Hormel Foods Corporation (HRL)

Updated June 9th, 2022, by Josh Arnold

Key Metrics

Current Price:	$45	**5 Year CAGR Estimate:**	6.1%	**Market Cap:**	$25 B
Fair Value Price:	$41	**5 Year Growth Estimate:**	6.0%	**Ex-Dividend Date:**	07/08/22[1]
% Fair Value:	111%	**5 Year Valuation Multiple Estimate:**	-2.0%	**Dividend Payment Date:**	08/15/22
Dividend Yield:	2.3%	**5 Year Price Target**	$54	**Years Of Dividend Growth:**	56
Dividend Risk Score:	A	**Retirement Suitability Score:**	B	**Rating:**	Hold

Overview & Current Events

Hormel Foods was founded in 1891 in Minnesota. Since that time, the company has grown into a $25 billion market capitalization juggernaut in the food products industry with about $12 billion in annual revenue. Hormel has kept with its core competency as a processor of meat products for well over a hundred years but has also grown into other business lines through acquisitions. The company sells its products in 80 countries worldwide, and its brands include Skippy, SPAM, Applegate, Justin's, and more than 30 others. In addition, Hormel is a member of the Dividend Kings, having increased its dividend for 56 consecutive years.

Hormel reported second quarter earnings on June 2nd, 2022, and results were better than expected on both the top and bottom lines. Earnings-per-share came to 48 cents, which was a penny ahead of estimates. Revenue was up 19% from last year's Q2, hitting $3.1 billion, and $30 million better than estimates.

Volume was 1.2 billion pounds, down 2% on a headline basis. Organic volume was down 8%, which excludes acquisitions and divestitures. However, strong pricing helped organic sales rise 10% despite the decline in volumes, and Q2 revenue was a record for Hormel.

Refrigerated foods saw volume decline 13%, as organic volume fell 14%. Net sales were up 13%, led by organic sales of +11% on strong pricing. Segment profit was up just 3% as rising revenue was largely offset by higher costs.

Grocery products saw volume rise 19% as organic volume was up 2%. Net sales rose 39% as organic sales were up 7%. The difference was the Planters acquisition. Segment profit declined 9%.

Operating income was $335 million, up 16% year-over-year. Operating margin was 10.8% of revenue, up from 10.5% last quarter, but down from 11.1% a year ago.

We cut our estimate of earnings-per-share for this year slightly following Q2 results, and we now stand at $1.85.

Growth on a Per-Share Basis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
EPS	$0.93	$0.98	$1.12	$1.32	$1.64	$1.57	$1.86	$1.74	$1.66	$1.73	***$1.85***	***$2.48***
DPS	$0.30	$0.34	$0.40	$0.50	$0.58	$0.68	$0.75	$0.84	$0.93	$0.98	***$1.04***	***$1.33***
Shares[2]	528	526	527	527	528	528	529	544	548	542	***542***	***542***

Hormel's earnings-per-share has grown nicely throughout the past decade, only dipping year-over-year three times in this span. Relatively consistent results have come from a steady stream of acquisitions and a bit of organic growth. This has afforded Hormel the ability to consistently raise its dividend as well.

We are forecasting forward earnings growth of 6% annually as Hormel could grow more slowly than it has in the past. We see sales growth as the primary driver of earnings-per-share expansion moving forward as recent results continue to show that margins and volumes can be unpredictable for this business. Hormel will likely continue to buy growth because its legacy businesses are not currently producing it outside of an extraordinary circumstance early in 2020. This

[1] Estimated date

[2] 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.

strategy has certainly worked in the past, and Planters is yet another example. However, margins are very much in focus for the balance of 2022 on cost inflation.

Valuation Analysis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	Now	2027
Avg. P/E	15.6	19.8	21.3	21.6	23.4	21.8	19.3	24.2	28.4	26.9	***24.3***	***22.0***
Avg. Yld.	2.1%	1.8%	1.7%	1.8%	1.5%	2.0%	2.1%	2.0%	2.0%	2.1%	***2.3%***	***2.4%***

Hormel's price-to-earnings ratio has been volatile in the last decade, sinking as low as 13 in 2009 before rebounding to 23.4 in 2016. It sits at 24.3 now and we believe it could move lower over time towards our fair value estimate of 22 times earnings. That works out to a modest headwind to total returns over the next five years as the stock remains expensive. Given Hormel's struggles with volume and margins, we believe investors are much more likely to reduce the earnings multiple than expand it further. We are forecasting a higher yield five years from now as the stock's valuation could move lower.

