Brown-Forman (BF-B)

Updated August 9th, 2018 by Jonathan Weber

Key Metrics

Current Price:	$54	**5 Year CAGR Estimate:**	6.2%	**Volatility Percentile:**	42.2%
Fair Value Price:	$44	**5 Year Growth Estimate:**	8.8%	**Momentum Percentile:**	87.9%
% Fair Value:	122%	**5 Year Valuation Multiple Estimate:**	-3.8%	**Valuation Percentile:**	28.5%
Dividend Yield:	1.2%	**5 Year Price Target**	$67	**Total Return Percentile:**	36.9%

Overview & Current Events

Brown-Forman is an alcoholic beverages company that is based in Louisville. The company was founded in 1870 and has a market capitalization of $25 billion. Brown-Forman produces and sells whiskeys, vodka, tequila, champagne and wine. Its brands include Jack Daniel's, Finlandia Vodka, Old Forester and many more.

Brown-Forman reported its fourth quarter results on June 6. During Q4 the company earned $0.23 per share, a decrease of 24% year over year. Profits were negatively impacted by the formation of a charitable foundation during the fourth quarter, which cost $70 million. Revenues were up by 6% during Q4, hitting $730 million during the quarter.

Management has guided for sales growth of 6%-7% during fiscal 2019. Earnings per share are forecasted to fall in a range of $1.75 to $1.85 during FY 2019.

Growth on a Per-Share Basis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
EPS	$0.82	$0.95	$0.95	$1.07	$1.22	$1.28	$1.38	$1.37	$1.65	$1.67	***$1.80***	***$2.74***
DPS	$0.31	$0.33	$0.36	$0.39	$0.44	$0.48	$0.52	$0.56	$0.59	$0.63	***$0.67***	***$0.97***

Brown-Forman has a strong growth track record. The company has been able to increase its profits even during the last financial crisis. In 2016 profitability declined slightly, but during the 2012 to 2017 time frame Brown-Forman still grew its profits per share by an attractive nine percent annually.

Adjusted for the formation of the charity during fiscal 2018 profits grew slightly during the last year. Underlying earnings growth was stronger than reported earnings growth due to a negative currency rate impact.

Brown-Forman's earnings growth has been based on revenue growth and some margin increases in the past. Thanks to the fact that Brown-Forman owns strong brands and is active in the super-and ultra-premium alcoholic beverages markets, which see consistent market growth, Brown-Forman should be able to keep its revenues growing going forward.

Brown-Forman's Jack Daniels brand as well as its American super-premium whiskeys showed strong growth during 2018. According to management momentum will remain positive during fiscal 2019.

Higher overall sales allow for margin increases due to better economics of scale, which makes the company more efficient overall. Share repurchases, which have lowered Brown-Forman's share count considerably over the last decade, have had a positive impact on the company's earnings per share growth as well. Brown-Forman has recently announced a new $200 million share repurchase program.

Valuation Analysis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	Now	2024
Avg. P/E	16.1	17.9	21.4	24.1	24.7	28.4	28.8	27.6	33.2	32.0	***29.9***	***24.6***
Avg. Yld.	2.4%	1.9%	1.8%	1.5%	1.4%	1.3%	1.3%	1.5%	1.1%	1.1%	***1.2%***	***1.4%***

Shares of Brown-Forman were never trading at an especially cheap valuation, but over the last couple of years the company's multiples rose to an even higher level. Right now shares are valued at ~30 times 2019's earnings.

Disclosure: This analyst has no position in the security discussed in this research report, and no plans to initiate one in the next 72 hours.

This is a premium over the long-term median, which is why we forecast some multiple contraction going forward. Brown-Forman does not pay out a high quarterly dividend yield, but it makes special dividend payments regularly. Including its most recent special dividend payment of $1.00 per share its trailing dividend yield is 3.0%.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
GP/A	45.4%	47.6%	46.4%	51.7%	54.0%	50.7%	52.0%	51.2%	43.6%	44.2%	***44.7%***	***45.0%***
Debt/A	47.7%	44.1%	44.5%	40.5%	55.1%	50.5%	54.4%	62.7%	70.4%	73.5%	***75.0%***	***80.0%***
Int. Cov.	21.5	25.5	33.0	28.3	27.3	40.5	41.1	34.9	17.7	11.9	***11.0***	***10.0***
Payout	37.8%	34.7%	37.9%	36.4%	36.1%	37.5%	37.7%	40.9%	35.8%	37.7%	***37.2%***	***35.3%***
Std. Dev.	29.5%	20.5%	26.2%	16.6%	16.6%	16.5%	18.1%	18.6%	20.1%	21.1%	***20.0%***	***19.0%***

Brown-Forman has leveraged up over the last decade, financing close to three quarters of its assets with debt. The company is in no way overleveraged, though, as the interest coverage ratio remains very high. Brown-Forman has taken advantage of the very low interest rates over the last couple of years, which is an intelligent and opportunistic move.

