



Illinois Tool Works Inc. (ITW)

Updated February 2nd, 2023 by Quinn Mohammed

Key Metrics

Current Price:	\$251	5 Year CAGR Estimate:	3.1%	Market Cap:	\$74 B
Fair Value Price:	\$187	5 Year Growth Estimate:	7.0%	Ex-Dividend Date¹:	03/30/23
% Fair Value:	134%	5 Year Valuation Multiple Estimate:	-5.7%	Dividend Payment Date¹:	04/14/23
Dividend Yield:	2.1%	5 Year Price Target	\$263	Years Of Dividend Growth:	58
Dividend Risk Score:	A	Retirement Suitability Score:	B	Rating:	Hold

Overview & Current Events

Illinois Tool Works is a diversified multi-industrial manufacturer with seven unique operating segments: Automotive, Food Equipment, Test & Measurement, Welding, Polymers & Fluids, Construction Products and Specialty Products. Last year the company generated \$15.9 billion in revenue. The \$74 billion market cap company is geographically diversified, with more than half of its revenue generated outside of the United States. Illinois Tool Works is a member of the Dividend Aristocrats Index and is a Dividend King.

On February 2nd, 2023, Illinois Tool Works reported fourth quarter and full year 2022 results for the period ending December 31st, 2022. For the quarter, revenue came in at \$4.0 billion, up 8% year-over-year. Sales were up 20% in the Automotive OEM segment, the largest out of the company's seven segments. Five out of these seven segments had double-digit organic sales growth in the quarter. Net income equaled \$907 million or \$2.95 per share compared to \$609 million or \$1.93 per share in Q4 2021.

Illinois Tool Works' earnings-per-share for the full year was \$9.77, exceeding \$8.51 earned in 2021 by 15%. Revenue rose 10% year-over-year to \$15.9 billion for 2022.

Illinois Tool Works initiated 2023 guidance and sees full-year GAAP EPS to be between \$9.40 and \$9.80. Additionally, the company expects to repurchase roughly \$1.5 billion of its own shares in the year.

Growth on a Per-Share Basis

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
EPS	\$3.63	\$4.67	\$5.13	\$5.70	\$6.78	\$7.60	\$7.74	\$6.63	\$8.51	\$9.77	\$9.60	\$13.46
DPS	\$1.60	\$1.75	\$2.07	\$2.40	\$2.73	\$3.56	\$4.14	\$4.42	\$4.72	\$5.06	\$5.24	\$6.53
Shares²	430	383	364	347	342	328	320	318	315	308	302	280

In the 2007 through 2019 period Illinois Tool Works increased its earnings-per-share by an average compound rate of 7.2% per annum. While there was cyclicity during the great recession, including a -40% drop in earnings from 2007 to 2009, generally the company has exhibited consistent progress. In the past, Illinois Tool Works was able to grow via moderate top-line growth that was aided significantly by margin expansion and share repurchases.

Results for 2020 dipped -14% amid the pandemic, but 2021 bounced back materially and 2022's results were outright impressive. Moving forward, growth becomes a bit more difficult as the company gets larger. Still, the balance sheet is in good shape allowing for some flexibility from a capital allocation standpoint. Moreover, attractive returns can be achieved without venturing outside Illinois Tool Works' existing core competencies. Illinois Tool Works can continue to invest in its sales networks, R&D, and production capacity and the company's cost-cutting efforts could continue to buoy margins.

We are using the midpoint of management's guidance, \$9.60, along with a 7.0% expected annual growth rate over the intermediate term. This is at the low end of the company's 7% to 10% annual EPS growth, but we prefer to remain cautious.

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	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	Now	2028
Avg. P/E	19.4	18.5	18	19	21	19.3	19.8	27.4	25.7	24.4	26.1	19.5
Avg. Yld.	1.70%	2.00%	2.20%	2.20%	1.90%	2.40%	2.70%	2.40%	2.20%	2.20%	2.1%	2.5%

Over the past decade shares of Illinois Tool Works have traded hands with an average P/E ratio of about 21.5 times earnings. We believe that a P/E ratio of 19.5 is a fair starting point, considering the quality of the business and growth prospects. With shares currently trading above 26 times the midpoint of management's guidance, this implies the potential for a valuation headwind.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
Payout	44%	37%	40%	42%	40%	47%	53%	67%	55%	52%	55%	48%

