Lancaster Colony Corporation (LANC)

Updated February 11th, 2020 by Josh Arnold

Key Metrics

Current Price:	$154	**5 Year CAGR Estimate:**	-0.2%	**Market Cap:**	$4.2B
Fair Value Price:	$112	**5 Year Growth Estimate:**	4.0%	**Ex-Dividend Date:**	03/06/20[1]
% Fair Value:	137%	**5 Year Valuation Multiple Estimate:**	-6.1%	**Dividend Payment Date:**	03/27/20[2]
Dividend Yield:	1.8%	**5 Year Price Target**	$136	**Years Of Dividend Growth:**	57
Dividend Risk Score:	A	**Retirement Suitability Score:**	B	**Last Dividend Increase:**	7.7%

Overview & Current Events

Lancaster Colony has been making food products since 1969, after shifting away from housewares. The move has afforded the company some meaningful growth in the past five decades and the stock sports a $4.2 billion market capitalization on $1.3 billion in annual revenue. Lancaster Colony makes various meal accessories like croutons and bread products in frozen and non-frozen categories. Lancaster also has one of the best dividend increase streaks in the entire market, with fiscal 2020 representing the 57th consecutive year of dividend increases.

Lancaster reported Q2 earnings on February 4th and results were mixed, as revenue was slightly below estimates, but earnings beat. Total sales increased 1.6% in Q2 to $355 million, a new record. Retail net sales were flat at $186 million, as net price realization gains and higher sales of frozen garlic bread and shelf-stable dressings were offset by lower sales of Marzetti dips and produce dressings. Foodservice revenue grew 3.4% to $169 million as this segment continues to be Lancaster's only source of growth. Gains were made from the company's Omni Baking and Bantam Bagels acquisitions once again.

Gross profit was up 9.3% to $100 million driven by cost savings programs, lower commodity costs, improved price realization, and favorable mix. SG&A costs were up $5.9 million to $45.7 million, almost entirely attributable to the company's enterprise resource planning initiative.

Operating income declined $7.1 million to $54 million thanks to a $9.7 million non-cash gain on the company's Angelic Bakehouse acquisition in last year's Q2, which made comparisons for this year more difficult. Without that, operating income would have risen slightly.

Earnings-per-share came to $1.58 in Q2, down 15 cents from last year's Q2. However, Q2 results were negatively impacted by a $0.27 gain in last year's Q2 due to the non-cash gain on Angelic, as well as a $0.14 reduction in this year's Q2 thanks to ERP costs. Our estimate for this year remains unchanged at $5.60 in earnings-per-share.

Growth on a Per-Share Basis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
EPS	$4.07	$3.84	$3.51	$3.99	$3.69	$3.72	$4.44	$4.20	$4.92	$5.46	***$5.60***	***$6.81***
DPS	$1.19	$1.29	$1.41	$1.52	$1.72	$1.82	$1.96	$2.15	$2.40	$2.55	***$2.80***	***$3.57***
Shares[3]	28	28	27	27	27	27	27	27	28	28	***28***	***28***

The company's earnings-per-share growth has been spotty as its revenue tends to ebb and flow with restaurant traffic. It recovered nicely from the Great Recession, but the drop in 2008 earnings was very steep. In addition, declines in earnings-per-share are common and thus, the multiple that should be assigned should reflect that risk going forward.

We are forecasting 4% earnings-per-share growth annually ahead, comprised of low-single-digit sales and flat margins. Lancaster does not buy back stock. The company's average revenue growth has been and should remain in the low-

[1] Estimated date
[2] Estimated date
[3] Share count in millions

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single-digits, but keep in mind the possibility for earnings volatility going forward - there will be years where it dips and other years where it may rise rapidly, as it did in 2018, and again in 2019. Organic growth has been a problem for Lancaster Colony, but it does complete sizable acquisitions regularly.

We are forecasting modest dividend growth annually for the next five years as Lancaster Colony continues its impressive streak of payouts to shareholders; the payout should crest $3.50 per share during the next five years. Lancaster is not an income stock, but it does prioritize growth in the payout each year, and that should continue.

Valuation Analysis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	Now	2025
Avg. P/E	12.8	14.2	18.6	18.6	23.5	24.5	24.3	31.2	31.4	28.8	***27.5***	***20.0***
Avg. Yld.	2.3%	2.4%	2.2%	2.0%	2.0%	2.0%	1.8%	1.6%	1.7%	1.6%	***1.8%***	***2.6%***

Lancaster Colony's price-to-earnings ratio was in excess of 31 in fiscal 2017 and 2018, but has moved down slightly of late. We see fair value at 20 times earnings, reflecting the risks discussed above, and the stock remains one of the most overvalued in our coverage universe at 137% of our estimate of fair value

Due to a forecast decline in the valuation and thus, the stock price, we are expecting the yield to climb closer to 3%. The stock's dividend yield was nearly cut in half from 2009 to 2017 due to a huge rally, but that situation could be rectified by a declining multiple and rising payout in the coming years.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
Payout	36%	29%	34%	40%	38%	47%	49%	44%	47%	47%	***50%***	***53%***

