



Air Products & Chemicals Inc. (APD)

Updated July 29th, 2020 by Jonathan Weber

Key Metrics

Current Price:	\$290	5 Year CAGR Estimate:	-4.1%	Market Cap:	\$64B
Fair Value Price:	\$151	5 Year Growth Estimate:	6.0%	Ex-Dividend Date:	09/30/20
% Fair Value:	192%	5 Year Valuation Multiple Estimate:	-12.2%	Dividend Payment Date:	11/09/20
Dividend Yield:	1.8%	5 Year Price Target	\$202	Years Of Dividend Growth:	38
Dividend Risk Score:	B	Retirement Suitability Score:	C	Last Dividend Increase:	15.5%

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 38-year streak of consecutive dividend increases qualifies it to be a member of the Dividend Aristocrats Index. The company is headquartered in Allentown, Pennsylvania.

Air Products & Chemicals reported financial results for the third quarter of fiscal 2020 on July 23. The company generated revenues of \$2.1 billion during the quarter, which was down 7% year-over-year, but which beat the analyst consensus nevertheless. Energy cost pass-through was a headwind for Air Products & Chemicals' revenues, although that was neutral to the company's earnings, as lower energy prices also led to lower expenses. The company also felt some headwinds from the coronavirus pandemic, which slowed down demand for some of its products.

Air Products & Chemicals managed to grow its EBITDA margin to 42.7% during the quarter, up 260 basis points year-over-year, which helped the company to generate earnings-per-share of \$2.01 during the quarter. Earnings-per-share declined by 7% compared to the previous year's quarter, mainly due to the impact of lower revenues caused by the pandemic. It still looks like, overall, earnings-per-share will grow versus 2019 during the current year, as demand should pick up in Q3, and since Q1 and Q2 were quite strong as well.

Growth on a Per-Share Basis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
EPS	\$5.02	\$5.73	\$5.40	\$5.50	\$5.78	\$6.57	\$7.55	\$6.31	\$7.45	\$8.21	\$8.40	\$11.24
DPS	\$1.92	\$2.23	\$2.50	\$2.77	\$3.02	\$3.20	\$3.39	\$3.71	\$4.40	\$4.58	\$5.36	\$7.52
Shares¹	213.8	210.2	212.5	211.2	213.5	215.4	217.4	218.3	220.9	220.7	220.0	220.0

Between 2010 and 2019, Air Products & Chemicals generated earnings-per-share growth of 6% annually, which is a 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. 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. During the third quarter, Air Products & Chemicals also announced a new \$7 billion Carbon-Free Hydrogen joint venture with ACWA Power and NEOM that will drive its green energy exposure. These investments, coupled with margin growth initiatives, should lead to meaningful earnings growth for the company over the coming years.

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	15.1	15.4	15.6	16.5	20.6	21.7	18.6	22.6	21.8	27.0	34.5	18.0
Avg. Yld.	2.5%	2.5%	3.0%	3.1%	2.5%	2.2%	2.4%	2.6%	2.6%	2.1%	1.8%	3.7%

Air Products & Chemicals has never traded at an especially low valuation, but more recently its shares have become even more expensive. Based on current estimates, shares are trading for around 35 times this year's net profits right now, which is why we believe that shares are heavily 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	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
Payout	38.2%	38.9%	46.3%	50.4%	52.2%	48.7%	44.9%	58.8%	59.1%	55.8%	63.8%	66.9%

