



Sherwin-Williams Company (SHW)

Updated August 15th, 2019 by Eli Inkrot

Key Metrics

Current Price:	\$520	5 Year CAGR Estimate:	4.6%	Volatility Percentile:	42.8%
Fair Value Price:	\$418	5 Year Growth Estimate:	8.0%	Momentum Percentile:	80.7%
% Fair Value:	125%	5 Year Valuation Multiple Estimate:	-4.3%	Growth Percentile:	77.3%
Dividend Yield:	0.9%	5 Year Price Target	\$614	Valuation Percentile:	19.9%
Dividend Risk Score:	A	Retirement Suitability Score:	C	Total Return Percentile:	19.9%

Overview & Current Events

Sherwin-Williams, founded in 1866 and headquartered in Cleveland, OH, is North America's largest manufacturer of paints and coatings. The company distributes its products through wholesalers as well as retail stores (including a chain of more than 4,900 company-operated stores and facilities) to 120 countries under the Sherwin-Williams name. The company also manufactures *Dutch Boy*, *Pratt & Lambert*, *Minwax*, *Martin-Senour*, *Thompson's Waterseal*, *Krylon*, *Valspar* (acquired in 2017), and other brands. Sherwin-Williams generates annual sales of approximately \$18 billion and has grown to a market capitalization of \$49 billion. With 40 years of consecutive dividend increases, Sherwin-Williams is a member of the Dividend Aristocrats Index.

On July 23rd, 2019 Sherwin-Williams released Q2 2019 results for the period ending June 30th, 2019. For the quarter Sherwin-Williams generated revenue of \$4.88 billion, up 2.1% from \$4.77 billion in Q2 2018. This improvement was driven primarily by higher paint sales volume in North America, a new customer program launched in 2018, and selling price increases, which were partially offset by some demand softness outside of the U.S. along with unfavorable currency translation. Reported net income per share came in at \$5.03 compared to \$4.25 in the year ago period; however, this includes a variety of special items. On an adjusted basis, net income per share came in at \$6.57 per share compared to the \$5.73 posted last year. Notably, all three of the company's segments – the Americas Group, Consumer Brands Group and Performance Coatings Group – saw increased profits and margins year-over-year.

Sherwin-Williams also updated its guidance for Q3 and full year 2019. For the third quarter the company anticipates that sales will grow by a low single-digit percentage. For the year, 2% to 4% sales grow is expected, while adjusted net income per share guidance was reaffirmed to be in the \$20.40 to \$21.40 range.

Growth on a Per-Share Basis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
EPS	\$3.78	\$4.21	\$4.14	\$6.02	\$7.26	\$8.78	\$11.16	\$11.99	\$15.07	\$18.53	\$20.90	\$30.71
DPS	\$1.42	\$1.44	\$1.46	\$1.56	\$2.00	\$2.20	\$2.68	\$3.36	\$3.40	\$3.44	\$4.52	\$7.68
Shares¹	109.4	107.0	103.9	103.2	100.1	94.7	92.3	93.0	93.9	93.1	93.6	88.0

Sherwin-Williams put together a very strong record in the past, with earnings-per-share growing at a 13.3% average compound rate dating back to 2007. This was driven by solid top line growth, significant margin improvement and a lower share count. More impressive is the idea that the last few years have shown even faster growth, despite coming off a larger base. However, it is important to point out that lately this has been impacted by one-time items such as a decline in the company's tax rate.

While Sherwin-Williams' historical growth rate is outstanding, we believe that the company is unlikely to replicate this performance moving forward. Still, we believe that Sherwin-Williams is capable of delivering 8% annualized earnings growth over full economic cycles. This growth can come from several factors, including revenue expansion – resting on higher sales at the company's existing stores – margin improvement, share repurchases and general economic growth. The company has reduced its share count by roughly 20% throughout the last decade, and we believe that the number of shares will continue to decline, albeit irregularly, over time.

1: In millions.

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	14.8	17.0	19.8	21.3	24.3	24.1	24.3	23.2	22.8	22.2	24.9	20.0
Avg. Yld.	2.5%	2.0%	1.8%	1.2%	1.1%	1.0%	1.0%	1.2%	1.0%	0.8%	0.9%	1.3%

Sherwin-Williams has been a high-quality growth name during the last decade and indeed over the company's history. As a result, shares have generally commanded a premium valuation – trading hands between 21 and 22 times earnings on average during the last 10 years. Given a slower (but still impressive) anticipated growth rate, we are using 20 times earnings as a starting point for fair value. With a multiple of nearly 25 times our expectation of this year's earnings, shares could face a moderate valuation headwind if shares were to revert back toward 20 times earnings.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
Payout	38%	34%	35%	26%	28%	25%	24%	28%	23%	19%	22%	25%

Sherwin-Williams has raised its dividend consistently for decades, but its dividend payout ratio has never risen to a high level. Indeed, the payout ratio has actually declined in the last decade, as dividend increases have trailed earnings-per-share improvement over the years. While the dividend appears exceptionally well covered, the combination of a low payout ratio and above average valuation make for a lackluster dividend yield.

