The Hershey Company (HSY)

Updated October 26th, 2018 by Jonathan Weber

Key Metrics

Current Price:	$103	**5 Year CAGR Estimate:**	8.6%	**Volatility Percentile:**	38.8%
Fair Value Price:	$100	**5 Year Growth Estimate:**	6.4%	**Momentum Percentile:**	56.0%
% Fair Value:	103%	**5 Year Valuation Multiple Estimate:**	-0.6%	**Growth Percentile:**	57.4%
Dividend Yield:	2.8%	**5 Year Price Target**	$136	**Valuation Percentile:**	42.1%
Dividend Risk Score:	B	**Retirement Suitability Score:**	B	**Total Return Percentile:**	42.1%

Overview & Current Events

The Hershey Company is chocolate and sugar confectionary products manufacturer that sells brands such as Hershey's and Reese's. Hershey operates in North America as well as internationally. The company is headquartered in Hershey, PA. Hershey was founded in 1894 and trades with a market capitalization of $21 billion.

Hershey reported its third quarter earnings results on October 25. The company generated revenues of $2.08 billion, an increase of 2.5% year over year. Currency rates did negatively impact the company's revenue growth, but that was offset by acquisitions that Hershey made during the past year.

Hershey was able to grow its earnings-per-share by 20% year over year, Q3's earnings-per-share totaled $1.55. Hershey has reiterated that it sees earnings-per-share for fiscal 2018 in a range of $5.33 to $5.43, which represents an increase of 15% versus fiscal 2017. Management forecasts a sales growth rate of ~4.5% during fiscal 2018.

Growth on a Per-Share Basis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
EPS	$1.88	$2.17	$2.55	$2.82	$3.24	$3.72	$3.98	$4.12	$4.41	$4.76	***$5.38***	***$7.34***
DPS	$1.19	$1.19	$1.28	$1.38	$1.56	$1.81	$2.04	$2.24	$2.40	$2.55	***$2.76***	***$3.87***
Shares	227	228	227	225	224	224	221	217	212	211	***209***	***202***

Hershey has recorded both strong and consistent growth over the last decade. Earnings-per-share have grown every year since 2008. Earnings-per-share grew at an annualized rate of 11% over the last decade. Hershey's earnings-per-share growth stems from several factors. The first one is organic revenue growth, which Hershey has managed to achieve despite the public becoming more conscious about healthy eating habits over the last decade.

Hershey also was able to improve its margins throughout the last decade. Hershey owns well-recognized brands. Pricing increases thus were not a headwind towards selling increasing volumes of its products. Hershey has also been repurchasing its shares relatively consistently over the last couple of years, which has added some additional growth to the company's earnings-per-share, above the already quite solid net earnings growth rate. In 2018 Hershey's earnings-per-share growth will be above the long-term average, but that is primarily due to the impact of a lower tax rate and the effect of the Amplify acquisition, which will be responsible for the majority of the company's revenue growth. Beyond 2018 Hershey will likely still be able to keep its top line growing, but future margin increases will be harder to achieve. This is why Hershey's earnings-per-share growth will most likely come down to a sub-10% level beyond 2018.

The company has raised its dividend at a solid rate of 8.8% annually since 2008, a growth rate that was a bit below its profit growth rate over the same time frame. 2018's dividend increase of 10.1% is slightly higher than the average.

Valuation Analysis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	Now	2023
Avg. P/E	19.5	16.9	17.9	19.8	20.9	24.2	24.5	23.0	21.9	22.8	***19.1***	***18.5***
Avg. Yld.	3.2%	3.2%	2.8%	2.5%	2.3%	2.0%	2.1%	2.4%	2.5%	2.3%	***2.8%***	***2.8%***

Hershey trades at roughly 19 times this year's earnings right now, after its valuation has declined substantially.

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During the last couple of years Hershey's shares were mostly valued at a price to earnings multiple of more than 20, but shares still trade marginally above the long-term median valuation. Hershey's share price could be negatively impacted by multiple compression going forward. The combination of an above-average dividend yield and a high-single-digits dividend growth rate makes Hershey look attractive for income focused investors.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
GP/A	48.4%	55.9%	56.5%	57.5%	60.2%	61.2%	59.3%	63.3%	57.2%	62.0%	***63.0%***	***65.0%***
Debt/A	90.4%	79.3%	78.1%	80.0%	77.9%	69.8%	73.0%	80.4%	85.0%	83.2%	***82.0%***	***80.0%***
Int. Cov.	6.0	8.4	9.4	11.5	11.7	15.2	16.7	12.7	13.2	12.3	***12.5***	***13.0***
Payout	63.3%	54.8%	50.2%	48.9%	48.1%	48.7%	51.3%	54.4%	54.4%	53.6%	***51.3%***	***52.7%***
Std. Dev.	28.9%	19.5%	18.8%	14.3%	12.4%	13.0%	15.2%	16.2%	23.8%	13.0%	***15.0%***	***15.0%***

