WestRock Co. (WRK)

Updated February 4th, 2021 by Aristofanis Papadatos

Key Metrics

Current Price:	$43	**5 Year CAGR Estimate:**	4.6%	**Market Cap:**	$11.0 B
Fair Value Price:	$36	**5 Year Growth Estimate:**	6.0%	**Ex-Dividend Date:**	2/10/2021
% Fair Value:	118%	**5 Year Valuation Multiple Estimate:**	-3.3%	**Dividend Payment Date:**	2/23/2021
Dividend Yield:	2.0%	**5 Year Price Target**	$49	**Years Of Dividend Growth:**	0
Dividend Risk Score:	C	**Retirement Suitability Score:**	D	**Last Dividend Increase:**	N/A

Overview & Current Events

WestRock was formed in July 2015 by the merger of Rock-Tenn and Mead-Westvaco. It is a leading provider of differentiated paper and packaging solutions, with a market capitalization of $11.0 billion. In its fiscal 2020, which ended on 9/30/2020, the corrugated packaging segment and the consumer packaging segment generated 64% and 36% of its total revenues and 76% and 24% of its pre-tax income, respectively.

WestRock completed the acquisition of KapStone Paper in November, 2018. The deal increased the leverage (Net Debt/EBITDA) of WestRock to 2.9 but the company has been reducing its debt at a fast clip since then. The acquisition of KapStone has enhanced the product offerings and the geographical presence of the company.

In late January, WestRock reported (1/28/21) financial results for the first quarter of fiscal 2021. Total packaging shipments increased 5% thanks to record North American box shipments, which grew 8% over the prior year's quarter. As a result, adjusted earnings-per-share rose 5%, from $0.58 to $0.61, and exceeded analysts' consensus by $0.07. The company has missed analysts' earnings-per-share estimates only twice in the last 23 quarters.

After the end of the first fiscal quarter, WestRock incurred a ransomware attack, which caused significant delays in many processes and has taken its toll on the results of the running quarter. Nevertheless, we expect the good business momentum to offset this headwind in the full year.

Growth on a Per-Share Basis

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
EPS	---	---	---	---	$3.89	$2.53	$2.62	$4.08	$3.98	$2.74	***$3.30***	***$4.42***
DPS	---	---	---	---	$0.38	$1.50	$1.60	$1.72	$1.82	$1.07	***$0.85***	***$1.25***
Shares[1]	---	---	---	---	257.0	251.0	254.5	259.2	259.0	260.0	***265.0***	***260.0***

WestRock has a short and somewhat volatile historical record. Since its foundation in its current form, the company grew its earnings-per-share at a 0.6% average annual rate until 2019 and incurred a decline in its earnings in fiscal 2020 due to the pandemic. Moreover, even before the pandemic, there were increasing concerns over high inventories in the containerboard market and a surge in the global supply of containerboard products in upcoming years. This factor, which is out of WestRock's control, will adversely affect its margins. However, we expect the pandemic to subside and the company to recover in the second half of this year. In addition, WestRock is likely to benefit from the growing North American corrugated market in the long run. Overall, we expect the company to grow its earnings-per-share by about 6% per year on average over the next five years off this year's somewhat low base.

Valuation Analysis

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	Now	2026
Avg. P/E	---	---	---	---	15.2	16.8	20.3	14.9	9.8	12.3	***13.0***	***11.0***
Avg. Yld.	---	---	---	---	0.6%	3.5%	3.0%	2.8%	4.7%	3.2%	***2.0%***	***2.6%***

[1] In millions.

