



J.M. Smucker Co. (SJM)

Updated November 22nd, 2019 by Eli Inkrot

Key Metrics

Current Price:	\$109	5 Year CAGR Estimate:	7.4%	Volatility Percentile:	49.5%
Fair Value Price:	\$106	5 Year Growth Estimate:	5.0%	Momentum Percentile:	25.7%
% Fair Value:	102%	5 Year Valuation Multiple Estimate:	-0.4%	Growth Percentile:	40.1%
Dividend Yield:	3.2%	5 Year Price Target	\$136	Valuation Percentile:	70.5%
Dividend Risk Score:	C	Retirement Suitability Score:	B	Total Return Percentile:	63.9%

Overview & Current Events

In 1897 Jerome Monroe Smucker founded a small cider mill in Orrville, Ohio. He used surplus apples, said to be cultivated by Johnny Appleseed, to make cider and apple butter. Since then the J.M. Smucker company has grown into an international powerhouse of packaged food and beverage products including iconic names like Smucker's, Jif, Crisco and Folgers, along with pet food brands like Milk Bone, Meow Mix, Kibbles 'n Bits and 9Lives. The company has a market capitalization of \$12 billion and is on pace to generate ~\$8 billion in sales and earn ~\$800 million this year.

On July 23rd, 2019 Smucker's announced a 3.5% quarterly dividend increase from \$0.85 to \$0.88.

On November 22nd, 2019 Smucker's reported Q2 fiscal year 2020 results for the period ending October 31st, 2019. (Smucker's fiscal year ends April 30th.) These results reflect the divestiture of the company's U.S. baking business on August 31st, 2018. For the quarter sales came in at \$1.96 billion, a -3.2% decline compared to Q2 fiscal year 2019, as the divestiture of the baking business had a -\$32.8 million impact on the top line. Even without this, comparable sales would have been down -1% as the company saw lower pricing in peanut butter and coffee. Meanwhile, adjusted earnings-per-share increased 4.1% from \$2.17 to \$2.26 for the quarter.

Smucker's also updated its guidance for fiscal year 2020. Sales are now anticipated to be down -3% compared to the prior year (from -1% to 0% previously), free cash flow is expected to be \$850 million (from \$875 to \$925 million previously) and adjusted earnings-per-share are expected to be in the \$8.10 to \$8.30 range (down from \$8.35 to \$8.55 and \$8.45 to \$8.65 in the two prior quarters). Further, keep in mind that this guidance is uniquely adjusted. It includes the expectation of \$6.77 to \$6.97 in earnings-per-share, with -\$0.36 taken away as unallocated losses or gains, \$0.13 added back in for special project costs and \$1.56 for amortization charges. We include the impact of amortization in our earnings expectations, so this guidance implies underlying earnings power of ~\$6.54 to ~\$6.74 this year (down from ~\$6.79 to ~\$6.99 and ~\$6.90 to ~\$7.09 in the two prior reports). We have adjusted our forecast accordingly.

Growth on a Per-Share Basis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
EPS	\$4.37	\$4.79	\$4.73	\$5.37	\$5.64	\$5.35	\$5.89	\$6.49	\$6.97	\$6.66	\$6.64	\$8.47
DPS	\$1.45	\$1.68	\$1.92	\$2.08	\$2.32	\$2.56	\$2.68	\$3.00	\$3.12	\$3.40	\$3.52	\$4.22
Shares¹	119	114	110	106	102	120	116	113	114	114	114	114

Note that while Smucker's has already completed its 2019 fiscal year, we have elected to present the data above closest to the actual calendar year. Also, the share count increase for 2014 was a result of the Big Heart Pet Brands acquisition.

In the 2008 through 2017 stretch, Smucker's increased earnings-per-share by about 7% annually. Moving forward the company has provided long-term guidance of 2% to 3% sales growth, 5% operating income growth and 8% annual earnings-per-share growth. While we believe this is a great goal, we are hesitant to extrapolate that sort of growth over the intermediate-term and have tempered it slightly to 5% annually. The company has a collection of iconic brands, but many of them are center-isle staples that have been losing popularity as consumers look for fresher, healthier options. Increased advertising spending and moving toward consumer preferences will require significant capital outlays in the

¹ In millions.

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years to come. On the positive side, coffee is a strong, sticky segment for the business and Smucker's is working to expand the current iconic lines (think Jif) to more on-trend products like granola bars and on-the-go snacks.

Valuation Analysis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	Now	2024
Avg. P/E	12.5	13.2	16.2	16.0	18.3	19.6	20.1	21.0	17.0	16.2	16.3	16.0
Avg. Yld.	2.7%	2.7%	2.5%	2.4%	2.2%	2.4%	2.3%	2.2%	2.6%	3.2%	3.2%	3.1%

Over the past decade shares of Smucker's have traded at an average P/E ratio of about 17 times earnings. While we believe this mark is more or less fair, we do caution that it could be overstated should earnings growth continue to stall and have baked in a bit of caution in our estimate as a result, using 16 times earnings as a starting point. With shares currently trading just over 16 times expected earnings, the security appears more or less fairly valued.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
Payout	33%	35%	41%	39%	41%	48%	46%	46%	45%	51%	53%	50%

