



DowDuPont, Inc. (DWDP)

Updated February 3rd, 2019 by Josh Arnold

Key Metrics

Current Price:	\$53	5 Year CAGR Estimate:	14.9%	Volatility Percentile:	30.6%
Fair Value Price:	\$75	5 Year Growth Estimate:	5.0%	Momentum Percentile:	13.2%
% Fair Value:	71%	5 Year Valuation Multiple Estimate:	7.1%	Growth Percentile:	33.1%
Dividend Yield:	2.8%	5 Year Price Target	\$96	Valuation Percentile:	91.0%
Dividend Risk Score:	D	Retirement Suitability Score:	D	Total Return Percentile:	85.5%

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 ~\$90 billion in annual revenue and a \$123 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 reported Q4 earnings on 1/31/19 and results were a bit weak. Total sales were flat against the year-ago period as volume and mix gains were offset by currency translation losses. Volume was up 1% on a consolidated basis as Asia Pacific and Latin America expanded 8% and 9%, respectively, but were offset by a 3% volume decline in the US & Canada, as well as a 1% decline in EMEA. Pricing rose 1% on a consolidated basis, but was offset by the 2 points of currency losses. The company achieved cost savings of \$500 million during the quarter, and has now delivered more than \$1.8 billion in synergies since the merger. Cash flow from operations was up \$900 million in Q4, affording DowDuPont the opportunity to return \$2.3 billion in Q4 via dividends (\$900 million) and buybacks (\$1.4 billion).

In total, earnings-per-share came in at 88 cents in Q4, a 6% rise over last year's comparable period. That capped a year that saw a strong rebound in earnings, although the company was largely reclaiming ground lost in 2017. The spinoffs of Dow and Corteva are on track for April 1 and June 1, respectively, so DowDuPont's Q1 report will be the last one in its current form.

Guidance from management for Q1 was underwhelming, forecasting a mid-single digit decline in revenue and a mid-teens decline in EBITDA, so we've moved our estimate for 2019 consolidated earnings down in sympathy to \$4.30. The big story is the spinoffs and we'll continue to monitor DowDuPont's progress, as well as how the companies are performing once they are spun off.

Growth on a Per-Share Basis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
EPS	\$0.32	\$1.72	\$2.05	\$0.71	\$3.68	\$2.87	\$3.32	\$3.52	\$3.07	\$4.11	\$4.30	\$5.49
DPS	--	--	--	--	--	--	--	--	\$0.38	\$1.52	\$1.52	\$1.92
Shares	1,054	1,144	1,158	1,176	1,290	1,187	1,241	1,123	2,327	2,293	2,260	2,100

The merger that took place in 2017 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 Q4's lackluster performance. 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. The buyback should help with earnings-per-share growth as well as DowDuPont is committed to shrinking the float.

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



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Valuation Analysis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	Now	2024
Avg. P/E	86.3	19.8	14.0	45.5	12.1	15.9	15.5	16.3	17.7	15.9	12.4	17.5
Avg. Yld.	--	--	--	--	--	--	--	--	0.7%	2.3%	2.8%	2.0%

DowDuPont shares are trading well below fair value today, going for just 12.4 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 now, we see this stock as undervalued. The yield has moved up to 2.8% after a huge dividend increase in 2018 and recent weakness in the stock, so we see this yield as unsustainable for the long term.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
Payout	--	--	--	--	--	--	--	--	12%	37%	35%	35%

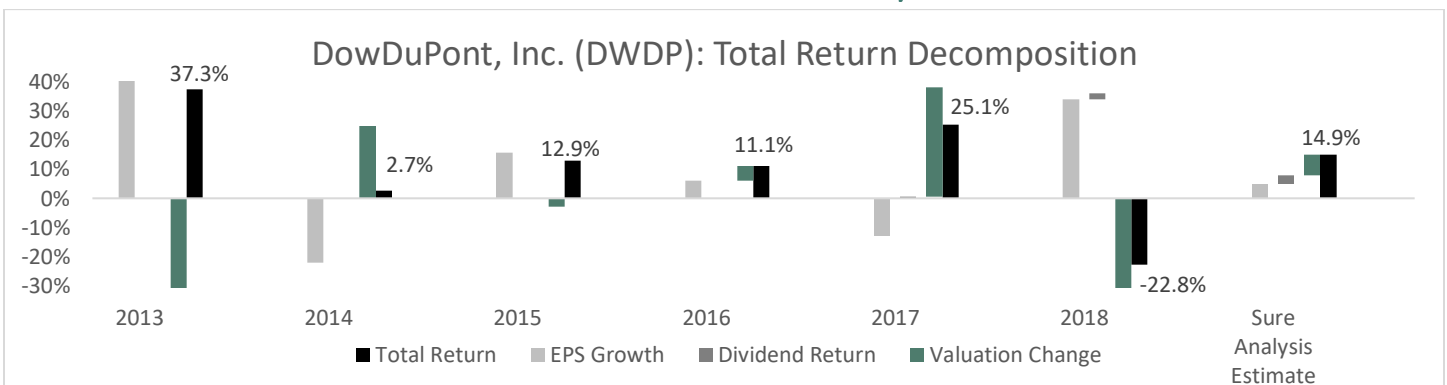
DowDuPont's quality metrics shifted significantly in some cases after the merger was completed. The company now has less than half of its assets financed by liabilities, so its balance sheet is much more robust. Interest coverage, however, has declined as the debt the company has is more expensive to 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 constant moving forward.

