

Waters Corporation (WAT)

\$220.80 (As of 07/15/20)

Price Target (6-12 Months): **\$232.00**

Long Term: 6-12 Months

Zacks Recommendation:

Neutral

(Since: 04/23/19)

Prior Recommendation: Outperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

4-Sell

Zacks Style Scores:

VGM:D

Value: D

Growth: C

Momentum: C

Summary

Waters is benefiting from the solid momentum across biomedical research applications. Further, the company's growing investments in LC, LC-MS and chemistry categories are aiding it in gaining traction in large molecule market. Also, improving performance of the company in Europe is a tailwind. Further, the company remains optimistic regarding its strong growth initiatives and new product introductions that are likely to instill investor optimism. Moreover, its continued focus toward innovation remains a major positive. However, coronavirus pandemic remains a major headwind. The company has withdrawn its full year guidance due to uncertainties related to it. Also, government policy changes in China remain concerns. Further, sluggish small molecule market is a headwind. The stock has underperformed its industry on a year-to-date basis.

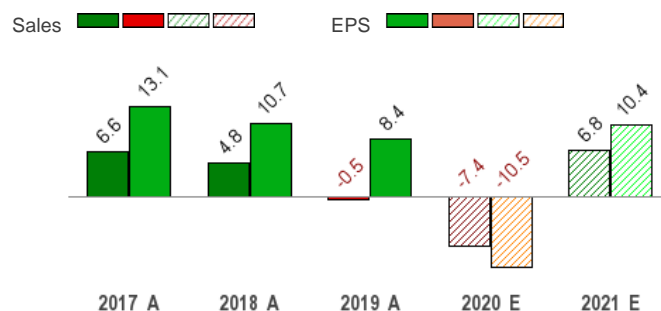
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$245.68 - \$154.39
20 Day Average Volume (sh)	883,436
Market Cap	\$13.7 B
YTD Price Change	-5.5%
Beta	0.94
Dividend / Div Yld	\$0.00 / 0.0%
Industry	Instruments - Scientific
Zacks Industry Rank	Top 11% (27 out of 251)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	-19.0%
Last Sales Surprise	-6.9%
EPS F1 Est- 4 week change	-0.5%
Expected Report Date	08/04/2020
Earnings ESP	1.5%
P/E TTM	25.6
P/E F1	27.4
PEG F1	2.6
P/S TTM	5.8

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	503 E	549 E	578 E	749 E	2,381 E
2020	465 A		552 E	723 E	2,230 E
2019	514 A	599 A	577 A	716 A	2,407 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$1.66 E	\$1.99 E	\$2.15 E	\$2.96 E	\$8.89 E
2020	\$1.15 A	\$1.47 E	\$2.15 E	\$3.31 E	\$8.05 E
2019	\$1.60 A	\$2.14 A	\$2.13 A	\$3.20 A	\$8.99 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 07/15/2020. The reports text is as of 07/16/2020.

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 (MS), liquid chromatography (LC) 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 2019, the total number of the company's sales offices stood at 56 across the world. Further, total number of field representatives were 4,000 in 2019, up from 3,900 in 2018.

Notably, the company generated \$2.4 billion of total revenues in 2019.

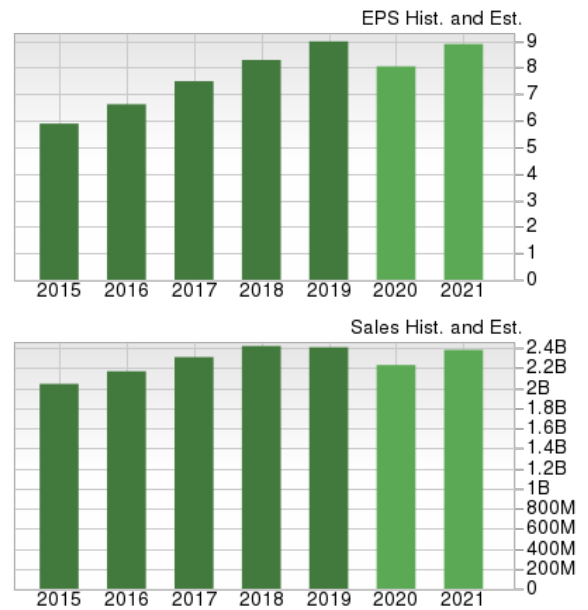
The company operates in Asia, Americas and Europe. Waters organizes its business into two operating segments: Waters Division and TA Division.

