



# Emerson Electric Company (EMR)

Updated August 16<sup>th</sup>, 2022, by Josh Arnold

## Key Metrics

<b>Current Price:</b>	\$89	<b>5 Year CAGR Estimate:</b>	8.7%	<b>Market Cap:</b>	\$53 B
<b>Fair Value Price:</b>	\$97	<b>5 Year Growth Estimate:</b>	5.0%	<b>Ex-Dividend Date:</b>	08/11/22
<b>% Fair Value:</b>	92%	<b>5 Year Valuation Multiple Estimate:</b>	1.7%	<b>Dividend Payment Date:</b>	09/09/22
<b>Dividend Yield:</b>	2.3%	<b>5 Year Price Target</b>	\$124	<b>Years Of Dividend Growth:</b>	65
<b>Dividend Risk Score:</b>	A	<b>Retirement Suitability Score:</b>	A	<b>Rating:</b>	Hold

## Overview & Current Events

Emerson Electric was founded in Missouri in 1890 and since that time, it has evolved through organic growth, as well as strategic acquisitions and divestitures, from a regional manufacturer of electric motors and fans into a \$53 billion diversified global leader in technology and engineering. Its global customer base and diverse product and service offerings afford it about \$20 billion in annual revenue. The company's very impressive 65-year dividend increase streak lands it on the prestigious Dividend Kings list.

Emerson reported third quarter earnings on August 9<sup>th</sup>, 2022, and results were somewhat mixed. Adjusted earnings-per-share came to \$1.38, which was nine cents ahead of estimates. Revenue was up 7% to \$5 billion, but missed expectations by \$100 million.

Underlying orders were up 10%, while net sales rose 7%. The Americas led the way with a 14% gain, Europe was flat, and AMEA was down fractionally. China was off 6%, due primarily to COVID-19 lockdowns.

Pretax operating margin was 23.9%, up 720 basis points year-over-year. Adjusted EBITA margin was 22.8% of revenue, up 270 bps.

Adjusted earnings-per-share rose 16% to \$1.38. Operating cash flow was \$740 million, down 33%. Free cash flow was \$630 million, down 36%, due to higher working capital due to increased sales and continued supply chain constraints.

The company updated guidance to net sales gains of 7% to 8% for the full year, down from 8% to 10% prior. On an organic basis, net sales are expected to rise 9% to 10%, with the balance coming from a headwind from the very strong US dollar.

Adjusted earnings-per-share is now expected to be \$5.05 to \$5.15, up from \$4.95 to \$5.10 previously. Operating cash flow is expected to be \$3 billion, and share repurchases should be about \$500 million.

## Growth on a Per-Share Basis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
<b>EPS</b>	\$2.67	\$3.54	\$3.75	\$3.17	\$2.46	\$2.54	\$3.46	\$3.71	\$3.46	\$4.10	<b>\$5.10</b>	<b>\$6.51</b>
<b>DPS</b>	\$1.60	\$1.66	\$1.72	\$1.88	\$1.90	\$1.92	\$1.94	\$1.96	\$2.00	\$2.04	<b>\$2.06</b>	<b>\$2.39</b>
<b>Shares<sup>1</sup></b>	724	707	697	655	643	642	641	632	601	595	<b>590</b>	<b>550</b>

The majority of Emerson's revenue is exposed to the oil and gas industry, where revenue and margins change significantly, introducing risk to forecasts. We're estimating growth at 5% as management remains bullish, and as there are signs of organic revenue growth improvement, as well as with respect to margins. We still think low single-digit growth in revenue and a tailwind from the buyback will be the key drivers of earnings-per-share growth in the coming years, and we see Emerson as rebounding. We see fiscal 2022 as a defining year for Emerson given the guidance on supply chain constraints, but we'll see how that plays out; guidance remains strong.

<sup>1</sup> Share count in millions

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The dividend is also expected to grow in the low single-digits as recent years have seen Emerson focus more on acquisitions and share repurchases than growing the dividend. Growth rates will likely be unimpressive as the company continues to focus on using its ample cash flow on acquisitions, not above average dividend growth.

