The Hershey Company (HSY)

Updated February 5th, 2021 by Eli Inkrot

Key Metrics

Current Price:	$148	**5 Year CAGR Estimate:**	4.0%	**Market Cap:**	$31 B
Fair Value Price:	$126	**5 Year Growth Estimate:**	5.0%	**Ex-Dividend Date:**	02/18/21
% Fair Value:	117%	**5 Year Valuation Multiple Estimate:**	-3.1%	**Dividend Payment Date:**	03/15/21
Dividend Yield:	2.2%	**5 Year Price Target**	$161	**Years Of Dividend Growth:**	11
Dividend Risk Score:	B	**Retirement Suitability Score:**	C	**Last Dividend Increase:**	4.0%

Overview & Current Events

The Hershey Company, founded in 1894, is a chocolate and sugar confectionary products manufacturer that sells major brands such as Hershey's, Reese's, Kisses, Cadbury, Ice Breakers, Kit Kat, Almond Joy, Jolly Rancher, Twizzlers, Heath and Milk Duds. Hershey primarily operates in North America but has international operations as well. The company is headquartered in Hershey, PA and trades with a market capitalization of $31 billion.

On February 4th, 2021 Hershey reported Q4 and full year 2020 results for the period ending December 31st, 2020. For the quarter the company generated consolidated net sales of $2.185 billion, representing a 5.7% increase compared to Q4 2019, driven by volume and price realization gains. The North America segment (90% of sales) saw an 8.9% increase in revenue. Reported net income totaled $291.4 million or $1.39 per share, a 41.8% increase, while adjusted earnings-per-share equaled $1.49 compared to $1.28 in last year's quarter, a 16.4% increase.

For the year Hershey generated consolidated net sales of $8.150 billion, representing a 2.0% increase compared to 2019. Reported net income equaled $1.279 billion or $6.11 per share, an 11.9% increase, while adjusted earnings-per-share equaled $6.29 – ahead of prior guidance - compared to $5.78 in 2019.

Hershey also outlined a 2021 outlook, anticipating performance to be in line with its long-term growth expectations of 2% to 4% sales growth and 6% to 8% earnings-per-share growth. In addition, Hershey announced a quarterly dividend of $0.804, making it the 365th consecutive dividend paid.

Growth on a Per-Share Basis

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
EPS	$2.82	$3.24	$3.72	$3.98	$4.12	$4.41	$4.76	$5.36	$5.78	$6.29	***$6.65***	***$8.49***
DPS	$1.38	$1.56	$1.81	$2.04	$2.24	$2.40	$2.55	$2.76	$2.99	$3.15	***$3.22***	***$4.11***
Shares[1]	225	224	224	221	217	212	211	210	209	209	***210***	***210***

Hershey has recorded both strong and consistent growth over the last decade, with earnings-per-share growing every year since 2008. Since 2007 the earnings-per-share growth rate has come in at an average of 8.9% per annum.

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. The company has also been able to improve its margins throughout the last decade. Hershey owns well-recognized brands, so pricing increases have not been a headwind to increasing the volume of its products. Hershey had also been moderately repurchasing its shares over the last couple of years, which has added some additional growth to the company's earnings-per-share. In 2018 Hershey's earnings-per-share growth was above the long-term average, but that was 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.

The COVID-19 pandemic is testing all businesses, but we believe Hershey is set up well for nearly any environment. To this point, 2020 proved to be a standout year. We are forecasting 5% annual growth over the intermediate term.

[1] In millions.

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Valuation Analysis

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	Now	2026
Avg. P/E	19.8	20.9	24.2	24.5	23.0	21.9	22.8	18.8	23.2	23.1	***22.2***	***19.0***
Avg. Yld.	2.5%	2.3%	2.0%	2.1%	2.4%	2.5%	2.3%	2.7%	2.2%	2.2%	***2.2%***	***2.5%***

During the past decade shares of Hershey have traded hands with an average P/E ratio of about 22 times earnings. While we believe a premium multiple is warranted, we are more cautious – using 19 times earnings as a starting place – given the reduced growth expectations. The security presently trades around 22 times our estimated earnings for this year. If shares revert to a 19 multiple, this would imply a moderate valuation headwind.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
Payout	49%	48%	49%	51%	54%	54%	54%	51%	52%	50%	***48%***	***48%***

