



Dow Inc. (DOW)

Updated May 6th, 2021 by Josh Arnold

Key Metrics

Current Price:	\$68	5 Year CAGR Estimate:	4.4%	Market Cap:	\$49 B
Fair Value Price:	\$78	5 Year Growth Estimate:	-2.0%	Ex-Dividend Date:	05/27/21 ¹
% Fair Value:	87%	5 Year Valuation Multiple Estimate:	2.8%	Dividend Payment Date:	06/11/21
Dividend Yield:	4.1%	5 Year Price Target	\$71	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 \$48 billion in revenue this year and trades with a market capitalization of \$49 billion.

Dow reported first quarter earnings on April 22nd, 2021, with results coming in well ahead of expectations on both the top and bottom lines. The company saw huge gains in revenue and earnings mostly from a combination of strong demand and renewed pricing power.

Earnings were up nearly 300% from the same period a year ago, with GAAP earnings at \$1.01 billion and \$1.32 per share, while the year-ago period saw respective comparables of \$258 million and 32 cents. Total revenue also soared 21% to nearly \$12 billion. Operating EBITDA was up 45% to \$2.27 billion.

The company saw strength in all of its segments, with packaging and specialty plastics soaring 32% year-over-year to \$6.08 billion. Industrial intermediates and infrastructure revenue was up 18% to \$3.61 billion, while the performance and coatings business was up a modest 3% to \$2.12 billion.

Local pricing soared 19% from the year-ago period as supply constraints helped drive massive pricing growth.

Given these factors, we've increased our estimate of earnings-per-share for this year to \$6.00, but note that the factors driving this performance are very unlikely to be repeated in subsequent years.

Growth on a Per-Share Basis

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
EPS	---	---	---	---	---	---	---	\$3.99	\$3.49	\$1.66	\$6.00	\$5.42
DPS	---	---	---	---	---	---	---	---	\$2.10	\$2.80	\$2.80	\$2.80
Shares²	---	---	---	---	---	---	---	747	743	745	747	600

We have reduced our earnings growth estimate once again, this time from 4% to -2%, as Dow's base of earnings is much higher for 2021. We also note that earnings growth for Dow and its predecessor companies has generally been a challenge, even under good conditions. With enormous pricing power helping drive results this year, we see it as very likely that 2021 marks a top in earnings for the foreseeable future.

Gains can accrue in the coming years from stabilized pricing, which management believes will continue to 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 under normalized conditions, but we see normalized pricing as offsetting these factors in 2022 and beyond. 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 Estimated date

² 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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The dividend was initiated at \$2.80 annually, good for a 4.1% yield on today's share price. However, given the protracted weakness in earnings, we believe the dividend will remain flat for the foreseeable future.

Valuation Analysis

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	Now	2026
Avg. P/E	---	---	---	---	---	---	---	---	14.4	26.5	11.3	13.0
Avg. Yld.	---	---	---	---	---	---	---	---	4.2%	6.4%	4.1%	4.0%

Since Dow only recently began trading on its own, there is no history in which to compare the current valuation. We see 13 times earnings as a reasonable valuation. That compares favorably to the current valuation of 11.3 times earnings, which implies the stock is undervalued. However, we note that expectations are currently for lower earnings after 2021, so the stock isn't quite as cheap as it appears. The yield is now down to 4.1% as well, so Dow's appeal as a pure income stock has waned with the recent rally.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
Payout	---	---	---	---	---	---	---	---	60%	169%	47%	52%

