Eaton Corporation (ETN)

Updated February 7th, 2022 by Nathan Parsh

Key Metrics

Current Price:	$152	**5 Year CAGR Estimate:**	1.4%	**Market Cap:**	$61 billion
Fair Value Price:	$120	**5 Year Growth Estimate:**	4.0%	**Ex-Dividend Date:**	3/15/2022[1]
% Fair Value:	127%	**5 Year Valuation Multiple Estimate:**	-4.6%	**Dividend Payment Date:**	3/30/2022[2]
Dividend Yield:	2.0%	**5 Year Price Target**	$146	**Years Of Dividend Growth:**	12
Dividend Risk Score:	D	**Retirement Suitability Score:**	D	**Last Dividend Increase:**	2.8%

Overview & Current Events

Eaton Corporation is a diversified industrial equipment and parts manufacturer. The company's engineered electrical systems and components are used by customers in the industrial, vehicle, commercial, and aerospace markets. The Ireland-based Eaton was founded in 1916 and today has annual sales of about $20 billion. The company employs about 85,000 people. Eaton has 6 divisions: Electrical Americas, Electrical Global, Aerospace, Vehicle, and eMobility.

On 8/2/2021, Eaton closed on its $3.3 billion sale of its Hydraulics segment to Danfoss.

Eaton reported earnings results for the fourth quarter and full year 2022 on 2/4/2022. For the quarter, revenue improved 2.1% to $4.8 billion, but missed estimates by $120 million. Adjusted earnings-per-share of $1.72 was a fourth quarter record and 19% better than the prior year. Adjusted earnings-per-share also topped estimates by $0.01. For 2021, revenue grew nearly 10% to $19.6 billion while adjusted earnings-per-share reached a record $6.62.

Organic growth was higher by 6% with divestitures reducing results by 2% and currency exchange acting as a 1% headwind. Electrical Americas segment was up 13%, with residential and data center markets still showing strong demand for products. Electrical Global grew 14% due, again, to strength in data center and residential markets, but also utility markets. Aerospace surged 40% due to higher demand in commercial markets. The Vehicle segment was lower by 2% due to weakness in global light motor vehicle markets. eMobility grew 4% due to new program wins.

Eaton provided an outlook for 2022 as well, with the company expecting adjusted earnings-per-share of $7.30 to $7.70 for the year. We have initiated our forecast accordingly.

Growth on a Per-Share Basis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
EPS	$3.96	$4.19	$4.67	$4.30	$4.21	4.60	$5.35	$5.74	$4.24	$6.62	***$7.50***	***$9.12***
DPS	$1.52	$1.68	$1.96	$2.20	$2.28	$2.40	$2.64	$2.84	$2.92	$3.04	***$3.04***	***$3.52***
Shares[3]	471	475	468	459	449	439	433	416	401	398	***398***	***390***

Prior to 2020, Eaton had delivered mid-single-digit organic growth in recent years, though the company's earnings-per-share decreased dramatically during the last recession. The short-term following the pandemic was challenging for the company, but our expect earnings-per-share growth has already returned. We reaffirm our expected growth rate of 4% through 2027.

Eaton paused dividend growth in 2009, as this was prudent given the earnings decline. Following the 4.1% dividend increase for the 3/30/2021 payment, Eaton has increased its dividend for 12 consecutive years. We expect dividend growth to be slightly below earnings growth.

[1] Estimated ex-dividend date

[2] Estimated dividend payment date

[3] In millions of shares

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Valuation Analysis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	Now	2027
Avg. P/E	11.8	15.6	15.2	14.6	14.6	16.3	14.7	14.3	22.7	26.1	***20.3***	***16.0***
Avg. Yld.	3.2%	2.6%	2.8%	3.5%	3.7%	3.2%	3.4%	3.5%	3.0%	1.8%	***2.0%***	***2.4%***

Shares of Eaton have decreased $20, or 11.6%, since our 11/2/2021 update. Based off of estimates for 2022, the stock now trades with a price-to-earnings multiple of 20.3. Eaton's stock has an average price-to-earnings ratio of 16.6 over the past decade. Given the steep drop in earnings that the company had in 2009, it appears that investors aren't usually willing to pay a high multiple for shares, given that the company is far from recession-proof. We have raised our five-year target valuation to 16 times earnings from 15 to better reflect the long-term average multiple. If shares were to trade at our target P/E by 2027, then valuation would be a 4.6% headwind to total returns over this time frame. Eaton has a current yield of 2.0%, which is well below the stock's 10-year average of more than 3%.

