



Union Pacific Corporation (UNP)

Updated July 23rd, 2020 by Nathan Parsh

Key Metrics

Current Price:	\$174	5 Year CAGR Estimate:	2.1%	Market Cap:	\$118 billion
Fair Value Price:	\$122	5 Year Growth Estimate:	7.0%	Ex-Dividend Date:	8/28/2020
% Fair Value:	143%	5 Year Valuation Multiple Estimate:	-6.9%	Dividend Payment Date:	9/30/2020 ¹
Dividend Yield:	2.2%	5 Year Price Target	\$171	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 \$19 billion in annual revenues.

On 7/23/2020, Union Pacific reported earnings results for the second quarter. Revenue decreased 24% to \$4.2 billion, which was \$100 million lower the analyst community had expected. Earnings-per-share declined \$0.55, or 25%, to \$1.67, though this as \$0.09 higher than anticipated. Union Pacific's operating ratio increased 140 basis points to 61%, but this was slightly below estimates of 62.3%.

Volumes decreased 20% while average revenue per car load declined 6%. Bulk revenues were down 17% while volumes were lower by 15%. Coal & Renewables volumes were down 24% due to weaker demand. Grain & Grain Products had volume declines of 6%, but grain exports were steady. Fertilizer volumes decreased 2% while Food & Refrigeration was down 21% due to COVID-19 related impacts. Industrial revenues were lower by 23%, mostly due to a 18% decline in volumes. Reduced demand for sand, petroleum and industrial chemicals led to a 26% drop in Energy volumes. Weak demand related to the economic shutdown stemming from the COVID-19 pandemic led to a volume decline of 19% for Metals & Minerals, and a 10% drop in Industrial Chemicals and Plastics. Premium was the weakest business for Union Pacific as revenues were down by 33% and volumes declined 23%. Much of this decline was due to a 64% decline in Automotive volume due primarily to production interruptions. Intermodal shipments decreased 12%. Total volumes are down 7% since the start of the third quarter with Premium shipments slightly higher. Union Pacific performance metrics did show improvements almost across the board. Train speed was higher by 10%, locomotive productivity increased 12% and terminal dwell was down 16%. Trip plan compliance, the percentage of cars on time, increased 17% to 76%. Analysts expect that the company will earn \$7.62 of earnings-per-share this year.

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	\$7.62	\$10.69
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 meaningfully higher after recovering from the COVID-19 pandemic.

¹ Estimated dividend payment date

² In millions of shares

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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	22.8	16.0
Avg. Yld.	2.0%	2.1%	2.0%	1.9%	2.2%	2.6%	2.2%	2.1%	2.1%	2.1%	2.2%	2.9%

Shares of Union Pacific have increased \$22, or 14.5%, since our 4/23/2020 update. Shares trade with a price-to-earnings multiple of 22.8 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 multiple by 2025, then valuation would likely be a 6.9% headwind to total returns over this time frame.

Safety, Quality, Competitive Advantage, & Recession Resiliency

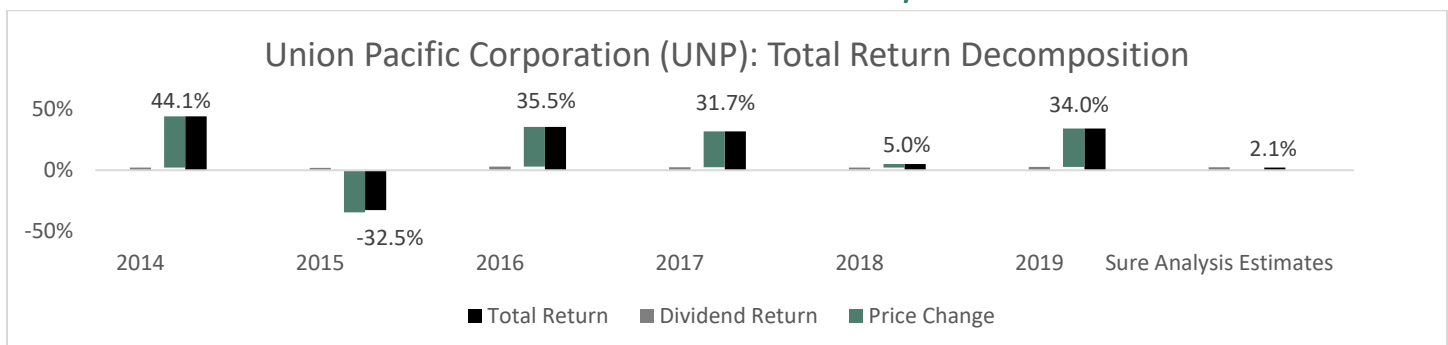
Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
Payout	24%	29%	30%	31%	33%	41%	45%	43%	39%	46%	51%	46%

