

## Wabtec Corp.

# Raise to Buy on backlog actualization into Sales, and International growth; PO \$150

Rating Change: BUY | PO: 150.00 USD | Price: 128.02 USD

## Leading rail service/equipment provider, PO \$150

We upgrade Wabtec's shares to Buy (from Neutral) and increase our PO to \$150 (from \$128) based on 22x our 2024E EPS est (from 19x), just above the top of its 15x-21x range as we factor in its rising International flow-through to its multiple, as well as our increased confidence in its ability to actualize its ramping backlog into Sales. We raise our 2024E and 2025E EPS estimates 1% and 2%, to \$6.80 and \$7.65, from \$6.75 and \$7.50, respectively, putting us further above consensus. Wabtec is a leading locomotive manufacturer, freight rail digital service provider, and transit equipment provider. It manufactured 50% of the North American installed base, with 80% of the Class I locomotive fleet with some form of Wabtec component or technology. Its locomotives operate at 5% better fuel efficiency vs its peer on a tier-for-tier basis. Its ramping 12-month backlog of \$7 billion is up 13% year-year, indicating potential upside to its mid-single digit top-line growth target with its Integration 2.0 plan leading to margin gains.

## International market a key growth opportunity

International sales have been working to offset muted North American sales as Class I carriers parked locomotives and increased turns. Wabtec highlighted that its overseas installed base continues to grow at a 4.5% CAGR, which will lead to increased recurring revenues as Wabtec cross-sells components and software to its existing customers. In 2023, approximately 40% of Wabtec's Freight business and 85% of its Transit business are non-North America based. We target 2024 net sales to increase 5% year-year, in-line with Wabtec's mid-single-digit top-line CAGR target yet see upside potential to our estimates given its ramping 12-month backlog of \$7 billion, which is up 13% year-year.

## Integration 2.0 to lead to increased margins

We target 2024 EBIT margins to improve 70 bps yr-yr in to 17.8%. The gains will be aided by cost cutting moves in Transit as it focuses on more profitable business. It aims to cull \$75-\$95 mil in costs on its Integration 2.0 plan through consolidating its capacity, streamlining its manufacturing and simplification of its systems, the bulk of its savings targeted for '24. We target Freight margins to improve 40 bps yr-yr to 21%, Transit margins to improve 50 bps yr-yr to 13%, and for corporate loss to decline 25% y-y.

Estimates (Dec) (US\$)	2021A	2022A	2023E	2024E	2025E
EPS	4.27	4.87	5.97	6.80	7.65
GAAP EPS	2.97	3.47	4.60	5.51	6.32
EPS Change (YoY)	13.0%	14.1%	22.6%	13.9%	12.5%
Consensus EPS (Bloomberg)			5.97	6.73	7.52
DPS	0.48	0.60	0.68	0.80	0.92
Valuation (Dec)					
P/E	30.0x	26.3x	21.4x	18.8x	16.7x
GAAP P/E	43.1x	36.9x	27.8x	23.2x	20.3x
Dividend Yield	0.4%	0.5%	0.5%	0.6%	0.7%
EV / EBITDA*	23.0x	21.3x	17.0x	14.6x	13.3x
Free Cash Flow Yield*	4.1%	3.8%	3.2%	6.6%	6.5%

\* For full definitions of *IQmethod*<sup>SM</sup> measures, see page 6.

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Timestamp: 16 January 2024 06:00AM EST

16 January 2024

### Equity

#### Key Changes

(US\$)	Previous	Current
Inv. Opinion	B-2-7	B-1-7
Inv. Rating	NEUTRAL	BUY
Price Obj.	128.00	150.00
2025E Rev (m)	10,533.0	10,595.0
2024E EPS	6.75	6.80
2025E EPS	7.50	7.65

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### Stock Data

Price	128.02 USD
Price Objective	150.00 USD
Date Established	16-Jan-2024
Investment Opinion	B-1-7
52-Week Range	91.89 USD - 128.48 USD
Mrkt Val (mn) / Shares Out (mn)	23,120 USD / 180.6
Free Float	99.0%
Average Daily Value (mn)	113.73 USD
BofA Ticker / Exchange	WAB / NYS
Bloomberg / Reuters	WAB US / WAB.N
ROE (2023E)	10.5%
Net Dbt to Eqty (Dec-2022A)	34.1%
ESGMeter <sup>TM</sup>	Medium

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".

