

Pentair plc

Raising numbers after a constructive investor day

Reiterate Rating: NEUTRAL | PO: 84.00 USD | Price: 79.17 USD

Transformation yields a positive margin runway

We attended PNR's 2024 investor day in New York City. The company articulated its focus on sourcing, operations, and 80/20. The 80/20 is focused on the company's pool, residential water treatment, and water supply/disposal operations and sales (~50% of sales). PNR initiated its new 80/20 program with an outside provider in Jan. '24. It appears to us that transformation is in early innings. PNR introduced a new margin target for 24% in 2026. While the official margin target for 24% in 2026 seems lower than investor expectations into the event, PNR articulated a reasonable path to 26% margins. We still see some headwinds on the volumes in 2024 from interest rates and historical cycles of commercial end markets following residential. Raise PO to \$84 on higher estimates, still on ~13.5x 2025E EV/EBITDA; methodology unchanged. Neutral.

"Official" 24% margin target accommodates a weak macro

PNR sees mid-single digit sales growth from '24-'26 and committed to 24% operating margins in 2026. However, this includes 200bps of "contingency" headwinds, which represent a downside macro scenario. It seems that transformation benefits would be marginally smaller on lower volumes. We view the 24% scenario as relatively unlikely. We estimate sales would have to fall 8.0% y/y in both 2025/2026 at 32% decrements in order to reach 24% margins in 2026, coupled with a ~15% Productivity haircut. The 2026 target reflects roughly 24% margins in Flow (600bps of expansion from 2023-2026), 26% margins in Water Solutions (500bps of expansion), and 35% margins in Pool (400bps of expansion). PNR committed to >100% cash conversion over 2024-2026. Long-term, we see low-hanging fruit that can be addressed through 80/20 activity to increase margins.

Raising our estimates, but including some cushion

We raise our 2025 estimate by \$0.21 to \$4.77 and our 2026 estimate by \$0.54 to \$5.44. Our previous forecast had assumed benefit from sourcing and operations decelerated y/y in 2025/2026. We now forecast modest acceleration as a) existing efforts roll through (90% of \$600mn in costs to address will be completed in 3Q24, 2) the company addresses an incremental \$1bn of costs, and 3) PNR increases footprint consolidation (namely in Flow). 15 of 41 total factories generate ~75% of PNR sales. We tweak pricing & volume leverage estimates. We haircut productivity guidance to account for potential timing delays and incremental reinvestment. We incorporate debt paydown in 2026.

Estimates (Dec) (US\$)	2021A	2022A	2023E	2024E	2025E
EPS	3.40	3.68	3.75	4.21	4.77
GAAP EPS	3.34	2.72	3.75	3.93	4.49
EPS Change (YoY)	36.0%	8.2%	1.9%	12.3%	13.3%
Consensus EPS (Bloomberg)			3.75	4.21	4.66
DPS	0.80	0.84	0.88	0.93	0.98
Valuation (Dec)					
P/E	23.3x	21.5x	21.1x	18.8x	16.6x
GAAP P/E	23.7x	29.1x	21.1x	20.1x	17.6x
Dividend Yield	1.0%	1.1%	1.1%	1.2%	1.2%
EV / EBITDA*	22.9x	20.5x	18.4x	16.8x	15.1x
Free Cash Flow Yield*	3.9%	2.0%	3.9%	5.0%	5.6%

* For full definitions of *IQmethod*SM measures, see page 7.

07 March 2024

Equity

Key Changes

(US\$)	Previous	Current
Price Obj.	80.00	84.00
2025E Rev (m)	4,367.3	4,389.8
2025E EPS	4.60	4.77

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Stock Data

Price	79.17 USD
Price Objective	84.00 USD
Date Established	7-Mar-2024
Investment Opinion	B-2-7
52-Week Range	50.15 USD - 80.14 USD
Mkt Val (mn) / Shares Out (mn)	14,140 USD / 178.6
Free Float	99.3%
Average Daily Value (mn)	137.00 USD
BofA Ticker / Exchange	PNR / NYS
Bloomberg / Reuters	PNR US / PNR.N
ROE (2023E)	21.1%
Net Dbt to Eqty (Dec-2022A)	81.5%
ESGMeter™	High

ESGMeter is not indicative of a company's future stock price performance and is not an investment recommendation or rating. ESGMeter is independent of BofA Global Research's equity investment rating, volatility risk rating, income rating, and price objective for that company. For full details, refer to "BofA ESGMeter Methodology".

