The Hershey Company (HSY)

Updated May 7th, 2019 by Jonathan Weber

Key Metrics

Current Price:	$124	**5 Year CAGR Estimate:**	5.5%	**Volatility Percentile:**	26.4%
Fair Value Price:	$105	**5 Year Growth Estimate:**	6.4%	**Momentum Percentile:**	94.9%
% Fair Value:	118%	**5 Year Valuation Multiple Estimate:**	-3.2%	**Growth Percentile:**	63.3%
Dividend Yield:	2.3%	**5 Year Price Target**	$144	**Valuation Percentile:**	25.8%
Dividend Risk Score:	B	**Retirement Suitability Score:**	C	**Total Return Percentile:**	27.0%

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 $26 billion.

Hershey reported its first quarter earnings results on April 25. The company generated revenues of $2.02 billion during the first quarter, which represents a growth rate of 2.5% versus the prior year's quarter. Hershey beat the top line analyst consensus estimate, even though revenue growth was negatively impacted by forex rates. Adjusted for that, sales would have been higher by 0.5%. Hershey generated earnings-per-share of $1.59 during the first quarter, which easily beat the analyst consensus estimate by $0.12. Hershey's earnings-per-share were up 13% compared to the previous year's first quarter. Hershey's strong earnings growth rate, despite the fact that revenues grew at a low single digit pace, was the result of generating higher margins, which was possible due to favorable raw material costs, cost savings thanks to Hershey's cost savings program, and favorable volume trends. The market reacted very positively to Hershey's stronger-than-expected profitability during the first quarter, shares rose by 10% on the day of the earnings release, and Hershey took out a new all-time high in April.

Hershey guides for revenue growth of 1% - 3% during fiscal 2019. Hershey also guides for earnings-per-share in a range of $5.63 to $5.74, which implies an earnings-per-share growth rate of ~6% at the midpoint.

Growth on a Per-Share Basis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
EPS	$2.17	$2.55	$2.82	$3.24	$3.72	$3.98	$4.12	$4.41	$4.76	$5.36	***$5.69***	***$7.76***
DPS	$1.19	$1.28	$1.38	$1.56	$1.81	$2.04	$2.24	$2.40	$2.55	$2.76	***$2.98***	***$4.10***
Shares	228	227	225	224	224	221	217	212	211	210	***209***	***205***

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, so pricing increases 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 solid net earnings growth rate. In 2018 Hershey's earnings-per-share growth was 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 was responsible for the majority of the company's revenue growth. In early 2019 Hershey has been able to grow its top line as well, but not at an overly strong pace. We believe that Hershey's earnings-per-share growth rate will remain below 10% annually going forward.

Hershey 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% was slightly higher than the average.

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Valuation Analysis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	Now	2024
Avg. P/E	16.9	17.9	19.8	20.9	24.2	24.5	23.0	21.9	22.8	20.0	***21.8***	***18.5***
Avg. Yld.	3.2%	2.8%	2.5%	2.3%	2.0%	2.1%	2.4%	2.5%	2.3%	2.7%	***2.3%***	***2.9%***

The positive reaction to Hershey's Q1 results has propelled shares to a new all-time high. This has made Hershey's shares substantially more expensive than they were at the time of our previous update, as they are looking quite overvalued today. We believe that multiple normalization will be a considerable headwind going forward.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
Payout	54.8%	50.2%	48.9%	48.1%	48.7%	51.3%	54.4%	54.4%	53.6%	51.5%	***52.4%***	***52.8%***

