



# Air Products & Chemicals Inc. (APD)

Updated May 9<sup>th</sup>, 2019 by Jonathan Weber

## Key Metrics

<b>Current Price:</b>	\$202	<b>5 Year CAGR Estimate:</b>	2.2%	<b>Volatility Percentile:</b>	8.1%
<b>Fair Value Price:</b>	\$148	<b>5 Year Growth Estimate:</b>	6.0%	<b>Momentum Percentile:</b>	87.8%
<b>% Fair Value:</b>	136%	<b>5 Year Valuation Multiple Estimate:</b>	-6.1%	<b>Growth Percentile:</b>	53.0%
<b>Dividend Yield:</b>	2.3%	<b>5 Year Price Target</b>	\$197	<b>Valuation Percentile:</b>	10.2%
<b>Dividend Risk Score:</b>	B	<b>Retirement Suitability Score:</b>	C	<b>Total Return Percentile:</b>	8.1%

## Overview & Current Events

Air Products & Chemicals is one of the world's largest producers and distributors of atmospheric and process gases, serving other businesses in the industrial, technology, energy, and materials sectors. Air Products & Chemicals operates through three main business units: Industrial Gases – Americas, Industrial Gases – EMEA, and Industrial Gases – Asia. Its 37-year streak of consecutive dividend increases qualifies it to be a member of the Dividend Aristocrats Index. The company is headquartered in Allentown, Pennsylvania and trades with a market capitalization of \$45 billion

On April 24, Air Products & Chemicals reported financial results for the second quarter of fiscal 2019. The company generated revenues of \$2.19 billion, which was up 1.4% year over year, but which missed the analyst consensus by 2% nevertheless. Currency rate movements had a major negative impact on Air Products & Chemicals' revenues, as currency adjusted revenues would have been up by 5.5% year over year, mainly thanks to strong pricing and volume gains of ~3%. The Gases America segment grew its sales by 9% year over year, to close to \$1.0 billion, while the Gases Asia segment grew its revenues by an even better 12% year over year. The Gases EMEA segment, though, saw its sales decline by 12%, with currency rate movements alone being responsible for a 7% drop.

Air Products & Chemicals managed to grow its EBITDA margin to a new record level of 37.7% during the second quarter, which helped the company to generate earnings-per-share of \$1.92 during the quarter, beating estimates by \$0.05. Earnings-per-share grew at a highly attractive rate of 12% compared to the previous year's second quarter. Air Products & Chemicals continued to generate strong cash flows during the second quarter, over the last twelve months distributable cash flows totaled \$2.4 billion, which equates to distributable cash flows of \$10.92 on a per-share basis.

## Growth on a Per-Share Basis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
<b>EPS</b>	\$4.06	\$5.02	\$5.73	\$5.40	\$5.50	\$5.78	\$6.57	\$7.55	\$6.31	\$7.45	<b>\$8.17</b>	<b>\$10.93</b>
<b>DPS</b>	\$1.79	\$1.92	\$2.23	\$2.50	\$2.77	\$3.02	\$3.20	\$3.39	\$3.71	\$4.40	<b>\$4.84</b>	<b>\$6.48</b>
<b>Shares</b>	211.3	213.8	210.2	212.5	211.2	213.5	215.4	217.4	218.3	220.9	<b>220.0</b>	<b>220.0</b>

Between 2009 and 2018, Air Products & Chemicals generated earnings-per-share growth of 7.0% annually, which is not an extremely high, but still very solid growth rate. There were some ups and downs over the year during that time.

Air Products & Chemicals growth over the coming years will be driven by international expansion, as the company's Gases Asia business has delivered the highest growth rate in the recent past, although its American business remains the largest segment for now. Air Products & Chemicals has a number of growth projects either recently completed or scheduled to be completed in the coming months. Some of these investments around the world include building a second liquid hydrogen plant in California, a new air separation unit (ASU) in Minnesota, an ASU plant in India, and helium investments in Algeria. Air Products & Chemicals was also recently awarded a sixth on-site nitrogen facility in Tianjin, China, to supply a major electronic components manufacturer's new production line.

