

The Timken Company (TKR)

\$46.43 (As of 07/06/20)

Price Target (6-12 Months): **\$38.00**

Long Term: 6-12 Months

Zacks Recommendation: Underperform

(Since: 07/05/20)

Prior Recommendation: Neutral

Short Term: 1-3 Months

Zacks Rank: (1-5)

3-Hold

Zacks Style Scores:

VGM:C

Value: B

Growth: C

Momentum: F

Summary

Timken anticipates revenues to decline significantly in second-quarter 2020 from the prior-year quarter due to the ongoing decline in its end markets on account of the COVID-19 pandemic. Mobile Industries business is expected to be hurt by significant declines in off highway and heavy truck and sluggish automotive market, while the Process Industries segment will bear the brunt of a weak industrial sector this year. The company had to adjust production schedules in response to customer and government shut-downs and other changes, which will also impact results. Higher costs related to manufacturing footprint initiatives will limit margins. Timken suspended sales and earnings guidance for 2020. The earnings estimates for the company's ongoing quarter and fiscal year's earnings have undergone negative revisions lately.

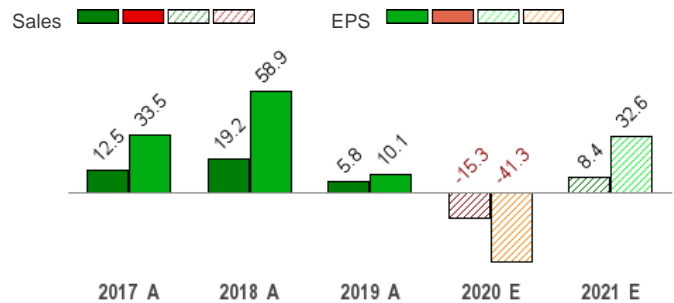
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$58.78 - \$22.26
20 Day Average Volume (sh)	719,615
Market Cap	\$3.5 B
YTD Price Change	-17.6%
Beta	1.81
Dividend / Div Yld	\$1.12 / 2.4%
Industry	Metal Products - Procurement and Fabrication
Zacks Industry Rank	Top 37% (94 out of 251)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	3.7%
Last Sales Surprise	-0.8%
EPS F1 Est- 4 week change	0.0%
Expected Report Date	08/03/2020
Earnings ESP	0.0%
P/E TTM	10.7
P/E F1	17.2
PEG F1	2.0
P/S TTM	0.9

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	917 E	834 E	844 E	857 E	3,479 E
2020	923 A	705 E	754 E	842 E	3,210 E
2019	980 A	1,000 A	914 A	896 A	3,790 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$1.11 E	\$0.87 E	\$0.99 E	\$0.84 E	\$3.58 E
2020	\$1.11 A	\$0.33 E	\$0.69 E	\$0.65 E	\$2.70 E
2019	\$1.35 A	\$1.27 A	\$1.14 A	\$0.84 A	\$4.60 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 07/06/2020. The reports text is as of 07/07/2020.

Overview

The Timken Company is a global manufacturer of bearings, friction management products, and mechanical power transmission components. The company serves a wide variety of end markets, including aerospace, automotive, construction, consumer, defense, energy, industrial equipment, health, heavy industry, machine tool, positioning control, power generation and rail markets.

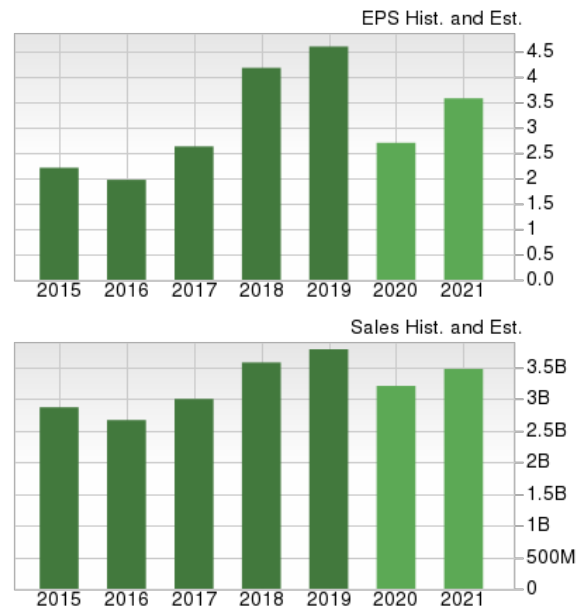
The company's portfolio features many strong brands, such as Timken, Philadelphia Gear, Drives, Cone Drive, Rollon, Lovejoy, Diamond, BEKA, and Groeneveld. Timken's global footprint consists of 125 manufacturing facilities, 21 technology and engineering centers, and 68 distribution centers and warehouses. The company employs more than 18,000 people across 42 countries.

