Packaging Corporation of America (PKG)

Updated January 29th, 2023 by Quinn Mohammed

Key Metrics

Current Price:	$138	**5 Year CAGR Estimate:**	8.4%	**Market Cap:**	$13 B
Fair Value Price:	$147	**5 Year Growth Estimate:**	4.0%	**Ex-Dividend Date[1]:**	03/14/23
% Fair Value:	94%	**5 Year Valuation Multiple Estimate:**	1.2%	**Dividend Payment Date[2]:**	04/15/23
Dividend Yield:	3.6%	**5 Year Price Target**	$179	**Years Of Dividend Growth:**	12
Dividend Risk Score:	D	**Retirement Suitability Score:**	D	**Rating:**	Hold

Overview & Current Events

Packaging Corporation of America (PKG) is a manufacturer of packaging products, including containerboard and corrugated packaging products used to protect goods during the shipping process. The company also makes products for the agricultural products industry and multi-color boxes and displays. PKG manufactures nearly 5.0 million tons of containerboard annually. Most of the containerboard is converted into corrugated boxes, and it ships about 65.7 billion square feet of corrugated products annually.

The company operates three segments: packaging, paper, and corporate / other. The packaging segment accounts for the vast majority (92%) of sales. The paper segment accounts for 7% of sales and includes office paper, printing paper, and converting paper, with paper mills in Jackson, AL and International Falls, MN. The remainder of sales is generated from Corporate and Other.

Packaging Corporation of America operates nearly 100 manufacturing plants throughout the U.S. The company was founded in 1867 in Quincy, Illinois and has a current market capitalization of $13 billion.

On January 25th, 2023, Packaging Corporation of America reported fourth quarter and full year 2022 results for the period ending December 31st, 2022. For the quarter, adjusted diluted earnings-per-share equaled $2.38, down from $2.76 in the prior year quarter. The decrease was due to lower volumes in the Packaging and Paper segments, as well as increased operating costs, and higher freight and logistics expenses.

Sales for the quarter were $1.98 billion, down from $2.04 billion in the prior year. PKG generated $408.7 million in EBITDA, with the Packaging segment contributing $392.2 million, the Paper segment contributing $39.4 million and the Corporate segment with -$22.9 million.

We are entering 2023 with an initial EPS estimate of $9.17 for the year.

Growth on a Per-Share Basis

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
EPS	$3.28	$3.99	$4.47	$4.75	$5.78	$7.79	$7.34	$5.78	$9.39	$11.14	***$9.17***	***$11.16***
DPS	$1.51	$1.60	$2.20	$2.36	$2.52	$3.00	$3.16	$3.37	$4.00	$4.75	***$5.00***	***$6.38***
Shares[3]	98.17	98.37	96.13	94.21	94.35	94.50	94.66	94.83	93.53	90.90	***90.00***	***88.00***

Earnings-per-share have grown rapidly over the last ten years at an average annual rate of 14.6%. In the last five years, Packaging Corporation of America increased earnings-per-share by an average growth rate of 3.3%. From here on out, earnings-per-share still appear to be elevated, and we expect a more sustainable 4.0% intermediate-term growth rate, as it should grow alongside GDP more broadly. This still does leave upside potential if we continue to see robust demand and the ability to increase prices in the future, as was seen in 2022. The company has also been actively repurchasing shares, reducing the outstanding count by nearly 1% per year since 2013, which will help boost the bottom line on a per-share basis.

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[1] Estimate based on last year's date

[2] Estimate based on last year's date

[3] In millions.

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Valuation Analysis

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	Now	2028
Avg. P/E	15.6	17.3	15.7	14.7	18.1	14.2	13.8	18.2	16.5	13.6	***15.1***	***16.0***
Avg. Yld.	3.00%	2.30%	3.10%	3.40%	2.40%	2.70%	3.10%	3.20%	3.20%	2.90%	***3.6%***	***3.6%***

PKG has traded at an average P/E ratio near 16 over the past 10 years, which captures performance through periods of stagnation and growth. We are using 16.0 times earnings as a fair value baseline. With shares presently trading at 15.1 times expected earnings, this implies the potential for a valuation tailwind.

PKG has a long history of paying a quarterly dividend dating back to 2003, and the dividend has grown gradually since 2009, albeit with some periods where the payment has been flat for more than 4 quarters. PKG most recently increased its quarterly dividend from $1.00 to $1.25 as of May 18th, 2022, an impressive 25% increase.

