Otis Worldwide Corp. (OTIS)

Updated July 26th, 2021, by Eli Inkrot

Key Metrics

Current Price:	$89	**5 Year CAGR Estimate:**	-2.2%	**Market Cap:**	$38 B
Fair Value Price:	$52	**5 Year Growth Estimate:**	7.0%	**Ex-Dividend Date[1]:**	08/20/21
% Fair Value:	169%	**5 Year Valuation Multiple Estimate:**	-10.0%	**Dividend Payment Date[1]:**	09/10/21
Dividend Yield:	1.1%	**5 Year Price Target**	$73	**Years Of Dividend Growth:**	1
Dividend Risk Score:	B	**Retirement Suitability Score:**	D	**Last Dividend Increase:**	20.0%

Overview & Current Events

Otis Worldwide Corp. debuted as an independent, publicly traded company on April 3rd, 2020, after being spun off from United Technologies (previously UTX, now Raytheon Technologies, RTX). However, the company's history is extensive after being founded in 1853 and having previously gone public in 1920. Today Otis is the leading company for elevator and escalator manufacturing, installation and service. The company's products move 2 billion people per day and maintain approximately 2.1 million customer units worldwide. Headquartered in Connecticut, the $38 billion market cap company generated $13 billion in sales in 2020 and employs 69,000 people.

Previously Otis was a constituent of the S&P 500 Dividend Aristocrat Index due to its United Technologies lineage. However, the company was removed in 2021. On April 19th, 2021, Otis announced a $0.24 quarterly dividend, marking a 20.0% boost and the company's first increase as a standalone company.

On July 26th, 2021, Otis reported Q2 2021 results for the period ending June 30th, 2021. For the quarter total revenue equaled $3.7 billion, representing a 22.2% increase compared to Q2 2020. New Equipment sales increased 33.5%, while the Service segment saw a 13.8% increase. Adjusted net income equaled $342 million or $0.79 per share compared to $244 million or $0.56 per share in the year ago period.

Otis also updated its 2021 outlook. The company now expects sales of $14.1 billion to $14.2 billion (from $13.6 - $13.9 billion) and adjusted earnings-per-share of $2.89 to $2.93 (up from $2.78 to $2.84 and $2.67 to $2.77 previously).

Growth on a Per-Share Basis

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
EPS	$5.49	$5.34	$6.21	$6.82	$6.29	$6.61	$6.60	$7.61	$8.26	$2.52	***$2.91***	***$4.08***
DPS	$1.87	$2.03	$2.20	$2.36	$2.56	$2.62	$2.72	$2.84	$2.94	$0.60	***$0.96***	***$1.35***
Shares[2]	907	919	917	909	838	809	799	861	864	433	***430***	***420***

Note that we have elected to show United Technologies historical data through 2019, to illustrate the type of operating company from which Otis was spun off. This is an imperfect measure as Otis made up less than 20% of United Technologies sales; however, it does offer some clues into the consistency of the new business.

Otis has a number of long-term growth drivers available in the way of increased urbanization, a growing middle class and digitalization. All these factors will continue to spur demand for Otis' products and should bode well for the category leader. At the very least, Otis stands a very good shot at capturing its "fair share" of growth in the industry.

Recent guidance continues to be encouraging. Moreover, the services segment adds some resiliency to the business. We are forecasting $2.91 in EPS, the midpoint of management's guidance, and a 7% growth rate over the next five years. While there is still a great deal of uncertainty in near-term results, we believe mid-to-high single-digit intermediate-term EPS growth can come to fruition. Of course, there are a lot of variables to keep an eye on.

[1] Estimated date.
[2] 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	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	Now	2026
Avg. P/E	14.6	14.7	16.0	16.4	17.0	15.3	17.7	16.8	16.1	18.2	***30.5***	***18.0***
Avg. Yld.	2.3%	2.6%	2.2%	2.1%	2.4%	2.6%	2.3%	2.2%	2.2%	1.3%	***1.1%***	***1.8%***

We are again using United Technologies history through 2019 to give you a sense for how shares traded in the past. During the past decade shares of UTX traded hands with an average P/E ratio of about 16 times earnings. We are now using 18 times earnings as a fair starting multiple for Otis, taking into consideration the enhanced risk to the standalone business paired against strong growth avenues and reoccurring revenue from servicing. Still, with shares currently trading near 31 times expected earnings, this could result in a significant valuation headwind. The new $0.24 quarterly dividend implies a payout ratio of about 33% of anticipated earnings.

