



# Parker-Hannifin Corporation (PH)

Updated May 12<sup>th</sup>, 2020 by Aristofanis Papadatos

## Key Metrics

<b>Current Price:</b>	\$158	<b>5 Year CAGR Estimate:</b>	9.5%	<b>Market Cap:</b>	\$20.6 B
<b>Fair Value Price:</b>	\$141	<b>5 Year Growth Estimate:</b>	10.0%	<b>Ex-Dividend Date:</b>	5/7/2020
<b>% Fair Value:</b>	112%	<b>5 Year Valuation Multiple Estimate:</b>	-2.3%	<b>Dividend Payment Date:</b>	6/5/2020
<b>Dividend Yield:</b>	2.2%	<b>5 Year Price Target</b>	\$227	<b>Years Of Dividend Growth:</b>	63
<b>Dividend Risk Score:</b>	A	<b>Retirement Suitability Score:</b>	B	<b>Last Dividend Increase:</b>	15.8%

## Overview & Current Events

Parker-Hannifin is a diversified industrial manufacturer specializing in motion and control technologies. The company was founded in 1917 and has grown to a market capitalization of \$20.6 billion with annual revenues of \$14 billion. Parker-Hannifin has paid a dividend for 69 years and has increased that dividend for a remarkable 63 consecutive years.

On October 29<sup>th</sup>, 2019, Parker-Hannifin completed the acquisition of LORD, a leading manufacturer of advanced adhesives and coatings, for \$3.675 billion in cash. On September 16<sup>th</sup>, 2019, Parker-Hannifin completed the acquisition of Exotic Metals Forming Company LLC for \$1.725 billion in cash. These two acquisitions are expected to add \$1.5 billion in annual revenues. Notably Parker-Hannifin has exceeded analysts' earnings-per-share estimates for 19 consecutive quarters.

In late April, Parker-Hannifin reported (4/30/20) financial results for the third quarter of fiscal 2020. Sales remained essentially flat but organic sales fell -7.4% and adjusted earnings-per-share fell -8%, from \$3.17 to \$2.92. The company is experiencing softening demand for its products mostly due to the global recession, which has resulted from the coronavirus. On the bright side, Parker-Hannifin exceeded analysts' earnings-per-share estimates by an impressive \$0.66 in the quarter, as analysts were expecting a much greater effect of the pandemic on results. On the other hand, the effect of the pandemic will be felt much more in the upcoming quarters. As a result, management withdrew its guidance for fiscal 2020, even though there is only one quarter left for the fiscal year of the company. Due to the pandemic, we have lowered our earnings-per-share forecast for the company from \$10.55 to \$9.40.

## Growth on a Per-Share Basis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
<b>EPS</b>	\$3.40	\$6.37	\$7.45	\$6.26	\$6.45	\$7.25	\$6.46	\$8.11	\$10.42	\$11.85	<b>\$9.40</b>	<b>\$15.14</b>
<b>DPS</b>	\$1.01	\$1.25	\$1.54	\$1.70	\$1.86	\$2.37	\$2.52	\$2.58	\$2.81	\$3.16	<b>\$3.52</b>	<b>\$4.80</b>
<b>Shares<sup>1</sup></b>	161.3	155.1	149.6	149.3	148.8	138.4	134.0	133.1	132.4	128.5	<b>129.5</b>	<b>120.0</b>

During the last decade, Parker-Hannifin has more than tripled its earnings-per-share. The growth trajectory of the company will be disrupted this year due to the global recession caused by the coronavirus. Moreover, even after the pandemic, the company will not be able to maintain its historical growth rate, particularly given the deceleration in North America and international markets before the pandemic. We expect the coronavirus crisis to subside and the global economy to recover from next year. As a result, we expect Parker Hannifin to grow its earnings-per-share at a 10.0% average annual rate over the next five years off this year's low base.

Parker-Hannifin's growth will come in part from acquisitions. The \$4.3 billion CLARCOR transaction and the two aforementioned acquisitions are examples of this. Parker Hannifin integrates the new products in its system while it achieves significant synergies.

