

Element Solutions Inc.

2H improvement expected off a weaker 1H base

Reiterate Rating: BUY | PO: 23.00 USD | Price: 17.92 USD

Sluggish demand in 1Q, likely to continue in 2Q

ESI reported 1Q EBITDA of \$112mn vs our \$108mn, representing a 22% decline y/y driven largely by the cyclically depressed Electronics business. While Assembly was down modestly, Circuitry and Semiconductor businesses posted high-teen sales declines y/y. ESI's Industrial & Specialty segment (~35% of EBITDA) was a bit more stable, largely due to strength in offshore drilling and US auto OEMs, offset by weak demand in Europe and Asia. ESI expects business fundamentals to remain flattish sequentially in 2Q, but with some price/cost benefit, consistent with our observations across all specialty chemicals. The company expects 2Q EBITDA to be near \$120mn, which we view as conservative due to sticky pricing, cost deflation, and higher assembly and energy solutions growth. Our 2Q EPS accordingly rises to \$0.31 from \$0.30.

2H recovery expected driven by cyclical improvements

Unlike many chemical end markets linked to construction and consumer products that are not expected to meaningfully recover and/or potentially contract further in 2H, ESI's key end markets of electronics and autos are showing signs of recovery. Smartphone shipments were down 11% in the quarter vs year-ago levels, whereas our colleague covering Global Smartphones, Simon Woo, expects this number to be up 15% by 4Q. Similarly, outlook for US and global auto production calls for stronger growth globally by 4Q. Our 2023 EBITDA rises to \$515 from \$510 prior, vs the company's guide of \$510mn. Our 2023 EPS increases to \$1.37 from \$1.35.

Focused on differentiated technologies

ESI's growth drivers are generally associated with technologies that provide meaningful value to customers either from increased production rates, improved product quality, or less waste. This strategy should lead to more share gains and pricing power, particularly with customer capacity expansions when these end key end markets begin to recover. We also see ESI using technology to expand into new markets and for cross selling. With net debt leverage at 3.3x (trailing 12 months), we expect ESI's M&A focus to be on small bolt-ons that provide additional differentiated and cross-selling technologies. Our PO remains at \$23, based on an unchanged 14x multiple, as applied to our 2023E EBITDA estimate. We reiterate our Buy.

Estimates (Dec) (US\$)	2021A	2022A	2023E	2024E	2025E
EPS	1.38	1.41	1.37	1.57	1.77
GAAP EPS	0.82	0.84	0.79	0.99	1.18
EPS Change (YoY)	42.3%	2.2%	-2.8%	14.6%	12.7%
Consensus EPS (Bloomberg)			1.38	1.55	1.73
DPS	0.25	0.32	0.38	0.44	0.50
Valuation (Dec)					
P/E	13.0x	12.7x	13.1x	11.4x	10.1x
GAAP P/E	21.9x	21.3x	22.7x	18.1x	15.2x
Dividend Yield	1.4%	1.8%	2.1%	2.5%	2.8%
EV / EBITDA*	12.0x	11.9x	12.2x	10.9x	9.9x
Free Cash Flow Yield*	6.5%	5.8%	5.3%	5.0%	7.7%

* For full definitions of *IQmethod*SM measures, see page 5.

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Timestamp: 27 April 2023 10:15PM EDT

27 April 2023

Equity

Key Changes

(US\$)	Previous	Current
2023E Rev (m)	2,539.8	2,665.7
2024E Rev (m)	2,701.7	2,833.7
2025E Rev (m)	2,854.7	2,987.1
2023E EPS	1.35	1.37
2024E EPS	1.56	1.57
2023E DPS	0.40	0.38

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Stock Data

Price	17.92 USD
Price Objective	23.00 USD
Date Established	17-Apr-2023
Investment Opinion	B-1-7
52-Week Range	15.31 USD - 22.14 USD
Mrkt Val (mn) / Shares Out (mn)	4,326 USD / 241.4
Average Daily Value (mn)	18.09 USD
BofA Ticker / Exchange	ESI / NYS
Bloomberg / Reuters	ESI US / ESI.N
ROE (2023E)	14.3%
Net Dbt to Eqty (Dec-2022A)	70.9%
ESGMeter™	High

ESGMeter is not indicative of a company's future stock price performance and is not an investment recommendation or rating. ESGMeter is independent of BofA Global Research's equity investment rating, volatility risk rating, income rating, and price objective for that company. For full details, refer to ["BofA ESGMeter Methodology"](#).

