ABB Ltd. (ABB)

Updated September 5th, 2018 by Nick McCullum

Key Metrics

Current Price:	$23	**5 Year CAGR Estimate:**	8.3%	**Volatility Percentile:**	41.6%
Fair Value Price:	$20	**5 Year Growth Estimate:**	8.0%	**Momentum Percentile:**	36.4%
% Fair Value:	115%	**5 Year Valuation Multiple Estimate:**	-3.1%	**Valuation Percentile:**	35.4%
Dividend Yield:	3.4%	**5 Year Price Target**	$29	**Total Return Percentile:**	53.9%

Overview & Current Events

ABB is a global provider of automation technologies and power solutions. The company operates in four business units: Power Grids, Electrification Products, Robotics & Motion, and Industrial Automation. ABB is incorporated in Switzerland, but domestic investors can initiate an ownership stake in the company through American Depository Receipts that trade with a market capitalization of US$50 billion under the ticker ABB on the New York Stock Exchange.

ABB reported (7/19/18) financial results for the second quarter of fiscal 2018 in mid-July. In the quarter, the company generated total order growth of 8% and consolidated revenue growth of 1%. The company's aggregated book-to-bill ratio was 1.07x – which means it generated more business than it could complete during the reporting period, a positive trend – and its book-to-bill ratio was above 1 in each of its operating segments. Moving down the income statement, ABB's operational EBITDA margin expanded 60 basis points to 13.0%, which allowed its net income to increase by 30% and its adjusted earnings-per-share to rise by 27%. ABB's second-quarter earnings release was received positively by the financial markets and its NYSE-listed shares rose by as much as 6% in the weeks following the earnings report.

Growth on a Per-Share Basis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
EPS	$1.37	$1.26	$1.11	$1.38	$1.18	$1.23	$1.13	$0.87	$0.88	$1.03	***$1.25***	***$1.84***
DPS	$0.47	$0.45	$0.49	$0.68	$0.71	$0.72	$0.77	$0.75	$0.75	$0.76	***$0.80***	***$1.20***
Shares	2282.7	2289.4	2283.5	2290.4	2295.9	2300.6	2314.7	2191.6	2138.7	2138.6	***2140.0***	***2150.0***

ABB's per-share growth in net income over the last decade has been far from compelling. With that said, ABB has a number of current growth opportunities that lead us to believe its future performance will be stronger than its historical track record.

First, ABB has been active on the acquisition front lately. Last year, the company closed (7/6/18) on the acquisition of B&R, the largest independent provider focused on product- and software-based, open-architecture solutions for machine and factory automation worldwide. More recently, ABB completed (7/2/18) the acquisition of GE Industrial Solutions. This transaction gives the company the #2 global position in electrification solutions while also being very attractive from a financial perspective. The GE purchase is expected to be accretive to earnings-per-share in the first year while generating annual cost synergies of approximately $200 million by year five.

Separately, ABB has a leadership position in the rapidly-growing field of electric vehicle infrastructure. The company was recently selected to supply its *Terra* charging stations within and around 17 metropolitan areas in the United States as part of a partnership with Electrify America, a Volkswagen subsidiary.

Because of these growth catalysts as well as the company's recent financial performance, we are forecasting a substantial jump in earnings-per-share to $1.25 in fiscal 2018. Beyond that, we believe that ABB is likely to generate 8% annualized growth in earnings-per-share over the next 5 years, although this estimate has some uncertainty and we would not be surprised if realized growth exceeds or falls short of this figure.

Valuation Analysis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	Now	2023
Avg. P/E	16.9	13.1	18.0	16.1	15.9	18.6	20.8	23.1	22.9	23.5	***18.7***	***16.0***
Avg. Yld.	2.0%	2.7%	2.5%	3.1%	3.8%	3.1%	3.3%	3.7%	3.7%	3.1%	***3.4%***	***4.1%***

ABB has traded at an average price-to-earnings ratio of 18.9 over the last decade. With that said, this sample includes several years (2014-2017) where the company's common stock was objectively overvalued. We believe that fair value for a company of ABB's caliber lies somewhere around 16 times earnings. ABB is trading at a price-to-earnings ratio of 18.7 today. If the company's valuation multiple were to revert to our fair value estimate over the next 5 years, this would reduce its annualized returns by 3.1% per year during this time period.

