



The Scotts Miracle-Gro Company (SMG)

Updated August 4th, 2021 by Nikolaos Sismanis

Key Metrics

Current Price:	\$178	5 Year CAGR Estimate:	11.8%	Market Cap:	\$9.89 B
Fair Value Price:	\$210	5 Year Growth Estimate:	7.0%	Ex-Dividend Date:	08/26/21
% Fair Value:	85%	5 Year Valuation Multiple Estimate:	3.4%	Dividend Payment Date:	09/10/21
Dividend Yield:	1.5%	5 Year Price Target	\$295	Years Of Dividend Growth:	12
Dividend Risk Score:	C	Retirement Suitability Score:	D	Last Dividend Increase:	6.5%

Overview & Current Events

The Scotts Miracle-Gro Company is one of the world's leading marketers of branded consumer lawn and garden as well as hydroponic and indoor growing products. The company offers fertilizers, grass seed products, spreaders, outdoor cleaners, and any lawn-related weed, pest, and disease control products. Scotts Miracle-Gro generates around \$4.3 billion in annual revenue and is headquartered in Marysville, Ohio.

On August 4th, 2021, Scotts Miracle-Gro reported its Q3-2021 results for the quarter ended July 3rd, 2021. The company achieved sales of \$1.61 billion during the period, an 8.1% increase compared to Q3-2020, primarily driven by a 48% increase in the Hawthorne segment and humbler growth in all divisions. The company continues to experience record levels of consumer demand for its lawn and garden products. For instance, in North America, lighting sales were up 77% during the quarter, while the nutrient and growing media segments grew by 54% and 33%, respectively.

Consequently, EPS also increased by 12% to \$4.00. Separately, the company announced a further strengthening of its Hawthorne Gardening portfolio with the acquisition of HydroLogic Purification Systems, a leading provider of products, accessories, and water filtration and purification systems. HydroLogic will add approximately \$20 million in annualized sales.

Management guided for sales growth of 7%-9% in its U.S. consumer segment and raised its Hawthorne segment growth expectations from 30%-40% to 40%-45%. Management also reaffirmed its non-GAAP FY2021 EPS estimates to \$9.00-\$9.30, the midpoint of which we have used in our calculations. In late July, the company hiked its quarterly dividend for the 12th consecutive year by 6.5% to \$0.66, implying an annualized rate of \$2.64.

Growth on a Per-Share Basis

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
EPS	\$2.60	\$1.75	\$2.61	\$2.70	\$2.62	\$5.16	\$3.68	\$1.13	\$8.30	\$6.96	\$9.15	\$12.83
DPS	\$1.05	\$1.23	\$1.41	\$1.76	\$1.82	\$1.91	\$2.03	\$2.14	\$2.23	\$2.36	\$2.64	\$3.53
Shares	64.7	61.0	61.7	61.6	61.1	61.1	59.4	56.2	55.5	55.7	55.7	55.7

Scotts Miracle-Gro's EPS has fluctuated over time due to its multiple acquisitions over the years. The jump in profitability post-2018 has been attributable to its Sunlight Supply acquisition, the largest distributor of hydroponic products in the U.S., which unlocked great synergies and substantial cost efficiencies.

The company's future growth lies mostly in the industry's organic growth, potential acquisitions, and the snowballing cannabis industry, which utilizes much of its products. Moving forward, we expect acquisitions to continue (with eight companies purchased since 2013) due to the highly fragmented agricultural industry. Dividend growth has been consistent, numbering 12 years of consecutive annual DPS hikes.

Over the past five years, DPS has grown by a compound annual growth rate of 6.7%. However, the latest increase of 6.5% may indicate a potential acceleration going forward due to the current payout ratio and available room for growth.

We also anticipate the company to keep expanding its net income margins, which have more than doubled over the past decade, currently north of 13%. Combined with its non-stop momentum, we raise our EPS growth estimates from 6.5%

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to 7% but retain our DPS growth estimates at 6%. These rates are likely to be stronger in the short term, but we remain prudent against a potential deceleration later on.

Valuation Analysis

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	Now	2026
Avg. P/E	17.2	22.9	19.2	22.2	25.0	17.1	26.1	---	12.0	11.9	19.5	23.0
Avg. Yld.	2.4%	3.1%	2.8%	2.9%	2.8%	2.2%	2.1%	2.7%	2.2%	1.7%	1.5%	1.2%

Over the past decade, Scotts Miracle-Gro's valuation has average around 24.4 times underlying net income. Despite the company delivering record top & bottom-line numbers, the forward P/E currently stands around 19.5.

Due to the company's ongoing growth catalysts, we believe the stock should trade at a P/E of around 23, which better reflects its rapid expansion and overall prospects while taking into account the growing competition too.

The Scotts Miracle-Gro's dividend yield currently hovers at around 1.5%, significantly higher since our last report due to shares retreating since then and the company's latest dividend hike.

