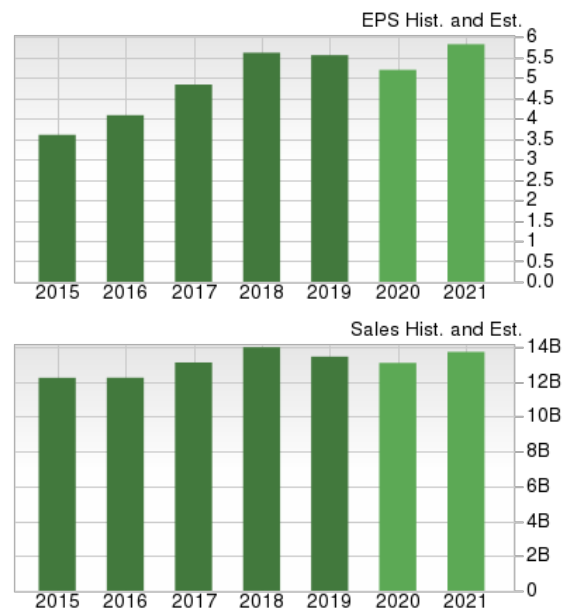
Industrial Solutions (29.4%): The segment caters to growing demand for the company's products in the end markets – industrial equipment, energy, and aerospace, defense, oil and gas. TE Connectivity supplies electronic components, including connectors, relays, circuit protection devices, antennas and heat shrink tubing for industrial machinery, consumer devices, data communications and household appliance markets. Further, it also offers intelligent building and rail products.

Communication Solutions (12.4%): The segment offers data and devices, appliances. Also, it is a leader in developing, manufacturing, installing, and maintaining some of the world's most advanced sub-sea fiber optic communications systems. This segment caters to demands of appliances, and data and devices end-markets.

Further, the company generates revenues by operating in three organized geographic regions – Europe/Middle East/Africa (EMEA), Asia-Pacific and Americas.

TE Connectivity had approximately 78,000 employees worldwide as of the end of fiscal year 2019. Out of this total employee strength, there were 25,000 employed in Americas, 22,000 in Asia-Pacific and 31,000 in EMEA region.

Notably, the company sells products via direct sales channels and third-party distributors in 150 countries.



Reasons To Buy:

- ▲ TE Connectivity's long-term growth strategy rests on three pillars — drives above market expansion through focus on harsh environment applications; leverage on "TEOA continuous improvement" system to expand margin and reduce fixed cost; and execute a balanced capital allocation strategy to conduct bolt-on acquisitions and return capital back shareholders— to stoke growth. Overall, strong demand in end markets, along with its overarching business model, continued progress on strategic priorities and solid execution continues to benefit TE Connectivity's sales.
- ▲ TE Connectivity is the market leader in the connectivity and sensor business, armed with a comprehensive portfolio. About 80% of TE Connectivity's revenues are driven by harsh environment applications. Over the past five years, the company's harsh business applications have had experienced mid-single digit growth, driving top-line growth. This apart, the sensor business is anticipated to see strong design win momentum, fuelled by the growth of automotive space and contribute significantly to the top-line growth of the company. Going forward, the company believes that this business will provide ample opportunities of margin expansion. In a nutshell, TE Connectivity expects its harsh-environment application business to perform well, mainly supported by secular trends like increased safety features, autonomous driving systems, higher emission standards and infotainment.
- ▲ TE Connectivity's Industrial business has ample room for growth. The company expects industrial solutions to grow on an organic basis, driven by the continued strength of industrial equipment and aerospace segments. In a bid to further focus more on gaining industrial leadership, the company has been continuously making efforts. It sold its subsea communications business (SubCom), which used to be sluggish since the last year. This will allow the company to focus more on its industrial pertaining solutions.

TE Connectivity's harsh-environment application business and industrial solutions are positives. Secular trends in autonomous driving systems and infotainment areas are tailwinds.

