Rockwell Automation (ROK)

Updated July 30th, 2020 by Jonathan Weber

Key Metrics

Current Price:	$218	**5 Year CAGR Estimate:**	1.5%	**Market Cap:**	$25B
Fair Value Price:	$153	**5 Year Growth Estimate:**	6.5%	**Ex-Dividend Date:**	08/10/20[1]
% Fair Value:	142%	**5 Year Valuation Multiple Estimate:**	-6.8%	**Dividend Payment Date:**	09/10/20[2]
Dividend Yield:	1.9%	**5 Year Price Target**	$210	**Years Of Dividend Growth:**	10
Dividend Risk Score:	B	**Retirement Suitability Score:**	D	**Last Dividend Increase:**	5.2%

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, and produces more than $6 billion in annual revenue.

Rockwell reported its third quarter (fiscal 2020) earnings results on July 28. Total revenue was $1.39 billion for the quarter, which was down 17% against the previous year's quarter. Organic sales were down 18% year-over-year, while acquisitions had a small positive impact on the company's reported revenue growth rate. Rockwell Automation's profitability was better than expected during the quarter, although profits were still down a lot versus the 2019.

Rockwell Automation's third quarter earnings-per-share came in at $1.27 on an adjusted basis, which was better than expected by the analyst community. Management believes that the impact that the coronavirus crisis will have on its earnings will decline going forward, which is why the forecast for this year's earnings-per-share has been increased to $7.40 to $7.60, or $7.50 at the midpoint. This is not reflecting the underlying earnings power, which we see at $8.50. We use this number to calculate fair value, in order to adjust for one-time issues during 2020 that will not occur again.

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	***$7.50***	***$11.65***
DPS	$1.22	$1.48	$1.75	$1.98	$2.32	$2.60	$2.90	$3.04	$3.68	$3.88	***$4.08***	***$5.72***
Shares[3]	142	142	140	139	137	132	129	128	122	117	***114***	***110***

Between 2007 and 2019, Rockwell Automation grew its earnings-per-share at a very solid pace of 8% 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 can be quite cyclical.

Rockwell Automation's strong earnings growth during fiscal 2018 was due to fundamental improvements and the impact of tax law changes. Higher sales, margin increases, a lower tax rate, and a decline in the company's share count explain how the company was able to grow its earnings-per-share by 28% during one single year. However, those gains were not repeated in fiscal 2019, which is why our long-term estimate is in the single-digits range. Rockwell sees long-term tailwinds from its China business, as well as from other emerging markets such as Brazil, Mexico, and other countries 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 coronavirus crisis has amplified pressures for the current year, which is why management now expects that sales will be down in the high-single-digits this year. This year's earnings decline will, in all likelihood, be more benign than the 50% drop during the financial crisis, however. Eventually, Rockwell Automation should recover from the current crisis, which is why we do not believe that its ultimate value will be permanently impaired by this year's pandemic.

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[1] Estimated date

[2] Estimated date

[3] In Millions

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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	***25.6***	***18.0***
Avg. Yld.	2.4%	1.9%	2.4%	2.3%	2.0%	2.3%	2.7%	2.0%	2.1%	2.3%	***1.9%***	***2.7%***

Rockwell Automation trades at almost 26 times the earnings power estimate for 2020 right now, which backs out one-time headwinds from the coronavirus crisis. This means that shares are trading well in excess of our estimate of fair value, which we see at 18 times earnings. We forecast a substantial multiple compression headwind to total returns in the coming years, as Rockwell Automation's valuation normalizes.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
Payout	40.0%	30.9%	34.1%	36.9%	39.3%	42.7%	52.2%	47.9%	45.4%	44.8%	***48.0%***	***49.1%***

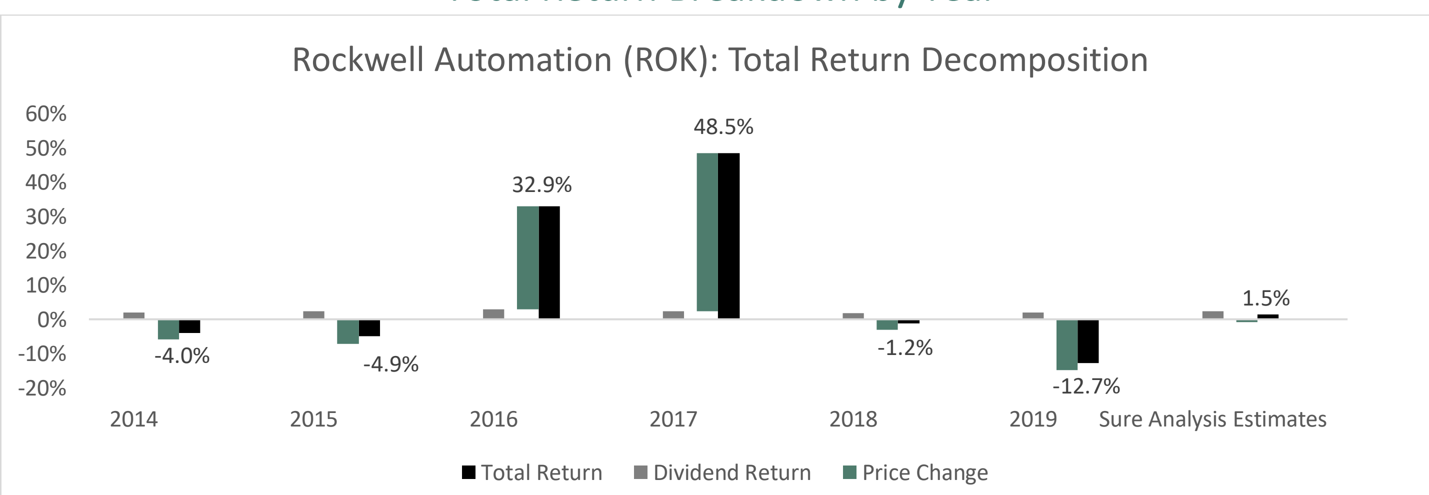
Rockwell's dividend payout ratio has been around 40%-50% throughout the majority of the last decade, although the payout ratio was substantially higher during the last financial crisis. The company did not have to cut its dividend during that especially harsh recession, though, which makes us believe that the company's dividend is relatively safe, despite the cyclicality of Rockwell Automation's business.

Rockwell's earnings-per-share dropped by more than 50% from 2008 to 2009, which shows that the company can be relatively vulnerable to broad economic downturns. During the coronavirus crisis, Rockwell Automation's profits will most likely not drop this much, but there will still be a decline. Rockwell is well positioned internationally, as it generates 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 peers that are more focused on lower-growth markets in industrial countries.

Final Thoughts & Recommendation

Rockwell Automation operates a business that can be quite cyclical, but the company nevertheless managed to generate solid earnings-per-share growth throughout much more than the last decade, even though the last financial crisis was an exceptionally harsh recession. The current coronavirus crisis will leave a mark, but we believe that the company will recover in the coming years and get back to pre-crisis profitability in the foreseeable future. We still rate the stock a sell, as shares trade well in excess of our fair value estimate at current prices, which hurts the total return outlook a lot.

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.