Timken reports its operations through two segments: Mobile Industries and Process Industries.

Mobile Industries (54% of 2019 revenues) serves OEM customers that manufacture off-highway equipment for the agricultural, mining and construction markets; on-highway vehicles, including passenger cars, light trucks, and medium- and heavy-duty trucks; rail cars and locomotives; outdoor power equipment; rotorcraft and fixed-wing aircraft; and other mobile equipment. The segment also provides aftermarket sales and services.

Process Industries (55%) serves OEM and end-user customers in industries that place heavy demand on the fixed operating equipment they make or use in heavy and other general industrial sectors. This includes metals, cement and aggregate production; coal power generation and renewable energy sources; oil and gas extraction and refining; pulp and paper and food processing; automation and robotics; and health and critical motion control equipment. Other applications include marine equipment, gear drives, cranes, hoists and conveyors. This segment also supports after-market sales and service needs of customers.

During 2018, the company completed three acquisitions — ABC Bearings Limited, Apiary Investments Holdings Limited and Rollon S.p.A. In 2019, Timken completed the acquisition of BEKA Lubrication, and The Diamond Chain Company.



Reasons To Sell:

▼ In early-February 2020, Timken's operations in China were shut down amid coronavirus outbreak. Operations in China have now resumed and are currently at near-normal levels. With coronavirus spreading across the world, Timken had to adjust production schedules in response to customer and government shut-downs and other changes. Europe has been the hardest-hit geography for Timken. There is considerable uncertainty at this point regarding the overall impact of the pandemic on its business as a whole. COVID-19 has impacted most of Timken's end markets. Heavy Truck, Automotive, Off-Highway, and Industrial sectors were all down year over year in the first quarter of 2020. Considering continued uncertainty surrounding the same, the company suspended its sales and earnings guidance for 2020. Timken anticipates revenues to drop significantly in the second quarter of 2020 from the prior-year quarter due to decline in its end markets.

Timken's results will be hurt by sluggish automotive, industrial, off-highway, and heavy truck markets. The overall impact of COVID-19 on its operations and end-markets remains a concern.

▼ Among its diverse end market mix, the Industrial sector generates the highest proportion of revenues for Timken. The sector, which had been reeling under the protracted U.S.-China trade tensions and waning global demand, has now been hit hard by the coronavirus pandemic and energy market volatility. Per the Institute for Supply Management's report, the U.S Purchasing Managers' Index (PMI) came in at 41.5% for April — the lowest since April 2009 when it registered 39.9%. In May, the PMI came in at 43.1%. A reading below 50 denotes contraction. Even though the index has climbed to 52.6% in June, it remains to be seen whether the recovery will sustain considering the surge in coronavirus cases in the United States. Overall for the second quarter, the manufacturing index averaged 45.7%. A sluggish industrial sector will continue to weigh on Timken's results, particularly on the Process Industries segment. The Mobile Industries segment is expected to be hurt by significant declines in off highway and heavy truck as well as weakness in the automotive market in the current year.

▼ Timken expects to incur higher costs related to manufacturing footprint initiatives. In the Mobile Industries segment, Timken announced reorganization of its bearing plant in Gaffney, SC. The company will transfer its high-volume bearing production and roller production to other facilities, which is expected to occur by the end of the second quarter of 2020. Timken expects to incur \$8-\$10 million of pretax costs related to this reorganization. In the Process Industries segment, Timken announced the closure of its chain plant in Indianapolis, IN in February. This plant was part of the Diamond Chain acquisition completed on Apr 1, 2019. The company will transfer the manufacturing of its Diamond Chain product line to its chain facility in Fulton, IL. The chain plant is expected to close by the end of the fourth quarter of 2021. Timken expects to incur approximately \$10 million to \$12 million related to this closure. The imposition of tariffs on certain foreign goods, including steel and other raw materials have led to higher input costs for Timken. This, in turn, will dent margins if the company is not able to pass the price increases to customers.