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Timestamp: 07 March 2024 05:00AM EST

iQprofileSM Pentair plc

iQmethodSM – Bus Performance*

(US\$ Millions)	2021A	2022A	2023E	2024E	2025E
Return on Capital Employed	16.4%	14.5%	13.2%	13.6%	13.9%
Return on Equity	25.2%	23.8%	21.1%	20.1%	19.6%
Operating Margin	18.2%	18.6%	20.8%	22.3%	24.0%
Free Cash Flow	553	279	545	704	791

iQmethodSM – Quality of Earnings*

(US\$ Millions)	2021A	2022A	2023E	2024E	2025E
Cash Realization Ratio	1.1x	0.6x	1.0x	1.1x	1.1x
Asset Replacement Ratio	0.8x	0.8x	0.7x	0.7x	0.7x
Tax Rate	15.0%	14.5%	14.8%	16.5%	17.5%
Net Debt-to-Equity Ratio	33.0%	81.5%	56.5%	33.8%	14.7%
Interest Cover	NM	14.6x	7.2x	9.3x	11.6x

Income Statement Data (Dec)

(US\$ Millions)	2021A	2022A	2023E	2024E	2025E
Sales	3,765	4,122	4,105	4,207	4,390
% Change	24.8%	9.5%	-0.4%	2.5%	4.4%
Gross Profit	1,319	1,388	1,519	1,551	1,619
% Change	24.7%	5.2%	9.5%	2.1%	4.4%
EBITDA	735	820	911	1,002	1,116
% Change	30.8%	11.6%	11.0%	10.0%	11.4%
Net Interest & Other Income	(14)	(54)	(122)	(101)	(91)
Net Income (Adjusted)	571	610	624	700	795
% Change	36.1%	6.9%	2.3%	12.2%	13.4%

Free Cash Flow Data (Dec)

(US\$ Millions)	2021A	2022A	2023E	2024E	2025E
Net Income from Cont Operations (GAAP)	571	610	624	700	795
Depreciation & Amortization	78	107	115	120	119
Change in Working Capital	(32)	(215)	(59)	(17)	(12)
Deferred Taxation Charge	(9)	(45)	(93)	0	0
Other Adjustments, Net	7	(93)	33	(11)	(22)
Capital Expenditure	(60)	(85)	(76)	(88)	(88)
Free Cash Flow	553	279	545	704	791
% Change	8.1%	-49.6%	95.2%	29.2%	12.4%
Share / Issue Repurchase	(150)	(50)	10	0	0
Cost of Dividends Paid	(133)	(139)	(145)	(155)	(162)
Change in Debt	55	1,412	(333)	(200)	(19)

Balance Sheet Data (Dec)

(US\$ Millions)	2021A	2022A	2023E	2024E	2025E
Cash & Equivalents	95	109	170	520	1,129
Trade Receivables	534	532	562	576	601
Other Current Assets	675	918	837	855	882
Property, Plant & Equipment	310	345	362	388	415
Other Non-Current Assets	3,140	4,545	4,632	4,575	4,517
Total Assets	4,754	6,448	6,563	6,913	7,544
Short-Term Debt	0	0	0	0	0
Other Current Liabilities	1,052	1,063	950	962	1,000
Long-Term Debt	894	2,317	1,988	1,788	1,769
Other Non-Current Liabilities	386	359	408	410	413
Total Liabilities	2,332	3,739	3,346	3,161	3,182
Total Equity	2,422	2,708	3,217	3,752	4,362
Total Equity & Liabilities	4,754	6,448	6,563	6,913	7,544

* For full definitions of iQmethodSM measures, see page 7.

