

## United Technologies (UTX)

**\$102.50** (As of 03/12/20)

Price Target (6-12 Months): **\$87.00**

Long Term: 6-12 Months

**Zacks Recommendation:** Underperform

(Since: 01/30/20)

Prior Recommendation: Neutral

Short Term: 1-3 Months

**Zacks Rank:** (1-5)

**4-Sell**

Zacks Style Scores:

VGM:B

Value: C

Growth: B

Momentum: C

### Summary

Over the past three months, United Technologies' shares have underperformed the industry. The company is experiencing softness in its equipment orders at the Carrier segment due to lower transport refrigeration orders. Equipment orders were down 11% and 4%, on an organic basis, in the third and fourth quarters of 2019, respectively. Higher costs and operating expenses might prove detrimental to its profitability. Moreover, rise in debt levels is expected to increase its financial obligations. Owing to extensive geographic presence, its financial performance is subject to foreign currency fluctuations. However, Collins Aerospace' recent plan to invest \$225 million in three U.S. states is expected to augment its Landing Systems facility and create more than 100 employment opportunities, reflecting brighter prospects for the company.

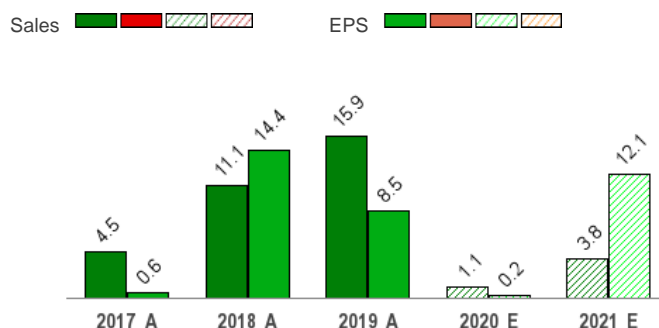
### Price, Consensus & Surprise



### Data Overview

52 Week High-Low	<b>\$158.44 - \$92.80</b>
20 Day Average Volume (sh)	<b>7,566,455</b>
Market Cap	<b>\$88.7 B</b>
YTD Price Change	<b>-31.6%</b>
Beta	<b>1.26</b>
Dividend / Div Yld	<b>\$2.94 / 2.9%</b>
Industry	<b>Diversified Operations</b>
Zacks Industry Rank	<b>Bottom 12% (222 out of 253)</b>

### Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	<b>5.4%</b>
Last Sales Surprise	<b>0.7%</b>
EPS F1 Est- 4 week change	<b>-0.5%</b>
Expected Report Date	<b>04/28/2020</b>
Earnings ESP	<b>-3.5%</b>

### Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021					80,873 E
2020	18,455 E	19,919 E	19,850 E	19,987 E	77,930 E
2019	18,365 A	19,634 A	19,496 A	19,551 A	77,046 A

### EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021					\$9.28 E
2020	\$1.66 E	\$2.16 E	\$2.22 E	\$2.07 E	\$8.28 E
2019	\$1.91 A	\$2.20 A	\$2.21 A	\$1.94 A	\$8.26 A

\*Quarterly figures may not add up to annual.

P/E TTM	<b>12.4</b>
P/E F1	<b>12.4</b>
PEG F1	<b>1.4</b>
P/S TTM	<b>1.2</b>

The data in the charts and tables, including the Zacks Consensus EPS and Sales estimates, is as of 03/12/2020. The reports text is as of 03/13/2020.

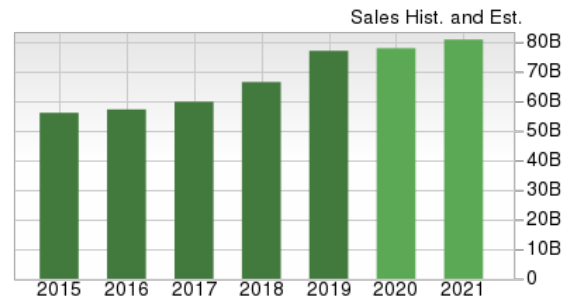
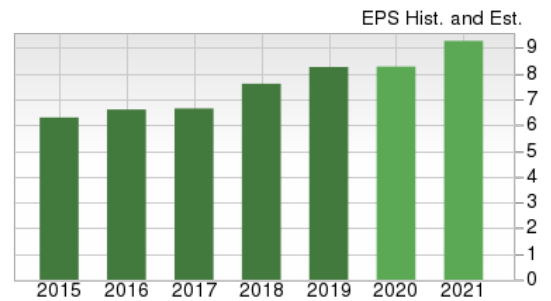
## Overview

