

Eaton Corp PLC

From strength to strength with 4Q23 results

Reiterate Rating: BUY | PO: 300.00 USD | Price: 264.57 USD

Steady demand trends; 2024 adj. EPS guide above Street

Trailing twelve months (TTM) Electrical orders fell (2)% y/y. However, Electrical backlog was flat sequentially implying a book-to-bill in the quarter of ~1.0x. Aerospace TTM orders were up 7% y/y and backlog rose sequentially. 2024 organic revenue guidance of 6.5-8.5% y/y is achievable in a wide range of economic scenarios, in our view. The midpoint of adj. EPS guidance (\$9.95-10.35) was \$0.13 above \$10.02 consensus. Olivier Leonetti will become CFO on 2/5. As a member of board since 2019, we expect a smooth transition and little change to the company's communications style. Reiterate Buy. We raise our Price Objective by \$25 to \$300, based on 22x 2025 EV/EBITDA multiple (versus 20x previously). Our target multiple is at a premium to the 15x peer average on 2024 estimates, reflecting Eaton's secular exposure & margin performance.

Tailwinds from megaproject, data centers

In 2023, megaprojects (defined as projects >\$1bn in size) represented 3% of Electrical Americas revenue, but 6% of segment orders and 16% of the negotiation pipeline. This suggests a growing tailwind to orders and revenue as these projects move forward. Data centers (~9% of total revenue) remain the hottest end market, in our view. Data center revenue grew 20% y/y in 4Q, with TTM orders up 30% y/y, and the negotiation pipeline up a remarkable 160% y/y.

Restructuring program aims for simplification & scale

Eaton announced a new, three-year \$375mn program that includes consolidation of facilities, building up shared services, and deploying new digital technologies. The program targets \$50mn of cost savings in 2024 (or ~20bp benefit to margins) ramping to \$325mn run-rate by 4Q26-end. A similarly sized ~\$450mn program which ran over 2015-17 drove 100+bp of margin expansion during a period with flattish revenue.

Raising our 2024 adj. EPS to \$10.15, +11% y/y

For 2024, we forecast 7.3% y/y organic revenue growth (versus guidance of 6.5-8.5%) and segment operating margin of 22.7% (up 70bp y/y). These assumptions yield our adj. EPS of \$10.15 (up \$0.20 from our prior estimate). For 2025, we forecast 7.0% y/y organic growth and 30% incremental margins driving our adj. EPS of \$10.84, +7% y/y.

Estimates (Dec) (US\$)	2022A	2023A	2024E	2025E	2026E
EPS	7.56	9.12	10.15	10.84	11.65
GAAP EPS	6.14	8.02	9.01	10.05	10.88
EPS Change (YoY)	14.2%	20.6%	11.3%	6.8%	7.5%
Consensus EPS (Bloomberg)			10.04	11.06	12.11
DPS	3.24	3.44	3.64	3.72	3.80
Valuation (Dec)					
P/E	35.0x	29.0x	26.1x	24.4x	22.7x
GAAP P/E	43.1x	33.0x	29.4x	26.3x	24.3x
Dividend Yield	1.2%	1.3%	1.4%	1.4%	1.4%
EV / EBITDA*	30.6x	24.9x	22.5x	20.8x	19.6x
Free Cash Flow Yield*	1.7%	2.5%	3.0%	3.2%	3.4%

* For full definitions of *IQmethod*SM measures, see page 8.

05 February 2024

Equity

Key Changes

(US\$)	Previous	Current
Price Obj.	275.00	300.00
2024E Rev (m)	24,706.7	24,901.5
2025E Rev (m)	26,254.0	26,643.6
2026E Rev (m)	27,772.5	28,233.9
2024E EPS	9.95	10.15
2025E EPS	10.59	10.84
2026E EPS	11.33	11.65

