JM Smucker (SJM)

Updated May 2nd, 2018 by Josh Arnold

Key Metrics

Current Price:	$115	**5 Year CAGR Estimate:**	11.2%	**Quality Percentile:**	N/A
Fair Value Price:	$135	**5 Year Growth Estimate:**	5.2%	**Momentum Percentile:**	N/A
% Fair Value:	85%	**5 Year Valuation Multiple Estimate:**	3.3%	**Total Return Percentile:**	N/A
Dividend Yield:	2.7%	**5 Year Price Target**	$174	**Valuation Percentile:**	N/A

Overview & Current Events

JM Smucker was founded in 1897 by its namesake in Ohio. He began with just an apple cider mill and small batches of apple butter. In the 121 years since, SJM has grown into an international powerhouse of packaged food and beverage products with high levels of name recognition. It has a market cap of $13B and should do $7.4B in revenue this year.

SJM's recent Q3 report was tough as it saw just 1% sales growth and lower gross margins. SJM's margins have been under pressure as a result of fierce competition that has led to promotions and discounting, crimping profitability. It has been growing sales at strong long-term rates due to acquisitions, however, so it has thus far been able to improve EPS despite weak gross margins. Lower levels of overhead costs are helping SJM overcome weak gross margins as well but guidance for the rest of this year wasn't particularly inspiring. It did recently announce a large pet food acquisition in Ainsworth, a purchase that would add a very meaningful $800M in annual sales and see SJM grow once again.

Growth on a Per-Share Basis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
EPS	$3.77	$4.37	$4.79	$4.73	$5.37	$5.64	$5.35	$5.89	$6.49	$7.72	***$8.15***	***$10.50***
DPS	$1.31	$1.45	$1.68	$1.92	$2.08	$2.32	$2.56	$2.68	$3.00	$3.09	***$3.12***	***$4.20***

SJM's EPS growth has been steady in the past decade considering the varying economic environments we've seen in that time. YoY declines have been slight when they've occurred and growth always returns the next year, the product of SJM's focus on acquisitions and cost savings. Its margins have been in question of late due to pricing pressures as well as commodity and freight inflation. However, SJM is heavily weighted toward the at-home coffee market and as of today, that is a good place to be. Its Ainsworth purchase will add significant bulk to its pet nutrition business and provide another catalyst for growth moving forward. As a result of all of these factors, we are expecting 5.2% EPS growth for the next five years, representing a significant slowdown from its historical average of roughly double that level. The reason we are more cautious on SJM is because of the slowdown in organic revenue growth as well as margin pressures, which are showing no signs of abating. SJM still offers some growth potential but not to the extent it has in the past.

We see mid-single digit growth in the dividend as well as SJM remains committed to returning cash to shareholders. Continued growth in EPS should allow for the payout ratio to remain roughly where it is today while rewarding long term shareholders with higher levels of cash returned over time.

Valuation Analysis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	Now	2023
Avg. P/E	12.0	12.5	13.2	16.2	16.0	18.3	19.6	20.1	21.0	16.9	***14.1***	***16.6***
Avg. Yld.	2.9%	2.7%	2.7%	2.5%	2.4%	2.2%	2.4%	2.3%	2.2%	2.4%	***2.7%***	***2.4%***

SJM's P/E multiple soared in recent years but has since come back down to what is nearly a decade low at 14.1. That makes the stock look like it is trading appreciably under fair value at this point and as a result, we see the P/E multiple increasing over time from the current 14.1 to over 16. That should provide a strong 3.3% tailwind to annual total returns going forward as investors seem to have digested SJM's slower rates of growth.

Given that we see a higher P/E multiple, the yield is likely to come down from 2.7% to 2.4%, which is a more normalized level for SJM. Dividend raises will continue but this is a secondary reason to own the stock at this point.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
GP/A	20.8%	27.2%	37.0%	32.5%	31.3%	36.1%	35.7%	25.2%	40.1%	38.4%	***38.2%***	***37.5%***
Debt/A	42%	40%	33%	36%	43%	43%	44%	58%	56%	56%	***62%***	***56%***
Int. Cov.	6.7	8.3	12.8	11.7	9.8	9.8	11.7	2.4	6.7	6.4	***5.5***	***7.0***
Payout	34%	32%	34%	40%	38%	40%	46%	45%	45%	43%	***38%***	***40%***
Std. Dev.	34.8%	27.8%	16.7%	18.0%	16.6%	15.1%	13.6%	16.0%	20.2%	24.5%	***23.0%***	***20.0%***

SJM's quality metrics have deteriorated somewhat in recent years but the moves have been slight and haven't impaired its financial position or growth. Gross margins have been and remain a concern for the reasons cited above and we see gradually lower gross margins going forward. Company debt is reasonable but should grow with the Ainsworth acquisition before settling back down into the mid-50% range. SJM is looking to offload its baking unit to offset some of the cost of Ainsworth. Interest coverage is ample, and the payout ratio is around 40%, making the dividend safe.

SJM's recession performance is terrific as it sells consumer staples and thus, its revenue isn't at great risk during downturns. Expect SJM to perform well once again during the next recession. Its competitive advantages include its large suite of highly recognizable consumer brands as well as its global distribution network. SJM leverages its 120+ year operating history in its advertising, conveying trust and quality to consumers, which drives positive brand perception.

Final Thoughts & Recommendation

Overall, SJM's growth profile has been impaired in recent years but the stock has traded down as a result, putting its valuation back in line with expectations. Years of weak stock returns relative to the market have put SJM in a position where total returns from here should be very favorable at 11.2%, consisting of the 2.7% yield, 5.2% EPS growth and 3.3% tailwind from the rising multiple. SJM is unlikely to return to double digit EPS growth anytime soon but its current valuation is favorable for those seeking a nice yield and safe, moderate growth at a reasonable price. We like SJM here for this reason as its slower rates of forward growth appear priced in after years of subpar returns.