Company Sector

Industrials/Multi-Industry

Company Description

Pentair is a residential and commercial pure-play water treatment company. Pentair generated \$4.1bn of revenue in 2022 from its three segments, Pool (40% of revenue, residential pool), Water Solutions (24% of revenue, water filtration and ice), and Industrial and Flow Technologies (36% of revenue, industrial filtration, irrigation, and commercial pumps).

Investment Rationale

Pentair's execution outperformed our expectations in 2023 and we see strong visibility on margins in 2024, largely on the back of its Transformation Initiatives. Our Neutral rating balances upside to consensus on margins in 1H24 with our more bearish topline outlook.

Stock Data

Average Daily Volume 1,730,432

Quarterly Earnings Estimates

	2022	2023
Q1	0.85A	0.91A
Q2	1.02A	1.03A
Q3	0.99A	0.94A
Q4	0.82A	0.87E

Where we're different than guidance

The company explicitly guided to \$160mn in savings from sourcing over 2024-2026 and \$100mn in operational excellence. We were previously modeling decelerating transformation activity. We now forecast some accelerating benefit as a) existing efforts roll through (90% of \$600mn in costs to address will be completed in 3Q24, 2) the company addresses an incremental \$1bn of costs, and 3) PNR increases footprint consolidation (namely in Flow). 15 of 41 total factories generate ~75% of PNR sales. We tweak pricing and volume leverage estimates. We haircut the guide for productivity to account for potential timing delays and incremental reinvestment.

Our estimates had been above the Street on margins (23.8% in 2026E vs. consensus on Visible Alpha for 23.4%). Our model reflects the company's framework for \$75mn productivity, net of reinvestment benefit in 2024, and the rest of the sourcing/operational excellence benefit split evenly between 2025 and 2026.

Exhibit 1: BofA estimates for margins/volumes/price, CURRENT

We adjust our estimates to account for accelerating productivity

Revenue	2023E	2024E	2025E	2026E
Revenue BOP	4,122	4,105	4,207	4,390
Volume	(462)	16	120	123
Price	262	86	63	66
Acq/Divestiture	183	-	-	-
FX	2	0	-	-
Revenue EOP	4,106	4,207	4,390	4,578
Revenue EOP from model	4,105	4,207	4,390	4,578
Difference		-		
Revenue growth	-0.4%	2.5%	4.4%	4.3%

Segment Income	2023	2024	2025	2026
Segment Income BOP	768	855	940	1,054
Growth/price/Acq.	208	96	95	99
Volume leverage assumption	27.5%	61.2%	27.0%	27.0%
FX	(3)	0	-	-
Inflation	(186)	(84)	(63)	(66)
Productivity	68	73	82	77
Segment Income EOP	855	940	1,054	1,165
Segment Income EOP from model	855	940	1,054	1,165
Difference	-	-	-	-
Segment income growth	11.4%	9.9%	12.2%	10.5%
Margins	2023	2024	2025	2026
Segment Margin BOP	18.6%	20.8%	22.3%	24.0%
Segment Margin EOP	20.8%	22.3%	24.0%	25.4%

Source: BofA Global Research estimates

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Exhibit 2: BofA margin bridge, PRIOR

We raise our volume estimates and lower our pricing estimates, in line with commentary

Revenue	2023E	2024E	2025E	2026E
Revenue BOP	4,122	4,105	4,207	4,367
Volume	(462)	16	82	86
Price	262	86	78	81
Acq/Divestiture	183	-	-	-
FX	2	0	-	-
Revenue EOP	4,106	4,207	4,367	4,534
Revenue EOP from model	4,105	4,207	4,367	4,534
Difference		-		
Revenue growth	-0.4%	2.5%	3.8%	3.8%