Safety, Quality, Competitive Advantage, & Recession Resiliency

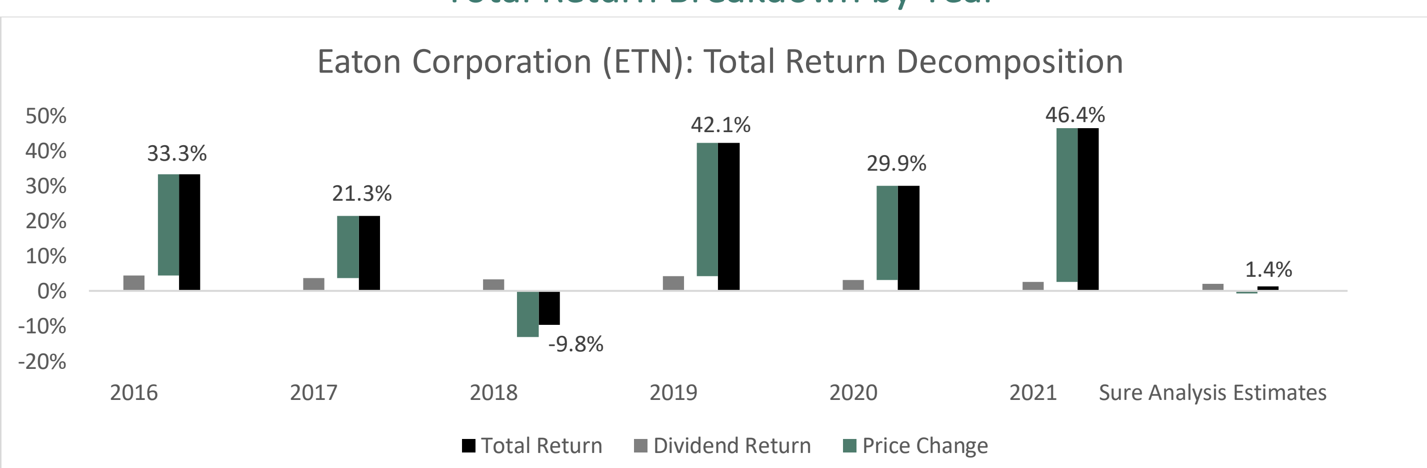
Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
Payout	38%	40%	42%	51%	54%	52%	49%	49%	69%	46%	***41%***	***39%***

Eaton suffered an extreme decline in earnings during the last recession that forced the company to pause its dividend growth. The company would likely experience a decline in earnings in another recession due to the nature of its business and could pause its dividend increases again. Eaton's key competitive advantages are its expertise and understanding of the businesses that it operates. The company specializes in providing highly engineered products to customers in niche end markets. Switching to a different provider could prove costly and comes with a risk of failure. While Eaton is not recession-proof, the company is likely to do well in an improving economy due to these factors.

Final Thoughts & Recommendation

Following fourth quarter results, Eaton Corporation is expected to return 1.4% annually through 2027, compared to our prior estimate of a loss of 4.3%. Our projection stems from a 4% earnings growth rate and a 2% starting dividend yield that are offset by a mid-single-digit headwind from multiple compression. Eaton ended the year on a solid note, posting record adjusted earnings-per-share for the quarter and year. In addition, the company has sold off weaker segments to focus on its core businesses. We have raised our five-year price target $25 to $146 to reflect earnings estimates and a higher valuation target, but maintain our sell rating on Eaton due to projected returns.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Revenue	16311	22046	22552	20855	19747	20404	21609	21390	17858	19628
Gross Profit	4863	6677	6906	6551	6351	6648	7098	7052	5450	6335
Gross Margin	29.8%	30.3%	30.6%	31.4%	32.2%	32.6%	32.8%	33.0%	30.5%	32.3%
SG&A Exp.	2894	3886	3810	3596	3464	3526	3548	3583	3075	3256
D&A Exp.	598	997	983	925	929	914	903	884	811	
Operating Profit	1530	2147	2449	2330	2300	2538	2966	2863	1824	2463
Op. Margin	9.4%	9.7%	10.9%	11.2%	11.6%	12.4%	13.7%	13.4%	10.2%	12.5%
Net Profit	1217	1861	1793	1972	1916	2985	2145	2211	1410	2144
Net Margin	7.5%	8.4%	8.0%	9.5%	9.7%	14.6%	9.9%	10.3%	7.9%	10.9%
Free Cash Flow	1071	1671	1246	1903	2073	2146	2093	2864	2555	
Income Tax	31	11	(42)	159	199	382	278	378	331	750

Balance Sheet Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Total Assets	35810	35491	33529	30996	30476	32623	31092	32805	31824	34027
Cash & Equivalents	577	915	781	268	543	561	283	370	438	297
Acc. Receivable	3474	3648	3667	3479	3560	3943	3858	3437	2904	3297
Inventories	2336	2382	2428	2323	2346	2620	2785	2805	2109	2969
Goodwill & Int.	22023	21681	20449	19493	18715	18833	18174	18094	17078	20606
Total Liabilities	20632	18628	17690	15765	15478	15333	14950	16672	16851	17576
Accounts Payable	1879	1960	1940	1758	1718	2166	2130	2114	1987	2797
Long-Term Debt	10836	9549	9034	8414	8277	7751	7521	8322	8058	8579
Total Equity	15113	16791	15786	15186	14954	17253	16107	16082	14930	16413
LTD/E Ratio	0.72	0.57	0.57	0.55	0.55	0.45	0.47	0.52	0.54	0.52

Profitability & Per Share Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Return on Assets	4.5%	5.2%	5.2%	6.1%	6.2%	9.5%	6.7%	6.9%	4.4%	6.5%
Return on Equity	10.8%	11.7%	11.0%	12.7%	12.7%	18.5%	12.9%	13.7%	9.1%	13.7%
ROIC	6.5%	7.1%	7.0%	8.1%	8.2%	12.4%	8.8%	9.2%	5.9%	8.9%
Shares Out.	471	475	468	459	449	439	433	416	401	398
Revenue/Share	46.48	46.25	47.30	44.65	43.26	45.65	49.46	50.83	44.20	48.87
FCF/Share	3.05	3.51	2.61	4.07	4.54	4.80	4.79	6.81	6.32	

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