



# Emerson Electric Company (EMR)

Updated February 8<sup>th</sup>, 2019 by Josh Arnold

## Key Metrics

<b>Current Price:</b>	\$66	<b>5 Year CAGR Estimate:</b>	8.0%	<b>Volatility Percentile:</b>	41.2%
<b>Fair Value Price:</b>	\$66	<b>5 Year Growth Estimate:</b>	5.0%	<b>Momentum Percentile:</b>	48.0%
<b>% Fair Value:</b>	100%	<b>5 Year Valuation Multiple Estimate:</b>	0.0%	<b>Growth Percentile:</b>	33.5%
<b>Dividend Yield:</b>	3.0%	<b>5 Year Price Target</b>	\$85	<b>Valuation Percentile:</b>	44.9%
<b>Dividend Risk Score:</b>	A	<b>Retirement Suitability Score:</b>	A	<b>Total Return Percentile:</b>	35.1%

## Overview & Current Events

Emerson Electric was founded in Missouri in 1890 and since that time, it has evolved through organic growth as well as strategic acquisitions and divestitures from a regional manufacturer of electric motors and fans into a \$42 billion diversified global leader in technology and engineering. Its global customer base affords it \$19 billion in annual revenue.

Emerson reported Q1 earnings on 2/5/19 and results were good enough for the company to raise its guidance for fiscal 2019. Total sales were up 9% during the quarter as organic growth accounted for 4.5%, while acquisitions added 6%, but was partially offset by a 1.5% loss thanks to currency translation. Sales strength came from broad demand in its global industrial markets, professional tools markets, as well as North American air conditioning markets. The company's trailing three-month underlying orders growth remained in the 5% to 10% range for the quarter, with December's number coming in at 7%. This bodes well for Emerson's near-term revenue growth.

Gross margins improved slightly year-over-year to 42.5%, driven by the benefits of cost reductions as well as leverage from higher revenue. EBIT margin came in 110bps higher in Q1 to 15.3%, thanks to lower incentive compensation expense and a lack of acquisition accounting charges that were present in the comparable period. Dilution partially offset some of these gains, but earnings-per-share rose 21% to \$0.74 in total.

Emerson repurchased \$800 million worth of stock in Q1, which helped management boost its forecasts for 2019. Net sales growth is now expected to be 7% to 10% with the bulk of it coming from underlying sales growth and the balance from acquisitions. Earnings-per-share are now expected in a range of \$3.60 to \$3.75; we've updated our estimate accordingly to \$3.68 per share.

Separately, Emerson closed the A.E. Valves acquisition in December and subsequent to the end of the quarter, it purchased GE Intelligent Platforms in January.

## Growth on a Per-Share Basis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
<b>EPS</b>	\$2.27	\$2.60	\$3.24	\$2.67	\$3.54	\$3.75	\$3.17	\$2.46	\$2.54	\$3.46	<b>\$3.68</b>	<b>\$4.70</b>
<b>DPS</b>	\$1.33	\$1.34	\$1.38	\$1.60	\$1.66	\$1.72	\$1.88	\$1.90	\$1.92	\$1.94	<b>\$1.96</b>	<b>\$2.15</b>
<b>Shares</b>	752	753	739	724	707	697	655	643	642	641	<b>640</b>	<b>635</b>

The majority of Emerson's revenue is exposed to the oil and gas industry, where revenue and margins change significantly, introducing risk to forecasts in out years. That said, we are forecasting 5% annual growth as the company's low single digit organic growth is coupled with acquisitions to fuel top line expansion. Emerson's Q1 results were better than this forecast, but peaks and valleys in the company's results are not unusual. We still think low to mid-single digit growth in revenue and a small tailwind from the buyback will be the key drivers of earnings-per-share growth in the coming years, and are not yet upgrading our forecast after Q1 results.

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. However, growth rates will likely be unimpressive as the company continues to focus using its ample cash flow on acquisitions, not dividend growth.

