

Industrials/Multi-Industry

Short cycle datapoints from MSM and AMT: end markets continue to slow

Industry Overview

Demand is slowing, sequential stabilization in October

MSC Industrial Supply (ticker: MSM; not covered) reported CY3Q23 earnings and issued FY24 guidance on 10/25. MSM is a leading distributor of metalworking and maintenance and repair suppliers. We view industrial distributors as a broad indication of short-cycle industrial demand. Broadly speaking, in our view demand is slowing but expectations are for sequential stabilization in October m/m. This is consistent with the slowing results of our proprietary biweekly fluid power survey. Into 3Q23 earnings, we largely previewed a worsening orders environment q/q; MSM commentary supports this outlook. We view commentary around softening demand in line with our expectations for PH, ROK & AME.

Rates, recessionary fears impacting customer wallets

On the conference call, CEO Erik Gershwind stated that “We experienced deceleration in September. A portion of this was expected, as public sector capital purchases wound down at the end of 4Q. But the sequential stepdown went beyond this and was indicative of further softening.” Gershwind noted that the slowdown was driven by sustained higher interest rates and recessionary fears from companies and consumers. Commentary around rates is consistent with PNR 3Q23 earnings call yesterday.

Low-single digit UAW strike headwinds

MSM is also being impacted by the United Auto Workers’ (UAW) strike, both directly but mostly indirectly (e.g., job shops & machine shops, “many of whom service the auto industry”). Driven by autos & broad softening, Sept. average daily sales were up +1.3% y/y and down 8% on a sequential basis. As of halfway through the month, the company anticipates flat sequential performance from September levels with low-single digit headwinds from the UAW strike to daily sales in September and October. While OEMs are likely to be less impacted by the UAW strike (less exposure to job shops /machine shops than a distributor), we do estimate impact to ITW, DOV, ETN, & ITT.

MSM average daily sales guide for FY24 of 0-5% y/y

The company reported sales of \$1.04bn vs. \$1.01bn consensus. Adjusted EPS of \$1.64 came in above the Street at \$1.62. '24 average daily sales guide to grow 0-5% brackets +3.2% y/y consensus. +9.3% y/y 4Q daily sales was driven by growth initiatives, price, and M&A. National accounts were up mid-single digits with public sector account >60%.

Monthly manufacturing technology orders weaker in Aug.

The Associate for Manufacturing Technology (AMT) publishes monthly new orders of manufacturing technology. This report mostly reflects machine tools. The latest new orders, reported on October 9, totaled \$427mn in August, down (7.2)% y/y. Volumes were down (22.4)% y/y with price up 19.6% y/y. Orders were up +5.7% sequentially from \$404mn in July. President of AMT, Douglas Woods, stated “We are seeing industries focused on shorter-term projects reduce their spending, but at the same time, OEMs focused on longer-term production timelines have been increasing their spending, keeping orders at an elevated level.” We expect September orders (out mid-November) to reflect UAW impact and further softening.

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Exhibit 1: Acronyms used in this report

See below for acronyms

AME	Ametek
DOV	Dover
ETN	Eaton
ITT	ITT
ITW	Illinois Tool Works
PH	Parker Hannifin
PNR	Pentair
ROK	Rockwell

Source: BofA Global Research

BofA GLOBAL RESEARCH

Stocks mentioned

BofA Ticker	Bloomberg ticker	Company name	Price	Rating
AME	AME US	AMETEK	US\$ 140.97	B-2-7
DOV	DOV US	Dover Corp	US\$ 132.33	B-1-7
ETN	ETN US	Eaton Corp PLC	US\$ 199.64	B-1-7
ITW	ITWUS	Illinois Tool Works	US\$ 223.06	B-2-7
ITT	ITT US	ITT Inc.	US\$ 94.21	B-2-7
PH	PH US	Parker Hannifin	US\$ 373.28	B-1-7
PNR	PNR US	Pentair plc	US\$ 59.47	B-3-7
ROK	ROK US	Rockwell	US\$ 265.86	B-2-7

Source: BofA Global Research

Price objective basis & risk**AMETEK Inc (AME)**

We base our \$175 price objective on an 19x EV/EBITDA multiple of our 2024 estimates. Our target 19x multiple is in line with the 19x peer average on 2023E, reflecting Ametek's below-peer revenue and earnings growth profile.

