



The Kraft-Heinz Company (KHC)

Updated November 13th, 2019 by Jonathan Weber

Key Metrics

Current Price:	\$33	5 Year CAGR Estimate:	9.2%	Volatility Percentile:	77.7%
Fair Value Price:	\$36	5 Year Growth Estimate:	3.0%	Momentum Percentile:	3.7%
% Fair Value:	91%	5 Year Valuation Multiple Estimate:	2.0%	Growth Percentile:	17.5%
Dividend Yield:	4.9%	5 Year Price Target	\$42	Valuation Percentile:	87.3%
Dividend Risk Score:	D	Retirement Suitability Score:	B	Total Return Percentile:	81.4%

Overview & Current Events

Kraft-Heinz is a processed food and beverages company whose product portfolio includes condiments, sauces, cheese & dairy, frozen & chilled meals, and infant diet & nutrition. The company was created in 2015 in a merger between Kraft Food Group and H. J. Heinz Company. Kraft-Heinz is headquartered in Chicago, IL, and is currently valued at \$38 billion.

The Kraft-Heinz Company has reported its third quarter and earnings results on October 31. The company reported that its revenues totaled \$6.08 billion during the third quarter, which was 4.7% less than the revenues that Kraft-Heinz generated during the previous year's period. This was slightly worse than what the analyst community had expected. Kraft-Heinz' organic sales were down, but by only 1.1%, which compares favorably to the analyst estimate which forecasted a 1.6% organic sales decline. Organic sales were positive in overseas markets, but down in the US. The sales growth rate represents an improvement on a sequential basis, which management explains by tailwinds from improved pricing and improving supply chain costs. This was also beneficial for Kraft-Heinz' EBITDA, which totaled \$1.47 billion.

Kraft-Heinz generated earnings-per-share of \$0.69 during the third quarter, which easily beat the consensus estimate of \$0.54. Earnings-per-share nevertheless were down versus the previous year's quarter, when the company generated earnings-per-share of \$0.76. The drop was not as large as it was during the first half of the current year, though, which management touts as a sign of stabilization. Kraft-Heinz has also announced that its deleveraging strategy was on track, the company has announced \$2.3 billion in debt take-out during the third quarter. The market reacted positively to the developments, sending Kraft-Heinz' shares to a level that is more than 30% above the 52-week low.

Growth on a Per-Share Basis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
EPS	---	---	---	---	---	---	\$2.19	\$3.33	\$3.55	\$3.51	\$2.80	\$3.25
DPS	---	---	---	---	---	---	\$1.13	\$2.35	\$2.45	\$2.50	\$1.60	\$1.95
Shares¹	---	---	---	---	---	---	1210	1226	1228	1220	1210	1160

The Kraft-Heinz Company does not have a long history in the form it currently exists in, which is why we are not able to provide much data. The two companies that merged to create Kraft-Heinz both have a long history, though. As a food and beverages company, Kraft-Heinz is not operating in a high-growth industry. The company therefore will, in all likelihood, not be able to generate enormous growth rates going forward. Even in a low-growth industry companies can generate positive returns, though. In Kraft-Heinz' case there are several avenues for growth the company can pursue.

The first is international expansion. Market penetration in many emerging countries is not very high. These markets are huge and growing relatively quickly. Due to steadily rising disposable incomes in countries such as China and India more consumers have the means to purchase consumer goods from Western companies such as Kraft-Heinz, which results in a positive outlook for Kraft-Heinz' international business. Another factor for earnings growth is margin expansion. Kraft-Heinz' management is experienced in cutting costs. Kraft-Heinz is headed by Bernardo Hees and Alex Behring, two 3G Capital managers that are famous for their cost-cutting, thus we believe that margins will continue to trend higher. Last but not least, Kraft-Heinz should benefit from debt reduction that results in declining interest expenses.

¹In 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	---	---	---	---	---	---	18.5	24.9	24.2	12.3	11.8	13.0
Avg. Yld.	---	---	---	---	---	---	2.8%	2.8%	2.9%	4.9%	4.9%	4.6%

The Kraft-Heinz Company's shares traded at quite high valuations during 2016 and 2017. This has not been justified, we believe, as Kraft-Heinz has never been a high-growth company, or a company that deserved a 20+ earnings multiple. The impairment charges over the last year have made investors more wary regarding the company's shares, which is why Kraft-Heinz' shares will likely continue to trade at a huge discount relative to how the company's shares were valued in the past. Shares are not as cheap as they were three months ago, but we still see upside potential towards a fair earnings multiple in the low-teens range. The dividend is at an above-average level on top of that.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
Payout	---	---	---	---	---	---	51.6%	70.6%	69.1%	71.2%	57.1%	60.0%