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 second quarter results, Union Pacific Corporation is expected to offer a total annual return of 2.1% through 2025, down from our previous estimate of 6.6%. Once again, the COVID-19 pandemic weighed heavily on quarterly results. This likely was expected by most investors as the related business shutdowns negatively impacted many end markets, like autos and energy, that Union Pacific supplies. One positive note is that volumes haven't decreased as drastically so far in the third quarter. We have lowered our 2025 price target \$16 due to lowered earnings estimates for the year and reiterate our hold rating on shares of Union Pacific.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Revenue	16,965	19,557	20,926	21,963	23,988	21,813	19,941	21,240	22,832	21,708
Gross Profit	5,700	6,506	7,533	8,295	9,677	8,976	8,240	9,054	9,539	9,614
Gross Margin	33.6%	33.3%	36.0%	37.8%	40.3%	41.1%	41.3%	42.6%	41.8%	44.3%
D&A Exp.	1,487	1,617	1,760	1,777	1,904	2,012	2,038	2,105	2,191	2,216
Operating Profit	4,981	5,724	6,745	7,446	8,753	8,052	7,243	8,106	8,517	8,554
Op. Margin	29.4%	29.3%	32.2%	33.9%	36.5%	36.9%	36.3%	38.2%	37.3%	39.4%
Net Profit	2,780	3,292	3,943	4,388	5,180	4,772	4,233	10,712	5,966	5,919
Net Margin	16.4%	16.8%	18.8%	20.0%	21.6%	21.9%	21.2%	50.4%	26.1%	27.3%
Free Cash Flow	1,623	2,697	2,423	3,327	3,039	2,694	4,020	3,992	5,249	5,156
Income Tax	1,653	1,972	2,375	2,660	3,163	2,884	2,533	(3,080)	1,775	1,828

Balance Sheet Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Total Assets	43,088	45,096	47,153	49,731	52,372	54,600	55,718	57,806	59,147	61,673
Cash & Equivalents	1,086	1,217	1,063	1,432	1,586	1,391	1,277	1,275	1,273	831
Acc. Receivable	1,184	1,401	1,331	1,414	1,611	1,356	1,258	1,493	1,755	1,595
Inventories	534	614	660	653	712	736	717	749	742	751
Total Liabilities	25,325	26,518	27,276	28,506	31,183	33,898	35,786	32,950	38,724	43,545
Accounts Payable	677	819	825	803	877	743	955	1,013	872	749
Long-Term Debt	9,242	8,906	8,997	9,577	11,413	14,201	15,007	16,944	22,391	25,200
Total Equity	17,763	18,578	19,877	21,225	21,189	20,702	19,932	24,856	20,423	18,128
D/E Ratio	0.52	0.48	0.45	0.45	0.54	0.69	0.75	0.68	1.10	1.39

Profitability & Per Share Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Return on Assets	6.5%	7.5%	8.5%	9.1%	10.1%	8.9%	7.7%	18.9%	10.2%	9.8%
Return on Equity	16.1%	18.1%	20.5%	21.4%	24.4%	22.8%	20.8%	47.8%	26.4%	30.7%
ROIC	10.4%	12.1%	14.0%	14.7%	16.3%	14.1%	12.1%	27.9%	14.1%	13.7%
Shares Out.	983	960	939	912	883	849	816	781	755	695
Revenue/Share	16.87	19.96	21.96	23.58	26.62	25.09	23.87	26.49	30.27	30.74
FCF/Share	1.61	2.75	2.54	3.57	3.37	3.10	4.81	4.98	6.96	7.30

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

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