Risks

- Timken continues to pursue strategic acquisitions to broaden its portfolio and capabilities across diverse markets, with a focus on bearings, adjacent power transmission products, and related services. In 2018, the company acquired Rollon, Cone Drive and ABC Bearings and divested the ICT Business. In 2019, Timken completed the acquisition of BEKA Lubrication and the Diamond Chain Company. The acquisition of BEKA Lubrication strengthened the company's global leadership in the automatic lubrication systems market sector. It also expanded its geographic reach in Europe and Asia. It enhanced the company's position in lucrative markets such as wind and food and beverage. Diamond Chain augments Timken's leadership in high-performance roller chains for industrial markets. These acquisitions have strengthened the company's global presence in growing markets, particularly China and Europe. These buyouts are expected to deliver significant cost and revenue synergies, going ahead.
 - Timken continues to measure a balanced approach to stoke growth, margins, returns and cash flow through industrial cycles. During the first quarter of 2020, Timken paid its 391st consecutive quarterly dividend and repurchased one million shares. Due to uncertainty caused by COVID-19, the company suspended its share buyback program for the time being. Timken's long term debt stood at \$1.78 billion at the first-quarter 2020 end, higher than \$1.65 billion as of fiscal 2019 end. The company has no significant long-term maturity before September 2023. Further, Timken's total debt to total capital ratio is 0.50, lower than its industry's 0.83. The company's times interest earned ratio was 7.3 as of Mar 31, 2020, better than the industry's 6.2. This underscores Timken's ability to meet debt obligations. The company drew \$350 million on its revolving credit facility on Apr 3, 2020, to boost financial flexibility. As of Apr 3, 2020, the company had over \$700 million of cash on hand. Cash flow is expected to improve through the year aided by favorable working capital and cost saving initiatives.
 - Timken is taking actions to enhance liquidity, reduce costs and generate strong cash flow. The company has implemented furloughs and salary reductions. It remains focused on improving working capital and reducing capital expenditure. Other cost and cash saving initiatives are currently underway. Timken meanwhile continues to advance its ongoing strategy – footprint, acquisition integration, and driving operational excellence. Timken's cost reduction actions will help sustain margins amid lower volumes.
 - Timken's products are essential for efficient and reliable operation of industrial equipment globally. Demand for the company's products will remain strong in the years to come. Its diversity in terms of end market, customer and geography, product innovation, and engineering expertise provide it with a competitive edge.
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Last Earnings Report

Timken's Q1 Earnings Beat Estimates, Revenues Miss

Timken reported first-quarter 2020 adjusted earnings per share of \$1.11, beating the Zacks Consensus Estimate of \$1.07. The reported figure declined 11% from \$1.35 per share in the prior-year quarter thanks to lower volumes due to the impact of COVID-19 as well as unfavorable currency.

On a reported basis, Timken delivered earnings per share of \$1.06 in the reported quarter compared with the prior-year quarter's \$1.19.

Total revenues in the quarter came in at \$923 million, down 6% from the year-ago quarter due to lower demand in most end markets and unfavorable currency. This was partially offset by the favorable impact of acquisitions and positive pricing. The top-line figure missed the Zacks Consensus Estimate of \$931 million.

Costs and Margins

Cost of sales was down 5% to \$645 million from the prior-year quarter. Gross profit declined 8% year over year to \$279 million. Gross margin came in at 30.2% compared with 30.9% in the year-ago quarter.

Selling, general, and administrative expenses inched up 1% to \$154 million from the prior-year quarter. Adjusted operating profit decreased 16% year over year to \$125 million. Operating margin came in at 13.6% compared with 15.3% in the comparable quarter last year. Adjusted EBITDA declined 12.5% year over year to \$177 million.

Segmental Performance

The Mobile Industries segment revenues decreased to \$467 million from \$500 million in the year-ago quarter. This downside mainly resulted from lower shipments in off-highway, automotive and heavy truck sectors and unfavorable currency. However, this was partially negated by the benefit from acquisitions and growth in the aerospace sector. The segment's adjusted EBITDA declined 5% year over year to \$76 million.