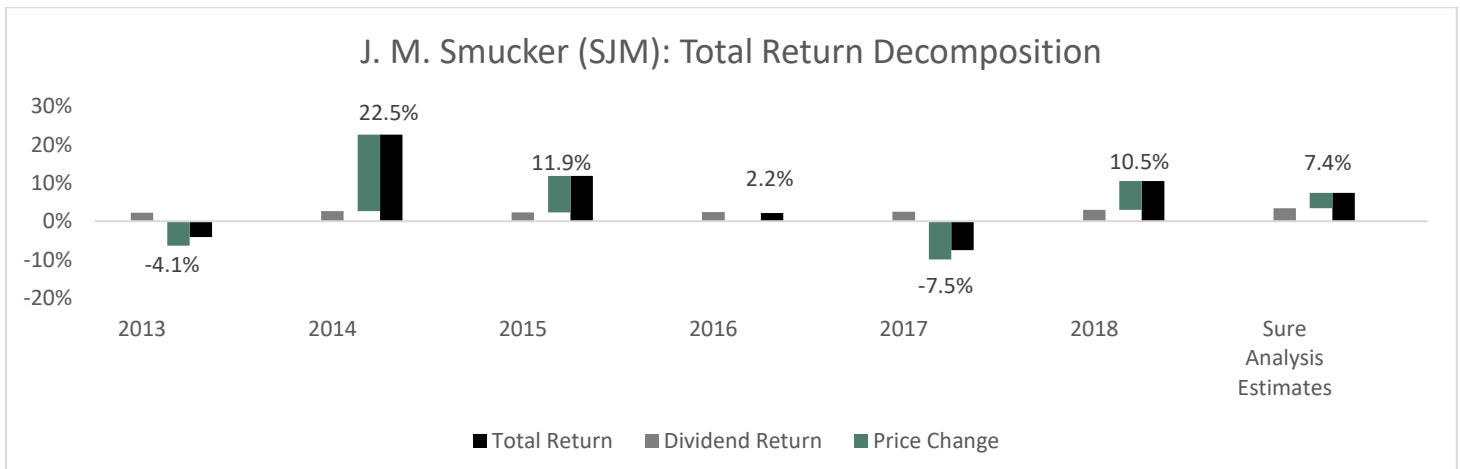
Smucker's iconic brands continue to enjoy recognition, but this competitive position is eroding as consumers look for fresher and healthier alternatives. During the last recession Smucker's held up exceptionally well, growing both earnings and dividends. Our apprehension is not with the next recession, but instead if the company can grow its core brands.

Smucker's acquisitions have levered up the balance sheet. Smucker's held ~\$900 million in long-term debt back in 2009 against ~\$320 million in net profit (2.8x). Today the number is closer to \$5.4 billion in debt against underlying earnings of ~\$750 million per year (~7.2x) with interest payments of ~\$200 million annually. Additionally, \$13.0 billion of the company's \$16.7 billion in total assets are held as goodwill and other intangible assets. The debt is serviceable, the payout ratio is reasonable, and profits are recession resistant, but the safety of the firm is not top-notch in our view.

Final Thoughts & Recommendation

Shares are up 6% since our last report, while earnings expectations have declined. We are forecasting total return potential of 7.4% per annum, stemming from 5% growth and a 3.2% starting yield offset by a slight valuation headwind. While the company has a strong history with a solid dividend and iconic brands, growth prospects are not robust from this point and the company needs to get a better handle on the balance sheet. Moreover, the industry as a whole appears to be facing increasing headwinds. Overall we rate the security as a hold.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Revenue	4605	4826	5526	5898	5611	5693	7811	7392	7357	7838
Gross Profit	1787	1799	1845	2028	2031	1969	2968	2835	2836	2916
Gross Margin	38.8%	37.3%	33.4%	34.4%	36.2%	34.6%	38.0%	38.4%	38.5%	37.2%
SG&A Exp.	878	863	893	974	989	1031	1510	1380	1363	1509
D&A Exp.	182	186	209	251	256	267	430	419	413	446
Operating Profit	824	861	867	960	945	830	1281	1253	1266	1198
Operating Margin	18%	18%	16%	16%	17%	15%	16%	17%	17%	15%
Net Profit	494	480	460	544	565	345	689	592	1339	514
Net Margin	10.7%	9.9%	8.3%	9.2%	10.1%	6.1%	8.8%	8.0%	18.2%	6.6%
Free Cash Flow	576	212	457	649	577	491	1260	867	896	781
Income Tax	237	238	242	273	285	178	289	286	-478	187

Balance Sheet Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Total Assets	7975	8325	9115	9032	9060	16806	15984	15640	15301	16711
Cash & Equivalents	284	320	230	256	154	126	110	167	193	101
Accounts Receivable	239	344	348	314	309	430	450	439	386	504
Inventories	655	864	962	946	931	1164	899	906	854	910
Goodwill & Int. Ass.	5834	5753	6242	6142	6123	12962	12586	12227	11859	13030
Total Liabilities	2649	3032	3952	3883	4031	9719	8976	8790	7410	8741
Accounts Payable	180	235	275	286	289	403	459	477	512	591
Long-Term Debt	910	1304	2071	2018	2216	6171	5430	5399	4832	5911
Shareholder's Equity	5326	5292	5163	5149	5030	7087	7009	6850	7891	7971
D/E Ratio	0.17	0.25	0.40	0.39	0.44	0.87	0.77	0.79	0.61	0.74

Profitability & Per Share Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Return on Assets	6.1%	5.9%	5.3%	6.0%	6.2%	2.7%	4.2%	3.7%	8.7%	3.2%
Return on Equity	9.6%	9.0%	8.8%	10.6%	11.1%	5.7%	9.8%	8.5%	18.2%	6.5%
ROIC	7.8%	7.5%	6.6%	7.6%	7.8%	3.4%	5.4%	4.8%	10.7%	3.9%
Shares Out.	119	114	110	106	102	120	116	113	114	114
Revenue/Share	39.01	41.20	49.22	54.18	54.20	55.25	65.64	63.95	65.11	69.30
FCF/Share	4.88	1.81	4.07	5.97	5.57	4.77	10.58	7.50	7.93	6.91

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

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