



United Parcel Service Inc. (UPS)

Updated January 30th, 2020 by Eli Inkrot

Key Metrics

Current Price:	\$108	5 Year CAGR Estimate:	12.3%	Market Cap:	\$92.9 B
Fair Value Price:	\$127	5 Year Growth Estimate:	6.0%	Ex-Dividend Date¹:	02/25/20
% Fair Value:	85%	5 Year Valuation Multiple Estimate:	3.2%	Dividend Payment Date¹:	03/12/20
Dividend Yield:	3.7%	5 Year Price Target	\$169	Years Of Dividend Growth:	10
Dividend Risk Score:	C	Retirement Suitability Score:	C	Last Dividend Increase:	5.5%

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 \$93 billion.

On January 30th, 2020 UPS reported Q4 and full year 2019 results for the period ending December 31st, 2019. For the quarter the company generated revenue of \$20.57 billion, representing a 3.6% increase compared to Q4 2018, driven by strong average daily volume growth during the peak holiday season. Adjusted net income equaled \$1.84 billion compared to \$1.69 billion prior, while adjusted earnings-per-share came in at \$2.11 versus \$1.94 prior. For the year UPS generated \$74.1 billion in revenue, a 3.1% year-over-year increase, driven by strong volume growth in the U.S. Adjusted earnings-per-share totaled \$7.53, up 4.0%, and within prior guidance of \$7.45 to \$7.75.

UPS also provided a 2020 outlook. For the year the company anticipates adjusted free cash flow to be between \$4.3 and \$4.47 billion, an effective tax rate between 22.5% and 23.5% and adjusted earnings-per-share are expected to be in the \$7.76 to \$8.06 range. We have initiated our 2020 forecast accordingly.

Growth on a Per-Share Basis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
EPS	\$3.56	\$4.23	\$4.53	\$4.61	\$4.75	\$5.43	\$5.75	\$6.01	\$7.24	\$7.53	\$7.91	\$10.59
DPS	\$1.88	\$2.08	\$2.28	\$2.48	\$2.68	\$2.92	\$3.12	\$3.32	\$3.64	\$3.84	\$4.00	\$5.35
Shares²	987	963	953	924	905	886	868	859	858	863	860	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 2007-2019 timeframe, earnings-per-share grew by 5.2% annually. The growth rate since 2010 has been 8.7% per annum.

Note: 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, 2020 may not be as robust, given management's guidance of 3.1% to 7.0% anticipated improvement.

¹ Estimate

² 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	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	Now	2025
Avg. P/E	18.1	16.7	16.7	19.3	21.2	18.5	18.4	18.6	15.6	14.5	13.7	16.0
Avg. Yld.	2.9%	2.9%	3.0%	2.8%	2.7%	2.9%	2.9%	3.0%	3.2%	3.5%	3.7%	3.2%

Over the past decade shares of UPS have traded with an average P/E ratio about 18 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 fair value baseline. Still, with shares trading near 14 times today, this implies the potential for a valuation tailwind.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
Payout	53%	49%	50%	54%	56%	54%	54%	55%	50%	51%	51%	51%

