

Initiated 2026-09-23 · Price \$107.85 (as of 2026-09-22, stockanalysis.com) · Mkt cap \$25.2bn · Industrials / Specialty Industrial Machinery (water technology) · Model: verified

Rating: Hold — Conviction: Medium

Xylem is the first name in this rotation whose base case lands on the market price rather than far below it — \$107.88 against \$107.85. That is not a coincidence to be talked around: after a 24.5% twelve-month fall to within 2% of its 52-week low, the stock is priced for what the business is currently doing. What makes it interesting rather than dull is the spread around that point — bull +62%, bear -47% — and the fact that the spread turns on one observable thing: whether Q2's 41% organic order growth converts into revenue. It has not yet; revenue grew 1%.

MODEL VALUE RANGE VS PRICE



Business overview

Xylem sells the pumps, treatment systems, meters and services that move and clean water, across four segments: Water Infrastructure (utility transport and treatment), Applied Water (commercial, residential and industrial pumps), Measurement & Control Solutions (smart meters and network intelligence), and Water Solutions & Services (outsourced treatment and operations, largely the 2023 Evoqua acquisition). Roughly half of revenue is non-US. Three things drive earnings: utility and municipal capital programmes, funded by rate cases and bond issuance and therefore slow; the productivity and price programme, currently doing all the work; and the mix shift toward recurring services.

Bull case

- Orders inflected violently in Q2** — \$3.1bn, up 42% reported and 41% organic, with Water Solutions & Services orders up 62% organic over six months, against 1% revenue growth. That gap is backlog. Plays out if utilities and industrial customers fund on normal timelines. *Model: rev_growth*
- Margin is delivering while revenue stalls** — adjusted EBITDA margin 23.3%, up 150bp, and adjusted EPS guidance *raised* to \$5.55–5.70 in the same release that cut revenue guidance. Plays out if productivity and price hold as volume returns. *Model: ebitda_margin*
- The multiple has already done the work** — 13.63x EV/EBITDA against a 17.99–27.80x five-year band and Veralto at 17.86x; 18.3x forward earnings against 31.7–56.1x trailing at the last five year-ends. Plays out if 13.6x proves the floor. *Model: exit_ev_ebitda*
- Water is a secular, non-discretionary, increasingly industrial end market** — network replacement and scarcity, now joined by semiconductor, power-generation and data-centre water intensity, which management named directly. *Model: terminal_growth, rev_growth*

Bear case

1. **Revenue has stopped growing** — 1% organic in Q2 and a guidance cut to +2–3% organic on electric metering delays. An order book is a promise; this one converts through municipal procurement, and receivables and inventory are already building ahead of it (NWC 20.6% of revenue against 19.1% at FY2025). *Model: rev_growth, nwc_pct_rev*
2. **The returns are mediocre for the multiple** — ROIC 8.99% against Veralto's 23.50%, the legacy of what was paid for Evoqua. The current margin story is productivity and price, not franchise economics, and productivity programmes finish. *Model: ebitda_margin, da_pct_rev*
3. **The customer cannot move fast** — utility capex is set by rate cases and municipal budgets, so even a genuine demand surge converts on a multi-year clock, and a rate shock slows the bond issuance that funds it. *Model: rev_growth, terminal_growth*
4. **The tax rate stepped up** — 26.0% for the six months to June 2026 against a 16–20% five-year history. If permanent, that is a straight reduction in free cash flow per dollar of EBIT with no offset. *Model: tax_rate*

Valuation & balance sheet

Metric (definition)	Current	Own history (range or 5y avg)	Peers	Source, as-of
EV/EBITDA (EV \$26.96bn / TTM EBITDA \$1.98bn)	13.63x	27.80x, 23.79x, 25.19x, 17.99x, 18.11x at FY2021–FY2025 year-ends	VLTO 17.86x	stockanalysis.com, 2026-09-23
Forward P/E	18.34x	trailing P/E 31.7–56.1x at the last five year-ends	VLTO 21.22x	stockanalysis.com, 2026-09-23
FCF yield (TTM FCF \$958mm / market cap)	3.8%	1.5–3.3% (P/FCF 29.9–65.5x, FY2021–FY2025)	VLTO 4.5%	stockanalysis.com, 2026-09-23
ROIC	8.99%	—	VLTO 23.50%	stockanalysis.com, 2026-09-23

Model-implied value range (from `model-summary.json` ; generic module, Gordon-growth DCF and exit-EV/EBITDA DCF, midpoints): Bear \$57.45 · Base \$107.88 · Bull \$174.89 per share, i.e. implied returns of –47% / **+0.0%** / +62% vs \$107.85. *These ranges show how the bull and bear drivers translate into value; they are not price targets.* The market is pricing the base case almost exactly — and note that the base case deliberately assumes the multiple stays at today's depressed 14x for five years rather than reverting, so none of the base value depends on a re-rating. The bull case is the order book converting into mid-to-high single-digit organic growth with margin reaching the high twenties; the bear is metering-style delays proving general and margin stalling once productivity is banked.

