General Mills (GIS)

Updated August 10th, 2018 by Aristofanis Papadatos

Key Metrics

Current Price:	$45	**5 Year CAGR Estimate:**	10.5%	**Volatility Percentile:**	30.8%
Fair Value Price:	$52	**5 Year Growth Estimate:**	3.2%	**Momentum Percentile:**	9.2%
% Fair Value:	86%	**5 Year Valuation Multiple Estimate:**	3.0%	**Valuation Percentile:**	82.3%
Dividend Yield:	4.3%	**5 Year Price Target**	$61	**Total Return Percentile:**	68.9%

Overview & Current Events

General Mills is a packaged food giant, with more than 100 brands and operations in more than 100 countries. It generates 65% of its sales in North America. Since it peaked two years ago, General Mills has dramatically underperformed the market, as it has lost 37% whereas S&P has rallied 31%. The main reasons behind this are rising interest rates, the acquisition of Blue Buffalo and the lackluster business performance of the company.

General Mills has not cut its dividend for 118 consecutive years. Thanks to this record, most of its shareholders own the stock for its dividend. However, now that interest rates are on the rise, the dividend of General Mills has become less attractive. The stock has also been burdened by its takeover of Blue Buffalo. As General Mills has a market cap of $27 billion, its $8 billion acquisition represents 30% of its market cap. The market is afraid that management does not see promising prospects in the core business of the company while the takeover may prove too large to assimilate.

General Mills has been facing some major challenges in recent years. As consumers have become more health-conscious, the company has failed to grow the sales of its flagship products. Moreover, competition has greatly heated in breakfast products and yogurt while large retailers have been pressuring their food suppliers for lower prices. As a result, General Mills has failed to meaningfully grow its revenues and earnings in the last five years.

In late June, General Mills reported (6/27/18) its financial results for fiscal 2018. It was just another year of lackluster performance for the company, as its organic sales and its earnings per share remained essentially flat. Moreover, management stated that it expected the annual sales to remain flat and the earnings per share to remain flat or decrease up to 3% in fiscal 2019. On the bright side, General Mills seems to be putting an effective stop in the bleeding process of its yogurt segment. About a year ago, the sales of this segment were falling about 20% on an annual basis. However, in the last three quarters, they have decreased by 11%, 8% and 5%, respectively, thus indicating that the segment is somewhat stabilizing and may return to growth trajectory from next year.

General Mills has great growth potential in the organic market. The company expects to surpass $1 billion in organic sales next year but the segment generates just 5% of its revenue and hence it cannot move the needle in its overall results. On the other hand, General Mills has promising prospects in pet food thanks to its takeover of Blue Buffalo. This $30 billion market has grown at a 5% average annual rate in the last decade and has not shown any signs of fatigue. Thanks to the strong brand of Blue Buffalo, this acquisition is a great vehicle for General Mills to return to growth mode.

Growth on a Per-Share Basis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
EPS	$1.99	$2.30	$2.48	$2.56	$2.69	$2.83	$2.86	$2.92	$3.08	**$3.11**	***$3.11***	***$3.61***
DPS	$0.86	$0.96	$1.12	$1.22	$1.32	$1.55	$1.67	$1.78	$1.92	**$1.96**	***$1.96***	***$2.08***

General Mills has grown its earnings-per-share at a 5.9% average annual rate in the last decade but it has decelerated in recent years and has thus grown its earnings-per-share at a 2.9% average annual rate in the last five years. Thanks to the growth prospects of Blue Buffalo and the improving outlook of the yogurt segment, the company is likely to grow its earnings by about 4.0% per year on average from 2020. For fiscal 2019 we assume flat EPS, as per management's guidance. Therefore, the company is likely to grow its EPS by about 3.2% per year on average over the next five years.

Valuation Analysis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	Now	2024
Avg. P/E	16.5	15.2	14.3	14.7	15.1	15.7	17.8	18.6	20.0	20.5	***14.5***	***16.8***
Avg. Yld.	2.7%	2.9%	2.9%	3.1%	3.2%	3.1%	3.1%	3.1%	3.1%	3.0%	***4.3%***	***3.4%***

Due to the above-mentioned headwinds, General Mills is trading at a P/E of 14.5, which is much lower than its 10-year average P/E of 16.8. This equates to a 3.0% annual tailwind from valuation multiple gains if General Mills' valuation mean reverts over the next five years.

