

## Kraton Corp. Summary

Date of Report: Nov 11, 2020  
Stock: Kraton Corporation (KRA)  
Sector: Materials  
Subsector: Specialty Chemicals

P/E ratio for KRA: -2.01  
Forward P/E ratio for industry: 22.1  
Price target: \$37.44  
Current Price: \$ 27.56

**Recommendation: BUY**



### Company Summary

Kraton Corporation (NYSE: KRA) is a leading global producer of styrenic block copolymers, specialty polymers and high-value performance products derived from pine wood pulping co-products. Kraton's polymers are used in a wide range of applications, including adhesives, coatings, consumer and personal care products, sealants and lubricants, and medical, packaging, automotive, paving and roofing applications. As the largest global provider in the pine chemicals industry, the company's pine-based specialty products are sold into adhesive, road and construction and tire markets, and it produces and sells a broad range of performance chemicals into markets that include fuel additives, oilfield chemicals, coatings, metalworking fluids and lubricants, inks and mining. Kraton offers its products to a diverse customer base in numerous countries worldwide.

### Industry Outlook

Chemical manufacturing was designated as essential critical infrastructure in all regions that Kraton operates and has allowed them to provide an uninterrupted supply of products to their customers. Many of Kraton's products are critical to the defense of COVID-19, such as adhesives, bandages, and other medical supplies. In addition, Kraton has begun the patent process for BIAXAMTM as a Self-Sterilizing Sulfonated Polymer which has been shown in studies to kill up to 99.99% of microbes including SARS-CoV-2 Virus in as little as 5 minutes.

<https://kraton.gcs-web.com/news-releases/news-release-details/kraton-corporation-announces-third-quarter-2020-results>

### Cash Flow History & Forecasts

Our earnings forecast for Kraton Corp. was completed using the same methodology as our previous Stock Valuation 2 calculations for forecasting quarterly earnings out to 2021. We compared the recent Q3 earnings report with our previous calculations to determine any adjustments that needed to be made to our forecasting assumptions.



Income Statement	2017	2018	2019	2020	2021	2022	2023	2024	2025
Revenue	1,960,362	2,011,675	1,804,436	1,548,496	1,602,693	1,658,788	1,716,845	1,776,935	1,839,127
Cost of goods sold	1,415,659	1,431,069	1,390,007	1,163,776	1,184,151	1,225,597	1,268,493	1,312,390	1,358,841
Gross profit	544,703	580,606	414,429	379,025	418,542	433,191	448,352	464,045	480,286
<b>Operating expenses:</b>									
Research and development	40,283	41,296	41,073	40,654	41,670	43,128	44,638	46,200	47,817
Selling, general, and administrative	161,260	153,897	149,800	159,794	112,189	116,115	120,179	124,385	128,739
Depreciation and amortization	137,162	141,410	136,171	125,156	112,189	116,115	120,179	124,385	128,739
Gain on insurance proceeds	-	(8,900)	(32,850)	-	-	-	-	-	-
Loss on disposal of fixed assets	514	2,169	773	(34)	-	-	-	-	-
Impairment on goodwill	-	-	-	400,000	-	-	-	-	-
Operating income	205,484	250,734	119,462	(346,544)	152,495	157,832	163,356	169,074	174,991
Other income (expense)	(3,360)	(3,472)	3,339	1,109	2,826	2,925	3,028	3,134	3,243
Disposition and exit of business activities	-	-	-	175,189	78,000	-	-	-	-
Loss on extinguishment of debt	(35,389)	(79,866)	(3,521)	(14,943)	-	-	-	-	-
Earnings of unconsolidated joint venture	486	471	506	415	469	465	464	453	463
Interest expense, net	(132,459)	(93,772)	(75,782)	(57,951)	(44,058)	(33,495)	(25,465)	(19,360)	(14,719)
Income before income taxes	34,762	74,095	44,004	(242,725)	189,733	127,727	141,382	153,300	163,979
Income tax benefit (expense)	57,884	(3,574)	11,813	53,847	46,513	31,312	34,660	37,581	40,199
Consolidated net income	92,646	70,521	55,817	(188,878)	236,246	159,039	176,042	190,882	204,178
Net (income) loss attributable to noncontrolling interests	4,903	(3,506)	(4,512)	(4,030)	(4,016)	(4,023)	(4,020)	(4,021)	(4,020)
<b>Net income attributable to Kraton</b>	<b>\$ 97,549</b>	<b>\$ 67,015</b>	<b>\$ 51,305</b>	<b>(192,908)</b>	<b>232,230</b>	<b>155,016</b>	<b>172,023</b>	<b>186,860</b>	<b>200,157</b>
Revenue growth (yfy%)		2.6%	-10.3%	-14.2%	3.5%	3.5%	3.5%	3.5%	3.5%
COGS as % of Revenue	72.2%	71.1%	77.0%	75.2%	73.9%	73.9%	73.9%	73.9%	73.9%
R&D as % of Revenue	2.1%	2.1%	2.3%	2.6%	2.6%	2.6%	2.6%	2.6%	2.6%
SG&A as % of Revenue	8.2%	7.7%	8.3%	10.3%	7.0%	7.0%	7.0%	7.0%	7.0%
Depreciation and amortization	7.0%	7.0%	7.5%	8.1%	7.0%	7.0%	7.0%	7.0%	7.0%
Other Income as % of Revenue	0.2%	0.2%	0.2%	-0.1%	0.2%	0.2%	0.2%	0.2%	0.2%
Interest expense yfy%		-29.2%	-19.2%	-23.5%	-24.0%	-24.0%	-24.0%	-24.0%	-24.0%
Effective Tax Rate, Benefit (% of Income before Tax) (L)	166.5%	4.8%	26.8%	22.2%	24.5%	24.5%	24.5%	24.5%	24.5%

