Johnson Controls Int'l PLC (JCI)

Updated May 1st, 2019 by Eli Inkrot

Key Metrics

Current Price:	$39	**5 Year CAGR Estimate:**	9.0%	**Volatility Percentile:**	48.1%
Fair Value Price:	$32	**5 Year Growth Estimate:**	10.0%	**Momentum Percentile:**	57.6%
% Fair Value:	121%	**5 Year Valuation Multiple Estimate:**	-3.7%	**Growth Percentile:**	91.3%
Dividend Yield:	2.7%	**5 Year Price Target**	$52	**Valuation Percentile:**	23.4%
Dividend Risk Score:	F	**Retirement Suitability Score:**	D	**Total Return Percentile:**	51.8%

Overview & Current Events

Johnson Controls, originally founded in 1885, is a $35 billion industrial company that offers Building Solutions (cooling, heating, ventilation and security) around the world, with roughly 40% of its sales coming from North America. Johnson Controls is headquartered in Ireland after its merger with Tyco in 2016. In November of 2018 the company announced it was selling its Power Solutions business. Reference to this segment moving forward is reported as "discontinued operations." The Power business made up about a fourth of Johnson Control's business and this sale now makes the company a "pure play" buildings technologies and solutions provider.

On April 30th, 2019 Johnson Controls completed the sale of its Power Business for $11.6 billion in net proceeds. The company expects to use $3.4 billion to repay debt and the remaining $8.2 billion to fund share repurchases. Indeed, the company has already announced plans to launch a $4.0 billion tender offer for its shares at prices ranging from $36 to $40. In addition, the purchase of $1.5 billion of the company's outstanding notes was indicated.

On May 1st, 2019 Johnson Controls reported Q2 2019 results for the period ending March 31st, 2019 (note Johnson Controls fiscal year ends September 30th). Sales came in at $5.78 billion, a 2.6% increase compared to Q2 2018, and a 6% increase on an organic basis. Adjusted net income from operations totaled $287 million, up 17%, while diluted earnings-per-share totaled $0.32 against $0.26 previously.

Johnson Controls also updated its guidance for fiscal year 2019, anticipating adjusted earnings-per-share to come in between $1.85 and $1.95 (from $1.75 to $1.85 previously). Keep in mind that this now excludes the Power Business and only accounts for continuing operations.

Growth on a Per-Share Basis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
EPS	$0.47	$2.00	$2.42	$2.54	$2.66	$3.19	$3.42	$3.98	$2.60	$1.59	***$1.90***	***$3.06***
DPS	$0.52	$0.55	$0.64	$0.72	$0.76	$0.88	$1.04	$1.16	$1.00	$1.04	***$1.04***	***$1.20***
Shares	669	674	680	682	685	666	647	936	928	932	***870***	***750***

The Johnson Controls of today looks very different from the Johnson Controls of five years ago due to the Tyco merger and automotive business spinoff, which is now publicly traded as Adient (ADNT). The 2016 merger with Tyco relocated Johnson Controls to Ireland for tax purposes. Yet Tax legislation changes in the U.S. meant that the benefit of that move has evaporated and Johnson Controls was left with the integration costs of the merger.

Moreover, the complexity of looking back at historical numbers continues to evolve with the recent sale of the Power Business. We have kept the historical numbers through 2017, but we have inputted only earnings from continuing operations starting with 2018. We believe the Building Solutions segment ought to do well, but keep in mind that the business results could be increasingly volatile, as the company has become more and more concentrated.

After the sale of the Power business, Johnson Controls has good deal of financial flexibility, which it will utilize to retire debt and buy back a significant amount of shares (~25% of the current market cap). This, combined with general economic growth in its building solutions segment, ought to continue Johnson Control's growth path, which we are modeling at 10% annually over the intermediate-term.

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Valuation Analysis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	Now	2024
Avg. P/E	40.0	14.5	15.4	11.9	12.7	15.0	13.9	10.5	16.2	16.0	***20.5***	***17.0***
Avg. Yld.	2.8%	1.9%	1.7%	2.4%	2.2%	1.8%	2.2%	2.8%	2.4%	2.8%	***2.7%***	***2.3%***

Looking at the 2010 through 2018 period, shares of Johnson Controls have traded hands with an average P/E ratio of about 14 times earnings. Against a current multiple over 20 times earnings, this appears to be elevated. However, this does not take into account the currently depressed earnings as a result of the sale of the Power Business, to go along with the idea that Johnson Controls has a significant amount of proceeds to be redeployed. Our fair value estimate is 17 times earnings, which still implies a valuation headwind, but this is weighed against an enhanced growth rate as share repurchases pick up steam in the years to come.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
Payout	111%	27%	26%	28%	29%	28%	30%	29%	39%	65%	***55%***	***39%***

