



Forbes

SPECIAL SITUATION SURVEY



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Forbes

SPECIAL SITUATION SURVEY

Special situation investing is like venture capitalism. From the broad spectrum of possibilities, only those with the greatest promise are selected. However, with greater potential for reward, there is usually also greater risk. But by rigorously cutting out investments falling short of expectations and taking profits where indicated, risk can be moderated without diminishing ultimate reward. We believe the investor willing to reduce exposure to less promising stocks even if this means sometimes selling at a loss and concentrating investments in the most promising situations will over the long run prove to be the most successful.

June 14, 2021

Huntsman Corporation	
Ticker symbol	HUN
Recent price	\$27.22
52-week price range	\$16.74 to \$32.35
Consensus 2021 earnings estimate	\$2.66
Consensus 2022 earnings estimate	\$2.88
Price-to-expected earnings multiple	10 x fiscal 2021 estimate
Indicated dividend	\$0.75
Current yield	2.8%
Market capitalization	\$6.03 billion
Industry	Diversified Chemicals

If you need an example of the influence carried by analysts from big financial institutions, look no further than what occurred with shares of diversified chemicals company, Huntsman, since its Q1 earnings announcement on April 30. Specifically, after being up over 10% and hitting a new 52-week high less than two weeks later on the strength of this favorable report, a downgrade by Goldman Sachs the next day triggered a sharp reversal that now has it down 16% from this level.

Yet while we agree that the sustainability of the favorable pricing/input cost dynamics HUN has enjoyed over the past several quarters—which appear to be the primary rationale behind this downgrade—is a legitimate concern, it’s also a perpetual one that’s been around as long as the company due to the unpredictable and often volatile nature of energy-based commodity prices that doubly affect profits by impacting both the cost of key raw materials and what HUN can charge for its own products. This is a big reason why shares of chemical producers have historically traded at a discount to the overall market and why its own stock was selling at just 12 times its current-year earnings estimate even at its high.

Thus, the slide in HUN’s stock since then, which now has it trading at an even lower forward P/E of just 10, seems wholly unmerited. This is even truer when you consider that the strong start to 2021 signaled by its better-than-expected Q1 results, along with the ongoing recovery in many of its markets, the expected rebound in demand from the important aerospace market, increasing synergies from key acquisitions made over the past year and the additional benefits from a cost optimization plan currently in place, had most analysts greatly revising their initial 2021 earnings estimates upward. This includes the expectation for sequential adjusted EBITDA growth of as much as 25% in its various segments in the current quarter.

Had there been an adverse development that materially reduced HUN’s ability to deliver on this goal, perhaps the recent drop in its share price would be appropriate. But to the contrary, the only news of note are the hiring of a well-qualified new CFO and the decision to greatly increase existing capacity for a key product that’s likely to see increasing demand from the fast-growing electric vehicle (EV) market—both of which should be viewed positively. More importantly, with these only adding to an already impressive list of reasons why HUN’s operations should continue to impress, we’re optimistic that the latter will help drive up its shares from their currently depressed level and to our target price of \$38 within two years.

THE COMPANY

Huntsman Corporation is a leading global producer of differentiated organic chemical products. Its offerings—which include MDI (methylene diphenyl diisocyanate), amines, maleic anhydride, epoxy-based polymer formulations and textile chemicals used in numerous applications, such as those in the adhesives, aerospace, automotive, construction, consumer products, electronics, insulation, medical, packaging, coatings, power generation, refining, synthetic fiber, textile chemicals and dyes industries.

HUN caters to a very diverse customer base that includes Andercol, Azelis, Bayer, BMW, Bosch, Chevron Oronite, Cytec, Dixie, DuPont, Electrolux, Firestone, Freeman, Fruit of the Loom, Guilford Mills, Haier, Hanesbrands, Henkel, Hexcel, Hexion, Ingevity, Lear, Louisiana Pacific, Lubrizol, MFG Chemical, Olin, PPG, Schneider, Sherwin-Williams, Siemens, Syngenta, Tate & Lyle, Quadra, Viasystems and Y.R.C. Textiles. Key competitors consist of 3M, Archroma, Bartek BASF, Cardolite, Delamine, Dow, DuPont, DyStar, Eastman, Elantas, Evonik, Henkel, Hexion, INEOS, Jihua, Kukdo, Lanxess, Longsheng, Nicca, Nouryon, Olin, Runtu, Sika, Sumitomo, Transfar/Tannatex, Wanhua Chemical and Xiongrum.

