

Woodward, Inc. (WWD)

\$74.71 (As of 08/04/20)

Price Target (6-12 Months): **\$64.00**

Long Term: 6-12 Months

Zacks Recommendation: Underperform

(Since: 08/04/20)

Prior Recommendation: Neutral

Short Term: 1-3 Months

Zacks Rank: (1-5)

5-Strong Sell

Zacks Style Scores:

VGM:A

Value: B

Growth: B

Momentum: B

Summary

Due to economic disruptions related to the COVID-19 pandemic, Woodward withdrew its guidance for fiscal 2020. The company faces demand-related challenges in the industrial gas and turbine market, thanks to higher penetration and greater energy efficiency of renewables. The Industrial segment is facing headwinds stemming from weakness in oil and gas markets as well as the impact of the pandemic on China's natural gas trucks. The availability of new products and services along with changes in OEM might hamper Woodward's relationship with clients. It has a significant presence in the commercial aerospace market, which is cyclical. It faces intense competition from several players. However, the company continues to see momentum in the Aerospace business driven by sales growth across commercial OEM and defense aftermarket.

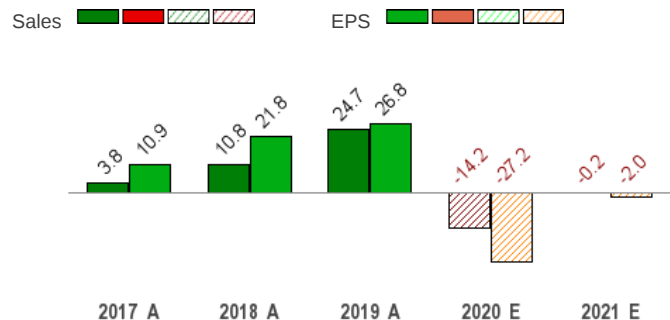
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$129.06 - \$46.51
20 Day Average Volume (sh)	363,169
Market Cap	\$4.6 B
YTD Price Change	-36.9%
Beta	1.49
Dividend / Div Yld	\$0.32 / 0.4%
Industry	Instruments - Control
Zacks Industry Rank	Bottom 9% (232 out of 254)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	64.3%
Last Sales Surprise	4.3%
EPS F1 Est- 4 week change	-0.4%
Expected Report Date	08/06/2020
Earnings ESP	-26.9%

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021					2,482 E
2020	720 A	720 A	513 E	534 E	2,488 E
2019	653 A	759 A	752 A	737 A	2,900 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$0.51 E	\$0.65 E	\$0.59 E	\$0.66 E	\$3.48 E
2020	\$1.10 A	\$1.61 A	\$0.34 E	\$0.49 E	\$3.55 E
2019	\$0.96 A	\$1.40 A	\$1.30 A	\$1.22 A	\$4.88 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 08/04/2020. The reports text is as of 08/05/2020.

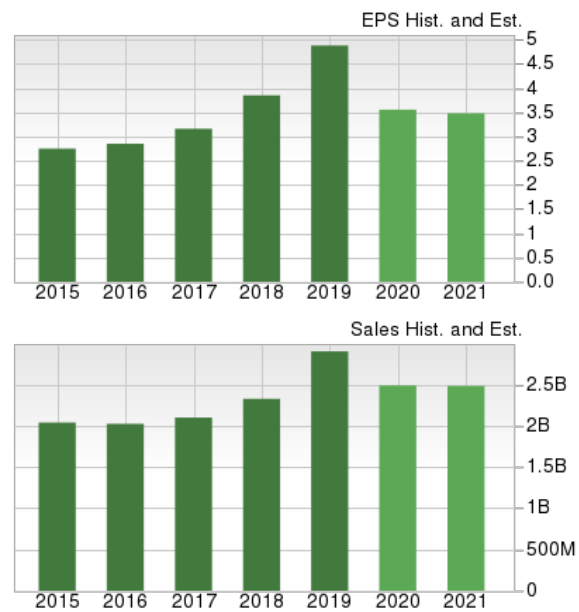
Overview

Headquartered in Fort Collins, CO, Woodward, Inc. is an independent designer, manufacturer and service provider of energy control and optimization solutions. The company provides a wide array of products for fuel, combustion, fluid, actuation and electronic applications, which serve the commercial aerospace, business jet, military and energy markets. Apart from serving Original Equipment Manufacturers (OEMs), it also engages in aftermarket repairs, replacements and other service support operations.