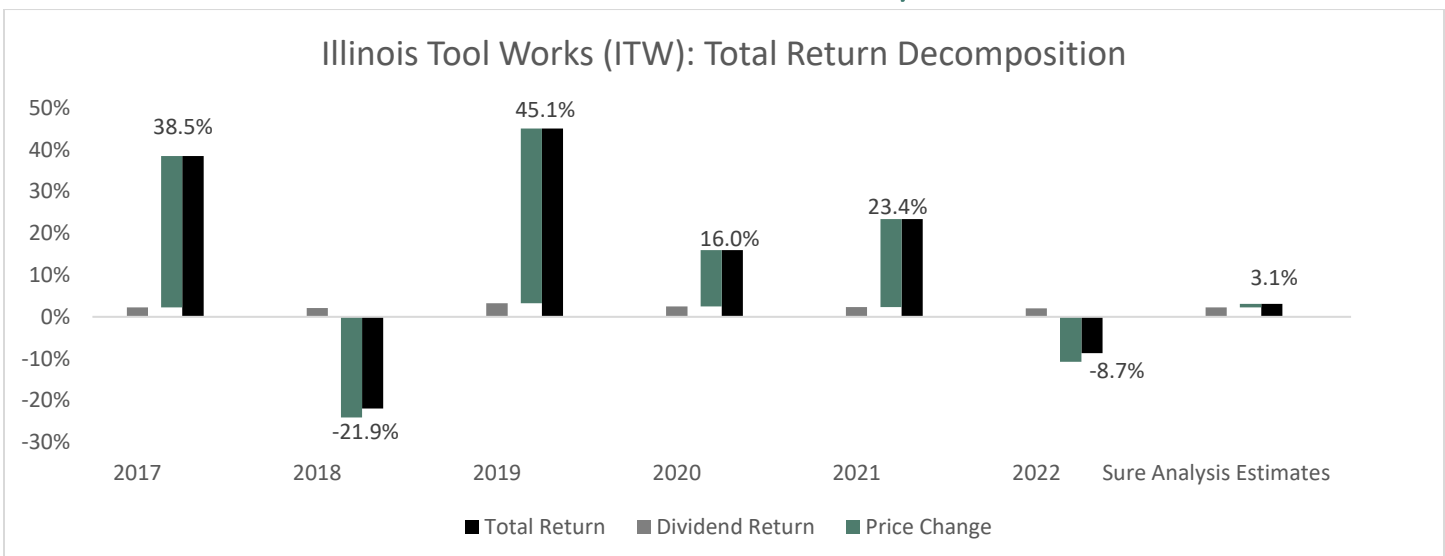
Illinois Tool Works has an excellent dividend growth history. Its payout ratio was relatively high during the last financial crisis, but the company was not forced to cut the payout. Today the dividend payout ratio sits at 51% of expected earnings, above the company's long-term target, meaning that future dividend growth may trail earnings growth.

Illinois Tool Works' industry is not glamorous or one with outstanding growth rates, but the company has established itself as a major player that continues to grow profitably. Its experienced management and strong fundamentals, such as an above-average return on capital, function as competitive advantages. The company's profits were reduced during the last financial crisis, posting earnings-per-share of \$3.36, \$3.05, \$1.93, and \$3.03 during the 2007 through 2010 stretch. This is something to consider for the next downturn, as the business was tested in 2020 as well.

Final Thoughts & Recommendation

Shares are up 14% year-to-date, which is favorable compared to the broader market's 9% gain. Illinois Tool Works has several positives, including solid earnings growth, a nice dividend yield, a long and successful dividend growth history, and a compelling long-term track record. However, total return potential comes in at 3.1% per annum, stemming from 7.0% growth and a 2.1% dividend yield offset by the possibility of a valuation headwind. We are enthused about the business, but we are less keen on the valuation. Shares earn a hold rating.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Revenue	14135	14484	13405	13599	14314	14768	14109	12570	14460	15932
Gross Profit	5581	5811	5517	5703	6005	6164	5922	5199	5966	6503
Gross Margin	39.5%	40.1%	41.2%	41.9%	42.0%	41.7%	42.0%	41.4%	41.3%	40.8%
SG&A Exp.	2815	2678	2417	2415	2400	2391	2361	2163	2356	2579
D&A Exp.	613	507	477	470	462	---	---	427	---	---
Operating Profit	2516	2888	2867	3064	3399	3584	3402	2882	3477	3790
Op. Margin	17.8%	19.9%	21.4%	22.5%	23.7%	24.3%	24.1%	22.9%	24.0%	23.8%
Net Profit	1679	2946	1899	2035	1687	2563	2521	2109	2694	3034
Net Margin	11.9%	20.3%	14.2%	15.0%	11.8%	17.4%	17.9%	16.8%	18.6%	19.0%
Free Cash Flow	2160	1255	2015	2029	2105	---	---	2571	---	1936
Income Tax	717	809	820	873	1583	831	767	595	632	808

Balance Sheet Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Total Assets	19966	17465	15729	15201	16780	14870	15068	15610	16080	15422
Cash & Equivalents	3618	3990	3090	2472	3094	1504	1981	2564	1527	708
Acc. Receivable	2365	2293	2203	2357	2628	2622	2461	2506	2840	3171
Inventories	1247	1180	1086	1076	1220	1318	1164	1189	1694	2054
Goodwill & Int.	6885	6466	5999	6021	6024	5717	5343	5471	5937	5632
Total Liabilities	10257	10641	10501	10942	12191	11612	12038	12430	12450	12333
Accounts Payable	634	512	449	511	590	524	472	534	585	594
Long-Term Debt	6344	7419	7422	7829	8328	7380	7758	8122	7687	7763
Total Equity	9703	6819	5224	4254	4585	3254	3026	3181	3625	3088
LTD/E Ratio	0.65	1.09	1.42	1.84	1.82	2.27	2.56	2.56	2.12	2.51

Profitability & Per Share Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Return on Assets	8.6%	15.7%	11.4%	13.2%	10.6%	16.2%	16.8%	13.8%	17.0%	19.3%
Return on Equity	16.6%	35.7%	31.5%	42.9%	38.2%	65.4%	80.3%	68.0%	79.2%	90.4%
ROIC	10.6%	19.4%	14.1%	16.5%	13.5%	21.8%	23.5%	19.1%	23.8%	27.4%
Shares Out.	430	383	364	347	342	328	320	318	316	311
Revenue/Share	31.46	35.80	36.22	38.08	41.27	43.81	43.33	39.5	45.69	51.28
FCF/Share	4.81	3.10	5.44	5.68	6.07	---	---	8.08	---	6.23

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

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