<sup>1</sup> 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	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	Now	2025
Avg. P/E	14.5	16.7	12.6	10.8	13.9	18.0	16.6	16.3	17.3	14.2	<b>16.8</b>	<b>15.0</b>
Avg. Yld.	2.2%	1.8%	1.6%	1.9%	2.0%	1.6%	2.0%	2.4%	1.8%	1.9%	<b>2.2%</b>	<b>2.1%</b>

Parker-Hannifin has shed -26% in less than three months due to the spread of the coronavirus. The stock is currently trading at a price-to-earnings ratio of 16.8, which is higher than our fair value estimate of 15.0. If the stock reverts to our fair value estimate over the next five years, it will incur a -2.3% annualized drag in its returns.

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

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
Payout	29.7%	19.6%	20.7%	27.2%	28.8%	32.7%	39.0%	31.8%	27.0%	26.7%	<b>37.4%</b>	<b>31.7%</b>

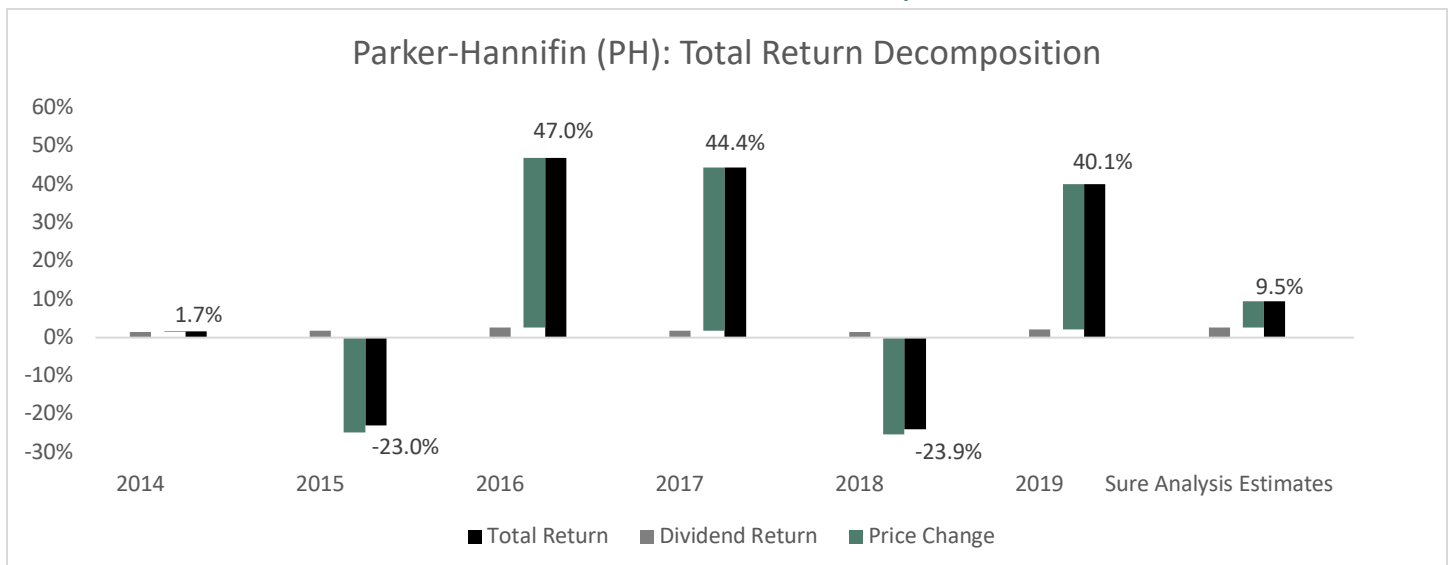
Parker-Hannifin has a number of competitive advantages, including its scale, global distribution network, and technical experience. Parker-Hannifin manufactures components that are relatively obscure yet absolutely critical to the operations of heavy machinery, factory equipment, aircrafts, and other large industrial devices. This is appealing because the company operates in a profitable niche that helps discourage large would-be competitors. The competitive advantage of Parker-Hannifin is clearly reflected in its dividend growth record, which is exceptional, particularly given the high cyclical nature of the industrial sector. The company raised its dividend by 16% last year and it has now raised its dividend for 63 consecutive years.