Reasons To Sell:

- ▼ The sluggishness in oil and gas markets and its derivative impact on industrial market will likely act as strong headwinds for TE Connectivity. Also, low prices in oil & gas are reducing sales in industrial equipment business as well as areas like factory equipments and rail. Helicopter demand has also been impacted negatively, which can prove to be a drag on the company's aerospace business. Also, a major portion of the company's net sales is invoiced in currencies other than the U.S. dollar and management expects non-U.S. dollar revenue to represent a significant and likely increased portion of future net revenue. Therefore, when the U.S. Dollar strengthens in relation to the currencies of the countries where TE Connectivity sells its products, the dollar reported revenue and income will decrease.
- ▼ As TE Connectivity operates in various economies globally, weak economic conditions considerably impact its revenues. Financial markets in certain foreign countries, especially in China, have been experiencing economic inconsistencies. Going forward, TE Connectivity believes that industrial, data & devices, and communications businesses will be heavily hit by the weakness in Chinese economy. Additionally, though TE Connectivity's ongoing restructuring and acquisition activities bode well for the long term, they tend to push up operating expenses and curb the quarterly results in the near term.
- ▼ TE Connectivity operates in a highly competitive market for electronic components and expects that both direct and indirect competition will increase in the future. Notably, the company faces stiff competition from Amphenol and Molex in all its reporting segments. The competition is across product lines from other companies ranging in size from large, diversified manufacturers to small, highly specialized manufacturers. In the recent times, the electronic components industry has become increasingly concentrated and globalized and the major competitors have significant financial resources and technological capabilities. A number of these competitors compete on the basis of price and in some cases enjoy lower production costs for certain products. Therefore, increased competition results in price reductions, reduced margins, or loss of market share, any of which has an adverse affect on the results of operations, financial position, and cash flows.

Sluggishness in oil and gas markets and its derivative impact on other industrial markets are acting as strong headwinds for TE Connectivity.

Last Earnings Report

TE Connectivity's Q1 Earnings & Revenues Beat Estimates

TE Connectivity reported first-quarter fiscal 2020 adjusted earnings of \$1.21 per share, beating the Zacks Consensus Estimate by 6.1%. Notably, the figure came well above management's guided range.

However, the bottom line declined 6.2% on a year-over-year basis and 9% sequentially.

Net sales in the reported quarter were \$3.2 billion, which surpassed the Zacks Consensus Estimate by 1.2%. Further, the figure came within the company's guided range. However, the figure declined 5.3% from the year-ago quarter and 4% from the prior quarter.

This can be attributed to weakness in the all the key end-markets, which impacted the performance of Transportation, Industrial and Communication segments during the reported quarter. Moreover, declining orders on year-over-year basis was an overhang.

Notably, the company's total orders came in at \$3.2 billion during the reported quarter.

Nevertheless, TE Connectivity witnessed 1% improvement in the total orders from the prior quarter. This indicates that the end markets are stabilizing.

Further, continued solid execution of the company's strategic plans especially cost reduction initiatives in order to generate strong cash flow, is likely to aid it in winning shareholders' confidence.

Top-Line in Detail

TE Connectivity operates in three organized segments.

Transportation Solutions: The company generated sales worth \$1.87 billion (58.9% of net sales) in the reported quarter, down 5.9% on a year-over-year basis. This can be attributed to weakness in auto production globally, which resulted in a year-over-year decline of 4% in automotive sales. Further, sluggishness in commercial transportation and industrial markets led to year-over-year decline of 7% in the company's sensor business.

Additionally, sales in its commercial transportation business was down 13% from the year-ago quarter due to sluggish performance in North America and Europe. Nevertheless, the business witnessed strong momentum in China during the reported quarter.

Industrial Solutions: This segment generated sales of \$927million (29.3% of net sales), which fell 0.1% year over year. This was primarily driven by inventory destocking, which led to year-over-year decline of 17% in the company's industrial equipment business.

Nevertheless, TE Connectivity experienced solid momentum in aerospace, defense and marine field where it witnessed year-over-year growth of 8%. Further, it saw an improvement of 7% in medical year over year owing to interventional medical applications. Additionally, the company witnessed 10% year over year growth in energy, courtesy of investments in renewable energy.