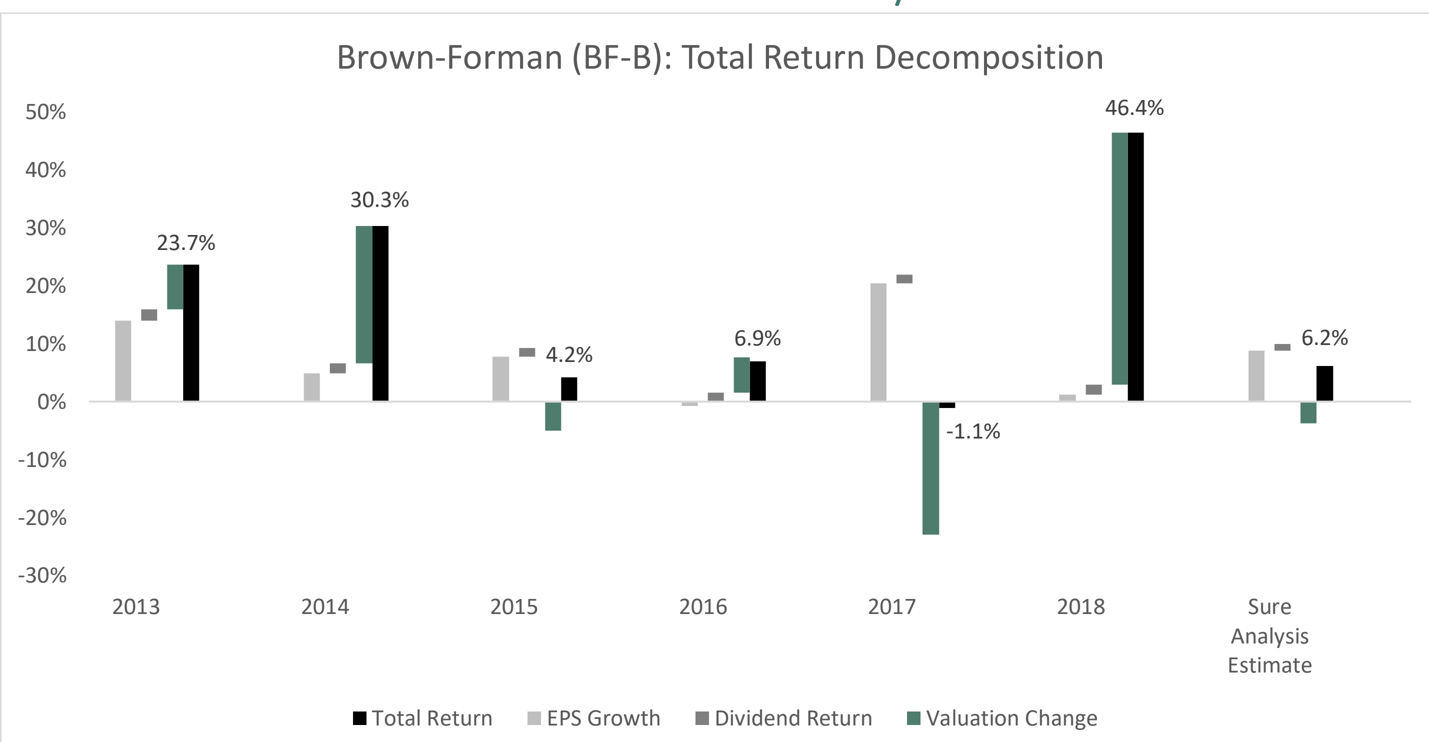
Brown-Forman's strong brands and the tendency of customers to stick with the brands they like is a big competitive advantage, along with the fact that Brown-Forman is one of the largest players in its industry, which allows for better economics of scale and a wider geographic reach.

During the last financial crisis Brown-Forman remained highly profitable and actually increased its earnings, which is unsurprising as demand for alcohol tends to be consistant. Brown-Forman should be able to weather recessions well.

Final Thoughts & Recommendation

Brown-Forman is a high-quality company with strong fundamentals, a great track record and Dividend Aristocrat status. Earnings growth over the coming years should be solid, but the high valuation will be a headwind for Brown-Forman's total returns over the coming five years. We rate Brown-Forman a great business, but due to the high valuation the stock is not a buy today. At or below fair value Brown-Forman would be a compelling buy. It earns a hold recommendation today.

Total Return Breakdown by Year



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