CSX Corporation (CSX)

Updated January 22nd, 2021 by Josh Arnold

Key Metrics

Current Price:	$92	**5 Year CAGR Estimate:**	4.9%	**Market Cap:**	$70 B
Fair Value Price:	$75	**5 Year Growth Estimate:**	8.0%	**Ex-Dividend Date:**	02/27/21[1]
% Fair Value:	123%	**5 Year Valuation Multiple Estimate:**	-4.1%	**Dividend Payment Date:**	03/15/21[2]
Dividend Yield:	1.1%	**5 Year Price Target**	$110	**Years Of Dividend Growth:**	16
Dividend Risk Score:	A	**Retirement Suitability Score:**	C	**Last Dividend Increase:**	8.3%

Overview & Current Events

CSX can trace its roots all the way back to 1827 when the B&O Railroad was first chartered. From just 13 miles of track, CSX has grown to cover 23 states and more than 20,000 route miles. CSX provides rail, rail-to-truck and intermodal transport services. The company's market capitalization is $70 billion after another rally in the stock, and it should produce well over $11 billion in revenue in 2021.

CSX reported fourth quarter and full year earnings on January 21st, 2021 with results coming in mixed. Revenue was down -2% in the fourth quarter to $2.83 billion, as the company saw growth in intermodal that was more than offset by lower fuel surcharge revenue and more declines in coal. Expenses were down -7%, however, to $1.61 billion and were driven lower by efficiency gains and lower fuel spending. This meant operating income was up 5% year-over-year to $1.22 billion as CSX' expenses declined more rapidly than revenue.

The company's operating ratio set a fourth quarter record of just 57%, down from 60% in the same period a year ago. For the full year, the operating ratio was 58.8%, down fractionally from the 59% produced in 2019 despite COVID-19 headwinds present in 2020.

Earnings came to $0.99 per share in Q4, including a charge of five cents per share related to the early extinguishment of debt. Earnings for the year came to $3.60 per share, exactly equal to our prior forecast. For 2021, we see $4.40 in earnings-per-share as CSX continues to rebound off of COVID-19-related weakness.

Growth on a Per-Share Basis

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
EPS	$1.67	$1.79	$1.83	$1.92	$2.00	$1.81	$2.30	$3.85	$4.17	$3.60	***$4.40***	***$6.47***
DPS	$0.45	$0.54	$0.59	$0.63	$0.70	$0.72	$0.78	$0.88	$0.96	$1.04	***$1.04***	***$1.75***
Shares[3]	1,049	1,021	1,009	992	966	928	890	860	778	768	***750***	***715***

CSX's earnings-per-share has grown somewhat unpredictably over the past decade as its fortunes are tied to rail volumes and pricing strength, both of which are heavily dependent upon particular industries and economic conditions. CSX stands to gain in the form of modest revenue increases in the coming years, helping to fuel our estimate of 8% earnings-per-share growth annually. The remainder will come from improved operating efficiency leading to higher margins, as well as sizable buyback spending, although this was nearly halted in 2020. We see the share count declining in the mid-single digits annually as CSX generates strong free cash flow and puts it to use. We see a path to recovery that has cleared up in the past couple of quarters and believe that CSX's growth will pick up substantially in 2021 and beyond.

Likewise, we see the dividend increasing at roughly the rate of earnings, reaching $1.75 in five years from today's level of $1.04. CSX has put buybacks first in recent years but with a much-reduced capex budget as part of its operational efficiency initiatives, more cash should be freed up for dividend increases. With the payout ratio still very low, CSX has plenty of room to continue its streak of dividend increases while still affording it the ability to buy back stock.

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[1] Estimated date
[2] Estimated date
[3] 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.

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Valuation Analysis

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	Now	2026
Avg. P/E	14.0	12.1	13.6	16.1	15.7	15.5	21.8	16.8	17.2	20.6	***20.9***	***17.0***
Avg. Yld.	1.9%	2.5%	2.4%	2.0%	2.2%	2.6%	1.6%	1.4%	1.3%	1.4%	***1.1%***	***1.6%***

CSX's price-to-earnings multiple is roughly equal to where it was at the time of our last update and is now at 20.9. This is well in excess of our slightly raised estimate of fair value of 17 times earnings, so we continue to see a sizable headwind to total returns from the valuation moving forward as we see the stock as remaining overvalued.

We expect the yield to move up to 1.6% over time from the current 1.1%, stemming from a higher dividend and lower valuation. The dividend was raised from $0.96 to $1.04 for 2020.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
Payout	26%	30%	32%	33%	35%	40%	34%	23%	23%	29%	***24%***	***27%***

