Rockwell Automation (ROK)

Updated December 2nd, 2019 by Josh Arnold

Key Metrics

Current Price:	$196	**5 Year CAGR Estimate:**	4.0%	**Volatility Percentile:**	63.7%
Fair Value Price:	$160	**5 Year Growth Estimate:**	6.0%	**Momentum Percentile:**	56.1%
% Fair Value:	122%	**5 Year Valuation Multiple Estimate:**	-3.9%	**Growth Percentile:**	57.0%
Dividend Yield:	2.1%	**5 Year Price Target**	$214	**Valuation Percentile:**	33.0%
Dividend Risk Score:	C	**Retirement Suitability Score:**	D	**Total Return Percentile:**	27.4%

Overview & Current Events

Rockwell Automation is an industrial company that is active in the industrial automation and information segments. Its business units include Architecture & Software as well as Control Products & Solutions. The company was founded in 1928, is headquartered in Milwaukee, WI, produces about $7 billion in annual revenue, and is currently trading with a market capitalization of $23 billion.

Rockwell reported Q4 and full-year fiscal 2019 earnings on 11/12/19. Total revenue was $6.7 billion for the full-year, up 0.4% against fiscal 2018. Organic sales rose nicely, adding 2.8% in fiscal 2019 while currency translation offset most of that, reducing the top line by -2.4% for the year.

Pre-tax margin was 13.5% of revenue for the year, down from 20% in the prior year. The decline was due to the revaluation of the company's investment of PTC, Inc., as fair value declined significantly. Total segment operating margin, which excludes the PTC revaluation, was up 40bps year-over-year to 22% of revenue. That meant total segment earnings rose 2.2%, up to $1.47 billion.

Total earnings came to $8.67 per share on an adjusted basis, up 7% from $8.11 in the prior year. Organic sales gains were the primary reason why adjusted earnings rose, along with slightly better segment operating margins.

The company guided for organic sales growth of -1.5% to +1.5% in fiscal 2020, and for adjusted earnings-per-share of $8.70 to $9.10 for the year. Our initial estimate is the midpoint of that guidance at $8.90.

Growth on a Per-Share Basis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
EPS	$3.05	$4.79	$5.13	$5.36	$5.91	$6.09	$5.56	$6.35	$8.11	$8.67	***$8.90***	***$11.91***
DPS	$1.22	$1.48	$1.75	$1.98	$2.32	$2.60	$2.90	$3.04	$3.68	$3.88	***$4.08***	***$5.46***
Shares[1]	142	142	140	139	137	132	129	128	122	117	***117***	***110***

Between 2007 and 2018 Rockwell Automation grew its earnings-per-share by 7.9% annually. Profits declined substantially during the financial crisis, though. Between 2008 and 2009, Rockwell Automation's earnings-per-share were cut in half, which shows that the company's business is quite cyclical.

Rockwell Automation's strong earnings growth during fiscal 2018 was due to fundamental improvements. Higher sales, margin increases, and a decline in the company's share count explain how the company was able to grow its earnings-per-share by 28% during fiscal 2018. However, those gains were not repeated in fiscal 2019, and we expect 6% annual earnings-per-share growth in the coming years.

Rockwell sees long-term tailwinds from its China business, as well as from other emerging markets such as Brazil and Mexico in Latin America. Trade troubles between the US and China, and worries about an economic slowdown around the globe have led to some deterioration in Rockwell's short-term growth outlook, and the company sees roughly flat organic sales for fiscal 2020 as a result. Share repurchases were a driver for earnings-per-share in the past, and this will likely remain the same going forward.

[1] In Millions

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	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	Now	2025
Avg. P/E	16.9	15.8	14.3	16.2	19.9	18.7	19.7	23.6	23.4	19.1	***22.0***	***18.0***
Avg. Yld.	2.4%	1.9%	2.4%	2.3%	2.0%	2.3%	2.7%	2.0%	2.1%	2.3%	***2.1%***	***2.5%***

Rockwell Automation trades at 22 times the net profits that the company's management forecasts for the current fiscal year. This means that shares are trading well in excess of our estimate of fair value, which we assess at 18 times earnings. The recent rally in the stock has made it far less attractive on a valuation and yield basis. We see a ~4% headwind to total returns in the coming years from the valuation.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
Payout	40%	31%	34%	37%	39%	43%	52%	48%	45%	45%	***46%***	***46%***