Prior to COVID-19, HUN had been aggressively executing on a bold, multiyear strategic plan aimed at minimizing the significant volatility in profits that has historically risen from cyclical changes in supply and demand and fluctuations in certain commodity prices (which impact both the cost of key raw materials it purchases and its own selling prices) in order to drive more stable earnings performance and sustainable growth. The biggest moves involved divesting low-margin product lines with limited pricing power and using the proceeds to reduce the heavy debt burden HUN accumulated over the years and selectively acquire businesses that bolster its ability to serve growing markets and provide higher-margin, value added products. This included spinning off its titanium dioxide business in August 2017, selling its chemical intermediates and its surfactants operations in January 2020, and acquiring CVC Thermoset Specialties in May 2020 and Gabriel Performance Products this past January. The latter two both augment HUN's existing portfolio of Advanced Materials solutions by adding highly specialized toughening, curing and other additives used in a wide range of composite, adhesive, sealants and coatings applications across the aerospace, automotive and industrial markets in North America, and should help offset the pandemic-driven weakness anticipated to persist in this business over the near-term.

The net result of these transactions—in particular, the divestiture of its chemical intermediates and surfactants businesses, which had generated \$1.7 billion in sales and \$360 million in EBITDA in the four quarters before this deal was announced—initially reduced the company's adjusted earnings per share to just \$1.79 in 2019 from \$3.34 in the prior year. But with the heavy lifting part of this business transformation plan mostly behind it, many were optimistic that HUN's profits would return to growth in 2020 with even stronger prospects on tap beyond it. This was clear from the pre-pandemic consensus adjusted earnings forecasts for 2020 and 2021 of \$1.89 and \$2.26 per share, which implied 5.6% growth last year and then a more than tripling in this rate to 19.6% in 2021. Unfortunately, the pandemic seemed to throw these ambitions out the window. And with growing fears over COVID-19's economic toll mounting, these estimates had sunk to just 37 cents and \$1.34 by the end of last June.

The good news is actual adjusted earnings of 98 cents in 2020 nearly tripled this pessimistic view. And like those of other firms that greatly exceeded their expectations, what began as an awful 2020 for HUN's stock—which was down nearly 50% year-to-date during the worst of the pandemic-fueled market sell-off to just \$12.23 on March 20, 2020—finished with it up 4.1% for the year overall to \$25.14.

That said, the strong rebound in HUN's shares over the rest of 2020 was built on investor goodwill. That is, many were willing to look past what was obviously going to be a very difficult year for most companies due to an anomalous and wide-reaching global crisis on the belief that the aggressive monetary and fiscal policies put in place would help minimize the immediate and sizable financial and economic fallout from it. Combined with the positive outcomes seen in the clinical trials of the multiple vaccine candidates in accelerated development, this had just about everyone expecting substantially better results in 2021.

Initially, HUN's positive Q1 announcement on April 30 appeared to extend this goodwill with its stock climbing as much as 10.2% over the next seven trading days to as high as \$32.35. But this proved short-lived as its shares have given back all of this and more and are now down 16% from this post-earnings high. What likely triggered this slide was a downgrade by Goldman Sachs on May 11, which cut its rating on several diversified chemical producers, including HUN, from Buy to Neutral on concerns over the sustainability of the strong margins these firms have recently enjoyed.

While we acknowledge this as a big risk factor borne from the unpredictability of commodity price fluctuations and the highly cyclical markets HUN serves, it's also the main reason why HUN's stock was trading at just 12.1 times its consensus earnings estimate for this year even at its high. Such a discount may have been appropriate several years back when the company was strapped with a mountain of debt and had just started its business transformation journey. However, with the increasing payoff from actions taken under this plan helping its earnings in the post-pandemic environment hold up far better than anticipated and allowing HUN to exit 2020 with virtually no net debt, that is no longer the case in our view.

Indeed, if there was anything positive to come out of the pandemic for the company, it's that it highlighted just how timely these strategic actions were, the major role they played in helping HUN's operations get through one of the worst operating environments in its history without much difficulty, and why they're likely to contribute to such strong growth over the rest of 2021 that analysts now believe adjusted earnings for the full-year will be up 171% from 2020 to \$2.66 per share. This is 20% higher than their previous view of \$2.22 and even well above their pre-pandemic forecast of \$2.26 from nearly a year-and-a-half earlier. It also implies adjusted earnings over the rest of 2021 will be 14% higher than what analysts were projecting.

