Tootsie Roll Industries, Inc. (TR)

Updated September 3rd, 2019 by Prakash Kolli

Key Metrics

Current Price:	$37	**5 Year CAGR Estimate:**	-1.6%	**Volatility Percentile:**	35.6%
Fair Value Price:	$28	**5 Year Growth Estimate:**	3.0%	**Momentum Percentile:**	92.1%
% Fair Value:	133%	**5 Year Valuation Multiple Estimate:**	-5.5%	**Growth Percentile:**	16.9%
Dividend Yield:	1.2%	**5 Year Price Target**	$32	**Valuation Percentile:**	22.9%
Dividend Risk Score:	A	**Retirement Suitability Score:**	C	**Total Return Percentile:**	4.8%

Overview & Current Events

Tootsie Roll Industries, Inc. traces its roots back to the late 1890's when its namesake product, the Tootsie Roll, was first created. Today, the company sells a wider variety of candy and gum products. Other well-known brands include DOTS, Junior Mints, Andes, Charms, Blow-Pops, Sugar Daddy, and Dubble Bubble. Tootsie Roll has a dual-class share structure with the Chairwoman and CEO, Ellen R. Gordon owning approximately 53.9% of common stock and 82.8% of Class B shares giving her effective control of the company. The company has a market capitalization of roughly $2.37B.

Tootise Roll reported Q2 2019 results on July 24, 2019. Net sales increased $398,000 to $106.02M for the quarter versus $105.62M in the prior year. In the same period, net earnings increased to $11.56M compared to $10.49M. Diluted EPS increased 12% or $0.02 to $0.18 per share from $0.16 on year-over-year basis. The company's Q2 2019 results benefited from higher prices allowing the company to recover earlier margin declines resulting from higher input costs. Tootsie Roll continues to experience foreign exchange headwinds that are adversely affecting results. Tootsie Roll is focused on investing in plant manufacturing operations to meet expected customer and consumer demands and increase operational efficiencies. Tootsie Roll is facing higher taxes this year of 25.8% in Q2 2019 versus 23.7% in the prior year. For 1H 2019 taxes are also trending higher at 25.2% compared to 22.9% in comparable periods. Higher taxes are due to higher state and foreign taxes. Earnings per share benefitted from a lower share count and the company continues to buy back shares. Note that Tootsie Roll's top line has slowly declined since 2014. So, the sales gain in 1H 2019 is a positive. However, changing tastes and the trend to smaller portions combined with the relative lack of product innovation have caused the company's top line to struggle. Saying that, the company recently introduced Tootsie Fruit Chews Mini Bites and Tootsie Roll Mini Bites.

Growth on a Per-Share Basis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
EPS[1]	$0.73	$0.74	$0.62	$0.75	$0.88	$0.93	$0.99	$1.02	$1.24	$0.89	***$0.92***	***$1.07***
DPS	$0.32	$0.32	$0.32	$0.32	$0.32	$0.32	$0.35	$0.36	$0.36	$0.36	***$0.36***	***$0.36***
Shares[2]	74.9	73.7	72.8	71.6	70.7	69.7	68.5	67.6	66.6	66.1	***65.4***	***62.2***

Tootsie Roll should achieve on average 3.0% earnings per share growth moving forward to 2024, mostly via small amounts of revenue growth driven by incremental product innovation and price increases. Influences on earnings per share growth include commodity input and freight cost inflation on the downside, and volume and price increases to the upside. Earnings per share growth will also benefit from ongoing share buybacks. The company has reduced share count from about 74.9M in 2009 to 66.1M in 2018. We expect the share count to decrease 1% on average annually.

The dividend was last increased in 2016 and is currently $0.36 per share. We are not expecting an increase of the regular dividend in the near future. But saying that, the payout ratio is only ~39% and there is room for an increase. The company does issue a 3% stock dividend each year in addition to the regular dividend giving a ~4% effective yield.

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[1] Earnings per share data is not adjusted for the 3% annual stock dividend.

[2] Share count is in millions.

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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Valuation Analysis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	Now	2024
Avg. P/E	24.9	27.6	35.2	27.5	30.3	27.5	29.5	33.0	38.3	35.0	***39.9***	***30.0***
Avg. Yld.	1.3%	1.2%	1.2%	1.6%	1.0%	1.1%	0.8%	1.0%	1.0%	1.2%	***1.2%***	***1.1%***

Tootsie Roll's P/E ratio is currently 39.9 and is significantly elevated relative to the S&P 500's average P/E ratio and the company's 10-year historical average P/E ratio of about 30.0. We attribute the high P/E ratio to the limited float and generally stable revenue and earnings per share over the past decade. Using our expected 2019 earnings and long-term P/E ratio our fair value estimate is $28. Our 5-year price target is currently $32, lower than the current stock price.

