



# DowDuPont, Inc. (DWDP)

Updated July 30<sup>th</sup>, 2018 by Josh Arnold

## Key Metrics

<b>Current Price:</b> \$68	<b>5 Year CAGR Estimate:</b> 7.0%	<b>Volatility Percentile:</b> 49.1%
<b>Fair Value Price:</b> \$67	<b>5 Year Growth Estimate:</b> 5.0%	<b>Momentum Percentile:</b> 39.8%
<b>% Fair Value:</b> 102%	<b>5 Year Valuation Multiple Estimate:</b> -0.2%	<b>Valuation Percentile:</b> 57.0%
<b>Dividend Yield:</b> 2.2%	<b>5 Year Price Target:</b> \$86	<b>Total Return Percentile:</b> 40.1%

## Overview & Current Events

DowDuPont is the product of a late-2017 merger that brought together the former Dow Chemical Company and E.I. du Pont de Nemours & Company. Together, they are a diversified chemical production entity with ~\$85 billion in annual revenue and a \$159 billion market capitalization. In addition, the company is underway with plans to split DowDuPont into three separate entities by late-2019. The three separate businesses will be called Corteva Agriscience, Dow, and DuPont, which are currently the agriculture business, materials science segment and specialty products division, respectively.

DowDuPont's Q1 report was released on 5/3/2018 and results were strong. Growth from the materials science and specialty products businesses offset weakness in the agriculture business, leading to \$21.5 billion in sales during the quarter. Unfavorable weather conditions led to a 2% decline in volume for the agriculture business but the other two segments both saw double digit gains in the top line. DowDuPont also provided very impressive guidance for Q2, stating it expected EBITDA to rise in the mid-30% range for the agriculture business, mid-20% for specialty products and mid-teens for the materials science segment.

## Growth on a Per-Share Basis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
<b>EPS</b>	\$0.62	\$0.32	\$1.72	\$2.05	\$0.71	\$3.68	\$2.87	\$3.32	\$3.52	\$3.07	<b>\$3.85</b>	<b>\$4.90</b>
<b>DPS</b>	--	--	--	--	--	--	--	--	--	\$0.38	<b>\$1.52</b>	<b>\$2.00</b>

DowDuPont's earnings-per-share history shows a company that hasn't produced a lot of growth in recent years. The merger took place last year, bringing two chemical giants together and the synergies it created are helping to drive growth for this year. However, the planned separation of the current business into three has created a unique situation. We see DowDuPont producing 5% annual earnings-per-share growth combined over the next few years, although when the companies are split off, growth rates will surely differ between them. DowDuPont should achieve this growth primarily through sales increases, which we believe will be in the mid-single digits for the foreseeable future. Recent weakness in the agricultural business should be temporary as prices continue to increase and light volume was weather-related. The company's exposure to consumer markets like mobile devices is a long-term positive. In addition, the world's growing middle class should afford plenty of growth opportunities for DowDuPont, even after the spinoffs are complete. A lower tax rate will help boost earnings this year but moving forward, we think margins will remain steady given volatile input costs and that sales growth will be the primary lever it can pull to boost earnings.

## Valuation Analysis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	Now	2023
<b>Avg. P/E</b>	24.3	86.3	19.8	14.0	45.5	12.1	15.9	15.5	16.3	17.7	<b>17.8</b>	<b>17.5</b>
<b>Avg. Yld.</b>	--	--	--	--	--	--	--	--	--	0.7%	<b>2.2%</b>	<b>2.3%</b>

DowDuPont's shares look to be trading right at fair value today, which we estimate at 17.5 times earnings. We therefore see a very small 0.2% headwind to total returns moving forward from the valuation, essentially having no impact. When the three businesses are spun off, they will almost certainly have different valuations but for now, we see this stock as

*Disclosure: This analyst has no position in the security discussed in this article, and no plans to initiate one in the next 72 hours.*

fairly valued. The yield is just above two percent after a huge dividend increase this year and that is where we believe it will remain. DowDuPont is paying about 40% of its earnings to shareholders and we don't see that increasing materially.

## Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
GP/A	9.5%	12.8%	14.7%	14.9%	15.8%	16.6%	18.4%	22.6%	21.8%	15.2%	<b>15.0%</b>	<b>15.0%</b>
Debt/A	70%	68%	67%	66%	69%	60%	66%	61%	66%	47%	<b>47%</b>	<b>45%</b>
Int. Cov.	3.4	1.3	3.0	3.8	2.4	7.5	6.7	12.4	7.0	2.4	<b>2.5</b>	<b>2.8</b>
Payout	--	--	--	--	--	--	--	--	--	12%	<b>39%</b>	<b>41%</b>
Std. Dev.	40%	99%	30%	35%	26%	21%	22%	26%	22%	12%	<b>20%</b>	<b>28%</b>