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Stock Data

Price	264.57 USD
Price Objective	300.00 USD
Date Established	5-Feb-2024
Investment Opinion	B-1-7
52-Week Range	155.38 USD - 264.75 USD
Mkt Val (mn) / Shares Out (mn)	114,400 USD / 432.4
Free Float	99.7%
Average Daily Value (mn)	375.47 USD
BofA Ticker / Exchange	ETN / NYS
Bloomberg / Reuters	ETN US / ETN.N
ROE (2024E)	21.0%
Net Dbt to Eqty (Dec-2023A)	46.0%
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: 05 February 2024 05:30AM EST

iQprofileSM Eaton Corp PLC

iQmethodSM – Bus Performance*

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Return on Capital Employed	9.0%	11.0%	11.8%	12.9%	13.5%
Return on Equity	18.1%	20.2%	21.0%	21.3%	21.0%
Operating Margin	14.4%	16.7%	18.1%	18.7%	19.0%
Free Cash Flow	1,935	2,867	3,397	3,618	3,930

iQmethodSM – Quality of Earnings*

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Cash Realization Ratio	0.8x	1.0x	1.0x	1.0x	1.0x
Asset Replacement Ratio	1.5x	1.7x	1.7x	1.7x	1.7x
Tax Rate	15.4%	15.8%	18.0%	18.0%	18.5%
Net Debt-to-Equity Ratio	47.4%	46.0%	45.0%	35.6%	26.8%
Interest Cover	21.1x	26.3x	31.8x	37.2x	42.2x

Income Statement Data (Dec)

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Sales	20,753	23,196	24,902	26,644	28,234
% Change	5.7%	11.8%	7.4%	7.0%	6.0%
Gross Profit	6,887	8,434	9,491	10,225	10,865
% Change	8.7%	22.5%	12.5%	7.7%	6.3%
EBITDA	4,009	4,918	5,444	5,881	6,264
% Change	19.8%	22.7%	10.7%	8.0%	6.5%
Net Interest & Other Income	(145)	(152)	(142)	(134)	(127)
Net Income (Adjusted)	3,030	3,658	4,040	4,280	4,576
% Change	14.0%	20.7%	10.4%	5.9%	6.9%

Free Cash Flow Data (Dec)

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Net Income from Cont Operations (GAAP)	2,462	3,223	3,590	3,969	4,274
Depreciation & Amortization	954	939	924	909	894
Change in Working Capital	(688)	(180)	(16)	(160)	(147)
Deferred Taxation Charge	(128)	(1,855)	(300)	(300)	(300)
Other Adjustments, Net	(67)	1,497	(4)	0	0
Capital Expenditure	(598)	(757)	(797)	(799)	(791)
Free Cash Flow	1,935	2,867	3,397	3,618	3,930
% Change	21.9%	48.2%	18.5%	6.5%	8.6%
Share / Issue Repurchase	(286)	(506)	(1,939)	(955)	(1,135)
Cost of Dividends Paid	(1,299)	(1,373)	(1,441)	(1,460)	(1,484)
Change in Debt	300	614	(467)	(682)	0

Balance Sheet Data (Dec)

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Cash & Equivalents	555	488	94	674	2,050
Trade Receivables	4,076	4,475	4,788	5,123	5,429
Other Current Assets	4,115	4,591	4,362	4,580	4,773
Property, Plant & Equipment	3,146	3,530	3,403	3,293	3,190
Other Non-Current Assets	23,122	25,348	25,348	25,348	25,348
Total Assets	35,014	38,432	37,995	39,019	40,791
Short-Term Debt	334	1,025	300	300	300
Other Current Liabilities	6,027	6,722	6,791	7,183	7,535
Long-Term Debt	8,321	8,244	8,502	7,820	7,820
Other Non-Current Liabilities	3,257	3,372	3,072	2,772	2,472
Total Liabilities	17,939	19,363	18,664	18,075	18,126
Total Equity	17,075	19,069	19,331	20,944	22,664
Total Equity & Liabilities	35,014	38,432	37,995	39,019	40,791

* For full definitions of iQmethodSM measures, see page 8.

Company Sector

Electrical Equipment

Company Description

Eaton Corp. (ETN) is a leading diversified industrial manufacturer of electrical control products, aerospace systems, and automotive systems.

Investment Rationale

We see ETN as a beneficiary of the US federal government's focus on potential green initiatives and reshoring. ETN is well positioned strategically with a localized supply chain, versus other competitors.