*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	14.8	17.8	16.8	18.3	15.8	17.6	18.0	20.6	22.9	20.5	<b>18.0</b>	<b>18.0</b>
Avg. Yld.	3.9%	2.9%	2.5%	3.3%	3.0%	2.6%	3.3%	3.8%	3.3%	2.7%	<b>3.0%</b>	<b>2.5%</b>

Emerson's price-to-earnings ratio has risen markedly in the past few years despite the fact that its earnings have been volatile. However, recent weakness in the share price has caused the valuation to come back down to fair value. We are therefore forecasting no impact from the valuation in the coming years as Emerson is trading at fair value for the first time in a few years. We see the yield to fall slightly over time to 2.5% from 3.0% as the share price outpaces gains in the payout, as has been the case for the past few years on average.

## Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
Payout	58%	51%	42%	60%	46%	61%	60%	77%	75%	58%	<b>53%</b>	<b>46%</b>

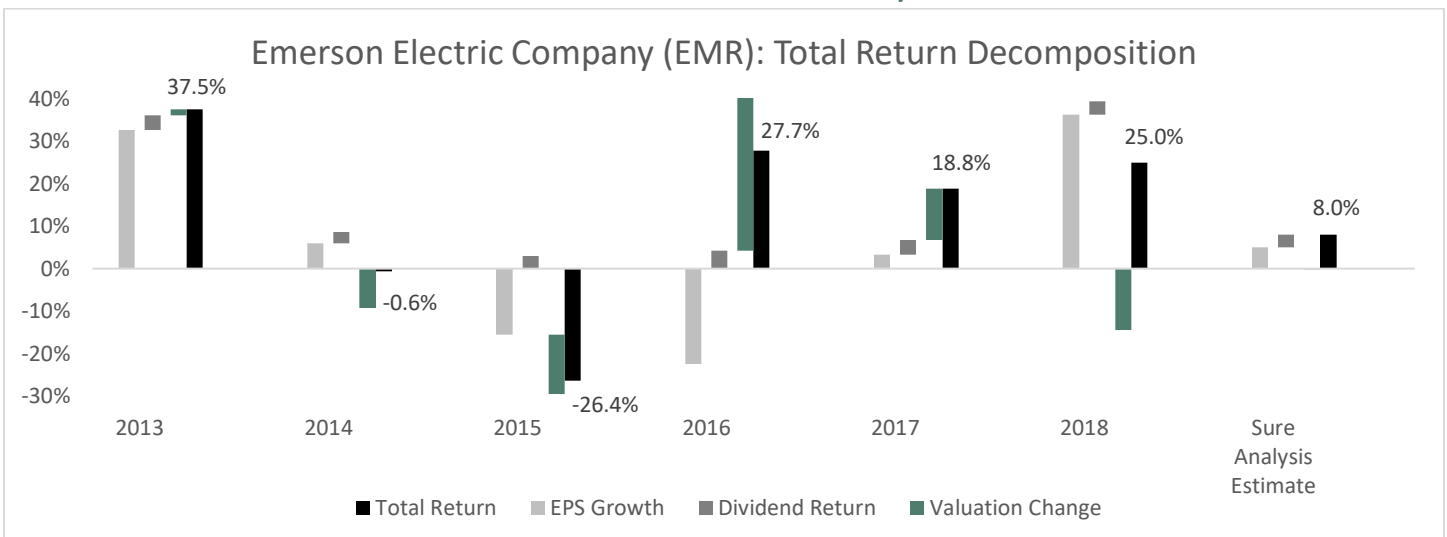
Emerson's payout ratio remains around half of earnings, and we believe it will continue to drift lower over time as Emerson focuses on acquisitions instead of boosting the payout by large amounts. The dividend is very safe as it is well covered by free cash flow, and the yield is strong, so it is certainly a suitable dividend stock.

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. It is very susceptible to recessions given its oil and gas exposure, however, so any signs of economic weakness should put investors on alert.

