JM Smucker (SJM)

Updated August 22nd, 2018 by Josh Arnold

Key Metrics

Current Price:	$108	**5 Year CAGR Estimate:**	13.8%	**Volatility Percentile:**	47.1%
Fair Value Price:	$140	**5 Year Growth Estimate:**	5.2%	**Momentum Percentile:**	11.7%
% Fair Value:	77%	**5 Year Valuation Multiple Estimate:**	5.5%	**Valuation Percentile:**	93.7%
Dividend Yield:	3.1%	**5 Year Price Target**	$182	**Total Return Percentile:**	89.1%

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 capitalization of $12.3 billion and should do $8 billion in revenue this year.

Smucker reported Q1 earnings on 8/21/18 and results were disappointing to investors. The company's revenue rose 9% but when excluding the recent Ainsworth Pet acquisition, sales fell 1%. Smucker cited lower pricing as the culprit for lower revenue as volume/mix was flat. Adjusted operating income rose 5%, reflecting the gains from Ainsworth as well as higher selling costs, which offset some of the gain in revenue. Smucker also announced it had signed an agreement to sell its US baking business for proceeds of $315 million after taxes. That reduced the revenue outlook for this year by $300 million but earnings-per-share guidance remained the same; our estimate of $8.50 is unchanged as a result.

Growth on a Per-Share Basis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
EPS	$4.37	$4.79	$4.73	$5.37	$5.64	$5.35	$5.89	$6.49	$7.72	$8.06	***$8.50***	***$10.95***
DPS	$1.45	$1.68	$1.92	$2.08	$2.32	$2.56	$2.68	$3.00	$3.09	$3.12	***$3.40***	***$4.20***

Smucker's earnings-per-share 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. This is the product of the company'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, Smucker 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 business and provide another catalyst for growth moving forward. As a result of all of these factors, we are expecting 5.2% earnings-per-share 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 is because of the slowdown in organic revenue growth as well as margin pressures, which are showing no signs of abating. Indeed, relatively weak Q1 results reflect these concerns. Smucker 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 Smucker remains committed to returning cash to shareholders. Continued growth in earnings 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	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	Now	2024
Avg. P/E	12.5	13.2	16.2	16.0	18.3	19.6	20.1	21.0	16.9	14.2	***12.7***	***16.6***
Avg. Yld.	2.7%	2.7%	2.5%	2.4%	2.2%	2.4%	2.3%	2.2%	2.4%	2.7%	***3.1%***	***2.3%***

Smucker's price-to-earnings multiple soared in recent years but has since come back down to what is nearly a decade low at 12.7. Thus, the stock is trading appreciably under fair value, and we see the multiple increasing over time to more than 16. That should provide a strong 5.5% tailwind to annual total returns going forward.

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.

Given that we see a higher price-to-earnings multiple, the yield is likely to come down from 3.1% to 2.3%, which is a more normalized level for Smucker. Dividend raises will continue but this is a secondary reason to own the stock.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
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%	***40%***	***38%***
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%***

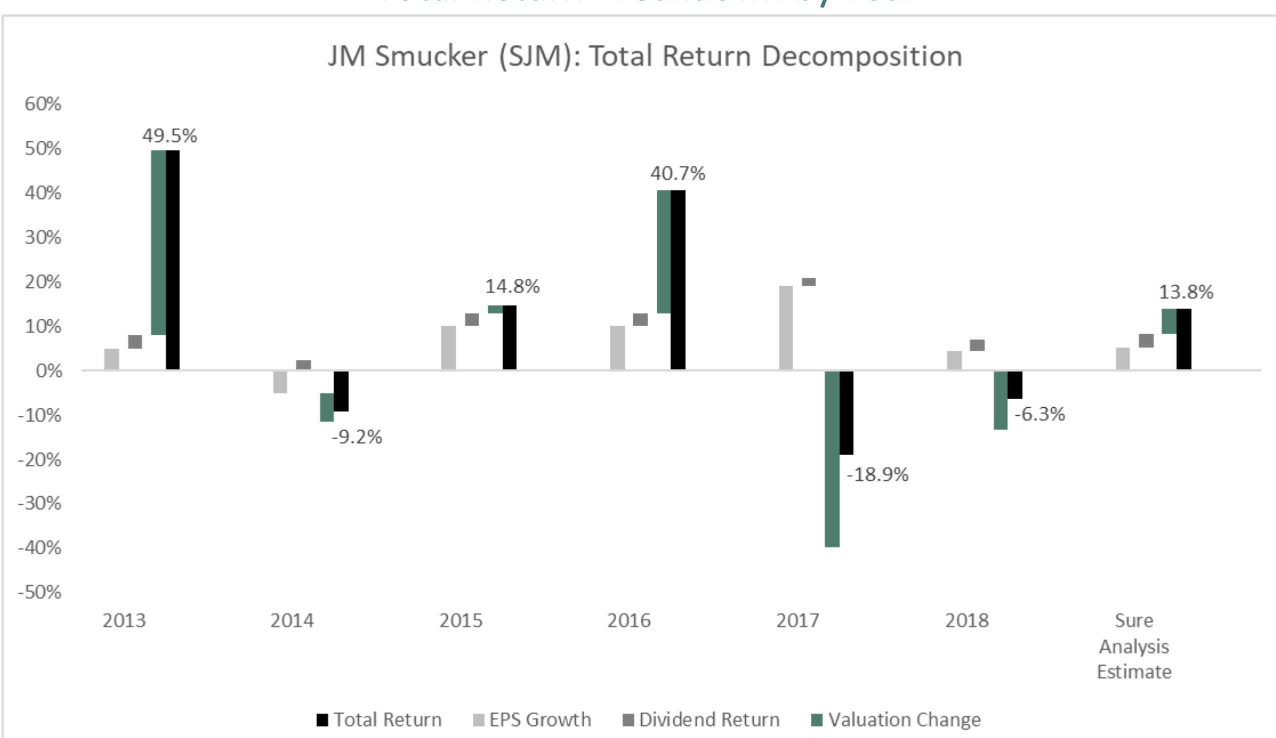
Smucker's quality metrics have deteriorated somewhat in recent years, but the moves have been slight and have not impaired its financial position or growth. Margins have been and remain a concern for the reasons cited above and we see gradually lower margins going forward. Debt is reasonable but should grow with the Ainsworth acquisition before settling back down into the mid-50% range; the divestiture of the US baking unit will help with this. Interest coverage is ample, and the payout ratio is just 40%, making the dividend safe.

Smucker's recession performance is terrific as it sells consumer staples and thus, its revenue is not at great risk during downturns; expect it 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. Smucker leverages its 120+ year operating history in its advertising, conveying trust and quality to consumers, which drives positive brand perception.

Final Thoughts & Recommendation

Overall, Smucker'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 Smucker in a position where total returns from here should be very favorable at 13.8%, consisting of the 3.1% yield, 5.2% earnings growth and 5.5% tailwind from the rising multiple. Smucker is unlikely to return to double-digit earnings growth anytime soon, but its current valuation is favorable for those seeking a nice yield and safe, moderate growth at a reasonable price. We rate it a buy for this reason; its slower rates of forward growth appear priced in after years of subpar returns.

Total Return Breakdown by Year



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