# iQprofile<sup>SM</sup> Wabtec Corp.

## iQmethod<sup>SM</sup> – Bus Performance\*

(US\$ Millions)	2021A	2022A	2023E	2024E	2025E
Return on Capital Employed	4.5%	5.2%	6.5%	7.2%	7.8%
Return on Equity	7.9%	8.8%	10.5%	11.4%	12.1%
Operating Margin	12.2%	12.7%	14.1%	15.2%	15.6%
Free Cash Flow	943	889	747	1,535	1,510

## iQmethod<sup>SM</sup> – Quality of Earnings\*

(US\$ Millions)	2021A	2022A	2023E	2024E	2025E
Cash Realization Ratio	1.3x	1.2x	0.8x	1.5x	1.4x
Asset Replacement Ratio	0.6x	0.8x	0.7x	0.7x	0.6x
Tax Rate	25.9%	24.9%	25.2%	25.0%	25.0%
Net Debt-to-Equity Ratio	35.0%	34.1%	33.7%	27.7%	20.3%
Interest Cover	5.4x	5.7x	6.1x	6.9x	8.0x

## Income Statement Data (Dec)

(US\$ Millions)	2021A	2022A	2023E	2024E	2025E
Sales	7,822	8,362	9,604	10,058	10,595
% Change	3.5%	6.9%	14.8%	4.7%	5.3%
Gross Profit	2,422	2,583	2,984	3,131	3,314
% Change	11.0%	6.6%	15.5%	4.9%	5.8%
EBITDA	1,185	1,282	1,604	1,865	2,045
% Change	-7.9%	8.2%	25.1%	16.2%	9.7%
Net Interest & Other Income	140	134	101	104	120
<b>Net Income (Adjusted)</b>	<b>803</b>	<b>890</b>	<b>1,070</b>	<b>1,187</b>	<b>1,297</b>
<b>% Change</b>	<b>11.6%</b>	<b>10.8%</b>	<b>20.3%</b>	<b>10.9%</b>	<b>9.3%</b>

## Free Cash Flow Data (Dec)

(US\$ Millions)	2021A	2022A	2023E	2024E	2025E
Net Income from Cont Operations (GAAP)	810	899	1,080	1,195	1,296
Depreciation & Amortization	491	479	521	635	696
Change in Working Capital	(63)	(109)	(458)	170	(2)
Deferred Taxation Charge	38	(17)	(39)	0	0
Other Adjustments, Net	(203)	(214)	(208)	(233)	(225)
Capital Expenditure	(130)	(149)	(149)	(233)	(255)
<b>Free Cash Flow</b>	<b>943</b>	<b>889</b>	<b>747</b>	<b>1,535</b>	<b>1,510</b>
<b>% Change</b>	<b>45.7%</b>	<b>-5.7%</b>	<b>-16.0%</b>	<b>105.4%</b>	<b>-1.6%</b>
Share / Issue Repurchase	(300)	(473)	(418)	(750)	(600)
Cost of Dividends Paid	(92)	(111)	(122)	(140)	(156)
Change in Debt	(161)	(30)	(51)	(375)	(250)

## Balance Sheet Data (Dec)

(US\$ Millions)	2021A	2022A	2023E	2024E	2025E
Cash & Equivalents	473	541	450	660	1,104
Trade Receivables	1,477	1,519	1,733	1,889	1,989
Other Current Assets	1,882	2,267	2,533	2,553	2,573
Property, Plant & Equipment	1,497	1,429	1,266	924	542
Other Non-Current Assets	13,125	12,760	12,765	12,839	12,912
<b>Total Assets</b>	<b>18,454</b>	<b>18,516</b>	<b>18,747</b>	<b>18,864</b>	<b>19,121</b>
Short-Term Debt	2	251	759	759	759
Other Current Liabilities	2,908	3,216	3,162	3,509	3,627
Long-Term Debt	4,056	3,751	3,188	2,813	2,563
Other Non-Current Liabilities	1,249	1,151	1,254	1,254	1,254
<b>Total Liabilities</b>	<b>8,215</b>	<b>8,369</b>	<b>8,363</b>	<b>8,335</b>	<b>8,203</b>
<b>Total Equity</b>	<b>10,239</b>	<b>10,147</b>	<b>10,383</b>	<b>10,529</b>	<b>10,918</b>
<b>Total Equity &amp; Liabilities</b>	<b>18,454</b>	<b>18,516</b>	<b>18,747</b>	<b>18,864</b>	<b>19,121</b>

\* For full definitions of iQmethod<sup>SM</sup> measures, see page 6.

