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Jan 06, 2020

Waters Corporation (WAT)

$231.01 (As of 01/03/20)

Price Target (6-12 Months): **$243.00**

Long Term: 6-12 Months	**Zacks Recommendation:** (Since: 04/23/19) Prior Recommendation: Outperform	**Neutral**
Short Term: 1-3 Months	**Zacks Rank:** (1-5)	**3-Hold**
	Zacks Style Scores:	VGM:D
	Value: D | Growth: C | Momentum: B	

Summary

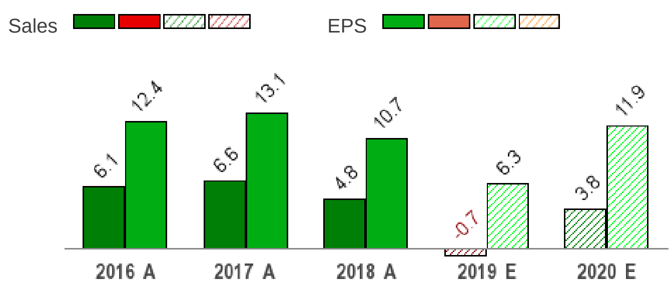
Waters is benefiting from growing momentum in the pharmaceutical market. Further, the company is gaining traction across Asia, which is contributing to the top line. Additionally, the company's growing investments in LC, LC-MS and chemistry categories are aiding it in gaining traction in large molecule market. Further, the company remains optimistic regarding its strengthening growth initiatives and new product introductions that are likely to instill investor optimism in the near term. Moreover, its continued focus toward innovation remains a major positive. However, weakness in Governmental & Academic market is a headwind. Sluggishness in TA segment remains a concern. Further, government policy changes in China and political uncertainties in Europe are overhangs. Notably, the stock has underperformed the industry over a year.

Price, Consensus & Surprise

Data Overview

52 Week High-Low	**$255.21 - $180.47**
20 Day Average Volume (sh)	**395,433**
Market Cap	**$14.9 B**
YTD Price Change	**-1.1%**
Beta	**1.04**
Dividend / Div Yld	**$0.00 / 0.0%**
Industry	**Instruments - Scientific**
Zacks Industry Rank	**Top 38% (96 out of 252)**
Last EPS Surprise	**0.0%**
Last Sales Surprise	**-2.0%**
EPS F1 Est- 4 week change	**0.0%**
Expected Report Date	**01/22/2020**
Earnings ESP	**1.3%**
P/E TTM	**26.4**
P/E F1	**23.4**
PEG F1	**2.3**
P/S TTM	**6.2**

Sales and EPS Growth Rates (Y/Y %)



Sales Estimates (millions of $)

	Q1	Q2	Q3	Q4	Annual*
2020	534 E	619 E	601 E	743 E	2,495 E
2019	514 A	599 A	577 A	714 E	2,404 E
2018	531 A	596 A	578 A	715 A	2,420 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2020	$1.87 E	$2.42 E	$2.37 E	$3.17 E	$9.86 E
2019	$1.60 A	$2.14 A	$2.13 A	$3.01 E	$8.81 E
2018	$1.59 A	$1.95 A	$1.92 A	$2.87 A	$8.29 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 01/03/2020. The reports text is as of 01/06/2020.

Overview

Milford, MA-based, Waters Corp. is an analytical instrument manufacturer and offers practical and sustainable products for laboratory-dependent organizations. Moreover, Waters provides analytical workflow solutions based on mass spectrometry, liquid chromatography and thermal analysis technologies.

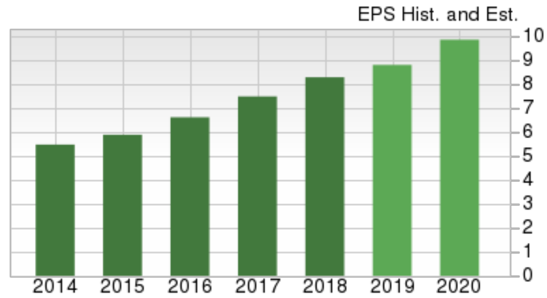
The company's products are used by pharmaceutical, life science, biochemical, industrial, academic and government customers, working in research and development, quality assurance and other laboratory applications.

