



Nucor (NUE)

Updated April 23th, 2018 by Aristofanis Papadatos

Key Metrics

Current Price: \$64	5 Year CAGR Estimate: 10.3%	Quality Percentile: N/A
Fair Value Price: \$74	5 Year Growth Estimate: 5.0%	Momentum Percentile: N/A
% Fair Value: 87%	5 Year Valuation Multiple Estimate: 2.9%	Total Return Percentile: N/A
Dividend Yield: 2.4%	5 Year Price Target: \$94	Valuation Percentile: N/A

Overview & Current Events

Nucor is a manufacturer of steel and steel products, with a market cap of \$20 B. During the last few years, the company has faced challenging business conditions due to the pronounced global overcapacity in its market. China is the world's largest producer and exporter of steel, covering almost half of the global steel output. In addition, Chinese producers are subsidized by their government and are thus able to sell at remarkably low prices, exerting great pressure on their competitors. As a result, Nucor has been unable to return to the record profitability it enjoyed before the last recession.

On the other hand, in 2017, the company reported its highest annual earnings since the last peak of its cycle thanks to 25% sales growth and a 15% increase in its prices per ton of products. The company has gained significant market share in the automotive industry and has thus increased its automotive shipments by 62% over the last five years.

Furthermore, it has acquired several pipe and tube manufacturers that serve niche markets and are thus expected to meaningfully contribute to the growth of the company.

It is also worth noting that Nucor has greatly benefited from the current U.S. government and is expected to benefit even further in the near future. First of all, the recent tax reform is expected to reduce the tax rate of the company from about 35% to 21%. The U.S. government is likely to provide strong protection to Nucor from its foreign competitors by imposing tariffs on foreign producers. Finally, the government is also expected to pass a meaningful infrastructure bill, which will greatly benefit industrial manufacturers. All these factors certainly bode well for Nucor. The company confirmed its promising growth prospects in its recent conference call, in which the management stated that it expected strong growth in Q2 thanks to a robust trend in orders and backlog.

Growth on a Per-Share Basis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
EPS	\$6.01	-\$0.94	\$0.42	\$2.45	\$1.58	\$1.52	\$2.22	\$1.11	\$2.48	\$3.59	\$4.60	\$5.87
DPS	\$1.91	\$1.41	\$1.44	\$1.45	\$1.46	\$1.47	\$1.48	\$1.49	\$1.50	\$1.51	\$1.52	\$1.60

Thanks to the tax reform and the improving business conditions, the analysts and the company expect EPS growth of ~28% this year, from \$3.59 to \$4.60. Going forward, the company is likely to enjoy the additional tailwinds of tariffs and the infrastructure bill. On the other hand, it is prudent to keep in mind that the strong competition from the foreign exporters will remain in place. Moreover, the steel business is highly cyclical and hence it is risky to extrapolate the current favorable conditions to the distant future. Therefore, it is prudent to assume approximate 5% EPS growth going forward, from \$4.60 this year to \$5.87 in 2023.

Valuation Analysis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	Now	2023
Avg. P/E	9.4	----	---	16.7	25.5	31.2	23.2	40.1	19.7	16.3	13.9	16.0
Avg. Yld.	3.4%	3.3%	3.4%	3.6%	3.6%	3.1%	2.9%	3.3%	3.1%	2.6%	2.4%	1.7%

Nucor has traded at an average P/E of 22.8 during the last decade but it is currently trading at a much lower P/E of 13.9. Over the long run, it is reasonable to expect the stock to revert to its average P/E ratio. On the other hand, if the above 5% annual EPS growth for the next five years materializes, the company will be much closer to the peak of its cycle in five years than it is now. Consequently, as cyclical stocks tend to trade at low P/E ratios near the peak of their cycle and

high P/E ratios near their bottom, it is prudent to assume that the stock will be trading at a much lower P/E ratio than its average in 2023, possibly around 16.0. If this occurs, the stock will enjoy a 2.9% annualized gain thanks to expansion of its P/E ratio over the next five years.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
GP/A	29.2%	1.2%	5.6%	12.9%	10.7%	9.3%	11.8%	7.8%	13.3%	16.2%	20.0%	15.0%
Debt/A	42.9%	41.2%	48.9%	48.7%	46.0%	49.7%	50.2%	47.8%	48.2%	44.8%	42.0%	45.0%
Int. Cov.	35.8	-2.1	2.7	8.6	6.3	6.4	7.8	2.4	8.7	11.2	13.0	10.0
Payout	31.8%	N/A	343%	59.2%	92.4%	96.7%	66.7%	134%	60.5%	42.1%	33.0%	27.3%
Std. Dev.	84.8%	54.2%	28.0%	34.8%	21.9%	20.5%	20.2%	27.5%	30.8%	26.1%	28.0%	30.0%

As Nucor operates in a commodity business, it is at the whims of market prices for steel. Thus the stock is very vulnerable to fluctuations in steel prices, and as a result, recessions. During the Great Recession, the company saw EPS decline from \$6.01 in 2008 to a loss of \$0.94 in 2009... And the stock lost 2/3 of its market cap in just six months. Investors should be aware of the significant downside risk of Nucor. There has not been a recession for ~9 years in the United States. Nucor is likely to perform poorly during the next recession.

On the other hand, Nucor has exhibited an exceptional performance for a cyclical stock. More precisely, it has raised its base dividend for 45 consecutive years. This degree of consistency is a testament to the strength of its business model and the quality of its management. Only 32 companies have achieved such a long dividend growth streak.

Final Thoughts & Recommendation

Nucor has been facing great challenges due to the fierce competition and the global overcapacity in its industry. However, it is likely to enjoy a series of tailwinds in the future: a drastic cut in its tax rate, a set of tariffs for its foreign competitors, and an infrastructure bill. Over the next five years, we expect Nucor to generate 10.3% annualized total returns from 5.0% EPS growth, a 2.4% dividend yield, and a 2.9% annualized P/E expansion. Nucor has the best track record of any steel company. With that said, the company sees steep declines during recessions. Nucor makes a good hold at current prices. Those looking to buy into Nucor should wait for a recession or steep decline in steel prices.

Total Return Breakdown by Year

