Retirement Suitability Score

D

Unsuitable

Constellation Brands (STZ)

Updated October 4th, 2018 by Bob Ciura

Key Metrics

Current Price:	$219	**5 Year CAGR Estimate:**	6.9%	**Volatility Percentile:**	11.8%
Fair Value Price:	$174	**5 Year Growth Estimate:**	10.0%	**Momentum Percentile:**	57.4%
% Fair Value:	126%	**5 Year Valuation Multiple Estimate:**	-4.5%	**Valuation Percentile:**	21.5%
Dividend Yield:	1.4%	**5 Year Price Target**	$281	**Total Return Percentile:**	37.2%

Overview & Current Events

Constellation Brands was founded in 1945. The company produces and distributes alcoholic beverages including beer, wine, and spirits. It has over 100 brands in its portfolio. It is the No. 3 beer company in the U.S. as it imports and sells beer brands such as Corona Extra, Corona Light, Modelo Especial, Modelo Negra, and Pacifico. It also has craft beer brands including Ballast Point and Funky Buddha Brewery. In addition, Constellation has many wine brands including Robert Mondavi, Clos du Bois, Kim Crawford, Meiomi, Mark West, and Black Box, as well as spirits brands including SVEDKA Vodka, Casa Noble Tequila and High West Whiskey.

On 10/4/18, Constellation Brands reported fiscal 2019 second-quarter financial results. Net sales increased 10% for the quarter to $2.3 billion, while adjusted earnings-per-share increased 16%. Revenue and earnings both beat analyst expectations. Earnings-per-share benefited from sales growth, margin expansion, share repurchases, and tax reform. Beer sales increased 10.5%, while wine and spirits sales increased 9.3% for the quarter.

Per-Share Growth

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
EPS	$1.69	$1.91	$2.35	$2.19	$3.25	$4.44	$5.43	$6.76	$8.72	$8.70	***$9.68***	***$15.59***
DPS	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$1.24	$1.60	$2.08	$1.96	***$2.96***	***$4.77***
Shares	222.2	210.1	194.3	189.8	196.5	199.6	199.5	194.6	191.3	200.7	***201.0***	***201.0***

In a highly competitive U.S. beer, wine, and sprits market, Constellation Brands has differentiated itself with a focus on what the company describes as premiumization trends. This means the company is pursuing growth in the high-end of the beer, wine and spirits categories. It is also expanding into new product categories to appeal to changing consumer preferences. An example of this is the August 2017 acquisition of Funky Buddha, which included a portfolio of craft beers to add exposure to the high-growth craft beer segment of the U.S. beer market. In 2018, Constellation Brands acquired Four Corners Brewing, and recently Constellation Brands invested $4 billion in cannabis producer Canopy Growth, giving it a 38% ownership stake. We expect 10% annual earnings growth over the next five years.

Valuation Analysis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	Now	2023
Avg. P/E	11.2	8.5	9.5	8.7	13.6	18.4	20.3	23.6	23.3	22.7	***22.6***	***18.0***
Avg. Yld.	N/A	N/A	N/A	N/A	N/A	N/A	N/A	1.0%	1.0%	1.0%	***1.4%***	***1.7%***

Constellation Brands has enjoyed rapid earnings growth in recent years, and shareholders have been rewarded with a rising valuation. The downside of this is that the stock now trades at a significant premium to its historical valuation, with a current price-to-earnings ratio of 22.6. Constellation Brands stock had an average price-to-earnings ratio of 16.0. The 10-year average valuation may be lower than where the stock deserves to trade, given its strong brands and high rate of earnings growth. The valuation was severely depressed during the Great Recession. However, the stock still appears to be overvalued. Our fair value estimate is a price-to-earnings ratio of 18.0, which means a declining valuation to fair value could result in negative returns of 4.5% per year over the next five years. Fortunately, earnings growth and dividends will offset a declining valuation multiple.

