WestRock Co. (WRK)

Updated February 3rd, 2023 by Aristofanis Papadatos

Key Metrics

Current Price:	$35	**5 Year CAGR Estimate:**	9.1%	**Market Cap:**	$8.7 B
Fair Value Price:	$34	**5 Year Growth Estimate:**	7.0%	**Ex-Dividend Date:**	2/9/2023
% Fair Value:	104%	**5 Year Valuation Multiple Estimate:**	-0.8%	**Dividend Payment Date:**	2/22/2023
Dividend Yield:	3.1%	**5 Year Price Target**	$47	**Years Of Dividend Growth:**	2
Dividend Risk Score:	D	**Retirement Suitability Score:**	D	**Rating:**	Hold

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 $8.7 billion. In its fiscal 2022, which ended on 9/30/2022, the corrugated packaging segment, the consumer packaging segment, global paper and distribution generated 39%, 23%, 35% and 3% of its pre-tax income, respectively.

On December1st, 2022, WestRock acquired the remaining 67.7% stake in Gondi, a leading producer of corrugated and consumer packaging in Mexico. The deal cost $970 million. The acquisitions of KapStone in 2018 and Gondi have greatly enhanced the product offerings and the geographical presence of WestRock, which can now grow in the attractive Latin American market.

In early February, WestRock reported (2/1/23) financial results for the first quarter of fiscal 2023. The company posted a -1% decrease in its sales and a 15% decrease in its adjusted earnings-per-share over the prior year's quarter, from $0.65 to $0.55, thus missing the analysts' consensus by $0.05. The poor performance was caused by high cost inflation, lower volumes due to price hikes as well as high maintenance and restructuring costs. Before this quarter, WestRock had missed the analysts' consensus in only 3 of the last 30 quarters. Due to strong business headwinds, WestRock stated that it cannot provide guidance for 2023. The stock plunged -13% on the news. Due to the poor business momentum, we have lowered our forecast for earnings-per-share from $3.90 to $3.05.

Growth on a Per-Share Basis

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
EPS	---	---	$3.89	$2.53	$2.62	$4.08	$3.98	$2.74	$3.39	$4.76	***$3.05***	***$4.28***
DPS	---	---	$0.38	$1.50	$1.60	$1.72	$1.82	$1.07	$0.93	$1.03	***$1.10***	***$1.62***
Shares[1]	---	---	257.0	251.0	254.5	259.2	259.0	260.0	268.9	256.4	***254.0***	***250.0***

WestRock has a short and volatile historical record. Since its foundation in its current form, it 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 concerns over a surge in the global supply of containerboard products in upcoming years. This factor, which is out of WestRock's control, may adversely affect its margins. Moreover, the company is currently hurt by excessive cost inflation. However, we view this headwind as temporary and expect WestRock to benefit from the growing North American corrugated market in the long run. Given the low comparison base formed by the disappointing earnings-per-share expected this year, we expect WestRock to grow its earnings-per-share by 7% per year on average over the next five years.

Valuation Analysis

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	Now	2028
Avg. P/E	---	---	15.2	16.8	20.3	14.9	9.8	12.3	14.3	9.4	***11.5***	***11.0***
Avg. Yld.	---	---	0.6%	3.5%	3.0%	2.8%	4.7%	3.2%	1.9%	2.3%	***3.1%***	***3.4%***

[1] In millions.

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WestRock is trading at a price-to-earnings ratio of 11.5, which is lower than its 8-year average of 14.1. Due to its short historical record and its cyclical business, the stock warrants a reduced valuation. We assume a fair price-to-earnings ratio of 11.0 for the stock. If the stock trades at our fair valuation level in five years, it will incur a -0.8% annualized drag in its returns.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
Payout	---	---	9.8%	59.3%	61.1%	42.2%	45.7%	39.1%	27.4%	21.6%	***36.1%***	***37.8%***