Stock Data

Average Daily Volume 1,419,188

Quarterly Earnings Estimates

	2023	2024
Q1	1.88A	2.25E
Q2	2.21A	2.50E
Q3	2.47A	2.64E
Q4	2.55A	2.77E

Raising 2024 adj. EPS to \$10.15, +11% y/y

We have raised our 2024 organic revenue growth by 30bp to 7.3%. Our segment operating margin is 10bp lower to 22.7%, due to a lower margin assumption in Vehicle & eMobility. A greater share repurchase assumption (\$1.9bn versus \$0.6bn prior) was offset by slightly higher tax rate and corporate expense. Net-net, our adjusted EPS is \$0.20 higher at \$10.15, +11% y/y.

Eaton's 2024 FCF is burdened by a \$800mn in capex (versus \$0.5bn of depreciation) to support incremental capacity. We also estimate ~\$100mn in cash restructuring expense (versus ~\$175mn of planned charges in 2023).

For 2025, we forecast 7.0% y/y organic revenue growth and 30% incremental margins driving our adj. EPS of \$10.84, +7% y/y. The new three-year restructuring plan likely adds upside risks to our incremental margin assumptions.

Exhibit 1: 2024 guidance and BofA estimate changes

We raise our adjusted EPS to \$10.15

	ETN Guidance	BofA Estimate	
	As of 4Q23	Prior	New
Organic revenue growth (y/y %)	6.5-8.5%	7.0%	7.3%
Segment operating margin	22.4%-22.8%	22.8%	22.7%
Tax rate	17-18%	17.5%	18.0%
Adjusted EPS	\$9.95-\$10.35	\$9.95	\$10.15
Operating Cash Flow	\$4.0-\$4.4bn	\$4.0bn	\$4.2bn
FCF	\$3.2-\$3.6bn	\$3.4bn	\$3.4bn
Capex	\$800mn	\$644mn	\$797mn
Share Repurchases	\$1,500-2,500mn	\$554mn	\$1,939mn

Source: BofA Global Research, company filings

BofA GLOBAL RESEARCH

For 1Q24, we forecast +6.3% y/y organic revenue growth (off the toughest year ago comparison in 2023) and a 21.0% segment operating margin, yielding our adjusted EPS estimate of \$2.25, which compares to \$2.21-\$2.31 guidance.

BofA segment-level estimates

Below, we outline changes to our segment-level assumptions. Lower build rates for commercial vehicles were more than offset by a better outlook for aerospace.

Exhibit 2: Segment organic revenue growth guidance vs. BofA

Raising our organic revenue growth forecast to 7.3% y/y

	ETN Guidance	BofA 2024E	
	As of 4Q23	Prior	New
Organic revenue growth			
Electrical Americas	9-11%	10.7%	11.4%
Electrical Global	2.5-4.5%	2.5%	2.4%
Electrical Total		7.6%	8.0%
Aerospace	9-11%	7.0%	10.3%
Vehicle	(4)-0%	2.0%	-3.6%
eMobility	25-35%	13.2%	24.3%
Total Eaton	6.5-8.5%	7.0%	7.3%

Source: BofA Global Research, company filings

BofA GLOBAL RESEARCH

We raised our forecast for Electrical margins by 30bp, but this was more than offset by continued investment in eMobility (which support the mid-20% top line growth) and associated decremental margins with the revenue decline in Vehicle. Similar to other aerospace companies, margins at Eaton's Aerospace are influenced by mix.

Exhibit 3: Segment margin guidance vs. BofA

Lowering our segment margin forecast to 22.7%

	ETN Guidance	BofA 2024E	
	As of 4Q23	Prior	New
Operating margin			
Electrical Americas	26.8-27.2%	26.8%	27.2%
Electrical Global	19.4-19.8%	19.4%	19.5%