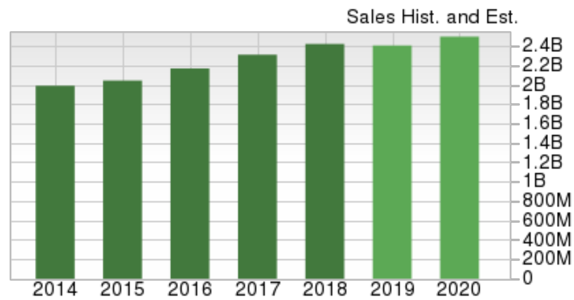
Waters serves customers through its strong sales and service networks. As of December 2018, the total number of the company's sales offices stood at 87 across the world. Further, total number of field representatives were 3,900 in 2018, up from 3,800 in 2017.

Notably, the company generated $2.42 billion of total revenues in 2018, improving 5% from 2017.

The company operates in Asia, Americas and Europe. Waters organizes its business into two operating segments: Waters Division and TA Division.

Waters Division (88.4% of total revenues in 2018)- High Performance and Ultra Performance Liquid Chromatography (HPLC).





Developed in the 1950s, HPLC is the standard technique used to identify and analyze the constituent components of a variety of chemicals and other materials. The company believes that HPLC's performance capabilities enable it to separate and identify approximately 80% of all known chemicals and materials. As a result, HPLC is used to analyze substances in a wide variety of industries for research and development purposes, quality control and process engineering applications.

TA Division (11.6%)- Thermal Analysis, Rheometry and Calorimetry.

Thermal analysis measures the physical characteristics of materials as a function of temperature. The techniques are widely used in the development, production and characterization of materials in various industries, such as plastics, chemicals, automobiles, pharmaceuticals and electronics. Rheometry instruments characterize the flow properties of materials and measures their viscosity, elasticity and deformation under different types of "loading" or conditions. The information obtained under such conditions provides insight into a material's behavior during manufacturing, transport, usage and storage.

Reasons To Buy:

▲ Waters has an average positive surprise of 0.55% over the last four trailing quarters. In the past few quarters, the company's bottom line has benefitted from disciplined spending and careful use of capital. Waters' key strengths include leading positions in the pharmaceutical market, broad global customer base and an impressive lineup of products.The company has delivered strong organic growth over the past few quarters on the back of continuous operational improvement and ever judicious use of shareholder capital. For 2019, Waters Corp. remains confident that solid demand from pharmaceutical business, modest recovery of industrial markets and growth in recurring revenue will accelerate its growth momentum. Healthy global industrial conditions and the overall rise of regulatory standards for performance and quality should boost demand for Waters Corp.'s products and offerings.

Waters remains confident on its improving position in the Governmental & Academic market. Also, its mass spectrometry portfolio and liquid chromatography systems continues to perform well.

▲ Waters has a strong presence in the chromatography instrument and pharmaceuticals markets, and expects to reap enhanced profit from these markets, going forward. The company, which is currently one of the leading players in the mass spectrometry market, has been garnering significantly from the sale of its advanced mass spectrometry instruments. Waters' global pharmaceuticals business, its largest single market and major revenue driver, is gaining traction over the last few quarters and fueling the growth of Waters Division. In third-quarter 2019, the company's global pharmaceuticals business accounted for 56.8% of the net sales. Positive macro trends including, rising global regulatory standards, increasing access of patients to prescription drugs, growing testing needs of newer biological drugs and ever-increasing complexity in molecular structure, are acting as tailwinds for the pharmaceutical business. Moreover, well-performing small and large molecule applications will continue to aid the top-line growth within this market.

▲ Waters continues to benefit from increasing regulation around food safety and quality, strict conditions for food testing, and environmental and fine chemical applications. Going forward, the company is very optimistic about the breadth of opportunity for this segment, across materials characterization, food safety and environmental applications. The company's governmental and academic category which accounted for 13.5% of the total revenues in the third quarter, is being driven largely by strong spending by academic institutions on biomedical research across U.S., Europe and Korea.

