A Closer Look: Eaton’s 4Q With Partial Cooper Numbers

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Industry analysts, distributors and manufacturers were eagerly waiting Eaton’s fourth quarter reporting recently as the diversified international manufacturer showed the partial results of its $13.2 billion acquisition of Cooper Industries [1].

Eaton CEO, Alexander M. “Sandy” Cutler, had warned analysts last quarter that the reporting would be “complex” because the results would show only one month’s (December) numbers of Cooper on its fourth quarter report. This was due to the acquisition, announced last spring, not being completed until Nov. 30th of 2012 – after months of approvals from regulating agencies around the world.

Despite this, the recently announced numbers clearly show that Eaton is far ahead in completing its synergistic capabilities within the two companies, and that the acquisition, clearly, is already paying off for Eaton.

In speaking on a conference call about Eaton’s fourth quarter, Cutler, according to a transcript from www.seekingalpha.com [2], said: “The Cooper acquisition is everything we expect it to be and more… We’re really pleased that we’re ahead of schedule in terms of our synergy activity and our financing plans.”

Cutler also noted that after the Cooper acquisition, Eaton “would be largely out of the M&A market for a couple of years.” This is noteworthy, considering Eaton has been extremely active in the acquisition market for some time.

Segment, Global Impacts

Eaton is an acknowledged leader or, in some cases, second in all the markets it serves from hydraulics, power management, electrical, truck, aerospace, and

automobile segments.

Its huge purchase of Cooper Industries caused shock in the distribution marketplace as Eaton, well known for its truck and automotive and hydraulics segments, greatly expanded its electrical product offerings.

Although Cooper and Eaton often sold to very similar customer segments, there was little actual overlap in products. Now, Eaton becomes a big player in electrical; in fact, more than 60 percent of Eaton’s sales now come from the electrical side of the business.

Cutler said half of Eaton’s total sales will be in the U.S., while the remainder will come from outside the country. About 18 percent of its sales will be in Europe, about 3 percent in the Middle-East and Africa, about 14 percent in Latin America and Canada, and about 15 percent in the Asia Pacific region.

Cooper’s sales were largely in the U.S., which brought the total revenues split between U.S. and abroad. Cooper is also heavily involved in the residential and non-residential construction markets as well as industrial end markets and utility end markets. Combining Eaton’s power management business with Cooper’s electrical offerings will mean customers in areas like data centers and utilities will have an easier time for one-stop shopping.

Effects on the Numbers

Despite an overall strong start in the fourth, the company’s hydraulic segment did not do as well this quarter.

Third quarter hydraulic sales were down four percent, and in the fourth quarter, that segment was down another 11 percent. Cutler sees a weak picture for hydraulics this year as well. While those results seemed to have caught some analysts by surprise, Eaton’s stock still rose sharply after its earnings report was released. In fact, stocks recently reached a 52-week high.

Relative to these dips in the hydraulic segment, Cutler partially blamed the construction markets, citing its “big exposure” for the company. Also: “While there has been some weakness on the distributor side, the big weakness has been on the OEM side, most particularly in the construction area then followed by agriculture,” he said. “The one good piece of news here is that China, which you recall we have a fairly large exposure to and has been quite weak here for a couple of years. We are beginning to see a better tone in January. I would not yet announce this as a breakout, but it's been the first indication of better tone that we have seen in that better part of the year in some months.”

Cutler was also asked about the effect of Superstorm Sandy on its businesses.

“As you can appreciate, it's hard to estimate because some of these orders come through our distribution partners and some of them we have orders come direct,” said Cutler, according to the transcript. “But our best estimate is the fourth quarter

was somewhere in the order of about $25 million of orders. We think that's likely to repeat again in the first quarter because not all of the repairs and services were able to be completed in the fourth quarter."

Eaton also took steps to right-size itself in the past year, as it closed two plants and downsized two others.

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