Woodward serves the aerospace and energy markets through two reportable segments: Aerospace and Industrial. Both segments have multiple business groups under them.

The Aerospace segment consists of the Aircraft Turbine Systems and the Airframe Systems business groups. This segment is mainly involved in the production, designing and servicing of products for the management of fuel, air, combustion and motion. The products developed at this segment, including pumps, cockpit controls, motors and sensors, are used by commercial aircraft manufacturers like The Boeing Company and General Dynamics Corp. They are also used in military aircraft and defense systems. This segment generated revenues of \$474 million in second-quarter fiscal 2020, representing 65.8% of total revenues.

The Industrial segment consists of the Industrial Turbo Machinery Systems, and the Engine Systems and Electrical Power Systems business groups. This segment produces power converters, ignition systems and injectors among others and generates revenues mainly from OEMs through aftermarket sales. This segment generated revenues of \$246 million in second-quarter fiscal 2020, representing 34.2% of total revenues.



Reasons To Sell:

- ▼ Within the power generation market, Woodward is witnessing demand-related challenges in the industrial gas and turbine market as well as a drop in volume tied to renewables penetration and greater energy efficiency. The weakness in the company's renewables business is due to the short-term unfavorable impact of platform transitions by some of its customers. With no notable improvement expected in these aspects before 2020, Woodward is projected to perform poorly in power generation market.
- ▼ Woodward has a significant presence in the commercial aerospace market, which is cyclical in nature. It also faces intense competition from a number of major players in the United States and abroad. Changes in competitive conditions, including factors like the availability of new products and services, introduction of new channels of distribution and changes in OEM and aftermarket pricing will likely hamper its association with clients and affect sales. For the near term, it expects softness in the regional aircraft.
- ▼ Woodward caters to fewer customers compared to companies with similar sales volume. Around 45% of the company's annual consolidated net sales come from its five largest customers. Therefore, loss of any one of its significant customers will have a material impact on its operational results. Woodward also faces the risk of third-party payments, which may hamper credit availability for further product offerings. Moreover, as the company caters to international customers, it is subject to risks arising from fluctuations in foreign exchange rates.
- ▼ Due to global uncertainty, Woodward has withdrawn its fiscal 2020 guidance. In second-quarter fiscal 2020, Woodward's Industrial sales were down 10.9% year over year. The downside was caused by weakness in oil and gas markets and the impact of COVID-19 on China's natural gas trucks. The segment's earnings were \$26 million, down 3.7% from \$27 million in the year-ago quarter primarily due to lower sales volume. The Zacks Consensus Estimate for the company's current-year earnings has been revised 0.6% downward in the past 30 days to \$3.55.

Woodward is likely to face challenges in the power generation market due to short-term headwinds. Softness in the regional aircraft business remains another concern.