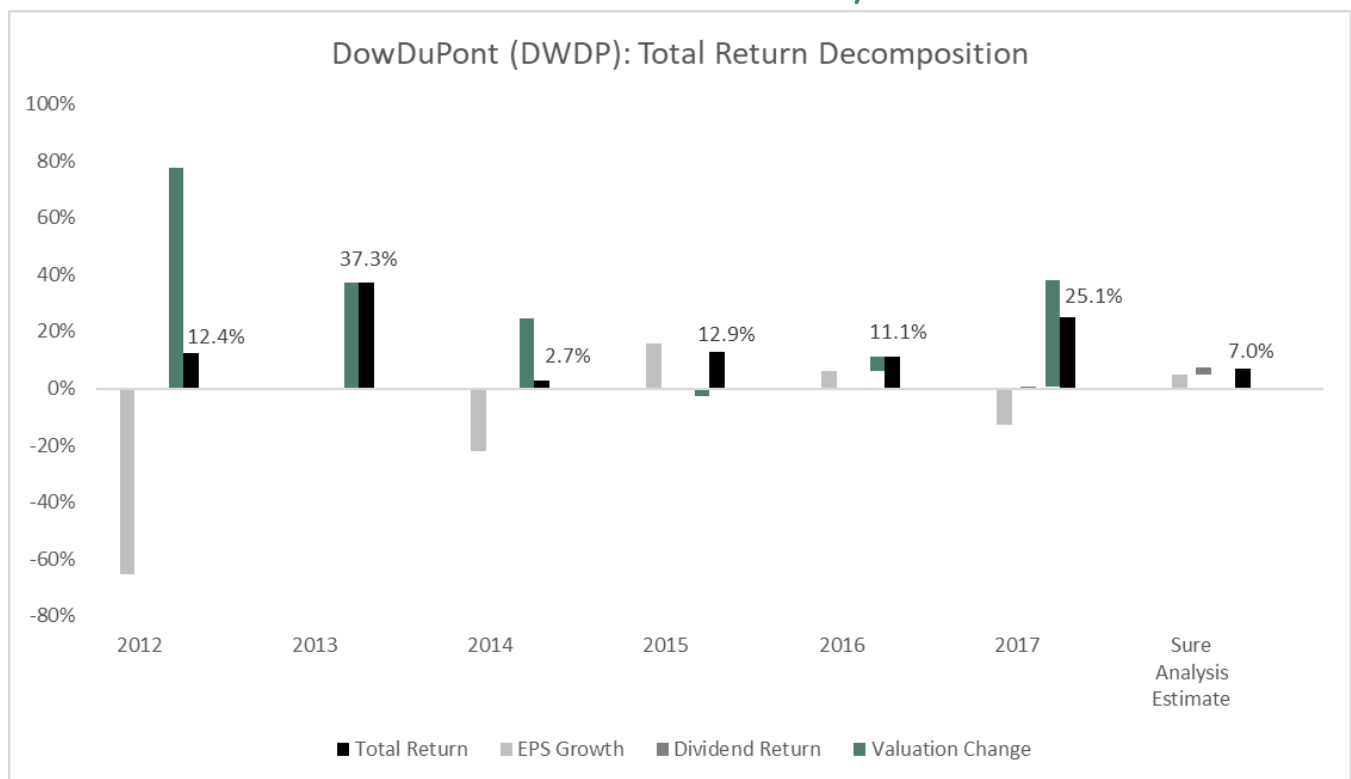
DowDuPont's quality metrics shifted significantly in some cases after the merger was completed. The company now has less than half of its assets financed by liabilities, so its balance sheet is much more robust. Interest coverage, however, has declined as the debt the company has is more expensive to service relative to operating income. Likewise, the combined margin profile of the companies has deteriorated somewhat, although we do not believe further deterioration is likely. The dividend is very safe at ~40% of earnings and we think the payout ratio will remain roughly where it is.

DowDuPont's competitive advantage is in its very long operating histories in the industries in which it operates. It has built tremendous expertise in a variety of specialty chemical businesses that have strong long-term outlooks. We think the spinoffs will be positive for shareholders of DowDuPont given the businesses will be pure-plays on their respective lines. Recessions aren't kind to chemical makers and DowDuPont is no exception, as earnings were cut in half in 2009.

## Final Thoughts & Recommendation

Overall, DowDuPont looks fairly valued here after years of nice returns. We are forecasting 7% total annual returns moving forward, consisting of the current 2.2% yield, 5% earnings-per-share growth and a 0.2% headwind from the valuation. The spinoffs of the three separate businesses should help unlock some value and we like the plan to do so. However, we rate DowDuPont as a hold today because of the full valuation and moderate growth prospects.

## Total Return Breakdown by Year



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