



# Air Products & Chemicals Inc. (APD)

Updated August 15<sup>th</sup>, 2019 by Jonathan Weber

## Key Metrics

<b>Current Price:</b>	\$224	<b>5 Year CAGR Estimate:</b>	0.1%	<b>Volatility Percentile:</b>	11.5%
<b>Fair Value Price:</b>	\$148	<b>5 Year Growth Estimate:</b>	6.0%	<b>Momentum Percentile:</b>	95.4%
<b>% Fair Value:</b>	151%	<b>5 Year Valuation Multiple Estimate:</b>	-7.9%	<b>Growth Percentile:</b>	54.7%
<b>Dividend Yield:</b>	2.0%	<b>5 Year Price Target</b>	\$198	<b>Valuation Percentile:</b>	7.5%
<b>Dividend Risk Score:</b>	B	<b>Retirement Suitability Score:</b>	C	<b>Total Return Percentile:</b>	6.5%

## 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 \$51 billion

Air Products & Chemicals reported financial results for the third quarter of fiscal 2019 on July 25. The company generated revenues of \$2.22 billion, which was down 1.8% year over year, and which missed the analyst consensus by \$100 million. Currency rate movements had a major negative impact on Air Products & Chemicals' revenues, as currency adjusted revenues would have been up by 2% year over year, mainly thanks to strong pricing and volume gains of ~3%. A contract modification for its business in India was another headwind for revenues, as was energy cost pass-through, although that was neutral to earnings.

Air Products & Chemicals managed to grow its EBITDA margin to a new record level of 40.1% during the third quarter, which helped the company to generate earnings-per-share of \$2.17 during the quarter, beating estimates slightly. Earnings-per-share grew at a highly attractive rate of 11% compared to the previous year's third quarter. Air Products & Chemicals forecasts earnings-per-share growth of roughly 10%-11% for the current fiscal year.

## 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>\$8.23</b>	<b>\$11.01</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>\$4.64</b>	<b>\$6.48</b>
<b>Shares<sup>1</sup></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 years 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 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.

<sup>1</sup> In Millions

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## Valuation Analysis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	Now	2023
<b>Avg. P/E</b>	19.0	14.9	15.1	15.4	15.6	16.5	20.6	21.7	18.6	23.3	<b>27.2</b>	<b>18.0</b>
<b>Avg. Yld.</b>	1.8%	3.0%	2.5%	2.5%	3.0%	3.1%	2.5%	2.2%	2.4%	2.4%	<b>2.0%</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 more than 27 times this year's net profits, which is why we believe that shares are highly overvalued today. The corresponding multiple contraction that we expect will negatively impact the stock's total returns to a significant degree.

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

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
<b>Payout</b>	44.1%	38.2%	38.9%	46.3%	50.4%	52.2%	48.7%	44.9%	58.8%	60.7%	<b>56.4%</b>	<b>58.9%</b>