The Process Industries segment revenues decreased 5% year over year to \$457 million in the quarter. Lower revenues in the industrial distribution and general and heavy industrial sectors, along with unfavorable currency mainly led to the decline. These negatives were somewhat mitigated by the benefit of acquisitions and strong growth in renewable energy. The segment's adjusted EBITDA slid 15% year over year to \$112 million.

Financial Position

Timken generated free cash flow of \$24 million in the first quarter of 2020 compared with \$36 million in the prior year quarter. Cash flow from operations came in at \$56 million in the reported quarter compared with \$52 million witnessed in the previous year quarter. Net debt as of Mar 31, 2020 was \$1.57 billion compared with \$1.52 billion as of Dec 31, 2019.

During the first quarter of 2020, the company returned around \$65 million of capital to shareholders through \$23 million of dividend payouts and \$42 million in share repurchases.

Guidance

On Apr 3, 2020, Timken withdrew its 2020 sales and earnings guidance due to the uncertainty of the impact of COVID-19 on the economy.

Quarter Ending **03/2020**

Report Date	May 01, 2020
Sales Surprise	-0.78%
EPS Surprise	3.74%
Quarterly EPS	1.11
Annual EPS (TTM)	4.36

Valuation

Timken's shares are down 17.5% in the year-to-date period and 6.2% over the trailing 12-month period. Stocks in the Zacks Metal Products – Procurement and Fabrication industry and Industrial Products sector are down 24.0% and 9.9% in the year-to-date period, respectively. Over the past year, the Zacks sub-industry and sector are down 16.8% and 2.7%, respectively.

The S&P 500 index is down 1.1% in the year-to-date period and up 7.4% in the past year.

The stock is currently trading at 14.73X forward 12-month earnings, which compares to 13.07X for the Zacks sub-industry, 21.46X for the Zacks sector and 22.72X for the S&P 500 index.

Over the past five years, the stock has traded as high as 22.22X and as low as 5.37X, with a 5-year median of 13.28X.

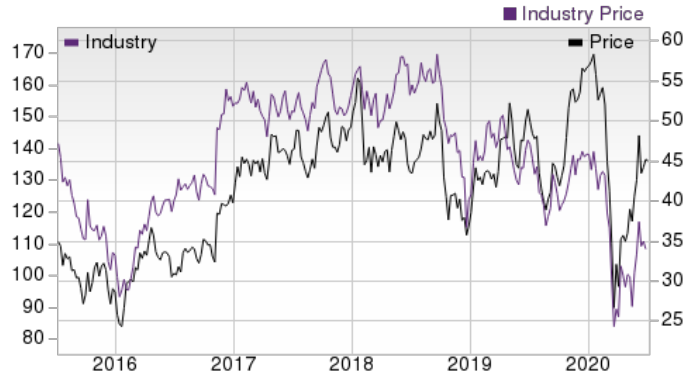
Our Underperform recommendation indicates that the stock will perform worse than the market. Our \$38 price target reflects 12.45X forward 12-month earnings per share.

The table below shows summary valuation data for TKR:

Valuation Multiples - TKR					
		Stock	Sub-Industry	Sector	S&P 500
P/E F12M	Current	14.73	13.07	21.46	22.72
	5-Year High	22.22	20.35	21.46	22.72
	5-Year Low	5.37	6.67	12.61	15.15
	5-Year Median	13.28	15.57	16.51	17.42
P/S F12M	Current	1.04	1.6	2.75	3.54
	5-Year High	1.44	2.44	2.75	3.54
	5-Year Low	0.48	0.66	1.51	2.54
	5-Year Median	0.96	1.1	2	3.01
EV/EBITDA TTM	Current	8.05	6.57	15.13	11.71
	5-Year High	29.54	19.13	17.29	12.81
	5-Year Low	5.22	6.46	10.63	8.24
	5-Year Median	8.1	10.79	14.71	10.75

As of 07/06/2020

Industry Analysis Zacks Industry Rank: Top 37% (94 out of 251)