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WestRock is trading at a price-to-earnings ratio of 13.0, which is lower than its 4-year average of 14.9. Due to its short historical record, its increased amount of debt from the KapStone acquisition, and the increased competition in its business, the stock warrants a reduced valuation. We assume a fair price-to-earnings ratio of 11.0 for the stock. If the stock reaches our fair valuation level over the next five years, it will incur a -3.3% annualized drag in its returns.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2020	2026
Payout	---	---	---	---	9.8%	59.3%	61.1%	42.2%	45.7%	39.1%	***25.8%***	***28.3%***

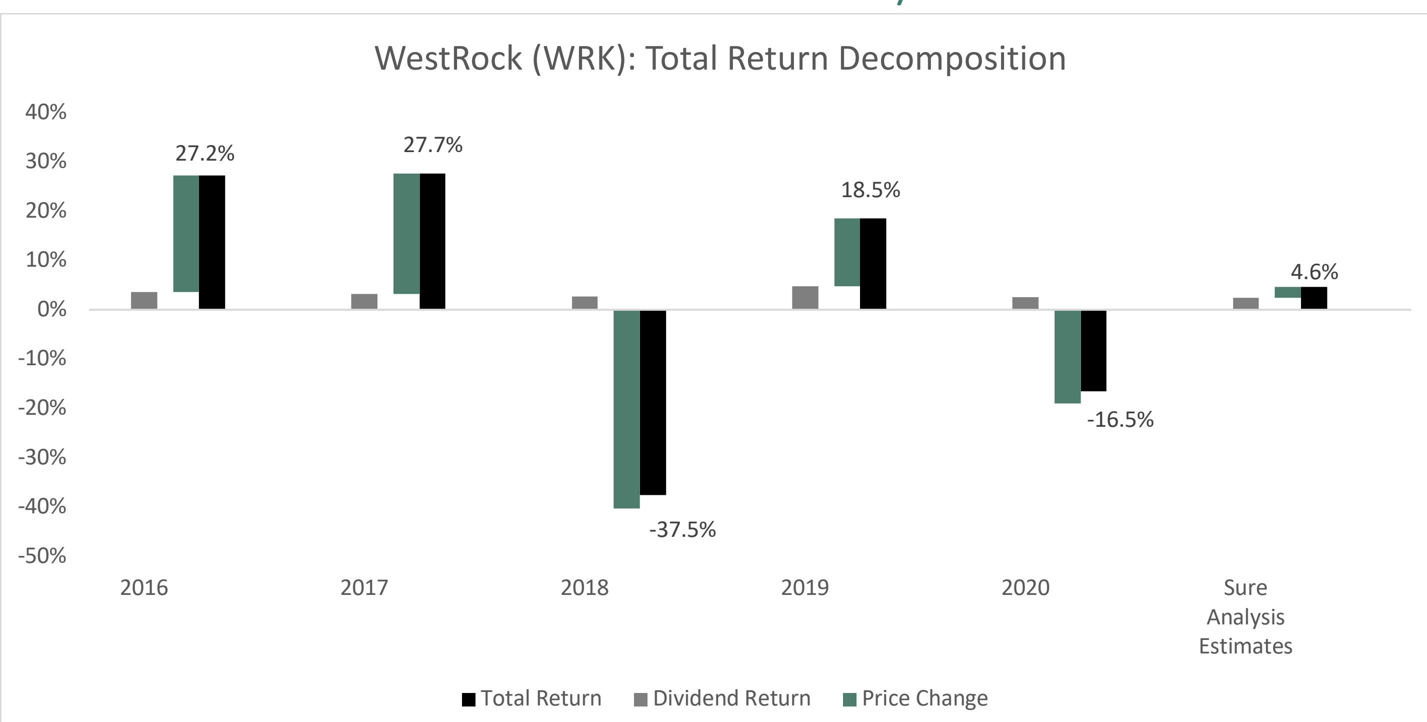
WestRock cannot control the total supply of paper products. As a result, it is vulnerable to the total production volume of its competitors. The business of WestRock is highly cyclical and hence investors should be especially careful before initiating a position in the stock. If they invest near the peak of the cycle, when business prospects usually look bright and the earnings multiple of the stock usually seems too low, they run the risk of incurring excessive losses.

