



The Kraft-Heinz Company (KHC)

Updated August 3rd, 2018 by Jonathan Weber

Key Metrics

Current Price: \$64	5 Year CAGR Estimate: 9.2%	Volatility Percentile: 20.6%
Fair Value Price: \$64	5 Year Growth Estimate: 5.3%	Momentum Percentile: 5.6%
% Fair Value: 100%	5 Year Valuation Multiple Estimate: 0.0%	Valuation Percentile: 61.2%
Dividend Yield: 3.9%	5 Year Price Target: \$82	Total Return Percentile: 59.0%

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 \$73 billion.

Kraft-Heinz reported its second quarter earnings results on August 3. The company reported earnings per share of \$1.00, an increase of 2% year over year. Revenues rose by 1%, hitting \$6.7 billion during the second quarter.

Management's comments during the Q2 earnings call were positive, pointing towards higher revenue growth during H2. Recently there has been talk about a possible bid for Campbell Soup by Kraft-Heinz, but so far nothing has come of it.

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 does not have a long history in the form it currently exists in, which is why there we are not able to provide much data. The two companies that merged to create Kraft-Heinz both have a long history, though.

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 second quarter, Kraft-Heinz was been able to grow its revenues at a strong pace in the EMEA region (9%) and in the Rest-of-World segment (14%), which includes Latin America, Asia-Pacific, Russia, India. Market penetration in the RoW is not high. Annual revenues for Kraft-Heinz total \$3 billion. The market is huge and growing relatively quickly, though. 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' management is experienced in cutting costs.

Kraft-Heinz is headed by Bernardo Hees and Alex Behring, two 3G Capital managers that are famous for their cost-cutting expertise. Kraft-Heinz continues to deliver on that front, lowering its product costs and its operating expenses.

Valuation Analysis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	Now	2023
Avg. P/E	-	-	-	-	-	-	-	18.5	24.9	24.2	17.1	17.0
Avg. Yld.	-	-	-	-	-	-	-	2.8%	2.8%	2.9%	3.9%	4.2%

Relative to the company's growth rate, which is not overly high, shares have traded at high valuations during 2016 and 2017. This was probably due to income investors that piled into the stock on the search for income. Due to rising bond yields, Kraft-Heinz' valuation will most likely be substantially lower going forward. We deem a PE ratio of 17 fair, which is in line with the price after the post-earnings share price pop.

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.

Shares of Kraft-Heinz yield 3.9% right now, which is an attractive yield relative to what investors can get from the broad market or peers from the food and beverages industry.

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 items 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. When we adjust for these two items, Kraft-Heinz' gross profits to tangible assets ratio is very compelling, 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. The recent trend of declining debt levels is a positive.

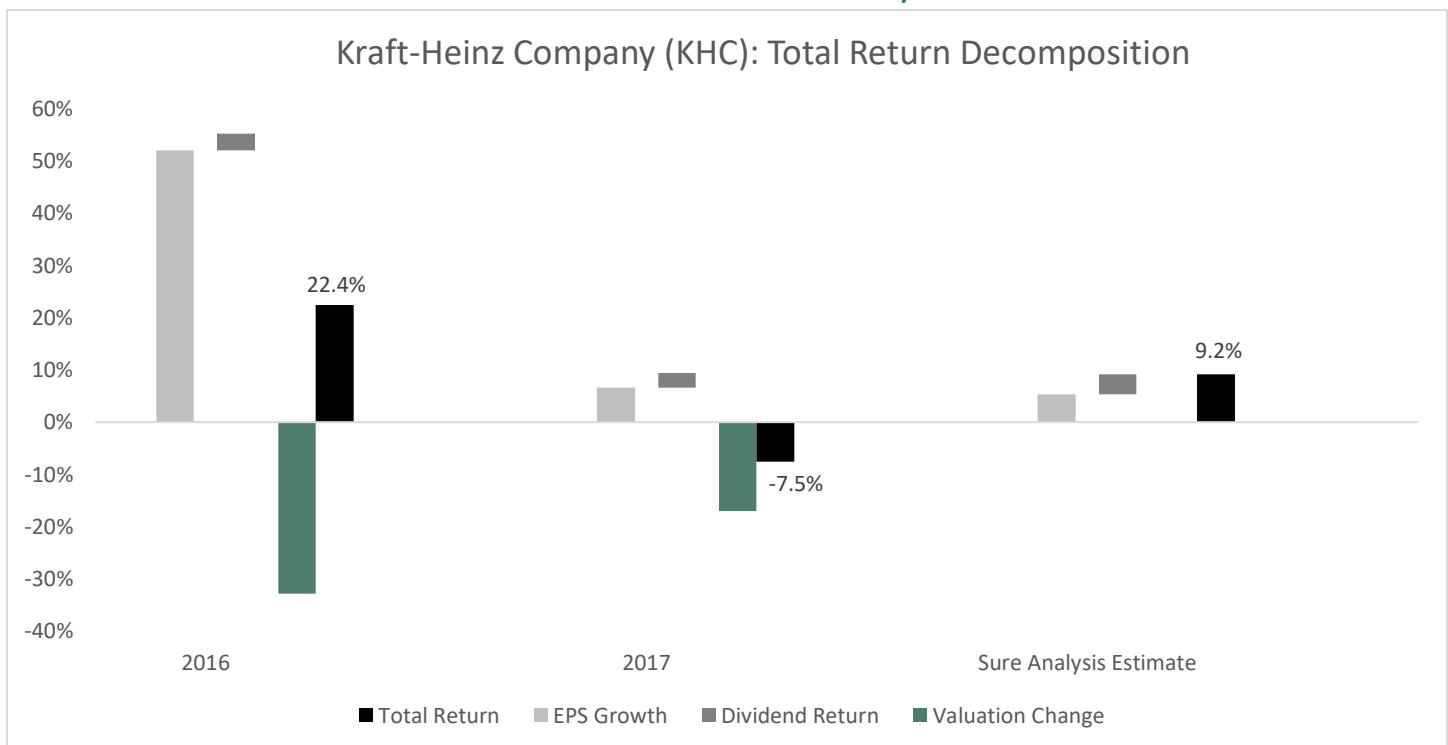
Kraft-Heinz' brands are strong and recognized by most consumers, and demand for its products is not cyclical or dependent on economic conditions. Kraft-Heinz therefore should be able to remain profitable in economic downturns, as do most consumer staples. The brands function as competitive advantages.

Final Thoughts & Recommendation

3G and Buffett's Berkshire Hathaway have created a food and beverages giant. Growth rates are not overly high and will not be overly high in the future, either. But when we factor in a strong dividend yield, Kraft-Heinz' shares should still deliver solid total returns over the coming years.

Kraft-Heinz' low-risk business model, non-cyclical demand for its products and a safe dividend yield make Kraft-Heinz a potential buy for income investors looking for more exposure to the food and beverages sector.

Total Return Breakdown by Year



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