



Union Pacific Corporation (UNP)

Updated April 23rd, 2020 by Nathan Parsh

Key Metrics

Current Price:	\$152	5 Year CAGR Estimate:	6.6%	Market Cap:	\$103 billion
Fair Value Price:	\$133	5 Year Growth Estimate:	7.0%	Ex-Dividend Date:	5/29/2020
% Fair Value:	114%	5 Year Valuation Multiple Estimate:	-2.6%	Dividend Payment Date:	6/26/2020 ¹
Dividend Yield:	2.6%	5 Year Price Target	\$187	Years Of Dividend Growth:	13
Dividend Risk Score:	B	Retirement Suitability Score:	C	Last Dividend Increase:	10.2%

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 generates about \$20 billion in annual revenues.

Union Pacific reported first quarter earnings results on 4/23/2020. The company's revenue declined 2.8% to \$5.2 billion, topping estimates by \$150 million. Earnings-per-share increased 11.4% to \$2.15, which was \$0.26 higher than estimates. The company's operating ratio improved 460 basis points to an all-time best 59%. Revenue per car increased 4.8% though this was offset by a decrease in volumes and lower fuel surcharge revenue. Bulk revenues were down 5% due to a drop in volume. Coal & Renewables volumes decreased 19% on weaker demand. Grain & Grain Products had 4% volume growth due to higher ethanol exports. An increase in domestic fertilizer demand drove a 7% increase in fertilizer volumes. Food & Beverage volumes were up 2% due to imported beer. Industrial revenues were up 3% on a 3% increase in volumes. Strong crude shipments led to 10% volume growth for Energy. Industrial Chemicals & Plastics improved 4% due to strength in construction markets. Premium revenues were down 6% as pricing increases only partially offset a 12% decline in volume. Intermodal experienced a weak environment for both domestic and international trade, leading to a 15% decline in volume. Automotive was down 1% due to suspension of automotive manufacturing related to the COVID-19 pandemic. The company's performance metrics improved across the board. Miles per day increased 8%, train speed was higher by 3% and terminal dwell was 11% better compared to the previous year. Intermodal trip compliance was up 19% to 85%. Union Pacific repurchased 14.3 million shares, or 5% of the average share balance, at an average price of ~\$182. Cash from operations was higher by 10%. Union Pacific withdrew its full year guidance due to uncertainty related to COVID-19 pandemic. The company does expect volumes to decline 25% in the second quarter. The company is taking measures to confront the impact of the pandemic, including suspending share repurchases, reducing capital expenditures and other cost control measure. The company does plan to maintain its dividend.

Growth on a Per-Share Basis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
EPS	\$2.77	\$3.36	\$4.14	\$4.71	\$5.75	\$5.41	\$5.07	\$5.79	\$7.91	\$8.38	\$7.87	\$11.70
DPS	\$0.66	\$0.97	\$1.25	\$1.48	\$1.91	\$2.20	\$2.26	\$2.48	\$3.06	\$3.88	\$3.88	\$4.95
Shares²	983	960	939	912	883	849	816	781	755	695	686	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.

The company has compounded assets per share by 7.3% over the last decade. Erring on the side of caution, we expect Union Pacific to grow earnings-per-share by 7% over the next five years as the company should see earnings move

¹ Estimated dividend payment date

² In millions of shares

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meaningfully higher after recovering from the COVID-19 pandemic. 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 were 24% higher than the total for 2018.

Valuation Analysis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	Now	2025
Avg. P/E	14.5	14.1	16.0	17.6	18.3	17.4	19.1	18.1	18.1	21.6	18.2	16.0
Avg. Yld.	2.0%	2.1%	2.0%	1.9%	2.2%	2.6%	2.2%	2.1%	2.1%	2.1%	2.6%	2.6%

Shares of Union Pacific have decreased \$35, or 18.7%, since our 1/23/2020 update. Using current assets divided by the average share count in the most recent quarter, Union Pacific has \$8.34 of earnings power. We will use this to determine fair value and total returns for the time being. Shares trade with a price-to-earnings multiple of 18.2 based off of our expected earnings power 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 2025, shareholders could see a 2.6% headwind to total returns over this time frame.

