



Caterpillar Inc. (CAT)

Updated January 29th, 2019 by Jonathan Weber

Key Metrics

Current Price:	\$124	5 Year CAGR Estimate:	17.9%	Volatility Percentile:	64.2%
Fair Value Price:	\$190	5 Year Growth Estimate:	6.2%	Momentum Percentile:	19.2%
% Fair Value:	65%	5 Year Valuation Multiple Estimate:	8.9%	Growth Percentile:	58.7%
Dividend Yield:	2.8%	5 Year Price Target	\$257	Valuation Percentile:	94.3%
Dividend Risk Score:	A	Retirement Suitability Score:	A	Total Return Percentile:	92.0%

Overview & Current Events

Caterpillar manufactures and sells construction and mining equipment as well as products in several other categories, including diesel engines and industrial gas turbines. Caterpillar was founded in 1925, is headquartered in Peoria, Illinois and is currently valued at \$73 billion.

Caterpillar reported its fourth quarter and fiscal 2018 earnings results on January 28. The company reported revenues of \$14.3 billion for the fourth quarter, which represents a growth rate of 10.9% compared to the prior year's quarter. This growth in Caterpillar's top line was driven by higher sales for Caterpillar's most important segments, as construction industries sales rose by 8% year over year, while resource industries sales rose by an even better 21% compared to the prior year's period. Energy & transportation sales were up by 11% year over year, but Caterpillar's financial products segment grew its revenues by a below-average 4% compared to Q4 of 2017.

The company's compelling revenue growth rate, coupled with margin benefits, allowed for operating profit growth of 36% compared to the prior year's quarter. Caterpillar's earnings-per-share totaled \$2.55 during the fourth quarter, which was 18% more than during the fourth quarter of 2017. Sales and earnings-per-share both rose at an attractive pace, but the analyst community and the market had expected an even better performance, which is why Caterpillar's share price reacted very negatively to the miss of the consensus estimates. Shares dropped 9% on January 28.

Caterpillar guides for earnings-per-share in a range of \$11.75 to \$12.75 during fiscal 2019.

Growth on a Per-Share Basis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
EPS	\$1.43	\$4.15	\$7.81	\$9.36	\$5.79	\$6.37	\$4.62	\$3.44	\$6.88	\$11.20	\$12.25	\$16.55
DPS	\$1.68	\$1.74	\$1.82	\$2.02	\$2.32	\$2.70	\$3.01	\$3.08	\$3.11	\$3.28	\$3.60	\$4.96
Shares	625	639	648	655	638	606	582	586	598	588	580	550

Caterpillar's customers, primarily mining companies & construction companies, operate in cyclical industries. During good times they are inclined to expand their operations and to upgrade their equipment in order to make operations more efficient. During weak times they are less likely to expand their operations, and they will defer the purchase of new equipment, which means lower sales for Caterpillar. Caterpillar's business therefore is relatively cyclical, which is clearly visible in the above table. During the last financial crisis profits experienced a tremendous decline, and during 2015-2016, when commodity prices were relatively low, Caterpillar's sales and profits declined significantly as well.

Right now much points into the right direction for Caterpillar. Mining companies are expanding their operations, and at the same time the construction industry is doing well in key markets such as the US and China. On top of that, Caterpillar will benefit from cost-cutting measures that were employed over the last couple of years during the cyclical downturn.

These cost savings will boost Caterpillar's profit margins going forward. With its rising cash flows Caterpillar will continue to reduce its share count, which results in a boost to the company's earnings-per-share growth rate. 2018 was a record year for Caterpillar, and it looks like 2019 will be even better. We believe that a double-digits earnings-per-share growth rate will not be maintained throughout the next five years, but we nevertheless believe that Caterpillar will be able to grow its earnings-per-share at a solid pace going forward, with buybacks being an important factor.

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.



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Valuation Analysis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	Now	2024
Avg. P/E	29.4	16.6	12.4	10.0	15.1	15.8	17.1	22.8	16.4	11.3	10.1	15.5
Avg. Yld.	4.0%	2.5%	1.9%	2.2%	2.7%	2.7%	3.8%	3.9%	2.8%	2.7%	2.8%	2.0%

Caterpillar trades at just above 10 times this year's expected earnings, using the midpoint of management's guidance. This is the lowest valuation shares have traded at in years, and very close to the absolute bottom of the 10-year range. We believe that there is considerable upside towards a fair valuation in the mid-teens range.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
Payout	117%	41.9%	23.3%	21.6%	40.1%	42.4%	65.2%	89.5%	45.2%	29.3%	29.4%	30.0%