OEM: original equipment manufacturer

iQprofileSM Element Solutions Inc.

iQmethodSM – Bus Performance*

(US\$ Millions)	2021A	2022A	2023E	2024E	2025E
Return on Capital Employed	8.7%	8.3%	8.2%	9.1%	10.0%
Return on Equity	14.4%	14.5%	14.3%	16.1%	17.6%
Operating Margin	20.3%	19.0%	17.6%	18.7%	19.5%
Free Cash Flow	280	250	228	215	333

iQmethodSM – Quality of Earnings*

(US\$ Millions)	2021A	2022A	2023E	2024E	2025E
Cash Realization Ratio	0.9x	0.9x	0.9x	0.8x	1.0x
Asset Replacement Ratio	0.3x	0.3x	0.4x	0.4x	0.4x
Tax Rate	20.0%	20.0%	20.3%	21.0%	21.0%
Net Debt-to-Equity Ratio	64.5%	70.9%	70.0%	68.8%	62.5%
Interest Cover	9.0x	9.5x	8.8x	10.1x	11.2x

Income Statement Data (Dec)

(US\$ Millions)	2021A	2022A	2023E	2024E	2025E
Sales	2,400	2,549	2,666	2,834	2,987
% Change	29.5%	6.2%	4.6%	6.3%	5.4%
Gross Profit	1,003	953	958	1,049	1,131
% Change	27.0%	-5.0%	0.6%	9.5%	7.8%
EBITDA	525	527	515	578	635
% Change	24.2%	0.3%	-2.3%	12.4%	9.9%
Net Interest & Other Income	(54)	(49)	(51)	(50)	(50)
Net Income (Adjusted)	346	348	333	378	421
% Change	42.2%	0.7%	-4.4%	13.6%	11.2%

Free Cash Flow Data (Dec)

(US\$ Millions)	2021A	2022A	2023E	2024E	2025E
Net Income from Cont Operations (GAAP)	549	534	522	613	698
Depreciation & Amortization	164	161	162	165	169
Change in Working Capital	(46)	(99)	(51)	(111)	(39)
Deferred Taxation Charge	(47)	15	(2)	(2)	(2)
Other Adjustments, Net	(295)	(314)	(334)	(378)	(421)
Capital Expenditure	(46)	(48)	(70)	(71)	(73)
Free Cash Flow	280	250	228	215	333
% Change	13.1%	-10.6%	-8.8%	-5.6%	54.7%

Balance Sheet Data (Dec)

(US\$ Millions)	2021A	2022A	2023E	2024E	2025E
Cash & Equivalents	330	266	289	297	410
Trade Receivables	492	456	480	555	585
Other Current Assets	392	467	480	566	582
Property, Plant & Equipment	278	277	216	122	25
Other Non-Current Assets	3,646	3,438	3,415	3,415	3,415
Total Assets	5,138	4,904	4,880	4,954	5,017
Short-Term Debt	13	12	12	12	12
Other Current Liabilities	403	333	313	362	369
Long-Term Debt	1,930	1,921	1,918	1,918	1,918
Other Non-Current Liabilities	292	290	293	291	289
Total Liabilities	2,638	2,555	2,536	2,582	2,588
Total Equity	2,501	2,349	2,344	2,373	2,430
Total Equity & Liabilities	5,138	4,904	4,880	4,955	5,018

* For full definitions of iQmethodSM measures, see page 5.

Company Sector

Chemicals-Specialty

Company Description

Element Solutions Inc (ESI) was founded in 2013 as a special purpose acquisition company (SPAC) with the intention of acquiring and integrating asset lite, high-touch specialty chemical businesses along different chemical verticals. The company has completed six acquisitions for \$9.3bn split between Agriculture and Industrial markets. End market sales are split among Agriculture (50%), Electronics (20%), Automotive (10%), Industrial (10%), Consumer Packaging (5%), and Offshore Energy (5%).

Investment Rationale

We expect continued EBITDA and FCF growth for the business and for shares to re-rate following the sale of the Ag business. ESI shares trade at a discount to peers despite owning businesses that are in niche areas of the market with barriers to entry and pricing power where ESI commands 20-40% market shares.

