



BRADLEY JOHNSON & WILL KRULL

KIANA CANON, JACOB MAURER, & AUSTIN PREECE

**Sector:** Materials

**Industry:** Chemicals

**Ticker:** ECL

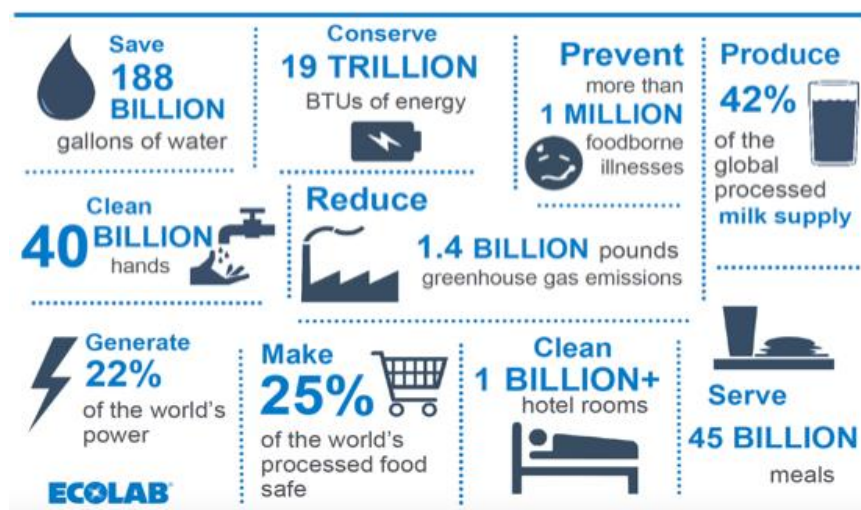
## COMPANY OVERVIEW

Ecolab is the global leader in water, hygiene and energy technologies and services that protect people and vital resources. Founded in 1923 as a detergent manufacturer and going public in 1957, Ecolab has grown to a large chemical company, with no direct competitors.

Ecolab is involved in more of a person's life than most know or would guess. The food we eat, the energy we use, the water we drink, and the environments in which we live, work, and play are all made cleaner, more sustainable, and cheaper by Ecolab.

One of Ecolab's slogans is "Clean Water, Safe Food, Abundant Energy, Healthy Environments;" if it doesn't have to do with any of the four, Ecolab has nothing to do with it. These are the areas they find and provide solutions for. Ecolab provides these solutions in a variety of different ways - from water treatment chemicals to surgical drapes.

## LAST YEAR, ECOLAB HELPED:



*Excellence. Our Measure. Our Motto. Our Goal.*

### **AWARDS:**

Ecolab often receives well accredited and highly competitive awards in numerous categories such as employer/diversity, sustainability, and ethics. So far in 2019, Ecolab has received five employer/diversity awards, two sustainability awards, and four ethics awards.

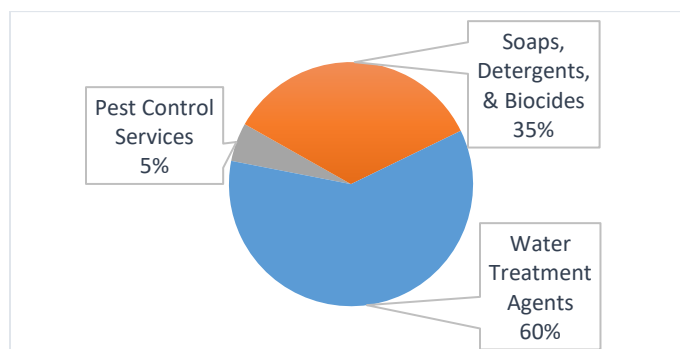
### **CUSTOMER SEGMENTS:**

Ecolab works with customers in more than 40 industries, those industries are broken down by the following customer segments:

- Industrial: Servicing manufacturing, mining, and transportation plants to increase efficiency and hygiene levels.
- Institutional:
  - Industries: Foodservice, Hospitality, Building and Facilities, Retail, and Healthcare
  - Top products and services offered: Cleaning and Sanitization Chemicals, HVAC Improvement Products, and Monitoring Programs.
- Energy:
  - Helping numerous types of energy companies be more efficient through proper care and analysis of their systems. A majority of this segment is serviced by their Nalco water division, which Ecolab acquired in 2011.
  - Top products and services offered: Corrosion Control, Fuel Additives, Inventory Management, Fuel Stabilizers, Raw and Wastewater Treatment, Cooling Tower Water Treatment, and Correlated Data and Actionable Insights.
- Other: Less common product offerings such as materials specially designed for the cleaning of electronic components.