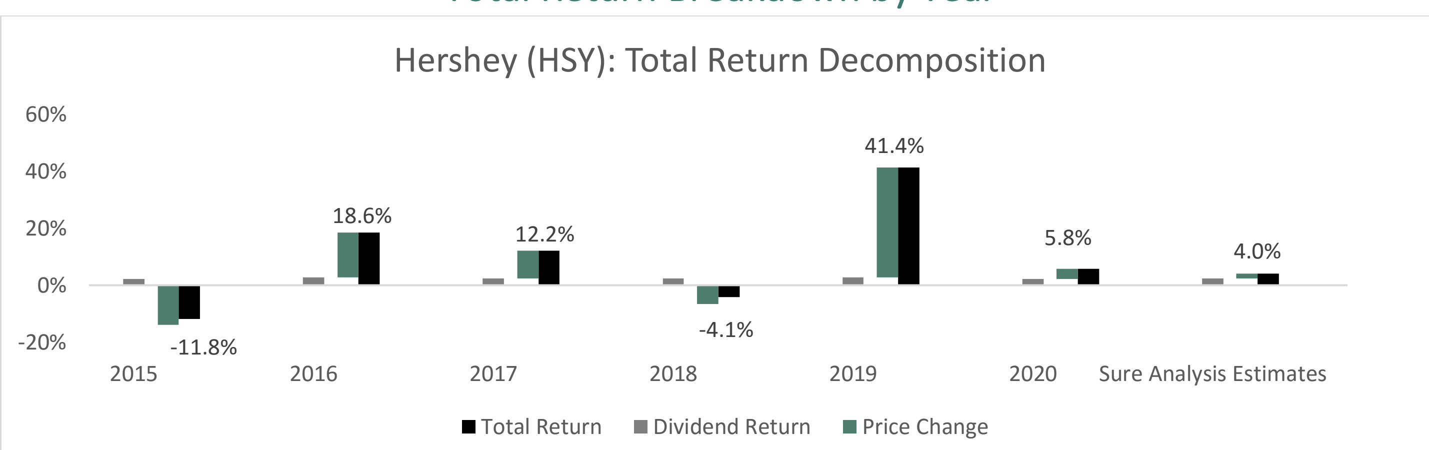
Hershey's dividend payout ratio has moved in a very narrow range throughout the last decade. The company has paid out marginally more than half of its net profits in the form of dividends throughout the majority of those years. The stability of the payout ratio even during the last financial crisis, 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, controlling iconic brands that are ubiquitous to consumers. Competition is not a terrific problem for the company, but if customers became more health-conscious, that could hurt the growth rate for the whole industry. During the last financial crisis – an especially severe recession – the company managed to increase both its profits and its sales, although the dividend was frozen. In addition, 2020 results were strong as well.

Final Thoughts & Recommendation

Shares are down marginally since our last report. Hershey is a solid company, generating highly attractive earnings and dividend growth in the past. On top of that, Hershey is not especially vulnerable to recessions, which makes the company's shares a viable choice for risk-averse investors. However, the total annual return potential of 4.0% per annum - stemming from 5% growth and a 2.2% starting dividend offset by a potential valuation headwind – does not look especially compelling. We are enthused by the quality of the business but believe the valuation could hinder an investment thesis from this point. This view could be too conservative if shares were to command a mid-20's multiple, but we are not ready to make that speculation. We rate shares as a hold.

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	2011	2012	2013	2014	2015	2016	2017	2018	2019
Revenue	6,081	6,644	7,146	7,422	7,387	7,440	7,515	7,791	7,986
Gross Profit	2,532	2,860	3,281	3,336	3,383	3,170	3,455	3,575	3,622
Gross Margin	41.6%	43.0%	45.9%	45.0%	45.8%	42.6%	46.0%	45.9%	45.4%
SG&A Exp.	1,478	1,704	1,924	1,898	1,969	1,891	1,885	1,875	1,906
D&A Exp.	216	210	201	212	245	302	262	295	
Operating Profit	1,054	1,156	1,357	1,438	1,413	1,278	1,570	1,700	1,717
Operating Margin	17.3%	17.4%	19.0%	19.4%	19.1%	17.2%	20.9%	21.8%	21.5%
Net Profit	629	661	820	847	513	720	783	1,178	1,150
Net Margin	10.3%	9.9%	11.5%	11.4%	6.9%	9.7%	10.4%	15.1%	14.4%
Free Cash Flow	240	817	840	474	900	744	992	1,271	
Income Tax	334	355	431	459	389	379	354	239	234

Balance Sheet Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019
Total Assets	4,407	4,755	5,357	5,623	5,344	5,524	5,554	7,703	8,140
Cash & Equivalents	694	728	1,119	375	347	297	380	588	493
Accounts Receivable	399	461	478	597	599	581	588	594	569
Inventories	649	633	660	801	751	746	753	785	815
Goodwill & Int. Ass.	629	803	828	1,151	1,132	1,400	1,295	3,206	3,327
Total Liabilities	3,526	3,706	3,741	4,103	4,297	4,697	4,622	6,296	6,395
Accounts Payable	420	442	462	482	474	523	523	502	551
Long-Term Debt	1,888	1,907	1,962	2,178	2,421	2,980	2,920	4,458	4,266
Shareholder's Equity	857	1,037	1,605	1,455	998	786	915	1,399	1,745
D/E Ratio	2.20	1.84	1.22	1.50	2.43	3.79	3.19	3.19	2.45

Profitability & Per Share Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019
Return on Assets	14.5%	14.4%	16.2%	15.4%	9.4%	13.2%	14.1%	17.8%	14.5%
Return on Equity	71.5%	69.8%	62.1%	55.4%	41.8%	80.7%	92.1%	102%	73.1%
ROIC	22.7%	23.1%	25.1%	23.3%	14.3%	19.8%	20.4%	24.2%	19.4%
Shares Out.	225	224	224	221	217	212	211	210	211
Revenue/Share	26.45	29.10	31.45	33.01	33.48	34.56	35.16	36.93	29.44
FCF/Share	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.