## Valuation Analysis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	Now	2027
<b>Avg. P/E</b>	18.3	15.8	17.6	18.0	20.6	22.9	20.5	17.7	18.8	18.2	<b>17.5</b>	<b>19.0</b>
<b>Avg. Yld.</b>	3.3%	3.0%	2.6%	3.3%	3.8%	3.3%	2.7%	3.0%	3.1%	2.3%	<b>2.3%</b>	<b>1.9%</b>

Emerson's price-to-earnings ratio is up since our last update, at 17.5 times earnings, which is below our estimate of fair value at 19. We are therefore forecasting a modest positive impact from the valuation in the coming years on total returns. We see the yield as declining over time, primarily from small dividend increases. If free cash flow weakens, growth rates in the dividend could moderate.

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

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
<b>Payout</b>	60%	46%	61%	60%	77%	75%	58%	53%	58%	50%	<b>40%</b>	<b>37%</b>

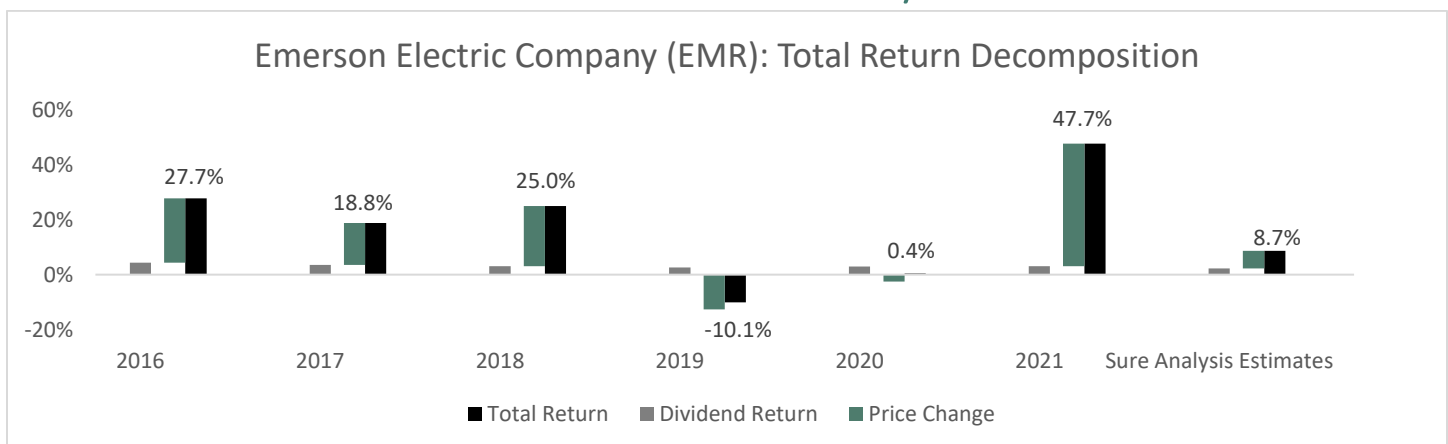
Emerson's payout ratio is just under half of earnings, and we believe it will continue to drift lower over time as Emerson focuses on acquisitions instead of boosting the payout by large amounts. The dividend is very safe as it is well covered by free cash flow, and the yield is decent, so it is a suitable dividend stock. We also note that Emerson likes to buy back its stock, which puts a natural cap on how much the company is willing to use for dividend payments.

Emerson's competitive advantage is in its many decades of experience in building customer relationships and engineering excellence. It has a global customer base that is seeing strong economic growth and that underlying sales tailwind should power results going forward. It is very susceptible to recessions given its oil and gas exposure, however, so any signs of economic weakness should put investors on alert, as we saw in 2020.

