Lancaster Colony Corporation (LANC)

Updated February 11th, 2021 by Josh Arnold

Key Metrics

Current Price:	$185	**5 Year CAGR Estimate:**	3.4%	**Market Cap:**	$5.1 B
Fair Value Price:	$158	**5 Year Growth Estimate:**	5.0%	**Ex-Dividend Date:**	03/04/21[1]
% Fair Value:	117%	**5 Year Valuation Multiple Estimate:**	-3.1%	**Dividend Payment Date:**	03/31/21[2]
Dividend Yield:	1.6%	**5 Year Price Target**	$202	**Years Of Dividend Growth:**	58
Dividend Risk Score:	A	**Retirement Suitability Score:**	B	**Last Dividend Increase:**	7.1%

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 $5.1 billion market capitalization on $1.4 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 2021 representing the 58th consecutive year of dividend increases.

Lancaster reported second quarter earnings on February 4th, 2021 with results coming in ahead of expectations on both the top and bottom lines once again. Total sales rose 5.6% year-over-year to a new second quarter record of $375 million. On an organic basis, sales rose 7.3%. Retail segment sales were up 19.5% to $223 million as COVID-19 buying behavior remains in effect for consumers, driving at-home food consumption in lieu of eating at restaurants. The foodservice segment continues to struggle due to restaurant closures and demand; sales fell -9.7% to $152 million.

Gross profit was up 7% to a second quarter record of $107 million, benefitting from strong retail sales growth and reduced promotional spending. This was partially offset by higher manufacturing costs, as well as higher commodity and freight prices. The company did note it has ongoing cost saving programs in place to help offset some of this. SG&A costs were up $2.5 million year-over-year to $48 million, entirely attributable to the company's ERP project. Operating income was up $4.5 million to $59 million during the quarter due to the factors discussed above.

Net income was $44.6 million, or $1.62 per diluted share, up from $1.58 in the same period a year ago. The company's ERP project incurred $0.23 per share in expenditures during the quarter, up from $0.14 per share in the year-ago period, which crimped growth. Lancaster noted its tax rate moved slightly higher as well.

We now expect $5.85 in earnings-per-share this year as Lancaster continues to perform extremely well.

Growth on a Per-Share Basis

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
EPS	$3.84	$3.51	$3.99	$3.69	$3.72	$4.44	$4.20	$4.92	$5.46	$4.97	***$5.85***	***$7.47***
DPS	$1.29	$1.41	$1.52	$1.72	$1.82	$1.96	$2.15	$2.40	$2.55	$2.75	***$3.00***	***$3.83***
Shares[3]	28	27	27	27	27	27	27	28	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.

We are forecasting 5% 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 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. After a decline in earnings in 2020, we are

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[1] Estimated date
[2] Estimated date
[3] Share count 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.

forecasting a strong rebound in earnings to get Lancaster back to its former growth track for fiscal 2021. Organic growth was strong for the first half as the strength of the retail business more than offset weakness in foodservice.

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 could be $3.83 per share in five years. Lancaster is not a strong income stock, but it does prioritize growth in the payout each year, and that should continue. The company raised the dividend in November 2020 for the 58th consecutive year, boosting the payout by 7%.

Valuation Analysis

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	Now	2026
Avg. P/E	14.2	18.6	18.6	23.5	24.5	24.3	31.2	31.4	28.8	30.0	***31.6***	***27.0***
Avg. Yld.	2.4%	2.2%	2.0%	2.0%	2.0%	1.8%	1.6%	1.7%	1.6%	1.8%	***1.6%***	***1.9%***

The stock's price-to-earnings ratio has spent the past few years around 30, but given the company's exposure to restaurants, we see fair value at 27 times earnings. Today, shares trade for 31.6 times our fiscal 2021 earnings estimate, so we see it as overvalued at present, as it has been for some time.