Stock Data

Average Daily Volume 1,019,948

Quarterly Earnings Estimates

	2022	2023
Q1	0.38A	0.30A
Q2	0.38A	0.31E
Q3	0.36A	0.37E
Q4	0.28A	0.38E

Exhibit 1: Element Solutions Income Statement Summary

Our 2023 EPS rises to \$1.37 from \$1.35 prior

Net Sales	2019	2020	2021	1Q22	2Q22	3Q22	4Q22	2022	1Q23	2Q23E	3Q23E	4Q23E	2023	2024	2025
Electronics	\$1,086	\$1,172	\$1,534	\$427	\$439	\$388	\$338	\$1,591	\$340	\$384	\$398	\$410	\$1,641	\$1,746	\$1,837
Industrial & Specialties	\$750	\$682	\$866	\$253	\$238	\$231	\$236	\$958	\$235	\$254	\$241	\$255	\$1,024	\$1,087	\$1,151
Total	1,836	1,854	2,400	680	677	619	574	2,549	574	638	639	665	2,666	2,834	2,987
EBITDA															
Electronics	253	277	355	97	102	91	68	358	73	76	93	98	339	380	413
Industrial & Specialties	164	145	170	48	39	42	40	168	40	45	45	46	175	199	222
Total	417	423	525	145	140	134	108	527	112	120	138	144	515	578	635
Depreciation and Amortization	42	42	38	11	10	11	10	42	10	11	11	13	45	49	52
Operating Income	375	381	487	134	130	123	98	485	103	109	127	131	470	530	583
Interest Expense, Net	(71)	(63)	(54)	(14)	(13)	(12)	(12)	(51)	(12)	(13)	(13)	(15)	(53)	(52)	(52)
Other Expense / (Income)	20	11	0	(1)	2	1	1	2	1	1	1	0	2	2	2
Profit Before Tax	325	328	433	119	118	112	87	436	92	96	114	117	418	479	533
Income Tax Provision (Benefit)	85	85	87	24	24	22	17	87	18	19	23	24	85	101	112
Tax Rate	26.0%	25.8%	20.0%	20.2%	19.8%	19.9%	20.0%	20.0%	20.0%	20.0%	20.6%	20.6%	20.3%	21.0%	21.0%
Preferred Dividends	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
Non-controlling Interest	(0)	0	(1)	(0)	(0)	0	(0)	(1)	(0)	(0)	(0)	(0)	(1)	(1)	(1)
Net Income	240	243	346	95	95	89	69	348	73	77	90	92	333	378	421
(+/-) Adjustments	163	165	144	40	29	36	57	144	30	36	36	42	144	144	144
GAAP Net Income	77	78	202	55	66	54	13	205	43	41	54	51	189	235	277
Diluted - Adjusted EPS	\$0.93	\$0.97	\$1.38	\$0.38	\$0.38	\$0.36	\$0.28	\$1.41	\$0.30	\$0.31	\$0.37	\$0.38	\$1.37	\$1.57	\$1.77
Adjusted Diluted Shares	258	250	251	250	248	245	243	246	244	245	243	243	243	240	238
Segment Sales Growth:															
Electronics	-6.2%	8.0%	30.9%	20.8%	14.9%	-2.7%	-15.6%	10.5%	-20.4%	-12.5%	2.6%	21.3%	3.2%	6.4%	5.2%
Industrial & Specialties	-6.5%	-9.1%	27.1%	28.8%	16.3%	6.1%	-4.4%	20.1%	-7.3%	6.8%	4.6%	8.1%	6.9%	6.1%	5.8%
Total	-6.3%	1.0%	29.5%	23.7%	15.4%	0.4%	-11.3%	13.9%	-15.6%	-4.6%	3.4%	15.9%	4.7%	6.3%	5.4%
Adjusted EBITDA Margin															
Electronics	23.3%	23.7%	23.2%	22.8%	23.1%	23.5%	20.2%	22.5%	21.4%	19.7%	23.4%	23.9%	20.7%	21.7%	22.5%
Industrial & Specialties	21.8%	21.3%	19.6%	18.8%	16.3%	18.3%	16.8%	17.6%	16.9%	17.5%	18.7%	18.0%	17.1%	18.3%	19.3%
Total	22.7%	22.8%	21.9%	21.3%	20.7%	21.6%	18.8%	20.7%	19.6%	18.8%	21.6%	21.7%	19.3%	20.4%	21.3%

Source: Company financials, BofA Global Research estimates

BofA GLOBAL RESEARCH



Price objective basis & risk

Element Solutions Inc. (ESI)

Our \$23 PO is based on a 14x multiple, as applied to our 2023E EBITDA estimate. This multiple is in line with the average for the broader specialty chemical universe, which we see as fair considering the defensive growth and robust free cash flow generation that ESI has been able to exhibit.