### **PRODUCT SEGMENTS:**

Ecolab's core technologies and offerings include digital solutions, antimicrobials, dispensing and monitoring, personal and environmental hygiene, polymers, surfactants, solid chemistry, water management, and data analytics.



## INVESTMENT THESIS

We recommend a **BUY** for ECOLAB at \$186 for the following reasons:

- Ecolab's ability to consistently outperform the market.
- Ecolab's ability to innovate and provide unique solutions to their broad, global, customer base.
- Institutional holders of Ecolab stock are increasing their positions.
- Ecolab's sub-industry dominance, having zero direct competitors.
- Ecolab has defensive and low-volatility characteristics that take advantage of market expansions and contractions.

## KEY DRIVERS

### INCREASING GLOBAL DEMAND:

Global demand for Ecolab's solutions is rising. In just ten years the world will need 40% more freshwater, 35% more food, 25% more energy, and more ways to stop the spread of disease. As the population grows, and countries continue to develop, demand for Ecolab's products and services will continue to increase.

A lot of their demand comes from increasing regulation. An example of this in the United States is waste treatment chemicals. Municipalities are one of the fastest-growing customers in need of these chemicals. This demand is stemming from the Environmental Protection Agency adding regulations to make our cities' water cleaner. The EPA estimates that US cities will spend 600 billion over the next two decades on replacing and improving their wastewater treatment areas.

### INNOVATION:

Ecolab is constantly innovating; they employ 1,600 scientists who are constantly creating new and more efficient solutions for their customers. They currently have over 9,400 active patents that help protect their market. A lot of their innovation is driven by their company culture. For their scientists and engineers, they have a wall displaying all the patents that each individual is responsible for. They also use everyone at Ecolab to help drive innovation. For example, interns are not simply tasked with getting coffee, they are used as idea generators and utilized to help drive sales growth.

One area that Ecolab has been shifting its investments is into digital solutions. One example is the hand hygiene compliance program for hospitals. It is a wearable device for nurses that will alert them if they have not washed their hands and are entering a patient zone. Another example is a "smart" dishwasher that can be connected to an app to track water usage and alert of unsafe temperature levels.

### SUSTAINABILITY:

Ecolab recently announced their pledge to cut their carbon emissions to half of their current amount and down to zero by 2050. They plan to do this by switching all their company vehicles to electric, using

100% renewable energy (99% of Europe operations are already from renewable energy), expanding their energy efficiency projects and innovations, and influencing their suppliers to adopt similarly ambitious climate goals.

Striving for and achieving such ambitious carbon footprint goals not only improves efficiency, reduces costs, and increases competitive advantage, it also puts them ahead of likely future climate regulations on large corporations, reducing the potential damage that would be caused by a blindside hit from government regulations.

## **VALUATION**

To find an intrinsic value of Ecolab's stock we used two valuation methods – a discounted cash flow model and economic value-added. We weighted each at 50% as we thought that they both were valid and provided equal explaining power. Using these methods, our target price for Ecolab is \$217.50. To provide a target price range, we ran each of the two valuation methods twice, with the independent variable being WACC, testing it at 6% and 6.5%. This provided us with a target price range of \$203.50 - \$231.

### **DISCOUNTED CASH FLOWS MODEL:**

In our discounted cash flows model we used a WACC of 6% and 6.5%. For the perpetual growth rate, we used 4% which was the commonly accepted rate for Ecolab. We projected the short-term cash flows and revenue by using Ecolab's previous growth rates over the past 7 years.

### **EVA METHOD:**

The EVA program used market-implied EVA margins. We input a sales growth rate of 5.5% and WACC at 6% & 6.5%. We found a reasonable target price to be \$202 and a target price range of \$195 – 209.

## **RISKS**

### **COMMODITY PRICES:**

Like any company in the materials sector, Ecolab is affected by fluctuating commodity prices. Ecolab has no control of their raw material costs but one way they are combatting their input costs is by producing the majority of their goods in the country they are selling it in. For example, 90% of the products they sell in China are produced in China.

They play such a large role in their customers' supply chain that their customers switching costs are high; there are also not other companies that can handle the size of the customers Ecolab serves. They also operate in a very regulated industry, so, many times, the last thing their customers will cut spending on is the products and services Ecolab is offering. The switching costs and regulations give Ecolab enough ability to flex their prices so that the commodity prices have low significance on Ecolab

## **CONSOLIDATION OF CUSTOMERS:**

Customers in most industries that Ecolab serves have consolidated in recent years and that trend will likely continue. Consolidations have the potential to cause an adverse impact on Ecolab's ability to retain customers and may hurt margins in addition to their consolidated results of operations.

