



Dow Inc. (DOW)

Updated May 2nd, 2020 by Josh Arnold

Key Metrics

Current Price:	\$34	5 Year CAGR Estimate:	11.9%	Market Cap:	\$25.1B
Fair Value Price:	\$39	5 Year Growth Estimate:	3.0%	Ex-Dividend Date:	05/28/20
% Fair Value:	88%	5 Year Valuation Multiple Estimate:	2.6%	Dividend Payment Date:	06/12/20
Dividend Yield:	8.3%	5 Year Price Target	\$45	Years Of Dividend Growth:	0
Dividend Risk Score:	F	Retirement Suitability Score:	D	Last Dividend Increase:	N/A

Overview & Current Events

Dow Inc. is a new standalone company that was recently spun off from its former parent, DowDuPont. That company has broken into three publicly traded, standalone parts, with the former Materials Science business becoming the new Dow Inc. Dow began trading on its own on April 1st, 2019 with the ticker DOW. It should produce about \$36 billion in revenue this year and trades with a market capitalization of \$25 billion.

Dow reported first quarter earnings on April 30th, with adjusted earnings and revenue both coming in higher than expectations. Total revenue declined -11% year-over-year to \$9.8 billion thanks primarily to the company's exposure to the global energy market. Declines in oil prices generally hurt Dow because its chemicals are used in various processes that help manufacture crude oil-based products. Volume was down -2% as the company also suffered from lower demand for consumer products packaging, surfactants and solvents used for cleaning products, and coatings.

Operating EBITDA was down -18% year-over-year to \$1.57 billion, implying margins declined as well, as the rate of profit decline outpaced that of revenue. In an attempt to improve profitability, the company said it would reduce operating expenses by \$350 million this year, and will idle some manufacturing units. In addition, capex will be cut from the prior target of \$2 billion to \$1.25 billion.

Free cash flow came to \$841 million in Q1, and the company had total liquidity of \$12 billion at the end of the quarter, with no long-term debt due until the second half of 2023.

Guidance is for a very weak second quarter, but a recovery in demand thereafter. We are quite cautious on Dow for the rest of the year, and have slashed our earnings-per-share estimate for 2020 from \$3.55 to \$1.45 following Q1 results, and a rather bleak outlook for the balance of the year.

Growth on a Per-Share Basis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
EPS	---	---	---	---	---	---	---	---	\$3.99	\$3.49	\$1.45	\$4.06
DPS	---	---	---	---	---	---	---	---	---	\$2.10	\$2.80	\$3.09
Shares¹	---	---	---	---	---	---	---	---	747	743	740	720

We previously cut our long-term growth estimate down from 5% to 3% given the revenue and margin issues the company is experiencing. Until Dow can show some level of volume and pricing improvement, growth will be challenged, and we continue to expect modest growth for the foreseeable future.

Gains can accrue in the coming years from stabilized pricing, which management believes will improve into 2021, margin gains from cost savings, and the company's share repurchase program. These factors combined should afford Dow the ability to produce some measure of earnings-per-share growth annually for the foreseeable future, with upside potential should pricing improve more than expected. We like the company's diverse product portfolio and it should see demand hold up in a variety of environments. We note that 2020 is a negative outlier due to collapsing demand in many of Dow's markets, but this should abate as the world's economy returns to normal over time.

¹ Share count 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.



Dow Inc. (DOW)

Updated May 2nd, 2020 by Josh Arnold

The dividend was initiated at \$2.80 annually, good for a ~8% yield on today's share price. We see the dividend rising along with earnings per management's commitment to offer a best-in-class yield.

Valuation Analysis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	Now	2024
Avg. P/E	---	---	---	---	---	---	---	---	---	14.4	9.7	11.0
Avg. Yld.	---	---	---	---	---	---	---	---	---	4.2%	8.3%	6.9%

With earnings temporarily depressed this year, we're using a normalized earnings power value of \$3.50 to compute fair value and valuation metrics. Since Dow only recently began trading on its own, there is no history in which to compare the current valuation. However, given that Dow could grow in the low single-digits or better in the coming years, in addition to how the parent company was valued before the spinoff, we see 11 times earnings as a reasonable valuation. That compares favorably to the current valuation of 9.7 times earnings power, implying an annual tailwind to total returns of just over 2%.

