



Nordson Corporation (NDSN)

Updated July 8th, 2018 by Josh Arnold

Key Metrics

Current Price: \$129	5 Year CAGR Estimate: 6.2%	Quality Percentile: 78.6%
Fair Value Price: \$107	5 Year Growth Estimate: 9.0%	Momentum Percentile: 49.1%
% Fair Value: 121%	5 Year Valuation Multiple Estimate: -3.7%	Valuation Percentile: 25.4%
Dividend Yield: 0.9%	5 Year Price Target \$164	Total Return Percentile: 36.6%

Overview & Current Events

Nordson, in its current form, was founded in 1954 but can trace its roots all the way back to 1909. The company's many decades of experience in solving the world's engineering problems has allowed it to grow to a \$7.5 billion market cap. It makes a wide assortment of products for industrial applications, boasting a diverse and deep customer base.

Nordson's second quarter earnings report was quite strong but was completely overshadowed by weak third quarter guidance. Revenue was up 12% during the second quarter and operating profit surged 22% against the comparable quarter last year. Its long history of acquiring growth, it would seem, is alive and well. However, Nordson guided for sales growth in the third quarter to be in the range of -3% to +1% and for earnings-per-share to be just \$1.47 to \$1.63 against consensus of \$1.91. That reduction in guidance has caused us to reduce our 2018 estimate for earnings-per-share commensurately.

Growth on a Per-Share Basis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
EPS	\$1.77	\$1.20	\$2.24	\$3.27	\$3.45	\$3.42	\$3.84	\$3.58	\$4.68	\$5.37	\$6.05	\$9.30
DPS	\$0.37	\$0.37	\$0.39	\$0.44	\$0.53	\$0.63	\$0.80	\$0.90	\$0.99	\$1.11	\$1.20	\$2.10

Earnings-per-share has been somewhat unpredictable in the past decade, but more recently Nordson has produced prodigious levels of growth. Nordson has been able to produce an average of 4% organic revenue growth annually in this time frame, but its acquisitions have provided the bulk of top line growth. Its operating margins have moved higher as acquisitions are fully integrated; gross margins have remained basically flat, however, so they are not an earnings driver.

We are forecasting 9% annual earnings-per-share growth as Nordson's fundamentals are well intact. Organic growth, combined with more acquisitions, should produce mid-single digit sales growth or higher, depending upon sizing and timing of future acquisitions. The balance of Nordson's earnings growth will come from continued operating margin expansion as the company's track record with integrating acquisitions is tremendous. Finally, Nordson buys back stock from time to time, although there is no steady cadence. Given that the weak guidance for Q3 was due to tough comparables and not diminishing fundamentals, we haven't reduced our forward growth estimate of 9%.

We are also forecasting continued double-digit growth for the dividend, creating a payout in excess of \$2 per share in five years. The priority is growth via acquisitions, so the yield isn't expected to be a significant driver of total returns.

Valuation Analysis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	Now	2023
Avg. P/E	16.1	16.1	14.5	14.7	15.0	20.0	19.5	21.0	17.0	22.0	21.3	17.6
Avg. Yld.	1.3%	1.9%	1.2%	0.9%	1.0%	0.9%	1.1%	1.2%	1.2%	0.9%	0.9%	1.3%

Nordson's growth has picked up in recent years and as a result, its valuation has as well. That led to enormous returns for shareholders in 2016 and 2017 but we are forecasting the price-to-earnings ratio falling back to more normalized levels over the next few years. That would create a 3.7% annualized headwind to total returns for shareholders from current levels as the stock looks meaningfully overvalued here. Although the stock has sold off since the second quarter report, the valuation is nearly identical to what it was before the report. The stock, therefore, is less costly as a result of the lower share price, but not less expensive.

Given that the valuation should drift lower over time while the payout grows, we are forecasting the dividend yield to rise to 1.3% in five years. As we said, Nordson isn't a high-yield stock and likely never will be, but the payout does grow at respectable rates, and that should continue.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
GP/A	56.0%	57.2%	59.7%	60.7%	58.4%	56.1%	55.5%	54.1%	54.9%	55.1%	55.0%	55.5%
Debt/A	51%	58%	49%	56%	63%	57%	60%	72%	65%	66%	62%	59%
Int. Cov.	12.7	---	43.6	71.0	31.6	22.6	25.4	18.2	18.9	12.9	15.0	20.0
Payout	20%	31%	17%	13%	15%	18%	20%	25%	21%	20%	20%	23%
Std. Dev.	66.7%	50.3%	34.8%	68.0%	28.7%	22.7%	20.3%	22.9%	30.6%	24.7%	25.0%	25.0%

Nordson's quality metrics have been fairly stable over the past decade, although debt has drifted higher. Nordson's financing strategy is still reasonably conservative, but it often assumes debt for acquisitions. The company's current leverage is near its historical highs but as it digests its FY2017 acquisitions, debt should drift lower over time and with it, interest coverage should improve. The payout ratio should remain about the same as well, around 20% of earnings.

Nordson's main competitive advantage is in its enormous installed base of customers around the world. The company provides niche, but critical, pieces involved in myriad manufacturing processes. Thus, it is difficult for competitors to supplant its position. That doesn't mean Nordson is immune to recessions, however, as it struggled mightily during the Great Recession. Nordson is beholden to the world economy and investors should not overlook that fact.

Final Thoughts & Recommendation

Overall, Nordson still looks overvalued here but the company's growth prospects are hard to ignore. We think shareholders will see total annual returns of 6.2%, comprised of the current 0.9% yield, a 3.7% headwind from the price-to-earnings falling and a 9% annual EPS growth rate. Nordson will never be a high-yield stock so it isn't suitable for income investors. At its current premium over fair value, it isn't particularly enticing for growth or value investors either. Those wanting to own Nordson should wait for the valuation to come down and enter at a better price.

Total Return Breakdown by Year