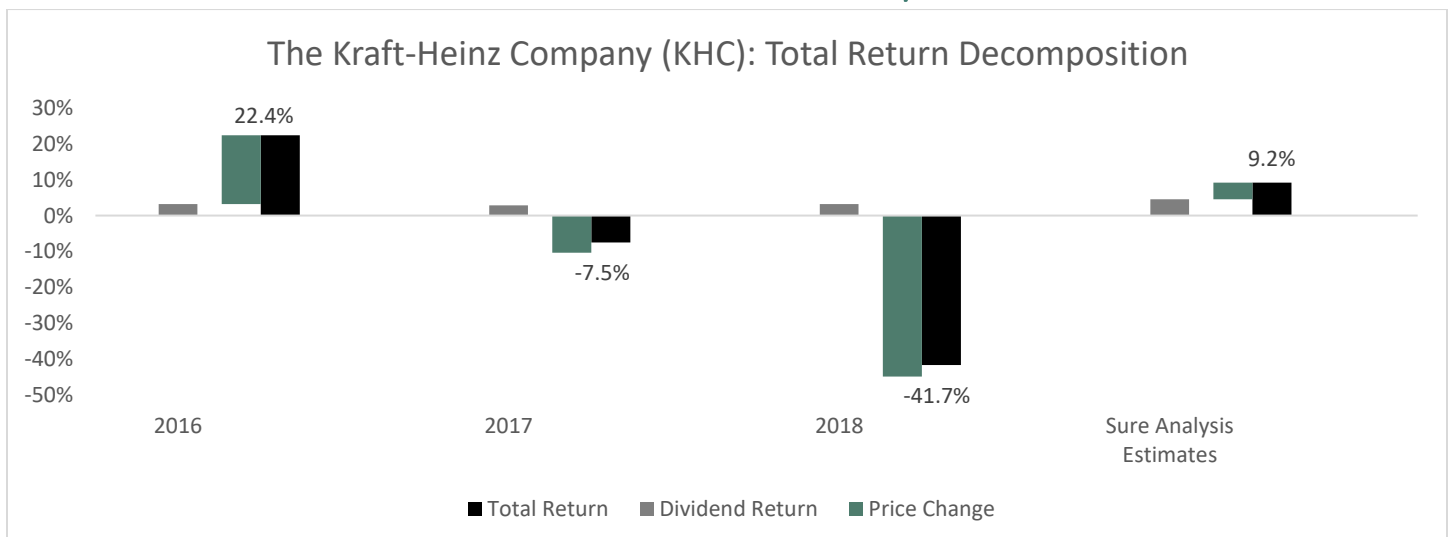
Kraft-Heinz does not have a long dividend history, and after the recent dividend cut, even its short dividend history is not convincing. The dividend looks sustainable at the new, lower level, another cut thus seems unlikely. We are forecasting the payout ratio to rise slightly over time as dividend growth barely outpaces earnings growth.

Kraft-Heinz' brands are strong and recognized by most consumers, and demand for food is not cyclical or dependent on economic conditions. Kraft-Heinz therefore should be able to remain profitable in economic downturns, as do most consumer staples. Kraft-Heinz' brands function as a competitive advantage. Shifting consumer preferences are a headwind for Kraft-Heinz, though, as more consumers chose healthier options of non-processed foods.

Final Thoughts & Recommendation

Kraft-Heinz' shares have performed very weak over the last year, but they are not trading close to 52-week lows any longer. We believe that, thanks to international growth, the company should be able to generate some earnings growth going forward. Due to a solid total return forecast, and due to the fact that Kraft-Heinz continues to trade below our fair value estimate, we rate the stock a buy at current prices.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Revenue	N/A	N/A	N/A	18271	18218	18205	18338	26487	26232	26259
Gross Profit	N/A	N/A	N/A	5772	6823	4845	5761	9586	9703	8950
Gross Margin	N/A	N/A	N/A	31.6%	37.5%	26.6%	31.4%	36.2%	37.0%	34.1%
SG&A Exp.	N/A	N/A	N/A	2961	2124	2956	3122	3444	2930	3204
D&A Exp.	N/A	N/A	N/A	428	393	385	740	1337	1036	N/A
Operating Profit	N/A	N/A	N/A	2811	4699	1889	2639	6142	6773	5746
Op. Margin	N/A	N/A	N/A	15.4%	25.8%	10.4%	14.4%	23.2%	25.8%	21.9%
Net Profit	N/A	N/A	N/A	1642	2715	1043	634	3632	10999	-10229
Net Margin	N/A	N/A	N/A	9.0%	14.9%	5.7%	3.5%	13.7%	41.9%	-39.0%
Free Cash Flow	N/A	N/A	N/A	2595	1486	1485	624	1402	-690	N/A
Income Tax	N/A	N/A	N/A	18271	18218	18205	18338	26487	26232	26259

Balance Sheet Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Total Assets (\$B)	N/A	N/A	N/A	23.18	23.15	22.95	122.97	120.48	120.23	103.63
Cash & Equivalents	N/A	N/A	N/A	1255	1686	1293	4837	4204	1629	1130
Accounts Receivable	N/A	N/A	N/A	1089	1048	1080	1454	898	1274	2129
Inventories	N/A	N/A	N/A	1928	1616	1775	2618	2684	2815	2683
Goodwill & Int. (\$B)	N/A	N/A	N/A	13.83	13.73	13.64	105.17	103.42	104.27	85.99
Total Liabilities	N/A	N/A	N/A	19607	17961	18582	65080	62906	53991	51724
Accounts Payable	N/A	N/A	N/A	1556	1548	1537	2844	3996	4449	4153
Long-Term Debt	N/A	N/A	N/A	9966	9980	10032	25234	32404	31536	31285
Shareholder's Equity	N/A	N/A	N/A	3572	5187	4365	57685	57358	66034	51785
D/E Ratio	N/A	N/A	N/A	2.79	1.92	2.30	0.44	0.56	0.48	0.60

Profitability & Per Share Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Return on Assets	N/A	N/A	N/A	7.3%	11.7%	4.5%	0.9%	3.0%	9.1%	-9.1%
Return on Equity	N/A	N/A	N/A	16.3%	62.0%	21.8%	2.0%	6.3%	17.8%	-17.4%
ROIC	N/A	N/A	N/A	10.9%	18.9%	7.1%	1.3%	4.2%	11.7%	-11.3%
Shares Out.	N/A	N/A	N/A	N/A	N/A	N/A	1210	1226	1228	1220
Revenue/Share	N/A	N/A	N/A	30.66	30.41	30.44	23.33	21.60	21.36	21.54
FCF/Share	N/A	N/A	N/A	4.35	2.48	2.48	0.79	1.14	-0.56	N/A

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

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