In addition, the yield is 8.3%, which is generally reserved for stocks like REITs or BDCs, so Dow is extremely attractive for income investors. We see the yield remaining very high in the coming years.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
Payout	---	---	---	---	---	---	---	---	---	60%	193%	76%

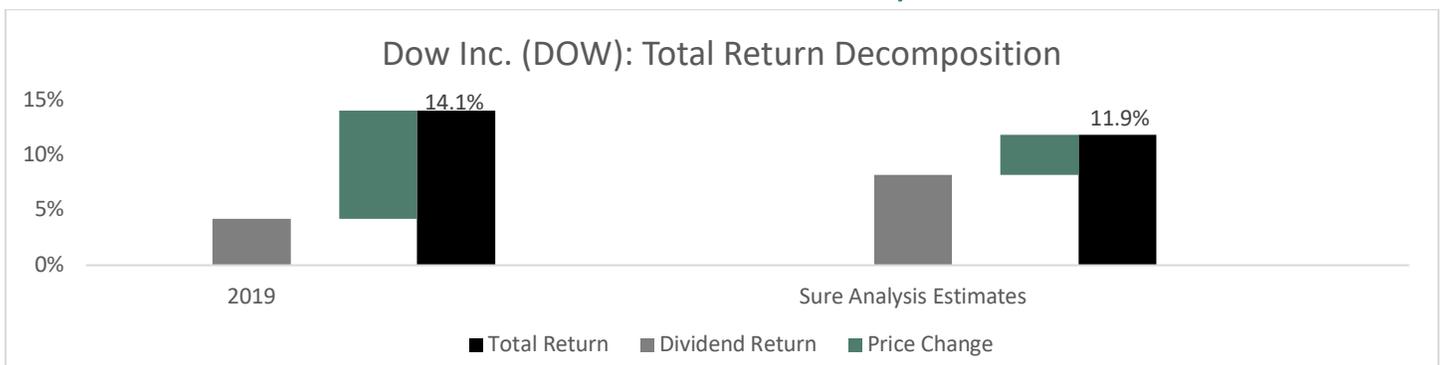
Dow's payout ratio is currently at 80% of earnings power, which is about where we expect it to stay. The reduced outlook for earnings growth has us a bit more cautious on Dow's dividend safety. We don't see any issues in the immediate future, but a deep recession could make it difficult for Dow to afford its ample payout.

While we don't have any data to understand how Dow will perform in a recession, given that the business has only existed in its current form since April of 2019, we believe the company's product portfolio is not only its competitive advantage, but also should perform well enough during downturns to keep the company profitable and able to pay the dividend under most circumstances. We see the company's focused efforts on high-growth areas such as consumer care, packaging, and infrastructure, as well as its very long operating history as a component of the former company, and its brand, as competitive advantages.

Final Thoughts & Recommendation

We see Dow producing 11.9% total returns in the coming years, consisting of the ample yield, with the valuation helping, along with projected earnings growth. We see a lot of bad news priced into the stock today and are upgrading it to buy.

Total Return Breakdown by Year



[Click here to rate and review this research report. Your feedback is important to us.](#)

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.



Dow Inc. (DOW)

Updated May 2nd, 2020 by Josh Arnold

Income Statement Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Revenue							48,158	55,508	60,278	42,951
Gross Profit							10,490	11,896	12,573	6,294
Gross Margin							21.8%	21.4%	20.9%	14.7%
SG&A Exp.							4,066	3,602	2,846	1,590
D&A Exp.							2,862	3,155	3,329	2,938
Operating Profit							4,287	6,022	7,569	3,520
Operating Margin							8.9%	10.8%	12.6%	8.2%
Net Profit							4,318	466	4,499	-1,359
Net Margin							9.0%	0.8%	7.5%	-3.2%
Free Cash Flow							-6,948	-8,102	1,336	3,969
Income Tax							9	2,204	1,285	470

Balance Sheet Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Total Assets								79,940	77,378	60,524
Cash & Equivalents								6,188	2,669	2,367
Accounts Receivable								7,338	8,246	4,844
Inventories								8,376	9,260	6,214
Goodwill & Int. Ass.								19,487	18,761	12,555
Total Liabilities								52,931	49,409	46,430
Accounts Payable								5,360	5,378	3,889
Long-Term Debt								21,001	19,899	16,996
Shareholder's Equity								25,823	26,831	13,541
D/E Ratio								0.81	0.74	1.26

Profitability & Per Share Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Return on Assets									5.7%	-2.0%
Return on Equity									17.1%	-6.7%
ROIC									9.4%	-3.4%
Shares Out.							747	748	747	743
Revenue/Share							64.21	74.01	80.37	57.85
FCF/Share							-9.26	-10.80	1.78	5.35

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

Disclaimer

Nothing presented herein is, or is intended to constitute, specific investment advice. Nothing in this research report should be construed as a recommendation to follow any investment strategy or allocation. Any forward-looking statements or forecasts are based on assumptions and actual results are expected to vary from any such statements or forecasts. No reliance should be placed on any such statements or forecasts when making any investment decision. While Sure Dividend has used reasonable efforts to obtain information from reliable sources, we make no representations or warranties as to the accuracy, reliability or completeness of third-party information presented herein. No guarantee of investment performance is being provided and no inference to the contrary should be made. There is a risk of loss from an investment in marketable securities. Past performance is not a guarantee of future performance.