Downside risks to our price objective are: 1) weaker industrial production trends, 2) slower pace of acquisitions, and 3) cyclical risks on shorter cycle component businesses. Upside risks are: 1) secular growth in automation and aerospace end markets, 2) accretive acquisitions, and 3) share gains for differentiated products.

Dover Corp (DOV)

We base our \$180 price objective on a 13x EV/EBITDA multiple of our 2025 estimates. Our target multiple is in line with multi-industrial peers, trading at 13x 2024 estimates. We argue that an in-line valuation discount is fair given Dover's improved portfolio mix, capital allocation strategy, and margin trajectory, offset by slower near-term revenue growth.

Downside risks to our PO are 1) slowing US industrial production, 2) not achieving expected returns from organic investments or acquisitions, and 3) slower-than-expected margin improvement.

Eaton Corp PLC (ETN)

We base our \$245 price objective on a 20x EV/EBITDA multiple of our 2024 estimates. Our target multiple is at a premium to the 15x peer average on 2023 estimates. We argue a premium valuation is warranted due to broad exposure to key growth end markets, expected upside from cyclical operating leverage, strong margin performance, and Eaton's less cyclical portfolio mix.

Downside risks to our PO are 1) a slower-than-expected manufacturing capex growth, 2) a more active M&A is inherently risky as it relies on the availability of accretive synergistic targets and the company's ability to integrate, and 3) the trajectory of the recovery in automotive and aerospace end markets.

Illinois Tool Works (ITW)

Our \$260 PO is based on a 17x multiple on our 2025 EV/EBITDA estimate, at a premium to the multis average trading 13x on 2024E and in line with high quality compounders. We believe valuation in line with high quality compounders is warranted given best-in-class operating margins, strong history of capital allocation, and the potential for cyclical end market recovery.

Downside risks to our PO are 1) Auto volumes constrained for longer by supply chain, limiting near-term margin expansion, 2) near-term macro headwinds (e.g., slowing PMI) and 3) industrial short-cycle exposure into a recession. Upside risks to our PO are 1) cyclical end market recovery drives better than expected organic growth, 2) restructuring and fixed cost savings drive more margin expansion than anticipated, and 3) broader macro holds up.

ITT Inc. (ITT)

We base our \$105 price objective on a 12x EV/EBITDA multiple of our 2024 estimates. Our 12x target multiple is at a discount to the peer group trading at 13x on 2023E. We think the below-peer valuation is warranted given above-average mix of European revenue and short-cycle industrial exposure.

Downside risks to our PO are: 1) ITT may overpay for deals in the pursuit of diversifying and expanding its product portfolio, 2) Lower than expected capex spending in the auto, oil & gas, power gen, and other key end markets, 3) Greater consolidation in the flow control market may increase competition and reduce prices across the industry.

Parker Hannifin Corporation (PH)

We base our \$475 price objective on a 13.4x EV/EBITDA multiple applied to our CY24E estimate. Our 13.4x target multiple is at a discount to the 16x multi-industrial peer average on 2023E and 19x Aerospace Suppliers peer average on 2023E. Parker has historically traded at a discount, but we believe it should start to close the gap with high quality peers AME and ITW.

Downside risks are: 1) industrial short-cycle destocking worse than expected, 2) Meggitt integration, and 3) the ability to offset material inflation through pricing. Upside risks: 1) Aerospace recovery has more upside given more exposure from Meggitt, and 2) Multiple expansion as the company closes the performance gap.

Pentair plc (PNR)

We base our \$46 price objective on a 8x EV/EBITDA multiple of our 2024 estimates. This is below the peer group trading at 13x on 2024 estimates. We think the below-peer group valuation is fair given below-average EBITDA margins and earnings growth longer term.

Upside risks are: 1) better-than-expected revenue growth in pools, 2) stronger execution may boost the company's valuation and provide more cash for buyback. Downside risks are: 1) Manitowoc Ice integration, 2) weaker spending growth in Industrial and Residential/Commercial markets.