So, for those taking count, HUN's profits fared much better than anticipated in the wake of the pandemic and will likely be up far more in 2021 than most. It also entered the year with arguably the healthiest balance sheet in its history and continues to have so much confidence in its future prospects that it raised its already generous dividend by 15% at the time of its Q1 report—marking only the third such increase in 14 years. Does this sound like a company whose shares should be trading at a forward P/E of just 10 and at roughly a 50% discount to the overall market? We sure don't think so. And if HUN continues to deliver favorable operating results in the periods ahead as we expect, it probably won't be for much longer.

Business Segments

Polyurethanes – The Polyurethanes segment (58.1% of Q1 revenues) manufactures polyurethane chemicals used to produce rigid and flexible foams, coatings, adhesives, sealants and elastomers. HUN focuses on the higher-margin, higher-growth markets for specialty MDI and MDI-based polyurethane systems, as they are continuing to replace traditional products in a wide range of end-use markets, including insulation in construction and appliances, cushioning for automotive and furniture, coatings, adhesives, wood binders for construction and furniture, footwear and other specialized engineering applications.

Performance Products – This segment (16.6% of Q1 revenues) produces a wide range of amines, many of which are used in epoxy curing agents, oil exploration and production, agrochemicals, and fuel and lubricant additives. It also sells maleic anhydride, a highly versatile chemical intermediate that is used to produce unsaturated polyester resins mainly needed in the production of fiberglass reinforced resins for marine, automotive and construction products, as well as lubricants, food additives and artificial sweeteners.

Advanced Materials – The Advanced Materials segment (15.1% of Q1 revenues) makes technologically-advanced epoxy, acrylic and polyurethane and acrylonitrile butadiene-based polymer products that are used to address customer-specific needs in a wide variety of industrial and consumer applications. These solutions are used either as replacements for traditional materials or in applications where traditional materials do not meet demanding engineering specifications. For example, structural adhesives are used to replace metal rivets and advanced composites are used to replace traditional aluminum panels and other steel materials to lighten structures in aerospace, automotive and other transportation.

Textile Effects – This segment (10.5% of Q1 revenues) performs wet processing of textiles across pretreatment, coloration, printing and finishing and provides a diverse portfolio of textile chemicals and dyes. Its textile solutions provide color and enhance the aesthetic, durability and performance of finished textiles, including functionality such as wrinkle resistance and water and stain repellence.

Recent Developments

On June 8, 2021, HUN announced plans to significantly increase its existing capacity for ULTRAPURE ethylene carbonate at its Conroe, Texas facility by mid-2023. ULTRAPURE ethylene carbonate is critical to the reliable operation and long working life of lithium-ion batteries for electric vehicles (EVs) and electronics. Motivated by the strong growth in ULTRAPURE ethylene carbonate tied to the evolution of EVs and the localization of lithium-ion battery production HUN has seen in recent years, this capacity expansion will leverage its position as the only U.S. producer of cyclic carbonates and support the rapid growth of the U.S. and European lithium-ion battery markets for EVs.

On June 4, 2021, HUN announced the appointment of Phil Lister as Executive Vice President and Chief Financial Officer (CFO), effective July 1, 2021. Having spent his entire 25-year career in various financial planning and operations, business management, and strategic development roles at Huntsman or its predecessors, we think Lister is well-qualified to take over for longtime company veteran Sean Douglas, who recently accepted a full-time calling to The Church of Jesus Christ of Latter-day Saints.

On May 26, 2021, HUN issued \$400 million worth of Senior Notes due 2031. The notes are intended to replace a \$400 million tranche of Senior Notes that was coming due in 2022, which will effectively extend the term of these borrowings by 9 years while reducing the rate on this debt to just 2.95% from the 5.125% it's currently paying. This should reduce annual interest expense by \$8.7 million after paying the accrued interest, premiums, fees and expenses related to the early redemption of the old notes.

Key Investment Risks

HUN's operations are highly cyclical—characterized by alternating periods of tight supply, which cause volumes, prices and margins to increase, followed by periods of lower capacity utilization, resulting in oversupply and declining prices and margins. This cycle is driven by changes in the demand for products as a consequence of global economic activity, fluctuating energy prices and shifting client requirements. For example, three of HUN's bigger markets are aerospace, housing and construction, which are usually among the most vulnerable to economic downturns. The supply-demand balance is also impacted by capacity additions or reductions that result in changes in utilization rates. Due to these factors, HUN's profits and cash flows can vary greatly from period to period and over the business cycle.

