The Hershey Company (HSY)

Updated July 28th, 2022, by Eli Inkrot

Key Metrics

Current Price:	$222	**5 Year CAGR Estimate:**	0.8%	**Market Cap:**	$46 B
Fair Value Price:	$162	**5 Year Growth Estimate:**	5.0%	**Ex-Dividend Date:**	08/18/22
% Fair Value:	137%	**5 Year Valuation Multiple Estimate:**	-6.0%	**Dividend Payment Date:**	09/15/22
Dividend Yield:	1.9%	**5 Year Price Target**	$207	**Years Of Dividend Growth:**	13
Dividend Risk Score:	B	**Retirement Suitability Score:**	D	**Rating:**	Sell

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 $46 billion.

On December 14th, 2021, Hershey completed the acquisition of Dot's Pretzels.

On February 1st, 2022, Hershey announced it was changing its reportable segments to North America Confectionery, North America Salty Snacks, and International.

On July 28th, 2022, Hershey declared a $1.036 quarterly dividend, marking a 15.0% increase.

Also on July 28th, 2022, Hershey reported Q2 2022 results for the period ending July 3rd, 2022. For the quarter, the company generated consolidated net sales of $2.373 billion, a 19.3% increase compared to Q2 2021. The North America Confectionary segment (80% of sales) increased 12.9%. Reported net income equaled $315.6 million or $1.53 per share, while adjusted earnings-per-share equaled $1.80 compared to $1.47 previously.

Hershey also raised its 2022 outlook. The company now anticipates 12% to 14% sales growth (from 10% - 12% and 8% - 10% previously) and 12% to 14% adjusted earnings-per-share growth (from 10% - 12% and 9% - 11% previously), working out to $8.05 to $8.20. We have updated our forecast accordingly.

Growth on a Per-Share Basis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
EPS	$3.24	$3.72	$3.98	$4.12	$4.41	$4.76	$5.36	$5.78	$6.29	$7.19	***$8.12***	***$10.36***
DPS	$1.56	$1.81	$2.04	$2.24	$2.40	$2.55	$2.76	$2.99	$3.15	$3.41	***$4.14***	***$5.29***
Shares[1]	224	224	221	217	212	211	210	209	209	207	***207***	***205***

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 9.3% 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. 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, 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 most 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 and 2021 proved to be a standout years. We are forecasting 5% annual growth.

[1] 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.

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Valuation Analysis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	Now	2027
Avg. P/E	20.9	24.2	24.5	23.0	21.9	22.8	18.8	23.2	23.4	23.8	***27.3***	***20.0***
Avg. Yld.	2.3%	2.0%	2.1%	2.4%	2.5%	2.3%	2.7%	2.2%	2.2%	2.0%	***1.9%***	***2.6%***

During the past decade shares of Hershey have traded hands with an average P/E ratio of about 23 times earnings. While we believe a premium multiple is warranted, we are a bit more cautious – using 20 times earnings as a starting place – given the reduced growth expectations. The security presently trades around 27 times our estimated earnings for this year. If shares revert to a 20 multiple, this will imply a material valuation headwind.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
Payout	48%	49%	51%	54%	54%	54%	51%	52%	50%	47%	***51%***	***51%***

