



# Union Pacific Corporation (UNP)

Updated July 19<sup>th</sup>, 2019 by Nathan Parsh

## Key Metrics

<b>Current Price:</b>	\$175	<b>5 Year CAGR Estimate:</b>	3.2%	<b>Volatility Percentile:</b>	39.1%
<b>Fair Value Price:</b>	\$144	<b>5 Year Growth Estimate:</b>	5.0%	<b>Momentum Percentile:</b>	85.3%
<b>% Fair Value:</b>	122%	<b>5 Year Valuation Multiple Estimate:</b>	-3.9%	<b>Growth Percentile:</b>	36.3%
<b>Dividend Yield:</b>	2.1%	<b>5 Year Price Target</b>	\$183	<b>Valuation Percentile:</b>	28.7%
<b>Dividend Risk Score:</b>	B	<b>Retirement Suitability Score:</b>	C	<b>Total Return Percentile:</b>	16.9%

## Overview & Current Events

President Lincoln signed the Pacific Railway Act of 1862 that authorized the Union Pacific Railroad Company to build a rail line west towards the coast from the Missouri River. Today, Union Pacific is the largest railroad company in the country and operates more than 32,000 miles of rail throughout the western two-thirds of the country. Union Pacific transports industrial and agricultural products, as well as coal and chemicals. The company trades with a market capitalization of \$125 billion and generates nearly \$23 billion in annual revenues.

Union Pacific reported financial results for the second quarter on 7/18/2019. The company earned \$2.22 per share, \$0.09 above estimates and a 12% increase from the previous year. Revenue declined 1.2% to \$5.6 billion, which was \$20 million below estimates. The company's operating ratio improved 3.4% to an all-time best 59.6%.

Total car loads decreased 4% due to declines in energy and premium shipments. Freight revenue was down 2% as price increases were offset by lower volumes. Agricultural revenues were up 4% despite flat volumes as continued weakness in grain exports continues to weigh on this shipment category. Energy revenues were down 13% as volumes decreased 9%. As in previous quarters, local sourcing for frac sand has reduced demand for this product to be shipped by rail. On the plus side, Union Pacific saw a 30% increase in revenues from petroleum, LPG and renewables. Premium volumes were down 5%, but price increases led to just a 2% drop in revenues. A 1% increase in revenues for international intermodal was more than offset by an 11% decrease in domestic intermodal. Union Pacific saw improvements in terminal dwell while train speed was slower than the previous year. Also helping to improve the operating margin were higher locomotive and workforce productivity levels. The company also decreased its workforce by 8% during the quarter. Fuel expenses were down 13% year-over-year. Union Pacific repurchased 3.7 million shares at an average price of ~\$173.

## Growth on a Per-Share Basis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
<b>EPS</b>	\$1.81	\$2.77	\$3.36	\$4.14	\$4.71	\$5.75	\$5.41	\$5.07	\$5.79	\$7.91	<b>\$8.96</b>	<b>\$11.43</b>
<b>DPS</b>	\$0.54	\$0.66	\$0.97	\$1.25	\$1.48	\$1.91	\$2.20	\$2.26	\$2.48	\$3.06	<b>\$3.52</b>	<b>\$4.49</b>
<b>Shares</b>	1010	983	960	939	912	883	849	816	781	755	<b>706</b>	<b>650</b>

Earnings-per-share have increased at a rate of almost 10% per year over the past decade, though much of this growth occurred in the years after the last recession. Earnings have increased at a rate of 5.3% over the past five years. We estimate that Union Pacific will grow earnings-per-share at a rate of 5% going forward due to revenue growth and continued business efficiency. Applying this growth rate to the company's guidance for 2019 means shares could earn \$11.43 by 2024.