Safety, Quality, Competitive Advantage, & Recession Resiliency

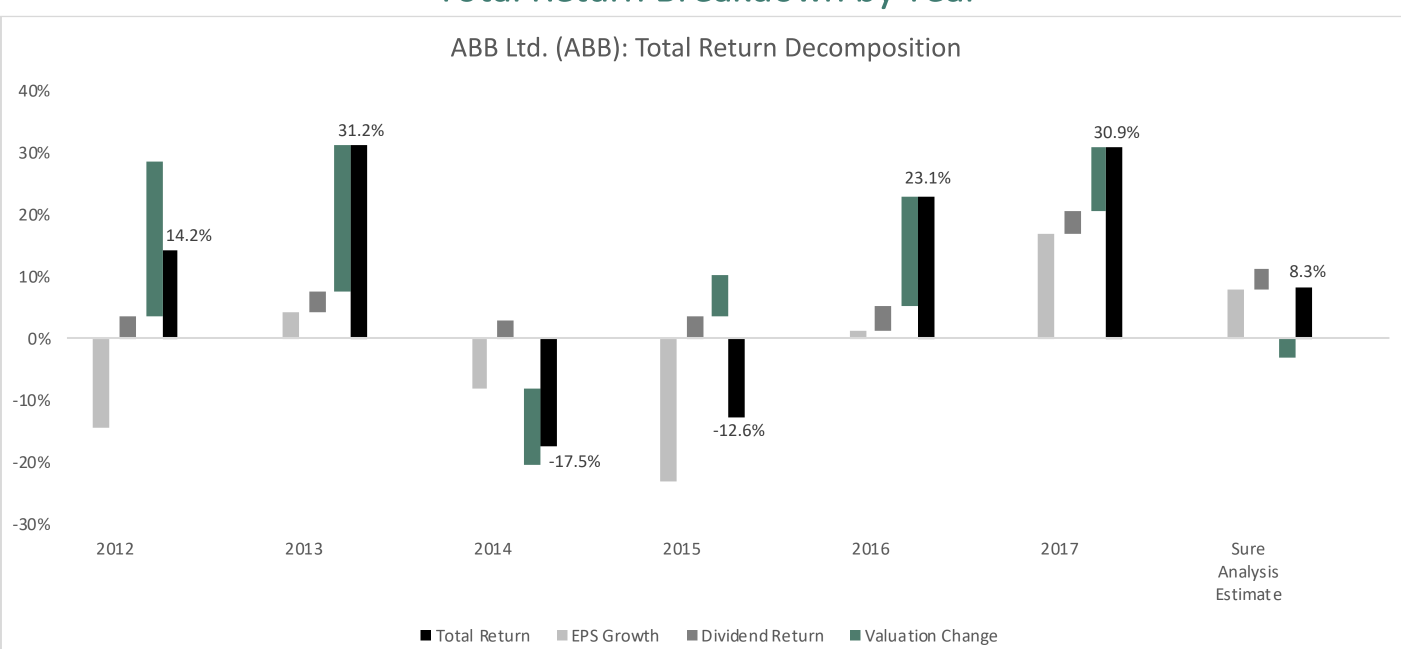
Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
GP/A	33.1%	26.9%	26.3%	28.8%	23.2%	25.0%	25.0%	24.5%	24.9%	23.7%	***24.0%***	***24.0%***
Debt/A	64.3%	58.3%	57.4%	58.8%	64.4%	60.0%	62.5%	63.8%	64.6%	64.5%	***65.0%***	***65.0%***
Int. Cov.	143	708	50.2	40.7	18.8	13.9	15.1	15.0	16.3	17.3	***15.0***	***15.0***
Payout	34.3%	35.7%	44.1%	49.3%	60.2%	58.5%	68.1%	86.2%	85.2%	73.8%	***64.0%***	***65.2%***
Std. Dev.	57.8%	37.6%	35.2%	31.2%	28.0%	13.9%	15.7%	18.3%	20.6%	17.1%	***22.0%***	***22.0%***

Several of ABB's quality metrics have declined over time. More specifically, the last decade has seen a decrease in its gross profits to total assets, an increase in its dividend payout ratio, and a decline in its interest coverage. We note that each of these quality metrics is still well within our acceptable range – particularly its interest coverage ratio, which is higher than many of ABB's peers in the industrial sector.

Final Thoughts & Recommendation

ABB has many appealing characteristics. It is a global business with leadership in many segments of the industrial sector. The company's recent acquisitions as well as its edge in electric vehicle infrastructure should propel its growth for the foreseeable future. In addition, ABB seems priced to deliver high single-digit total returns moving forward. Despite these positive traits, ABB fails to earn a buy recommendation as it is trading above our estimate of fair value.

Total Return Breakdown by Year



Click here to rate and review this report. Your feedback is important to us.

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.