



United Parcel Service Inc. (UPS)

Updated October 22nd, 2019 by Eli Inkrot

Key Metrics

Current Price:	\$115	5 Year CAGR Estimate:	10.1%	Volatility Percentile:	59.4%
Fair Value Price:	\$122	5 Year Growth Estimate:	6.0%	Momentum Percentile:	35.9%
% Fair Value:	95%	5 Year Valuation Multiple Estimate:	1.1%	Growth Percentile:	57.4%
Dividend Yield:	3.3%	5 Year Price Target	\$163	Valuation Percentile:	71.0%
Dividend Risk Score:	C	Retirement Suitability Score:	C	Total Return Percentile:	72.4%

Overview & Current Events

United Parcel Service, founded in 1907 and headquartered in Atlanta, GA, is a logistics and package delivery company that offers services including transportation, distribution, ground freight, ocean freight, insurance and financing. Its operations are split into three segments: US Domestic Package, International Package, and Supply Chain & Freight. UPS trades with a market capitalization of \$100 billion.

On October 22nd, 2019 UPS reported Q3 2019 results for the period ending September 30th, 2019. For the quarter the company generated revenue of \$18.32 billion, representing a 5.0% increase compared to Q3 2018, driven by strong average daily volume growth (increasing over 9%) in the U.S. The U.S. Domestic segment grew sales by 9.8% and the International segment saw revenue increase 0.5% (+2.3% adjusting for currency), while the Supply Chain & Freight segment's revenue declined by -4.5%. Adjusted net income came in at \$1.78 billion or \$2.07 per share versus \$1.58 billion or \$1.82 in prior year period.

UPS also updated its 2019 outlook. For the year the company now anticipates adjusted free cash flow to be over \$4 billion (from \$3.5 billion to \$4 billion previously), an effective tax rate between 22% and 23% (from 22% to 24% prior) and adjusted earnings-per-share are expected to be in the \$7.45 to \$7.75 range (unchanged from previous guidance).

Growth on a Per-Share Basis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
EPS	\$2.31	\$3.56	\$4.23	\$4.53	\$4.61	\$4.75	\$5.43	\$5.75	\$6.01	\$7.24	\$7.60	\$10.17
DPS	\$1.80	\$1.88	\$2.08	\$2.28	\$2.48	\$2.68	\$2.92	\$3.12	\$3.32	\$3.64	\$3.84	\$5.14
Shares¹	993	987	963	953	924	905	886	868	859	858	868	850

During the last financial crisis, UPS' profitability declined substantially. Earnings-per-share dropped from \$4.11 in 2007 to \$2.31 in 2009. Since then profits have risen relatively consistently. When we look at the 2007-2018 timeframe, earnings-per-share grew by 5.3% annually. The growth rate since 2010 has been 9.3% per annum.

Profit growth during 2018 was higher than in recent years, which is due to the positive one-time impact of a tax rate decline due to tax legislation changes in late 2017. Even without that impact the growth rate would have been solid, though, as UPS benefits from macro tailwinds and is performing well operationally. One such tailwind is e-commerce, which leads to growth in the number of packages that have to be transported across the country. The strong economy drives demand for UPS' services by businesses as well as by consumers, which increase their spending due to higher disposable incomes. With online shopping growth continuing to outpace brick-and-mortar growth in the foreseeable future, UPS should continue to benefit from strong demand for its services.

Collectively, we believe UPS can grow by 6% annually over the intermediate-term. However, 2019 may not be as robust, given management's guidance of 2.9% to 7.0% anticipated improvement.

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	22.6	18.1	16.7	16.7	19.3	21.2	18.5	18.4	18.6	15.6	15.1	16.0
Avg. Yld.	3.5%	2.9%	2.9%	3.0%	2.8%	2.7%	2.9%	2.9%	3.0%	3.2%	3.3%	3.2%

Over the past decade shares of UPS have traded with an average P/E ratio between 18 and 19 times earnings. While we believe a moderate premium is warranted for the quality of the business, we are more comfortable with 16 times earnings as a starting fair value baseline. Still, with shares trading near 15 times today, this implies the potential for a small valuation tailwind.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
Payout	78%	53%	49%	50%	54%	56%	54%	54%	55%	50%	51%	51%