Due to a forecast decline in the valuation, we are expecting the yield to climb closer to 2%. The stock's dividend yield was nearly cut in half from 2009 to 2017 due to a huge rally, but some of that could be unwound in the coming years.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
Payout	29%	34%	40%	38%	47%	49%	44%	47%	47%	55%	***51%***	***51%***

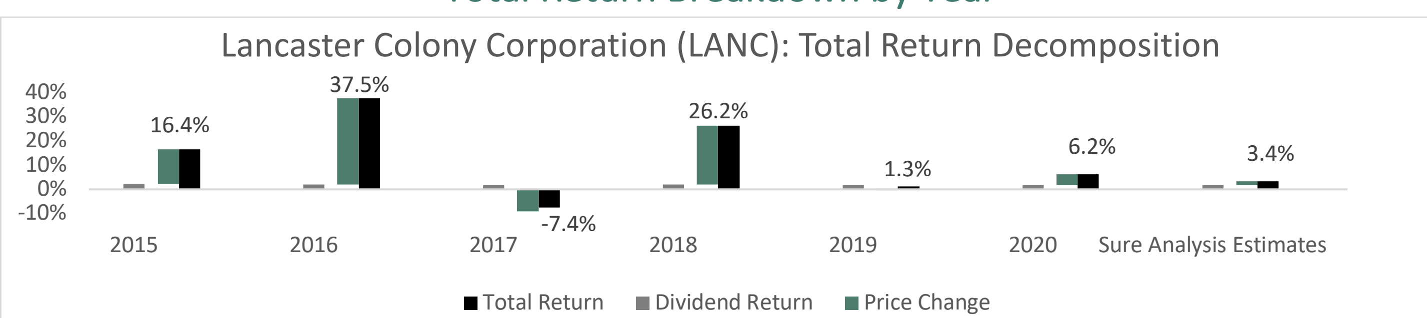
Lancaster Colony's payout should remain near where it is today as dividend growth roughly matches earnings growth. Given its Dividend King status, we know the payout is important to management and the dividend is very safe.

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 Walmart 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. Lancaster's first quarter results showed its exposure to restaurants once again, and while the retail business is booming, it still gets nearly half of its revenue from foodservice.

Final Thoughts & Recommendation

We expect Lancaster Colony to provide shareholders with total annualized returns of 3.4% over the next five years as it continues to be 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. Lancaster Colony continues to earn a sell rating.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Revenue	1090	989	1014	1041	1105	1191	1202	1223	1308	1,334
Gross Profit	242	223	245	249	258	300	319	304	326	358
Gross Margin	22.2%	22.6%	24.1%	23.9%	23.3%	25.2%	26.5%	24.8%	24.9%	26.8%
SG&A Exp.	95	82	91	95	103	115	143	130	150	181
D&A Exp.	19	20	20	20	21	24	25	27	32	38
Operating Profit	147	141	154	154	155	185	176	174	176	177
Operating Margin	13.5%	14.3%	15.2%	14.8%	14.0%	15.5%	14.6%	14.2%	13.5%	13.3%
Net Profit	106	96	109	75	102	122	115	135	151	137
Net Margin	9.8%	9.7%	10.8%	7.2%	9.2%	10.2%	9.6%	11.1%	11.5%	10.3%
Free Cash Flow	112	106	108	113	114	129	119	130	127	88
Income Tax	55	49	50	52	53	63	60	39	45	42

Balance Sheet Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Total Assets	622	683	620	639	702	635	716	804	905	993
Cash & Equivalents	132	192	123	212	182	118	143	206	196	198
Accounts Receivable	64	73	56	58	62	66	70	73	76	87
Inventories	112	110	68	75	78	76	76	91	86	85
Goodwill & Int. Ass.	98	97	96	95	192	189	228	224	279	274
Total Liabilities	105	118	119	110	121	121	140	152	179	210
Accounts Payable	43	41	36	38	39	40	41	58	77	71
Long-Term Debt	0	0	0	0	0	0	0	0	0	0
Shareholder's Equity	518	564	501	529	581	514	576	652	727	783
D/E Ratio	0	0	0	0	0	0	0	0	0	0

Profitability & Per Share Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Return on Assets	17.6%	14.7%	16.8%	11.9%	15.2%	18.2%	17.1%	17.8%	17.6%	14.4%
Return on Equity	21.2%	17.7%	20.5%	14.6%	18.3%	22.2%	21.2%	22.0%	21.8%	18.1%
ROIC	21.2%	17.7%	20.5%	14.6%	18.3%	22.2%	21.2%	22.0%	21.8%	18.1%
Shares Out.	28	27	27	27	27	27	27	28	28	28
Revenue/Share	39.36	36.27	37.16	38.12	40.42	43.51	43.80	44.54	47.49	48.53
FCF/Share	4.05	3.89	3.94	4.14	4.19	4.72	4.35	4.72	4.60	3.21

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