Safety, Quality, Competitive Advantage, & Recession Resiliency

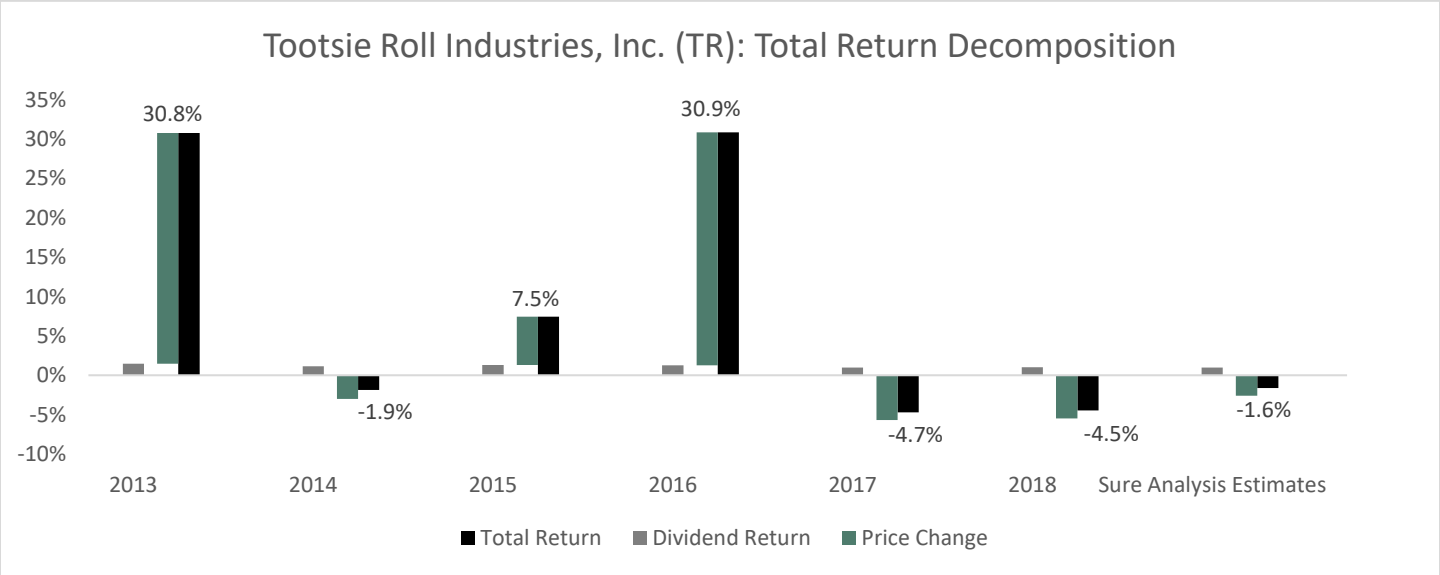
Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
Payout	44%	43%	52%	43%	36%	34%	35%	35%	29%	40%	***39%***	***34%***

The company's competitive advantage is the brand strength of its core product, the Tootsie Roll, and its lack of direct competition given the uniqueness of the product. Some of the company's other brands are also well known. But saying that, Tootsie Roll tends to move slowly with product changes and growth initiatives. Changing tastes to more healthier options and smaller portion sizes are an ongoing risk to the top line. Margins are under pressure due to higher freight, packaging, and commodity costs. Tootsie Roll's balance sheet is conservative. The company's long-term debt in an industrial revenue bond has been only $7.5M since 2014. The interest rate resets weekly based on the current market rate so there is little risk of rapidly increasing interest expense.

Final Thoughts & Recommendation

At present we are forecasting (1.6%) annualized return over the next five years comprising mostly of 3.0% EPS growth, 1.2% dividend yield and (5.5%) from P/E multiple contraction. This stock may be of interest to those seeking income due to the combined regular and stock dividends. But at the current share price, Tootsie Roll is not attractive from a total return perspective and earns a strong sell recommendation from Sure Dividend.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Revenue	499	521	533	550	543	544	540	521	519	519
Gross Profit	180	171	166	183	191	202	199	199	192	188
Gross Margin	36.0%	32.8%	31.2%	33.3%	35.2%	37.1%	36.9%	38.2%	37.0%	36.3%
SG&A Exp.	104	106	108	114	119	118	108	108	121	118
D&A Exp.	18	18	19	20	20	21	20	20	19	19
Operating Profit	76	65	58	69	72	84	91	91	70	70
Operating Margin	15.2%	12.4%	10.9%	12.6%	13.3%	15.4%	16.9%	17.5%	13.6%	13.6%
Net Profit	54	53	44	52	61	63	66	68	81	57
Net Margin	10.8%	10.2%	8.3%	9.5%	11.2%	11.6%	12.2%	13.0%	15.6%	11.0%
Free Cash Flow	56	70	34	93	94	78	76	82	26	73
Income Tax	10	20	17	22	24	28	26	31	4	16

Balance Sheet Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Total Assets	838	860	858	847	888	910	909	920	931	947
Cash & Equivalents	91	116	79	64	88	100	126	119	96	111
Accounts Receivable	38	37	42	42	41	43	51	43	47	50
Inventories	56	59	72	62	62	70	62	58	55	55
Goodwill & Int. Ass.	248	248	248	248	248	248	248	248	248	248
Total Liabilities	183	191	192	197	208	219	210	209	197	197
Accounts Payable	9	10	11	9	9	12	11	10	12	12
Long-Term Debt	8	8	8	8	8	8	8	8	8	8
Shareholder's Equity	655	669	666	650	680	691	698	711	734	751
D/E Ratio	0.01	0.01	0.01	0.01	0.01	0.01	0.01	0.01	0.01	0.01

Profitability & Per Share Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Return on Assets	6.5%	6.2%	5.1%	6.1%	7.0%	7.0%	7.3%	7.4%	8.7%	6.1%
Return on Equity	8.4%	8.0%	6.6%	7.9%	9.1%	9.2%	9.5%	9.6%	11.2%	7.7%
ROIC	8.3%	7.9%	6.5%	7.8%	9.0%	9.1%	9.4%	9.5%	11.1%	7.6%
Shares Out.	73	72	71	70	69	68	66	66	65	64
Revenue/Share	6.83	7.23	7.49	7.85	7.87	7.98	8.05	7.90	7.98	8.08
FCF/Share	0.77	0.97	0.48	1.32	1.36	1.15	1.13	1.25	0.40	1.14

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

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