Union Pacific Corporation

Union Pacific Railroad Company is the principal operating company of Union Pacific Corporation. One of America's most recognized companies, Union Pacific Railroad Company links 23 states in the western two-thirds of the country by rail, providing a critical link in the global supply chain. The Railroad's diversified business mix includes Agricultural Products, Energy, Industrial and Premium. Union Pacific serves many of the fastest-growing U.S. population centers, operates from all major West Coast and Gulf Coast ports to eastern gateways, connects with Canada's rail systems and is the only railroad serving all six major Mexico gateways. Union Pacific provides value to its roughly 10,000 customers by delivering products in a safe, reliable, fuel-efficient and environmentally responsible manner.

Union Pacific Corporation was incorporated in Utah in 1969 and maintains its principal executive offices at 1400 Douglas Street, Omaha, NE 68179. The telephone number at that address is (402) 544-5000. The common stock of Union Pacific Corporation is listed on the New York Stock Exchange (NYSE) under the symbol "UNP".

Comparative Analysis Chart A

Item	Canadian Pacific Railway	Canadian National Railway
A. Showing the effect of general improvement:		
Average Price of Common, 2012	80	42
Earned Per Share, 2012 (adjusted)	$3.7	$4.2
% Earned on market price, 2012	4.63%	10%
Fixed charges earned, 2012	0.19 times	0.77 times
Ratio of gross to market value of common, 2012	19.6%	27.1%
Increase in gross, 2014 over 2012	16.24%	22.3%
Earned per share of common, 2014	$11.8	$5.32
Increase in earnings of common, 2014 over 2012	218.92%	26.67%
Average price of common, 2014	177	63
Increase in average price, 2014 over 2012	121%	50%
B. Showing the effect of a general decline in business:		
Average Price of Common, 2007	64	25
Earned Per Share, 2007 (adjusted)	$6.98	$5.4
Earned on average price, 2007	10.91%	21.6%
Fixed charges earned, 2007	0.45 times	0.73 times
Ratio of gross to market value of common, 2007	48%	63%
Decrease in gross, 2009 below 2007	9.4%	7.2%
Earned on common, 2009	$3.7	$4.82
Decrease in earnings for common, 2009 below 2007	88.6%	33.33%
Average price of common, 2009	40	22
Decrease in average price, 2009	60%	13.63%

below 2007		

Chart B

Item	CSX Transportation	Union Pacific Corporation
A. Showing the effect of general improvement:		
Average Price of Common, 2012	21	58
Earned Per Share, 2012 (adjusted)	$2.86	$6.68
% Earned on market price, 2012	13.62%	11.42%
Fixed charges earned, 2012	0.37 times	0.48 times
Ratio of gross to market value of common, 2012	54%	35.9%
Increase in gross, 2014 over 2012	7.7%	14.6%
Earned per share of common, 2014	$3.1	$9.3
Increase in earnings of common, 2014 over 2012	8.4%	39.2%
Average price of common, 2014	30	101
Increase in average price, 2014 over 2012	42.9%	74%
B. Showing the effect of a general decline in business:		
Average Price of Common, 2007	14	28
Earned Per Share, 2007 (adjusted)	$4.5	$5.66
Earned on average price, 2007	32.14%	20.21%
Fixed charges earned, 2007	0.28 times	0.24 times
Ratio of gross to market value of common, 2007	17%	50%
Decrease in gross, 2009 below 2007	10.94%	15.8%
Earned on common, 2009	$4.5	$5.94
Increase in earnings for common, 2009 below 2007	0%	4.95%
Average price of common, 2009	12	26
Decrease in average price, 2009	16.67%	7.7%

