



The Kraft-Heinz Company (KHC)

Updated May 22th, 2018 by Jonathan Weber

Key Metrics

Current Price: \$57	5 Year CAGR Estimate: 12.0%	Quality Percentile: N/A
Fair Value Price: \$64	5 Year Growth Estimate: 5.3%	Momentum Percentile: N/A
% Fair Value: 89%	5 Year Valuation Multiple Estimate: 2.3%	Total Return Percentile: N/A
Dividend Yield: 4.4%	5 Year Price Target \$82	Valuation Percentile:

Overview & Current Events

Kraft-Heinz is a processed food and beverages company whose product portfolio includes condiments, sauces, cheese & dairy, frozen & chilled meals, infant diet and nutrition. The company was created in 2015 (in a merger between Kraft Food Group and H. J. Heinz Company). Kraft-Heinz is headquartered in Chicago, IL, and is currently valued at \$71 billion.

Kraft-Heinz' most recent results were announced on May 2nd. The company reported earnings per share of \$0.89, an increase of 6% year over year. The company's revenues of \$6.3 billion were unchanged from the prior year's quarter.

Growth on a Per-Share Basis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
EPS	-	-	-	-	-	-	-	\$2.19	\$3.33	\$3.55	\$3.75	\$4.85
DPS	-	-	-	-	-	-	-	\$1.13	\$2.35	\$2.45	\$2.55	\$3.25

The Kraft-Heinz Company doesn't have a long history in the form it currently exists in (the two companies that merged to create Kraft-Heinz both have a long history, though), which is why there isn't a lot of historic data.

As a food and beverages company Kraft-Heinz is not operating in a high-growth industry, the company therefore will, in all likelihood, not be able to generate enormous growth rates going forward. Even in a low-growth industry companies can generate solid returns, though, in Kraft-Heinz' case there are several avenues for growth the company can pursue. The first is international expansion. During the most recent quarter Kraft-Heinz has been able to grow its revenues organically in all geographic markets except for the United States. Kraft-Heinz' Rest-of-World- segment (which includes Latin America, Asia-Pacific, Russia, India) is a promising growth vector going forward. Market penetration is not very high yet (annual revenues for Kraft-Heinz total about \$3 billion), but the market is huge and growing relatively quickly. Due to steadily rising disposable incomes in countries such as China and India more consumers have the means to purchase consumer goods from Western companies such as Kraft-Heinz.

Another factor for earnings growth is margin expansion. This usually is easier when revenues are increasing (due to improving economics of scale and operating leverage), but Kraft-Heinz managed to increase its operating income in the last quarter even without any top line growth. Kraft-Heinz is headed by Bernardo Hees and Alex Behring, two 3G Capital managers (that orchestrated the merger that created the company), that are famous for their cost-cutting expertise. Kraft-Heinz continues to deliver on that front, lowering its product costs and its operating expenses continually.

Valuation Analysis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	Now	2023
Avg. P/E	-	-	-	-	-	-	-	18.5	24.9	24.2	15.2	17.0
Avg. Yld.	-	-	-	-	-	-	-	2.8%	2.8%	2.9%	4.4%	4.2%

Kraft-Heinz has been valued at a relatively high valuation in 2016 and 2017, especially when we factor in that its growth rate hasn't been particularly high, and will very likely not be high in the future either. The high valuation can, most likely, be attributed to the fact that income investors piled into the stock after the company was created, as fixed income investments did offer even worse income yields, which pushed prices up.

Right now Kraft-Heinz is looking relatively inexpensive, but its valuation will most likely remain well below a 20 P/E ratio as income investors have more alternatives in a rising rates environment. Kraft-Heinz' yield of 4.4% is looking quite compelling right now, even though the dividend growth rate is not especially high.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
GP/A	-	-	-	-	-	-	-	4.7%	8.0%	8.1%	9.0%	11.0%
Debt/A	-	-	-	-	-	-	-	52.8%	52.5%	45.0%	42.0%	40.0%
Int. Cov.	-	-	-	-	-	-	-	1.8	5.4	5.5	6.0	7.0
Payout	-	-	-	-	-	-	-	51.6%	70.6%	69.1%	68.0%	67.0%
Std. Dev.	-	-	-	-	-	-	-	18.2%	13.6%	13.5%	17.0%	16.0%

Kraft-Heinz has a huge asset base, although most of those assets do not consist of material things like plants, buildings and machines but of intangible assets and goodwill. These two items make up \$104 billion of the company's \$121 billion in assets. Their size can be explained by the fact that the company was recently established in a huge merger. Those assets are more of an accounting item than something that had to be bought with cash, but they are the reason for a huge amount of assets on the company's balance sheet and therefore for a low gross profit to assets ratio. When we exclude these two items from Kraft-Heinz' balance sheet, its gross profits to tangible assets ratio would be very strong at roughly 53%. Kraft-Heinz' balance sheet holds a sizeable amount of debt, but due to a solid interest coverage ratio and a non-cyclical business the company is not overleveraged. Kraft-Heinz' strategy (paying down debt to reduce its leverage) nevertheless looks like an opportune move in a rising rates environment.

Kraft-Heinz' brands are strong and recognized by most consumers, and demand for its products is not cyclical or dependent on economic conditions. Kraft-Heinz therefore should be able to remain profitable in economic downturns, as do most consumer staples. The brands function as competitive advantages.

Final Thoughts & Recommendation

Kraft-Heinz, created by Warren Buffett's Berkshire Hathaway and 3G Capital, is one of the biggest food & beverages companies in the world. Its growth rates are not overly high, but with International expansion and a focus on costs the company still is able to create some earnings growth. Coupled with a sizeable dividend yield and an inexpensive valuation this should be enough for solid total returns over the coming years. Kraft-Heinz is a buy at current prices, especially for income investors looking for a high degree of safety.

Total Return Breakdown by Year