HUN purchases a substantial portion of its raw materials from third parties, which represents a significant portion of its operating expenses. Many of these costs generally follow price trends of, and vary with market conditions for, crude oil and natural gas feedstocks, which are highly volatile and cyclical. For example, the market for crude oil and natural gas feedstocks experienced depressed pricing throughout 2020, leading to favorable raw material prices. But this can also put downward pressure on selling prices for certain of HUN's products leading to reduced revenue. Thus, timing differences between raw material prices, which may change daily, and contract product prices, which in many cases are negotiated far less often, have had and may continue to have a negative effect on HUN's cash flows. This is especially true if the company is unable to pass on these cost increases to its customers as has historically been the case.

VALUING THE STOCK

Compared to its peer group of publicly-traded diversified chemicals producers shown below, HUN stacks up well with the lowest price-to-sales (P/S) ratio and the second lowest price-to-expected earnings (P/E) and price-to-book (P/B) ratios. In fact, only Covestro AG offers similarly attractive ratios across the board.

Perhaps that's why our more important discount cash flow analysis found these two as the most undervalued from the list. In fact, all things equal, this might have been a tough choice. However, what makes our decision to go with HUN an easy one is the fact that Covestro AG's shares aren't officially listed in the U.S. They trade as American Depositary Receipts (ADRs) in the over-the-counter (OTC) market, which is less regulated, less liquid, generally ignored by a large swathe of both institutional and retail investors, and therefore, offers additional risks unrelated to the company's actual fundamentals.

Company	P/E ¹	P/S	P/B
Huntsman (HUN)	10.2	0.96	1.67
Dow Chemical (DOW)	11.5	1.25	3.70
BASF (BASFY)	16.0	1.04	1.67
Covestro AG (COVTY)	9.0	0.97	1.70
Eastman Chemical (EMN)	14.4	1.99	2.73
DuPont de Nemours (DD)	21.2	2.62	1.62
Olin (OLN)	10.0	1.24	4.53
3M (MMM)	20.8	3.61	8.56

¹Based on current consensus earnings estimates for the next 12 months.

That's fine with us given how much of a bargain our analysis found HUN's stock to be following its recent slide of 16%. What's more, this proved to be the case even with the uncertainty surrounding the pace of economic recovery around the world from COVID-19 and the high cyclicity in HUN's operations necessitating an even more conservative approach to this valuation than we normally would utilize. Indeed, this is clear from our very first assumption—for net sales in the current year—which we forecast to be \$7.0 billion despite our belief that actual sales for 2021 will likely come in materially higher.

This also appears to be the general consensus with the current analysts' net sales estimate for the year standing at \$7.27 billion, which indicates year-over-year growth of 20.8% and is up from \$6.90 billion following HUN's stronger-than-expected start to the year and the favorable outlook maintained for the balance of 2021. We believe this will be supported by improving volumes over the rest of 2021 driven by rebounding demand from the hard-hit, but important aerospace market, which likely bottomed at the end of 2020, and further recovery and acceleration in demand trends already seen across many of its other markets and product lines—such automobile, construction and retail—over the rest of year.

Given the steady normalization in volumes back to pre-pandemic levels that we expect to see throughout 2021, and the tougher comparisons this should bring, sales growth will slow in 2022. That said, we also don't expect overall demand to be fully back to pre-pandemic levels until sometime next year either. Combined with an increasingly greater mix of higher-value solutions from HUN's ongoing focus on providing more differentiated solutions through new product launches (including the transition to more eco-friendly, energy efficient solutions) and contributions from selective acquisitions—such as CVC Thermoset Specialties and Gabriel Performance Products—this suggests volume growth could remain well above the pace of nominal GDP in its various markets for years, which we peg at 2% to 3%. Nevertheless, we project annual growth beyond the current year to trend at the lower end of this range.

Like the top line, there are many factors to consider in forecasting HUN's margins. The biggest determinants in our view are the positive/negative sales leverage from rising/declining volumes, the spread between selling prices and the cost of raw materials, mix of products, and how efficient its operations are overall. The first two are often driven by external factors—such as changes in overall market demand and fluctuations in commodity prices. In fact, the latter actually contributed to HUN's better-than-expected adjusted operating margin performance in 2020 since input costs fell at a faster rate than its own selling prices. And while inflationary pressures point to a less favorable spread this year, we expect such commodity price swings to have a neutral impact on margins over the longer term.