Why the spread is this wide on a boring industrial. The two methods agree closely (base \$95.42 Gordon, \$120.34 exit multiple), unlike the high-growth names in this rotation — the width comes from the drivers, not method disagreement. Revenue growth of 2–5% versus 2–9% and FY2030 margin of 20.8% versus 26.8% compound into a 3x value range. That is what one unresolved question — does the order book convert — looks like on an operationally levered business.

Balance sheet: net debt \$1,784mm, model net leverage 0.99x on FY0 EBITDA (1.44x on the company's trailing basis), turning to net cash by FY2028 in the base path; coverage 15.2x; liquidity \$1,276mm cash plus ~\$600mm undrawn revolver (estimated); nearest material maturity \$500mm of 3.250% notes on 2026-11-01, already earmarked for repayment from the 2026 offering; ratings n/a (unverified). Debt/equity has fallen from 0.85x to 0.21x since FY2021.

Model note: Built and verified — LibreOffice matched Python across all 3,188 formula cells. Two unverified inputs. (1) `market.diluted_shares` of 237.0mm is derived from Q2 net income of \$263mm over \$1.11 diluted EPS (adjusted figures give 236.3mm). (2) Four debt series totalling \$1,900mm are individually sourced, but the remaining ~\$1,160mm — principally the 2026 senior and "blue" notes, whose sizes and coupons were placeholder fields in the prospectus retrieved — sits in one estimated tranche, so the ladder beyond those four series should not be relied on. EBITDA is GAAP operating income plus D&A, i.e. after restructuring and special charges, so it runs 200–300bp below the company's adjusted margin. No assumptions lack a basis; no consistency CHECKs. Generator note (2026-09-24): in this module `share_change` , `capital_return_pct` and `cost_of_debt` move EPS and the net-cash path only, and `peer_pe` feeds a cross-check only; none changes the value range, so bull/bear tags no longer cite them. Scenario deltas were rebuilt after `multiple_pct` shocks were extended to the Gordon method (previously they moved only the exit-multiple half), and EPS now uses average diluted shares.

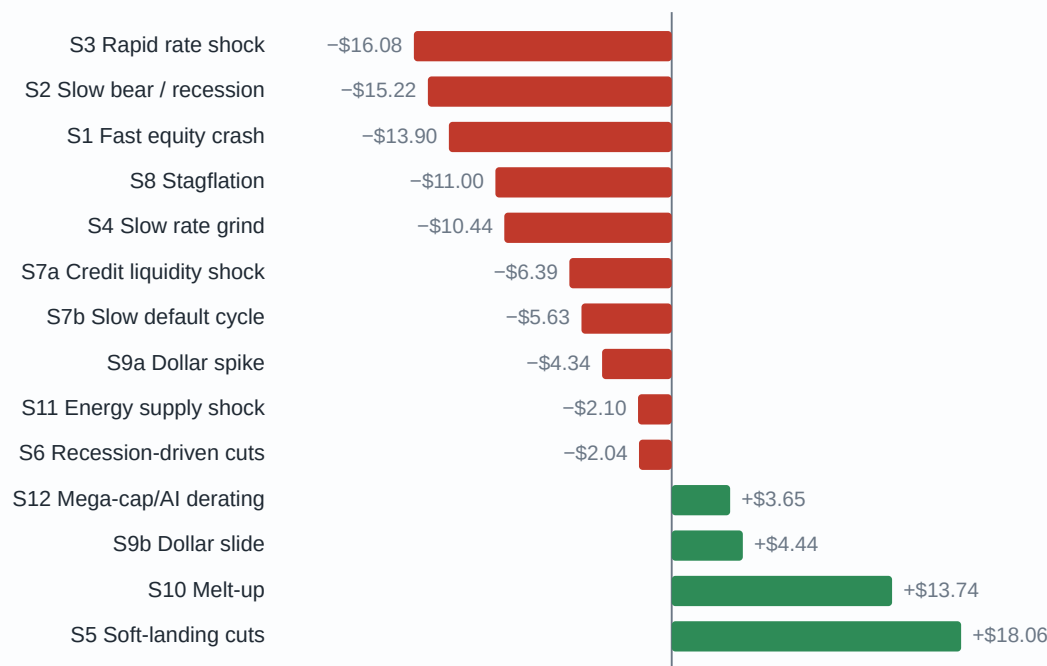
Scenario stress test

Reasoned from the bull/bear drivers above. The model column comes from the scenario overlays (Base case + shock).