## Company Sector

Rail Equipment

## Company Description

Wabtec is one of the world's largest providers of technology-based products and services for the global freight rail and passenger transit industries. Its products are on most locomotives, freight cars, & transit cars and buses around the world. Wabtec has ops in more than 50 countries & its products are used in more than 100 countries. Nearly 60% of revs are from customers outside the U.S. Headquartered in Pittsburgh, Wabtec's roots trace back to the Westinghouse Air Brake Co., founded in 1896.

## Investment Rationale

We rate Wabtec Buy. We believe its scaling International installed base, strong backlog conversion, as well as rebounding rail volumes will more than offset the lagging effects of the tail rollout of Precision Scheduled Railroading (PSR) implementation. We are also positive on its Integration 2.0 efforts as it pulls costs from its operating model to improve its Transit margins.

## Stock Data

Average Daily Volume 888,392

## Quarterly Earnings Estimates

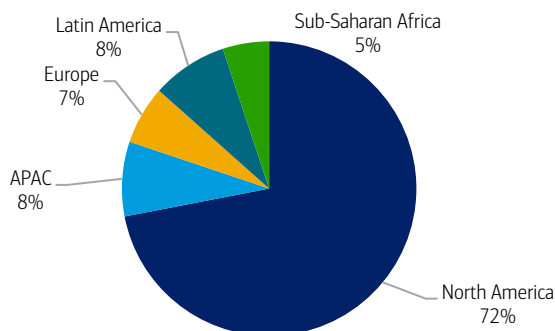
	2022	2023
Q1	1.13A	1.28A
Q2	1.23A	1.42A
Q3	1.22A	1.70A
Q4	1.30A	1.58E

## Telematics provide additional growth upside

Wabtec's entry in December into the \$4-\$8 billion Telematics market, which involves the tracking of location and conditions of railcars, could provide additional growth upside. Improved safety and reliability are key drivers for rail carrier service metrics, which leads to share gains over truck. As Wabtec begins providing real-time data to railcar owners through leveraging sensors and gateways, we expect end user uptake to potentially drive its Freight Digital and Services revenues. We target Freight Digital revenues to grow 10% year-year and Services revenues to grow 4% year-year in 2024.

### Exhibit 1: Wabtec's Locomotive Installed Base

Wabtec's installed base of 23k locomotive is 72% in North America.

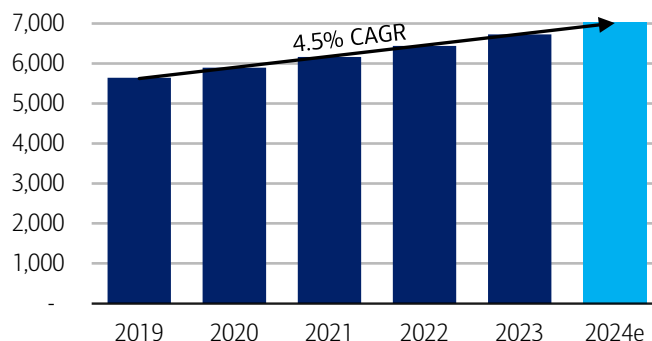


Source: Company reports.

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### Exhibit 2: Wabtec International Installed Base

International locomotive installed base has been growing at a 4.5% CAGR.

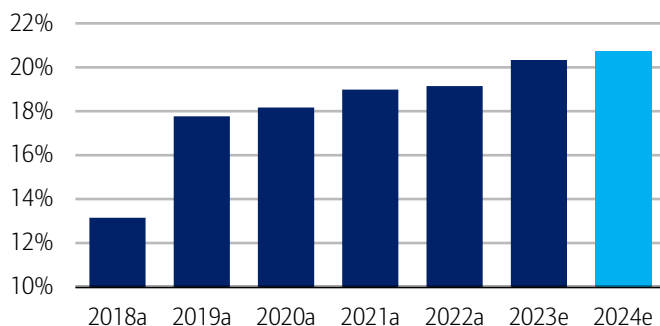


Source: BofA Global Research estimates and company reports

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### Exhibit 3: Wabtec Freight Margins

We target 21% Freight margins in 2024, a 40 bps improvement y-y.

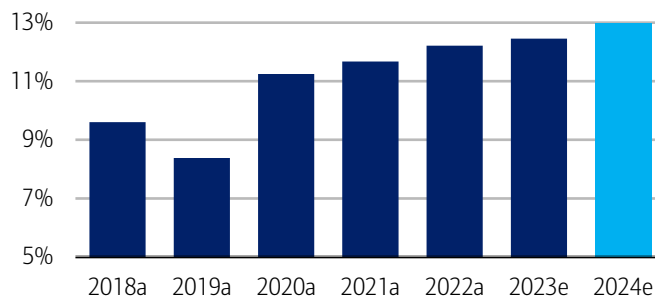


Source: BofA Global Research estimates and company reports.