Waters Division (88.8% of total revenues in 2019) - High Performance and Ultra Performance Liquid Chromatography (HPLC and UPLC).

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 (11.2% of total revenues in 2019)- 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' key strengths include leading positions in the pharmaceutical market, broad global customer base and an impressive lineup of products. Waters remains confident that solid demand in large molecule pharma, 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' products and offerings.
- ▲ Waters has a strong presence in the chromatography instrument and pharmaceuticals markets, and expects to reap benefits 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 first-quarter 2020, the company's global pharmaceuticals business accounted for 59% 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 10% of the total revenues in the first quarter, is being driven largely by strong spending by academic institutions on biomedical research across U.S., Europe and Korea.
- ▲ Waters 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' business which has been on an uptrend lately. Going forward, Waters remains confident that its industry-leading Empower software, tailored to QDa methodologies, will offer it a distinct advantage in this high-potential product category.

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.

Reasons To Sell:

- ▼ Significant portions of Waters' 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.
- ▼ Waters' balance sheet remains highly leveraged. As of Mar 31, 2020, the company's net debt was \$1.6 billion compared with \$1.4 billion as of Dec 31, 2019. Also, debt-to-total capital was 121.1% as of Mar 31, 2020, much higher than the industry average of 53.3%. Accumulating high debt levels may impede sufficient cash flow generation, which is needed to meet future debt obligations. Moreover, this may keep the company from accessing the debt market and refinancing at suitable rates.
- ▼ Waters 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 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' business significantly by reducing the ongoing research and development activities. The company's business in Japan and China also depends largely on such funding. 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.

Waters continually grapples with currency volatility and high fixed-cost structure, which does not bode well for its revenues as well as margins. Further, high debt level remains a major headwind.

Last Earnings Report

Waters' Q1 Earnings & Revenues Miss Estimates

Waters Corporation reported first-quarter 2020 non-GAAP earnings of \$1.15 per share, which missed the Zacks Consensus Estimate by 19%. Further, the bottom line declined 28% on a year-over-year basis and 64.1% sequentially.

Net sales of \$464.9 million lagged the Zacks Consensus Estimate of \$481.3 million. The top line was down 10% from the year-ago quarter on the reported basis and 8% on constant currency basis. Further, the figure declined 35.1% from the prior quarter.

The decline can be attributed to coronavirus-induced disruptions, which led to sluggish demand in China during the reported quarter. Further, foreign currency headwinds hurt sales by 2%.

Further, softness in pharmaceutical, industrial, and academic and governmental markets remained a headwind. Further, the company encountered weakness in the Americas and Asia regions during the first quarter.

Nevertheless, Waters witnessed growth in European region during the quarter under review.

However, the company has withdrawn full-year 2020 guidance owing to uncertainty in demand environment.

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 (89.1% of net sales) generated \$414.2 million of sales, down 10% from the year-ago quarter. Sales in TA segment came in \$50.7 million and accounted for 10.9% of the net sales. The figure reflected year-over-year decline of 6%.

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

Instruments sales (38% of sales) came in \$176.9 million, down 20% on a year-over-year basis.

Service sales (41% of the sales) were \$190.8 million, declining 1% year over year.

Chemistry sales (21% of the sales) were \$97.2 million, declining 2% from the year-ago quarter.

Moreover, service and chemistry sections together generated recurring revenues of \$288 million, down 2% from the year-ago quarter.

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

Pharmaceutical market (59% of net sales) generated sales of \$272.6 million, down 7% on a year-over-year basis.

Industrial market (31% of sales) sales came in \$143.3 million, down 8% from the year-ago quarter.

Governmental & Academic (10% of sales) generated \$49 million of sales. The figure declined 24% year over year.