Safety, Quality, Competitive Advantage, & Recession Resiliency

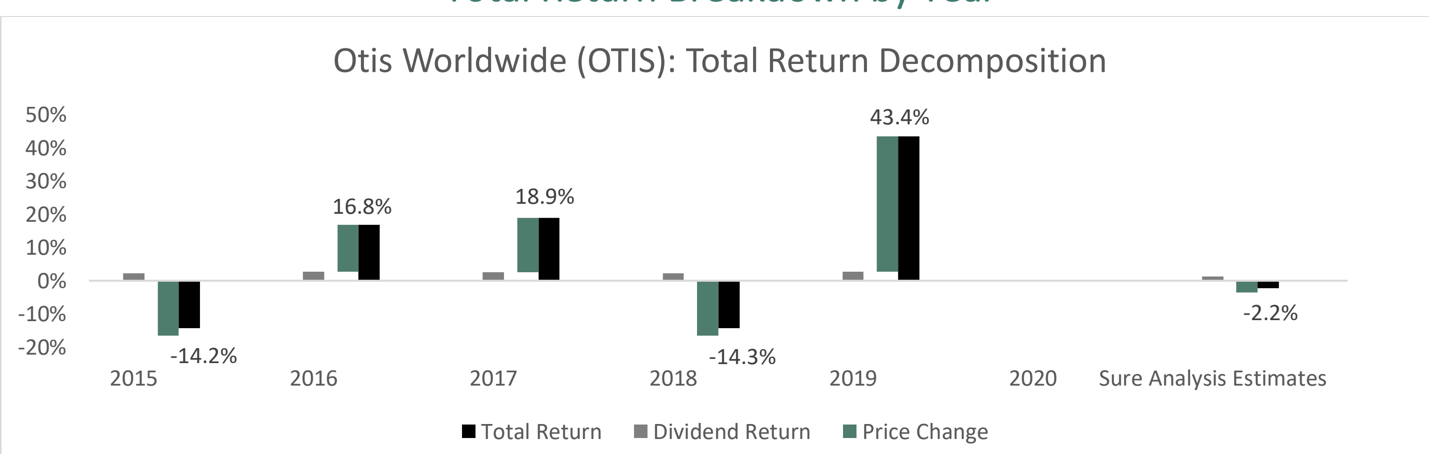
Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
Payout	34%	38%	35%	35%	41%	40%	41%	37%	36%	24%	***33%***	***33%***

Otis enjoys a competitive advantage in its namesake brand, along with the #1 position in the category the company created. Moreover, with the largest installed base of elevators and escalators, reoccurring service revenue can smooth out results in less certain times. During the last recession United Technologies posted earnings-per-share of $4.90, $4.12, $4.74 and $5.49 during the 2008 through 2011 timeframe. While some of that ballast is gone with the company splitting up, we still believe Otis should perform reasonably well in leaner times. Moreover, the targeted ~40% payout ratio will allow for flexibility in the future.

Final Thoughts & Recommendation

After being up 17% in our last report, shares are up another 17% in the last three months. Otis has been a very strong business for over 165 years. Now that it is once again a standalone company, it offers a "pure play" on a variety of important and growing trends around the world. While the cyclicality of the firm may have increased, we are encouraged by the ongoing service revenue. However, today's valuation continues to leave something to be desired in our view. Total return potential comes in at -2.2% per annum, driven by 7% growth and a 1.1% dividend yield, offset by the potential for a significant valuation headwind. This view could be too conservative if the business performs better than expected or if the valuation remains elevated, but we are not yet willing to make either speculation at this juncture. Shares earn a sell rating.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Revenue	55,754	57,708	56,600	57,900	56,098	57,244	59,837	66,501	77,046	12,760
Gross Profit	15,385	15,555	16,132	17,002	15,667	15,773	15,636	16,516	19,981	3,779
Gross Margin	27.6%	27.0%	28.5%	29.4%	27.9%	27.6%	26.1%	24.8%	25.9%	29.6%
SG&A Exp.	6,161	6,452	6,364	6,172	5,886	5,958	6,429	7,066	8,521	1,924
D&A Exp.	1,263	1,524	1,735	1,820	1,863	1,962	2,140	2,433	3,783	191
Operating Profit	7,846	7,684	8,549	9,593	7,291	8,221	8,138	8,553	8,966	1,639
Op. Margin	14.1%	13.3%	15.1%	16.6%	13.0%	14.4%	13.6%	12.9%	11.6%	12.8%
Net Profit	4,979	5,130	5,721	6,220	7,608	5,055	4,552	5,269	5537	906
Net Margin	8.9%	8.9%	10.1%	10.7%	13.6%	8.8%	7.6%	7.9%	7.2%	7.1%
Free Cash Flow	5,661	3,714	4,586	5,134	4,294	1,793	3,237	4,020	6,276	1,297
Income Tax	2,134	1,711	1,999	2,244	2,111	1,697	2,843	2,626	2,295	455

Balance Sheet Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Total Assets	61,452	89,409	90,594	91,206	87,484	89,706	96,920	134,211	139,716	10,710
Cash & Equivalents	5,960	4,819	4,619	5,229	7,075	7,157	8,985	6,152	7,378	1,782
Acc. Receivable	9,546	11,099	11,458	10,448	10,653	11,481	12,595	14,271	13,524	3,309
Inventories	7,797	9,537	10,330	7,642	8,135	8,704	9,881	10,083	10,950	659
Goodwill & Int.	21,861	42,990	43,689	42,976	42,904	42,743	43,793	74,536	74,109	2,257
Total Liabilities	38,632	62,340	57,375	58,642	58,640	60,537	65,499	93,601	95,485	13,990
Accounts Payable	5,570	6,431	6,965	6,250	6,875	7,483	9,579	11,080	10,809	1,453
Long-Term Debt	10,260	23,221	20,241	19,701	20,425	23,901	27,485	45,537	43,648	5,963
Total Equity	21,880	25,914	31,866	31,213	27,358	27,579	29,610	38,446	41,774	-3,832
D/E Ratio	0.47	0.90	0.64	0.63	0.75	0.87	0.93	1.18	1.04	-1.56

Profitability & Per Share Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Return on Assets	8.3%	6.8%	6.4%	6.8%	8.5%	5.7%	4.9%	4.6%	4.0%	8.9%
Return on Equity	23.0%	21.5%	19.8%	19.7%	26.0%	18.4%	15.9%	15.5%	13.8%	---
ROIC	15.1%	12.3%	11.0%	11.8%	15.0%	9.9%	8.1%	7.3%	6.4%	36.6%
Shares Out.	907	919	917	909	838	809	799	795	864	435
Revenue/Share	61.48	63.65	61.85	63.51	63.52	69.29	74.88	82.09	89.18	29.35
FCF/Share	6.24	4.10	5.01	5.63	4.86	2.17	4.05	4.96	7.26	2.98

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