Fortunately, HUN has more direct control over its mix of products and the efficiency of its operations, which are where much of the company's business transformation efforts have been focused. Specifically,

margins in 2020 clearly benefited from the divesting of low-profit businesses and the focus on new products and acquisitions offering more differentiated and value-added solutions, as well as from the actions taken to cut the fat and drive stronger margins through investments in its manufacturing and supply chain infrastructure and cost optimizations across the enterprise. Those benefits are not only likely to persist, but their favorable impact on margins should be even more pronounced as overall market demand continues to rebound back to pre-COVID-19 levels and payback from the \$40 million in annual cost synergies projected from its recent acquisitions steadily increases.

Discounted Cash Flow Analysis

(In millions)

	2021	2022	2023	2024	2025	Terminal Value
Revenue	\$ 7,000	\$ 7,140	\$ 7,283	\$ 7,428	\$ 7,577	
Depreciation	-	-	-	-	-	
Operating expenses	6,314	6,390	6,482	6,593	6,706	
Operating income	686	750	801	836	871	
Net interest expense	60	60	60	60	60	
Taxable income	626	690	741	776	811	
Income taxes	150	166	178	186	195	
Net income	476	524	563	590	617	
Noncontrolling interest	(38)	(42)	(45)	(47)	(49)	
Projected cash flows	\$ 483	\$ 528	\$ 564	\$ 588	\$ 613	\$ 9,618
Cost of capital	8.5%	The cost of capital represents a firm's weighted-average cost of financing. Key determinants include the company's credit rating, capital structure, effective tax rate and the beta of its stock. Value of operating assets is arrived at by discounting projected cash flows at the cost of capital. Value of non-operating assets consists of HUN's equity investments. Value of firm is derived by adding these two values together. Subtracting out total debt yields value of equity. Terminal value represents cash flows projected for all years beyond 2025. Numbers may not sum due to rounding.				
Value of operating assets	8,563					
Value of non-operating assets	373					
Value of firm	8,936					
Book value of debt	1,567					
Value of equity	7,369					
Number of shares (m)	223					
Intrinsic value per share	\$ 33.05					

We believe this is why HUN is optimistic in its ability to get back to the adjusted EBITDA of \$1.16 billion it achieved back in 2018 in the current year. If so, this would likely yield an adjusted operating margin (excludes restructuring, acquisition/integration and other special costs) close to the 11.9% enjoyed back then with good potential for further margin expansion well in excess of 12% possible beyond 2021 from these ongoing and other business realignment efforts—which also include its new splitter in Geismar that will come online in 2022 and reduce annual costs by \$30 million once fully integrated and are projected to ultimately boost annual cash operating income by a total of \$120 million by 2023. Yet to be conservative, we assumed an adjusted operating margin of just 9.8% this year and have it improving to and maxing out at only 10.5% by 2025.

As for noncash items, there are several to consider. The obvious ones not already excluded from our operating margin assumptions are depreciation and amortization, which totaled \$283 million in 2020. While the \$249 million in capital spending last year indicates a net cash contribution of \$34 million, we expect expenditures and depreciation levels to largely cancel each other over the long run and assumed no lift in our projected cash flows from the addback of these noncash charges.

Another noncash item that needs to be addressed is the equity in income of investment in unconsolidated affiliates. This is just a fancy way of saying the portion of earnings from businesses HUN has a minority stake in. Yet while the earnings they produce are real and should be accounted for on the income statement, the company doesn't actually receive any cash since these earnings are retained and reinvested by these businesses. Thus, from a cash flow standpoint, this income needs to be ignored. Instead, it's more appropriate to account for these "nonoperating assets" in our model by adding HUN's latest estimate of their carrying values—which stood at \$373 million—to our total value of the firm.

Conversely, HUN also operates several joint ventures which it has direct control over, and thus, are consolidated with the rest of its operations for reporting purposes. But since it does not fully own these businesses, cash flows should only reflect the portion of profits that the company is entitled to through its controlling stake. This reduced net earnings by \$32 million in 2020. And while it's difficult to predict how these joint ventures will fare, we believe that they will grow with the overall level of net income, more or less. Thus, we have this climbing to \$38 million in 2021 and rising in line with the latter longer out.

Based on HUN's cash and debt levels of \$673 million and \$1.57 billion at the end of Q1, the interest earned on the former and paid on the latter, and assuming no material change in these balances, we estimate net annual interest expense of roughly \$55 million and modeled accordingly.