Union Pacific has increased its dividend for each of the past 13 years. The company has been very aggressive in raising its dividend recently, with four increases in the past six quarters. The most recent increase was announced 2/7/2019 and resulted in a 10% dividend raise. Dividends-per-share in 2019 should be 15% higher than dividends received in 2018 as a result. Erring on the conservative side, we expect dividends to grow at the same rate as earnings through 2024. Union Pacific's irregular dividend policy makes it somewhat difficult to forecast future payouts, but we believe its commitment to boosting the dividend is strong.

*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	14.7	13.8	14.5	14.1	16.0	17.6	18.3	17.4	19.1	18.6	19.5	16.0
Avg. Yld.	2.0%	1.7%	2.0%	2.1%	2.0%	1.9%	2.2%	2.6%	2.2%	2.3%	2.1%	2.6%

Shares of Union Pacific have decreased \$2, or 1.1%, since our 4/20/2019 update. Shares trade with a price-to-earnings multiple of 19.5 based off of our expected earnings-per-share for the current year. Union Pacific shares have an average price-to-earnings multiple of 16 over the past decade. If the stock reverts to its average valuation by 2024, shareholders could see a 3.9% headwind to total returns over this time frame.

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

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
Payout	30%	24%	29%	30%	31%	33%	41%	45%	43%	39%	39%	39%

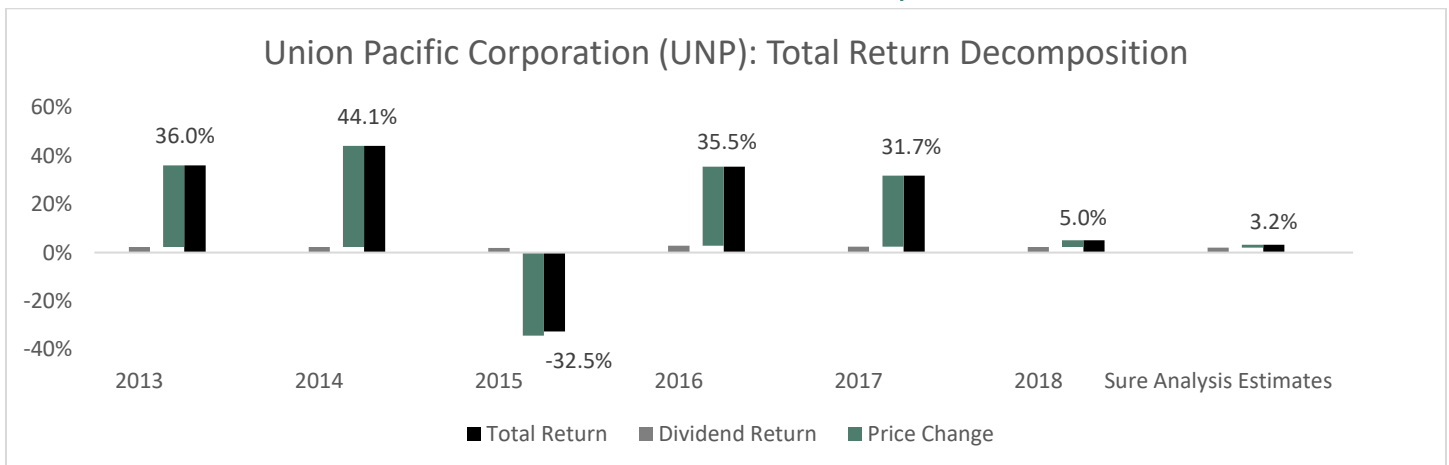
Union Pacific's earnings were impacted during the last recession. A decline in earnings would be likely to occur in the next recession as many of the products that the company transports, like automotive vehicles, are in high demand when the U.S. economy is strong. Union Pacific's dividend payout ratio has generally stayed below 40% over the last ten years. We feel that the company is unlikely to expand its dividend payout ratio much beyond current levels. Accelerated dividend growth will likely have to come from higher earnings growth.

Union Pacific is the largest railroad in the U.S. and spans the western two-thirds of the country. This gives the company pricing power for its shipments, as was seen in the most recent quarter due to strong network effects that railroads enjoy. The railroad has stops along both the Canadian and Mexican borders, making Union Pacific an attractive option for businesses looking to ship goods to almost any place in North America.