## **PERFORMANCE**

### **MANAGEMENT:**

Ecolab has benefitted from having excellent leaders. The leadership team has helped turn Ecolab into a global chemical powerhouse and also one of the best places to work in the world.

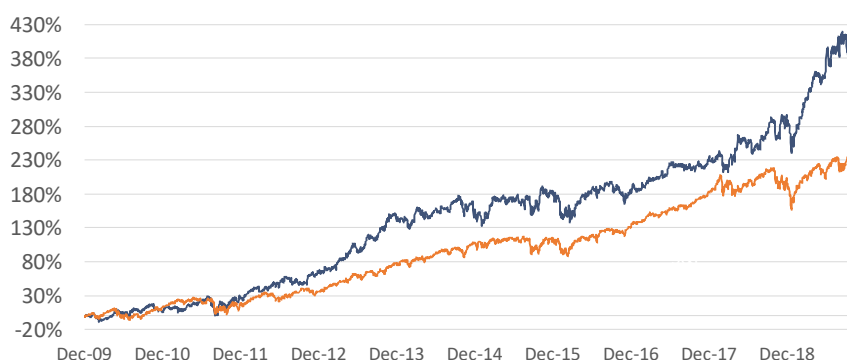
Their Chairman and CEO is Douglas Baker. He has been with Ecolab since 1989 and has been CEO since 2004. Since the beginning of his tenure as CEO, the stock has seen an increase of 517%. Recently on November 22<sup>nd</sup>, 2019, he was presented with the inaugural Dayton Award. This award recognizes businesses in Minnesota which are practicing moral capitalism and corporate responsibility.

Their President and COO is Christophe Beck. He has been with the company since 2007 and was promoted to his current position earlier this year after shadowing the previous President and COO. He has held many leadership positions such as overseeing Ecolab's \$5.4 billion acquisition of Nalco. Beck has been praised for his innovative thinking and excellent execution capabilities in the past; earlier in his career he was nominated as a Young Global Leader of the World Economic Forum.

### **STOCK PERFORMANCE:**

Ecolab's diverse product and customer portfolio make it is a defensive player in the market. Especially since most of Ecolab's product and service offerings are relatively inelastic, and 90% of Ecolab's revenue is recurring. Ecolab has historically outperformed the market with low volatility. Their 52-week beta being 0.73 which places it in the top 2% for the least volatile companies in the materials sector.

Ecolab's recent downtrend in performance is due to the market correction in addition to missing their past 4 sales estimates (by about 1% each time). Ecolab consistently beats EPS estimates, beating quarterly EPS estimates consistently including 9 out of the last 10.



### PEER ANALYSIS:

Ecolab's competitors are generally smaller companies that compete with a few product line offerings of Ecolab's. So, we decided to compare them to other large chemical companies with similar market caps in different chemical sub-industries.

|                                   | Market Cap (M)  | EBIT (M)       | P/E          |
|-----------------------------------|-----------------|----------------|--------------|
| <b>ECOLAB®</b>                    | <b>\$54,835</b> | <b>\$2,101</b> | <b>30.19</b> |
| <b>Peer Average</b>               | <b>\$51,535</b> | <b>\$2,811</b> | <b>31.35</b> |
| <b>Sherwin-Williams</b>           | \$54,683        | \$2,185        | 33.72        |
| <b>Dupont</b>                     | \$48,357        | \$4,128        | 32.41        |
| <b>Air Products and Chemicals</b> | \$51,566        | \$2,121        | 27.93        |

### OWNERSHIP OF ECOLAB

1. Cascade Investment LLC
  2. The Vanguard Group, Inc.
  3. BlackRock Fund Advisors
  4. SSgA Funds Management, Inc.
  5. Morgan Stanley Investment Management, Inc.
- Of the top 15 institutional holders, 13 have been increasing their position in Ecolab.
  - Of the top 5 insiders/stakeholders, all 5 have been increasing their position in Ecolab.

#### Ownership Statistics



SHARES OUTSTANDING  
**288,244,000**  
89.10% TOTAL OWNERSHIP

- 88.50% Inst. Ownership
- 38.31% Top 10 Inst. Holders
- 0.59% Insider Ownership
- 10.91% Unknown