



Union Pacific Corporation (UNP)

Updated October 19th, 2019 by Nathan Parsh

Key Metrics

Current Price:	\$162	5 Year CAGR Estimate:	4.9%	Volatility Percentile:	40.6%
Fair Value Price:	\$143	5 Year Growth Estimate:	5.0%	Momentum Percentile:	64.0%
% Fair Value:	113%	5 Year Valuation Multiple Estimate:	-2.4%	Growth Percentile:	40.8%
Dividend Yield:	2.4%	5 Year Price Target	\$183	Valuation Percentile:	33.9%
Dividend Risk Score:	C	Retirement Suitability Score:	C	Total Return Percentile:	23.1%

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 \$114 billion and generates \$22 billion in annual revenues.

Union Pacific reported earnings results for the third quarter on 10/17/2019. The company's earnings-per-share totaled \$2.22, which was \$0.09 below estimates, but was an increase of 3.3% from the prior year. Revenue declined 7% to \$5.5 billion, which was \$134 million below estimates. Union Pacific's operating ratio improved 2.2% to an all-time best 59.5%. Total revenue carloads dropped 8% as all product categories suffered during the quarter. Agricultural products had a 1% decline in revenue and a 2% drop in volumes as higher demand for biofuels was more than offset by continued weaker grain exports. Revenue for energy shipments was down 20% while volumes decreased by 15%. Coal remains challenged and local sourcing for frac sand reduced demand for shipments of this product. Premium revenues were lower by 9% and volumes were down 11%. Union Pacific saw lower demand for autos and intermodal, with tariffs and trade weighing on results. Industrial revenue was down 1%, but volumes were higher by 2%. Demand for construction and plastic products was offset by lower lumber and paper shipments. One positive area was the company's operating ratio. Despite declines nearly across the board in revenues and volumes, Union Pacific was able to produce a record operating ratio. Average quarterly diesel fuel price dropped 12%, train velocity improved 10% and terminal dwell was lower by 20%, all helping to achieve the operating ratio. Union Pacific retired 6.4 million shares at an average price of ~\$172. The company also repurchased another 3.2 million shares through its accelerated share repurchase program.

Growth on a Per-Share Basis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
EPS	\$1.81	\$2.77	\$3.36	\$4.14	\$4.71	\$5.75	\$5.41	\$5.07	\$5.79	\$7.91	\$8.96	\$11.44
DPS	\$0.54	\$0.66	\$0.97	\$1.25	\$1.48	\$1.91	\$2.20	\$2.26	\$2.48	\$3.06	\$3.88	\$4.95
Shares¹	1010	983	960	939	912	883	849	816	781	755	702	650

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 \$11.44 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. The most recent increase raised the dividend 10.2% for the payment made 9/30/2019. This marks the fifth ~10% increase in the last eight quarters. Dividends for 2019 should be 27% higher than 2018's total.

¹ In millions of shares

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	18.0	16.0
Avg. Yld.	2.0%	1.7%	2.0%	2.1%	2.0%	1.9%	2.2%	2.6%	2.2%	2.3%	2.4%	2.7%

Shares of Union Pacific have decreased \$13, or 7.4%, since our 7/19/2019 update. Shares trade with a price-to-earnings multiple of 18 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 2.4% 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%	43%	43%