## Final Thoughts & Recommendation

With recent price action, Emerson still appears undervalued. Our growth forecast, combined with shares at 92% of our estimate of fair value, and a higher dividend yield, means we are forecasting 8.7% total annual returns in the coming years. We are reiterating Emerson at a hold rating given the improvement in the valuation. We note there's significant margin uncertainty for this year, but management seems confident at the moment that it's transitory.

## Total Return Breakdown by Year



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## Income Statement Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
<b>Revenue</b>	24,412	24,669	17,733	16,249	14,522	15,264	17,408	18,372	16,785	18,236
<b>Gross Profit</b>	9,768	9,952	7,762	7,008	6,262	6,431	7,432	7,815	7,009	7,563
<b>Gross Margin</b>	40.0%	40.3%	43.8%	43.1%	43.1%	42.1%	42.7%	42.5%	41.8%	41.5%
<b>SG&amp;A Exp.</b>	5,436	5,648	4,164	3,735	3,464	3,607	4,269	4,457	3,986	4,179
<b>D&amp;A Exp.</b>	823	819	569	573	568	636	758	822	854	969
<b>Operating Profit</b>	3,972	4,006	3,503	3,179	2,714	2,688	2,952	3,120	2,784	3,084
<b>Op. Margin</b>	16.3%	16.2%	19.8%	19.6%	18.7%	17.6%	17.0%	17.0%	16.6%	16.9%
<b>Net Profit</b>	1,968	2,004	2,147	2,710	1,635	1,518	2,203	2,306	1,965	2,303
<b>Net Margin</b>	8.1%	8.1%	12.1%	16.7%	11.3%	9.9%	12.7%	12.6%	11.7%	12.6%
<b>Free Cash Flow</b>	2,388	2,971	3,041	1,941	2,434	1,436	2,275	2,412	2,545	2,994
<b>Income Tax</b>	1,091	1,130	953	1,267	697	660	443	531	345	585

## Balance Sheet Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
<b>Total Assets</b>	23,818	24,711	24,177	22,088	21,732	19,589	20,390	20,497	22,882	24,715
<b>Cash &amp; Equivalents</b>	2,367	3,275	3,149	3,054	3,182	3,062	1,093	1,494	3,315	2,354
<b>Acc. Receivable</b>	4,983	4,808	5,019	2,870	2,701	3,072	3,023	2,985	2,802	2,971
<b>Inventories</b>	2,125	1,895	2,057	1,265	1,208	1,696	1,813	1,880	1,928	2,050
<b>Goodwill &amp; Int.</b>	9,864	9,181	8,871	4,785	4,811	7,206	9,206	9,151	9,202	10,600
<b>Total Liabilities</b>	13,376	13,993	14,010	13,960	14,114	10,819	11,400	12,224	14,435	14,792
<b>Accounts Payable</b>	2,767	2,725	2,951	1,537	1,517	1,776	1,943	1,874	1,715	2,108
<b>Long-Term Debt</b>	5,293	5,642	6,024	6,841	6,635	4,656	4,760	5,721	7,486	6,665
<b>Total Equity</b>	10,295	10,585	10,119	8,081	7,568	8,718	8,947	8,233	8,405	9,883
<b>LTD/E Ratio</b>	0.51	0.53	0.60	0.85	0.88	0.53	0.53	0.69	0.89	0.67

## Profitability & Per Share Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
<b>Return on Assets</b>	8.3%	8.3%	8.8%	11.7%	7.5%	7.3%	11.0%	11.3%	9.1%	9.7%
<b>Return on Equity</b>	19.0%	19.2%	20.7%	29.8%	20.9%	18.6%	24.9%	26.8%	23.6%	25.2%
<b>ROIC</b>	12.5%	12.5%	13.2%	17.4%	11.2%	11.0%	16.2%	16.6%	13.1%	14.2%
<b>Shares Out.</b>	724	707	697	655	643	642	641	632	601	595
<b>Revenue/Share</b>	33.23	34.13	25.19	24.02	22.45	23.72	27.40	29.60	27.67	30.30
<b>FCF/Share</b>	3.25	4.11	4.32	2.87	3.76	2.23	3.58	3.89	4.20	4.98

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

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