Exhibit 3: Segment margin guidance vs. BofA

Lowering our segment margin forecast to 22.7%

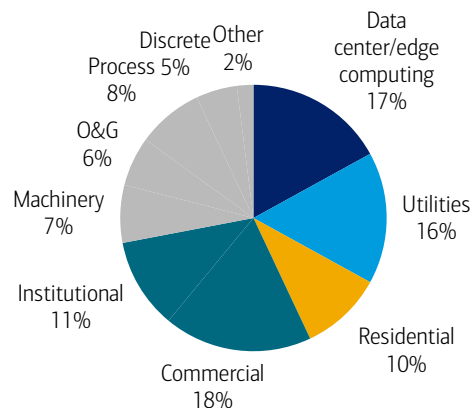
	ETN Guidance	BofA 2024E	
Electrical Total		24.2%	24.5%
Aerospace	23.3%-23.7%	24.1%	23.5%
Vehicle	16.3%-16.7%	17.9%	16.5%
eMobility	1.0%-2.0%	5.1%	0.5%
Total Eaton segment margin	22.4%-22.8%	22.8%	22.7%

Source: BofA Global Research, company filings

BofA GLOBAL RESEARCH

Electrical: 11% y/y sales, (2)% y/y orders**Exhibit 4: Electrical total breakout by end market**

Data centers represent a growing portion of Electrical segment

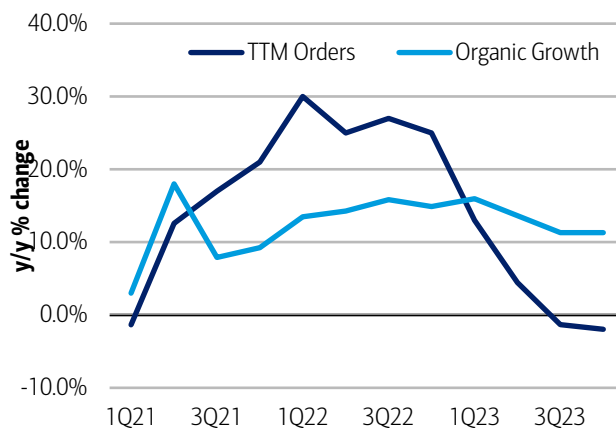


Source: BofA Global Research estimates, company reports

BofA GLOBAL RESEARCH

Exhibit 5: Electrical total TTM orders and organic revenue y/y %

Revenue +11% y/y in 4Q23, TTM orders (2)% y/y



Source: BofA Global Research

BofA GLOBAL RESEARCH

4Q trailing twelve month orders declined ~(-2)% y/y. By region, Americas' orders declined (4)% y/y and Global rose +1%. Backlog was flat sequentially.

Organic revenue growth of 11% y/y was steady with last quarter's pace. Americas (+16% y/y) continues to outpace global (+4% y/y).

Incremental margin was a remarkable 51%, driving 320bp of y/y margin expansion to 25.0%.

Aerospace: modest revenue deceleration on tough comps

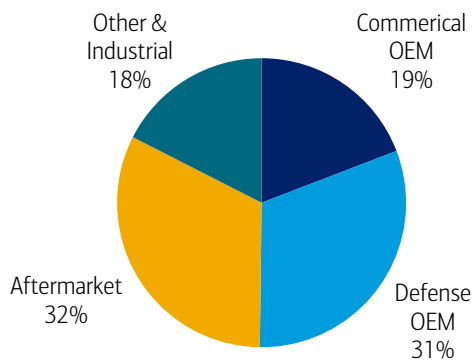
Orders slightly decelerated to 7% y/y on a rolling twelve-month basis from 16% last quarter. However, backlog rose 3% sequentially and the trailing twelve month book-to-bill was 1.1x.

Organic growth of 8% y/y was a deceleration from last quarter's 10% pace, on a 300bp harder year ago comparison. Commercial OEM grew 25% y/y and commercial aftermarket grew 18% y/y, partially offset by softer defense OEM shipments.

Segment margin of 22.4% was down 240bp y/y, largely reflecting product mix in the quarter.