Safety, Quality, Competitive Advantage, & Recession Resiliency

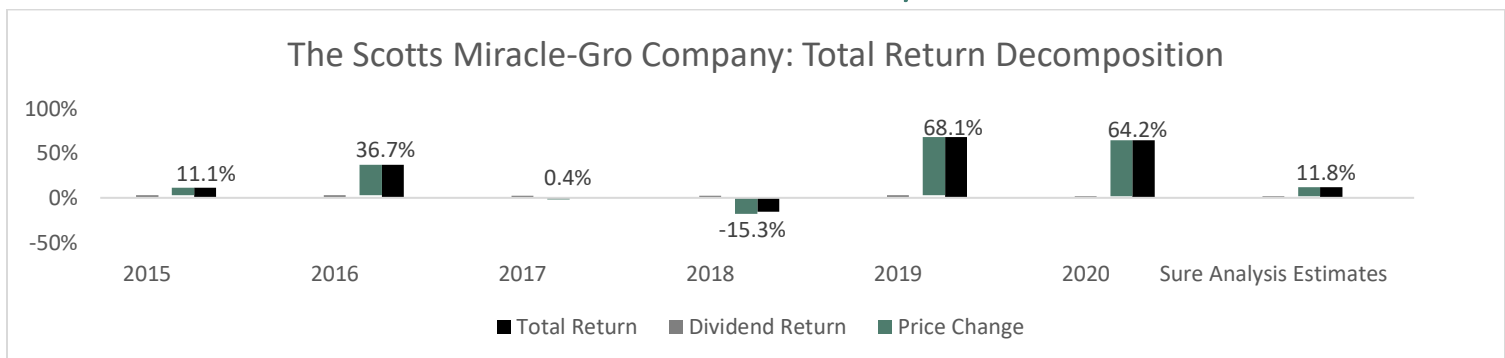
Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
Payout	40%	70%	54%	65%	69%	37%	55%	---	27%	34%	29%	28%

Scotts Miracle-Gro's dividend should be quite safe. Over the past couple of years, the company's expanded profitability has improved DPS coverage, even encouraging a potential acceleration in its growth. During the last recession, in 2008, the company posted a loss but quickly rebounded. In 2020, despite the adverse effects of COVID-19, sales accelerated driven by the work-from-home economy boosting demand for SMG's products. Hence, the company's resiliency was once again proven. Still, it's important not to overlook the fact that the company's growth is limited to the agricultural industry's growth, which is a very mature one, with few expansion avenues in the consumer market. Moreover, the company faces significant competition and is quite indebted, with a long-term debt/equity ratio of 263.8%, though interest payments remain easily manageable, covered by nearly ten times its operating income.

Final Thoughts & Recommendation

Despite Scotts Miracle-Gro's niche business model, the company has managed to grow over the decades, assisted by management's successful acquisitions. The stock features a decent dividend growth record, while catalysts such as the growing cannabis industry and its accretive acquisitions should keep fueling its growth. We forecast annualized returns of around 11.8% in the medium term, powered by the company's EPS & DPS growth capacity, further boosted by the possibility for valuation tailwinds following the recent multiple compression. Shares earn a buy 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	2,800	2,771	2,774	2,578	2,371	2,506	2,642	2,663	3,156	4,132
Gross Profit	1,009	957	978	890	811	900	973	865	1,020	1,347
Gross Margin	36.0%	34.5%	35.3%	34.5%	34.2%	35.9%	36.8%	32.5%	32.3%	32.6%
SG&A Exp.	686	644	660	512	444	468	489	469	529	687
D&A Exp.	62	62	66	64	69	74	80	83	89	95
Operating Profit	312	248	319	329	326	393	422	325	418	585
Op. Margin	11.1%	8.9%	11.5%	12.8%	13.7%	15.7%	16.0%	12.2%	13.3%	14.2%
Net Profit	168	107	161	167	160	315	218	64	461	387
Net Margin	6.0%	3.8%	5.8%	6.5%	6.7%	12.6%	8.3%	2.4%	14.6%	9.4%
Free Cash Flow	49	84	282	153	(115)	186	294	274	184	495
Income Tax	83	68	92	80	76	138	117	(12)	145	124

Balance Sheet Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Total Assets	2,052	2,074	1,937	2,058	2,527	2,756	2,747	3,055	3,029	3,381
Cash & Equivalents	131	132	130	89	71	29	121	34	19	17
Acc. Receivable	324	331	207	224	158	127	198	226	224	475
Inventories	387	415	325	385	396	395	408	481	540	622
Goodwill & Int.	629	617	600	654	939	1,062	1,191	1,400	1,246	1,223
Total Liabilities	1,492	1,473	1,227	1,491	1,894	2,022	2,085	2,695	2,306	2,678
Accounts Payable	150	152	138	193	193	131	153	151	214	391
Long-Term Debt	795	783	571	784	1,158	1,216	1,401	2,016	1,652	1,522
Total Equity	560	602	711	554	621	715	649	355	719	697
D/E Ratio	1.42	1.30	0.80	1.42	1.87	1.70	2.16	5.69	2.30	2.18

Profitability & Per Share Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Return on Assets	8.0%	5.2%	8.0%	8.3%	7.0%	11.9%	7.9%	2.2%	15.1%	12.1%
Return on Equity	25.4%	18.3%	24.6%	26.3%	27.2%	47.2%	32.0%	12.7%	85.8%	54.7%
ROIC	12.2%	7.8%	12.1%	12.6%	10.2%	16.9%	10.9%	2.9%	19.4%	16.8%
Shares Out.	64.7	61.0	61.7	61.6	61.1	61.1	59.4	56.2	55.5	55.7
Revenue/Share	42.29	44.61	44.31	41.12	38.12	40.42	43.89	46.64	56.06	72.61
FCF/Share	0.75	1.35	4.50	2.45	(1.85)	3.00	4.88	4.80	3.28	8.70

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

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