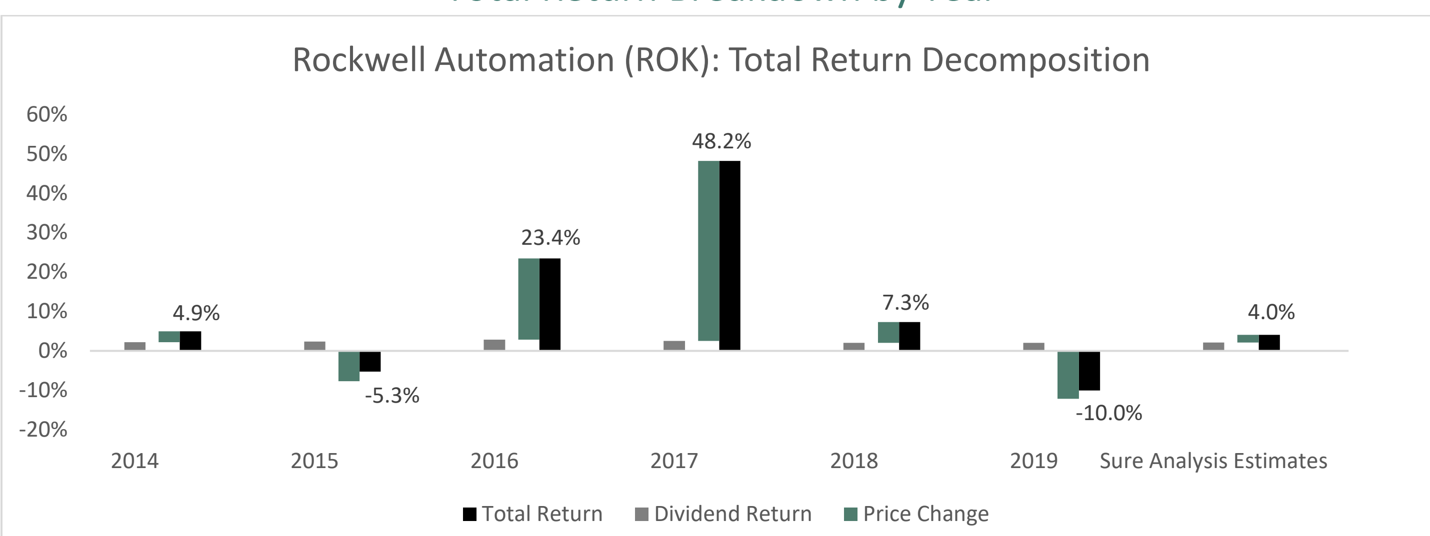
Rockwell's dividend payout ratio has been around 40% throughout the majority of the last decade, although the payout ratio was substantially higher during the last financial crisis. The company did not have to cut its dividend during the especially harsh recession, though, which makes us believe that the company's dividend is relatively safe, despite the cyclicality of its business.

Rockwell's earnings-per-share dropped by more than -50% from 2008 to 2009, which shows that the company is somewhat vulnerable to broad economic downturns. During a more benign, smaller recession, the company would likely see its earnings-per-share decline to a smaller degree. Rockwell is well positioned internationally, as it produces roughly half of its sales outside of the US. Rockwell's strong position in the higher-growth emerging markets could provide a growth advantage versus its peers.

Final Thoughts & Recommendation

Rockwell Automation operates a business that can be cyclical, but the company managed to generate solid earnings-per-share growth throughout the last decade, even though the last financial crisis was an exceptionally harsh recession. However, we rate the stock a sell as shares trade well in excess of our fair value estimate at current prices.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Revenue	4857	6000	6259	6352	6624	6308	5880	6311	6666	6695
Gross Profit	1936	2390	2523	2574	2754	2703	2476	2668	2885	2900
Gross Margin	39.9%	39.8%	40.3%	40.5%	41.6%	42.9%	42.1%	42.3%	43.3%	43.3%
SG&A Exp.	1323	1461	1492	1538	1570	1506	1467	1558	1588	1539
D&A Exp.	127	131	139	145	153	163	172	169	165	152
Operating Profit	613	929	1031	1036	1184	1197	1008	1110	1297	1362
Operating Margin	12.6%	15.5%	16.5%	16.3%	17.9%	19.0%	17.1%	17.6%	19.5%	20.3%
Net Profit	464	698	737	756	827	828	730	826	536	696
Net Margin	9.6%	11.6%	11.8%	11.9%	12.5%	13.1%	12.4%	13.1%	8.0%	10.4%
Free Cash Flow	395	524	579	869	892	1065	830	892	1175	1049
Income Tax	104	171	229	225	307	300	213	212	795	205

Balance Sheet Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Total Assets	4748	5285	5637	5845	6224	6405	7101	7162	6262	6113
Cash & Equivalents	813	989	904	1201	1191	1427	1526	1411	619	1018
Accounts Receivable		1063	1187	1186	1216	1041	1079	1136	1190	1179
Inventories	603	642	619	615	588	536	527	559	582	576
Goodwill & Int. Ass.	1130	1171	1158	1236	1297	1258	1329	1316	1291	1265
Total Liabilities	3288	3537	3785	3259	3566	4148	5111	4498	4645	5709
Accounts Payable	436	609	716	722	705	694	720	812	920	894
Long-Term Debt	905	905	1062	1084	1225	1501	1965	1844	1776	2257
Shareholder's Equity	1460	1748	1852	2586	2658	2257	1990	2664	1618	404
D/E Ratio	0.62	0.52	0.57	0.42	0.46	0.67	0.99	0.69	1.10	5.58

Profitability & Per Share Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Return on Assets	10.3%	13.9%	13.5%	13.2%	13.7%	13.1%	10.8%	11.6%	8.0%	11.2%
Return on Equity	33.4%	43.5%	40.9%	34.1%	31.5%	33.7%	34.4%	35.5%	25.0%	68.8%
ROIC	20.2%	27.8%	26.5%	23.0%	21.9%	21.7%	18.9%	19.5%	13.6%	23.0%
Shares Out.	142	142	140	139	137	132	129	128	122	117
Revenue/Share	33.73	41.33	43.65	45.08	47.41	46.48	44.85	48.59	52.53	56.12
FCF/Share	2.74	3.61	4.04	6.16	6.39	7.85	6.33	6.87	9.26	8.79

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