



DowDuPont, Inc. (DWDP)

Updated November 3rd, 2018 by Josh Arnold

Key Metrics

Current Price:	\$58	5 Year CAGR Estimate:	12.0%	Volatility Percentile:	42.0%
Fair Value Price:	\$72	5 Year Growth Estimate:	5.0%	Momentum Percentile:	10.2%
% Fair Value:	80%	5 Year Valuation Multiple Estimate:	4.4%	Growth Percentile:	30.4%
Dividend Yield:	2.6%	5 Year Price Target	\$92	Valuation Percentile:	83.3%
Dividend Risk Score:	D	Retirement Suitability Score:	D	Total Return Percentile:	73.7%

Overview & Current Events

DowDuPont is the product of a late-2017 merger that combined the former Dow Chemical Company and E.I. du Pont de Nemours & Company. Together, they are a diversified chemical production entity with ~\$87 billion in annual revenue and a \$133 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 posted Q3 earnings on 11/1/18 and results beat expectations. Double-digit revenue gains in all segments led to the top line advancing a whopping 31% over the year-ago period. Volume gains totaled 6% during the quarter while merger integration and separation costs combined to lead SG&A costs higher by 88%. Still, EBITDA was up 8% and the company boosted its expected synergies to a total of \$3.6 billion, up from \$3.3 billion. DowDuPont said it would buy back \$3 billion worth of shares in the next five months, good for about 2.3% of the float. Management reiterated guidance for this year and we've moved our estimates up to \$4.10 after a very strong Q3 report.

Growth on a Per-Share Basis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
EPS	\$0.62	\$0.32	\$1.72	\$2.05	\$0.71	\$3.68	\$2.87	\$3.32	\$3.52	\$3.07	\$4.10	\$5.25
DPS	--	--	--	--	--	--	--	--	--	\$0.38	\$1.52	\$2.00
Shares	939	1,054	1,144	1,158	1,176	1,290	1,187	1,241	1,123	2,327	2,300	2,150

The merger that took place last year has helped drive earnings growth through synergies and cost savings. 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, notwithstanding Q3's blockbuster revenue gains. Recent weakness in the agricultural business appears to have passed, bolstering the growth case. 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. The buyback should help with earnings-per-share growth as well as DowDuPont is committed to shrinking the float.

Valuation Analysis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	Now	2023
Avg. P/E	24.3	86.3	19.8	14.0	45.5	12.1	15.9	15.5	16.3	17.7	14.1	17.5
Avg. Yld.	--	--	--	--	--	--	--	--	--	0.7%	2.6%	2.3%

DowDuPont shares are trading well below fair value today, going for just 14.1 times earnings against our fair value estimate of 17.5. When the three businesses are spun off, they will almost certainly have different valuations but for

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now, we see this stock as undervalued. The yield has moved up to 2.6% after a huge dividend increase this year and we see it remaining in the mid-2% range for the foreseeable future.

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%	14.5%	15.0%
Debt/A	70%	68%	67%	66%	69%	60%	66%	61%	66%	47%	47%	45%
Int. Cov.	3.4	1.3	3.0	3.8	2.4	7.5	6.7	12.4	7.0	2.4	2.5	2.8
Payout	--	--	--	--	--	--	--	--	--	12%	37%	38%
Std. Dev.	40%	99%	30%	35%	26%	21%	22%	26%	22%	12%	20%	28%

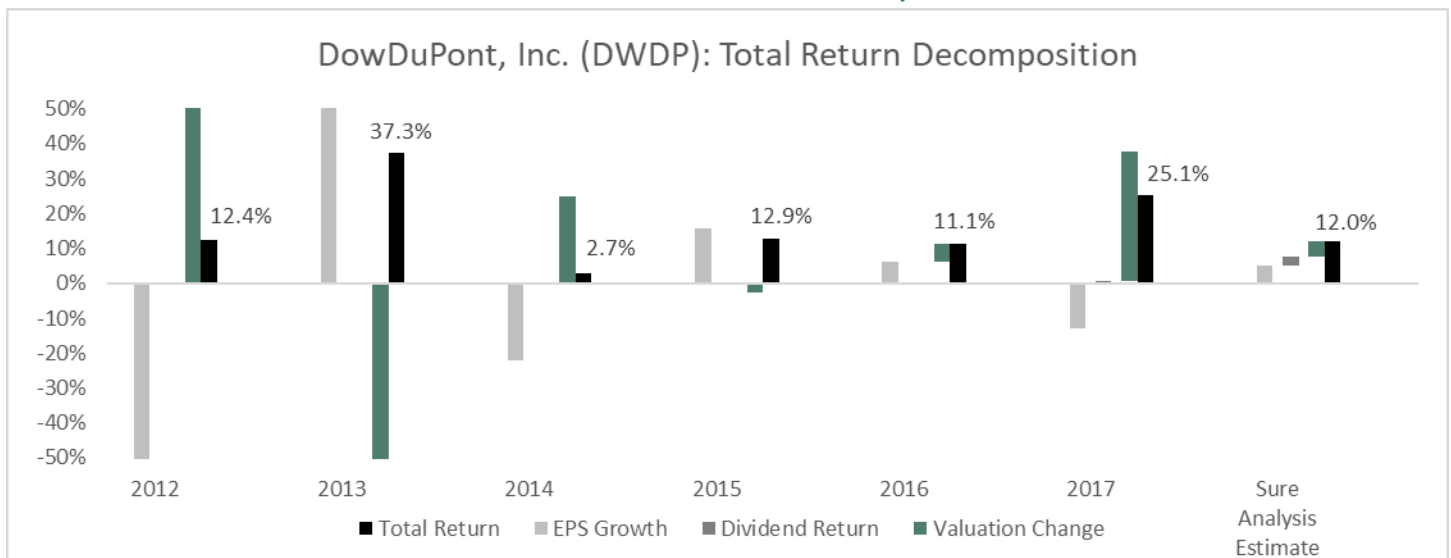
DowDuPont's quality metrics shifted significantly in some cases after the merger was completed. The company now has less than half of its assets financed by liabilities, so its balance sheet is much more robust. Interest coverage, however, has declined as the debt the company has is more expensive to 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. This is particularly true in light of the fact that we see higher profitability from planned synergies in the years to come. The dividend is very safe, and we think the payout ratio will remain roughly where it is.