## Final Thoughts & Recommendation

With the stock back at fair value, Emerson should deliver 8% total returns going forward. This will be comprised of the 3.0% current yield, earnings-per-share growth of 5% and no impact from the valuation. Emerson is finally trading at fair value again and while the stock doesn't offer much for value investors, it would be suitable for those seeking a high current yield. We're reiterating Emerson at a hold for this update as Q1's strong results and 2019's guidance raise are certainly positives when combined with the lower valuation.

## Total Return Breakdown by Year



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## Income Statement Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
<b>Revenue</b>	20102	21039	24222	24412	24669	17733	16249	14522	15264	17408
<b>Gross Profit</b>	7560	8326	9557	9768	9952	7762	7008	6262	6404	7460
<b>Gross Margin</b>	37.6%	39.6%	39.5%	40.0%	40.3%	43.8%	43.1%	43.1%	42.0%	42.9%
<b>SG&amp;A Exp.</b>	4416	4817	5328	5436	5648	4164	3735	3464	3618	4258
<b>D&amp;A Exp.</b>	727	816	867	823	819	569	573	568	636	758
<b>Operating Profit</b>	3144	3509	3849	3881	3942	3426	3081	2600	2578	2891
<b>Op. Margin</b>	15.6%	16.7%	15.9%	15.9%	16.0%	19.3%	19.0%	17.9%	16.9%	16.6%
<b>Net Profit</b>	1724	2164	2480	1968	2004	2147	2710	1635	1518	2203
<b>Net Margin</b>	8.6%	10.3%	10.2%	8.1%	8.1%	12.1%	16.7%	11.3%	9.9%	12.7%
<b>Free Cash Flow</b>	2555	2768	2586	2388	2971	3041	1941	2434	1436	2275
<b>Income Tax</b>	688	848	1127	1091	1130	953	1267	697	660	443

## Balance Sheet Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
<b>Total Assets</b>	19763	22843	23861	23818	24711	24177	22088	21732	19589	20390
<b>Cash &amp; Equivalents</b>	1560	1592	2052	2367	3275	3149	3054	3182	3062	1093
<b>Acc. Receivable</b>		4087	4611	4983	4808	5019	2870	2701	3072	3344
<b>Inventories</b>	1855	2105	2100	2125	1895	2057	1265	1208	1696	1813
<b>Goodwill &amp; Int.</b>	8222	10806	10740	9864	9181	8871	4785	4811	7206	9206
<b>Total Liabilities</b>	11057	12891	13310	13376	13993	14010	13960	14114	10819	11400
<b>Accounts Payable</b>	1949	2409	2677	2767	2725	2951	1537	1517	1776	1943
<b>Long-Term Debt</b>	4575	5066	5201	5293	5642	6024	6841	6635	4656	4760
<b>Total Equity</b>	8555	9792	10399	10295	10585	10119	8081	7568	8718	N/A
<b>D/E Ratio</b>	0.5348	0.5174	0.5001	0.5141	0.533	0.5953	0.8466	0.8767	0.5341	N/A

## Profitability & Per Share Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
<b>Return on Assets</b>	8.5%	10.2%	10.6%	8.3%	8.3%	8.8%	11.7%	7.5%	7.3%	11.0%
<b>Return on Equity</b>	19.5%	23.6%	24.6%	19.0%	19.2%	20.7%	29.8%	20.9%	18.6%	N/A
<b>ROIC</b>	12.8%	15.3%	16.1%	12.5%	12.5%	13.2%	17.4%	11.2%	11.0%	N/A
<b>Shares Out.</b>	752	753	739	724	707	697	655	643	642	641
<b>Revenue/Share</b>	26.50	27.79	32.15	33.23	34.13	25.19	24.02	22.45	23.72	27.40
<b>FCF/Share</b>	3.37	3.66	3.43	3.25	4.11	4.32	2.87	3.76	2.23	3.58

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

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