Exhibit 6: Aerospace segment by end market

Aftermarket includes Commercial and Defense

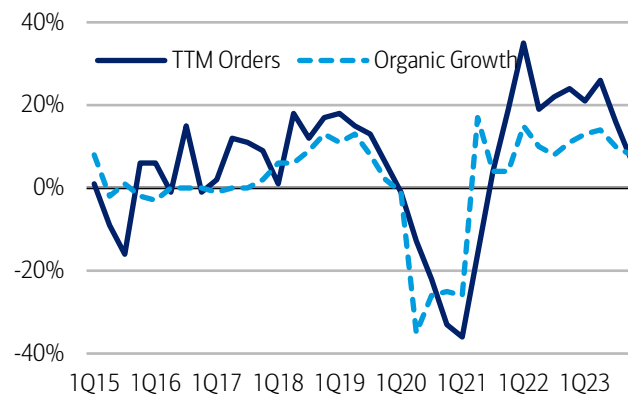


Source: BofA Global Research estimates, company report

BofA GLOBAL RESEARCH

Exhibit 7: Aerospace orders vs. organic growth

Organic bookings up 7% y/y on a 12-month rolling basis



Source: BofA Global Research company filings

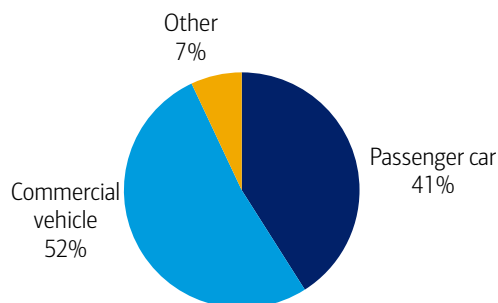
BofA GLOBAL RESEARCH

Vehicle: solid margin performance

Vehicle organic revenue growth was flat y/y, a slight improvement from down (1)% last quarter. Margins expanded 270bp y/y, aided by operational improvements and price/cost.

Exhibit 8: Vehicles revenue by end market

Balanced mix of end markets



Source: BofA Global Research, company filings

BofA GLOBAL RESEARCH

eMobility: strong growth as investments continue

In 4Q, eMobility segment grew 18% y/y organically. Margins continue to be negative as the company invests heavily in R&D as part of its long-term goal to build out its electric vehicle business. Margins declined 810bp y/y to (9.4)%. The company highlighted platform wins that will yield over \$1bn in annual sales at maturity. This compares to 2023 revenue of \$636mn.

Valuation

We base our \$300 price objective on a 22x EV/EBITDA multiple of our 2025 estimates. Our target multiple is at a premium to the 15x peer average on 2024 estimates. We argue a premium valuation is warranted due to expected upside from cyclical operating leverage, strong margin performance, and Eaton's less cyclical portfolio mix.

Exhibit 9: Eaton valuation vs. peers

Our \$300 price objective reflects 17x EV/EBITDA multiple on our 2024 estimates

Company	Ticker	Stock Price 2/2/2024	P/E		EV/EBITDA		EBITDA margin		EPS Growth	
			2024E	2025E	2024E	2025E	2024E	2025E	2024E	2025E
ABB	ABLZF	\$44.09	21.4 x	19.4 x	13.3 x	12.2 x	19.1%	19.7%	5%	11%
Dover	DOV	\$157.59	17.4 x	15.7 x	13.4 x	12.4 x	21.6%	22.1%	3%	11%
Emerson	EMR	\$93.92	17.5 x	16.1 x	11.8 x	11.0 x	26.0%	26.5%	15%	9%
General Electric	GE	\$137.02	32.5 x	26.1 x	19.3 x	15.2 x	15.7%	14.9%	59%	24%
Honeywell	HON	\$196.44	19.5 x	17.5 x	13.0 x	12.1 x	26.6%	27.1%	10%	11%
Hubbell*	HUBB	\$353.81	21.7 x	20.3 x	15.5 x	14.2 x	22.5%	22.9%	7%	7%
Trane Technologies	TT	\$275.83	28.6 x	26.9 x	20.1 x	19.0 x	18.0%	18.2%	7%	7%
Illinois Tool Works	ITW	\$254.26	25.0 x	23.2 x	18.2 x	17.3 x	28.0%	28.3%	4%	8%
Johnson Controls	JCI	\$53.90	13.8 x	11.8 x	10.0 x	9.2 x	15.7%	16.5%	10%	17%
Legrand	LGRVF	\$90.74	21.4 x	19.7 x	14.3 x	13.3 x	22.0%	23.0%	-13%	9%
Schneider	SBGSF	\$202.93	27.1 x	24.5 x	16.4 x	15.1 x	20.4%	20.8%	9%	11%
AVERAGE			22.4 x	20.1 x	15.0 x	13.7 x	21.4%	21.8%	11%	11%
Eaton	ETN	\$270.39	26.6 x	24.9 x	21.4 x	19.8 x	21.9%	22.1%	11%	7%
Eaton at PO		\$300.00	29.6 x	27.7 x	23.5 x	21.8 x				

