The Timken Co. (TKR)

Updated February 19th, 2024, by Ian Bezek

Key Metrics

Current Price:	$82	**5 Year CAGR Estimate:**	4.8%	**Market Cap:**	$5.7 B
Fair Value Price:	$79	**5 Year Growth Estimate:**	4.0%	**Ex-Dividend Date:**	02/16/24
% Fair Value:	103%	**5 Year Valuation Multiple Estimate:**	-0.7%	**Dividend Payment Date:**	03/06/24
Dividend Yield:	1.6%	**5 Year Price Target**	$96	**Years Of Dividend Growth:**	10
Dividend Risk Score:	C	**Retirement Suitability Score:**	D	**Rating:**	Hold

Overview & Current Events

Timken is an industrial company focused on making bearings, belts, gear drives, and other such assorted products. The company is heavily involved in vehicles but also sells to aerospace, energy, and agricultural end markets among others. Timken historically was also a significant player in the steel industry, but it spun off that business in 2014.

Timken has generally been viewed as a cyclical company prone to booms and busts. However, management has refocused operations around new verticals, such as renewable energy applications, which should have a more sustained demand growth profile. Timken also completed the acquisition of Spinea in 2022. In 2023, Timken announced additional acquisitions of American Roller Bearing Company, and Nadella, a European firm which makes industrial motion solutions along with a number of additional smaller acquisitions for that industrial motion division.

Timken delivered fairly strong Q4 earnings figures, which were released February 5th, 2024. Revenues were $1.09 billion, which rose 1% year-over-year. This was a favorable result, as the company had posted negative year-over-year comps in Q3. Adjusted net earnings of $1.37 per share rose from $1.34 last year and greatly exceeded analyst expectations.

While the Q4 results were upbeat, the outlook is much less favorable for 2024. Timken slashed guidance for the upcoming year, warning that it sees end market demand falling well short of prior expectations. While Timken has made impressive moves with its margin improvement efforts and M&A, it appears this won't be enough to sustain earnings as customer activity in several key markets has rolled over. Between higher interest rates, various geopolitical conflicts and a soft energy market, Timken will operate in a challenging macroenvironment this year.

Growth on a Per-Share Basis

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2029
EPS	$2.55	$2.21	$1.97	$2.63	$4.18	$4.60	$4.10	$4.72	$5.48	*$7.05*	***$6.10***	***$7.42***
DPS	$1.00	$1.03	$1.04	$1.07	$1.11	$1.12	$1.13	$1.19	$1.23	*$1.30*	***$1.32***	***$1.53***
Shares	88	80	77	78	76	76	76	75	73	*71*	***70***	***68***

Timken has had an uneven earnings profile historically. Earnings fell every year sequentially from 2013 through 2016, though this was impacted by the spin-off of the company's former steel business. Earnings jumped dramatically between 2017 and 2019 and have continued rising during the current pandemic-induced period of economic volatility. The company achieved record results in 2023. But that appears to have been the company's near-term peak, as a more troubled economic environment will limit intermediate-term profit growth.

The company has had a modest approach to capital returns to shareholders. In the early part of the 2010s, Timken repurchased a substantial amount of its stock. After a pause, it appears Timken is returning to more aggressive share repurchases. The company retired another two million shares of stock in 2023 on top of its prior repurchases. However, we expect that buybacks may slow down as the company funds its continuing M&A strategy.

Timken has given investors steady dividend hikes dating back to 2014. They have been conservative in size, though, with the company averaging just a 3% annualized dividend growth rate. On the other hand, Timken's dividend has been incredibly consistent; it has paid a dividend for 407 consecutive quarters.

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Valuation Analysis

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	Now	2029
Avg. P/E	20.5	16.1	16.8	17.5	10.9	10.1	12.6	16.4	15.0	11.3	***13.4***	***13.0***
Avg. Yld.	1.9%	2.9%	3.1%	2.3%	2.4%	2.4%	2.2%	1.5%	1.6%	1.6%	***1.6%***	***1.6%***

Timken stock has rarely received a high P/E multiple from the market; it's had a historical range of 10 to 20 times earnings over the past decade. Today's P/E multiple seems fair.

On a yield basis, Timken offered a yield as high as 3% in the wake of the spin-off of the steel business in 2014. However, the yield has settled under 2% in recent years. That seems likely to persist, given Timken's increasing focus on growth and M&A of late. The company's current 1.6% dividend yield is in-line with our long-term expectations for Timken.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2029
Payout	39%	47%	53%	41%	27%	24%	28%	25%	22%	18%	***22%***	***21%***