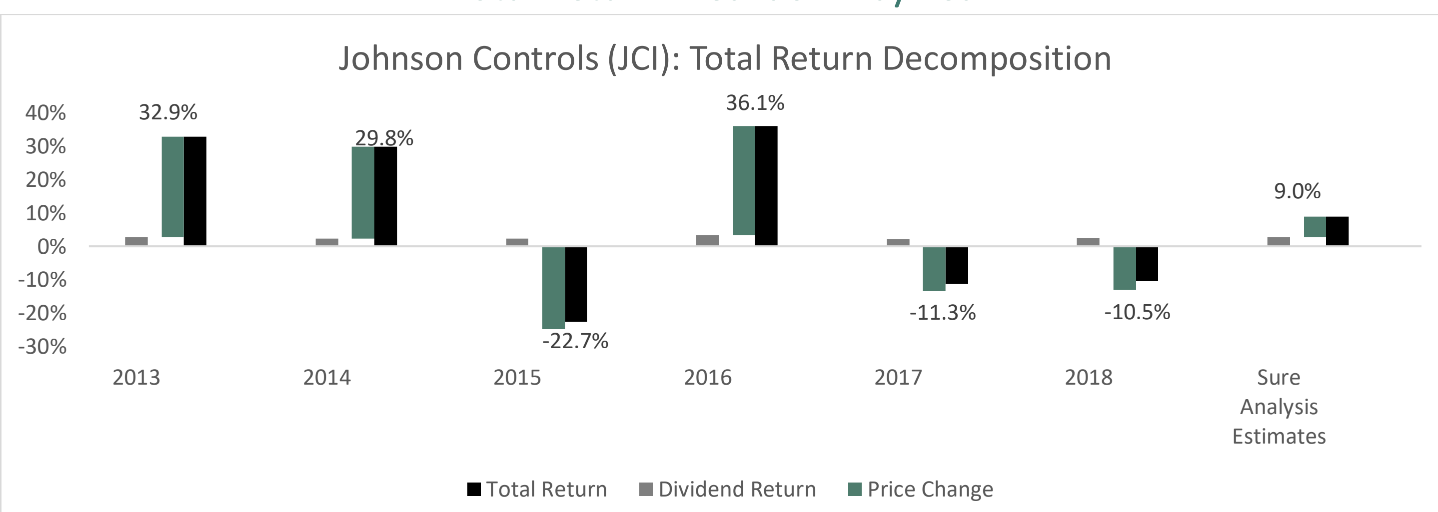
Johnson Controls is one of the key players in the building construction industry, where it provides products and services for heating, ventilation, cooling and security systems. The company's sales network and expertise are hard to replicate for new entrants. Moreover, the sale of the Power business ought to lead to financial flexibility, an increased focus on secular growth trends, lower capital intensity, and margin expansion.

As of the most recent report, Johnson Controls held $12.8 billion in cash and $48.5 billion in total assets against $13.4 billion in current liabilities and $28.5 billion in total liabilities.

Final Thoughts & Recommendation

Shares are up 15% since our last update. Johnson Controls business continues to transform, with the newest iteration being a "pure play" Buildings Solution company. It should be noted that this transformation comes with added uncertainty in the way of a less diversified business. We are forecasting 9% annual total return potential, driven by 10% growth, a 2.7% starting dividend yield and a 3.7% valuation headwind. We are reducing our rating from buy to hold, noting that recession performance is likely to be poor.

Total Return Breakdown by Year



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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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Income Statement Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Revenue	28497	34305	40833	40604	37145	38749	17100	20837	30172	31400
Gross Profit	3549	5221	6059	5837	6146	6305	4531	5654	9339	9380
Gross Margin	12.5%	15.2%	14.8%	14.4%	16.5%	16.3%	26.5%	27.1%	31.0%	29.9%
SG&A Exp.	3210	3796	4393	4311	3627	4216	3191	4190	6158	6010
D&A Exp.	745	691	731	824	952	955	860	953	1188	1085
Operating Profit	339	1425	1666	1526	2519	2089	1340	1464	3181	3370
Op. Margin	1.2%	4.2%	4.1%	3.8%	6.8%	5.4%	7.8%	7.0%	10.5%	10.7%
Net Profit	-338	1307	1415	1184	1178	1215	1563	-868	1611	2162
Net Margin	-1.2%	3.8%	3.5%	2.9%	3.2%	3.1%	9.1%	-4.2%	5.3%	6.9%
Free Cash Flow	270	661	-249	-272	1309	1196	465	659	-1312	1483
Income Tax	32	127	258	161	674	407	71	197	705	518

Balance Sheet Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Total Assets	24088	25743	29676	30954	31518	32804	29622	63179	51884	48797
Cash & Equivalents	761	560	257	265	1055	409	597	579	321	200
Acc. Receivable	5528	6095	7151	7308	7206	5871	5751	6394	6666	7065
Inventories	1521	1786	2316	2343	2325	2477	2377	2888	3209	3224
Goodwill & Int.	7288	7242	7961	7929	7588	8766	8340	28564	26429	25821
Total Liabilities	14749	15370	18496	19181	18944	21242	19124	38089	30517	26339
Accounts Payable	4434	5426	6159	6114	6318	5270	5174	4000	4271	4644
Long-Term Debt	3966	3389	5146	6068	5498	6680	6610	12759	13572	10995
Total Equity	9100	10071	11042	11625	12314	11311	10335	24118	20447	21164
D/E Ratio	0.44	0.34	0.47	0.52	0.45	0.59	0.64	0.53	0.66	0.52

Profitability & Per Share Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Return on Assets	-1.4%	5.2%	5.1%	3.9%	3.8%	3.8%	5.0%	-1.9%	2.8%	4.3%
Return on Equity	-3.6%	13.6%	13.4%	10.4%	9.8%	10.3%	14.4%	-5.0%	7.2%	10.4%
ROIC	-2.5%	9.7%	9.4%	6.9%	6.6%	6.7%	8.8%	-3.2%	4.4%	6.3%
Shares Out.	669	674	680	682	685	666	647	936	928	932
Revenue/Share	47.87	50.26	59.19	58.97	53.90	57.42	25.85	30.98	31.94	33.70
FCF/Share	0.45	0.97	-0.36	-0.40	1.90	1.77	0.70	0.98	-1.39	1.59

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