Safety, Quality, Competitive Advantage, & Recession Resiliency

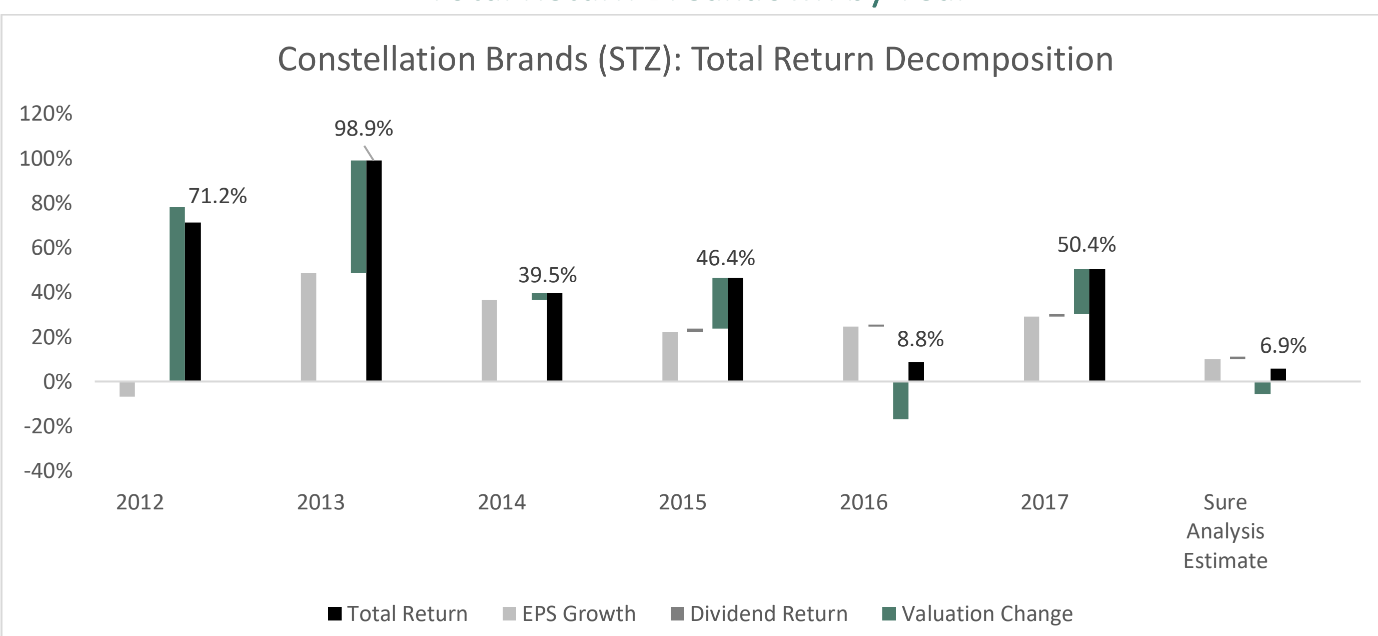
Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
GP/A	15.3%	14.1%	16.6%	14.9%	14.5%	13.9%	17.1%	17.3%	19.0%	18.6%	***18.5%***	***18.5%***
Debt/A	76.3%	68.2%	64.4%	62.4%	62.6%	65.2%	61.0%	60.6%	63.0%	60.7%	***61.0%***	***61.0%***
Int. Cov.	1.2	1.7	3.8	3.9	3.3	7.8	4.5	5.8	7.3	6.9	***7.0***	***7.0***
Payout	N/A	N/A	N/A	N/A	N/A	N/A	22.8%	23.7%	23.9%	22.5%	***30.6%***	***30.6%***
Std. Dev.	42.9%	42.3%	41.8%	41.8%	41.9%	41.3%	40.8%	40.1%	40.0%	39.1%	***39.0%***	***39.0%***

Constellation Brands scores highly in the safety and quality section of this research report. It has a modest level of debt, and a high level of interest coverage. The company has a fairly low dividend payout ratio of 31%, which leaves plenty of room for dividend increases down the road. Constellation Brands also has a number of competitive advantages. Its long list of strong brands gives the company pricing power. It has six of the top 15 imported U.S. beer brands, and 19 of the 100 top-selling wine brands. Its strong distributor network provides an effective route-to-market for the company's strategy in premium categories. Another benefit of Constellation Brands' business is that it can withstand recessions very well. Alcoholic beverages are generally resistant to recessions. Consumers tend to drink as much (or more) beer, wine, and spirits when the economy is in a downturn.

Final Thoughts & Recommendation

Constellation Brands has generated incredible returns for shareholders since 2011. Much of the returns were fueled by an expanding valuation, and to a much lesser extent, earnings growth. While we expect the company continue growing earnings at a high rate going forward, the valuation is likely to come down toward fair value. This could dampen total shareholder returns moving forward. The combination of earnings growth, dividends, and valuation changes result in expected annual returns of 6.9%. This is not high enough to warrant a buy recommendation; investors should wait for the valuation to come down before buying shares, making the stock a sell. Constellation Brands earns a D rating for Retirement Suitability, as its very low yield does not offset the overall safety of its current dividend payment.

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.