BEHIND THE NUMBERS
EARNINGS QUALITY & DIVIDEND SUSTAINABILITY RESEARCH

BTN Research

Jeff Middleswart
jmiddleswart@btnresearch.com

Bill Whiteside, CFA
bwhiteside@btnresearch.com

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# Ball Corp. (BLL) EQ Update 12/19 Qtr.

| Current EQ Rating* | Previous EQ Rating |
|---|---|
| 3+ | 2- |

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|---|
| 6- "Exceptionally Strong" |
| 5- "Strong" |
| 4- "Acceptable" |
| 3- "Minor Concern" |
| 2- "Weak" |
| 1- "Strong Concerns" |

Note that a "+" sign indicates the earnings quality improved in the most recent quarter while a "–" sign indicates deterioration

*For an explanation of the EQ Review Rating scale, please refer to the end of this report

**We are raising our earnings quality rating to 3+ (Minor Concern) from 2- (Weak) with the improvement largely reflecting the deceleration of the pace of receivables factoring.**

- BLL's pace of factored receivables is still outrunning sales growth. Receivables sold but outstanding on a days of sales basis rose by 6 days versus the year-ago fourth quarter. However, this compares to a mid-teens YOY growth rate at the end of 2018. Meanwhile, receivables still on the balance sheet declined by almost 5 days on a days of sales basis. The resulting 1-day increase in adjusted receivable DSOs is not overly alarming, although this measure is likely distorted by the October 2019 disposal of the Argentina Aerosol business and the September 2019 sale of the China Beverage Packaging business. In fact, the company stated in the liquidity section of its 10-K that "Excluding the impact of the sale of the U.S. steel food and steel aerosol packaging business in 2018 and the sale of the China beverage packaging and Argentina steel aerosol businesses in 2019, our working capital movements reflect a decrease of days sales outstanding from 42 days in 2018 to 39 days in 2019 and an increase in days payable outstanding from 112 days in 2018 to 121 days in 2019. We will continue to monitor these trends going forward.

- Unbilled receivable days of sales rose by 3 in the 12/19 quarter to almost 19. As we have noted before, this could be influenced by rising aerospace sales, but as with the previous quarter, unbilled receivables on a days of aerospace sales basis rose as well. This continues to erode the quality of reported revenue, in our opinion.

- The loss of a customer in its Saudi Arabia beverage packaging business led to a $64 million write-down of PP&E and goodwill associated with the segment. The company also warned in the 10-K that beginning in 2020, it will change how it reports its AMEA and Asia Pacific beverage packaging segments which had goodwill balances of $102 million and $27 million, respectively. This will result in a new segment to which $62 million of goodwill will be allocated. The disclosure warned that "*Based on the information available at this time, it is reasonably possible that the company will be required to record a non-cash impairment charge for some or all of the goodwill associated with this reporting unit in the first quarter of 2020, as the carrying amount of this reporting unit may exceed its fair value."*

- Pension costs declined by 5.6 cps in the quarter due to a $22 million settlement gain last year, but this was adjusted out of non-GAAP figures.

# Explanation of EQ Rating Scale

| | |
|---|---|
| 6- "Exceptionally Strong" | Indicates uncommonly conservative accounting policies to the point that revenue and earnings are essentially understated relative to the company's peers. Higher possibility of reporting positive earnings surprises |
| 5- "Strong" | Indicates the company has no areas of concern with its reported results and we see very little risk of the company disappointing due to recent results being overstated from aggressive reporting in recent periods. |
| 4- "Acceptable" | Indicates the company may have exhibited a minor "red flag", but the severity of the issue is not yet a concern. Minimal risk of an earnings disappointment resulting from previous earnings or cash flow overstatement |
| 3- "Minor Concern" | Indicates the company has exhibited either a larger number of or more serious warning signs than companies receiving a 4. The likelihood of an immediate earnings or cash flow disappointment is not considered to be high, but the signs mentioned deserve a higher degree of attention in the future. |
| 2- "Weak" | Indicates the company's recently reported results have benefitted materially from aggressive accounting. Follow up work should be performed to determine the nature and extent of the problem. There is a possibility that upcoming results could disappoint as the impact of unsustainable benefits disappears. |
| 1- "Strong Concerns" | Indicates that the company's recent results are significantly overstated and that we view a disappointment in upcoming quarters is highly likely. |

In addition to the numerical rating, the EQ Review Rating may also include either a minus or plus sign. A minus sign indicates that our analysis shows the overall earnings quality of the company has worsened since the last review and there is a possibility the numerical rating will fall should the problem continue into the next quarter. Likewise, a positive sign indicates that the overall earnings quality is improving, and the company may see an upgrade in its numerical rating should the trend continue.

**Key Points to Understand About the EQ Score**

**The EQ Review Rating is much more than a blind, quantitative scoring method**. While we utilize proprietary adjustments, ratios, and methods developed over decades of earnings quality analysis, the foundation of all of our analysis is reading recent SEC filings, press releases, conference call transcripts and in some cases, conversations with managements.

**The EQ Review Rating is not comparable to a traditional buy/sell rating**. The Rating is intended to specifically convey the extent to which reported earnings may be over/understated. Fundamental factors such as forecasts for future growth, increasing competition, and valuation are not reflected in the rating. Therefore, a high score does not in itself indicate a company is a buy but rather indicates that recent results are a good indication of the underlying earnings and cash generation capacity of the company. A low score (1-2) will likely result in us performing a more thorough review of fundamental factors to determine if the company warrants a full-blown sell recommendation.

# Disclosure

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