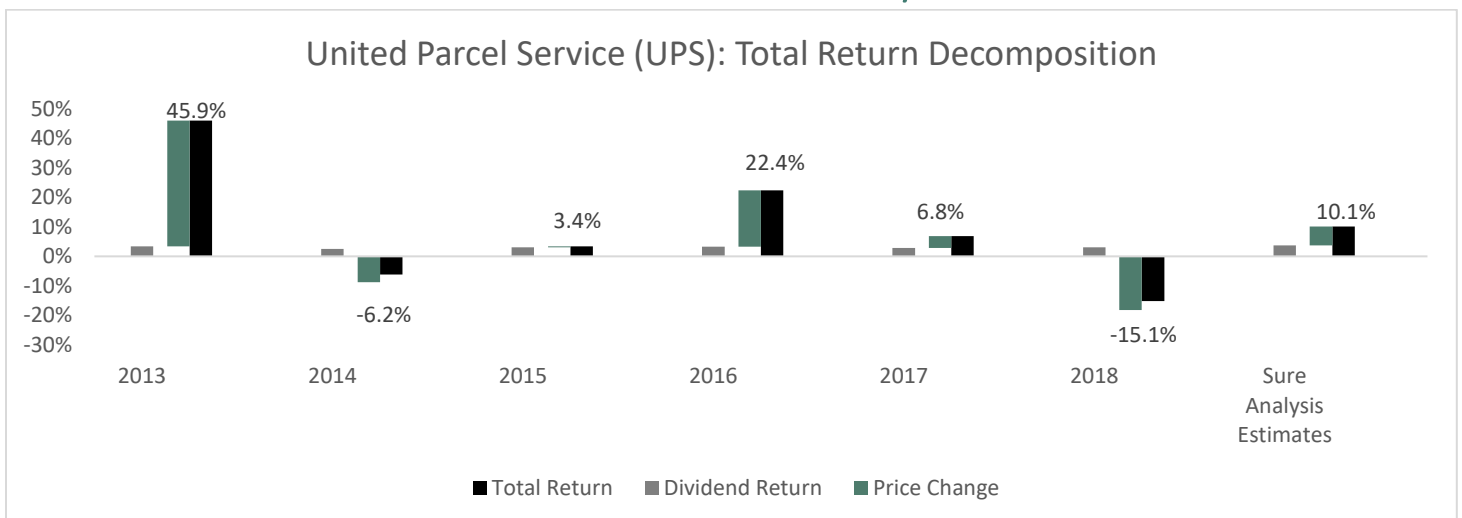
United Parcel Service did not cut its dividend during the last financial crisis, but its payout ratio rose to a relatively high level due to the decline in the company's net profits. Since then, the payout ratio has stabilized around 50%, which appears highly sustainable. We believe that a dividend cut is unlikely, although not impossible during a steep recession.

UPS is the largest logistics/package delivery company in the US. Its top peers include FedEx, DHL Express, and the United States Postal Service. The macro environment is beneficial for the whole industry, thanks to the megatrend of online shopping, as well as a strong economy. None of the big players have an interest in a price war, so volumes could continue to rise even if base pricing is increased over time. Competitive pressures should therefore remain muted for the foreseeable future. UPS was impacted significantly during the last financial crisis, but it remained profitable.

Final Thoughts & Recommendation

Shares are more or less unchanged since our last report, while earnings expectations remain unchanged as well. United Parcel Service is one of the key companies in an industry that benefits from the online shopping megatrend. The business-to-business segment is doing well, too, and it seems likely that UPS will be able to grow its earnings-per-share at a solid pace during the next couple of years. Total return potential comes in at 10.1% per annum, consisting of 6% growth, a 3.3% dividend yield and the potential for a small valuation tailwind. We continue rate shares as a buy at the current quotation, although we are becoming less enthused as the valuation inches upward.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Revenue	45297	49545	53105	54127	55438	58232	58363	61610	66585	71861
Gross Profit	36478	10453	11184	6495	12261	10550	13326	13344	13739	13851
Gross Margin	80.5%	21.1%	21.1%	12.0%	22.1%	18.1%	22.8%	21.7%	20.6%	19.3%
D&A Exp.	1747	1792	1782	1858	1867	1923	2084	2224	2282	2207
Operating Profit	3801	5641	6080	1343	7034	4968	7668	7688	7529	7024
Op. Margin	8.4%	11.4%	11.4%	2.5%	12.7%	8.5%	13.1%	12.5%	11.3%	9.8%
Net Profit	2152	3338	3804	807	4372	3032	4844	3422	4905	4791
Net Margin	4.8%	6.7%	7.2%	1.5%	7.9%	5.2%	8.3%	5.6%	7.4%	6.7%
Free Cash Flow	3683	2446	5068	5063	5239	3398	5051	3508	-3748	6428
Income Tax	1214	1952	1972	167	2302	1605	2498	1699	2232	1228

Balance Sheet Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Total Assets	31883	33597	34701	38863	36212	35440	38311	40377	45574	50016
Cash & Equivalents	1542	3370	3034	7327	4665	2291	2730	3476	3320	4225
Acc. Receivable	5369	5627	6246	6111	6502	6661	7134	7695	8773	8958
Inventories	N/A	N/A	345	393	403	344	308	342	404	421
Goodwill & Int.	2685	2680	2686	2776	2965	3031	4968	5515	5836	5887
Total Liabilities	24187	25550	27593	34130	29724	33282	35820	39948	44550	46979
Accounts Payable	1766	1974	2300	2278	2478	2754	2587	3042	3934	5188
Long-Term Debt	9521	10846	11128	12870	10872	10779	14334	16075	24289	22202
Total Equity	7630	7979	7035	4653	6474	2141	2470	405	994	3021
D/E Ratio	1.25	1.36	1.58	2.77	1.68	5.03	5.80	39.69	24.44	7.35

Profitability & Per Share Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Return on Assets	6.8%	10.2%	11.1%	2.2%	11.6%	8.5%	13.1%	8.7%	11.4%	10.0%
Return on Equity	29.9%	42.8%	50.7%	13.8%	78.6%	70.4%	210%	238%	701%	239%
ROIC	12.7%	18.5%	20.5%	4.5%	25.0%	20.0%	32.6%	20.5%	23.5%	19.0%
Shares Out.	993	987	963	953	924	905	886	868	859	850
Revenue/Share	45.12	49.40	53.59	55.86	58.48	63.02	64.42	69.46	76.10	82.60
FCF/Share	3.67	2.44	5.11	5.23	5.53	3.68	5.58	3.95	-4.28	7.39

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

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