Top Peers

Company (Ticker)	Rec	Rank
Century Aluminum Company (CENX)	Outperform	3
TriMas Corporation (TRS)	Outperform	1
AmpcoPittsburgh Corporation (AP)	Neutral	3
CIRCOR International, Inc. (CIR)	Neutral	2
Kaiser Aluminum Corporation (KALU)	Neutral	3
NN, Inc. (NNBR)	Neutral	4
Worthington Industries, Inc. (WOR)	Neutral	3
GrafTech International Ltd. (EAF)	Underperform	3

Industry Comparison Industry: Metal Products - Procurement And Fabrication				Industry Peers		
	TKR	X Industry	S&P 500	AP	CENX	WOR
Zacks Recommendation (Long Term)	Underperform	-	-	Neutral	Outperform	Neutral
Zacks Rank (Short Term)	3	-	-	3	3	3
VGM Score	C	-	-	A	B	A
Market Cap	3.49 B	570.75 M	22.04 B	40.43 M	648.59 M	1.96 B
# of Analysts	6	2	14	1	2	2
Dividend Yield	2.41%	0.00%	1.89%	0.00%	0.00%	2.74%
Value Score	B	-	-	A	C	B
Cash/Price	0.12	0.22	0.07	0.35	0.24	0.07
EV/EBITDA	7.02	6.90	12.81	2.98	35.46	8.00
PEG Ratio	2.02	3.69	2.94	NA	NA	NA
Price/Book (P/B)	1.83	1.56	3.01	0.71	0.96	2.03
Price/Cash Flow (P/CF)	6.80	6.26	11.87	1.18	NA	6.40
P/E (F1)	17.20	17.19	21.54	NA	NA	15.06
Price/Sales (P/S)	0.93	0.71	2.35	0.11	0.37	0.64
Earnings Yield	5.82%	4.95%	4.39%	-18.67%	-9.24%	6.65%
Debt/Equity	0.98	0.45	0.76	0.91	0.46	0.75
Cash Flow (\$/share)	6.83	2.51	6.94	2.67	-0.52	5.47
Growth Score	C	-	-	A	A	B
Hist. EPS Growth (3-5 yrs)	22.34%	6.76%	10.90%	NA	NA	3.24%
Proj. EPS Growth (F1/F0)	-41.27%	-42.76%	-9.51%	-259.46%	50.37%	-1.06%
Curr. Cash Flow Growth	8.64%	-11.05%	5.51%	329.76%	-159.66%	15.25%
Hist. Cash Flow Growth (3-5 yrs)	6.82%	4.92%	8.55%	20.02%	NA	5.91%
Current Ratio	2.72	2.63	1.30	1.53	2.05	2.53
Debt/Capital	49.42%	31.46%	44.46%	47.63%	31.46%	42.87%
Net Margin	9.40%	-0.46%	10.62%	-0.44%	-2.77%	2.58%
Return on Equity	17.93%	7.01%	15.75%	11.84%	-8.97%	14.13%
Sales/Assets	0.78	0.89	0.55	0.74	1.16	1.28
Proj. Sales Growth (F1/F0)	-15.31%	-12.66%	-2.57%	-18.02%	-15.65%	-12.66%
Momentum Score	F	-	-	F	F	A
Daily Price Chg	3.29%	0.91%	1.12%	2.27%	4.17%	-1.66%
1 Week Price Chg	-0.38%	2.44%	3.66%	0.98%	2.81%	4.06%
4 Week Price Chg	-6.60%	-6.63%	-7.12%	1.94%	-7.88%	-10.32%
12 Week Price Chg	32.69%	21.48%	11.84%	7.48%	75.12%	34.28%
52 Week Price Chg	-6.20%	-16.66%	-6.03%	-18.56%	5.84%	-10.87%
20 Day Average Volume	719,615	96,341	2,400,079	97,044	1,216,799	602,057
(F1) EPS Est 1 week change	0.00%	0.00%	0.00%	0.00%	0.00%	0.43%
(F1) EPS Est 4 week change	0.00%	0.00%	0.00%	0.00%	-18.58%	2.20%
(F1) EPS Est 12 week change	-20.97%	-28.06%	-8.26%	-242.11%	-131.03%	-1.06%
(Q1) EPS Est Mthly Chg	0.00%	0.00%	0.00%	0.00%	-21.05%	NA

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	B
Growth Score	C
Momentum Score	F
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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