In terms of taxes, HUN's effective tax rate adjusted for special items was just 19% in 2020. But this still included several unusual tax benefits—most notably, a \$35 million credit related to the sale of its India-based DIY business—that are not likely to recur. As such, the company expects its effective tax rate to be 22-24% for the current year—with Q1 coming in right at the midpoint at 23%. Overall, we believe this range represents a good run-rate since it accounts for the biggest recurring tax consequences, such as the U.S. federal statutory rate of 21%, the slightly higher 25% rate found in its other major operating regions (China, the Netherlands, India and Luxemburg) and the minimal amount of state taxes the company has historically paid. To play it safe, we went with the higher 24% range throughout our analysis.

Despite operating in a highly cyclical industry, the beta of HUN's stock of 1.24 isn't as big as you might expect and suggests it has displayed a level of price volatility or systematic risk that is about 24% higher than the overall market in the past five years. This results in a relatively high cost of equity of almost 9%. However, HUN's beta has steadily shrunk in recent years—with its three-year beta at 1.18 and its one-year beta of 1.05 almost matching the market. If we were to go with the latter, the company's cost of equity would be less than 8%. Further factoring in HUN's cost of debt—which we calculate to be only 2.4% (or just slightly higher than the 2.3% after-tax rate implied by the 3.02% coupon on its recently priced \$400 million senior note offering)—this indicates a weighted average cost of capital (WACC) between 6.7-7.7%. And while we believe its actual WACC lies at the lower end of this range, we discounted our projected cash flows using a much higher 8.5% rate. Yet even after doing so, our analysis finds HUN's stock to be worth at least \$33.05, which is 21% higher than where it currently trades.

EARNINGS

Bolstered by recovering volumes and favorable pricing across numerous markets and regions, Q1 revenues rose 15.3% year-over-year to \$1.84 billion. This was led by the Polyurethanes segment where sales climbed 20.3% to \$1.07 billion on higher MDI average selling prices that more than offset flat volumes driven by planned downtime related to a scheduled turnaround of its Geismar, Louisiana, facility. Sales from its Performance Products segment were up 4.5% to \$305 million as higher average selling prices more than made up for lower sales volumes. Similarly, higher average selling prices and contributions from its recent CVC Thermoset Specialties and Gabriel acquisitions also outweighed volume declines and drove a 15.4% increase in Advanced Materials segment sales to \$278 million. Lastly, with higher sales volumes more than offsetting lower average selling prices, its Textile Effects segment saw a 7.2% jump in sales to \$193 million. Further aided by lower fixed costs, the adjusted operating margin expanded 361 basis points to 9.64%. As a result, adjusted net income more than doubled to \$147 million or 66 cents per share and topped the consensus estimate by 7 cents.

FINANCES

HUN's finances are in very good shape. It has sufficient short-term liquidity with a current ratio of 1.9 and \$673 million in cash at the end of Q1, and only \$57 million in debt coming due over the next twelve months. While its cash balance was down \$921 million from the \$1.594 billion it had at the end of Q1 in 2020, its debt balance also declined by \$616 million over this span to \$1.567 billion. Taken together, this marks

only a \$305 million increase in HUN's net debt to \$894 million over the past 12 months, despite the company spending a combined \$554 million to acquire CVC Thermoset Specialties Acquisition in May of 2020 and Gabriel Performance Products this past January and shelling out \$144 million in dividend payments, thanks to the solid operating cash flow produced in this span and proceeds from the sale of certain noncore businesses and its remaining stake in Venator Materials PLC. This includes a lower-than-expected use of \$115 million in free cash flow in Q1 (typically characterized by high cash use due to the seasonal buildup of inventory), which is \$21 million less than in the previous year.

As a result, HUN ended Q1 with a net leverage ratio of just 1.2, which is actually lower than the 1.5 it stood at on a pro forma basis a year earlier. Along with the decreased interest expense that should result from the company's recently announced \$400 million debt offering, it's no wonder that HUN now expects its free cash flow conversion in 2021 to be 25% of its adjusted EBITDA forecast compared to its initial estimate for 20% (and to be closer to 40% when excluding the incremental spending on growth projects, synergies and cost optimization initiatives). This also implies HUN will have no difficulty further chipping away at its debt load while funding its aggressive capital spending plan for the year and its recently raised dividend payments. For good measure, HUN can access a combined \$1.457 billion under its revolving credit facility and U.S. and European accounts receivable securitization programs to satisfy any additional liquidity needs.