Communications Solutions: This segment generated sales of \$373 million (11.8% of net sales), declining 13.9% year over year. This can be attributed to inventory destocking, which resulted in a decline of 15% in data & devices and 13% in appliances solutions on a year-over-year basis.

Operating Details

Per the company, gross margin came in 32.5%, contracting 80 bps from the year-ago quarter.

We note that R&D expenses were \$161 million, which remained flat year over year. Further, selling, general, and administrative expenses came in at \$367 million, down 5.6% year over year. Further, restructuring costs decreased 68% from the year-ago quarter to \$24 million in the reported quarter.

However, acquisition and integration expenses totaled \$7 million, up 40% from the year-ago quarter.

Consequently, adjusted operating margin came in at 15.8%, contracting 110 bps from the prior-year quarter.

Balance Sheet & Cash Flow

As of Dec 27, 2019, TE Connectivity's cash and cash equivalents of \$742 million, lower than \$927 million as of Sep 27, 2019.

Long-term debt was \$3.41 billion, up from \$3.39 billion in the previous quarter.

The company generated \$411 million of cash from operation in the reported quarter, compared with \$878 million in the previous quarter.

Further, free cash flow of \$243 million was generated in the reported quarter. Additionally, TE Connectivity paid out \$297 million to shareholders through share repurchases and dividend payments.

Guidance

For fiscal second-quarter 2020, the company expects net sales in the range of \$3.1 billion to \$3.3 billion.

Quarter Ending **12/2019**

Report Date	Jan 29, 2020
Sales Surprise	1.74%
EPS Surprise	6.14%
Quarterly EPS	1.21
Annual EPS (TTM)	5.46

Adjusted earnings per share are projected in the band of \$1.22-\$1.28 for the fiscal second quarter.

For fiscal 2020, TE Connectivity has updated net sales guidance to \$12.85 billion-\$13.25 billion from \$12.7 billion-\$13.3 billion.

Further, adjusted earnings for fiscal 2020 are expected between \$4.95 and \$5.25 per share. The company has revised the lower end of the guided range upward from \$4.95.

Recent News

On **Nov 6, 2019**, TE Connectivity announced a quarterly dividend of 46 cents per share for the shareholders of the record as of Nov 22, 2019 which will be paid on Dec 6, 2019.

Valuation

TE Connectivity shares are down 6.2% in the past six-month period while the same are up 3% over the trailing 12-month period. While stocks in the Zacks sub-industry are down 1.1%, the same in the Zacks Computer & Technology sector are up 7.9% in the past six-month period. Over the past year, the Zacks sub-industry is down 2.4% while the sector is up 12.5%.

The S&P 500 index is up 5.5% in the past six-month period and 9.6% in the past year.

The stock is currently trading at 15.65X forward 12-month earnings, which compares to 19.17X for the Zacks sub-industry, 19.91X for the Zacks sector and 16.86X for the S&P 500 index.

Over the past five years, the stock has traded as high as 18.92X and as low as 12.1X, with a 5-year median of 15.67X. Our Neutral recommendation indicates that the stock will perform in-line with the market. Our \$90 price target reflects 16.51X forward 12-month earnings.

The table below shows summary valuation data for TEL

Valuation Multiples - TEL					
		Stock	Sub-Industry	Sector	S&P 500
P/E F 12M	Current	15.65	19.17	19.91	16.86
	5-Year High	18.92	21.69	22.04	19.34
	5-Year Low	12.1	13.76	16.87	15.18
	5-Year Median	15.67	16.88	19.33	17.44
P/S F12M	Current	2.14	1.73	3.34	3.12
	5-Year High	2.56	1.95	3.58	3.43
	5-Year Low	1.54	0.92	2.3	2.54
	5-Year Median	2.08	1.44	3.05	3.01
EV/EBITDA TTM	Current	10.38	9.11	11.27	10.93
	5-Year High	24.6	15.81	12.61	12.88
	5-Year Low	8.23	5.46	7.68	8.49
	5-Year Median	12.34	8.92	10.55	10.79

As of 03/02/2020

Industry Analysis Zacks Industry Rank: Bottom 31% (175 out of 255)



