



PPG Industries (PPG)

Updated April 11th, 2018 by Nick McCullum

Key Metrics

Current Price: \$109	5 Year CAGR Estimate: 12.1%	Quality Percentile: N/A
Fair Value Price: \$128	5 Year Growth Estimate: 7.0%	Momentum Percentile: N/A
% Fair Value: 85%	5 Year Valuation Multiple Estimate: 3.4%	Total Return Percentile: N/A
Dividend Yield: 1.7%	5 Year Price Target: \$128	Valuation Percentile: N/A

Overview & Current Events

PPG Industries is the world's largest paints and coatings company. Its only competitors of similar size are Sherwin-Williams and Dutch paint company Akzo Nobel. PPG Industries was founded in 1883 as a manufacturer and distributor of glass (its name stands for Pittsburgh Plate Glass) and today has approximately 3,500 technical employees located in more than 70 countries at 100 unique locations. With 45 years of consecutive dividend increases, PPG Industries is a member of the Dividend Aristocrats Index.

In mid-January, PPG Industries reported (1/18/18) financial results for the fourth quarter of fiscal 2017. Sales increased by 8% versus the prior year, driven by a 3% increase in volume, 1% higher prices and a 4% tailwind from foreign exchange. Adjusted earnings-per-share increased by 2.6%, largely due to share repurchases (company-wide adjusted earnings actually declined). Full-year results were slightly better. Adjusted earnings-per-share increased by 3.5% over 2016's figure. While PPG Industries' bottom line showed some weakness, it experienced repeated disruptions to its supply chain that resulted in significant input cost inflation. We believe performance will improve moving forward.

Growth on a Per-Share Basis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
EPS	\$1.63	\$1.02	\$2.32	\$3.44	\$3.03	\$4.14	\$4.05	\$5.14	\$3.28	\$6.31	\$6.75	\$9.45
DPS	\$1.05	\$1.07	\$1.09	\$1.13	\$1.17	\$1.21	\$1.31	\$1.42	\$1.56	\$1.70	\$1.87	\$3.00

PPG Industries has compounded its adjusted earnings-per-share at 16.2% per year since 2008, largely because 2008 earnings were depressed due to the housing market crash. We believe that PPG Industries is capable of delivering 7% annualized earnings-per-share growth over full economic cycles, which gives a 2018 earnings-per-share estimate of \$6.75 and a 2023 earnings-per-share estimate of \$9.45. Dividends will likely grow at a slightly faster rate but are unlikely to exceed low-double-digit growth rates over any meaningful time period.

PPG's growth will come from intelligent portfolio management. Last year, it divested its last remaining glass business – the North American fiberglass unit – for \$545 million. The company is also a disciplined acquirer. Last year, it made three bids for Dutch paints and coatings company Akzo Nobel before eventually walking away from the acquisition. PPG's CEO said in a statement that *"We believe it is in the best interests of PPG and its shareholders to withdraw our proposal to AkzoNobel at this time."* We were pleased with the company's willingness to leave negotiations once prices became unreasonable and believe that acquisitions should continue to generate returns for the foreseeable future.

Valuation Analysis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	Now	2023
Avg. P/E	17.9	23.9	14.8	12.3	17.5	19.0	24.7	20.9	31.1	16.9	16.1	19.0
Avg. Yld.	3.6%	4.4%	3.2%	2.7%	2.2%	1.5%	1.3%	1.3%	1.5%	1.6%	1.7%	1.5%

We believe that PPG Industries is capable of delivering \$6.75 in adjusted earnings-per-share for fiscal 2018. Using this earnings estimate, the company is trading at a forward price-to-earnings ratio of 16.1. PPG Industries' average price-to-earnings ratio over the last decade has been 19.9. We believe that around 19 times earnings is a reasonable approximation for the fair value of PPG Industries. If the company's valuation can expand to 19 times earnings over a period of 5 years, this will add 3.4% to the company's annualized returns.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
GP/A	38.7%	33.0%	34.8%	36.8%	32.0%	37.5%	36.7%	37.8%	41.7%	39.6%	40.0%	40.0%
Debt/A	77.3%	73.6%	75.7%	77.4%	74.4%	68.9%	70.5%	70.8%	69.4%	66.4%	65.0%	60.0%
Int. Cov.	5.1	4.9	9.6	8.5	6.1	9.3	11.2	21.7	9.2	24.9	10.0	10.0
Payout	64.4%	104.9%	47.0%	32.8%	38.6%	29.2%	32.3%	27.6%	47.6%	26.9%	27.7%	31.7%
Std. Dev.	48.9%	38.7%	24.8%	30.5%	24.1%	20.6%	18.7%	21.2%	23.0%	16.1%	20.0%	20.0%

PPG Industries scores well on a number of quality metrics relative to our broad universe of public equities. The company's ratio of gross profits to total assets is much higher than average. With that said, it is significantly lower than its main peer, Sherwin-Williams Company (SHW). Investors should also note that PPG Industries' balance sheet has consistently deleveraged over the last decade. This is a trend that we expect to continue.

From an income perspective, PPG Industries' conservative payout ratio gives it room to continue increasing its dividend should profits stall for a temporary period of time. We believe that the company is likely to grow its dividend at a faster rate than its per-share earnings for the foreseeable future.

Qualitatively, PPG Industries' competitive advantage is based on its industry-leading scale. The company is the largest player in the paints and coatings sector. This provides PPG Industries with economies of scale and brand recognition among millions of consumers around the world. The downside to the company's leadership in the paints and coatings industry is its reliance on a healthy housing and remodeling market. Paint sales are driven by home construction, so housing market crashes have a profound impact on PPG's financial results.

Final Thoughts & Recommendation

PPG Industries' size and brand recognition give it a durable competitive advantage in the paints and coatings industry. Moreover, its multi-decade streak of dividend increases shows that it is willing and able to prioritize its profit distributions to shareholders.

Best of all, the company is trading at a discount to our perception of its intrinsic value. Valuation expansion should provide a tailwind to PPG's future returns. We're recommending the company as a buy today, with the warning that better buying opportunities are likely to arise if weakness in the general economy appears in any meaningful form.

Total Return Breakdown by Year