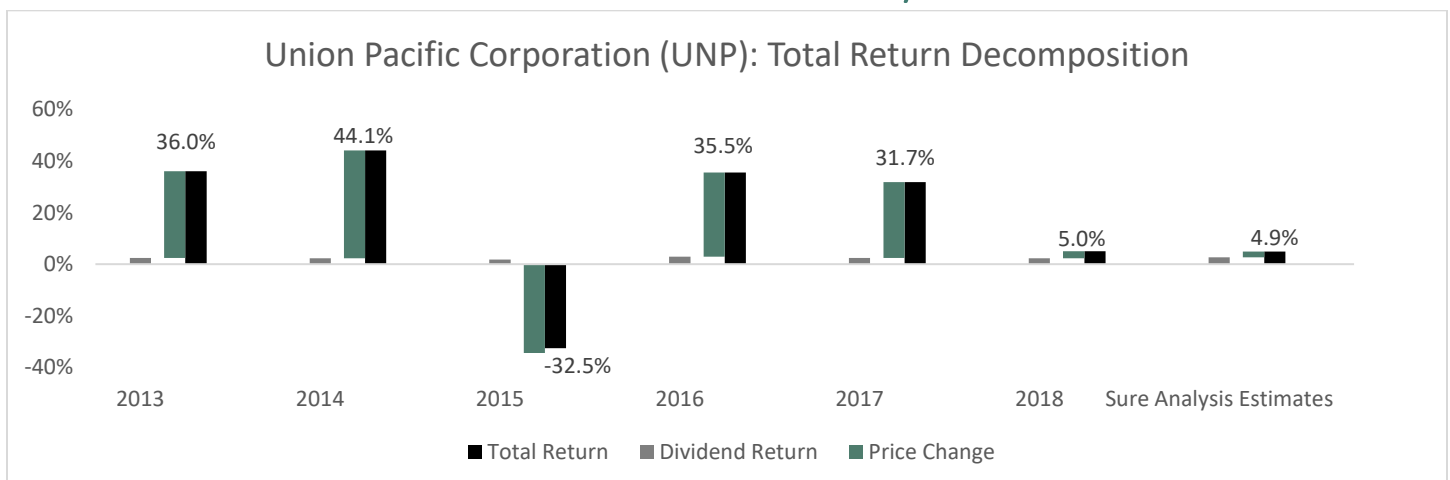
Union Pacific's earnings were impacted during the last recession. A decline in earnings would be likely to occur in the next recession as many of the products that the company transports, like automotive vehicles, are in high demand when the U.S. economy is strong. Union Pacific's dividend payout ratio 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

After reviewing third quarter results, Union Pacific Corporation is expected to offer a total annual return of 4.9% through 2024, up from our previous estimate of 3.2%. Every product category experienced a decline in revenue, while just Industrial products saw an improvement in volumes. Even with this, Union Pacific's efficiencies were impressive during the quarter. Shares have pulled back from our last report, but not enough to earn a buy recommendation. We do raise our rating to hold from sell and maintain our 2024 price target of \$183. On a further pullback, the stock should start to interest income investors, given the company's capital returns via dividends and buybacks.

Total Return Breakdown by Year



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Income Statement Metrics

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

Balance Sheet Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Total Assets	42184	43088	45096	47153	49731	52372	54600	55718	57806	59147
Cash & Equivalents	1850	1086	1217	1063	1432	1586	1391	1277	1275	1273
Acc. Receivable	666	1184	1401	1331	1414	1611	1356	1258	1493	N/A
Inventories	475	534	614	660	653	712	736	717	749	N/A
Total Liabilities	25383	25325	26518	27276	28506	31183	33898	35786	32950	38724
Accounts Payable	612	677	819	825	803	877	743	955	1013	N/A
Long-Term Debt	9848	9242	8906	8997	9577	11413	14201	15007	16944	22391
Total Equity	16801	17763	18578	19877	21225	21189	20702	19932	24856	20423
D/E Ratio	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
Return on Assets	4.6%	6.5%	7.5%	8.5%	9.1%	10.1%	8.9%	7.7%	18.9%	10.2%
Return on Equity	11.7%	16.1%	18.1%	20.5%	21.4%	24.4%	22.8%	20.8%	47.8%	26.4%
ROIC	7.4%	10.4%	12.1%	14.0%	14.7%	16.3%	14.1%	12.1%	27.9%	14.1%
Shares Out.	1010	983.13	959.86	938.93	912	883.37	849.21	815.8	780.9	755
Revenue/Share	13.98	16.87	19.96	21.96	23.58	26.62	25.09	23.87	26.49	30.27
FCF/Share	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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