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 quite undervalued again after some recent weakness in the share price. We are forecasting 14.9% total annual returns moving forward, consisting of the current 2.8% yield, 5% earnings-per-share growth and a 7.1% tailwind from the valuation. The spinoffs of the three separate businesses should help unlock some value and we like the plan to do so. We're sticking with our buy recommendation ahead of the spinoffs as investors seem to be undervaluing the sum-of-the-parts by a fairly wide margin. Given the robust yield, strong long-term growth outlooks of the various businesses, spinoff prospects and the cheap valuation of the stock, we think it is worth a look for investors ahead of the planned spinoffs.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Revenue	44875	53674	59985	56786	57080	58167	48778	48158	62484	85977
Gross Profit	5727	7894	8956	8994	9486	10703	11033	10518	12070	20644
Gross Margin	12.8%	14.7%	14.9%	15.8%	16.6%	18.4%	22.6%	21.8%	19.3%	24.0%
SG&A Exp.	2487	2609	2788	2861	3024	3106	2948	2956	4021	6709
D&A Exp.	2827	2962	2883	2698	2681	2747	2521	2862	3969	N/A
Operating Profit	1349	3116	4026	3947	4254	5514	6068	5434	4926	8972
Op. Margin	3.0%	5.8%	6.7%	7.0%	7.5%	9.5%	12.4%	11.3%	7.9%	10.4%
Net Profit	648	2310	2742	1182	4787	3772	7685	4318	1460	3844
Net Margin	1.4%	4.3%	4.6%	2.1%	8.4%	6.5%	15.8%	9.0%	2.3%	4.5%
Free Cash Flow	-321	1972	1192	1461	5521	2930	3781	1609	5125	N/A
Income Tax	-97	481	817	565	1988	1426	2147	9	-476	1489

Balance Sheet Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Total Assets	66018	69588	69224	69605	69501	68687	67938	79511	192B	188B
Cash & Equivalents	2846	7039	5444	4318	5940	5654	8577	6607	13438	13482
Acc. Receivable	9195	4616	4900	5074	4935	4685	4078	4666	11314	12376
Inventories	6847	7087	7577	8476	8303	8101	6871	7363	16992	16621
Goodwill & Int.	19179	18497	17991	17450	17112	16400	15771	21298	92801	89997
Total Liabilities	44894	46946	45933	47738	41577	45333	41755	52282	90237	91851
Accounts Payable	6167	4356	4778	5010	4590	4481	3577	4519	9134	9457
Long-Term Debt	22373	23827	21600	20987	17960	19674	17210	21363	34071	40464
Total Equity	16555	17839	18281	16877	22898	18423	21374	25987	100B	94571
D/E Ratio	1.09	1.09	0.97	1.01	0.67	0.88	0.68	0.82	0.34	0.43

Profitability & Per Share Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Return on Assets	1.2%	3.4%	4.0%	1.7%	6.9%	5.5%	11.2%	5.9%	1.1%	2.0%
Return on Equity	4.3%	13.4%	15.2%	6.7%	24.1%	18.3%	38.6%	18.2%	2.3%	3.9%
ROIC	1.9%	5.1%	6.0%	2.7%	10.8%	8.5%	17.8%	9.4%	1.6%	2.8%
Shares Out.	1,054	1,144	1,158	1,176	1,290	1,187	1,241	1,123	2,327	2,293
Revenue/Share	42.58	46.93	51.79	48.27	44.23	49.00	39.29	42.88	39.10	37.13
FCF/Share	-0.30	1.72	1.03	1.24	4.28	2.47	3.05	1.43	3.21	N/A

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

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