In early 2019, Air Products & Chemicals announced it will build the first hydrogen fuel cell vehicle fueling station in Saudi Arabia, along with oil giant Saudi Aramco. Air Products & Chemicals has announced several more projects that will come on line through 2022, including a major \$3.5 billion joint venture with Yankuang in China.

*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	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	Now	2023
Avg. P/E	19.0	14.9	15.1	15.4	15.6	16.5	20.6	21.7	18.6	23.3	<b>24.7</b>	<b>18.0</b>
Avg. Yld.	1.8%	3.0%	2.5%	2.5%	3.0%	3.1%	2.5%	2.2%	2.4%	2.4%	<b>2.3%</b>	<b>3.3%</b>

Air Products & Chemicals has never traded at an especially low valuation, but more recently its shares have become even more expensive. Based on our estimate, shares are trading for almost 25 times this year's net profits, which is why we believe that shares are substantially overvalued today. The corresponding multiple contraction that we expect will negatively impact the stock's total returns significantly.

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

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
Payout	44.1%	38.2%	38.9%	46.3%	50.4%	52.2%	48.7%	44.9%	58.8%	60.7%	<b>59.3%</b>	<b>59.3%</b>

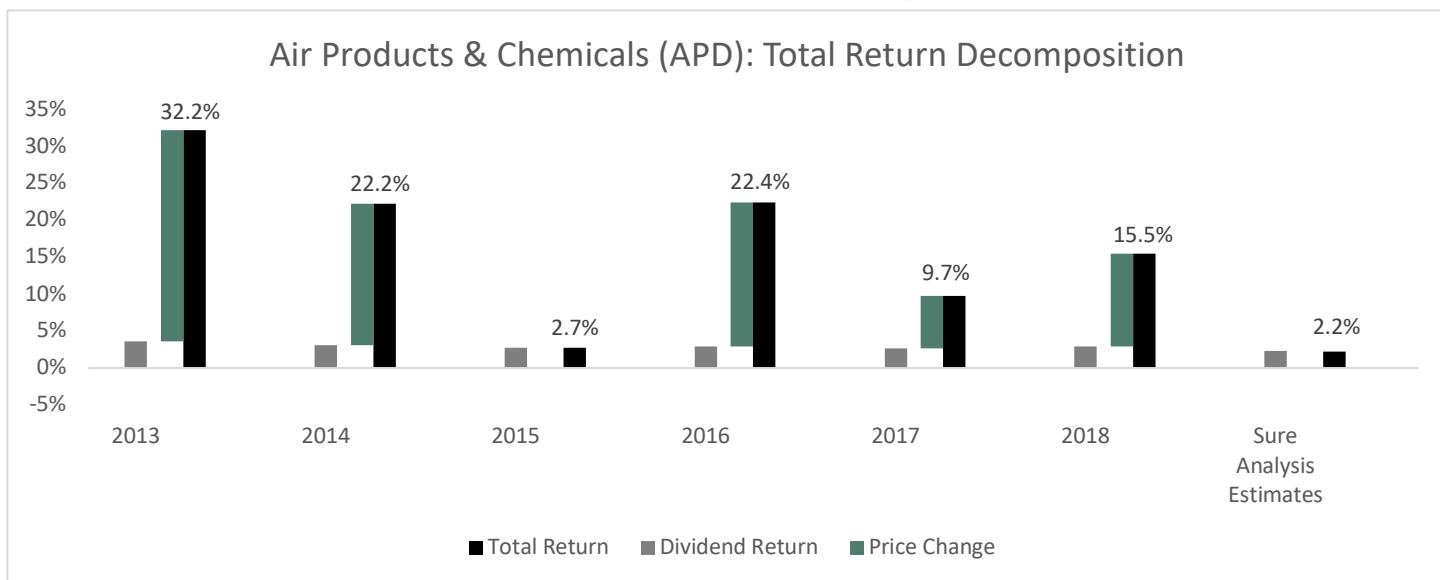
Air Products & Chemicals will pay out roughly 60% of its net profits in the form of dividends this year. This is not an especially low payout ratio, but the dividend looks highly sustainable at the current level. The company's reasonable payout ratio also ensures that it can continue its streak of dividend increases.