DIVIDENDS

HUN pays a quarterly dividend of 18.75 cents per share, which translates into a solid annual yield of 2.8%. As not even COVID-19 was able to interrupt this payout and given the fact that HUN actually raised it by 15% in late April for just the third time since it began in 2007, we view this payout as quite safe and likely to rise further as the company's cash flows continue to grow in the years ahead.

CONCLUSION

Had the COVID-19 pandemic arrived a few years earlier—when HUN was strapped with debt and still very early in its business transformation—the company might not have survived. But due in large part to the much healthier financial position it was able to enter last year with from the divestiture and monetization of noncore businesses and assets, as well as the improved profitability from the emphasis of differentiated products that carry higher-margins and actions taken to drive down operating costs, HUN's bottom line ultimately fared much better than expected in 2020. That has continued into the current year with its operating performance in Q1 also comfortably exceeding analysts' estimates and its outlook pointing to a better year overall than what most were projecting. What hasn't continued, however, are the favorable gains in share value these prior beats have contributed. Specifically, while HUN's shares did initially climb as much as 10.2% to a new 52-week high over the seven trading days following its Q1 report, they've given it all back and more and are now down roughly 16% since. And while we understand the rationale behind the downgrade by the analyst from Goldman Sachs, which triggered this slide, it's important to note that his revised target price of \$33 (from \$37) is now more than 21% above where the stock has sunk to. It's also nearly identical to the intrinsic value derived by our own conservative analysis of \$33.05. Thus, with both suggesting that the recent sell-off has been overdone, we think HUN's improving operations will be strong enough to take its stock to at least \$38 over the next two years.

CONSOLIDATED STATEMENTS OF INCOME*(in millions)*

	3 Months Ended	
	Mar. 31, 2021	Mar. 31, 2020
Total revenues	\$ 1,837	\$ 1,593
Cost of goods sold	1,445	1,296
Gross profit	392	297
Operating expenses:		
Selling, general and administrative	207	199
Research and development	38	36
Restructuring, impairment and plant closing costs	24	3
Other operating (income) expense, net	(3)	5
Total operating expenses	266	243
Operating income	126	54
Interest expense, net	(19)	(18)
Equity in income of investment in unconsolidated affiliates	38	2
Fair value adjustments to Venator investment	(19)	(110)
Other income, net	7	10
Income (loss) from continuing operations before income taxes	133	(62)
Income tax expense	(34)	(7)
Income (loss) from continuing operations	99	(69)
Income from discontinued operations, net of tax	1	777
Net income	100	708
Net income attributable to noncontrolling interests	(17)	(3)
Net (loss) income	\$ 83	\$ 705
Earnings per share – basic	\$ 0.38	\$ 3.16
Earnings per share – diluted	\$ 0.37	\$ 3.16
Weighted average shares outstanding – basic	220.4	223.2
Weighted average shares outstanding – diluted	222.6	223.2

CONSOLIDATED BALANCE SHEETS*(in millions)*

	Mar. 31, 2021	Dec. 31, 2020
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 673	\$ 1,593
Accounts and notes receivable	1,010	902
Accounts receivable from affiliates	12	8
Inventories	1,006	848
Other current assets	228	217
	<u>2,929</u>	<u>3,568</u>
Non-current assets:		
Property, plant and equipment, net	2,514	2,505
Investment in unconsolidated affiliates	411	373
Intangible assets, net	422	453
Goodwill	739	533
Deferred income taxes	282	288
Operating lease right-of-use assets	432	445
Other noncurrent assets	571	548
	<u>5,371</u>	<u>5,145</u>
Total assets	<u><u>\$ 8,300</u></u>	<u><u>\$ 8,713</u></u>
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	\$ 909	\$ 842
Accounts payable to affiliates	44	34
Accrued liabilities	505	458
Current portion of debt	57	593
Current operating lease liabilities	49	52
	<u>1,564</u>	<u>1,979</u>
Non-current liabilities:		
Long-term debt	1,510	1,528
Deferred income taxes	216	212
Noncurrent operating lease liabilities	401	411
Other noncurrent liabilities	875	910
	<u>3,002</u>	<u>3,061</u>
Shareholders' equity:		
Common stock \$0.01 par value; 1,200,000,000 shares authorized; 259,184,140 and 258,520,411 issued; 220,712,124 and 220,046,262 outstanding	3	3
Additional paid-in capital	4,085	4,048
Treasury stock, 38,477,091 shares	(731)	(731)
Unearned stock-based compensation	(38)	(19)
Retained earnings	1,603	1,564
Accumulated other comprehensive loss	(1,359)	(1,346)
Noncontrolling interests in subsidiaries	171	154
	<u>3,734</u>	<u>3,673</u>
Total liabilities and shareholders' equity	<u><u>\$ 8,300</u></u>	<u><u>\$ 8,713</u></u>