## Final Thoughts & Recommendation

Factoring in second quarter results, we forecast that Union Pacific Corporation has the potential to return 3.2% annually through 2024, up from our previous estimate of 2.8%. The stock is up almost 30% year-to-date, which has removed much of the potential return from our estimates. The railroad only saw volume improvements in one product category. Even with price increases, freight revenue was still down from the previous year. Due to the growth in the share price this year and the mixed quarterly results, Union Pacific continues to receive a sell recommendation from Sure Dividend. We maintain our 2024 price target of \$183, which is less than 5% above the current share price.

## Total Return Breakdown by Year



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## Income Statement Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
<b>Revenue</b>	14143	16965	19557	20926	21963	23988	21813	19941	21240	22832
<b>Gross Profit</b>	9556	10014	11187	12218	13102	14753	14137	13019	13993	14595
<b>Gross Margin</b>	67.6%	59.0%	57.2%	58.4%	59.7%	61.5%	64.8%	65.3%	65.9%	63.9%
<b>SG&amp;A Exp.</b>	4063	4314	4681	4685	4807	5076	5161	4750	4984	5056
<b>D&amp;A Exp.</b>	1427	1487	1617	1760	1777	1904	2012	2038	2105	2191
<b>Operating Profit</b>	4066	4981	5724	6745	7446	8753	8052	7272	8061	8517
<b>Op. Margin</b>	28.7%	29.4%	29.3%	32.2%	33.9%	36.5%	36.9%	36.5%	38.0%	37.3%
<b>Net Profit</b>	1890	2780	3292	3943	4388	5180	4772	4233	10712	5966
<b>Net Margin</b>	13.4%	16.4%	16.8%	18.8%	20.0%	21.6%	21.9%	21.2%	50.4%	26.1%
<b>Free Cash Flow</b>	750	1623	2697	2423	3327	3039	2694	4020	3992	5249
<b>Income Tax</b>	1084	1653	1972	2375	2660	3163	2884	2533	-3080	1775

## Balance Sheet Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
<b>Total Assets</b>	42184	43088	45096	47153	49731	52372	54600	55718	57806	59147
<b>Cash &amp; Equivalents</b>	1850	1086	1217	1063	1432	1586	1391	1277	1275	1273
<b>Acc. Receivable</b>	666	1184	1401	1331	1414	1611	1356	1258	1493	N/A
<b>Inventories</b>	475	534	614	660	653	712	736	717	749	N/A
<b>Total Liabilities</b>	25383	25325	26518	27276	28506	31183	33898	35786	32950	38724
<b>Accounts Payable</b>	612	677	819	825	803	877	743	955	1013	N/A
<b>Long-Term Debt</b>	9848	9242	8906	8997	9577	11413	14201	15007	16944	22391
<b>Total Equity</b>	16801	17763	18578	19877	21225	21189	20702	19932	24856	20423
<b>D/E Ratio</b>	0.59	0.52	0.48	0.45	0.45	0.54	0.69	0.75	0.68	1.10

## Profitability & Per Share Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
<b>Return on Assets</b>	4.6%	6.5%	7.5%	8.5%	9.1%	10.1%	8.9%	7.7%	18.9%	10.2%
<b>Return on Equity</b>	11.7%	16.1%	18.1%	20.5%	21.4%	24.4%	22.8%	20.8%	47.8%	26.4%
<b>ROIC</b>	7.4%	10.4%	12.1%	14.0%	14.7%	16.3%	14.1%	12.1%	27.9%	14.1%
<b>Shares Out.</b>	1010	983.13	959.86	938.93	912	883.37	849.21	815.8	780.9	755
<b>Revenue/Share</b>	13.98	16.87	19.96	21.96	23.58	26.62	25.09	23.87	26.49	30.27
<b>FCF/Share</b>	0.74	1.61	2.75	2.54	3.57	3.37	3.10	4.81	4.98	6.96

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

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