Deere & Company (DE)

Updated November 27th, 2019 by Eli Inkrot

Key Metrics

Current Price:	$171	**5 Year CAGR Estimate:**	1.2%	**Volatility Percentile:**	69.4%
Fair Value Price:	$123	**5 Year Growth Estimate:**	6.0%	**Momentum Percentile:**	52.8%
% Fair Value:	140%	**5 Year Valuation Multiple Estimate:**	-6.4%	**Growth Percentile:**	57.2%
Dividend Yield:	1.8%	**5 Year Price Target**	$164	**Valuation Percentile:**	20.4%
Dividend Risk Score:	C	**Retirement Suitability Score:**	D	**Total Return Percentile:**	16.4%

Overview & Current Events

Deere & Company is the largest manufacturer of farm equipment in the world. The company also makes equipment used in construction, forestry & turf care, produces engines and provides financial solutions to its customers. Deere was founded in 1837, is headquartered in Moline, Illinois and is currently valued at $55 billion.

On November 27th, 2019 Deere reported Q4 fiscal year 2019 results for the period ending November 3rd, 2019. For the quarter sales came in at $9.90 billion, representing a 5.1% increase compared to Q4 2018. The Equipment Operations, Agriculture & Turf and Construction & Forestry segments saw sales increases of 4%, 3% and 8% respectively during the quarter. Adjusted Net Income equaled $681 million compared to $748 million in Q4 2018, while adjusted earnings-per-share equaled $2.14 versus $2.30 previously, helped slightly by a lower share count.

For the year revenue equaled $39.26 billion, also representing a 5.1% increase compared to 2018. Equipment Operations, Agriculture & Turf and Construction & Forestry saw respective sales improvements of 5%, 2% and 10%. Adjusted Net Income for the year totaled $3.19 billion (just below prior guidance of about $3.2 billion) compared to $3.07 billion in 2018. Meanwhile, adjusted earnings-per-share came in at $9.94 versus $9.39 previously.

Deere also provided an outlook for fiscal year 2020. For next year the company anticipates Net Income of $2.7 billion to $3.1 billion, indicating the expectation of company-wide earnings falling -15.4% to -2.8%.

Growth on a Per-Share Basis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
EPS	$4.35	$6.36	$7.64	$9.08	$8.63	$5.77	$4.81	$6.68	$9.39	$9.94	***$9.10***	***$12.18***
DPS	$1.16	$1.52	$1.79	$1.99	$2.22	$2.40	$2.40	$2.40	$2.58	$3.04	***$3.04***	***$3.88***
Shares[1]	422	406	388	374	346	317	315	322	318	321	***320***	***305***

Deere's earnings-per-share are relatively cyclical. Depending on the conditions in the markets the company addresses (agriculture, forestry, and construction), demand for Deere's products can wary widely on a year-to-year basis. Overall the earnings-per-share growth trend is positive, but it took Deere five years to grow its EPS above the peak from 2013. Still, dating back to 2008 Deere has been able to grow its earnings-per-share by an average compound rate of 7% per annum. That said, earnings are expected to be materially lower this year. Moving forward we believe 6% annual growth is achievable, despite recent uncertainties.

During fiscal 2020 and beyond there are several factors that could prove positive for the company's profitability. For instance, acquisitions such as the takeover of Wirtgen Group that closed during December of 2017. Wirtgen is a German manufacturer of construction machinery, which has increased Deere's market share in this segment considerably. Expanding its presence in the construction machinery industry is an opportunistic move by Deere, as growth rates in the construction machinery business are higher than in the agriculture & turf business. With a wider presence in construction machinery Deere should be able to benefit from strong construction activity in markets such as the US and China. Although, the current trade war with China puts a large question mark over this area and indeed over the business in general.

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[1] In millions.

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In addition, Deere could ramp up its share repurchases in the near future. The company reduced its share count by -25% in the 2008 to 2016 timeframe, but its share count has been stagnant since. During fiscal 2018, Deere spent $1 billion on buybacks, which is still well below the peak buyback level from 2015, when Deere bought back $2.5 billion worth of stock in a single year.

Valuation Analysis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	Now	2025
Avg. P/E	13.7	12.5	10.4	9.5	10.1	15.2	16.7	17.1	16.1	15.7	***18.8***	***13.5***
Avg. Yld.	1.9%	1.8%	2.3%	2.3%	2.5%	2.7%	3.0%	2.1%	1.7%	1.9%	***1.8%***	***2.4%***

During the past decade shares of Deere have traded hands with an average P/E ratio between 13 and 14 times earnings. We believe this is a fair starting place, considering the company's reasonable growth prospects coupled with its cyclical nature. With a current valuation near 19 times earnings, this could imply a significant valuation headwind.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
Payout	27%	24%	23%	22%	26%	42%	50%	36%	27%	31%	***33%***	***32%***