Rockwell (ROK)

We base our \$335 price objective on a 17x EV/EBITDA multiple of our CY24 estimate. Our target multiple is a premium to the 14x peer average on 2023E. We argue a premium is warranted given ROK's position in the US automation market.

Upside risks are 1) supply chain improvement, 2) potentially accretive acquisitions.

Downside risks are 1) slowing global industrial production, 2) delays in global capex, 3) greater competition, and 4) supply-chain constraints.

Analyst Certification

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US - Multi-Industrials/Engineering and Construction Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
BUY				
	Ansys, Inc.	ANSS	ANSS US	Andrew Obin
	APi Group	APG	APG	Andrew Obin
	AspenTech	AZPN	AZPN US	Andrew Obin
	Atmus Filtration	ATMU	ATMU US	Andrew Obin
	Dover Corp	DOV	DOV US	Andrew Obin
	Eaton Corp PLC	ETN	ETN US	Andrew Obin
	Emerson Electric Co	EMR	EMR US	Andrew Obin
	Flowserve	FLS	FLS US	Andrew Obin
	General Electric Company	GE	GE US	Andrew Obin
	Honeywell International Inc.	HON	HON US	Andrew Obin
	Montrose Environmental Group, Inc.	MEG	MEG US	Andrew Obin
	Parker Hannifin Corporation	PH	PH US	Andrew Obin
	PTC Inc.	PTC	PTC US	Andrew Obin
	Rush	RUSHA	RUSHA US	Andrew Obin
	Vertiv	VRT	VRT US	Andrew Obin
NEUTRAL				
	3M Company	MMM	MMM US	Andrew Obin
	AMETEK Inc	AME	AME US	Andrew Obin
	Illinois Tool Works	ITW	ITW US	Andrew Obin
	ITT Inc.	ITT	ITT US	Andrew Obin
	Johnson Controls International PLC	JCI	JCI US	Andrew Obin
	Rockwell	ROK	ROK US	Andrew Obin
	Trane Technologies PLC	TT	TT US	Andrew Obin
	Vontier	VNT	VNT US	Andrew Obin
UNDERPERFORM				
	Allegion	ALLE	ALLE US	Andrew Obin
	Carrier Global Corp.	CARR	CARR US	Andrew Obin
	Core & Main	CNM	CNM US	Andrew Obin
	John Bean Technologies	JBT	JBT US	Andrew Obin
	Keysight	KEYS	KEYS US	David Ridley-Lane, CFA
	Pentair plc	PNR	PNR US	Andrew Obin
RSTR				
	Fortive Corporation	FTV	FTV US	Andrew Obin

Disclosures

Important Disclosures

Equity Investment Rating Distribution: Electrical Equipment Group (as of 30 Sep 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships ^{R1}	Count	Percent
Buy	15	55.56%	Buy	11	73.33%
Hold	5	18.52%	Hold	3	60.00%
Sell	7	25.93%	Sell	1	14.29%

Equity Investment Rating Distribution: Industrials/Multi-Industry Group (as of 30 Sep 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships ^{R1}	Count	Percent
Buy	43	48.86%	Buy	22	51.16%
Hold	26	29.55%	Hold	17	65.38%
Sell	19	21.59%	Sell	10	52.63%

Equity Investment Rating Distribution: Global Group (as of 30 Sep 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships ^{R1}	Count	Percent
Buy	1869	53.48%	Buy	1046	55.97%
Hold	828	23.69%	Hold	461	55.68%
Sell	798	22.83%	Sell	370	46.37%

^{R1} Issuers that were investment banking clients of BofA Securities or one of its affiliates within the past 12 months. For purposes of this Investment Rating Distribution, the coverage universe includes only stocks. A stock rated Neutral is included as a Hold, and a stock rated Underperform is included as a Sell.



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Investment rating	Total return expectation (within 12-month period of date of initial rating)	Ratings dispersion guidelines for coverage cluster ^{R2}
Buy	≥ 10%	≤ 70%
Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

^{R2} Ratings dispersions may vary from time to time where BofA Global Research believes it better reflects the investment prospects of stocks in a Coverage Cluster.

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