Safety, Quality, Competitive Advantage, & Recession Resiliency

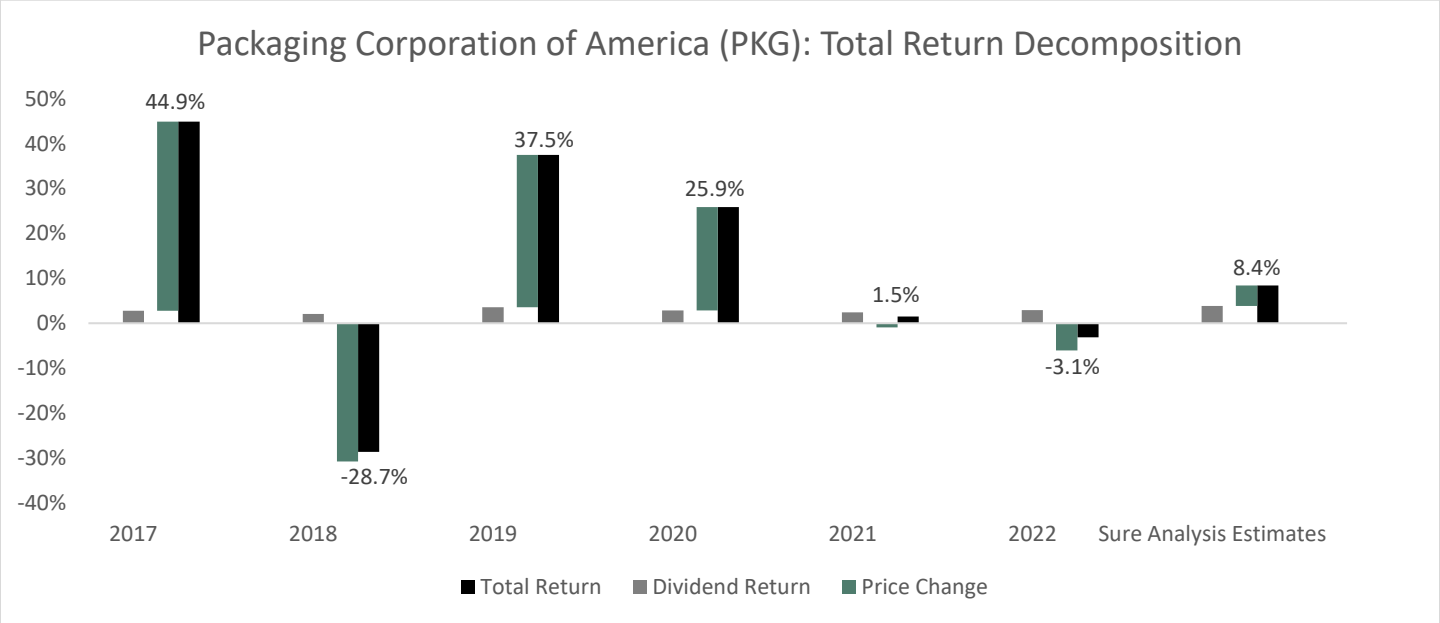
Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
Payout	46%	40%	49%	50%	44%	39%	43%	58%	43%	43%	***55%***	***57%***

PKG has maintained a fairly safe dividend payout ratio between 40-60%. It operates in the packaging industry which has secular tailwinds supporting it along with significant scale. Risks to the business include operating in a competitive industry with several similarly sized competitors such as International Paper, Westrock, and Sonoco Products. There are modest barriers to entry in the cardboard industry due to the large capital requirements to build manufacturing plants and scale across the country. We expect the dividend to continue to be protected at current levels given the strong growth the company has shown over the past decade and optimistic commentary from the CEO.

Final Thoughts & Recommendation

Packaging Corporation of America has put together a solid earnings and dividend record in the last decade. Total projected returns come in at 8.4% annually, driven by a 3.6% dividend yield, 4.0% earnings-per-share growth rate and the potential for a valuation tailwind. We are downgrading shares from buy to hold on lower total return expectations.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Revenue	3,665	5,853	5,742	5,779	6,445	7,015	6,964	6,658	7,730	8478
Gross Profit	868	1,230	1,208	1,276	1,471	1,645	1,644	1,369	1,873	2,090
Gross Margin	23.7%	21.0%	21.0%	22.1%	22.8%	23.5%	23.6%	20.6%	24.2%	24.7%
SG&A Exp.	327	470	451	469	520	536	558	540	577	608.6
Operating Profit	541	760	760	808	951	1,109	1,086	830	1,296	1,482
Op. Margin	14.8%	13.0%	13.2%	14.0%	14.8%	15.8%	15.6%	12.5%	16.8%	17.5%
Net Profit	441	393	437	450	669	738	696	461	841	1,029
Net Margin	12.0%	6.7%	7.6%	7.8%	10.4%	10.5%	10.0%	6.9%	10.9%	12.1%
Free Cash Flow	374	316	454	533	513	629	808	612	489	
Income Tax	(18)	222	228	239	160	233	221	172	268	335

Balance Sheet Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Total Assets	5,244	5,273	5,272	5,777	6,198	6,570	7,236	7,433	7,837	
Cash & Equivalents	191	125	184	239	217	362	680	975	619	
Acc. Receivable	643	646	637	689	831	902	846	832	1,071	
Inventories	594	665	677	724	763	796	794	788	903	
Goodwill & Int.	837	840	815	1,105	1,293	1,296	1,258	1,159	1,232	
Total Liabilities	3,887	3,751	3,639	4,017	4,015	3,897	4,165	4,187	4,230	
Accounts Payable	358	331	294	324	403	382	352	387	452	
Long-Term Debt	2,548	2,355	2,297	2,646	2,630	2,484	2,477	2,479	2,472	
Total Equity	1,357	1,521	1,633	1,760	2,183	2,672	3,071	3,246	3,607	
LTD/E Ratio	1.88	1.55	1.41	1.50	1.21	0.93	0.81	0.76	0.69	

Profitability & Per Share Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Return on Assets	11.5%	7.5%	8.3%	8.1%	11.2%	11.6%	10.1%	6.3%	11.0%	
Return on Equity	37.9%	27.3%	27.7%	26.5%	33.9%	30.4%	24.3%	14.6%	24.5%	
ROIC	15.6%	10.1%	11.2%	10.8%	14.5%	14.8%	13.0%	8.2%	14.3%	
Shares Out.	98.2	98.4	96.1	94.2	94.4	94.5	94.7	94.8	93.5	92.9
Revenue/Share	37.59	60.27	59.38	61.68	68.78	74.70	74.01	70.53	81.80	91.22
FCF/Share	3.83	3.25	4.70	5.68	5.48	6.70	8.59	6.48	5.17	

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

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