Moreover, due to the high debt load that has resulted from the acquisition of KapStone, WestRock is vulnerable to the ongoing recession, which has resulted from the pandemic. Its interest expense consumes 30% of operating income while its net debt of $15.5 billion is about 22 times its annual earnings and hence it is excessive. The weak balance sheet of the company helps explain the recent -57% dividend cut.

Final Thoughts & Recommendation

We expect the pandemic to subside and WestRock to recover later this year. However, the stock has doubled off its bottom almost a year ago, partly thanks to optimism related to the massive vaccination programs. The stock may offer just a 4.6% average annual return over the next five years. It thus maintains its hold rating. Moreover, due to its high leverage, the company may come under stress if the pandemic lasts much longer than currently anticipated. While we expect the pandemic to subside in the second half of the year, investors should keep this risk factor in mind.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Revenue	5399.6	9207.6	9545.4	9895.1	11125	14172	14860	16285	18,289	17,579
Gross Profit	991.9	1532.7	1846.5	1933.6	2138.3	2758.6	2740.2	3393.9	3,749	3,197
Gross Margin	18.4%	16.6%	19.3%	19.5%	19.2%	19.5%	18.4%	20.8%	20.5%	18.2%
SG&A Exp.	541	928	869	938	1,026	1,750	1,457	1,731	1,709	1,623
Operating Profit	451	605	892	910	993	797	1,031	1,335	1,640	1,173
Op. Margin	8.3%	6.6%	9.3%	9.2%	8.9%	5.6%	6.9%	8.2%	9.0%	6.7%
Net Profit	141	249	727	480	507	(396)	708	1,906	863	(691)
Net Margin	2.6%	2.7%	7.6%	4.8%	4.6%	-2.8%	4.8%	11.7%	4.7%	-3.9%
Free Cash Flow	262	187	592	618	618	892	685	931	941	1,093
Income Tax	70	137	(22)	287	233	90	159	(875)	277	164

Balance Sheet Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Total Assets	10,566	10,687	10,733	11,040	25,372	23,038	25,089	25,361	30,157	28,780
Cash & Equivalents	42	37	36	33	208	341	298	637	152	251
Accounts Receivable	1,110	1,076	1,135	1,119	1,575	1,592	1,887	2,011	2,193	2,143
Inventories	850	862	938	1,029	1,761	1,638	1,797	1,830	2,108	2,023
Goodwill & Int. Ass.	2,639	2,660	2,562	2,618	7,442	7,377	8,858	8,700	11,345	9,629
Total Liabilities	7,187	7,281	6,421	6,732	13,589	13,208	14,703	13,878	18,473	18,132
Accounts Payable	781	709	802	813	1,231	1,054	1,492	1,717	1,832	1,674
Long-Term Debt	3,446	3,413	2,845	2,985	5,622	5,789	6,555	6,415	10,063	9,431
Shareholder's Equity	3,372	3,406	4,312	4,307	11,652	9,729	10,343	11,469	11,670	10,631
D/E Ratio	1.02	1.00	0.66	0.69	0.48	0.60	0.63	0.56	0.86	0.89

Profitability & Per Share Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Return on Assets	2.1%	2.3%	6.8%	4.4%	2.8%	-1.6%	2.9%	7.6%	3.1%	-2.3%
Return on Equity	6.4%	7.4%	18.8%	11.1%	6.4%	-3.7%	7.1%	17.5%	7.5%	-6.2%
ROIC	3.1%	3.7%	10.4%	6.6%	4.1%	-2.4%	4.4%	10.9%	4.4%	-3.3%
Shares Out.	---	---	---	---	257.0	251.0	254.5	259.2	259.0	260.0
Revenue/Share	53.46	63.90	65.33	67.77	64.19	54.95	58.11	62.68	70.59	67.82
FCF/Share	2.60	1.30	4.05	4.23	3.57	3.46	2.68	3.58	3.63	4.22

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