Risks

- Despite the Boeing 737 MAX production halt, Woodward's Aerospace segment is expected to deliver strong performance, driven by strong flight utilization trends, sustained global passenger growth and higher defense spending. In the Industrial markets, while the industrial turbine market remains uncertain, the company is witnessing robust growth in distributed power for data center applications. Woodward L'Orange is likely to continue to enhance its Industrial segment with respect to both sales and earnings. It is well positioned to capitalize on the near-term production ramp-up along with opportunities that lies ahead.
 - Woodward has been investing significantly in technologies in order to secure fresh businesses. It is spending on new manufacturing units and automation equipment to perk up efficiency as the company intends to accelerate production. Woodward continues to focus on diversifying its revenue stream. Its strategic plan to become a systems integrator has increased contract flow substantially enabling it to capture a larger market share in the wide-body commercial aircraft field. Notably, the commercial aerospace market is expanding substantially, driven by record passenger and cargo traffic and ongoing elevated load factors. Increased production in this space has been observed as aircraft operators continue to take delivery of new aircraft models that are more fuel efficient and retire older. Driven by the strong demand for smart weapons, it is witnessing continued increase in defense sales that's coming from both domestic as well as foreign military sales.
 - Woodward's Aerospace business performed well in the first quarter on broad-based sales growth across commercial OEM and defense aftermarket. Momentum within its defense OEM business also remained strong, supported by guided weapon sales as well as fixed-wing, rotorcraft and ground programs. The acquisition of L'Orange, a supplier of fuel injection systems for industrial diesel, heavy fuel oil and dual-fuel, expanded its footprint in the OEM market. The buyout enhanced Woodward's product portfolio as well as extended its presence in key end markets. The company has been shifting resources from its industrial market to support new activity in aerospace. Overall, the aerospace industry is reflecting solid growth prospects driven by continued improvement in the business jet and rotorcraft markets. Also, global uncertainty continues to drive increased defense activity, which in turn will likely boost Woodward's top line.
 - As of Mar 31, 2020, the company had \$103 million in cash and cash equivalents with \$869 million of long-term debt compared with the respective tallies of \$148 million and \$729 million at the end of the prior quarter. Woodward currently has a debt-to-capital ratio of 0.36 compared with 0.51 of the sub-industry. The times interest earned (TIE) ratio has improved steadily over the past quarters to 9.8 at present compared with 3.7 of the sub-industry. This suggests that the company is more likely to meet its debt obligations. Woodward has a dividend payout rate of 14.7% compared with 9.3% of the sub-industry. The rate has also increased over the past quarters, indicating that the company is sharing more of its earnings with stockholders. It is to be seen whether Woodward can maintain the momentum in the coming days amid disruptions caused by the COVID-19 crisis.
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Last Earnings Report

Woodward Tops Q2 Earnings Estimates, Withdraws Guidance

Woodward reported healthy second-quarter fiscal 2020 results, with the bottom and the top line beating the respective Zacks Consensus Estimate.

The results were largely in line with the company's expectations cited before it began to experience disruptions related to COVID-19. Due to global uncertainty, Woodward has withdrawn its fiscal 2020 guidance.

Quarter Ending **03/2020**

Report Date	May 04, 2020
Sales Surprise	4.31%
EPS Surprise	64.29%
Quarterly EPS	1.61
Annual EPS (TTM)	5.23

Net Income

On a GAAP basis, net earnings in the fiscal second quarter amounted to \$91.3 million or \$1.41 per share compared with \$77.6 million or \$1.20 per share in the year-ago quarter. The improvement was primarily driven by lower expenses.

Quarterly adjusted net earnings were \$104 million or \$1.61 per share compared with \$90 million or \$1.40 per share in the prior-year quarter. The bottom line beat the Zacks Consensus Estimate by 63 cents.

Revenues

Net sales in the March quarter fell 5.1% year over year to \$720.2 million due to lower sales in the Aerospace and Industrial segments. However, the top line surpassed the consensus estimate of \$704 million.

Segment Results

Aerospace: Net sales fell 1.9% year over year to \$474 million, primarily due to the Boeing 737 MAX production halt and related lower initial provisioning. However, the defense continued to perform well in both OEM and aftermarket on strong demand for Woodward programs. The segment's earnings were \$118 million, up 15.7% from \$102 million in the year-ago quarter. The upside can be attributed to the elimination of the annual bonus for 2020, which was partially offset by lower sales volume.