▲ Waters Corp. has an active research and development (R&D) division that is primarily focused on the development and commercialization of products that complement as well as update its existing product offerings. The company spends a significant amount on R&D as most of its products are manufactured in-house across its facilities. Moreover, an increased demand for research intensive products, especially the company's mass spectrometry solutions, is a positive for Waters Corp.'s business which has been on an uptrend lately. Apart from this, the company has started shipping its recently launched next generation screening system called RenataDX. Further, it recently introduced BioAccord LCMS system. The company also introduced ACQUITY UPLC PLUS series, a series of three new ACQUITY systems. Going forward, Waters Corp. remains confident that its industry-leading Empower software, tailored to QDa methodologies, will offer it a distinct advantage in this high-potential product category. Also, the company's DMA 850 continues to boost the performance of TA product line. Overall, robust product pipeline and strength in end markets is anticipated to drive top-line growth for the upcoming quarters.

Reasons To Sell:

- Waters Corp. faces competition from several international instrument manufacturers and other companies in both domestic and foreign markets. The company's key technologies like HPLC, UPLC, MS, LC-MS, thermal analysis, rheometry and calorimetry product lines are part of a highly competitive industry and are subject to rapid changes in technology. Although the company continues to invest in its research and development (R&D) division to outdo its peers, this tends to push the expenses higher. Waters Corp. has been incurring high R&D expenses over the last few years. The company intends to increase its spending on research and development in order to boost product innovations in the coming quarters. The higher outlay, although beneficial in the long run, will push expenses higher and hurt immediate profits.

Waters continually grapples with currency volatility and stiff competition, which hurt its revenues as well as margins. Further, high debt level of the company remains a major headwind.

- Waters Corp.'s debt levels and the consequent interest expenses remain a burden. Moreover, significant portions of the company's contracts are on a fixed-price basis. As the company generally executes these contracts via third parties, it runs the risks of losses if the sub-contractors are not able to complete the required amount of work in scheduled time. Additionally, such contracts are generally from outside U.S. and hence, are subject to several economic and political uncertainties across the globe. The company may also have to bear losses if these costs exceed expectations. In recent times, slower budgetary releases in the U.S. have hurt the company's pharmaceutical business in the U.S. The company sales were limited due to macroeconomic and government policy uncertainties, which seem to be affecting general business activity in the US.

- Waters Corp. generates a substantial portion of its revenues from non-U.S. markets. Therefore, currency volatility considerably impacts its revenues. Financial markets in certain foreign countries have been experiencing economic inconsistencies. The inherent instability of the currency markets poses a risk to the company's financials. In recent times, the negative impact of currency translation has reduced sales growth, and this remains a risk for future quarters as well.

- Waters Corp. is highly dependent on capital spending and any delay in its release can hinder its business. The company's business is significantly reliant on government, academic and research institutions capital spending. Fluctuations in these funds can affect Waters Corp.'s business significantly by reducing the ongoing research and development activities. The company's business in Japan and China also depends largely on such funding. Moreover, softeness in Indian market is expected to continue, which is a headwind. The company's government and academic businesses has suffered in the past on account of increased variability in the purchasing pattern and high selling prices of the advanced systems. There is a risk that this segment might revert to such performance in the future. In addition, the company's industrial business also remains susceptible to high quarterly variability.

Last Earnings Report

Waters' Q3 Earnings In Line, Revenues Lag Estimates

Quarter Ending	09/2019
Report Date	Oct 29, 2019
Sales Surprise	-2.04%
EPS Surprise	0.00%
Quarterly EPS	2.13
Annual EPS (TTM)	8.74

Waters Corporation reported third-quarter 2019 non-GAAP earnings of $2.13 per share, which matched the Zacks Consensus Estimate. Further, the figure improved 11% on a year-over-year basis but declined 0.5% sequentially.

Net sales of $577.3 million were marginally down 0.1% from the year-ago quarter and 3.6% from the previous quarter. Further, the figure missed the Zacks Consensus Estimate of $589.3 million.

The company encountered softness in the U.S. market, which impacted sales growth negatively in the Americas region during the third quarter. This was primarily responsible for sluggish top line.

Further, weakness in the Governmental & Academic market remains a concern.

Nevertheless, Waters witnessed solid momentum across Asia throughout the reported quarter.

Further, the company remains optimistic regarding its strengthening growth initiatives and new product introductions, which are likely to instill investor optimism.

Top Line in Detail

Waters’ net sales figure can be categorized in four ways:

By Operating Segment: The company operates in two organized segments — Waters and TA.

Waters segment (88.7% of net sales) generated $515.15 million of sales, down 0.7% from the year-ago quarter. Sales in TA segment came in $65.13 million and accounted for 11.3% of the net sales. The figure reflected year-over-year growth of 4.7%.