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

Asia (34.2% of net sales) generated \$159.1 million of sales, down 21% on a year-over-year basis. This was primarily due to softness in China where sales declined 48% from the year-ago quarter.

Americas (37% of sales) generated \$172.2 million of sales, decreasing 5% year over year. Sales in United States declined 4% year over year.

Europe (28.8% of sales) generated \$133.7 million of sales, up 2% from prior-year quarter.

Operating Details

In the first quarter, non-GAAP selling and administrative expenses were \$127.2 million, reflecting an increase of 2.4% from the year-ago quarter.

Research and development spending was \$34.9 million, indicating a decline of 0.2% from the year-ago reported figure.

Adjusted operating margin was 19.8%, which contracted 620 basis points (bps) year over year.

Balance Sheet & Cash Flow

As of Mar 28, 2020, cash, cash equivalents and investments came in \$393.9 million, higher than \$337.1 million as of Dec 31, 2019.

Further, total liabilities were \$3 billion, up from \$2.8 billion in the prior quarter.

Waters generated cash from operation of \$151.6 million in the first quarter, down from \$191.9 million in the previous quarter.

Further, free cash flow of \$121.05 million in the reported quarter.

Quarter Ending 03/2020

Report Date	Apr 28, 2020
Sales Surprise	-6.86%
EPS Surprise	-19.01%
Quarterly EPS	1.15
Annual EPS (TTM)	8.62

Outlook

Waters' cost structure is expected to realize \$100 million for the full-year 2020 owing to its current salary deduction strategy, freezing hiring and controlling non-essential operating expenses.

Further, the company has postponed capital expenditures. This along with its working capital reduction initiatives is expected to improve cash flow by \$45 million for the full year.

Additionally, it has put a halt on its share repurchase program and withdrawn previous plans to repurchase \$800 million of shares during 2020.

All these initiatives are likely to help Waters to combat COVID-19 induced crisis situation throughout 2020.

Recent News

On **Jan 13, 2020**, Waters agreed to acquire Andrew Alliance for an undisclosed amount. The acquisition will help Waters to bolster presence in the growing pharmaceutical market. The software and new technologies acquired from the deal will help Waters provide enhanced offerings to customers.

Valuation

Waters shares are down 5.5% in the year-to-date period but up 3.8% over the trailing 12-month period. While stocks in the Zacks sub-industry are down 0.7%, the same in the Zacks Computer & Technology sector are up 15% in the year-to-date period. Over the past year, the Zacks sub-industry is down 0.1% and the sector is up 26.5%.

The S&P 500 index is up 0.4% in the year-to-date period and 8.8% in the past year.

The stock is currently trading at 25.97X forward 12-month earnings, which compares to 24.81X for the Zacks sub-industry, 26.2X 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 26.87X and as low as 17.02X, with a 5-year median of 22.11X. Our Neutral recommendation indicates that the stock will perform in-line with the market. Our \$232 price target reflects 27.29X 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 F12M	Current	25.97	24.81	26.2	22.72
	5-Year High	26.87	26.74	26.2	22.72
	5-Year Low	17.02	18.41	16.72	15.25
	5-Year Median	22.11	22.49	19.33	17.52
P/S F12M	Current	5.91	5.3	3.94	3.55
	5-Year High	7.25	5.92	3.94	3.55
	5-Year Low	4.08	3.63	2.32	2.53
	5-Year Median	5.69	4.91	3.14	3.02
EV/EBITDA TTM	Current	19.07	25.27	13.06	11.88
	5-Year High	20.57	27.59	13.2	12.86
	5-Year Low	8.66	14.94	7.59	8.25
	5-Year Median	15.56	21.33	10.85	10.87

As of 07/15/2020

Industry Analysis Zacks Industry Rank: Top 11% (27 out of 251)