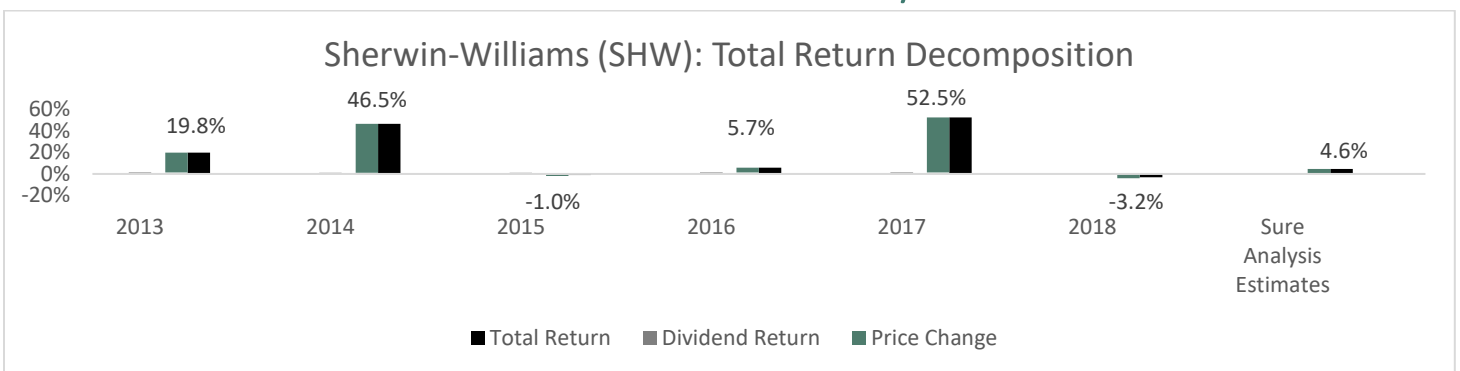
Sherwin-Williams is not necessarily in a high-growth industry, but its entrenched position offers the company its fair share of competitive advantages; allowing the business to grow consistently. Further, acquisitions are a way for Sherwin-Williams to enhance its presence, with the recent Valspar transaction being a good example.

During the last recession Sherwin-Williams posted earnings-per-share of \$4.70, \$4.00, \$3.78 and \$4.21 over the 2007 through 2010 stretch (with a growing dividend to boot). This is somewhat surprising for a company in the paints and coatings industry – generally thought to be a cyclical business – but illustrates the underlying strength of the company.

Final Thoughts & Recommendation

Shares are up 18% since our last report, while earnings expectations for this year are unchanged. Sherwin-Williams has been a great investment during the majority of the last decade. However, moving forward we are forecasting just 4.6% total return potential, stemming from 8% growth and a 0.9% starting dividend yield offset by the potential for a -4.3% valuation headwind. While we are not enthused by the current valuation, we are encouraged by the underlying strength of the business and continue to rate shares as a hold.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Revenue	7094	7776	8766	9534	10186	11130	11339	11856	14984	17534
Gross Profit	3263	3481	3745	4206	4617	5164	5560	5921	6719	7419
Gross Margin	46.0%	44.8%	42.7%	44.1%	45.3%	46.4%	49.0%	49.9%	44.8%	42.3%
SG&A Exp.	2535	2728	2961	3260	3468	3823	3886	4140	4798	5034
D&A Exp.	171	175	181	179	188	199	199	197	492	596
Operating Profit	695	746	775	940	1152	1305	1615	1713	1699	1890
Operating Margin	9.8%	9.6%	8.8%	9.9%	11.3%	11.7%	14.2%	14.4%	11.3%	10.8%
Net Profit	436	462	442	631	753	866	1054	1133	1728	1109
Net Margin	6.1%	5.9%	5.0%	6.6%	7.4%	7.8%	9.3%	9.6%	11.5%	6.3%
Free Cash Flow	768	581	582	731	917	881	1213	1070	1661	1693
Income Tax	187	215	300	276	333	392	495	463	-300	251

Balance Sheet Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Total Assets	4324	5169	5229	6235	6383	5699	5779	6753	19900	19134
Cash & Equivalents	69	59	33	863	745	41	206	890	204	156
Accounts Receivable	696	917	990	1033	1098	1131	1114	1231	2105	2019
Inventories	738	918	927	920	971	1034	1019	1068	1742	1815
Goodwill & Int. Ass.	1294	1423	1414	1504	1492	1447	1399	1382	12817	12158
Total Liabilities	2833	3560	3712	4443	4608	4703	4911	4874	16252	15404
Accounts Payable	675	910	965	923	998	1042	1158	1035	1792	1799
Long-Term Debt	818	1045	993	1705	1722	1799	1950	1953	10521	9344
Shareholder's Equity	1274	1393	1357	1691	1734	996	868	1878	3648	3731
D/E Ratio	0.55	0.65	0.65	0.95	0.97	1.81	2.25	1.04	2.88	2.50

Profitability & Per Share Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Return on Assets	10.0%	9.7%	8.5%	11.0%	11.9%	14.3%	18.4%	18.1%	13.0%	5.7%
Return on Equity	32.7%	34.7%	32.1%	41.4%	43.9%	63.4%	113%	82.5%	62.5%	30.1%
ROIC	18.4%	18.6%	17.1%	21.0%	21.5%	27.5%	37.6%	34.1%	19.2%	8.1%
Shares Out.	109.4	107.0	103.9	103.2	100.1	94.7	92.3	93.0	93.9	92.9
Revenue/Share	61.98	71.48	82.95	91.74	98.84	112.72	119.94	125.47	157.85	184.60
FCF/Share	6.71	5.34	5.51	7.03	8.90	8.92	12.83	11.32	17.50	17.82

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

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