Risks to our PO are a stronger dollar, decline in electronics demand, closing of the Coventya deal does not occur, and reduced OEM automotive production.

Analyst Certification

I, Steve Byrne, CFA, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.

US - Chemicals Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
BUY				
	Axalta Coating Systems	AXTA	AXTA US	Steve Byrne, CFA
	Bunge Limited	BG	BG US	Salvator Tiano, CFA
	Celanese Corporation	CE	CE US	Matthew DeYoe, CFA
	CF Industries	CF	CF US	Steve Byrne, CFA
	Chemours Company	CC	CC US	Matthew DeYoe, CFA
	DuPont	DD	DD US	Steve Byrne, CFA
	Eastman Chemical Co	EMN	EMN US	Matthew DeYoe, CFA
	Element Solutions Inc.	ESI	ESI US	Steve Byrne, CFA
	FMC Corporation	FMC	FMC US	Steve Byrne, CFA
	Linde	LIN	LIN US	Steve Byrne, CFA
	Linde	LINGY	LIN GY	Steve Byrne, CFA
	Livent	LTHM	LTHM US	Matthew DeYoe, CFA
	Nutrien	NTR	NTR US	Steve Byrne, CFA
	Olin Corp	OLN	OLN US	Steve Byrne, CFA
	Origin Materials	ORGN	ORGN US	Steve Byrne, CFA
	PPG Industries Inc.	PPG	PPG US	Steve Byrne, CFA
	Sigma Lithium	SGML	SGML US	Matthew DeYoe, CFA
	The Mosaic Company	MOS	MOS US	Steve Byrne, CFA
	Tronox Holdings	TROX	TROX US	Matthew DeYoe, CFA
NEUTRAL				
	Air Products	APD	APD US	Steve Byrne, CFA
	Archer-Daniels-Midland Company	ADM	ADM US	Salvator Tiano, CFA
	Corteva	CTVA	CTVA US	Steve Byrne, CFA
	Dow Inc	DOW	DOW US	Steve Byrne, CFA
	Green Plains	GPPE	GPPE US	Salvator Tiano, CFA
	International Flavors & Fragrances	IFF	IFF US	Matthew DeYoe, CFA
	Sherwin-Williams Company	SHW	SHW US	Steve Byrne, CFA
	Westlake Corp	WLK	WLK US	Steve Byrne, CFA
UNDERPERFORM				
	Albemarle	ALB	ALB US	Matthew DeYoe, CFA
	Ecolab Inc	ECL	ECL US	Steve Byrne, CFA
	Huntsman Corp	HUN	HUN US	Matthew DeYoe, CFA
	LyondellBasell Industries	LYB	LYB US	Steve Byrne, CFA
	RPM International Inc	RPM	RPM US	Steve Byrne, CFA
	Venator Materials	VNTR	VNTR US	Matthew DeYoe, CFA
	Westlake Chemical Partners, LP	WLKP	WLKP US	Steve Byrne, CFA
RSTR				
	Diversey Holdings	DSEY	DSEY US	Steve Byrne, CFA

IQmethodSM Measures Definitions

Business Performance

Return On Capital Employed

Return On Equity

Operating Margin

Earnings Growth

Free Cash Flow

Quality of Earnings

Cash Realization Ratio

Asset Replacement Ratio

Tax Rate

Net Debt-To-Equity Ratio

Interest Cover

Valuation Toolkit

Price / Earnings Ratio

Price / Book Value

Dividend Yield

Free Cash Flow Yield

Enterprise Value / Sales

EV / EBITDA

Numerator

NOPAT = (EBIT + Interest Income) × (1 – Tax Rate) + Goodwill Amortization

Net Income

Operating Profit

Expected 5 Year CAGR From Latest Actual

Cash Flow From Operations – Total Capex

Numerator

Cash Flow From Operations

Capex

Tax Charge

Net Debt = Total Debt – Cash & Equivalents

EBIT

Numerator

Current Share Price

Current Share Price

Annualised Declared Cash Dividend

Cash Flow From Operations – Total Capex

EV = Current Share Price × Current Shares + Minority Equity + Net Debt +

Other LT Liabilities

Enterprise Value

Denominator

Total Assets – Current Liabilities + ST Debt + Accumulated Goodwill Amortization

Shareholders' Equity

Sales

N/A

N/A

Denominator

Net Income

Depreciation

Pre-Tax Income

Total Equity

Interest Expense

Denominator

Diluted Earnings Per Share (Basis As Specified)