Segment Income	2023	2024	2025	2026
Segment Income BOP	768	855	940	1,012
Growth/price/Acq.	208	96	109	113
Volume leverage assumption	27.5%	61.2%	37.5%	37.5%
FX	(3)	0	-	-
Inflation	(186)	(84)	(78)	(81)
Productivity	68	73	41	35
Segment Income EOP	855	940	1,012	1,079
Segment Income EOP from model	855	940	1,012	1,079
Difference	-	-	-	-
Segment income growth	11.4%	9.9%	7.6%	6.6%
Margins	2023	2024	2025	2026
Segment Margin BOP	18.6%	20.8%	22.3%	23.2%
Segment Margin EOP	20.8%	22.3%	23.2%	23.8%

Source: BofA Global Research estimates

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Below we show the illustrative midpoint of the company's guidance for its 2026 "upside-scenario" margin target of 26% versus the "contingency"-adjusted 24% target.

Exhibit 3: Illustrative margin bridge to 26% margins

The 26% margin guide assumes the \$260mn in sourcing and operations is not offset by incremental reinvestment or execution risk

Revenue	2023E	2024E	2025E	2026E
Revenue BOP	4,122	4,106	4,209	4,420
Volume	(462)	41	147	155
Price	262	62	63	66
Acq/Divestiture	183	-	-	-
FX	2	0	-	-
Revenue EOP	4,106	4,209	4,420	4,640
Revenue EOP from model	4,105	n/a	n/a	n/a
Difference	-			
Revenue growth	-0.4%	2.5%	5.0%	5.0%
Segment Income	2023	2024	2025	2026
Segment Income BOP	768	855	937	1,071
Growth/price/Acq.	208	66	103	108
Volume leverage assumption	27.5%	10.0%	27.0%	27.0%
FX	(3)	0	-	-
Inflation	(186)	(60)	(61)	(64)
Productivity	68	75	93	93
Segment Income EOP	855	937	1,071	1,208
Segment Income EOP from model	855			
Segment income growth	11.4%	9.5%	14.4%	12.7%
Segment Margin BOP	18.6%	20.8%	22.3%	24.2%
Segment Margin EOP	20.8%	22.3%	24.2%	26.0%

Source: BofA Global Research estimates

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Exhibit 4: Illustrative margin bridge to 24% margins

It seems that 24% margins would require a macro downturn

Revenue	2023E	2024E	2025E	2026E
Revenue BOP	4,122	4,106	4,209	3,872
Volume	(462)	103	(400)	(368)
Price	262	-	63	58
Acq/Divestiture	183	-	-	-
FX	2	-	-	-
Revenue EOP	4,106	4,209	3,872	3,563
Revenue EOP from model	4,105	n/a	n/a	n/a
Difference	-			
Revenue growth	-0.4%	2.5%	-8.0%	-8.0%
Segment Income	2023	2024	2025	2026
Segment Income BOP	768	855	942	893
Growth/price/Acq.	208	10	(65)	(60)
Volume leverage assumption	27.5%	10.0%	32.0%	32.0%
FX	(3)	-	-	-
Inflation	(186)	2	(63)	(58)
Productivity	68	75	79	79
Segment Income EOP	855	942	893	855
Segment Income EOP from model	855			
Segment income growth	11.4%	10.2%	-5.2%	-4.3%
Segment Margin BOP	18.6%	20.8%	22.4%	23.1%
Segment Margin EOP	20.8%	22.4%	23.1%	24.0%

Source: BofA Global Research estimates

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Valuation

We base our \$84 price objective on a ~13.5x multiple on our 2025E estimates. This is at a discount to the peer average at 15x 2024E. We think a slight discount is warranted given better EBITDA margins, offset by more cyclical businesses.