Air Products & Chemicals' most compelling competitive advantage is its industry expertise. The company also benefits from high switching costs -- it is difficult to find a competitor that offers identical services in a particular geographic region. However, Air Products & Chemicals is not a recession-resistant business. Earnings-per-share declined 18% in 2009, during the Great Recession, investors thus have to stomach some volatility during recessions.

## Final Thoughts & Recommendation

Air Products & Chemicals looks highly attractive at first sight: The company has a multi-decade streak of consecutive dividend increases, a strong globalized business model, and leadership in the gas industry. Despite these positives, Air Products & Chemicals appears positioned to deliver subpar total returns because of its overly high valuation multiple. We estimate that Air Products & Chemicals will generate low single digits annual returns going forward, which is why we rate the stock a sell at the current, elevated price.

## Total Return Breakdown by Year



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## Income Statement Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Revenue	8838	8928	9833	10595	9442	10226	10939	11668	12380	13326
Gross Profit	4016	3898	4125	4392	3868	4185	4511	4828	5110	5483
Gross Margin	45.4%	43.7%	41.9%	41.4%	41.0%	40.9%	41.2%	41.4%	41.3%	41.1%
SG&A Exp.	2190	2127	2315	2453	2200	2370	2497	2637	2783	2972
D&A Exp.	308	309	315	319	251	267	278	289	316	378
Operating Profit	1825	1771	1810	1939	1668	1815	2014	2191	2327	2512
Operating Margin	20.7%	19.8%	18.4%	18.3%	17.7%	17.7%	18.4%	18.8%	18.8%	18.8%
Net Profit	1333	1211	1254	1389	1406	1516	1453	1493	1733	1621
Net Margin	15.1%	13.6%	12.8%	13.1%	14.9%	14.8%	13.3%	12.8%	14.0%	12.2%
Free Cash Flow	1309	1455	1428	1661	1342	1518	1639	1511	1655	2044
Income Tax	575	656	673	727	588	637	694	741	798	550

## Balance Sheet Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Total Assets	25352	26862	34238	30817	32268	32060	33111	43670	37180	37089
Cash & Equivalents	2265	1643	1389	1548	1699	1584	1639	3191	2780	2170
Acc. Receivable	1051	1037	1288	1315	1516	1415	1547	1743	1704	1984
Goodwill & Int.	2954	2926	3789	3750	3682	2375	2297	2216	2361	3130
Total Liabilities	20029	21383	28228	24703	26078	25390	28302	39188	33203	33629
Accounts Payable	130	150	153	167	157	152	195	152	150	135
Long-Term Debt	773	40	34	17	15	12	9	2008	2002	2002
Total Equity	5323	5479	6010	6114	6190	6670	4809	4482	3977	3460
D/E Ratio	0.15	0.01	0.01	0.00	0.00	0.00	0.00	0.45	0.50	0.58

## Profitability & Per Share Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Return on Assets	5.4%	4.6%	4.1%	4.3%	4.5%	4.7%	4.5%	3.9%	4.3%	4.4%
Return on Equity	25.6%	22.4%	21.8%	22.9%	22.9%	23.6%	25.3%	32.1%	41.0%	43.6%
ROIC	23.7%	20.9%	21.7%	22.8%	22.8%	23.5%	25.3%	26.4%	27.8%	28.3%
Shares Out.	211.3	213.8	210.2	212.5	211.2	213.5	215.4	217.4	218.3	220.9
Revenue/Share	17.47	17.72	19.73	21.53	19.38	21.17	22.99	25.41	27.49	30.06
FCF/Share	2.59	2.89	2.87	3.37	2.76	3.14	3.44	3.29	3.68	4.61

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

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