United Technologies Corporation provides high-end technology products and services to the building systems and aerospace industries worldwide. The operations of the company are primarily classified into two principal businesses: Commercial and Aerospace. Under its commercial business, the company has Otis, and Carrier (formerly UTC Climate Control and Security) division. The aerospace business consists of Collins Aerospace Systems and Pratt & Whitney divisions.

Notably, Collins Aerospace Systems comprises Rockwell Collins assets (acquired in November 2018) and United Technologies' former UTC Aerospace Systems. A brief discussion on the company's four business segments is given below:

- **Otis** (16.9% of fourth-quarter 2019 revenues): Otis is the world's largest elevator and escalator manufacturing, installation and servicing company, serving customers in the commercial and residential property industries around the world.
- **Carrier** (22.5%): Carrier is the world's largest manufacturer and distributor of HVAC and refrigeration systems for residential, commercial, industrial and transportation applications. UTC Fire & Security is a global provider of security and fire safety products and services.
- **Pratt & Whitney** (28.3%): It is among the world's leading suppliers of aircraft engines for the commercial, military, business jet and general aviation markets.
- **Collins Aerospace Systems** (32.3%): Collins Aerospace Systems is a global leader in providing mechanical, electrical and software solution to the military and commercial aviation industry.

In March 2020, the company received a green signal from its board of directors for the separation of its Otis and Carrier businesses into two independent companies. Notably, this marks a major development required to divide its businesses into three independent companies — United Technologies, Otis and Carrier. It's worth noting here that United Technologies will comprise the businesses of Collins Aerospace Systems and Pratt & Whitney.



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## Reasons To Sell:

- ▼ Over the past three months, United Technologies' shares have lost 31.4% compared with the industry's decline of 25.7%. Rising cost of sales has been a major cause of concern for United Technologies over the past few quarters. Notably, in the third quarter and fourth quarter of 2019, the company's cost of sales was up 13.4% and 7.2% year over year, respectively. In addition, restructuring costs had an adverse impact of 6 cents and 16 cents on third and fourth quarters' bottom-line numbers, respectively. Also, the company's high R&D costs remain a concern. For instance, in the third and fourth quarters, its R&D expenditures increased 24.9% and 10.8%, respectively, on a year-over-year basis. Moreover, in the third and fourth quarters, selling, general and administrative expenses jumped 25.2% and 20.8%, respectively, on a year-over-year basis. In addition, analysts have become increasingly bearish on the company in the past 30 days. Consequently, the Zacks Consensus Estimate for first-quarter 2020 earnings has trended downward over the past seven days from \$1.71 to \$1.66 on account of one downward estimate revision versus none upward. Moreover, the consensus estimate for second-quarter earnings over the past 30 days has trended downward from \$2.19 to \$2.16 due to one downward estimate revision against none upward.
- ▼ United Technologies intends to bolster revenues and profitability on the back of overseas business expansion. However, this escalates certain political, economic and environmental risks for the company. For instance, unfavorable foreign currency movement had hurt United Technologies' revenues by 1 percentage point in both the third quarter and fourth quarter. As a matter of fact, fluctuations in foreign exchange rates may affect the company's top line in the quarters ahead.
- ▼ United Technologies is experiencing softness in its equipment orders at Carrier segment over the past few quarters, on account of continued lower transport refrigeration orders. Notably, equipment orders at the segment were down 11% and 4%, on an organic basis in the third and fourth quarters, respectively. Moreover, persistent soft orders for fire & security product remain a concern for the segment. For instance, in third quarter and fourth quarter, the fire & security product orders recorded decline of 2% and 3%, respectively. The company expects sales for Carrier segment to decline for the first quarter of 2020 due to weakness in the refrigeration business and foreign exchange headwinds.
- ▼ United Technologies' long-term debt in the last five years (2015-2019) increased 14.4% (CAGR). At the end of 2019, the company's long-term debt was \$ 37,788 million. Also, in 2019, net interest expenses surged 55.2% year over year to \$1,611 million. We believe, if unchecked, high-debt levels can increase the company's financial obligations and prove detrimental to its profitability.