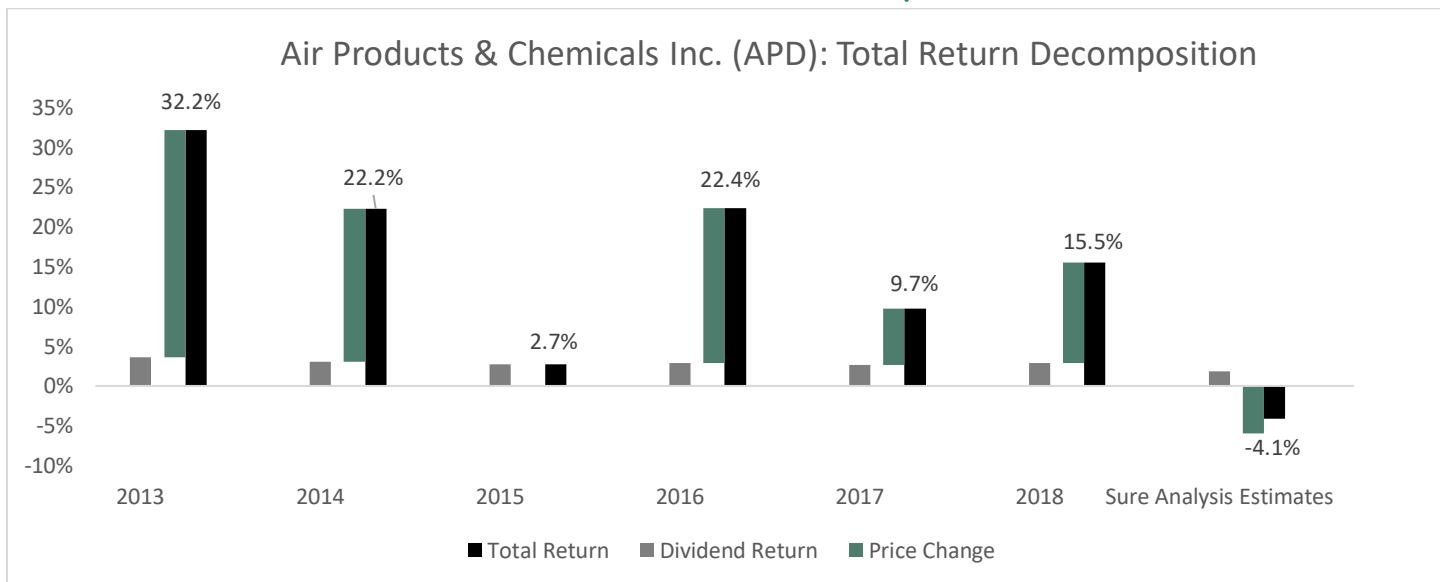
Air Products & Chemicals will pay out roughly 65% of its net profits in the form of dividends this year. This is not an especially low payout ratio, but the dividend looks easily sustainable at the current level. The company's reasonable payout ratio also ensures that it can continue its streak of dividend 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 the full range of identical services in a particular geographic region. Air Products & Chemicals operates a relatively recession-resistant business. Earnings-per-share declined by just 18% in 2009, during the Great Recession, one of the steepest downturns of the last decades.

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 quite unimpressive total returns due to its overly high valuation. We estimate that Air Products & Chemicals will not generate meaningful positive 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	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Revenue	8616	9674	9612	10180	10439	7824	7504	8188	8930	8919
Gross Profit	2327	2575	2560	2708	2809	2226	2326	2436	2741	2943
Gross Margin	27.0%	26.6%	26.6%	26.6%	26.9%	28.5%	31.0%	29.8%	30.7%	33.0%
SG&A Exp.	898	942	947	1089	1060	792	684	714	761	750
D&A Exp.	827	834	841	907	957	859	855	866	971	1083
Operating Profit	1334	1545	1519	1533	1648	1385	1613	1756	1963	2170
Operating Margin	15.5%	16.0%	15.8%	15.1%	15.8%	17.7%	21.5%	21.4%	22.0%	24.3%
Net Profit	1029	1224	1167	994	992	1278	631	3000	1498	1760
Net Margin	11.9%	12.7%	12.1%	9.8%	9.5%	16.3%	8.4%	36.6%	16.8%	19.7%
Free Cash Flow	534	444	278	43	824	1307	1753	528	974	980
Income Tax	306	375	287	308	369	300	433	261	524	480

Balance Sheet Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Total Assets	13506	14291	16942	17850	17779	17335	18029	18467	19178	18943
Cash & Equivalents	374	421	454	450	337	206	1293	3274	2791	2249
Acc. Receivable	1482	1362	1545	1544	1486	1406	1146	1174	1207	1260
Goodwill & Int.	1200	1057	2360	2371	1853	1640	1233	1090	1227	1217
Total Liabilities	7808	8352	10319	10651	10258	9953	10815	8282	8002	7555
Accounts Payable	1702	794	1005	1026	741	622	579	660	595	1636
Long-Term Debt	4128	4562	5292	6274	6119	5879	5211	3963	3813	3326
Total Equity	5547	5796	6477	7042	7366	7249	7080	10086	10858	11054
D/E Ratio	0.74	0.79	0.82	0.89	0.83	0.81	0.74	0.39	0.35	0.30

Profitability & Per Share Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Return on Assets	7.8%	8.8%	7.5%	5.7%	5.6%	7.3%	3.6%	16.4%	8.0%	9.2%
Return on Equity	19.9%	21.6%	19.0%	14.7%	13.8%	17.5%	8.8%	35.0%	14.3%	16.1%
ROIC	10.7%	12.0%	10.4%	7.8%	7.3%	9.5%	4.9%	22.6%	10.3%	11.9%
Shares Out.	213.8	210.2	212.5	211.2	213.5	215.4	217.4	218.3	220.9	220.7
Revenue/Share	39.69	44.46	44.77	47.95	48.51	36.01	34.37	37.25	40.44	40.25
FCF/Share	2.46	2.04	1.29	0.20	3.83	6.02	8.03	2.40	4.41	4.42

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

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