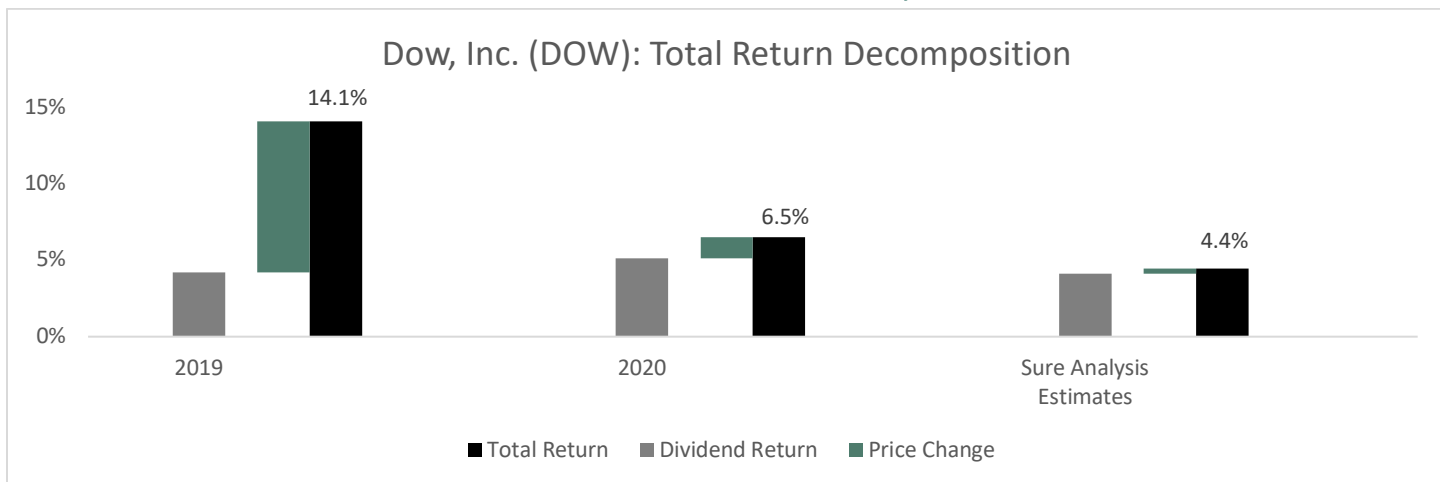
Dow's payout ratio is currently at 47% of estimated earnings. We think dividend raises will be tough to come by in the coming years, even as earnings are forecast to be quite strong this year.

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. 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 just 4.4% total returns in the coming years, consisting of the ample yield, but earnings peaking in 2021. Dow's earnings outlook has improved since our last update, and we're reiterating the stock at a hold rating. The safety of the dividend appears to have improved with the 2021 outlook. However, we are very cautious on the company's ability to grow earnings from extremely high levels in 2021.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Revenue	---	---	---	---	---	48,158	55,508	60,278	42,951	38,542
Gross Profit	---	---	---	---	---	10,490	11,896	12,573	6,294	5,196
Gross Margin	---	---	---	---	---	21.8%	21.4%	20.9%	14.7%	13.5%
SG&A Exp.	---	---	---	---	---	4,066	3,602	2,846	1,590	1,471
D&A Exp.	---	---	---	---	---	2,862	3,155	3,329	2,938	2,874
Operating Profit	---	---	---	---	---	4,287	6,022	7,569	3,520	2,556
Operating Margin	---	---	---	---	---	8.9%	10.8%	12.6%	8.2%	6.6%
Net Profit	---	---	---	---	---	4,318	466	4,499	-1,359	1,225
Net Margin	---	---	---	---	---	9.0%	0.8%	7.5%	-3.2%	3.2%
Free Cash Flow	---	---	---	---	---	-6,948	-8,102	1,336	3,969	4,839
Income Tax	---	---	---	---	---	9	2,204	1,285	470	777

Balance Sheet Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Total Assets	---	---	---	---	---	---	79,940	77,378	60,524	61,470
Cash & Equivalents	---	---	---	---	---	---	6,188	2,669	2,367	5,104
Accounts Receivable	---	---	---	---	---	---	7,338	8,246	4,844	4,839
Inventories	---	---	---	---	---	---	8,376	9,260	6,214	5,701
Goodwill & Int. Ass.	---	---	---	---	---	---	19,487	18,761	12,555	12,260
Total Liabilities	---	---	---	---	---	---	52,931	49,409	46,430	48,465
Accounts Payable	---	---	---	---	---	---	5,360	5,378	3,889	3,763
Long-Term Debt	---	---	---	---	---	---	21,001	19,899	16,996	17,107
Shareholder's Equity	---	---	---	---	---	---	25,823	26,831	13,541	12,435
D/E Ratio	---	---	---	---	---	---	0.81	0.74	1.26	1.38

Profitability & Per Share Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Return on Assets	---	---	---	---	---	---	---	5.7%	-2.0%	2.0%
Return on Equity	---	---	---	---	---	---	---	17.1%	-6.7%	9.4%
ROIC	---	---	---	---	---	---	---	9.4%	-3.4%	4.0%
Shares Out.	---	---	---	---	---	747	748	747	743	745
Revenue/Share	---	---	---	---	---	64.21	74.01	80.37	57.85	51.92
FCF/Share	---	---	---	---	---	-9.26	-10.80	1.78	5.35	6.52

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

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