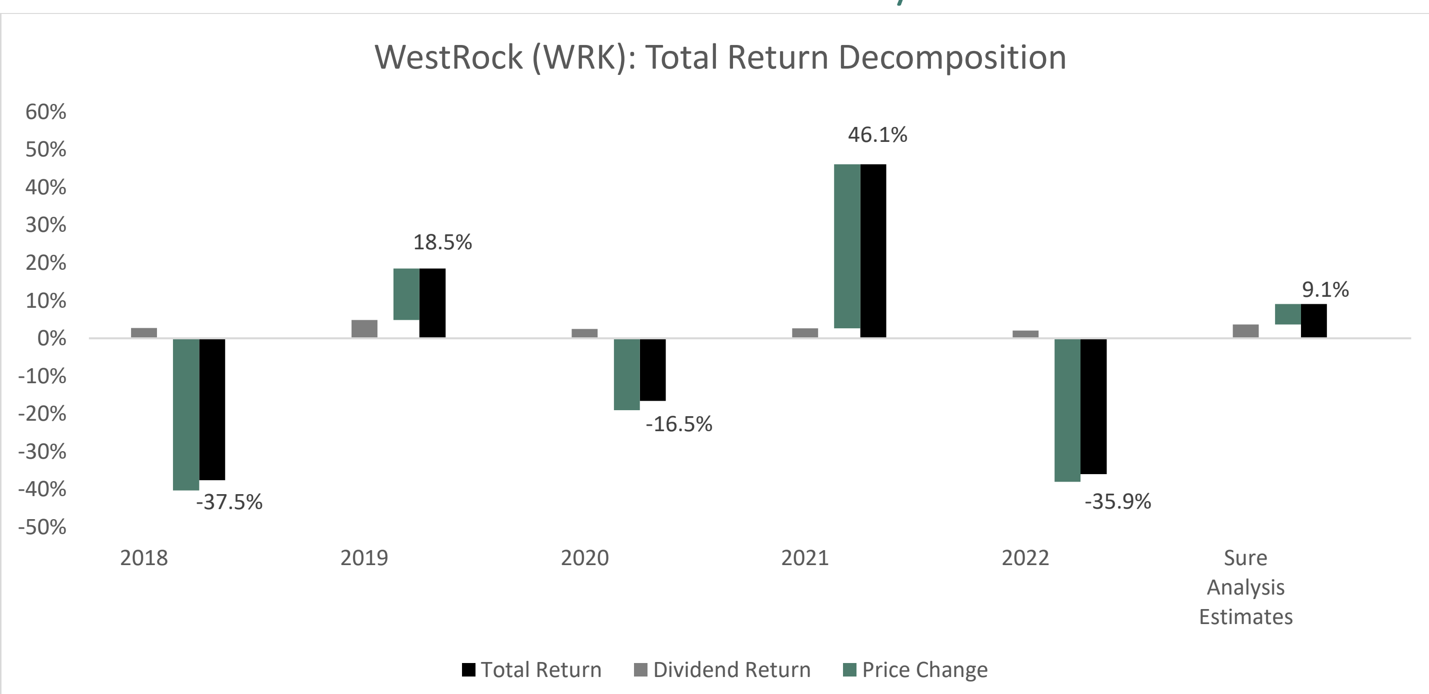
WestRock cannot control the total supply of paper products. As a result, it is vulnerable to the total production volume of its competitors. The business of WestRock is highly cyclical and hence investors should be especially careful before initiating a position in the stock. If they invest near the 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 material debt load that has resulted from the acquisitions of KapStone and Gondi, WestRock will be somewhat vulnerable whenever the next downturn in its business shows up. Its interest expense consumes 19% of operating income while its net debt of $15.7 billion is about 20 times its annual earnings and hence it is high. The weak balance sheet of the company helps explain the -57% dividend cut in 2020 amid the pandemic, despite a solid payout ratio of 66% before the dividend cut.

Final Thoughts & Recommendation

WestRock has recovered from the pandemic but it is now facing strong headwinds due to high cost inflation and a global economic slowdown. We view these headwinds as temporary and expect the stock to offer a 9.1% average annual return over the next five years thanks to 7.0% growth of earnings-per-share and a 3.1% dividend, partly offset by a -0.8% annualized contraction of the valuation level. The stock earns a hold rating. If it corrects further, to the low $30s, it will earn a buy rating.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Revenue	9545.4	9895.1	11125	14172	14860	16285	18,289	17,579	18,746	21,257
Gross Profit	1846.5	1933.6	2138.3	2758.6	2740.2	3393.9	3,749	3,197	3,430	4,021
Gross Margin	19.3%	19.5%	19.2%	19.5%	18.4%	20.8%	20.5%	18.2%	18.3%	18.9%
SG&A Exp.	869	938	1,026	1,750	1,457	1,731	1,709	1,623	1,759	1,933
Operating Profit	892	910	993	797	1,031	1,335	1,640	1,173	1,314	1,738
Op. Margin	9.3%	9.2%	8.9%	5.6%	6.9%	8.2%	9.0%	6.7%	7.0%	8.2%
Net Profit	727	480	507	(396)	708	1,906	863	(691)	838	945
Net Margin	7.6%	4.8%	4.6%	-2.8%	4.8%	11.7%	4.7%	-3.9%	4.5%	4.5%
Free Cash Flow	592	618	618	892	685	931	941	1,093	1,464	1,158
Income Tax	(22)	287	233	90	159	(875)	277	164	243	270

Balance Sheet Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Total Assets	10,733	11,040	25,372	23,038	25,089	25,361	30,157	28,780	29,254	28,406
Cash & Equivalents	36	33	208	341	298	637	152	251	291	260
Accounts Receivable	1,135	1,119	1,575	1,592	1,887	2,011	2,193	2,143	2,587	2,684
Inventories	938	1,029	1,761	1,638	1,797	1,830	2,108	2,023	2,173	2,317
Goodwill & Int. Ass.	2,562	2,618	7,442	7,377	8,858	8,700	11,345	9,629	9,278	8,816
Total Liabilities	6,421	6,732	13,589	13,208	14,703	13,878	18,473	18,132	17,564	16,980
Accounts Payable	802	813	1,231	1,054	1,492	1,717	1,832	1,674	2,124	2,252
Long-Term Debt	2,845	2,985	5,622	5,789	6,555	6,415	10,063	9,431	8,194	7,787
Shareholder's Equity	4,312	4,307	11,652	9,729	10,343	11,469	11,670	10,631	11,670	11,402
D/E Ratio	0.66	0.69	0.48	0.60	0.63	0.56	0.86	0.89	0.70	0.68

Profitability & Per Share Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Return on Assets	6.8%	4.4%	2.8%	-1.6%	2.9%	7.6%	3.1%	-2.3%	2.9%	3.3%
Return on Equity	18.8%	11.1%	6.4%	-3.7%	7.1%	17.5%	7.5%	-6.2%	7.5%	8.2%
ROIC	10.4%	6.6%	4.1%	-2.4%	4.4%	10.9%	4.4%	-3.3%	4.2%	4.8%
Shares Out.	---	---	257.0	251.0	254.5	259.2	259.0	260.0	268.9	261.5
Revenue/Share	65.33	67.77	64.19	54.95	58.11	62.68	70.59	67.82	70.08	81.29
FCF/Share	4.05	4.23	3.57	3.46	2.68	3.58	3.63	4.22	5.47	4.43

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