Soft equipment orders at Carrier segment, escalating cost of sales and long-term debt remain major concerns for United Technologies.

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## Risks

- Rising reported better-than-expected fourth-quarter 2019 earnings. Adjusted earnings of \$1.94 per share were roughly flat year over year and surpassed the Zacks Consensus Estimate by 5.4%. United Technologies invests its cash flow in improving organic growth capabilities, reducing costs, making acquisitions, as well as repurchasing shares. In 2019, the company's cash flow from operations totaled \$8,883 million, an improvement of 40.5% from 2018. Also, the company used the net proceeds to pay off its long-term debt (net) of \$2,742 million in 2019. The company recorded strong free cash flow of \$6,627 million, a surge of 49.9% year over year. We believe that improvement in cash flows will effectively support the company's capital-allocation strategies. In addition, it remains on track to separate its existing businesses into three entities, which is likely to be completed in early second-quarter 2020. Notably, this portfolio separation will help companies to innovate, provide better customized solutions to customers and create greater values for shareholders.
  - United Technologies reported better-than-expected revenues in the fourth quarter. The top line was 8.4% higher than the year-ago figure and also surpassed the Zacks Consensus Estimate by 0.7%. Revenues improved 1% annually on an organic basis. The aerospace business' top line jumped on the back of continued strength in commercial aftermarket and military businesses at both Pratt & Whitney and Collins Aerospace segments and solid commercial OEM (Original Equipment Manufacturer) sales at Pratt & Whitney. In addition, impressive contribution from its acquired Rockwell Collins business (November 2018) boosted revenues of the aerospace business. With robust defense end market and growth in orders (for Geared Turbofan engines) coupled with strong commercial air traffic in the United States, prospects of the company's aerospace business look bright. For first-quarter 2020, the company expects revenues to be up slightly on a year-over-year basis, with expected low to mid-single digit revenue growth at the aerospace businesses. In addition, the company remains committed to rewarding shareholders handsomely through dividend payments and share buybacks. In the fourth quarter of 2019, the company paid out dividends worth \$612 million to shareholders and repurchased approximately shares worth \$40 million. It is worth noting that the quarterly dividend rate was hiked 5% in October 2018. Such diligent capital deployment strategies boost shareholders' wealth.
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## Last Earnings Report

### United Technologies Q4 Earnings and Revenues Beat

United Technologies reported better-than-expected fourth-quarter 2019 results. Quarterly adjusted earnings came in at \$1.94 per share, surpassing the Zacks Consensus Estimate of \$1.84. However, the bottom line was lower than the year-ago figure of \$1.95.

The company reported adjusted earnings of \$8.26 for 2019, an increase of 8.5% from the prior year.

In the fourth quarter, revenues came in at \$19,551 million, up 8.4% year over year. The top line also outpaced the consensus estimate of \$19,424 million. The rise was driven by 1% contribution from organic sales growth and 8% positive impact of acquisitions, partially offset by 1% negative impact of currency translation.

In 2019, the company reported total revenues of \$77,046 million compared with \$66,501 million in the previous year.

Quarter Ending **12/2019**

Report Date	Jan 28, 2020
Sales Surprise	0.66%
EPS Surprise	5.43%
Quarterly EPS	1.94
Annual EPS (TTM)	8.26

### Segmental Breakup

Otis' revenues for the reported quarter were \$3,362 million, up 1.9% year over year. Aggregate sales for Carrier totaled \$4,501 million, down 2.8%. Pratt & Whitney's fourth-quarter revenues were \$5,642 million, up 1.8% while the same for Collins Aerospace Systems surged 31.5% to \$6,444 million.