Shareholders' Equity / Current Basic Shares

Current Share Price

Market Cap = Current Share Price × Current Basic Shares

Sales

Basic EBIT + Depreciation + Amortization

IQmethodSM is the set of BofA Global Research standard measures that serve to maintain global consistency under three broad headings: Business Performance, Quality of Earnings, and valuations. The key features of *IQmethod* are: A consistently structured, detailed, and transparent methodology. Guidelines to maximize the effectiveness of the comparative valuation process, and to identify some common pitfalls.

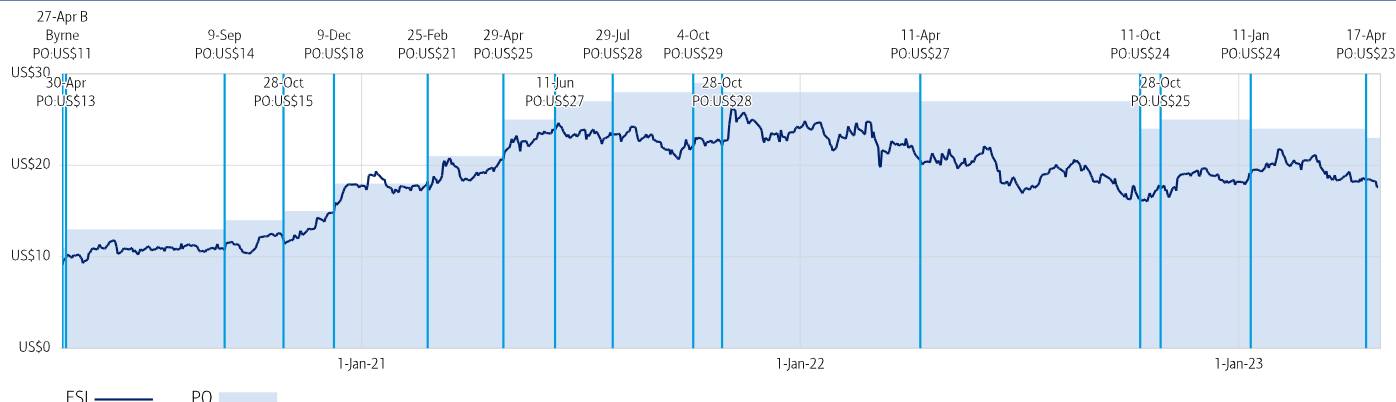
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Disclosures

Important Disclosures

Element Solutions (ESI) Price Chart



B: Buy, N: Neutral, U: Underperform, PO: Price Objective, NA: No longer valid, NR: No Rating

The Investment Opinion System is contained at the end of the report under the heading "Fundamental Equity Opinion Key". Dark grey shading indicates the security is restricted with the opinion suspended. Medium grey shading indicates the security is under review with the opinion withdrawn. Light grey shading indicates the security is not covered. Chart is current as of a date no more than one trading day prior to the date of the report.

Equity Investment Rating Distribution: Chemicals Group (as of 31 Mar 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships ^{R1}	Count	Percent
Buy	68	51.52%	Buy	32	47.06%
Hold	31	23.48%	Hold	19	61.29%
Sell	33	25.00%	Sell	18	54.55%

Equity Investment Rating Distribution: Global Group (as of 31 Mar 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships ^{R1}	Count	Percent
Buy	1869	53.01%	Buy	1030	55.11%
Hold	827	23.45%	Hold	476	57.56%
Sell	830	23.54%	Sell	389	46.87%

^{R1} Issuers that were investment banking clients of BofA Securities or one of its affiliates within the past 12 months. For purposes of this Investment Rating Distribution, the coverage universe includes only stocks. A stock rated Neutral is included as a Hold, and a stock rated Underperform is included as a Sell.

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Investment rating	Total return expectation (within 12-month period of date of initial rating)	Ratings dispersion guidelines for coverage cluster ^{R2}
Buy	≥ 10%	≤ 70%
Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

^{R2} Ratings dispersions may vary from time to time where BofA Global Research believes it better reflects the investment prospects of stocks in a Coverage Cluster.

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