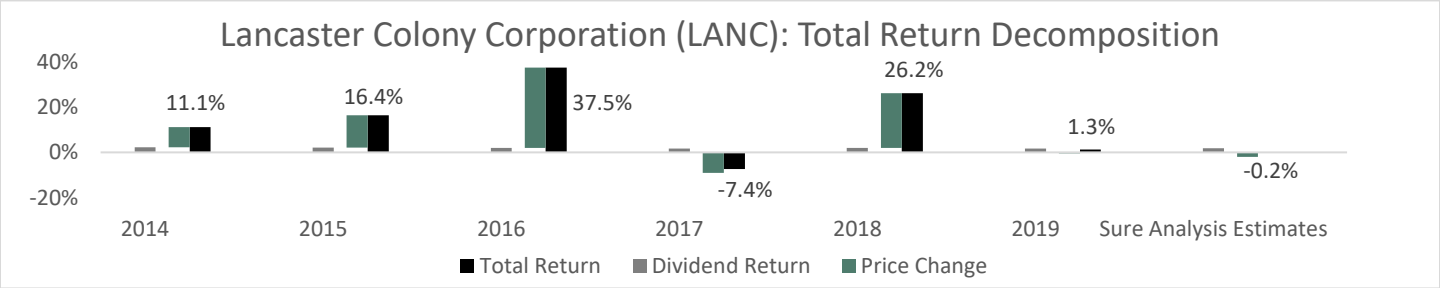
Lancaster Colony's payout should remain near where it is today as dividend growth roughly matches earnings growth. Given its Dividend King status, we know the payout is important to management and the dividend is very safe.

Lancaster Colony's competitive advantage is in its leadership position within the niche categories in which it competes. The company goes after accessory categories like bread, dressings and croutons where competition tends to be lighter. It also has strong distribution partnerships with companies like Wal-Mart and McLane Company, a major restaurant distributor. Its recession performance track record is spotty because it is reliant upon restaurant traffic, something that suffers mightily during times of economic stress.

Final Thoughts & Recommendation

We expect Lancaster Colony to provide shareholders with total annualized returns of -0.2% over the next five years as it continues to be quite overvalued in our view. Investors seeking income may want to wait for a better price with a higher yield, and those seeking growth or value may simply look elsewhere. Overall, Lancaster Colony continues to earn a sell recommendation from Sure Dividend at current prices.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Revenue	1057	1090	989	1014	1041	1105	1191	1202	1223	1308
Gross Profit	270	242	223	245	249	258	300	319	304	326
Gross Margin	25.6%	22.2%	22.6%	24.1%	23.9%	23.3%	25.2%	26.5%	24.8%	24.9%
SG&A Exp.	94	95	82	91	95	103	115	143	130	150
D&A Exp.		19	20	20	20	21	24	25	27	32
Operating Profit	177	147	141	154	154	155	185	176	174	176
Operating Margin	16.7%	13.5%	14.3%	15.2%	14.8%	14.0%	15.5%	14.6%	14.2%	13.5%
Net Profit	115	106	96	109	75	102	122	115	135	151
Net Margin	10.9%	9.8%	9.7%	10.8%	7.2%	9.2%	10.2%	9.6%	11.1%	11.5%
Free Cash Flow	95	112	106	108	113	114	129	119	130	127
Income Tax	60	55	49	50	52	53	63	60	39	45

Balance Sheet Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Total Assets	586	622	683	620	639	702	635	716	804	905
Cash & Equivalents	101	132	192	123	212	182	118	143	206	196
Accounts Receivable	68	64	73	56	58	62	66	70	73	76
Inventories	122	112	110	68	75	78	76	76	91	86
Goodwill & Int. Ass.	99	98	97	96	95	192	189	228	224	279
Total Liabilities	102	105	118	119	110	121	121	140	152	179
Accounts Payable	42	43	41	36	38	39	40	41	58	77
Long-Term Debt	0	0	0	0	0	0	0	0	0	0
Shareholder's Equity	485	518	564	501	529	581	514	576	652	727
D/E Ratio	0	0	0	0	0	0	0	0	0	0

Profitability & Per Share Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Return on Assets	21.2%	17.6%	14.7%	16.8%	11.9%	15.2%	18.2%	17.1%	17.8%	17.6%
Return on Equity	25.9%	21.2%	17.7%	20.5%	14.6%	18.3%	22.2%	21.2%	22.0%	21.8%
ROIC	25.9%	21.2%	17.7%	20.5%	14.6%	18.3%	22.2%	21.2%	22.0%	21.8%
Shares Out.	28	28	27	27	27	27	27	27	28	28
Revenue/Share	37.50	39.36	36.27	37.16	38.12	40.42	43.51	43.80	44.54	47.49
FCF/Share	3.37	4.05	3.89	3.94	4.14	4.19	4.72	4.35	4.72	4.60

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