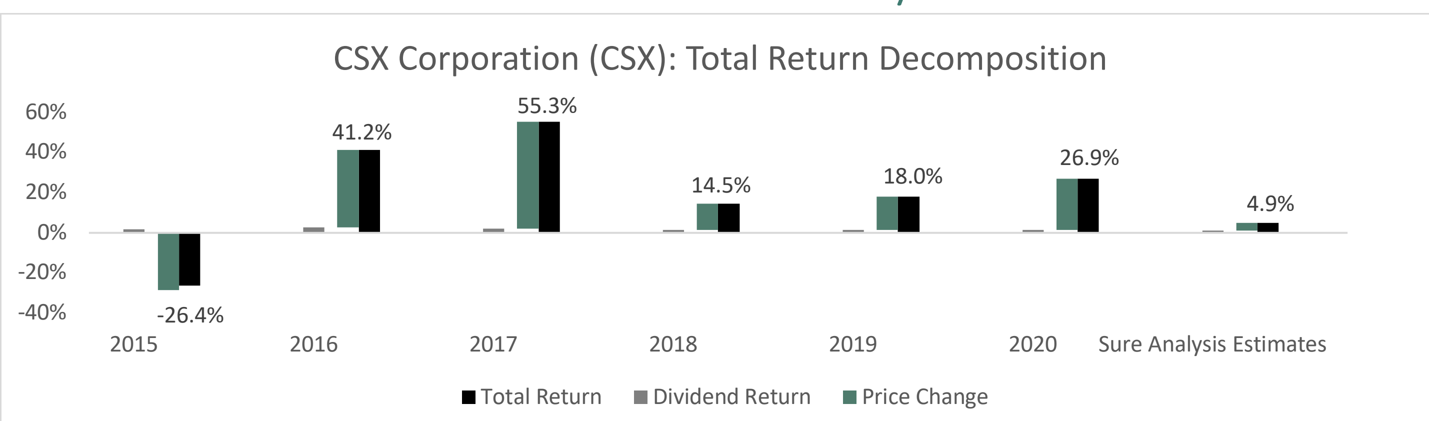
CSX's payout ratio remains low and as a result, is well covered. The company has experienced high rates of earnings growth in recent years, so the payout ratio has fallen as a result of earnings rising, not because the company cannot afford to pay its dividend. Indeed, its dividend safety is outstanding, but we note that the company has made it clear buybacks take priority over dividend growth.

The company's competitive advantage is in its lean operating structure, as well as its dominance in its service area. CSX looks poised to gain from its leverage to intermodal transport and the coal export market, although these things will not save it from recessions; rail operators are particularly sensitive to economic conditions and we see that as the key risk to owning CSX in the coming years, particularly in light of the pandemic. That weakness should be temporary, though, and indeed we forecast a robust rebound in earnings for 2021.

Final Thoughts & Recommendation

In our view, CSX is still trading above fair value. It could see total annual returns in the next five years of 4.9%, consisting of the low current yield, 8% earnings growth and a meaningful headwind from the valuation. CSX could therefore be appropriate for dividend growth investors as well as those seeking earnings growth, but the low current yield would make it unattractive for those seeking current income. In addition, the valuation has kept CSX out of value stock territory once again. Given this, we're reiterating CSX at a hold rating, but would rate the stock a buy if the valuation were closer to our estimate of fair value given its strong growth prospects and ever-improving margins.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Revenue	11,795	11,763	12,026	12,669	11,811	11,069	11,408	12,250	11,937	10,583
Gross Profit	3,470	3,464	3,473	3,613	3,544	3,363	3,741	4,773	4,874	4,362
Gross Margin	29.4%	29.4%	28.9%	28.5%	30.0%	30.4%	32.8%	39.0%	40.8%	41.2%
D&A Exp.	976	1,059	1,104	1,151	1,208	1,301	1,315	1,331	1,349	1,383
Operating Profit	3,470	3,464	3,473	3,613	3,544	3,363	3,741	4,773	4,874	4,362
Operating Margin	29.4%	29.4%	28.9%	28.5%	30.0%	30.4%	32.8%	39.0%	40.8%	41.2%
Net Profit	1,854	1,863	1,864	1,927	1,968	1,714	5,471	3,309	3,331	2,765
Net Margin	15.7%	15.8%	15.5%	15.2%	16.7%	15.5%	48.0%	27.0%	27.9%	26.1%
Free Cash Flow	1,194	605	954	894	808	643	1,432	2,896	3,193	2,637
Income Tax	1,086	1,108	1,058	1,117	1,170	1,027	-2,329	995	985	862

Balance Sheet Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Total Assets	29,344	30,723	31,782	33,053	34,745	35,414	35,739	36,729	38,257	39,793
Cash & Equivalents	783	784	592	669	628	603	401	858	958	3,129
Acc. Receivable	1,000	1,114	1,052	1,129	982	938	793	828	769	---
Inventories	240	274	252	273	350	407	372	263	261	---
Goodwill & Int.	64	64	64	63	63	63	---	---	---	---
Total Liabilities	20,876	21,587	21,278	21,877	23,077	23,720	21,018	24,149	26,394	26,683
Accounts Payable	1,018	948	957	845	764	806	847	949	1,043	---
Long-Term Debt	9,241	9,832	9,555	9,742	10,535	11,293	11,809	14,757	16,238	16,705
Total Equity	8,455	9,122	10,483	11,152	11,652	11,679	14,705	12,563	11,848	13,110
D/E Ratio	1.09	1.08	0.91	0.87	0.90	0.97	0.80	1.17	1.37	1.27

Profitability & Per Share Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Return on Assets	6.5%	6.2%	6.0%	5.9%	5.8%	4.9%	15.4%	9.1%	8.9%	7.1%
Return on Equity	21.6%	21.2%	19.0%	17.8%	17.3%	14.7%	41.5%	24.3%	27.3%	22.2%
ROIC	10.6%	10.2%	9.6%	9.4%	9.1%	7.6%	22.1%	12.3%	12.0%	9.5%
Shares Out.	1,049	1,021	1,009	992	966	928	890	860	778	768
Revenue/Share	10.83	11.31	11.80	12.64	12.00	11.68	12.48	14.23	14.96	13.78
FCF/Share	1.10	0.58	0.94	0.89	0.82	0.68	1.57	3.36	4.00	3.43

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