Safety, Quality, Competitive Advantage, & Recession Resiliency

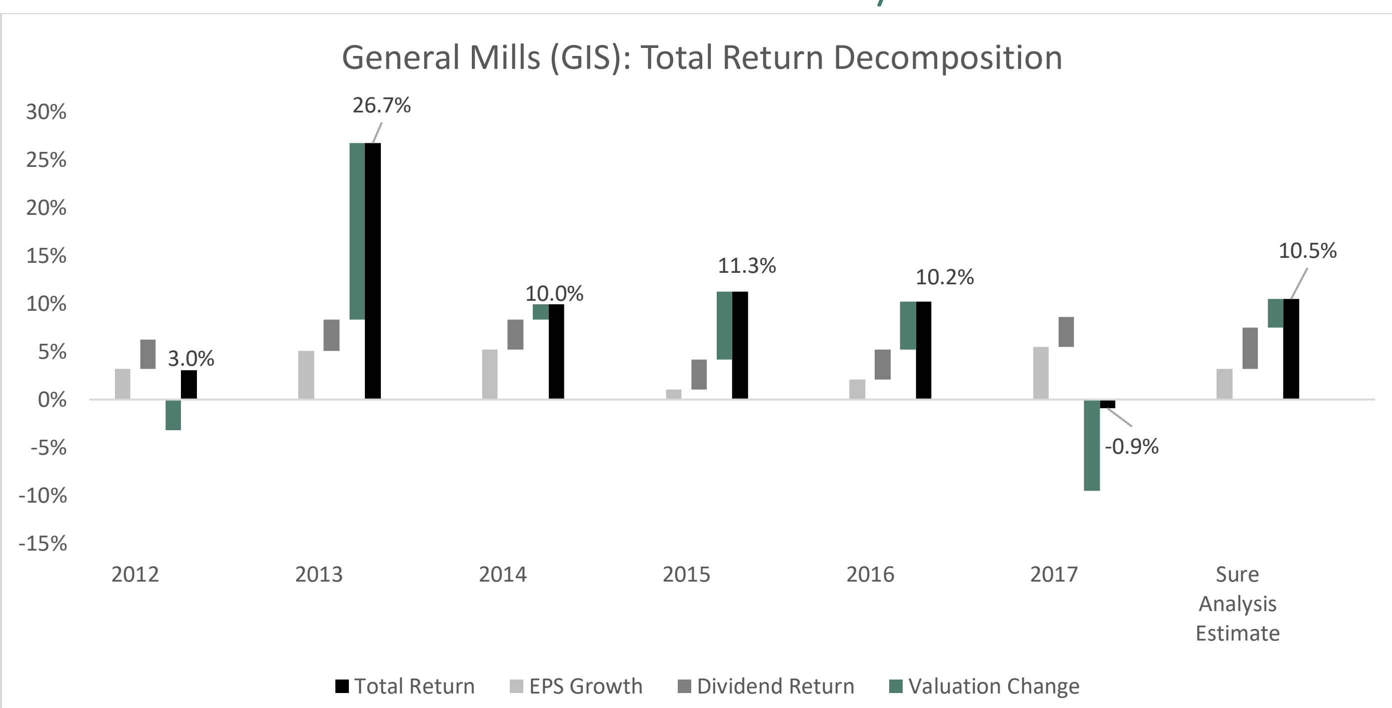
Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
GP/A	29.3%	32.8%	31.9%	28.7%	28.4%	27.5%	27.2%	26.8%	25.5%	**24.4%**	***24.0%***	***25.0%***
Debt/A	69.7%	68.1%	64.6%	67.4%	68.5%	65.5%	75.3%	75.6%	78.5%	**78.0%**	***78.0%***	***75.0%***
Int. Cov.	6.1	7.1	8.0	7.3	9.0	9.8	6.6	8.9	8.7	**7.0**	***7.0%***	***8.5***
Payout	43.2%	41.7%	45.2%	47.7%	49.1%	54.8%	58.4%	61.0%	62.3%	**63.0%**	***63.0%***	***57.6%***
Std. Dev.	20.6%	12.5%	12.1%	7.9%	15.8%	11.4%	10.6%	18.9%	15.7%	**18.0%**	***17.0%***	***16.0%***

Due to the acquisition of Blue Buffalo, General Mills has announced that it will freeze its current dividend until it reduces its debt load to a more comfortable level. On the other hand, as the stock is trading around its 5-year lows, its dividend yield has climbed to an almost decade-high level of 4.3%. Moreover, the stock has proved markedly resilient during recessions thanks to the strength of its brands. In the Great Recession, while most companies saw their earnings collapse, General Mills grew its earnings-per-share by more than 10% per year from 2007 to 2010.

Final Thoughts & Recommendation

Thanks to its dramatic underperformance, General Mills is now trading at an opportune valuation and is offering an almost decade-high dividend yield. Therefore, it can offer a 10.5% average annual return over the next five years thanks to 3.2% EPS growth, a 4.3% dividend and a 3.0% annualized gain from P/E expansion. General Mills is a buy at current prices for conservative investors looking for a higher yield and double-digit expected total returns.

Total Return Breakdown by Year



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.