Exhibit 5: PNR comparable valuation analysis

Our \$84 price objective is based on ~13.5x 2025E EV/EBITDA

Company	Ticker	Stock Price 3/6/2024	P/E		EV/EBITDA		EBITDA Margin		EPS growth	
			2024E	2025E	2024E	2025E	2024E	2025E	2024E	2025E
Dover	DOV	\$170.92	18.8 x	17.0 x	14.4 x	13.3 x	21.8%	22.5%	3.2%	10.6%
Hayward Holdings	HAYW	\$13.95	1.4 x	1.3 x	18.9 x	17.7 x	27.2%	27.8%	1.3%	9.3%
Mueller Water*	MWA	\$15.41	23.0 x	19.6 x	12.2 x	10.3 x	18.0%	19.2%	19.4%	13.1%
Thermon*	THR	\$27.54	15.3 x	14.2 x	10.2 x	8.6 x	20.0%	19.6%	9.6%	1.9%
Watts Water*	WTS	\$204.35	23.9 x	22.6 x	15.2 x	14.5 x	19.9%	20.2%	6.1%	6.1%
Xylem*	XYL	\$126.35	30.6 x	27.8 x	16.7 x	14.9 x	19.8%	20.6%	10.5%	10.0%
Zurn Water Solutions*	ZWS	\$31.40	<u>27.4 x</u>	<u>24.8 x</u>	<u>17.4 x</u>	<u>14.1 x</u>	<u>23.9%</u>	<u>24.5%</u>	<u>20.6%</u>	<u>10.6%</u>
AVERAGE			20.1 x	18.2 x	15.0 x	13.4 x	21.5%	22.1%	10.1%	8.8%
Pentair	PNR	\$79.17	18.8 x	16.7 x	14.4 x	13.0 x	23.8%	25.3%	12.1%	13.0%
Pentair at PO	PNR	\$84.00	20.0 x	17.7 x	15.2 x	13.7 x				

Source: BofA Global Research, Bloomberg (*based on Bloomberg consensus estimates)

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Price objective basis & risk

Pentair plc (PNR)

We base our \$84 price objective on a 13.5x EV/EBITDA multiple of our 2025 estimates. This slightly below the peer group trading at 15x on 2024 estimates. We think the below-peer valuation is fair given above average EBITDA margins offset by more cyclical topline.

Upside risks are: 1) better-than-expected revenue growth in pools, 2) success on incremental productivity actions. Downside risks are: 1) Reinvestment in most profitable (Pool) segment, 2) execution risk on sourcing & consolidation activities.

Analyst Certification

I, Andrew Obin, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.

US - Multi-Industrials/Engineering and Construction Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
BUY				
	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
	ITT Inc.	ITT	ITT 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
	Vontier	VNT	VNT US	Andrew Obin
NEUTRAL				
	3M Company	MMM	MMM US	Andrew Obin
	AMETEK Inc	AME	AME US	Andrew Obin
	Fortive Corporation	FTV	FTV US	Andrew Obin
	Johnson Controls International PLC	JCI	JCI US	Andrew Obin
	Pentair plc	PNR	PNR US	Andrew Obin
	Rockwell	ROK	ROK US	Andrew Obin
	Trane Technologies PLC	TT	TT 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
	Illinois Tool Works	ITW	ITW US	Andrew Obin
	John Bean Technologies	JBT	JBT US	Andrew Obin
	Keysight	KEYS	KEYS US	David Ridley-Lane, CFA

iQmethodSM Measures Definitions

Business Performance

Return On Capital Employed

Return On Equity

Operating Margin

Earnings Growth

Free Cash Flow

Quality of Earnings

Cash Realization Ratio

Asset Replacement Ratio

Tax Rate

Net Debt-To-Equity Ratio

Interest Cover

Valuation Toolkit

Price / Earnings Ratio

Price / Book Value

Dividend Yield

Free Cash Flow Yield

Enterprise Value / Sales

EV / EBITDA

Numerator

NOPAT = (EBIT + Interest Income) × (1 – Tax Rate) + Goodwill Amortization

Net Income

Operating Profit

Expected 5 Year CAGR From Latest Actual

Cash Flow From Operations – Total Capex

Numerator

Cash Flow From Operations

Capex

Tax Charge

Net Debt = Total Debt – Cash & Equivalents

EBIT

Numerator

Current Share Price

Current Share Price

Annualised Declared Cash Dividend

Cash Flow From Operations – Total Capex

EV = Current Share Price × Current Shares + Minority Equity + Net Debt +

Other LT Liabilities

Enterprise Value

Denominator

Total Assets – Current Liabilities + ST Debt + Accumulated Goodwill

Amortization

Shareholders' Equity

Sales

N/A

N/A

Denominator

Net Income

Depreciation

Pre-Tax Income

Total Equity

Interest Expense

Denominator

Diluted Earnings Per Share (Basis As Specified)