### Costs and Margins

Cost of products and services sold during the fourth quarter was \$14,734 million, up 7.2% year over year.

Selling, general and administrative expenses jumped 20.8% to \$2,314 million.

Adjusted operating profit margin was 13.1%, up 60 basis points.

### Balance Sheet/Cash Flow

Exiting the fourth quarter, United Technologies had cash and cash equivalents of \$7,378 million, up from \$6,152 million on Dec 31, 2018. Long-term debt was \$37,788 million, down from \$41,192 million recorded at the end of 2018.

During the quarter, the company generated \$2,782 million cash from operating activities compared with \$2,005 million a year ago. Its capital expenditures were up 15% to \$897 million.

### Outlook

For 2020, the company estimates Pratt & Whitney segment's sales to be up in the mid-single digit range, while Collins Aerospace segment's sales are projected to decline in low single digit.

Adjusted operating profit for Pratt & Whitney is estimated to rise the range of \$225-\$275 million from its reported figure in 2019. Collins Aerospace segment's adjusted operating profit is projected to decline in the range of \$275-\$325 million from 2019.

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## Recent News

### United Technologies' Board Okays Otis and Carrier Separation

On **Mar 11, 2020**, United Technologies moved a step forward toward the separation of its Otis and Carrier businesses into two independent companies, as it received a green signal from its board of directors.

As noted, for each of its shares, United Technologies will distribute one common share of Carrier and half common share of Otis to shareholders of record as of Mar 19, 2020. Adjustment for fractional shareholding will be done in cash. Ownership of United Technologies' shares will remain the same as before. The spin-off distribution will be effective on Apr 3, 2020.

The separate companies, with solid innovative capabilities, will be leaders in their respective fields and will likely bring in more customized solutions for their customers as well as create greater value for shareholders. The separation procedure will be tax-free.

### Dividend

On **Mar 10, 2020**, United Technologies paid out a quarterly cash dividend of 73.5 cents per share to shareholders of record as on Feb 14, 2020.

### United Technologies Unveils compressor facility

On **Feb 18, 2020**, United Technologies announced the opening of a new \$40 million 9,000 square-foot compressor facility at United Technologies Research Center (UTRC), located in East Hartford, Connecticut.

### Investments

On **Feb 10, 2020**, United Technologies' Aerospace Unit, Collins Aerospace, announced that it intends to establish a Landing Systems facility in Texas to address the burgeoning demand for its brakes, wheels and landing gear from various commercial and military aviation customers in the global market. To augment the prospects of this particular segment, the company also plans to expand its carbon brake manufacturing sites in Colorado and Washington. With \$225 million investment, this promising venture is expected to create more than 100 employment opportunities.

### Partnership

On **Dec 9, 2019**, United Technologies' business unit Carrier announced that it has entered into a collaboration with Tim Hortons to support the latter's store expansion plan in the country. Per the deal, Carrier will provide integrated HVAC (heating, ventilating and air conditioning) solutions and services for Tim Hortons' current and prospective coffee stores in China.

Per the pact, Carrier will be responsible for offering Tim Hortons (recognized as Tims Coffee House in China) its advanced Variable Refrigerant Flow (VRF) technology along with a custom services package, which will support optimal HVAC operation in Tims coffee houses in China.

### United Technologies' & Raytheon's Shareholders Approve Merger

On **Oct 11, 2019**, United Technologies and Raytheon Company announced that shareholders of both the companies have approved all the proposals required for the acquisition of latter by the former in a deal termed as a "merger of equals".

Notably, the approval keeps both the companies well on track to complete the merger in the first half of 2020, conditional upon customary closing conditions and separation of the Otis and Carrier businesses from parent United Technologies (as announced in November 2018).

### United Technologies to Merge With Raytheon in All-Stock Deal

On **June 9, 2019**, United Technologies agreed to acquire Raytheon Company and merge it with its aerospace business. The all-stock merger of equals, as it has been termed by the participating companies, will create an aerospace and defense giant.