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### Exhibit 4: Wabtec Transit Margins

We target 13.0% Transit margins, a 50 bps improvement year-year.

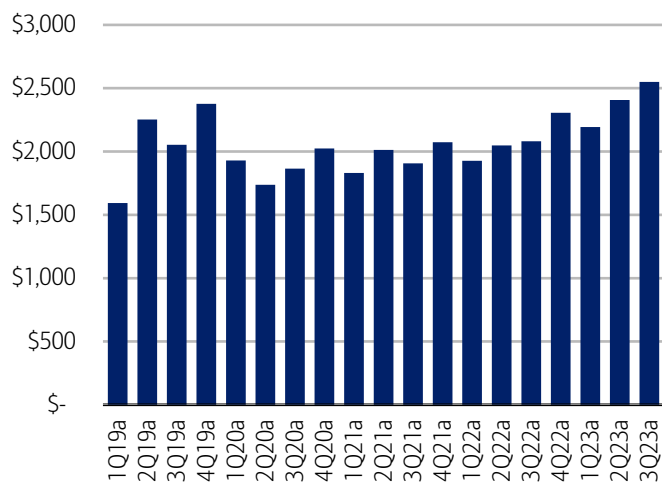


Source: BofA Global Research and company reports.

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**Exhibit 5: Wabtec Sales**

Wabtec 3Q23 net sales were \$2.55 billion, up 22.5% year-year

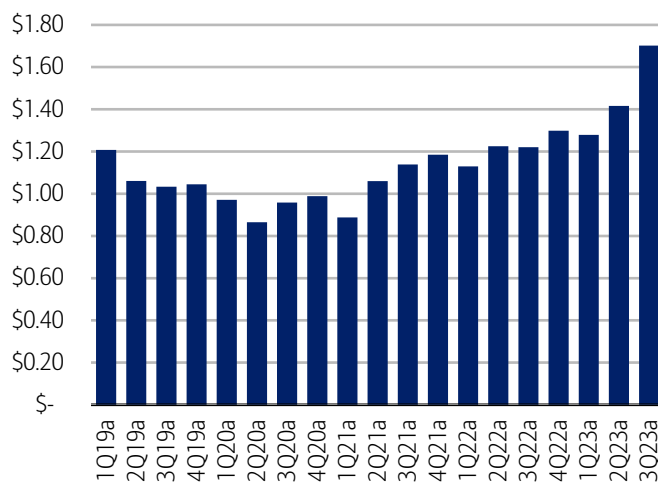


Source: BofA Global Research estimates and company reports.

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**Exhibit 6: Wabtec Adj Earnings per Share**

Wabtec 3Q23 adj EPS was \$1.70, up 40% year-year.



Source: BofA Global Research estimates and company reports.

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## Price objective basis & risk

### Wabtec Corp. (WAB)

Our \$150 PO is based on an 22x target P/E multiple on our 2024e EPS, above its 9-year historical 15x-21x range on forward earnings (which was normalized, and historically on cash EPS, though before its Feb 2019 GE-T acquisition would have been fairly similar) as we assign a premium to its target multiple given increased confidence on its actualization of backlog and International sales growth.

Downside risks to our PO are a quicker decline in rail volumes/economic activity, delayed replacement capex from the railroads, shrinking government budgets for Transit projects or increasing austerity measures, increased warranty claims on its equipment, and improved parts that delays replacement of equipment.

Upside risks to our PO are larger than expected synergy gains from its GE-T merger, a rapid rebound in rail carloadings, and accelerated rail capex spend on technology and upgrade investments from positive train control. Additionally, increased government expenditures for eco-friendly rail projects could provide upside potential.