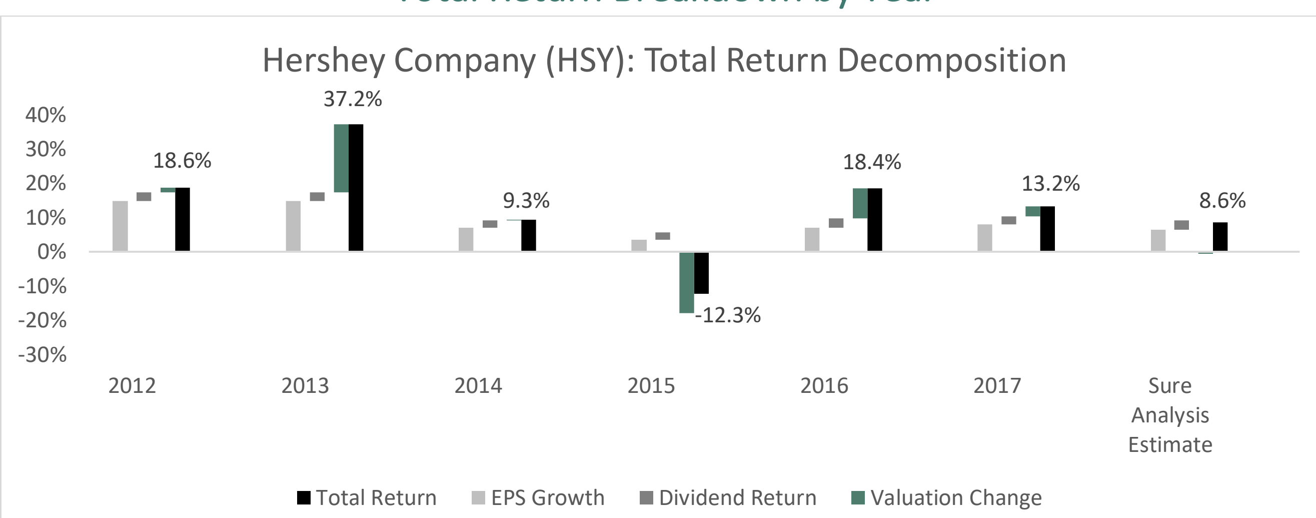
Hershey's fundamentals look quite strong. The company is very good at generating returns with the assets it owns, and although its debt to assets ratio is quite high, its debt is not a problem at all. Long term debt totals just $2 billion out of total liabilities of more than $7 billion, which means relatively low interest expenses, which is why Hershey's interest coverage is quite strong. The company pays out roughly half of its earnings in the form of dividends, and its shares are not very volatile; even during the financial crisis its share price movements were less severe than those of most stocks.

Hershey is one of the top chocolate and confectionary companies in the world, and it controls iconic brands that are ubiquitous to consumers. Competition isn't much of a problem for the company, but if customers became more health-conscious that could hurt growth rates for the whole industry. Customers do not tend to cut back on low-cost chocolate when the economy is weak, which is why Hershey is not vulnerable to recessions. During the last financial crisis – an especially severe recession – the company managed to increase both its profits and its sales.

Final Thoughts & Recommendation

Hershey is one of the top chocolate companies in the world. It owns well-renowned brands and has generated compelling earnings-per-share growth and dividend growth during the last decade. Going forward its growth rate will likely slow down a bit, and its valuation is slightly above fair value, which will be a headwind for total returns. Hershey nevertheless is a low-risk investment that will remain stable during another recession. We rate the stock a hold.

Total Return Breakdown by Year



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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.

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Income Statement Metrics

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Revenue	5133	5299	5671	6081	6644	7146	7422	7387	7440	7515
Gross Profit	1758	2053	2415	2532	2860	3281	3336	3383	3158	3445
Gross Margin	34.2%	38.7%	42.6%	41.6%	43.0%	45.9%	45.0%	45.8%	42.4%	45.8%
SG&A Exp.	1073	1209	1426	1478	1704	1924	1898	1969	1915	1913
D&A Exp.	249	182	197	216	210	201	212	245	302	262
Operating Profit	685	844	989	1054	1156	1357	1438	1413	1243	1531
Operating Margin	13.3%	15.9%	17.4%	17.3%	17.4%	19.0%	19.4%	19.1%	16.7%	20.4%
Net Profit	311	436	510	629	661	820	847	513	720	783
Net Margin	6.1%	8.2%	9.0%	10.3%	9.9%	11.5%	11.4%	6.9%	9.7%	10.4%
Free Cash Flow	237	920	700	240	817	840	474	900	744	992
Income Tax	181	235	299	334	355	431	459	389	379	354

Balance Sheet Metrics

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Total Assets	3635	3675	4273	4407	4755	5357	5623	5344	5524	5554
Cash & Equivalents	37	254	885	694	728	1119	375	347	297	380
Accounts Receivable	455	410	390	399	461	478	597	599	581	588
Inventories	593	520	534	649	633	660	801	751	746	753
Goodwill & Int. Ass.	665	697	647	629	803	828	1151	1132	1400	1295
Total Liabilities	3285	2915	3335	3526	3706	3741	4103	4297	4697	4622
Accounts Payable	249	288	411	420	442	462	482	474	523	523
Long-Term Debt	2007	1542	1827	1888	1907	1962	2178	2421	2980	2920
Shareholder's Equity	318	720	902	857	1037	1605	1455	998	786	915
D/E Ratio	6.31	2.14	2.03	2.20	1.84	1.22	1.50	2.43	3.79	3.19

Profitability & Per Share Metrics

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Return on Assets	7.9%	11.9%	12.8%	14.5%	14.4%	16.2%	15.4%	9.4%	13.2%	14.1%
Return on Equity	68.4%	84.0%	62.8%	71.5%	69.8%	62.1%	55.4%	41.8%	80.7%	92.1%
ROIC	12.2%	18.7%	20.1%	22.7%	23.1%	25.1%	23.3%	14.3%	19.8%	20.4%
Shares Out.	227	228	227	225	224	224	221	217	212	211
Revenue/Share	22.44	23.14	24.62	26.45	29.10	31.45	33.01	33.48	34.56	35.16
FCF/Share	1.03	4.02	3.04	1.05	3.58	3.70	2.11	4.08	3.46	4.64

Note: All figures in millions of U.S. Dollars unless per share or indicated otherwise.