below 2007		

Chart C

Item	Canadian National Railway	Union Pacific Corporation
A. Showing the effect of general improvement:		
Average Price of Common, 2012	42	58
Earned Per Share, 2012 (adjusted)	$4.2	$6.68
% Earned on market price, 2012	10%	11.42%
Fixed charges earned, 2012	0.77 times	0.48 times
Ratio of gross to market value of common, 2012	0.1%	35.9%
Increase in gross, 2014 over 2012	22.3%	14.6%
Earned per share of common, 2014	$5.32	$9.3
Increase in earnings of common, 2014 over 2012	26.67%	39.2%
Average price of common, 2014	63	101
Increase in average price, 2014 over 2012	50%	74%
B. Showing the effect of a general decline in business:		
Average Price of Common, 2007	25	28
Earned Per Share, 2007 (adjusted)	$5.4	$5.66
Earned on average price, 2007	21.6%	20.21%
Fixed charges earned, 2007	0.73 times	0.24 times
Ratio of gross to market value of common, 2007	63%	50%
Decrease in gross, 2009 below 2007	7.2%	15.8%
Earned on common, 2009	$4.82	$5.94
Increase in earnings for common, 2009 below 2007	33.33% (*d*)	4.95%
Average price of common, 2009	22	26
Decrease in average price, 2009	13.63%	7.7%

below 2007		

Conclusions From Comparative Analysis

This beginning section of the analysis of Union Pacific Corporation began with an analysis of other public railroad companies in the industry.

Chart A:
The first companies that were reviewed through comparative analysis were that of the Canadian Pacific Railway (CP) and the Canadian National Railway (CNI). In this chart, we can see that Canadian National is superior. During a time of general business improvement, CP was classified as a speculative issue. This is due to the fact that it was trading at 21x earnings, and also based on the fact that its earnings increased excessively, compared to that of CNI. On the other hand, CNI was a conservative issue, based on the fact that it was trading at merely 9x earnings, and based on the fact that its earnings did not increase speculatively. Also, during this time, CNI held a better earned on common percentage, along with better fixed charges earned, ratio of gross to market value of common, and increase in gross. CP only shined when it came to earnings growth and share price growth. During a general decline in business, CNI proved better. It again held the best earned on average price percentage, fixed charges earned, and ratio of gross to market value of common. Canadian Pacific did not prove better at generating money. While both lost revenue, earnings, and share value, CP lost excessively more. Compared to Canadian National, Canadian Pacific's gross decreased by an extra 2.2%, its earnings fell by an extra 55.27%, and its earnings fell by an extra 46.37%. Canadian Pacific’s massive upward movements were matched with massive downward movements. Therefore, I deem that Canadian National Railway is superior to Canadian Pacific. It may be argued that while the upward movements were matched with downward movements, the upward movements allowed the company to expand. While this may be true in other cases, it seems not true in this case. This is because the Canadian Pacific did not seem to grow. In 2012-2014, after the world economy had recovered from the recession, Canadian Pacific had worse, for example, fixed charges earned than in 2008. In addition, Canadian Nationals network is more diversified than that of Canadian Pacific’s.

Chart B:
Now onto the other side of the bracket, Union Pacific Corp, and CSX Transportation. One of the first things I noticed while looking at CSXs map is that it had a large trucking section. This is not favorable, as one talking point of railroads is that they are more fuel efficient than trucks. During a general increase in business

activity, CSX only has 2 points that were better than UNP, which were that it had a better ratio of gross to market value of common, along with a better % earned on common. UNP dominated, with 4 positive points, which included better earnings increases, better price increases, better gross increases, and a better fixed charges earned ratio. During a general decline in business, CSX had 4 positive notes, which were that it had better fixed charges earned, lighter decreases in gross,a better ratio of gross to market value to common, and better earnings on the average price. However, on Union Pacific's side, there were only 2 positive notes, which were that it made a profit, and that its share price did not decrease as much. Totaling these up, Union Pacific had 6, and CSX had 6. Despite the points being equal, I believe that Union Pacific is superior. It focuses more on railroad, and less on trucking. Also, the fact that UNP had earnings growth during the financial crisis of 2008 surely adds more than one point. Lastly, Union Pacific has a far vaster railroad than CSX, which means that UNP always will earn more than CSX. Overall, my consensus is that Union Pacific is superior.