Industrial: Net sales totaled \$246 million, down 10.9% year over year. The downside was caused by weakness in oil and gas markets and the impact of COVID-19 on China's natural gas trucks. This was partially offset by improvements in gas turbines and renewable power. The segment's earnings were \$26 million, down 3.7% from \$27 million in the year-ago quarter primarily due to lower sales volume.

Other Details

Total expenses declined to \$613 million from \$668.7 million year over year primarily due to lower cost of goods sold.

On Apr 6, Woodward announced the mutual termination of its merger with Hexcel. The decision was made in the spirit of doing what's best for individual businesses with a focus on managing through this unprecedented crisis. It also decided to shift Bob Weber back to the role of vice chairman and chief financial officer.

On Apr 30, the company closed the previously-announced divestiture of its renewable power systems and related businesses.

Cash Flow & Liquidity

In the first six months of fiscal 2020, Woodward generated \$52.2 million of net cash from operations compared with \$141 million in the year-ago period. Free cash flow for the first half of fiscal 2020 was \$23 million compared with \$87 million in the prior-year period, attributable to higher working capital.

As of Mar 31, the company had \$102.8 million in cash and equivalents with \$869.2 million of long-term debt (less current portion).

Recent News

On Apr 30, 2020, Woodward announced that it has closed the previously-announced divestiture of its renewable power systems and related businesses.

On Apr 13, Woodward communicated its decision to shift Bob Weber back to the role of vice chairman and chief financial officer.

On Apr 6, Woodward announced the mutual termination of its merger with Hexcel. The decision was made in the spirit of doing what's best for individual businesses with a focus on managing through this unprecedented crisis.

Valuation

Woodward shares are down 28.9% over the trailing 12-month period. Stocks in the Zacks sub-industry are down 15.5% over the past year, but stocks in the Zacks Computer and Technology sector are up 37.2% in the same period.

The S&P 500 Index is up 14.7% in the past year.

The stock is currently trading at 8.79X trailing 12-month EV/EBITDA, which compares to 9X for the Zacks sub-industry, 13.6X for the Zacks sector and 12.76X for the S&P 500 Index.

Over the past five years, the stock has traded as high as 19.12X and as low as 6.51X, with a 5-year median of 14.26X. Our Underperform recommendation indicates that the stock will perform worse than the market. Our \$64 price target reflects 2.99X forward 12-month earnings.

The table below shows summary valuation data for WWD

Valuation Multiples - WWD					
		Stock	Sub-Industry	Sector	S&P 500
EV/EBITDA TTM	Current	8.79	9	13.6	12.76
	5-Year High	19.12	12.91	13.6	12.85
	5-Year Low	6.51	6.78	7.59	8.24
	5-Year Median	14.26	11.34	10.89	10.89
P/E F12M	Current	21.41	20.36	26.41	22.58
	5-Year High	25.73	20.55	26.41	22.58
	5-Year Low	9.3	12.28	16.72	15.25
	5-Year Median	19.33	15.7	19.47	17.55
P/S F12M	Current	1.87	2.11	4.07	3.6
	5-Year High	2.59	2.42	4.07	3.6
	5-Year Low	1.05	1.53	2.32	2.53
	5-Year Median	1.93	2.03	3.14	3.04

As of 08/04/2020

Industry Analysis Zacks Industry Rank: Bottom 9% (232 out of 254)



Top Peers

Company (Ticker)	Rec	Rank
Allied Motion Technologies, Inc. (AMOT)	Neutral	3
Roper Technologies, Inc. (ROP)	Neutral	3
Sensata Technologies Holding N.V. (ST)	Neutral	3
Thermon Group Holdings, Inc. (THR)	Neutral	3
Transcat, Inc. (TRNS)	Neutral	3
Watts Water Technologies, Inc. (WTS)	Neutral	3
Xylem Inc. (XYL)	Neutral	3
Badger Meter, Inc. (BMI)	Underperform	5