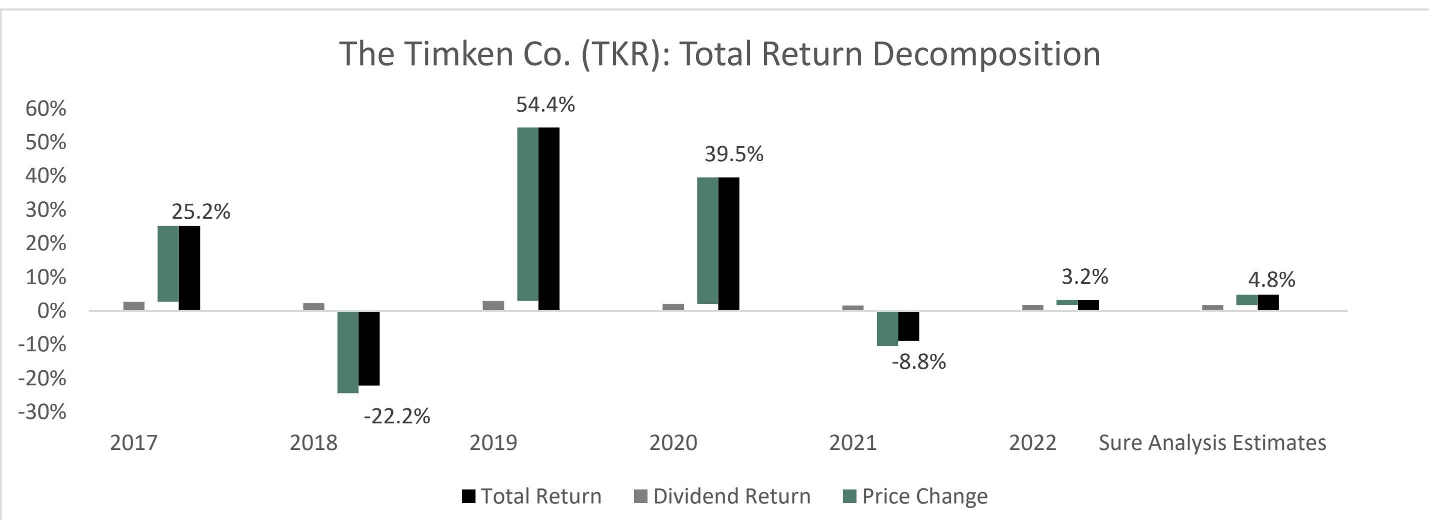
Timken's overall balance sheet is in fine shape with $419 million of cash on hand at year-end 2023 and plenty of total assets to manage its short- and long-term debt obligations. Historically, the company has been able to tap the bond market at reasonable rates, showing the market's confidence in the firm. Timken's profitability has improved in recent years, and it has the financial capacity to withstand a significant recession.

The company's dividend is also well-covered from earnings. The payout ratio has fallen from a high of 53% in 2016 to just 22% now. This seemingly gives the company room for faster dividend increases in the future.

Final Thoughts & Recommendation

Historically, investors tended to view Timken as a lower-quality cyclical business. For several years coming out of the pandemic, it appeared that Timken was enjoying stronger pricing power and improving business quality. However, 2024's downbeat guidance has suggested that the industrial cycle is rearing its ugly head once again. We have significantly trimmed our fair value estimate based on this guidance cut and as such we foresee just 4.8% annual shareholder returns through 2029. Timken earns 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	3,035	3,076	2,872	2,670	3,004	3,581	3,790	3,513	4,133	4,497
Gross Profit	868	898	820	706	812	1,040	1,142	1,010	1,103	1,288
Gross Margin	28.6%	29.2%	28.5%	26.5%	27.0%	29.0%	30.1%	28.7%	26.7%	28.6%
SG&A Exp.	554	576	578	440	508	581	619	534	581	637
D&A Exp.	142	137	131	132	138	146	161	167	168	164
Operating Profit	315	322	242	266	304	459	523	476	522	651
Op. Margin	10.4%	10.5%	8.4%	10.0%	10.1%	12.8%	13.8%	13.6%	12.6%	14.5%
Net Profit	263	171	189	141	203	303	362	285	369	407
Net Margin	8.7%	5.6%	6.6%	5.3%	6.8%	8.5%	9.6%	8.1%	8.9%	9.1%
Free Cash Flow	296	180	275	266	132	220	410	456	239	285
Income Tax	115	55	26	61	58	103	98	104	95	134

Balance Sheet Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Total Assets	4,478	3,001	2,784	2,763	3,402	4,445	4,860	5,042	5,171	5,772
Cash & Equivalents	385	279	130	149	122	133	210	320	257	332
Acc. Receivable	444	476	455	438	525	547	545	581	626	700
Inventories	583	586	543	554	739	836	842	841	1,043	1,191
Goodwill & Int.	554	499	599	629	932	1,694	1,752	1,789	1,692	1,864
Total Liabilities	1,829	1,412	1,440	1,452	1,928	2,803	2,905	2,816	2,793	3,420
Accounts Payable	140	144	160	176	265	273	302	351	430	404
Long-Term Debt	446	530	657	659	962	1,682	1,730	1,565	1,465	1,963
Total Equity	2,637	1,576	1,325	1,280	1,443	1,580	1,868	2,153	2,295	2,268
LTD/E Ratio	0.17	0.34	0.50	0.52	0.67	1.06	0.93	0.73	0.64	0.87

Profitability & Per Share Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Return on Assets	6.0%	4.6%	6.5%	5.1%	6.6%	7.7%	7.8%	5.7%	7.2%	7.4%
Return on Equity	10.8%	8.1%	13.0%	10.8%	14.9%	20.0%	21.0%	14.2%	16.6%	17.9%
ROIC	9.0%	6.6%	9.2%	7.1%	9.2%	10.5%	10.3%	7.6%	9.7%	10.0%
Shares Out.	93	88	80	77	78	76	76	76	75	73
Revenue/Share	31.68	33.72	33.65	33.70	38.07	45.71	49.29	45.98	53.67	60.50
FCF/Share	3.09	1.98	3.22	3.36	1.67	2.81	5.33	5.97	3.10	3.84

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