Shareholders' Equity / Current Basic Shares

Current Share Price

Market Cap = Current Share Price × Current Basic Shares

Sales

Basic EBIT + Depreciation + Amortization

iQmethodSM is the set of BofA Global Research standard measures that serve to maintain global consistency under three broad headings: Business Performance, Quality of Earnings, and validations. The key features of iQmethod are: A consistently structured, detailed, and transparent methodology. Guidelines to maximize the effectiveness of the comparative valuation process, and to identify some common pitfalls.

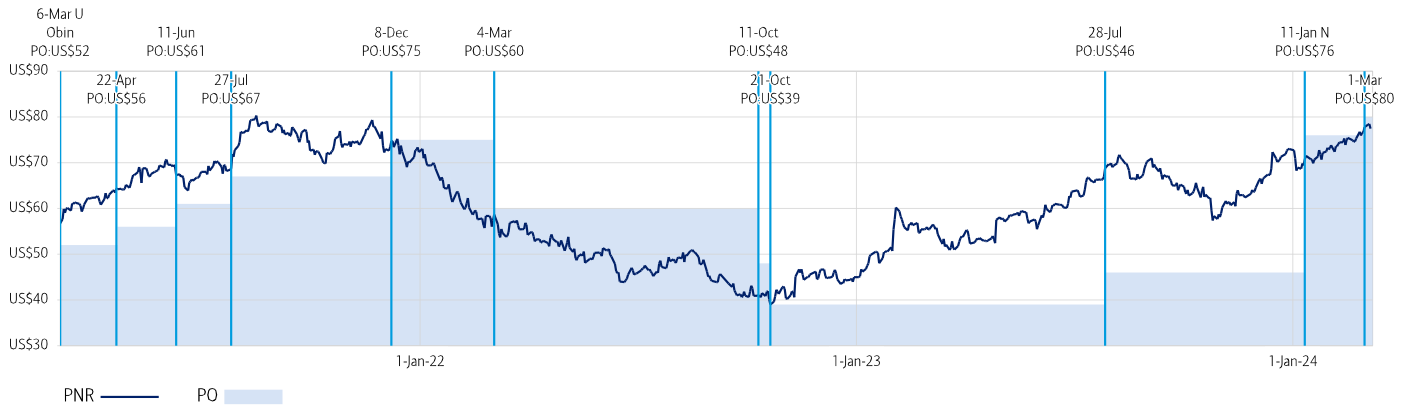
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Disclosures

Important Disclosures

Pentair plc (PNR) Price Chart



The Investment Opinion System is contained at the end of the report under the heading "Fundamental Equity Opinion Key". Dark grey shading indicates the security is restricted with the opinion suspended. Medium grey shading indicates the security is under review with the opinion withdrawn. Light grey shading indicates the security is not covered. Chart is current as of a date no more than one trading day prior to the date of the report.

Equity Investment Rating Distribution: Industrials/Multi-Industry Group (as of 31 Dec 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships ^{R1}	Count	Percent
Buy	45	50.56%	Buy	25	55.56%
Hold	26	29.21%	Hold	13	50.00%
Sell	18	20.22%	Sell	7	38.89%

Equity Investment Rating Distribution: Global Group (as of 31 Dec 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships ^{R1}	Count	Percent
Buy	1895	53.62%	Buy	1083	57.15%
Hold	832	23.54%	Hold	454	54.57%
Sell	807	22.84%	Sell	383	47.46%

^{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}
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Underperform	N/A	≥ 20%

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