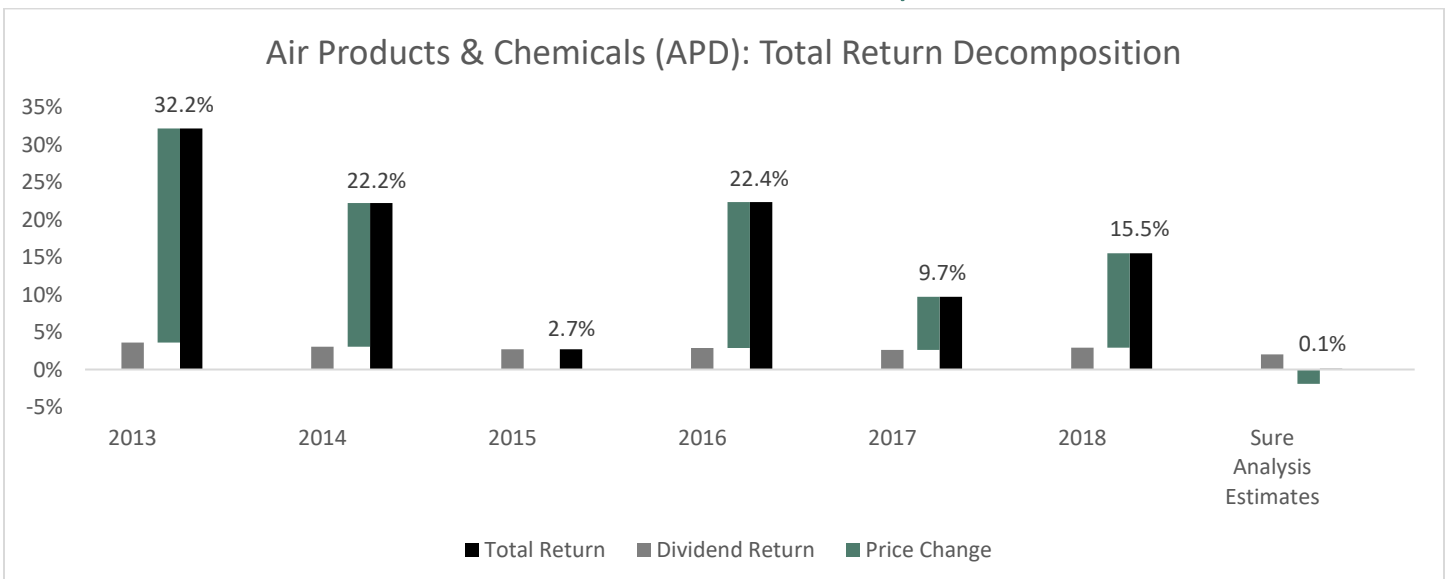
Air Products & Chemicals will pay out slightly less than 60% of its net profits in the form of dividends this year. This is not an especially low payout ratio, but the dividend looks highly sustainable at the current level. The company's reasonable payout ratio also ensures that it can continue its streak 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 an overly 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 is an attractive company at first sight: it holds a multi-decade streak of consecutive dividend increases, a strong globalized business model, and a leadership position in the gases industry. Despite these positives, Air Products & Chemicals appears positioned to deliver very unimpressive total returns because of its overly high valuation multiple. We estimate that Air Products & Chemicals will not generate meaningful annual returns over the coming five years, 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
<b>Revenue</b>	8838	8928	9833	10595	9442	10226	10939	11668	12380	13326
<b>Gross Profit</b>	4016	3898	4125	4392	3868	4185	4511	4828	5110	5483
<b>Gross Margin</b>	45.4%	43.7%	41.9%	41.4%	41.0%	40.9%	41.2%	41.4%	41.3%	41.1%
<b>SG&amp;A Exp.</b>	2190	2127	2315	2453	2200	2370	2497	2637	2783	2972
<b>D&amp;A Exp.</b>	308	309	315	319	251	267	278	289	316	378
<b>Operating Profit</b>	1825	1771	1810	1939	1668	1815	2014	2191	2327	2512
<b>Operating Margin</b>	20.7%	19.8%	18.4%	18.3%	17.7%	17.7%	18.4%	18.8%	18.8%	18.8%
<b>Net Profit</b>	1333	1211	1254	1389	1406	1516	1453	1493	1733	1621
<b>Net Margin</b>	15.1%	13.6%	12.8%	13.1%	14.9%	14.8%	13.3%	12.8%	14.0%	12.2%
<b>Free Cash Flow</b>	1309	1455	1428	1661	1342	1518	1639	1511	1655	2044
<b>Income Tax</b>	575	656	673	727	588	637	694	741	798	550

## Balance Sheet Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
<b>Total Assets</b>	25352	26862	34238	30817	32268	32060	33111	43670	37180	37089
<b>Cash &amp; Equivalents</b>	2265	1643	1389	1548	1699	1584	1639	3191	2780	2170
<b>Acc. Receivable</b>	1051	1037	1288	1315	1516	1415	1547	1743	1704	1984
<b>Goodwill &amp; Int.</b>	2954	2926	3789	3750	3682	2375	2297	2216	2361	3130
<b>Total Liabilities</b>	20029	21383	28228	24703	26078	25390	28302	39188	33203	33629
<b>Accounts Payable</b>	130	150	153	167	157	152	195	152	150	135
<b>Long-Term Debt</b>	773	40	34	17	15	12	9	2008	2002	2002
<b>Total Equity</b>	5323	5479	6010	6114	6190	6670	4809	4482	3977	3460
<b>D/E Ratio</b>	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
<b>Return on Assets</b>	5.4%	4.6%	4.1%	4.3%	4.5%	4.7%	4.5%	3.9%	4.3%	4.4%
<b>Return on Equity</b>	25.6%	22.4%	21.8%	22.9%	22.9%	23.6%	25.3%	32.1%	41.0%	43.6%
<b>ROIC</b>	23.7%	20.9%	21.7%	22.8%	22.8%	23.5%	25.3%	26.4%	27.8%	28.3%
<b>Shares Out.</b>	211.3	213.8	210.2	212.5	211.2	213.5	215.4	217.4	218.3	220.9
<b>Revenue/Share</b>	17.47	17.72	19.73	21.53	19.38	21.17	22.99	25.41	27.49	30.06
<b>FCF/Share</b>	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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