The Timken Co. (TKR)

Updated May 9th, 2024, by Ian Bezek

Key Metrics

Current Price:	$90	**5 Year CAGR Estimate:**	4.7%	**Market Cap:**	$6.3 B
Fair Value Price:	$87	**5 Year Growth Estimate:**	4.0%	**Ex-Dividend Date:**	05/13/24
% Fair Value:	104%	**5 Year Valuation Multiple Estimate:**	-0.7%	**Dividend Payment Date:**	05/28/24
Dividend Yield:	1.5%	**5 Year Price Target**	$106	**Years Of Dividend Growth:**	11
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 upbeat Q1 earnings figures, which were released on April 30th, 2024. Revenues of $1.19 billion fell 5.7% year-over-year. This was a favorable result, as analysts had been projecting a sharper year-over-year decline. Adjusted net earnings of $1.77 per share slipped from $2.09 in the year prior, but were also far ahead of analyst expectations.

Timken had previously warned investors that 2024 could be a rough year for the firm. This set a low bar heading into this quarter, and Timken was able to deliver results that were not nearly as bad as feared. Timken has made impressive moves with its margin improvement efforts and M&A, and it appears these efforts have helped the firm offset the meaningful deceleration currently being witnessed in Timken's end markets. Timken continues to face a challenging macroeconomic outlook, and certain customer groups – such as renewable energy – are in a deep slump right now. However, Timken's diversified customer base and strong internal operations should limit the decline in earnings.

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*	***$6.20***	***$7.54***
DPS	$1.00	$1.03	$1.04	$1.07	$1.11	$1.12	$1.13	$1.19	$1.23	*$1.30*	***$1.36***	***$1.58***
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 recent 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, with the company retiring two million shares of stock in 2023.

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 May 3rd, 2024, Timken announced another 3%

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dividend hike, increasing its quarterly payout from 33 cents to 34 cents per share. Notably, Timken's dividend has been incredibly consistent; it has paid a dividend for 408 consecutive quarters.

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	***14.5***	***14.0***
Avg. Yld.	1.9%	2.9%	3.1%	2.3%	2.4%	2.4%	2.2%	1.5%	1.6%	1.6%	***1.5%***	***1.5%***

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 1.5% 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%***

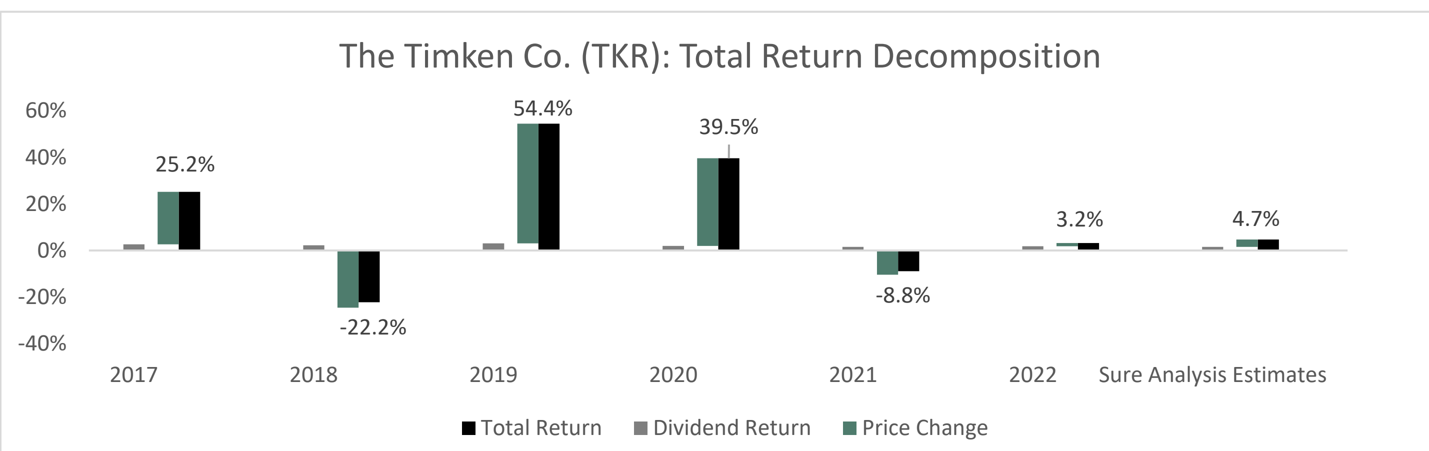
Timken's overall balance sheet is in fine shape with $422 million of cash on hand as of March 31st, 2024, and plenty of total assets to manage its short- and long-term debt obligations. Historically, the company has been able to tap the bond market at reasonable rates, showing the market's confidence 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 much softer industrial market outlook has put a temporary pause to Timken's longer-term growth strategy. It appears Timken's strong operations and cost controls will help it endure this current downturn. Regardless, the near-term outlook is muted, with an annualized 4.7% total expected return. Shares earn a hold rating today.