Scenario	Effect	Mechanism	Magnitude	Model Δ value vs Base (\$/sh)
S1 Fast equity crash	–	Beta 1.00, already 30% below its high and 2% above its 52-week low: it participates, but there is far less air in this multiple than elsewhere in the rotation	Med	–\$13.90
S2 Slow bear / recession	–	About half of revenue is utility and municipal, the most recession-resistant industrial demand there is; Applied Water's building exposure and the industrial order book are not	Med	–\$15.22
S3 Rapid rate shock	–	Two channels, one name-specific: the usual discount-rate and multiple hit, plus a yield spike slowing the municipal bond issuance that funds the very projects in the order book	Med	–\$16.08
S4 Slow rate grind	–	Same channels, slower, with more time for the 1.950% and 2.250% green notes to reprice on refinancing	Low	–\$10.44
S5 Soft-landing cuts	+	The best row: cheaper municipal funding accelerates utility capital programmes while the discount rate and multiple improve — numerator and denominator move together	Med	+\$18.06
S6 Recession-driven cuts	±	Rate relief and cheaper municipal funding against a weakening industrial and commercial order book; they roughly cancel	Low	–\$2.04
S7a Credit liquidity shock	–	The company is insulated — investment grade, \$1,276mm cash, undrawn revolver, only \$500mm due before 2028; the transmission is customers' bond market access	Low	–\$6.39
S7b Slow default cycle	–	Weak: customers are utilities and municipalities, not levered corporates	Low	–\$5.63
S8 Stagflation	–	Price realisation is already a named margin driver so revenue is partly protected, but steel, copper and electronics costs move before contracted prices reset and municipal budgets are set in nominal terms	Low	–\$11.00
S9a Dollar spike	–	Roughly half of revenue is non-US, mostly European: one of the more material revenue shocks in this table	Low	–\$4.34
S9b Dollar slide	+	The same translation effect in reverse	Low	+\$4.44
S10 Melt-up	+	A laggard at its 52-week low gains less from a narrow momentum melt-up than the high-multiple names; most of the benefit comes through the discount rate	Med	+\$13.74
S11 Energy supply shock	±	Genuinely two-sided: an oil spike raises freight, resin and energy costs through a manufacturing footprint, but Xylem sells pumps and treatment into oil, gas, mining and power customers whose capital budgets expand when energy prices spike	Low	–\$2.10
S12 Mega-cap/AI derating	+	One of the few plausible net beneficiaries in this rotation: no AI premium to lose, and a rotation out of mega-cap growth into cheap quality industrials is exactly where a stock at 13.6x and the bottom of its own range gets re-rated	Low	+\$3.65

Currently active/on watch per the playbook: S3 partially active (price-level leg no longer met at 4.96% on 2026-09-21); S8, S10 and S11 on watch. S3 is this name's worst row and is the one closest to live; S11, on watch after the Riyadh/Yanbu escalation, is roughly neutral here rather than negative.

MODEL VALUE CHANGE VS BASE, BY SCENARIO



What would change the call

Upgrades if: FY2027 organic revenue guidance comes in at 5% or better, which would confirm order conversion and move the base path toward the bull path; or the price falls toward \$90 while orders and backlog hold, which would restore a margin of safety the base case currently lacks. **Downgrades if:** Q3 or Q4 organic order growth turns negative, giving back the Q2 surge; or adjusted EBITDA margin misses the 23.1% guidance floor, which would remove the one thing currently working.

Watch items

- **W1:** Order conversion — does the 41% organic order growth appear in revenue? Look for FY2027 organic revenue guidance $\geq 5\%$ — Q3 2026 release and FY2026 results — late October 2026 and February 2027 — *Model: rev_growth*
- **W2:** Electric metering delays — Measurement & Control Solutions organic revenue back to positive, having run 0% over six months — Q3 2026 release — late October 2026 — *Model: rev_growth*
- **W3:** Adjusted EBITDA margin against the 23.1–23.5% guide — Q3 and Q4 2026 releases — *Model: ebitda_margin*
- **W4:** Effective tax rate — whether the H1 2026 26.0% persists into FY2027 or reverts toward the high-teens history — FY2026 10-K — February 2027 — *Model: tax_rate*

Sources

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- Xylem reports second quarter 2026 results (2026-07-24) — <https://www.xylem.com/en-us/resources/press-releases/xylem-reports-second-quarter-2026-results/> — accessed 2026-09-23

- Xylem Form 424B5 prospectus supplement, 2026 senior notes and blue notes offering — <https://www.stocktitan.net/sec-filings/XYL/424b5-xylem-inc-prospectus-supplement-debt-securities-d783742f7b77.html> — accessed 2026-09-23
- SEC EDGAR XBRL companyconcept, CIK 0001524472 — Revenue, OperatingIncomeLoss, DepreciationDepletionAndAmortization, AccountsReceivableNetCurrent, InventoryNet, AccountsPayableCurrent, EffectiveIncomeTaxRateContinuingOperations — <https://data.sec.gov/api/xbrl/companyconcept/CIK0001524472/us-gaap/OperatingIncomeLoss.json> — accessed 2026-09-23
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- Portfolio command center macro log, 2026-09-21 — [logs/macro-2026-09.md](#) — accessed 2026-09-23

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