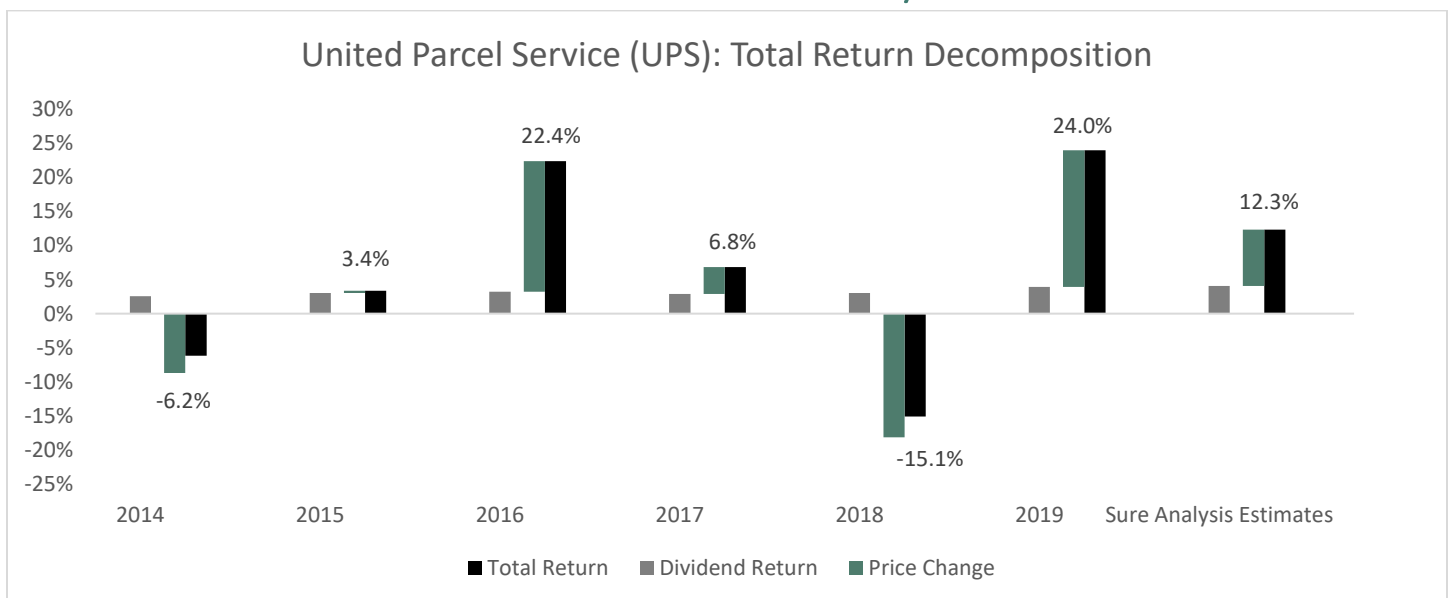
United Parcel Service did not cut its dividend during the last financial crisis, but its payout ratio rose to a relatively high level due to the decline in the company's net profits. Since then, the payout ratio has stabilized around 50%, which appears highly sustainable. We believe that a dividend cut 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 down -6% since our last report. 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 over the intermediate term. Total return potential comes in at 12.3% per annum, consisting of 6% growth, a 3.7% dividend yield and the potential for a valuation tailwind. We continue rate shares as a buy at the current quotation.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Revenue	49545	53105	54127	55438	58232	58363	61610	66585	71861	74094
Gross Profit	10453	11184	6495	12261	10550	13326	13344	13739	13851	13717
Gross Margin	21.1%	21.1%	12.0%	22.1%	18.1%	22.8%	21.7%	20.6%	19.3%	18.5%
D&A Exp.	1792	1782	1858	1867	1923	2084	2224	2282	2207	
Operating Profit	5641	6080	1343	7034	4968	7668	7688	7529	7024	7798
Op. Margin	11.4%	11.4%	2.5%	12.7%	8.5%	13.1%	12.5%	11.3%	9.8%	10.5%
Net Profit	3338	3804	807	4372	3032	4844	3422	4905	4791	4440
Net Margin	6.7%	7.2%	1.5%	7.9%	5.2%	8.3%	5.6%	7.4%	6.7%	6.0%
Free Cash Flow	2446	5068	5063	5239	3398	5051	3508	-3748	6428	8639
Income Tax	1952	1972	167	2302	1605	2498	1699	2232	1228	1212

Balance Sheet Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Total Assets	33597	34701	38863	36212	35440	38311	40377	45574	50016	57857
Cash & Equivalents	3370	3034	7327	4665	2291	2730	3476	3320	4225	
Acc. Receivable	5627	6246	6111	6502	6661	7134	7695	8773	8958	
Inventories	N/A	345	393	403	344	308	342	404	421	
Goodwill & Int.	2680	2686	2776	2965	3031	4968	5515	5836	5887	
Total Liabilities	25550	27593	34130	29724	33282	35820	39948	44550	46979	54574
Accounts Payable	1974	2300	2278	2478	2754	2587	3042	3934	5188	
Long-Term Debt	10846	11128	12870	10872	10779	14334	16075	24289	22202	21818
Total Equity	7979	7035	4653	6474	2141	2470	405	994	3021	3283
D/E Ratio	1.36	1.58	2.77	1.68	5.03	5.80	39.69	24.44	7.35	6.65

Profitability & Per Share Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Return on Assets	10.2%	11.1%	2.2%	11.6%	8.5%	13.1%	8.7%	11.4%	10.0%	8.2%
Return on Equity	42.8%	50.7%	13.8%	78.6%	70.4%	210%	238%	701%	239%	141%
ROIC	18.5%	20.5%	4.5%	25.0%	20.0%	32.6%	20.5%	23.5%	19.0%	17.6%
Shares Out.	987	963	953	924	905	886	868	859	850	
Revenue/Share	49.40	53.59	55.86	58.48	63.02	64.42	69.46	76.10	82.60	85.26
FCF/Share	2.44	5.11	5.23	5.53	3.68	5.58	3.95	-4.28	7.39	9.94

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

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