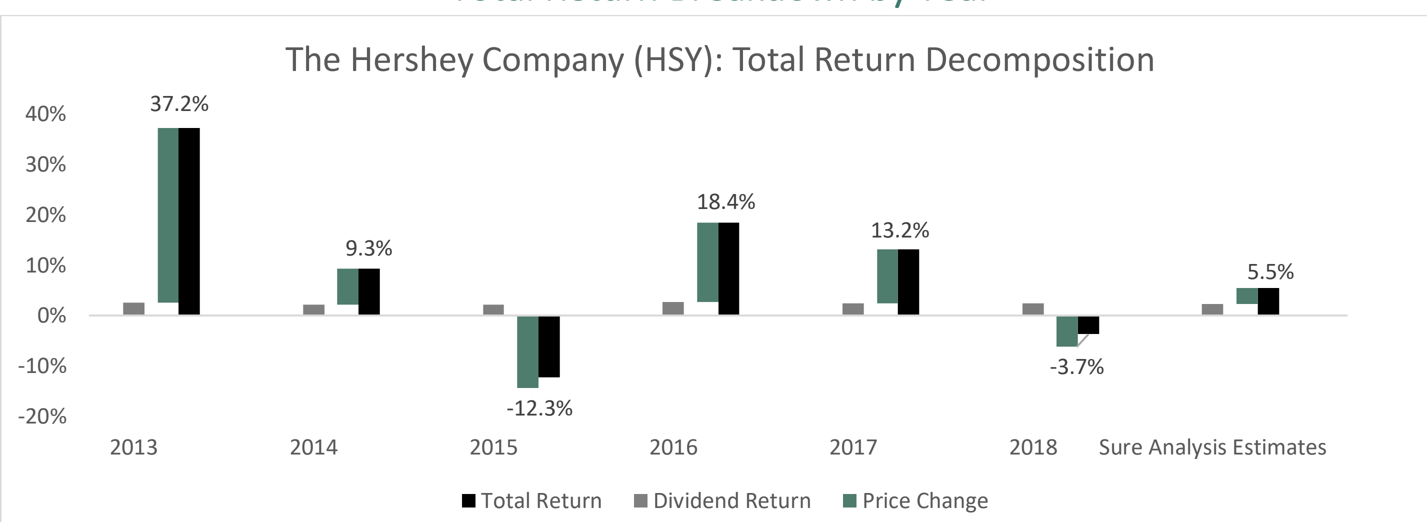
Hershey's dividend payout ratio has moved in a very narrow range throughout the last decade. The company has paid out marginally more than half of its net profits in the form of dividends throughout the majority of those years. The stability of the payout ratio even during the last financial crisis, coupled with the fact that the payout ratio is not overly high on an absolute basis, makes us believe that Hershey's dividend is relatively safe.

Hershey is one of the top chocolate and confectionary companies in the world, and it controls iconic brands that are ubiquitous to consumers. Competition is not 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 a top chocolate company, and it has generated highly attractive earnings and dividend growth during the past. Hershey is not vulnerable versus recessions on top of that, which makes the company's shares a viable choice for risk-averse investors. Going forward, earnings-per-share growth will be a bit lower than it was in the past, though, and due to the fact that shares are looking overvalued, we believe that total returns will not be overly high from the current level. We thus rate Hershey a hold for now.

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	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Revenue	5299	5671	6081	6644	7146	7422	7387	7440	7515	7791
Gross Profit	2053	2415	2532	2860	3281	3336	3383	3170	3455	3575
Gross Margin	38.7%	42.6%	41.6%	43.0%	45.9%	45.0%	45.8%	42.6%	46.0%	45.9%
SG&A Exp.	1209	1426	1478	1704	1924	1898	1969	1891	1885	1875
D&A Exp.	182	197	216	210	201	212	245	302	262	295
Operating Profit	844	989	1054	1156	1357	1438	1413	1278	1570	1700
Operating Margin	15.9%	17.4%	17.3%	17.4%	19.0%	19.4%	19.1%	17.2%	20.9%	21.8%
Net Profit	436	510	629	661	820	847	513	720	783	1178
Net Margin	8.2%	9.0%	10.3%	9.9%	11.5%	11.4%	6.9%	9.7%	10.4%	15.1%
Free Cash Flow	920	700	240	817	840	474	900	744	992	1271
Income Tax	235	299	334	355	431	459	389	379	354	239

Balance Sheet Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Total Assets	3675	4273	4407	4755	5357	5623	5344	5524	5554	7703
Cash & Equivalents	254	885	694	728	1119	375	347	297	380	588
Accounts Receivable	410	390	399	461	478	597	599	581	588	594
Inventories	520	534	649	633	660	801	751	746	753	785
Goodwill & Int. Ass.	697	647	629	803	828	1151	1132	1400	1295	3206
Total Liabilities	2915	3335	3526	3706	3741	4103	4297	4697	4622	6296
Accounts Payable	288	411	420	442	462	482	474	523	523	502
Long-Term Debt	1542	1827	1888	1907	1962	2178	2421	2980	2920	4458
Shareholder's Equity	720	902	857	1037	1605	1455	998	786	915	1399
D/E Ratio	2.14	2.03	2.20	1.84	1.22	1.50	2.43	3.79	3.19	3.19

Profitability & Per Share Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Return on Assets	11.9%	12.8%	14.5%	14.4%	16.2%	15.4%	9.4%	13.2%	14.1%	17.8%
Return on Equity	84.0%	62.8%	71.5%	69.8%	62.1%	55.4%	41.8%	80.7%	92.1%	102%
ROIC	18.7%	20.1%	22.7%	23.1%	25.1%	23.3%	14.3%	19.8%	20.4%	24.2%
Shares Out.	228	227	225	224	224	221	217	212	211	210
Revenue/Share	23.14	24.62	26.45	29.10	31.45	33.01	33.48	34.56	35.16	36.93
FCF/Share	4.02	3.04	1.05	3.58	3.70	2.11	4.08	3.46	4.64	6.03

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