Source: BofA Global Research, Bloomberg

BofA GLOBAL RESEARCH

Price objective basis & risk

Eaton Corp PLC (ETN)

We base our \$300 price objective on a 22x EV/EBITDA multiple of our 2025 estimates. Our target multiple is at a premium to the 15x peer average on 2024 estimates. We argue a premium valuation is warranted due to 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.

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				
	APi Group	APG	APG US	Andrew Obin
	AspenTech	AZPN	AZPN US	Andrew Obin
	Atmos 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

$\text{NOPAT} = (\text{EBIT} + \text{Interest Income}) \times (1 - \text{Tax Rate}) + \text{Goodwill Amortization}$

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

$\text{EV} = \text{Current Share Price} \times \text{Current Shares} + \text{Minority Equity} + \text{Net Debt} +$

Other LT Liabilities

Enterprise Value

Denominator

$\text{Total Assets} - \text{Current Liabilities} + \text{ST Debt} + \text{Accumulated Goodwill}$

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

$\text{Market Cap} = \text{Current Share Price} \times \text{Current Basic Shares}$

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.

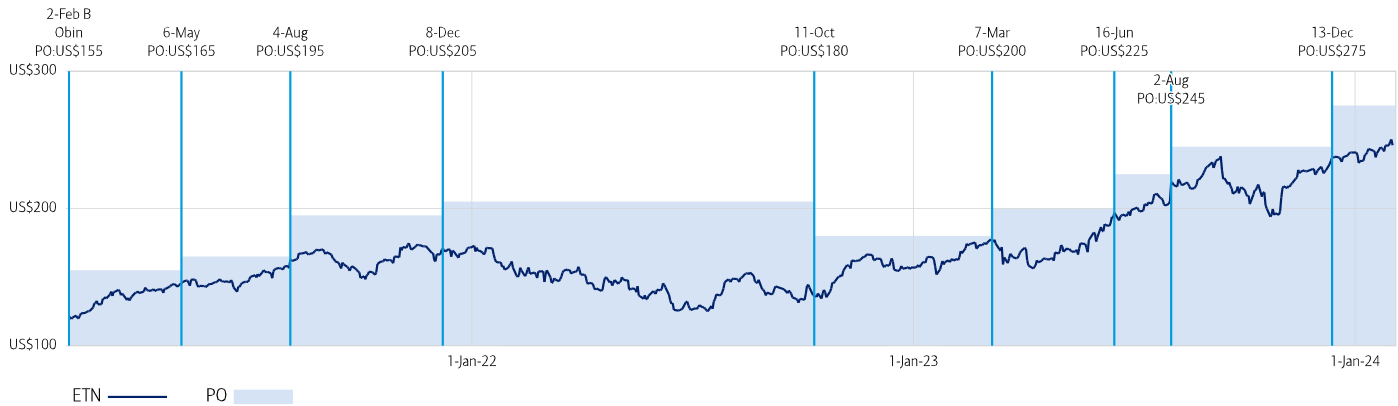
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Disclosures

Important Disclosures

Eaton Corp PLC (ETN) Price Chart



B: Buy, N: Neutral, U: Underperform, PO: Price Objective, NA: No longer valid, NR: No Rating

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: Electrical Equipment Group (as of 31 Dec 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships ^{R1}	Count	Percent
Buy	14	53.85%	Buy	10	71.43%
Hold	6	23.08%	Hold	3	50.00%
Sell	6	23.08%	Sell	1	16.67%

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}
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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