By Products & Services: This division comprises three segments — Instruments, Services and Chemistry.

Instruments sales (46.8% of sales) came in $270.32 million, down 4% on a year-over-year basis.

Service sales (35.8% of the sales) were $206.71 million, improving 4% year over year.

Chemistry sales (17.4% of the sales) were $100.26 million, advancing 4.5% from the year-ago quarter.

Moreover, service and chemistry sections together generated recurring revenues of $306.96 million, up 4% from the year-ago quarter.

By Markets: The company serves three end markets — Pharmaceutical, Industrial and Governmental & Academic.

Pharmaceutical market (56.8% of net sales) generated sales of $328.23 million, up 1% on a year-over-year basis.

Industrial market (29.7% of sales) sales came in $171.35 million, down 0.4% from the year-ago quarter.

Governmental & Academic (13.5% of sales) generated $77.69 million of sales. The figure decreased 3.9% year over year.

By Geography: This company’s operating regions include Asia, Americas and Europe.

Asia (41.2% of net sales) generated $237.78 million of sales, up 7% on a year-over-year basis.

Americas (34% of sales) generated $196.46 million of sales, decreasing 5% year over year.

Europe (24.8% of sales) generated $143.04 million of sales, down 4% from prior-year quarter.

Operating Details

In the third quarter, non-GAAP selling and administrative expenses were $124.4 million, suggesting a decline of 1.5% from the year-ago quarter.

Per the company, research and development spending was $34.3 million, indicating a decline of 2.4% form the year-ago reported figure.

Adjusted operating margin was 30.7%, which expanded 40 bps year over year.

Balance Sheet & Cash Flow

As of Sep 28, 2019, cash, cash equivalents and investments came in $404.65 million, lower than $675.77 million as of Jun 29, 2019.

Further, total liabilities were $2.45 billion, up from $2.27 billion in the previous quarter.

Waters also generated free cash flow of $124.45 million in the third quarter.

Guidance

For fourth-quarter 2019, Waters expects non-GAAP earnings in the range of $2.95-$3.05 per share.

The company anticipates net sales growth between 0% and 2% on a constant currency basis.

For 2019, Waters lowered guided range for non-GAAP earnings from $8.95-$9.10 per share to $8.73-$8.83.

Further, the company's net sales growth on a year-over-year basis is projected at 1% on a constant currency basis.

Recent News

On **Nov 5, 2019**, Waters revealed that its ACQUITY Advanced Polymer Chromatography System is a fully solvent-compatible UltraPerformance Liquid Chromatography/ultra-high performance size exclusion chromatography which is first of its kind. The company is likely to gain momentum among research scientists with this product.

On **Oct 1, 2019**, Waters unveiled TA Instruments MSF16 Multi-Specimen Fatigue Instrument, thus expanding its TA product portfolio.

Valuation

Waters shares are up 6.4% in the six-month period and 23.4% over the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Computer & Technology sector are down 3.4% and up 12.9% in the six-month period, respectively. Over the past year, the Zacks sub-industry and the sector are up 30.8% and 32.2%, respectively.

The S&P 500 index is up 9.3% in the six-month period and 25.7% in the past year.

The stock is currently trading at 23.39X forward 12-month earnings, which compares to 24.7X for the Zacks sub-industry, 22.17X for the Zacks sector and 18.71X for the S&P 500 index.

Over the past five years, the stock has traded as high as 26.87X and as low as 17.95X, with a 5-year median of 21.96X. Our Neutral recommendation indicates that the stock will perform in-line with the market. Our $243 price target reflects 24.59X forward 12-month earnings.

The table below shows summary valuation data for WAT

Valuation Multiples - WAT

		Stock	Sub-Industry	Sector	S&P 500
P/E F 12M	Current	23.39	24.7	22.17	18.71
	5-Year High	26.87	26.74	22.17	19.34
	5-Year Low	17.95	18.41	16.86	15.17
	5-Year Median	21.96	22.15	19.24	17.44
P/S F12M	Current	5.96	5.15	3.57	3.47
	5-Year High	7.25	5.92	3.57	3.47
	5-Year Low	4.33	3.63	2.3	2.54
	5-Year Median	5.66	4.8	3.01	3
EV/EBITDA TTM	Current	18.21	24.96	12.12	11.99
	5-Year High	20.57	27.54	12.6	12.86
	5-Year Low	8.82	15.24	7.67	8.48
	5-Year Median	14.9	21.05	10.52	10.67