## Analyst Certification

I, Ken Hoexter, 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 - Transportation Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
<b>BUY</b>				
	Canadian Pacific Kansas City Ltd	CP	CP US	Ken Hoexter
	CSX Corporation	CSX	CSX US	Ken Hoexter
	FedEx Corp.	FDX	FDX US	Ken Hoexter
	J.B. Hunt Transport Services	JBHT	JBHT US	Ken Hoexter
	Kirby Corp	KEX	KEX US	Ken Hoexter
	Knight-Swift Transportation Holdings Inc	KNX	KNX US	Ken Hoexter
	Norfolk Southern	NSC	NSC US	Ken Hoexter
	Old Dominion Freight Line	ODFL	ODFL US	Ken Hoexter
	RXO, Inc.	RXO	RXO US	Ken Hoexter
	Saia Inc.	SAIA	SAIA US	Ken Hoexter
	Union Pacific	UNP	UNP US	Ken Hoexter
	Wabtec Corp.	WAB	WAB US	Ken Hoexter
	XPO, Inc.	XPO	XPO US	Ken Hoexter
<b>NEUTRAL</b>				
	Canadian National	CNI	CNI US	Ken Hoexter
	Schneider National	SNDR	SNDR US	Ken Hoexter
	Scorpio Tankers Inc.	STNG	STNG US	Ken Hoexter
	Teekay Tankers Limited	TNK	TNK US	Ken Hoexter
	TFI International	TFII	TFII US	Ken Hoexter
	TFI International	YTFII	TFII CN	Ken Hoexter
	UPS	UPS	UPS US	Ken Hoexter
<b>UNDERPERFORM</b>				
	ArcBest Corporation	ARCB	ARCB US	Ken Hoexter
	C.H. Robinson	CHRW	CHRW US	Ken Hoexter
	The Greenbrier Companies	GBX	GBX US	Ken Hoexter
	Werner Enterprises	WERN	WERN US	Ken Hoexter
	World Kinect	WKC	WKC US	Ken Hoexter



## iQmethod<sup>SM</sup> Measures Definitions

### Business Performance

Return On Capital Employed

Return On Equity

Operating Margin

Earnings Growth

Free Cash Flow

### 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

### Denominator

Total Assets – Current Liabilities + ST Debt + Accumulated Goodwill

Amortization

Shareholders' Equity

Sales

N/A

N/A

### Quality of Earnings

Cash Realization Ratio

Asset Replacement Ratio

Tax Rate

Net Debt-To-Equity Ratio

Interest Cover

### Numerator

Cash Flow From Operations

Capex

Tax Charge

Net Debt = Total Debt – Cash &amp; Equivalents

EBIT

### Denominator

Net Income

Depreciation

Pre-Tax Income

Total Equity

Interest Expense

### Valuation Toolkit

Price / Earnings Ratio

Price / Book Value

Dividend Yield

Free Cash Flow Yield

Enterprise Value / Sales

### 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

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

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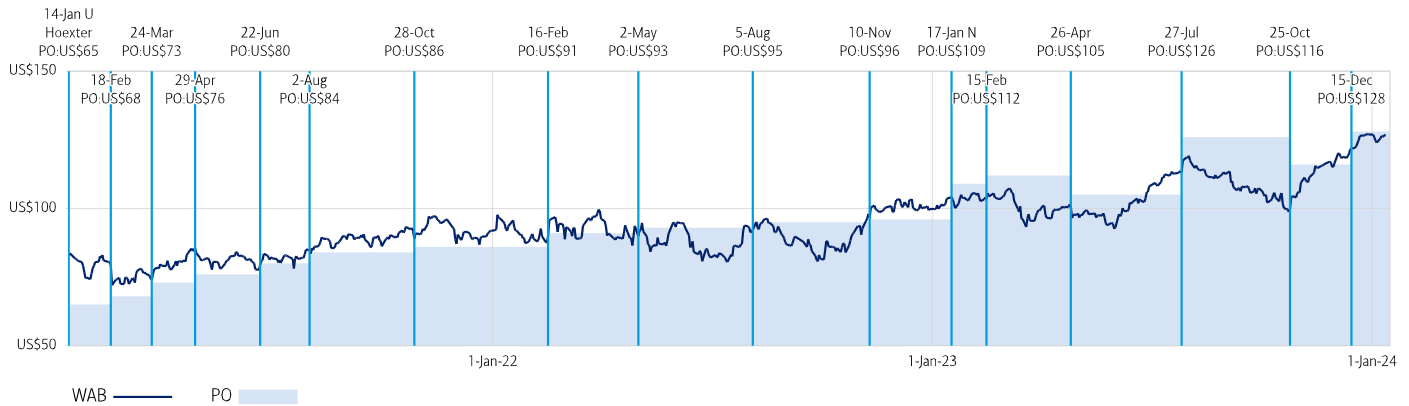
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## Important Disclosures

### Wabtec (WAB) 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: Transport/Infrastructure Group (as of 31 Dec 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships <sup>R1</sup>	Count	Percent
Buy	67	50.38%	Buy	44	65.67%
Hold	31	23.31%	Hold	13	41.94%
Sell	35	26.32%	Sell	17	48.57%

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

Coverage Universe	Count	Percent	Inv. Banking Relationships <sup>R1</sup>	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%

<sup>R1</sup> 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 <sup>R2</sup>
Buy	≥ 10%	≤ 70%
Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

<sup>R2</sup> 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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