



# McCormick & Company (MKC)

Updated June 28<sup>th</sup>, 2018 by Nate Parsh

## Key Metrics

<b>Current Price:</b> \$115	<b>5 Year CAGR Estimate:</b> 6.6%	<b>Volatility Percentile:</b> 2.6%
<b>Fair Value Price:</b> \$98	<b>5 Year Growth Estimate:</b> 8.0%	<b>Momentum Percentile:</b> 76.6%
<b>% Fair Value:</b> 117%	<b>5 Year Valuation Multiple Estimate:</b> -3.2%	<b>Total Return Percentile:</b> 35.3%
<b>Dividend Yield:</b> 1.8%	<b>5 Year Price Target:</b> \$144	<b>Valuation Percentile:</b> 26.3%

## Overview & Current Events

McCormick & Company produces, markets and distributes seasoning mixes, spices, condiments and other products to customers in the food industry. McCormick was founded in 1889 by Willoughby M. McCormick. Today the company has a market cap of \$13.9 billion and had sales in excess of \$4.8 billion in 2017. McCormick has approximately 20% market share of the \$11 billion seasoning and spice industry.

McCormick reported second quarter earnings On June 28<sup>th</sup>. As with Q1, the company had very impressive results.

McCormick earned \$1.02 during the quarter, a \$0.09 beat of estimates and a 24.4% improvement from Q2 2017.

Revenue grew almost 20% to \$1.33 billion. This was \$10 million above analysts' expectations. By divisions, Consumer sales rose 16% on a constant currency basis while Flavor Solutions, formerly known as Industrial, grew 15.2%. Gross margins improved 340 basis points to 43.3%. McCormick's stock finished the trading session 8.4% higher.

Why such an impressive return? The answer has to do with the company's July 2017 purchase of RB Foods. McCormick paid more than \$4 billion for Frank's Red Hot, French's Mustard and other condiments. At that time, the market greatly disliked the deal, but after these products contributed 12.4% of sales growth in Q1, they added 13% to Q2 sales.

## Growth on a Per-Share Basis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
<b>EPS</b>	\$2.14	\$2.34	\$2.65	\$2.79	\$3.04	\$3.13	\$3.37	\$3.48	\$3.78	\$4.25	<b>\$4.90</b>	<b>\$7.20</b>
<b>DPS</b>	\$0.88	\$0.96	\$1.04	\$1.12	\$1.24	\$1.36	\$1.48	\$1.60	\$1.72	\$1.88	<b>\$2.08</b>	<b>\$3.20</b>

McCormick has increased earnings per share every year for the past ten years. Over this time frame, EPS have increased at an average of 7.1% per year. As stated, the addition of RB Foods has worked very well in the company's favor in the last two quarters. Frank's Red Hot is the #1 hot sauce in the world and French's Mustard holds a top position in its own category. Although shares of McCormick dropped more than 6% the day the acquisition was announced, RB Foods is already accretive to earnings and the products that were acquired should help drive sales and earnings growth in the future. In fact, we feel that this acquisition will help to increase earnings growth going forward as we now project that McCormick can grow EPS at a rate of at least 8% per year, up from our previous estimate of 7%, through 2023.

On the Q2 conference call, McCormick reaffirmed its guidance for the year. The company still expects an EPS midpoint of \$4.90 per share for 2018. Applying our updated EPS growth rate to the midpoint of guidance, we forecast that McCormick could earn \$7.20 per share by 2023, up from our previous estimate of \$6.90. As such, we've raised our 2023 price target to \$144 from \$138. McCormick has increased its dividend for thirty-two years while raising its dividend an average of 8.9% over the last ten years. McCormick raised its dividend 10.6% on 11/28/2017. The new annualized dividend is \$2.08 per share. Due to a low payout ratio, we assume dividends will grow by 9% annually through 2023.

## Valuation Analysis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	Now	2023
<b>Avg. P/E</b>	17.2	13.2	14.8	17.1	18.7	22	20.6	22.5	25.1	23.0	<b>23.5</b>	<b>20.0</b>
<b>Avg. Yld.</b>	2.4%	3.0%	2.6%	2.3%	2.2%	2.0%	2.1%	2.0%	1.8%	1.9%	<b>2.0%</b>	<b>2.2%</b>

McCormick has traded with an average price to earnings multiple of 19.4 from 2008-2017. Based off of the company's guidance for 2018, shares trade with a P/E of 23.5, up from 21.6 at the time of our last update. After today's gain,

shares are more expensive versus their historical average than they were at the end of March. That being said, McCormick's purchase of RB Foods is already rewarding shareholders. We maintain a target P/E of 20, up slightly from the stock's 10-year average P/E. If the stock reverted to this target P/E, shares would experience a multiple contraction of 3.2% annually through 2023. If future results mirror Q1 & Q2, we could raise our target P/E.

## Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
<b>GP/A</b>	40%	39.2%	41.5%	37.2%	38.8%	37.4%	39.2%	38.8%	39.5%	19.4%	<b>22%</b>	<b>35%</b>
<b>Debt/A</b>	67.2%	60.6%	57.5%	60.8%	59.6%	56.6%	59.4%	62.7%	64.9%	75.4%	<b>73%</b>	<b>65%</b>
<b>Int. Cov.</b>	6.96	8.89	10.39	10.60	10.64	10.37	12.15	10.31	11.52	7.22	<b>8.0</b>	<b>10.0</b>
<b>Payout</b>	41.2%	41%	39.2%	40.1%	40.8%	43.5%	44.0%	46.0%	45.5%	44.2%	<b>42%</b>	<b>44%</b>
<b>Std. Dev.</b>	21.7%	16.7%	11.6%	15.2%	9.5%	11.9%	11.7%	12.9%	13.1%	12.9%	<b>13.1%</b>	<b>13.7%</b>

Note: GP/A decreased in 2017 due to large goodwill and intangible assets from the RB Foods acquisition.

McCormick's competitive advantage stems from its large market share of the seasoning and spice global market. McCormick is four times as large as its nearest competitor, which gives it unmatched size and scale. With a portfolio of popular products, the company has the ability to negotiate with retailers on pricing and shelf space.

Shares of McCormick performed remarkably well during the last recession. While many companies saw declining earnings per share during the Great Recession, McCormick actually increased its EPS in 2008 and 2009. Even with 9% annual dividend increases over the past decade, McCormick's payout ratio is reasonably low. This shows that the company is increasing earnings at a very steady rate.

## Final Thoughts & Recommendation

We now expect shares of McCormick to return 6.6% annually through 2023. This is down from our previous estimate of 7.6%. Higher earnings growth (8%) is offset by a somewhat lower dividend yield (1.8%) and a higher multiple reversion (3.2%). McCormick continues to be the dominate player in its industry and that should continue thanks to RB Foods. The company is fairly recession proof and has a proven dividend growth track record. McCormick is an excellent long-term hold. Now is not the best time to buy shares of this stock, however, due to the high valuation.

## Total Return Breakdown by Year

