



Praxair Inc. (PX)

Updated April 10th, 2018 by Nick McCullum

Key Metrics

Current Price: \$147	5 Year CAGR Estimate: 5.1%	Quality Percentile: N/A
Fair Value Price: \$125	5 Year Growth Estimate: 6.0%	Momentum Percentile: N/A
% Fair Value: 118%	5 Year Valuation Multiple Estimate: -3.2%	Total Return Percentile: N/A
Dividend Yield: 2.3%	5 Year Price Target \$167	Valuation Percentile: N/A

Overview & Current Events

Praxair Inc. is one of the world's largest industrial gas corporations. The company produces, sells, and distributes atmospheric, process, and specialty gases, along with high-performance surface coatings. Praxair trades with a market capitalization of \$42 billion and generates sales of \$11 billion in its most recent fiscal year. With 25 consecutive years of dividend increases, Praxair qualifies to be a member of the Dividend Aristocrats Index.

In late January, Praxair reported (1/25/18) financial results for the fourth quarter of fiscal 2018. Quarterly sales increased by 12% year-on-year while adjusted earnings-per-share increased by 8%. For the twelve-month reporting period, sales increased by 9% and adjusted earnings-per-share increased by 7%. Praxair's strong performance was driven by progress on its project backlog and several new onsite projects.

Growth on a Per-Share Basis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
EPS	\$4.19	\$4.01	\$3.84	\$5.45	\$5.61	\$5.87	\$5.73	\$5.35	\$5.21	\$5.68	\$6.02	\$8.06
DPS	\$1.50	\$1.60	\$1.80	\$2.00	\$2.20	\$2.40	\$2.60	\$2.86	\$3.00	\$3.15	\$3.40	\$4.55

Praxair has compounded its adjusted earnings-per-share at a rate of 3.4% per year since 2008. We believe that this historical growth rate downplays the company's future growth prospects. Praxair is likely to deliver 6% annualized growth for the foreseeable future. A 6% annualized rate of earnings growth gives a 2018 earnings-per-share estimate of \$6.02 and a 2023 earnings-per-share estimate of \$8.06.

Praxair's future growth will be driven by its pending merger with Linde AG, a German multinational chemical company. This merger, which was announced (7/1/2017) last summer, combines Linde's long-standing leadership in engineering and technology with Praxair's operational excellence. The transaction is expected to generate \$1.2 billion in annual cost synergies, creating a company with approximately \$29 billion of revenues and a current market value in excess of \$70 billion. The merger is all-stock in nature, with current Linde shareholders receiving 1.54 shares in the new holding company for each Linde shares and Praxair investors receiving the new stock on a one-for-one basis. The combined company will be named Linde and will be cross-listed on both the New York Stock Exchange and the Frankfurt Stock Exchange. Praxair continues to believe that the merger will close in the second half of fiscal 2018.

Valuation Analysis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	Now	2023
Avg. P/E	19.3	18.2	22.0	18.4	19.3	20.0	22.6	21.7	21.8	23.2	24.4	20.7
Avg. Yld.	1.9%	2.2%	2.1%	2.0%	2.0%	2.0%	2.0%	2.5%	2.6%	2.4%	2.3%	2.6%

Praxair has traded at an average price-to-earnings ratio of 20.7 over the last decade. Using our fiscal 2018 earnings-per-share estimate of \$6.02, the company is currently priced at an earnings multiple of 24.4, potentially due to excitement surrounding the aforementioned merger with Linde AG. If the company reverts to 20.7x earnings over the next 5 years, this will reduce its annualized returns by 3.2% during this time period.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
GP/A	32.9%	27.4%	28.6%	29.3%	26.7%	25.6%	26.9%	26.3%	24.2%	24.4%	25.0%	25.0%
Debt/A	69.3%	62.9%	62.1%	66.4%	66.5%	67.4%	71.6%	76.0%	74.0%	70.6%	70.0%	65.0%
Int. Cov.	9.5	11.8	16.7	15.5	17.3	14.7	14.5	14.4	12.8	15.2	14.0	15.0
Payout	35.8%	39.9%	46.9%	36.7%	39.2%	40.9%	45.4%	53.5%	57.6%	55.5%	56.5%	56.5%
Std. Dev.	56.1%	32.7%	19.2%	25.0%	16.8%	13.6%	14.7%	17.5%	18.7%	14.3%	18.0%	18.0%

Praxair scores well on a number of quality metrics. The company has consistently been able to generate more than ten times in interest expense in operating earnings, and its balance sheet employs a level of leverage that we believe is reasonable given the consistency inherent in its business model. Although Praxair's dividend has steadily climbed over the last decade, the company's dividend payout ratio is still at a level that will support additional dividend growth if earnings stagnate temporarily.

Qualitatively, Praxair's most compelling competitive advantage is the company's global scale. The company worldwide operating footprint gives it a breadth of service offerings that are unmatched by the majority of its competitors, making switching costs high for Praxair's customers. In addition, industrial gas companies have high switching costs in general. It is difficult for Praxair's customers to find a new supplier with the same offerings in a particular geography, which makes the company's entrenched industry positioning even more powerful. Importantly, these scale-based competitive advantages will become even stronger when the Linde merger is completed.

Final Thoughts & Recommendation

Praxair's entrenched position in the industrial gas sector gives it a strong and durable competitive advantage. Moreover, the company's multi-decade streak of consecutive dividend increases shows that it is willing and able to prioritize its return of capital to shareholders.

Unfortunately, the company is trading at a premium to its long-term historical valuation multiples. This will introduce meaningful headwinds to Praxair's future total returns. With ~5% annualized total returns appearing baked into Praxair's current stock price, we're not recommending Praxair as a buy as it's expected total returns aren't high enough to justify taking the risk of investing in this business.

Total Return Breakdown by Year