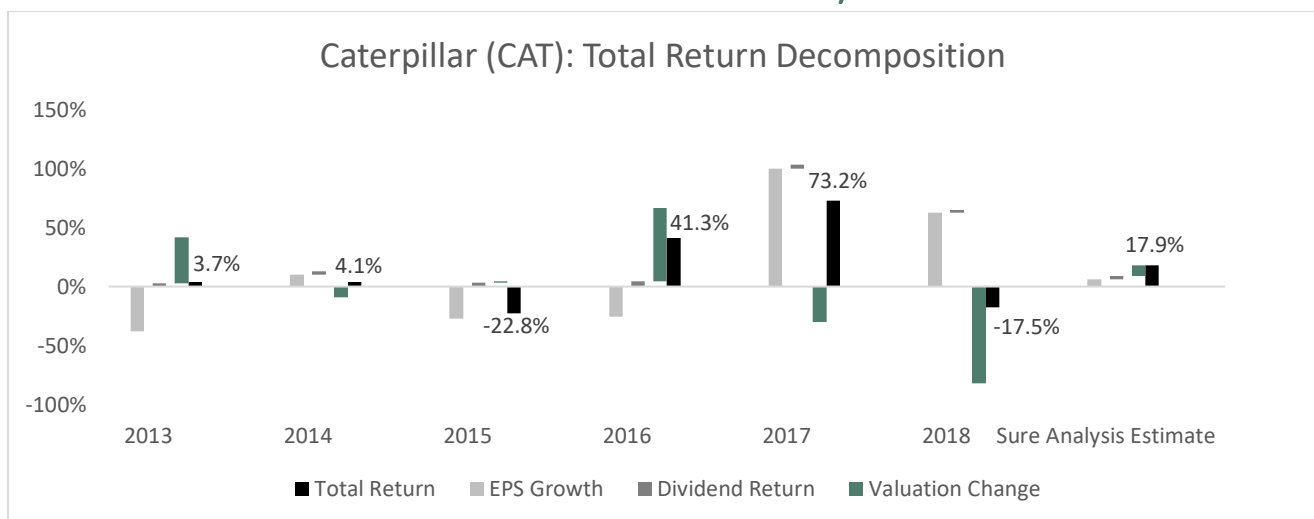
Caterpillar's dividend payout ratio has moved up and down throughout the last couple of years, which is not surprising as the company's profits were quite cyclical. The significant increase in Caterpillar's earnings-per-share made the payout ratio decline substantially during 2018. Due to the fact that the payout ratio rose above 100% during the last financial crisis, the dividend is somewhat risky, even though Caterpillar did not cut its dividend during the last financial crisis.

Qualitatively, Caterpillar is one of the largest players in the markets it addresses, with a brand that is well-known and recognized around the globe. The fact that Caterpillar has a global presence and is selling its products to several industries (construction, mining, etc.) makes it less dependent on any single market. During global economic downturns, such as during the last financial crisis, Caterpillar's business is hit hard. This was visible during the last recession, when earnings-per-share declined by 75% between 2008 and 2009. To summarize, Caterpillar is not a recession resistant stock.

Final Thoughts & Recommendation

Caterpillar is a leader in its industry, and the company has hit a record in 2018, while 2019 should be an even better year. We believe that Caterpillar's earnings growth will slow down, but when we add in the stock's considerable potential for multiple expansion as well as Caterpillar's above-average dividend yield, the total return outlook still looks promising. For those that are not afraid of the cyclicity, Caterpillar earns a buy recommendation at current prices.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Revenue	51324	32396	42588	60138	65875	55656	55184	47011	38537	45462
Gross Profit	12909	8510	11307	15734	18023	14202	13842	12878	9632	13767
Gross Margin	25.2%	26.3%	26.5%	26.2%	27.4%	25.5%	25.1%	27.4%	25.0%	30.3%
SG&A Exp.	4399	3645	4248	5203	5919	5547	6529	4951	4686	5177
D&A Exp.	1980	2336	2296	2527	2813	3087	3163	3046	3034	2877
Operating Profit	6782	3444	3963	7153	9153	5628	3314	3785	1093	4406
Op. Margin	13.2%	10.6%	9.3%	11.9%	13.9%	10.1%	6.0%	8.1%	2.8%	9.7%
Net Profit	3557	895	2700	4928	5681	3789	2452	2512	-67	754
Net Margin	6.9%	2.8%	6.3%	8.2%	8.6%	6.8%	4.4%	5.3%	-0.2%	1.7%
Free Cash Flow	786	4027	2423	3033	108	5745	4678	3438	2708	3366
Income Tax	953	-270	968	1720	2528	1319	692	916	192	3339

Balance Sheet Metrics

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Total Assets	67782	60038	64020	81218	88970	84896	84681	78342	74704	76962
Cash & Equivalents	2736	4867	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Acc. Receivable	N/A	N/A	8494	10057	9706	8413	7737	6695	5981	7436
Inventories	8781	6360	9587	14544	15547	12625	12205	9700	8614	10018
Goodwill & Int.	2772	2734	3419	11448	10958	10552	9770	9436	8369	8311
Total Liabilities	61068	50738	53156	68289	71388	64018	67855	63457	61491	63196
Accounts Payable	4827	2993	5856	8161	6753	6560	6515	5023	4614	6487
Long-Term Debt	35535	31631	28337	34546	40070	37653	39200	37936	36715	34441
Total Equity	6087	8740	10824	12883	17532	20811	16746	14809	13137	13697
D/E Ratio	5.84	3.62	2.62	2.68	2.29	1.81	2.34	2.56	2.79	2.51

Profitability & Per Share Metrics

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Return on Assets	5.7%	1.4%	4.4%	6.8%	6.7%	4.4%	2.9%	3.1%	-0.1%	1.0%
Return on Equity	47.5%	12.1%	27.6%	41.6%	37.4%	19.8%	13.1%	15.9%	-0.5%	5.6%
ROIC	8.9%	2.2%	6.7%	11.4%	10.8%	6.5%	4.3%	4.6%	-0.1%	1.5%
Shares Out.	602	625	639	648	655	638	606	582	586	598
Revenue/Share	81.74	51.75	65.48	90.28	98.38	84.51	87.75	78.18	65.95	75.86
FCF/Share	1.25	6.43	3.73	4.55	0.16	8.72	7.44	5.72	4.63	5.62

Note: All figures in millions of U.S. Dollars unless per share or indicated otherwise.

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