Top Peers

Company (Ticker)	Rec	Rank
Thermo Fisher Scientific Inc. (TMO)	Outperform	1
Agilent Technologies, Inc. (A)	Neutral	3
BioRad Laboratories, Inc. (BIO)	Neutral	3
Bruker Corporation (BRKR)	Neutral	2
Danaher Corporation (DHR)	Neutral	3
General Electric Company (GE)	Neutral	4
MettlerToledo International, Inc. (MTD)	Neutral	3
PerkinElmer, Inc. (PKI)	Neutral	1

Industry Comparison Industry: Instruments - Scientific				Industry Peers		
	WAT	X Industry	S&P 500	A	GE	MTD
Zacks Recommendation (Long Term)	Neutral	-	-	Neutral	Neutral	Neutral
Zacks Rank (Short Term)	4	-	-	3	4	3
VGM Score	D	-	-	A	F	D
Market Cap	13.67 B	250.70 M	22.66 B	28.68 B	62.45 B	20.78 B
# of Analysts	7	6	14	6	8	5
Dividend Yield	0.00%	0.00%	1.83%	0.78%	0.56%	0.00%
Value Score	D	-	-	C	C	F
Cash/Price	0.03	0.07	0.07	0.05	1.53	0.02
EV/EBITDA	18.25	14.43	12.99	23.67	3.58	27.20
PEG Ratio	2.70	4.98	2.97	2.98	48.82	6.83
Price/Book (P/B)	NA	2.49	3.12	6.01	1.69	67.81
Price/Cash Flow (P/CF)	19.82	16.53	12.14	23.43	5.53	32.20
P/E (F1)	28.07	32.46	22.04	29.83	219.69	41.43
Price/Sales (P/S)	5.80	2.81	2.38	5.48	0.63	6.98
Earnings Yield	3.65%	3.15%	4.32%	3.35%	0.42%	2.41%
Debt/Equity	-5.65	0.79	0.76	0.38	1.80	4.94
Cash Flow (\$/share)	11.14	1.81	6.94	3.96	1.29	26.99
Growth Score	C	-	-	B	F	C
Hist. EPS Growth (3-5 yrs)	10.39%	10.86%	10.85%	14.42%	-21.62%	15.15%
Proj. EPS Growth (F1/F0)	-10.47%	-8.09%	-9.64%	0.11%	-95.00%	-7.89%
Curr. Cash Flow Growth	-4.57%	7.99%	5.51%	9.85%	-8.00%	7.99%
Hist. Cash Flow Growth (3-5 yrs)	5.07%	8.45%	8.55%	-2.46%	-12.27%	9.94%
Current Ratio	2.41	2.05	1.30	1.63	1.91	1.77
Debt/Capital	NA%	42.93%	44.46%	27.27%	64.30%	83.16%
Net Margin	22.77%	2.59%	10.59%	13.04%	-2.39%	18.38%
Return on Equity	1,937.83%	5.68%	15.75%	20.76%	13.66%	134.62%
Sales/Assets	0.89	0.78	0.54	0.57	0.36	1.09
Proj. Sales Growth (F1/F0)	-7.35%	0.00%	-2.52%	0.82%	-24.39%	-6.36%
Momentum Score	C	-	-	A	F	C
Daily Price Chg	11.48%	3.24%	1.91%	2.41%	3.78%	2.32%
1 Week Price Chg	4.39%	3.99%	-0.41%	0.83%	-1.91%	0.55%
4 Week Price Chg	17.14%	7.59%	1.88%	5.64%	-1.38%	11.08%
12 Week Price Chg	16.00%	22.68%	16.37%	23.56%	11.04%	23.41%
52 Week Price Chg	3.75%	4.99%	-4.22%	33.47%	-28.46%	6.22%
20 Day Average Volume	883,436	119,585	2,266,132	1,391,605	77,074,736	107,392
(F1) EPS Est 1 week change	0.00%	0.00%	0.00%	0.00%	-21.21%	0.00%
(F1) EPS Est 4 week change	-0.48%	0.29%	0.00%	0.16%	-21.21%	0.00%
(F1) EPS Est 12 week change	-6.68%	-7.26%	-5.76%	0.63%	-91.42%	-7.85%
(Q1) EPS Est Mthly Chg	0.00%	0.00%	0.00%	0.22%	-44.44%	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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