As of 01/03/2020

Industry Analysis Zacks Industry Rank: Top 38% (96 out of 252)

Top Peers

Agilent Technologies, Inc. **(A)**	Neutral
Bio-Rad Laboratories, Inc. **(BIO)**	Neutral
Bruker Corporation **(BRKR)**	Neutral
Danaher Corporation **(DHR)**	Neutral
General Electric Company **(GE)**	Neutral
Mettler-Toledo International, Inc. **(MTD)**	Neutral
PerkinElmer, Inc. **(PKI)**	Neutral
Thermo Fisher Scientific Inc. **(TMO)**	Neutral

Industry Comparison Industry: Instruments - Scientific

Industry Peers

	WAT Neutral	X Industry	S&P 500	A Neutral	GE Neutral	MTD Neutral
VGM Score	D	-	-	B	D	C
Market Cap	14.88 B	290.21 M	23.66 B	26.23 B	104.54 B	19.23 B
# of Analysts	8	6	13	9	7	6
Dividend Yield	0.00%	0.00%	1.79%	0.85%	0.33%	0.00%
Value Score	D	-	-	D	D	F
Cash/Price	0.03	0.05	0.04	0.05	0.78	0.01
EV/EBITDA	18.82	19.10	13.88	21.64	-15.53	26.24
PEG Ratio	2.23	2.20	1.99	1.98	2.53	2.38
Price/Book (P/B)	128.88	2.21	3.36	5.52	3.59	43.87
Price/Cash Flow (P/CF)	23.26	17.81	13.62	21.33	7.50	32.49
P/E (F1)	23.22	22.24	18.74	24.78	17.07	31.56
Price/Sales (P/S)	6.19	2.28	2.67	5.08	0.93	6.45
Earnings Yield	4.27%	4.51%	5.32%	4.03%	5.85%	3.17%
Debt/Equity	11.40	0.67	0.72	0.38	2.67	2.57
Cash Flow ($/share)	9.93	1.81	6.94	3.96	1.60	24.30
Growth Score	C	-	-	B	C	B
Hist. EPS Growth (3-5 yrs)	10.49%	6.93%	10.56%	9.28%	-20.34%	15.10%
Proj. EPS Growth (F1/F0)	11.97%	12.35%	7.41%	9.72%	14.99%	10.28%
Curr. Cash Flow Growth	5.99%	5.99%	14.83%	9.85%	-18.18%	12.72%
Hist. Cash Flow Growth (3-5 yrs)	7.84%	8.44%	9.00%	-2.46%	-8.86%	9.65%
Current Ratio	2.25	2.02	1.23	1.53	1.84	1.34
Debt/Capital	91.94%	41.07%	42.92%	27.39%	72.76%	71.95%
Net Margin	23.98%	4.83%	11.08%	20.74%	-4.39%	18.42%
Return on Equity	77.73%	7.29%	17.10%	20.13%	11.69%	105.34%
Sales/Assets	0.78	0.78	0.55	0.57	0.38	1.13
Proj. Sales Growth (F1/F0)	3.79%	1.66%	4.20%	7.08%	-1.68%	3.32%
Momentum Score	B	-	-	A	F	A
Daily Price Chg	-1.72%	-0.89%	-0.61%	-1.61%	0.34%	-1.93%
1 Week Price Chg	0.21%	0.16%	0.13%	0.27%	1.36%	-0.06%
4 Week Price Chg	3.27%	2.78%	2.60%	3.73%	10.94%	7.15%
12 Week Price Chg	9.33%	15.65%	8.87%	14.28%	41.66%	17.43%
52 Week Price Chg	31.00%	15.50%	29.34%	33.66%	48.51%	53.74%
20 Day Average Volume	395,433	66,009	1,603,615	1,354,649	45,137,568	134,527
(F1) EPS Est 1 week change	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
(F1) EPS Est 4 week change	0.00%	0.00%	0.00%	0.03%	-0.81%	0.00%
(F1) EPS Est 12 week change	-2.71%	-0.76%	-0.57%	-0.01%	-5.58%	-1.90%
(Q1) EPS Est Mthly Chg	0.00%	0.00%	0.00%	0.00%	0.00%	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	B
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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