Cintas Corporation (CTAS)

Updated July 22nd, 2018 by Nick McCullum

Key Metrics

Current Price:	$204	**5 Year CAGR Estimate:**	-0.7%	**Volatility Percentile:**	20.1%
Fair Value Price:	$124	**5 Year Growth Estimate:**	8.0%	**Momentum Percentile:**	94.8%
% Fair Value:	165%	**5 Year Valuation Multiple Estimate:**	-9.5%	**Valuation Percentile:**	3.1%
Dividend Yield:	0.8%	**5 Year Price Target**	$182	**Total Return Percentile:**	4.8%

Overview & Current Events

Cintas Corporation is the U.S. industry leader in uniform design, manufacturing, & rental. The company also offers first aid supplies, safety services, and other business-related services. Cintas was founded in 1968 and has grown to a market capitalization of $18 billion and annual revenues of more than $5 billion. Cintas' CEO is Scott Farmer, the son of its founder Richard Farmer. Scott Farmer owns more than 14% of Cintas' stock, which shows that the company's upper management is incentivized to act in the best interests of its shareholders. Cintas qualifies to be a member of the Dividend Aristocrats Index with 35 years of consecutive dividend increases.

In mid-July, Cintas reported (7/19/18) financial results for the fourth quarter of fiscal 2018 (the company operates with a unique financial calendar that ends on May 31). In the quarter, revenue of $1.67 billion increased by 9.1% over the prior year's period. the company delivered excellent organic revenue growth of 5.1%, driven by 5.3% growth in the Uniform Rental & Facility Services division and a 9.4% organic sales increase in First Aid & Safety Services revenue. The stark difference between Cintas' realized sales growth and its organic sales growth can be attributed to the acquisition of G&K Services, Inc. (which closed on March 21, 2017). On the bottom line, results were even stronger as Cintas was able to realize meaningful cost services from the G&K acquisition. More specifically, adjusted earnings-per-share of $1.77 increased by 41.6% over the $1.25 reported in the prior year's period. For the twelve-month reporting period, Cintas generated adjusted earnings-per-share of $7.03, well above our prior estimate for $5.83 in per-share net income. The company's fourth quarter earnings release beat consensus expectations on both the top and bottom line and shares rose by as much as 5% following the announcement.

Cintas also provided initial 2019 financial guidance with the release of fourth quarter earnings. Management expects to generate fiscal 2019 sales of between $6.75 billion to $6.82 billion and adjusted earnings-per-share of between $7.00 and $7.15. We are initiating our 2019 earnings-per-share estimate at the midpoint of this guidance band, or $7.08.

Growth on a Per-Share Basis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
EPS	$1.83	$1.49	$1.68	$2.27	$2.52	$2.79	$3.44	$4.09	$4.17	$7.03	***$7.08***	***$10.40***
DPS	$0.47	$0.48	$0.49	$0.54	$0.64	$0.77	$0.85	$1.05	$1.33	$1.62	***$1.78***	***$2.87***

Cintas has compounded its earnings-per-share at a rate of 7.6% since 2008. Over full economic cycles, we believe the company is capable of delivering continued earnings growth in the range of 8% per year. In fiscal 2018, Cintas is expecting to report earnings-per-share in the range of $7.00 and $7.15. Applying an 8% growth rate to the midpoint of this earnings guidance gives a 2024 earnings-per-share estimate of $10.40.

In the near-term, Cintas' growth will be driven by the aforementioned acquisition of G&K Services, which closed in March of 2017. The transaction is anticipated to be accretive to Cintas' earnings in fiscal 2019 and is expected to generate between $130 million and $140 million of annual cost synergies. Importantly, the acquisition was non-dilutive to continuing Cintas shareholders. The acquisition was funded using a combination of existing cash, assumption of existing G&K Services debt, and new debt. The integration has accelerated as of late, with the company stating in its most recent earnings press release that "*We have now closed nearly all operations necessary to eliminate redundancies,* *which is 63 operations to date. Also, all G&K operations have been converted to Cintas operating systems."* We believe exciting opportunities exist to merge the companies into one cohesive business unit.

Valuation Analysis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	Now	2023
Avg. P/E	15.7	13.8	17.9	16.6	14.9	16.6	19.4	21.4	21.5	27.2	***28.8***	***17.5***
Avg. Yld.	1.4%	1.9%	1.8%	1.8%	1.6%	1.5%	1.4%	1.2%	1.2%	1.2%	***0.8%***	***1.5%***

Cintas' P/E has varied from ~14 to ~27 over the last decade. We believe that excluding 2017's figure makes sense due to the irrationally high valuation assigned to the company at that data point. Ex-2017, Cintas has traded at an average price-to-earnings ratio of 17.5 over the last decade. We believe that this represents a fair price to pay for a company of Cintas' caliber. If the company's valuation reverts to 17.5 times earnings over the next decade, this will introduce a significant 9.5% *per year* headwind to the company's annualized returns during this time period.