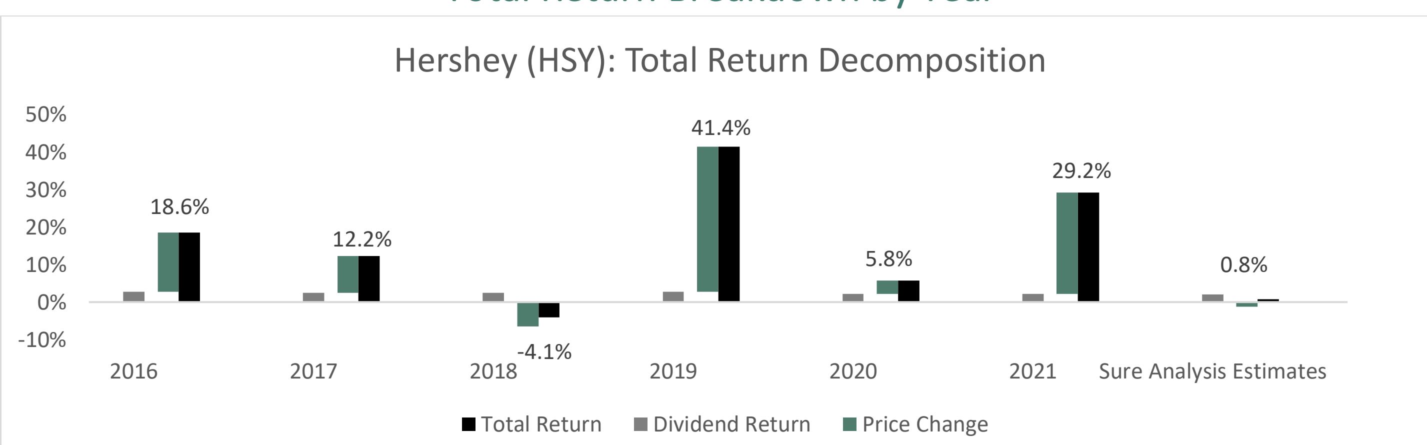
Hershey's dividend payout ratio has moved in a very narrow range throughout the last decade. The company has paid out marginally more than half of its net profits in the form of dividends throughout the majority of those years. The stability of the payout ratio even during the last financial crisis, 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 up 25% in the last year. 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 0.8% per annum - stemming from 5% growth and a 1.9% starting dividend offset by a potential valuation headwind – is not 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 high-20's multiple, but we are not ready to make that speculation. Shares earn a sell 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	6,644	7,146	7,422	7,387	7,440	7,515	7,791	7,986	8,150	8,971
Gross Profit	2,860	3,281	3,336	3,383	3,170	3,455	3,575	3,622	3,701	4,049
Gross Margin	43.0%	45.9%	45.0%	45.8%	42.6%	46.0%	45.9%	45.4%	45.4%	45.1%
SG&A Exp.	1,704	1,924	1,898	1,969	1,891	1,885	1,875	1,906	1,891	2,001
D&A Exp.	210	201	212	245	302	262	295	292	295	---
Operating Profit	1,156	1,357	1,438	1,413	1,278	1,570	1,700	1,717	1,810	2,047
Operating Margin	17.4%	19.0%	19.4%	19.1%	17.2%	20.9%	21.8%	21.5%	22.2%	22.8%
Net Profit	661	820	847	513	720	783	1,178	1,150	1,279	1,478
Net Margin	9.9%	11.5%	11.4%	6.9%	9.7%	10.4%	15.1%	14.4%	15.7%	16.5%
Free Cash Flow	817	840	474	900	744	992	1,271	1,446	1,258	---
Income Tax	355	431	459	389	379	354	239	234	220	314

Balance Sheet Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Total Assets	4,755	5,357	5,623	5,344	5,524	5,554	7,703	8,140	9,132	10,410
Cash & Equivalents	728	1,119	375	347	297	380	588	493	1,144	329
Accounts Receivable	461	478	597	599	581	588	594	569	615	671
Inventories	633	660	801	751	746	753	785	815	964	989
Goodwill & Int. Ass.	803	828	1,151	1,132	1,400	1,295	3,206	3,327	3,471	4,671
Total Liabilities	3,706	3,741	4,103	4,297	4,697	4,622	6,296	6,395	6,894	7,655
Accounts Payable	442	462	482	474	523	523	502	551	580	692
Long-Term Debt	1,907	1,962	2,178	2,421	2,980	2,920	4,458	4,266	4,522	5,029
Shareholder's Equity	1,037	1,605	1,455	998	786	915	1,399	1,745	2,234	2,757
LTD/E Ratio	1.84	1.22	1.50	2.43	3.79	3.19	3.19	2.45	2.02	1.82

Profitability & Per Share Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Return on Assets	14.4%	16.2%	15.4%	9.4%	13.2%	14.1%	17.8%	14.5%	14.8%	15.1%
Return on Equity	69.8%	62.1%	55.4%	41.8%	80.7%	92.1%	102%	73.1%	64.4%	59.2%
ROIC	23.1%	25.1%	23.3%	14.3%	19.8%	20.4%	24.2%	19.4%	20.2%	20.3%
Shares Out.	224	224	221	217	212	211	210	211	209	208
Revenue/Share	29.10	31.45	33.01	33.48	34.56	35.16	36.93	29.44	38.92	43.18
FCF/Share	3.58	3.70	2.11	4.08	3.46	4.64	6.03	6.86	6.01	---

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