Chart C:
Lastly, the final comparative chart. This one is between the two superior companies of the other two charts, Union Pacific Corporation and Canadian National Railway. During the industrial expansion during the years 2012-2014, Canadian National had 2 positive notes. These were that CNI had a better fixed charges earned, along with a better increase in gross. However,UNP had a total of 4 positive notes during this time period. During the financial crisis of 2007-2009, CNI had 4 positive notes, which were that it had better fixed charges earned, better ratio of gross to market value of common, a lighter drop in gross, and more earned on average market price. Union Pacific had 2 positive notes, which were that it had a lighter price decrease, along with an increase in earnings. This resulted in a total of 6 positive notes each. Although these are equal, Union Pacific still is better. One other positive note that could be made on Union Pacific is that it utilizes speculative increases in earnings and price to grow the company. After the economy recovered from the financial crisis, the number of times that its fixed charges were earned doubled. Also, Union Pacific is larger than Canadian National, which means more revenue. Therefore, I conclude that Union Pacific is the best of all these. But, before any conclusions can be drawn, full-blown quantitative and qualitative studies must be initiated. This is what is contained in the rest of this document. If the studies fail to produce positive results, then quantitative and qualitative studies will be done on the Canadian National Railway.

Quantitative Study

Financial Metrics

	2019	2018	2017	2016	Average	Trend
ROE	32	29	43	21	31.25	Good
ROIC	14	14	26	12	16.5	Good
Fixed Charges Earned	0.7	0.65	1.23	0.5	0.77	Good
Net deductions earned	1.25	1.23	2.32	1.11	1.5	Good
Earnings Coverage	10.12	11.94	7.33	14.32	10.93	Bad

Income Statement Analysis

(Per Share)	2019	2018	2017	Average	Trend
Net Income	$8.41	8.5	15.23	10.71	Bad
Adjusted Net Income	$8.41	8.5	10.85	9.25	Bad
Revenue	$30.86	32.5	30.2	31.2	OK
Owner Earnings	$6.55	7.1	13.1	8.92	Bad

Balance Sheet Analysis

	2019	2018	2017	% Change
Cash Per Share	$1.18	1.81	1.82	54% (*d*)
Asset:Liabili	1.42	1.53	1.8	26.8% (*d*)

ty				
Debt:Equity	1.4	1.1	0.7	100%
Book Value	$73.1	68.32	62.7	16.6%
Liquidation Value	$46.3	45.23	44.5	4%
Acid Test	Fail	Fail	Fail	-
Surplus	$48,605	45,284	41,317	17.64%

Conclusions – Income Statement & Financial Metrics

Both the net income and the adjusted net income showed a decline over the past 3 years. This is not seen as unfavorable, in my eyes.

After seeing the growth of the Dow Jones, and combining that with my knowledge that Union Pacific has been around since the 1860s, I find this as an opportunity. Look at all the declines the market has had. But railroads held strong; they are the backbone of the American Economy. However, before I can conclude that now is a perfect buying opportunity for UNP, I must confer with the balance sheet to see if the the company is financially stable. It is also important to note that the company has paid a dividend every year since about 1900. Beyond the declines, ROE, ROIC, Fixed Charges Earned, and Net Deductions earned increased for 4 years.

Conclusions – Balance Sheet

From this, I can conclude that Union Pacific is financially sound. Although it does not have an asset:liability ratio of 2 currently, I think it can easily return to that. And even if it stayed at 1.42, the stability of the railroad industry will compensate for it. This table comes to show even more that there is a possible buying opportunity in this stock. Also, Union Pacific has an ultra-conservative capital structure. This is common with railroads, and I believe that this is acceptable for UNP. Union Pacific’s Return on invested capital has not been great since Lance Fritz’s assumption as CEO of UNP. However, it may be said that during this time, there has always been a crisis going on. Industrials are in a recession. However, I think it will most likely work out in the future.

Qualitative Study

Management and Reputation

Union Pacific has a good reputation. According to Fortune Magazine, Union Pacific was ranked #1 in:

- People management
- Innovation
- Use of corporate assets
- Social responsibility
- Quality of management
- Financial soundness
- Long-term investment value
- Quality of products/services
- Global competitiveness

Although some employee reviews are not excellent, that is to be expected in railroad companies. Many of UNP’s peers experience the same thing.