Safety, Quality, Competitive Advantage, & Recession Resiliency

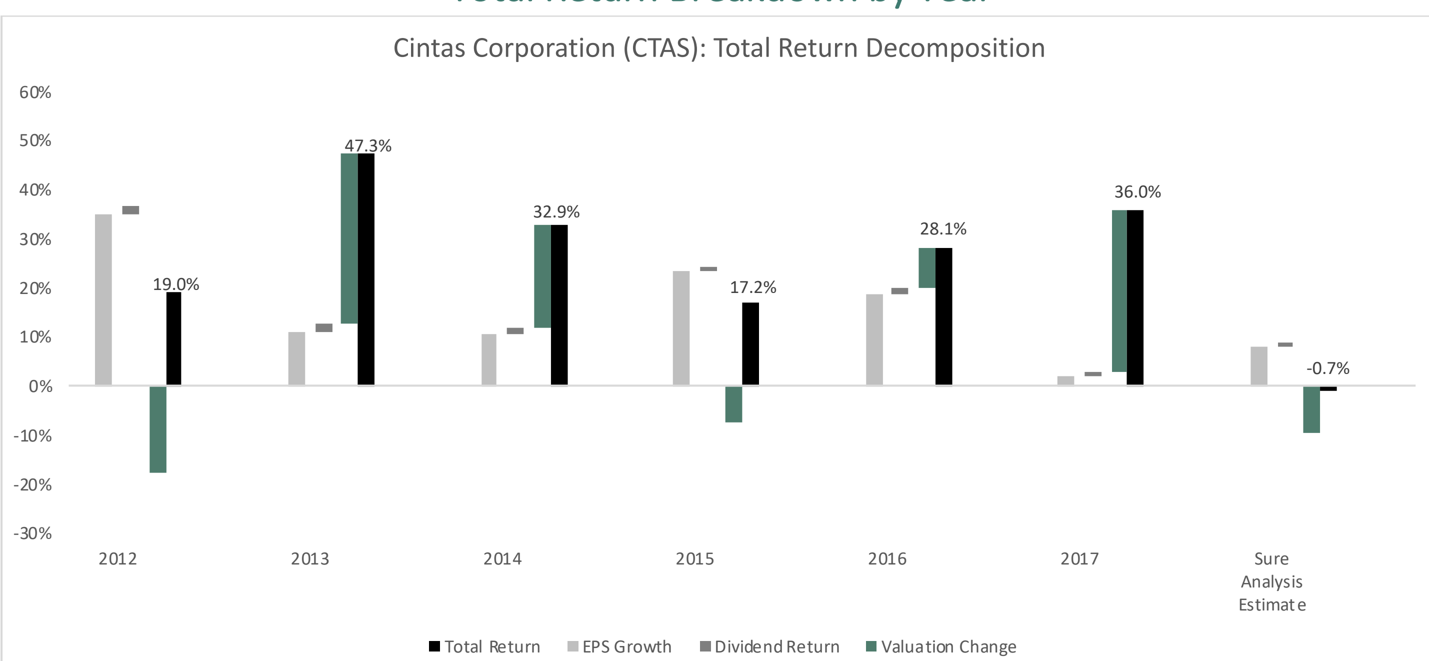
Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
GP/A	44.2%	41.7%	37.7%	37.0%	41.7%	40.3%	39.2%	45.2%	51.3%	34.8%	***40.0%***	***42.0%***
Debt/A	40.8%	36.4%	36.2%	47.1%	48.6%	49.3%	50.9%	53.9%	55.0%	66.4%	***65.0%***	***55.0%***
Int. Cov.	13.3	12.5	8.7	8.4	9.3	7.9	8.7	9.2	10.9	9.0	***9.0***	***11.0***
Payout	21.4%	25.7%	32.2%	29.2%	23.8%	25.4%	27.6%	24.7%	25.7%	31.9%	***27.8%***	***29.2%***
Std. Dev.	45.3%	33.1%	22.5%	32.4%	16.1%	14.6%	18.8%	17.9%	19.4%	17.7%	***18.0%***	***18.0%***

Cintas Corporation's debt as a proportion of its total assets has ballooned following the G&K Services acquisition. Accordingly, we expect the company to focus on debt repayment over the next several years. Conservative investors should also note that Cintas' gross profits as a percent of total assets are quite high, and the company's below-average payout ratio leaves room for continued dividend growth in the event that earnings growth slows.

Final Thoughts & Recommendation

While the Cintas *business* may be attractive, we have no doubt that the *stock* is not. Cintas' common stock is grossly overvalued right now. Accordingly, we are placing a strong sell recommendation on this security, and recommending that investors look elsewhere for more appealing investment opportunities.

Total Return Breakdown by Year



Disclosure: This analyst has no position in the security discussed in this research report, and no plans to initiate one in the next 72 hours.