Top Peers

Applied Materials, Inc. (AMAT)	Outperform
STMicroelectronics N.V. (STM)	Outperform
Amphenol Corporation (APH)	Neutral
Broadcom Inc. (AVGO)	Neutral
Belden Inc (BDC)	Neutral
Honeywell International Inc. (HON)	Neutral
MACOM Technology Solutions Holdings, Inc. (MTSI)	Neutral
Eastman Chemical Company (EMN)	Underperform

Industry Comparison Industry: Electronics - Miscellaneous Components				Industry Peers		
	TEL Neutral	X Industry	S&P 500	AMAT Outperform	APH Neutral	MTSI Neutral
VGM Score	C	-	-	D	B	C
Market Cap	28.52 B	201.42 M	22.14 B	55.25 B	28.30 B	1.76 B
# of Analysts	9	2	13	10	8	7
Dividend Yield	2.16%	0.00%	1.98%	1.40%	1.05%	0.00%
Value Score	C	-	-	D	D	D
Cash/Price	0.03	0.13	0.05	0.07	0.03	0.13
EV/EBITDA	11.60	8.79	12.79	14.47	15.89	-8.00
PEG Ratio	1.60	1.75	1.92	1.46	2.44	NA
Price/Book (P/B)	2.70	1.82	3.00	6.38	6.12	6.00
Price/Cash Flow (P/CF)	11.13	11.84	11.97	17.16	19.25	25.74
P/E (F1)	16.45	18.24	17.43	14.53	24.55	57.23
Price/Sales (P/S)	2.15	1.17	2.48	3.68	3.44	3.76
Earnings Yield	6.08%	5.24%	5.74%	6.88%	4.08%	1.73%
Debt/Equity	0.32	0.19	0.70	0.54	0.70	2.33
Cash Flow (\$/share)	7.67	0.81	6.94	3.51	4.93	1.03
Growth Score	C	-	-	D	B	A
Hist. EPS Growth (3-5 yrs)	11.53%	14.68%	10.85%	35.63%	13.37%	-41.02%
Proj. EPS Growth (F1/F0)	-6.47%	8.57%	6.48%	36.22%	3.41%	260.10%
Curr. Cash Flow Growth	-2.61%	-2.61%	6.03%	-35.58%	-1.02%	-30.98%
Hist. Cash Flow Growth (3-5 yrs)	3.85%	10.07%	8.52%	13.90%	10.51%	-8.89%
Current Ratio	1.64	2.39	1.23	2.36	1.97	4.34
Debt/Capital	24.43%	16.57%	42.57%	35.25%	41.07%	69.99%
Net Margin	12.01%	5.27%	11.57%	18.83%	14.04%	-83.56%
Return on Equity	17.72%	9.06%	16.66%	36.15%	26.78%	-15.36%
Sales/Assets	0.67	0.87	0.54	0.79	0.78	0.39
Proj. Sales Growth (F1/F0)	-2.67%	0.00%	4.07%	19.87%	1.95%	1.53%
Momentum Score	B	-	-	D	A	C
Daily Price Chg	2.99%	0.03%	3.82%	3.51%	3.54%	5.14%
1 Week Price Chg	-9.66%	-8.17%	-12.06%	-9.57%	-9.90%	-15.23%
4 Week Price Chg	-9.20%	-6.67%	-6.43%	0.74%	-5.02%	-7.78%
12 Week Price Chg	-6.78%	-3.27%	-5.15%	6.29%	-9.12%	8.18%
52 Week Price Chg	2.94%	0.00%	4.77%	53.94%	0.49%	38.24%
20 Day Average Volume	1,735,535	43,521	2,363,047	9,685,970	1,511,231	428,014
(F1) EPS Est 1 week change	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
(F1) EPS Est 4 week change	0.04%	0.00%	-0.04%	9.72%	-0.06%	0.00%
(F1) EPS Est 12 week change	1.69%	-1.40%	-0.33%	9.72%	-3.45%	NA
(Q1) EPS Est Mthly Chg	0.11%	0.00%	-0.38%	11.19%	0.00%	0.00%

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	C
Growth Score	C
Momentum Score	B
VGM Score	C

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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