Competitive Conditions

According to Union Pacific’s 10k:

We are subject to competition from other railroads, motor carriers, ship and barge operators,and pipelines. Our main railroad competitor is Burlington Northern Santa Fe LLC. Its primary subsidiary, BNSF Railway Company (BNSF), operates parallel routes in many of our main traffic corridors. In addition, we operate in corridors served by other railroads and motor carriers. Motor carrier competition exists for all four of our commodity groups (excluding most coal shipments). Because of the proximity of our routes to major inland and Gulf Coast waterways, barges can be particularly competitive, especially for grain and bulk commodities in certain areas where we operate. In addition to price competition, we also face competition with respect to transit times, quality and reliability of service from motor carriers and other railroads. Motor carriers in particular can have an advantage over railroads with respect to transit times and timeliness of service. However, railroads are much more fuel-efficient than trucks, which reduces the impact of transporting goods on the environment and public infrastructure, and we have been making efforts to convert certain truck traffic to rail. Additionally, we must build or acquire and maintain our rail system; trucks and barges are able to use public rights-of-way maintained by public entities. Any of the following could also affect the competitiveness of our transportation services for some or all of our commodities: (i) improvements or expenditures materially increasing the quality or reducing the costs of these alternative modes of transportation, (ii) legislation that eliminates or significantly increases the size or weight limitations applied to motor carriers, or (iii) legislation or regulatory changes that impose operating restrictions on railroads or that adversely affect the profitability of some or all railroad traffic. Finally, many movements face product or geographic competition where our customers can use different products (e.g. natural gas instead of coal, sorghum instead of corn) or commodities from different locations (e.g. grain from states or countries that we do not serve, crude oil from different regions). Sourcing different commodities or different locations allows shippers to substitute different carriers and such competition may reduce our volume or constrain prices. For more information regarding risks we face from competition, see the Risk Factors in Item 1A of this report.

Future Prospects (Probable Changes in volume, price, cost, etc.)

It is likely that a recession is upcoming in the economy. Therefore, Union Pacific can get an amazing jumpstart, which could possibly lead to massive growth in the company. However, through careful examination of Union Pacific’s history, holders, and other factors, I find a weakness in the future prospects of this company. The company Blackrock has full control over the company. That means that they can authorize massive stock buybacks to pump up the stock. Additionally, I wouldn’t be able to build a big stake in it if it is mostly controlled by Blackrock. Lastly, I must determine an intrinsic value using a Discounted Cash Flow Model.

Intrinsic Value Model

Growth Rate of FCF - 7%

Discount Rate - 10%

Infinite Growth Rate - 3%

Future Cash Flows -

2020	2021	2022	2023	2024
7.8217	8.369219	8.95506433	9.581918833	10.25265315

Discounted Cash Flows - 33.66608911

Terminal Value - 150.8604678

Intrinsic Value - 145

True Intrinsic Value - 191

Note 1. Growth Rate of FCF

For this figure, I initially chose 8%, which was the average of the growth rate of surplus for the past three years. I drained it down to 7% since most employees hate their jobs. This is not exactly a big factor, but just a possibility that workers will strike in the future.

Note 2. Discount Rate

This is the standard discount rate used to for this formula. Long term treasuries would currently make the intrinsic value of this company negative, which is clearly not true.

Note 3. Infinite Growth Rate

This is assuming that Union Pacific can grow as fast as the economy for the rest of its lifetime. However, this is a conservative number.

Note 4. True Intrinsic Value

This is equivalent to Intrinsic Value + Liquidation value + Cash. I believe that liquidation value adds value that cannot be calculated using this formula. (Cash excluded - only $1)

Note 5. Conclusion

Union Pacific can be bought once it has reached significantly below 145, and once it is trading at less than 20x earnings.

Final Results

Pros

- Margin of Safety
- Good Results

Cons

- Lots of long term debt
- Not as much market share as BNSF
- ‘Vulture Capitalism’ by Black rock

From this study, I can conclude that Union Pacific will not be bought until there is some sort of restructuring in the company. The company could be prone to ‘Vulture Capitalism’, brought on by collaboration between the new COO and it’s major holder, Blackrock. I will have to see what happens after the markets hit bottom in roughly 2023. So, in 2023-2024, if Blackrock is not a major holder and the financial condition is OK, then I would be fine purchasing this.