DowDuPont's competitive advantage is in its very long 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 are not kind to chemical makers and DowDuPont is no exception, as earnings were cut in half in 2009.

Final Thoughts & Recommendation

Overall, DowDuPont looks undervalued again after some recent weakness in the share price. We are forecasting 12.0% total annual returns moving forward, consisting of the current 2.6% yield, 5% earnings-per-share growth and a 4.4% headwind from the valuation. The spinoffs of the three separate businesses should help unlock some value and we like the plan to do so. We've therefore upgraded the stock to buy given the robust yield, strong long-term growth outlooks of the various businesses, spinoff prospects and the cheap valuation of the stock.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Revenue	57361	44875	53674	59985	56786	57080	58167	48778	48158	62484
Gross Profit	5448	5727	7894	8956	8994	9486	10703	11033	10518	12070
Gross Margin	9.5%	12.8%	14.7%	14.9%	15.8%	16.6%	18.4%	22.6%	21.8%	19.3%
SG&A Exp.	1966	2487	2609	2788	2861	3024	3106	2948	2956	4021
D&A Exp.	2236	2827	2962	2883	2698	2681	2747	2521	2862	3969
Operating Profit	2080	1349	3116	4026	3947	4254	5514	6068	5434	4926
Op. Margin	3.6%	3.0%	5.8%	6.7%	7.0%	7.5%	9.5%	12.4%	11.3%	7.9%
Net Profit	579	648	2310	2742	1182	4787	3772	7685	4318	1460
Net Margin	1.0%	1.4%	4.3%	4.6%	2.1%	8.4%	6.5%	15.8%	9.0%	2.3%
Free Cash Flow	2372	-321	1972	1192	1461	5521	2930	3781	1609	5125
Income Tax	651	-97	481	817	565	1988	1426	2147	9	-476

Balance Sheet Metrics

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Total Assets	45474	66018	69588	69224	69605	69501	68687	67938	79511	192B
Cash & Equivalents	2800	2846	7039	5444	4318	5940	5654	8577	6607	13438
Acc. Receivable	3782	9195	4616	4900	5074	4935	4685	4078	4666	11314
Inventories	6036	6847	7087	7577	8476	8303	8101	6871	7363	16992
Goodwill & Int.	4223	19179	18497	17991	17450	17112	16400	15771	21298	92801
Total Liabilities	31894	44894	46946	45933	47738	41577	45333	41755	52282	90237
Accounts Payable	5533	6167	4356	4778	5010	4590	4481	3577	4519	9134
Long-Term Debt	11856	22373	23827	21600	20987	17960	19674	17210	21363	34071
Total Equity	13511	16555	17839	18281	16877	22898	18423	21374	25987	100B
D/E Ratio	0.88	1.09	1.09	0.97	1.01	0.67	0.88	0.68	0.82	0.34

Profitability & Per Share Metrics

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Return on Assets	1.2%	1.2%	3.4%	4.0%	1.7%	6.9%	5.5%	11.2%	5.9%	1.1%
Return on Equity	3.5%	4.3%	13.4%	15.2%	6.7%	24.1%	18.3%	38.6%	18.2%	2.3%
ROIC	2.1%	1.9%	5.1%	6.0%	2.7%	10.8%	8.5%	17.8%	9.4%	1.6%
Shares Out.	939	1,054	1,144	1,158	1,176	1,290	1,187	1,241	1,123	2,327
Revenue/Share	61.09	42.58	46.93	51.79	48.27	44.23	49.00	39.29	42.88	39.10
FCF/Share	2.53	-0.30	1.72	1.03	1.24	4.28	2.47	3.05	1.43	3.21

Note: All figures in millions of U.S. Dollars unless per share or indicated otherwise.

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