Hormel boosted its dividend once more at the beginning of 2022, this time adding just over 6% to its payout, marking its 56th consecutive year of dividend increases.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
Payout	30%	33%	34%	35%	33%	41%	40%	48%	56%	57%	***56%***	***54%***

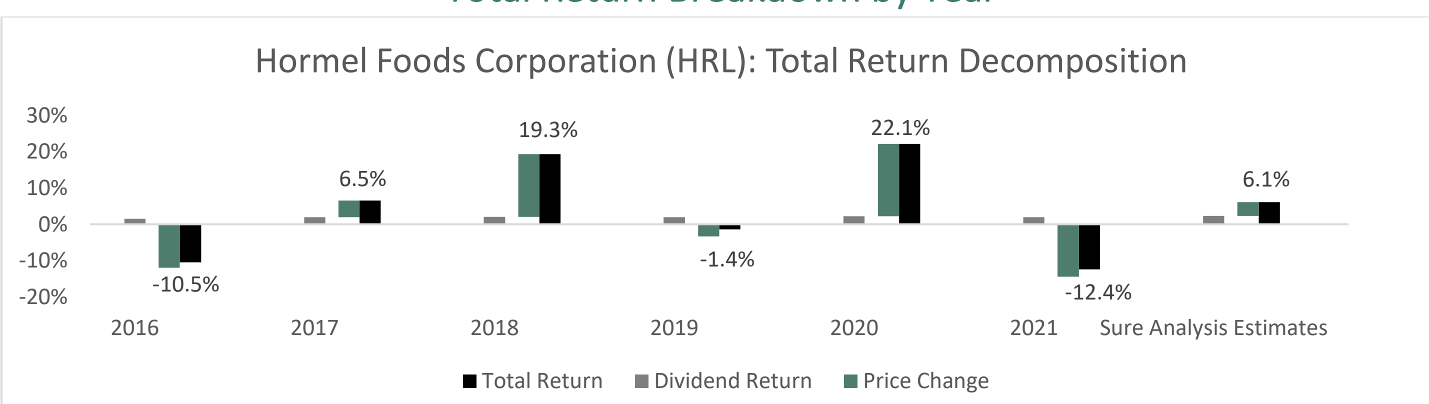
Hormel's payout ratio is just over half of earnings, and we expect that it will remain this way for the foreseeable future. Management is certainly committed to the dividend, but it wants to acquire growth as well, which uses cash.

Hormel's main competitive advantage is its ~40 products that are either #1 or #2 in their category. Hormel has brands that are proven, and that leadership position is difficult for competitors to supplant. In addition, Hormel has a global network of distributors that few food companies can rival. Hormel's earnings-per-share actually grew during the Great Recession while most of the world was in rather dire straits, a testament to the company's defensive nature.

Final Thoughts & Recommendation

Hormel looks overvalued today in our view, which is consistent with our last update. The company is in a tough spot as it tries to grow without sacrificing margins, which simply isn't working, as seen again in Q2. With the valuation still elevated and margins struggling, we forecast just 6.1% total annual returns for Hormel. However, we're reiterating Hormel at a hold rating.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Revenue	8231	8752	9316	9264	9523	9168	9546	9497	9,608	11,386
Gross Profit	1332	1413	1565	1809	2158	1997	1979	1885	1,826	1,928
Gross Margin	16.2%	16.1%	16.8%	19.5%	22.7%	21.8%	20.7%	19.8%	19.0%	16.9%
SG&A Exp.	606	627	651	744	872	759	841	728	761	853
D&A Exp.	119	125	130	133	132	131	162	165	206	228
Operating Profit	726	785	914	1065	1286	1237	1138	1157	1,065	1,075
Operating Margin	8.8%	9.0%	9.8%	11.5%	13.5%	13.5%	11.9%	12.2%	11.1%	9.4%
Net Profit	500	526	603	686	890	847	1012	979	908	909
Net Margin	6.1%	6.0%	6.5%	7.4%	9.3%	9.2%	10.6%	10.3%	9.5%	8.0%
Free Cash Flow	385	531	588	848	784	813	852	629	761	770
Income Tax	253	268	316	370	427	432	169	231	206	217

Balance Sheet Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Total Assets	4564	4916	5456	6140	6370	6976	8142	8109	9,908	12,696
Cash & Equivalents	682	434	334	347	415	444	459	673	1,714	614
Accounts Receivable	507	552	610	606	591	618	600	574	702	896
Inventories	951	968	1055	993	986	921	964	1042	1,073	1,369
Goodwill & Int. Ass.	754	1313	1781	2527	2738	3147	3921	3516	3,689	6,751
Total Liabilities	1739	1599	1844	2138	1919	2036	2537	2183	3,478	5,718
Accounts Payable	386	387	484	495	482	553	619	590	645	793
Long-Term Debt	250	250	250	435	250	250	625	250	1,304	3,324
Shareholder's Equity	2819	3311	3606	3998	4448	4936	5601	5921	6,426	6,973
LTD/E Ratio	0.09	0.08	0.07	0.11	0.06	0.05	0.11	0.04	0.20	0.48

Profitability & Per Share Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Return on Assets	11.4%	11.1%	11.6%	11.8%	14.2%	12.7%	13.4%	12.0%	10.1%	8.0%
Return on Equity	18.3%	17.2%	17.4%	18.0%	21.1%	18.0%	19.2%	17.0%	14.7%	13.6%
ROIC	16.7%	15.8%	16.2%	16.5%	19.5%	17.1%	17.7%	15.8%	13.1%	10.1%
Shares Out.	528	526	527	527	528	528	529	544	548	542
Revenue/Share	15.30	16.19	17.24	17.12	17.56	17.00	17.55	17.42	17.58	20.79
FCF/Share	0.72	0.98	1.09	1.57	1.45	1.51	1.57	1.15	1.39	1.41

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