It is worth mentioning here that Raytheon's products and services mainly cater to customers in defense and government markets. The company, founded in 1922, is headquartered in Waltham, MA.

### Details of the Merger Deal

As noted, United Technologies' board of directors approved the merger and it can be accomplished only after it separates from its Otis and Carrier businesses. Post the separation, the company will be left with its Collins Aerospace Systems and Pratt & Whitney businesses.

Raytheon will be required to reorganize its four business operations into two, namely Integrated Defense & Missile Systems; and Intelligence, Space & Airborne Systems. At the time of the merger, each share of Raytheon can be exchanged for 2.3348 shares of the new company.

Raytheon Technologies — as the combined company will be known — will comprise the aforementioned future businesses of United Technologies and Raytheon. Of its total shareholding, roughly 57% will be with United Technologies while the rest will be with Raytheon. Its headquarters will be in the greater Boston metro area while the board of directors will have 8 members from United Technologies and 7 from Raytheon.

Pro forma sales of Raytheon Technologies are anticipated to be approximately \$74 billion in 2019. Net debt will likely be \$26 billion, of which \$24 billion relates to United Technologies. Healthy free cash flow generation and solid balance sheet will be beneficial. Research and development spendings are likely to be \$8 billion annually.

Apart from sophisticated technologies and products, the combined company intends on rewarding shareholders with \$18-\$20 billion in the initial 36 months. Annual run-rate cost synergies will likely be \$1 billion in the first four years. Of this, annual savings of \$500 million will be returned to

shareholders.

With all pre-conditions fulfilled and the receipt of required regulatory approvals, the merger is likely to be completed in the first half of 2020.

## Valuation

United Technologies' shares are down 31.6% and 19.2% in the year-to-date period and over the trailing 12-month period, respectively. Stocks in both the Zacks sub-industry and the Zacks Conglomerates sector are down 26.4% in the year-to-date period. Over the past year, both the Zacks sub-industry and sector have moved down 20.1%.

The S&P 500 Index has moved down 23% in the year-to-date period and 12.5% in the past year.

The stock is currently trading at 10.51X forward 12-month EV/EBITDA, which compares to 25.36X for both the Zacks sub-industry and for the Zacks sector and 12.34X for the S&P 500 index.

Over the past five years, the stock has traded as high as 12.74X and as low as 8.07X, with a 5-year median of 10.12X. Our Underperform recommendation indicates that the stock will perform worse than the market. Our \$87 price target reflects 10.25X forward 12-month earnings per share.

The table below shows summary valuation data for UTX.

Valuation Multiples - UTX					
		Stock	Sub-Industry	Sector	S&P 500
EV/EBITDA F12M	Current	10.51	25.36	25.36	12.34
	5-Year High	12.74	81.18	81.18	14.18
	5-Year Low	8.07	17.86	17.86	9.08
	5-Year Median	10.12	22.71	22.71	10.82
P/E F12M	Current	12.08	14.99	14.99	14.38
	5-Year High	19.9	20.06	20.06	19.34
	5-Year Low	12.08	14.99	14.99	14.38
	5-Year Median	16.28	17.76	17.76	17.42
EV/Sales F12M	Current	1.88	3.72	3.72	3.04
	5-Year High	2.21	4.32	4.32	3.51
	5-Year Low	1.48	2.82	2.82	2.3
	5-Year Median	1.83	3.66	3.66	2.8

As of 03/12/2020

## Industry Analysis Zacks Industry Rank: Bottom 12% (222 out of 253)



## Top Peers

General Dynamics Corporation (GD)	Neutral
General Electric Company (GE)	Neutral
Honeywell International Inc. (HON)	Neutral
Lockheed Martin Corporation (LMT)	Neutral
3M Company (MMM)	Neutral
Northrop Grumman Corporation (NOC)	Neutral
Raytheon Company (RTN)	Neutral
Woodward, Inc. (WWD)	Neutral