Total Return Breakdown by Year



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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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Income Statement Metrics

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Revenue	3,076	2,872	2,670	3,004	3,581	3,790	3,513	4,133	4,497	4,769
Gross Profit	898	820	706	812	1,040	1,142	1,010	1,103	1,288	1,509
Gross Margin	29.2%	28.5%	26.5%	27.0%	29.0%	30.1%	28.7%	26.7%	28.6%	31.6%
SG&A Exp.	576	578	440	508	581	619	534	581	637	741
D&A Exp.	137	131	132	138	146	161	167	168	164	201
Operating Profit	322	242	266	304	459	523	476	522	651	703
Op. Margin	10.5%	8.4%	10.0%	10.1%	12.8%	13.8%	13.6%	12.6%	14.5%	14.7%
Net Profit	171	189	141	203	303	362	285	369	407	394
Net Margin	5.6%	6.6%	5.3%	6.8%	8.5%	9.6%	8.1%	8.9%	9.1%	8.3%
Free Cash Flow	180	275	266	132	220	410	456	239	285	357
Income Tax	55	26	61	58	103	98	104	95	134	123

Balance Sheet Metrics

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Total Assets	3,001	2,784	2,763	3,402	4,445	4,860	5,042	5,171	5,772	6,542
Cash & Equivalents	279	130	149	122	133	210	320	257	332	419
Acc. Receivable	476	455	438	525	547	545	581	626	700	672
Inventories	586	543	554	739	836	842	841	1,043	1,191	1,229
Goodwill & Int.	499	599	629	932	1,694	1,752	1,789	1,692	1,864	2,401
Total Liabilities	1,412	1,440	1,452	1,928	2,803	2,905	2,816	2,793	3,420	3,839
Accounts Payable	144	160	176	265	273	302	351	430	404	367
Long-Term Debt	530	657	659	962	1,682	1,730	1,565	1,465	1,963	2,396
Total Equity	1,576	1,325	1,280	1,443	1,580	1,868	2,153	2,295	2,268	2,582
LTD/E Ratio	0.34	0.50	0.52	0.67	1.06	0.93	0.73	0.64	0.87	0.93

Profitability & Per Share Metrics

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Return on Assets	4.6%	6.5%	5.1%	6.6%	7.7%	7.8%	5.7%	7.2%	7.4%	6.4%
Return on Equity	8.1%	13.0%	10.8%	14.9%	20.0%	21.0%	14.2%	16.6%	17.9%	15.6%
ROIC	6.6%	9.2%	7.1%	9.2%	10.5%	10.3%	7.6%	9.7%	10.0%	8.4%
Shares Out.	88	80	77	78	76	76	76	75	73	72
Revenue/Share	33.72	33.65	33.70	38.07	45.71	49.29	45.98	53.67	60.50	66.16
FCF/Share	1.98	3.22	3.36	1.67	2.81	5.33	5.97	3.10	3.84	4.96

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