Safety, Quality, Competitive Advantage, & Recession Resiliency

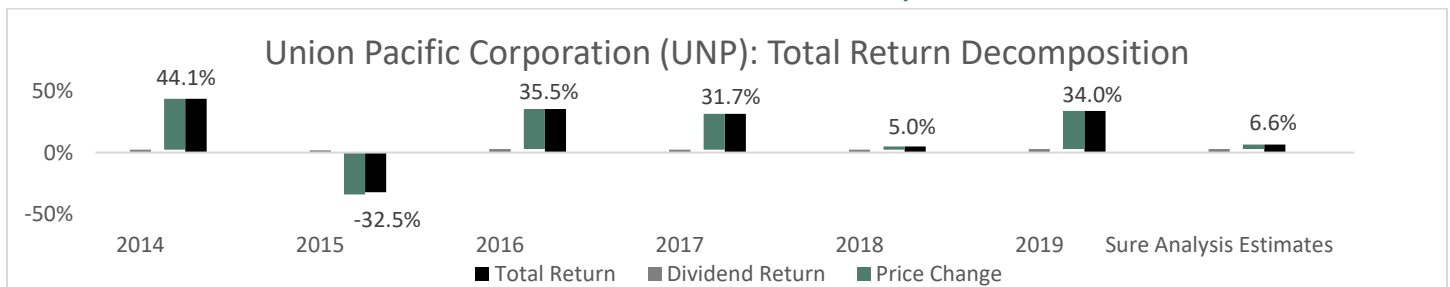
Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
Payout	24%	29%	30%	31%	33%	41%	45%	43%	39%	46%	47%	42%

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 first quarter results, Union Pacific Corporation is expected to offer a total annual return of 6.6% through 2025, up from our previous estimate of 2.8%. The company saw declines in several key areas and expects volumes to decline 25% in the second quarter. The COVID-19 impact on Union Pacific will likely be significant, but the company has had a solid return on assets over the last decade. While the short term could be difficult, we expect that the railroad will see expanded earnings growth once the pandemic has ended. We rate shares as a hold due to projected returns.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Revenue	14,143	16,965	19,557	20,926	21,963	23,988	21,813	19,941	21,240	22,832
Gross Profit	9,556	5,700	6,506	7,533	8,295	9,677	8,976	8,240	9,054	9,539
Gross Margin	67.6%	33.6%	33.3%	36.0%	37.8%	40.3%	41.1%	41.3%	42.6%	41.8%
SG&A Exp.	4,063									
D&A Exp.	1,427	1,487	1,617	1,760	1,777	1,904	2,012	2,038	2,105	2,191
Operating Profit	4,066	4,981	5,724	6,745	7,446	8,753	8,052	7,243	8,106	8,517
Op. Margin	28.7%	29.4%	29.3%	32.2%	33.9%	36.5%	36.9%	36.3%	38.2%	37.3%
Net Profit	1,890	2,780	3,292	3,943	4,388	5,180	4,772	4,233	10,712	5,966
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	1,623	2,697	2,423	3,327	3,039	2,694	4,020	3,992	5,249
Income Tax	1,084	1,653	1,972	2,375	2,660	3,163	2,884	2,533	(3,080)	1,775

Balance Sheet Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Total Assets	42,184	43,088	45,096	47,153	49,731	52,372	54,600	55,718	57,806	59,147
Cash & Equivalents	1,850	1,086	1,217	1,063	1,432	1,586	1,391	1,277	1,275	1,273
Acc. Receivable	666	1,184	1,401	1,331	1,414	1,611	1,356	1,258	1,493	1,755
Inventories	475	534	614	660	653	712	736	717	749	742
Total Liabilities	25,383	25,325	26,518	27,276	28,506	31,183	33,898	35,786	32,950	38,724
Accounts Payable	612	677	819	825	803	877	743	955	1,013	872
Long-Term Debt	9,848	9,242	8,906	8,997	9,577	11,413	14,201	15,007	16,944	22,391
Total Equity	16,801	17,763	18,578	19,877	21,225	21,189	20,702	19,932	24,856	20,423
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.	1012	983	960	939	912	883	849	816	781	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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