Industry Comparison Industry: Diversified Operations				Industry Peers		
	UTX Underperform	X Industry	S&P 500	GD Neutral	GE Neutral	HON Neutral
<b>VGM Score</b>	<b>B</b>	-	-	<b>A</b>	<b>B</b>	<b>C</b>
Market Cap	88.69 B	4.65 B	17.38 B	38.30 B	63.19 B	96.09 B
# of Analysts	7	3	13	8	8	10
Dividend Yield	2.87%	1.80%	2.51%	3.09%	0.55%	2.67%
<b>Value Score</b>	<b>C</b>	-	-	<b>B</b>	<b>B</b>	<b>C</b>
Cash/Price	0.07	0.17	0.05	0.02	1.03	0.09
EV/EBITDA	8.89	7.24	10.90	8.45	4.43	10.75
PEG Ratio	1.42	1.57	1.54	1.32	2.08	1.68
Price/Book (P/B)	2.00	0.85	2.35	2.82	2.12	5.14
Price/Cash Flow (P/CF)	8.10	5.97	9.60	8.88	5.60	13.63
P/E (F1)	12.51	12.38	13.98	10.38	13.00	15.33
Price/Sales (P/S)	1.15	0.91	1.89	0.97	0.60	2.62
Earnings Yield	8.08%	7.67%	7.07%	9.63%	7.75%	6.53%
Debt/Equity	0.90	0.75	0.70	0.66	2.36	0.59
Cash Flow (\$/share)	12.65	2.19	7.01	14.89	1.29	9.89
<b>Growth Score</b>	<b>B</b>	-	-	<b>B</b>	<b>B</b>	<b>B</b>
Hist. EPS Growth (3-5 yrs)	4.27%	9.12%	10.85%	7.05%	-20.84%	8.56%
Proj. EPS Growth (F1/F0)	0.21%	4.56%	5.99%	6.38%	-14.42%	7.83%
Curr. Cash Flow Growth	26.99%	8.17%	6.15%	3.16%	-8.00%	-1.43%
Hist. Cash Flow Growth (3-5 yrs)	5.99%	5.29%	8.52%	6.36%	-12.27%	5.69%
Current Ratio	1.08	2.00	1.24	1.18	1.70	1.34
Debt/Capital	47.51%	42.18%	42.57%	39.89%	70.19%	37.28%
Net Margin	7.19%	5.33%	11.64%	8.85%	-4.71%	16.73%
Return on Equity	16.60%	10.89%	16.74%	26.70%	14.12%	32.21%
Sales/Assets	0.56	0.78	0.54	0.81	0.37	0.62
Proj. Sales Growth (F1/F0)	1.15%	1.44%	3.54%	3.66%	-12.84%	1.89%
<b>Momentum Score</b>	<b>C</b>	-	-	<b>B</b>	<b>D</b>	<b>D</b>
Daily Price Chg	-4.66%	-8.62%	-10.03%	-10.93%	-11.94%	-12.09%
1 Week Price Chg	-3.15%	-0.76%	-0.67%	2.09%	-13.60%	1.15%
4 Week Price Chg	-33.03%	-24.51%	-28.22%	-30.20%	-44.13%	-25.13%
12 Week Price Chg	-31.07%	-25.49%	-25.63%	-25.98%	-34.51%	-23.60%
52 Week Price Chg	-19.22%	-30.61%	-16.72%	-22.03%	-29.81%	-13.14%
20 Day Average Volume	7,566,455	83,643	3,061,271	2,312,776	88,255,352	4,319,781
(F1) EPS Est 1 week change	-0.14%	0.00%	0.00%	0.00%	-0.67%	-0.08%
(F1) EPS Est 4 week change	-0.48%	-0.41%	-0.32%	0.61%	-3.62%	-0.29%
(F1) EPS Est 12 week change	-5.26%	-2.60%	-0.65%	-1.60%	-20.70%	-0.11%
(Q1) EPS Est Mthly Chg	-2.92%	-0.52%	-0.62%	0.00%	-19.31%	-0.33%



## 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	B
Momentum Score	C
VGM Score	B

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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