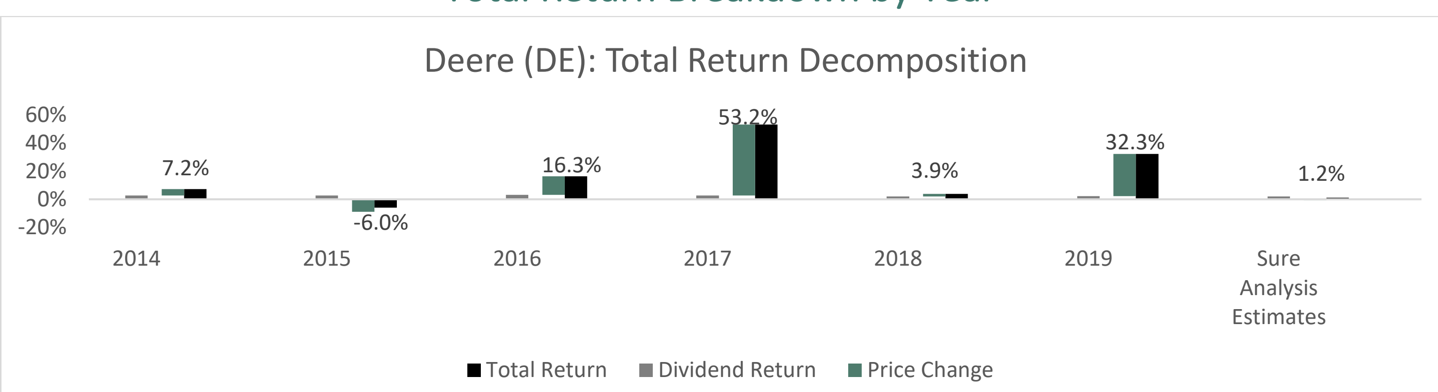
Deere's dividend payout ratio has never been especially high. The company paid out a maximum of ~50% of its net profits during 2016. Since then, the payout ratio has trended downwards as earnings-per-share have risen considerably. We believe that the dividend is quite safe, but dividend growth has not been overly reliable in the past – during 2015 to 2017 the company froze its dividend at $2.40 each year.

Deere is the largest player in the agricultural machinery manufacturing industry. This means that it is hard for new competitors to steal market share from Deere, especially since it is difficult to replicate the company's global sales and dealership network. Deere has also been growing its presence in the higher-growth construction machinery market, both organically as well as via takeovers. The company is impacted by downturns in the industries it addresses. During the last financial crisis Deere remained profitable, but its earnings-per-share declined by 40%.

Final Thoughts & Recommendation

Shares are up 14% since our last report, while earnings expectations have declined. Deere is the market leader in the agricultural equipment industry. The company's global presence provides sizeable competitive advantages. Growth has been acceptable during the last decade, and quite strong during 2018. However, total return potential comes in at just 1.2% per annum, stemming from 6% expected growth and a 1.8% dividend yield offset by the potential for a significant valuation headwind. As a result, we are moving our rating from hold to sell.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Revenue	25873	31842	35963	37621	35816	28609	26364	29116	37021	39258
Gross Profit	7464	9048	10051	11069	10225	7626	7242	8182	10036	11000
Gross Margin	28.9%	28.4%	27.9%	29.4%	28.5%	26.7%	27.5%	28.1%	27.1%	28.0%
SG&A Exp.	3115	3362	3662	3810	3608	3056	2979	3285	3631	3551
D&A Exp.	915	915	1004	1140	1307	1382	1560	1716	1927	2019
Operating Profit	3015	4212	4720	5468	4781	2755	2134	2762	4056	4088
Op. Margin	11.7%	13.2%	13.1%	14.5%	13.3%	9.6%	8.1%	9.5%	11.0%	10.4%
Net Profit	1865	2800	3065	3537	3162	1940	1524	2159	2368	3253
Net Margin	7.2%	8.8%	8.5%	9.4%	8.8%	6.8%	5.8%	7.4%	6.4%	8.3%
Free Cash Flow	969	646	-953	879	867	933	815	-393	-1130	-37
Income Tax	1162	1424	1659	1946	1627	840	700	971	1727	852

Balance Sheet Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Total Assets	43267	48207	56266	59521	61336	57948	57919	65786	70108	73011
Cash & Equivalents	3791	3647	4652	3504	3787	4162	4336	9335	3904	3857
Acc. Receivable	23385	26123	29576	33544	35302	32695	31840	33188	36080	38808
Inventories	3063	4371	5170	4935	4210	3817	3341	3904	6149	5975
Goodwill & Int.	1116	1127	1026	922	860	790	920	1251	4663	4297
Total Liabilities	36963	41393	49404	49254	52271	51190	51388	56226	58817	61594
Accounts Payable	2277	2675	2986	2739	2325	1872	2096	2551	2894	
Long-Term Debt	24349	26589	32421	34476	36958	36850	35612	40045	42257	45334
Total Equity	6290	6800	6842	10266	9063	6743	6520	9557	11288	11413
D/E Ratio	3.87	3.91	4.74	3.36	4.08	5.46	5.46	4.19	3.74	3.97

Profitability & Per Share Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Return on Assets	4.4%	6.1%	5.9%	6.1%	5.2%	3.3%	2.6%	3.5%	3.5%	4.5%
Return on Equity	33.6%	42.8%	44.9%	41.4%	32.7%	24.5%	23.0%	26.9%	22.7%	28.7%
ROIC	6.2%	8.7%	8.4%	8.4%	7.0%	4.3%	3.6%	4.7%	4.6%	5.9%
Shares Out.	422	406	388	374	346	317	315	322	318	321
Revenue/Share	60.37	75.38	89.57	96.66	97.83	85.15	83.27	90.06	113.11	122.45
FCF/Share	2.26	1.53	-2.37	2.26	2.37	2.78	2.57	-1.21	-3.45	-0.12

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