CONSOLIDATED STATEMENTS OF CASH FLOW

(in millions)

	3 Months Ended	
	Mar. 31, 2021	Mar. 31, 2020
Cash flows from operating activities:		
Net income	\$ 100	\$ 708
Less: Income from discontinued operations, net of tax	(1)	(777)
Income (loss) from continuing operations	99	(69)
Adjustments to reconcile income (loss) from continuing operations to net cash used in operating activities from continuing operations:		
Equity in income of investment in unconsolidated affiliates	(38)	(2)
Unrealized losses on fair value adjustments to Venator investment	19	110
Depreciation and amortization	74	67
Noncash lease expense	17	15
Noncash restructuring and impairment charges	8	-
Deferred income taxes	-	(2)
Stock-based compensation	9	7
Other, net	2	(1)
Changes in operating assets and liabilities:		
Accounts and notes receivable	(117)	(34)
Inventories	(156)	(92)
Prepaid expenses	6	6
Other current assets	(16)	1
Other noncurrent assets	(30)	(7)
Accounts payable	94	61
Accrued liabilities	20	(44)
Taxes paid on sale of Chemical Intermediates Businesses	-	(2)
Other noncurrent liabilities	(7)	(54)
Net cash used in operating activities from continuing operations	(16)	(40)
Net cash used in operating activities from discontinued operations	(1)	(35)
Net cash used in operating activities	(17)	(75)
Cash flows from investing activities:		
Capital expenditures	(98)	(61)
Cash received from sale of businesses	15	1,915
Acquisition of businesses, net of cash acquired	(240)	(346)
Other, net	-	3
Net cash (used in) provided by investing activities	(323)	1,511
Cash flows from financing activities:		
Net borrowings (repayments) on revolving loan facilities	9	(158)
Repayments of long-term debt	(548)	-
Repayments of notes payable	-	(32)
Dividends paid to noncontrolling interests	-	(23)
Dividends paid to common stockholders	(37)	(37)
Repurchase and cancellation of stock awards	(6)	(6)
Repurchase of common stock	-	(96)
Other, net	3	(2)
Net cash used in financing activities	(579)	(354)
Effect of exchange rate changes on cash	(1)	(13)
(Decrease) increase in cash, cash equivalents and restricted cash	(920)	1,069
Cash, cash equivalents and restricted cash at beginning of period	1,593	525
Cash, cash equivalents and restricted cash at end of period	\$ 673	\$ 1,594

OPEN POSITIONS

The index below allows subscribers to determine if they have received the recommendations and reviews to which they are entitled. The first column lists the stock's ticker symbol. The third column lists the issuance date of each initial report. The seventh column lists the date of the most recent review. The eighth column lists the number of reviews that have been issued since a stock was recommended. Recommendations closed during the previous month are designated as such in the fifth column. Those closed more than a month ago are no longer listed. However, our [website](#) provides a complete listing of stocks closed out in recent months.

Ticker	Company Name	Rec. Date	Rec. Price	Price at 6/11/21	Current Rating	Latest Review	No. of Reviews
HBI	Hanesbrands	11/18/16	25.35	19.53	Buy	5/12/21	19
ACCO	ACCO Brands	11/16/18	8.23	9.22	Buy	4/28/21	11
DLX	Deluxe	2/21/20	38.91	47.62	Buy	5/7/21	7
CSGS	CSG Systems	7/10/20	38.38	45.43	Buy	5/6/21	4
VEC	Vectrus	8/21/20	41.66	51.15	Buy	5/12/21	4
SPTN	SpartanNash	9/11/20	17.06	20.77	Buy	6/3/21	4
RGP	Resources Connection	1/15/21	12.20	15.18	Buy	4/8/21	1
STRL	Sterling Construction	3/12/21	22.67	24.24	Buy	5/4/21	1
CLW	Clearwater Paper	4/16/21	34.57	29.23	Buy	5/6/21	1
UEIC	Universal Electronics	5/21/21	48.20	48.92	Buy		
HUN	Huntsman	6/14/21	27.22	27.22	Buy		

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