Industry Comparison Industry: Instruments - Control				Industry Peers		
	WWD	X Industry	S&P 500	BMI	ST	WTS
Zacks Recommendation (Long Term)	Underperform	-	-	Underperform	Neutral	Neutral
Zacks Rank (Short Term)	5	-	-	5	3	3
VGM Score	A	-	-	B	C	D
Market Cap	4.65 B	376.05 M	22.75 B	1.86 B	6.13 B	2.93 B
# of Analysts	5	3	14	2	8	8
Dividend Yield	0.44%	0.00%	1.76%	1.06%	0.00%	1.06%
Value Score	B	-	-	D	A	D
Cash/Price	0.02	0.09	0.07	0.05	0.21	0.09
EV/EBITDA	10.69	10.93	13.09	20.69	9.98	12.03
PEG Ratio	1.54	3.70	2.95	NA	2.03	3.70
Price/Book (P/B)	2.44	2.45	3.16	5.47	2.46	2.97
Price/Cash Flow (P/CF)	10.12	14.13	12.32	26.14	7.36	15.83
P/E (F1)	21.05	29.62	21.81	42.69	22.39	29.62
Price/Sales (P/S)	1.59	1.53	2.46	4.48	2.01	1.93
Earnings Yield	4.75%	3.38%	4.40%	2.34%	4.46%	3.38%
Debt/Equity	0.46	0.36	0.76	0.00	1.30	0.27
Cash Flow (\$/share)	7.38	2.22	6.94	2.45	5.30	5.48
Growth Score	B	-	-	A	D	D
Hist. EPS Growth (3-5 yrs)	17.00%	12.85%	10.46%	13.89%	5.10%	13.92%
Proj. EPS Growth (F1/F0)	-27.17%	-28.79%	-7.16%	-6.83%	-51.05%	-28.01%
Curr. Cash Flow Growth	26.08%	4.02%	5.47%	3.00%	-3.40%	5.03%
Hist. Cash Flow Growth (3-5 yrs)	13.42%	6.29%	8.55%	8.54%	5.87%	6.29%
Current Ratio	2.25	3.10	1.32	3.56	2.46	2.39
Debt/Capital	31.30%	26.17%	44.36%	0.00%	56.58%	21.04%
Net Margin	9.48%	4.35%	10.25%	11.15%	2.96%	7.67%
Return on Equity	18.93%	12.09%	14.67%	13.93%	15.56%	13.15%
Sales/Assets	0.73	0.81	0.51	0.97	0.44	0.89
Proj. Sales Growth (F1/F0)	-14.22%	-5.53%	-1.71%	-5.24%	-18.74%	-10.79%
Momentum Score	B	-	-	B	F	B
Daily Price Chg	-0.92%	0.15%	0.42%	-0.03%	0.85%	0.93%
1 Week Price Chg	-6.34%	-0.72%	0.14%	-0.89%	-6.04%	-0.55%
4 Week Price Chg	-0.56%	9.03%	4.97%	1.06%	8.15%	9.90%
12 Week Price Chg	30.91%	12.98%	15.30%	13.02%	12.75%	15.46%
52 Week Price Chg	-28.95%	0.29%	2.34%	19.23%	-14.41%	-6.27%
20 Day Average Volume	363,169	79,818	2,082,836	149,681	1,427,013	136,722
(F1) EPS Est 1 week change	0.00%	0.00%	0.00%	0.00%	-1.69%	0.00%
(F1) EPS Est 4 week change	-0.43%	0.00%	0.93%	-5.36%	-0.14%	2.49%
(F1) EPS Est 12 week change	-2.41%	-5.36%	0.78%	-5.36%	-0.14%	-19.73%
(Q1) EPS Est Mthly Chg	-1.62%	-1.62%	0.17%	-3.75%	-2.27%	3.30%

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	B
Momentum Score	B
VGM Score	A

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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