Due to the recent acquisitions of Parker Hannifin, its interest expense has increased more than 50%. However, its interest expense still consumes only 14% of its operating income. In addition, thanks to its strong free cash flows, Parker-Hannifin will reduce its interest expense at a fast clip, just as it has done after past acquisitions.

## Final Thoughts & Recommendation

Parker-Hannifin has become reasonably valued thanks to the pandemic. We expect Parker-Hannifin to recover strongly as soon as the coronavirus crisis subsides and offer a 9.5% average annual return over the next five years. However, we need a higher expected return amid the uncertainty arising from the pandemic and thus we rate the stock as a hold.

## Total Return Breakdown by Year



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## Income Statement Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Revenue	9,993	12,346	13,146	13,016	13,216	12,712	11,361	12,029	14,302	14,320
Gross Profit	2,146	2,958	3,188	2,929	3,028	3,056	2,537	2,910	3,565	3,617
Gross Margin	21.5%	24.0%	24.2%	22.5%	22.9%	24.0%	22.3%	24.2%	24.9%	25.3%
SG&A Exp.	1,277	1,468	1,519	1,555	1,634	1,545	1,359	1,413	1,640	1,544
D&A Exp.	363	340	322	336	337	317	307	355	466	436
Operating Profit	869	1,491	1,668	1,374	1,394	1,512	1,178	1,497	1,925	2,073
Op. Margin	8.7%	12.1%	12.7%	10.6%	10.5%	11.9%	10.4%	12.4%	13.5%	14.5%
Net Profit	554	1,049	1,152	948	1,041	1,012	807	983	1,061	1,512
Net Margin	5.5%	8.5%	8.8%	7.3%	7.9%	8.0%	7.1%	8.2%	7.4%	10.6%
Free Cash Flow	1,090	960	1,312	925	1,172	1,148	1,061	1,097	1,349	1,535
Income Tax	198	357	421	362	515	420	308	345	641	420

## Balance Sheet Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Total Assets	9,910	10,887	11,170	12,541	13,274	12,279	12,034	15,490	15,320	17,577
Cash & Equivalents	576	657	838	1,781	1,614	1,181	1,222	885	822	3,220
Accounts Receivable	1,443	1,770	1,782	1,841	1,858	1,620	1,594	1,931	2,146	2,131
Inventories	1,172	1,412	1,401	1,377	1,372	1,300	1,173	1,549	1,621	1,678
Goodwill & Int. Ass.	3,936	4,187	4,021	4,514	4,360	3,956	3,826	7,894	7,520	7,237
Total Liabilities	5,451	5,398	6,265	6,799	6,612	7,172	7,455	10,223	9,455	11,609
Accounts Payable	889	1,174	1,195	1,156	1,252	1,092	1,035	1,300	1,430	1,413
Long-Term Debt	1,777	1,766	1,730	2,830	2,325	2,947	3,014	5,870	4,957	7,108
Shareholder's Equity	4,368	5,384	4,897	5,738	6,659	5,104	4,575	5,262	5,860	5,962
D/E Ratio	0.41	0.33	0.35	0.49	0.35	0.58	0.66	1.12	0.85	1.19

## Profitability & Per Share Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Return on Assets	5.6%	10.1%	10.4%	8.0%	8.1%	7.9%	6.6%	7.1%	6.9%	9.2%
Return on Equity	12.8%	21.5%	22.4%	17.8%	16.8%	17.2%	16.7%	20.0%	19.1%	25.6%
ROIC	8.6%	15.6%	16.6%	12.5%	11.9%	11.9%	10.3%	10.5%	9.7%	12.7%
Shares Out.	161.3	155.1	149.6	149.3	148.8	138.4	134.0	133.1	132.4	128.5
Revenue/Share	61.34	74.92	85.00	85.86	87.27	87.60	82.98	88.74	105.61	108.67
FCF/Share	6.69	5.82	8.48	6.10	7.74	7.91	7.75	8.11	9.99	11.65

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

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