Emerson Electric Company (EMR)

Updated April 10th, 2018 by Josh Arnold

Key Metrics

Current Price:	$66	**5 Year CAGR Estimate:**	4.4%	**Quality Percentile:**	N/A
Fair Value Price:	$55	**5 Year Growth Estimate:**	5.0%	**Momentum Percentile:**	N/A
% Fair Value:	120%	**5 Year Valuation Multiple Estimate:**	-3.5%	**Total Return Percentile:**	N/A
Dividend Yield:	2.9%	**5 Year Price Target**	$71	**Valuation Percentile:**	N/A

Overview & Current Events

Emerson Electric was founded in Missouri in 1890 and since that time, it has evolved through organic growth and strategic acquisitions and divestitures from a regional manufacturer of electric motors and fans into a $42B diversified global leader in technology and engineering. The company serves manufacturing customers all around the world.

Emerson's Q1 was outstanding as it produced 19% total sales growth comprised of 12% from acquisitions and divestitures and 7% in organic sales growth. Adjusted EBIT margin rose as well but on a reported basis, fell due to dilution from the company's recent Valves & Controls acquisition. Emerson saw fit to substantially raise guidance for this year after Q1 as growth is looking up on organic revenue growth and share repurchases. Margins have been a bit of a struggle recently for Emerson but sales growth like what we saw in Q1 has been enough.

Growth on a Per-Share Basis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
EPS	$3.11	$2.27	$2.60	$3.24	$2.67	$3.54	$3.75	$3.17	$2.46	$2.54	***$3.10***	***$3.95***
DPS	$1.20	$1.33	$1.34	$1.38	$1.60	$1.66	$1.72	$1.88	$1.90	$1.92	***$1.94***	***$2.15***

Emerson's EPS has been all over the place during the past decade as we've seen meaningful swings in both directions. Indeed, estimates for earnings this year are right in line with what the company produced in 2008, highlighting that EPS growth is highly uncertain with Emerson. The majority of Emerson's revenue is exposed to the oil and gas industry so revenue and margins move around a lot, and not always in the right direction. That means forward projections are always at risk for Emerson as visibility in the out years is limited. That said, we are forecasting 5% annual growth for the next five years as the company's low single digit organic growth is coupled with acquisitions to fuel top line expansion. Margins are expected to rise slightly from where they are now and EPS will be further fueled by a small amount of share repurchases.

The dividend is also expected to grow in the low single digits as recent years have seen Emerson focus more on acquisitions and share repurchases than growing the dividend. Weak EPS expansion lately has led to a higher-than-normal payout ratio for Emerson and we are forecasting that this will fall back towards the historical mean from currently elevated levels. Dividend growth likely will not be significant for the foreseeable future.

Valuation Analysis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	Now	2023
Avg. P/E	16.6	14.8	17.8	16.8	18.3	15.8	17.6	18.0	20.6	22.9	***21.4***	***17.9***
Avg. Yld.	2.3%	3.9%	2.9%	2.5%	3.3%	3.0%	2.6%	3.3%	3.8%	3.3%	***2.9%***	***3.0%***

Emerson's PE has risen markedly in the past few years despite the fact that its earnings have bounced around a lot. This has created a situation where its current PE is well in excess of historical norms and thus, the stock appears to be overvalued. When you add in that its forward estimates are subject to significant risk, the idea that the PE should come back down to prior levels has more credence. Emerson's exposure to oil and gas remains a primary risk in estimates. We are thus forecasting a 3.5% annual headwind to total returns as the PE should come back down to 18 or so.

We are also forecasting that the yield will rise slightly from current levels to 3.0% as the stock struggles to move higher on tame earnings growth, and as dividend growth rates are expected to remain very low.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
GP/A	36.8%	36.1%	39.6%	39.5%	40.0%	40.3%	31.6%	31.4%	43.1%	42.0%	***42.5%***	***43.0%***
Debt/A	57%	57%	57%	56%	57%	57%	58%	63%	65%	55%	***55%***	***55%***
Int. Cov.	20.4	12.1	12.0	17.4	15.0	15.7	17.4	22.9	13.5	15.4	***15.8***	***16.2***
Payout	38%	58%	51%	42%	60%	46%	61%	60%	77%	75%	***63%***	***54%***
Std. Dev.	53.7%	37.3%	27.5%	34.2%	20.9%	17.5%	17.5%	22.3%	22.8%	17.0%	***22.0%***	***27.0%***

Emerson's quality metrics are strong and have improved somewhat in recent years. Margins have been roughly flat since 2016 but should rise slightly in the coming years as Emerson digests its recent acquisitions and divestitures and moves past related costs. Just over half of its assets are financed by debt and its interest coverage is very strong, so there are no financing concerns to speak of. This will allow Emerson to complete more acquisitions should the need arise without undue stress on the balance sheet. The payout ratio has grown significantly in recent years but should begin to fall in 2018 and beyond back to historical norms. Emerson's spotty EPS record saw the payout ratio rise significantly but stronger EPS growth forecasts and slow dividend growth should help rectify that problem.

Emerson's competitive advantage is in its many decades of experience in building customer relationships and engineering excellence. It has a global customer base that is seeing strong economic growth and that underlying sales tailwind should power results going forward.

Final Thoughts & Recommendation

With the stock looking expensive at 120% of fair value, Emerson should deliver only 4.4% total returns going forward. This will be comprised of the 2.9% current yield, EPS growth of 5.0% and a 3.5% headwind from the valuation. With low EPS and dividend growth and an expensive valuation, Emerson does not look attractive here. It would be suitable for those seeking a high current yield but those looking for high rates of earnings growth, dividend growth or value should pass on Emerson.

Total Return Breakdown by Year