## Valuation

In our Valuation calculations for Kraton, we used a long-term growth rate of 3.50% and referred to [www.yardeni.com](http://www.yardeni.com) for the most current Industry Forward P/E ratio in order to come up with a discount rate (Cost of Equity) of 8.02% Capital Expenditures, Change to Net Working Capital, and Change to Debt for 2021 through 2025 were all calculated using rolling averages for the year-over-year changes from 2016 through 2019.

Valuation		2021	2022	2023	2024	2025
Year						
Net income attributable to Kraton		232,230	155,016	172,023	186,860	200,157
Add: Depreciation and amortization		112,189	116,115	120,179	124,385	128,739
Less: CapEx		(115,453)	(113,074)	(113,733)	(114,087)	(113,631)
Less: Change in NWC		(42,047)	(44,143)	(46,357)	(48,675)	(51,108)
Less: Change in Debt		(36,061)	(38,315)	(38,037)	(39,405)	(100,519)
FCFE		90,856	15,593	34,074	43,080	63,637
						Terminal Value
Sum of Discounted FCFE		203,802				
Discounted Terminal Value			989,522			
Equity Value			1,193,324			
Shares Outstanding			31,870			
<b>Target Price</b>			<b>\$ 37.44</b>			
Current Price			\$ 27.56			
Analyst Target Price (Low, Avg., High)			15, 25, 45			
52 Week High			31.44			
Est. Return			36%			
Industry Forward P/E			22.1			
Discount			8.02%			
Long Term Growth Rate			3.5%			
<b>Recommendation: BUY/HOLD</b>						

## Sensitivity Analysis

In our sensitivity analysis you can see the effects of altering the discount rate (Cost of Equity) by (+/-) 1.5% and the residual effects on the Valuation calculations and final price target.

Sum of Discount FCFE	211,756
Discounted Terminal Value	1,590,338
Equity Value	1,802,094
Shares Outstanding	31,870
<b>Target Price</b>	<b>\$ 56.55</b>
Current Price	\$ 27.56
Analyst Target Price (Low, Avg., High)	15, 25, 45
52 Week High	31.44
Est. Return	105%
Industry Forward P/E	22.1
Discount	6.52%
Long Term Growth Rate	3.5%
<b>Recommendation: BUY/HOLD</b>	

Sum of Discount FCFE	196,398
Discounted Terminal Value	694,366
Equity Value	890,764
Shares Outstanding	31,870
<b>Target Price</b>	<b>\$ 27.95</b>
Current Price	\$ 27.56
Analyst Target Price (Low, Avg., High)	15, 25, 45
52 Week High	31.44
Est. Return	1%
Industry Forward P/E	22.1
Discount	9.52%
Long Term Growth Rate	3.5%
<b>Recommendation: BUY/HOLD</b>	

## Conclusion

Our stake in Kraton Corp. was originally purchased on 10/22/2019 and has been held through two semesters. It is our recommendation that we continue to hold Kraton as our price target indicates that this stock remains undervalued by ~36%.