



The Scotts Miracle-Gro Company (SMG)

Updated November 3rd, 2023 by Nikolaos Sismanis

Key Metrics

Current Price:	\$53	5 Year CAGR Estimate:	10.9%	Market Cap:	\$2.95 B
Fair Value Price:	\$35	5 Year Growth Estimate:	16.0%	Ex-Dividend Date:	11/24/23
% Fair Value:	150%	5 Year Valuation Multiple Estimate:	-7.7%	Dividend Payment Date:	12/08/23
Dividend Yield:	5.0%	5 Year Price Target	\$74	Years Of Dividend Growth:	N/A
Dividend Risk Score:	F	Retirement Suitability Score:	D	Rating:	Buy

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 \$3.9 billion in annual revenue and is headquartered in Marysville, Ohio.

On November 1st, 2023, Scotts Miracle-Gro reported its Q4-2023 and full-year results for the period ending September 30th, 2023, with numbers remaining rather underwhelming. The company recorded sales of \$374.5 million during the quarter, a 24.1% decline compared to Q4-2022, primarily driven by a 35% sales decline in the Hawthorne division, further compounded by a 3% decline in the sales of the U.S. Consumer division. The decline in Hawthorne's sales reflected the continued challenges in the hydroponic industry.

The company is currently being pressured by higher commodity prices that have led to a significant margin decline despite multiple pricing actions. Consequently, it posted an adjusted loss-per-share of \$2.77 compared to an adjusted loss-per-share of \$2.04 in the same period of last year. For the year, GAAP losses per share landed at \$6.79.

Moving into fiscal 2024, management expects an improvement in the company's growth margin combined with tight control of SG&A, which should result in an operating income margin between 10.5% and 11%. Below the operating line, interest expenses are expected to be essentially flat year-over-year as higher borrowing costs should be offset by the debt pay-down that will take place in Q4.

Our updated estimates point toward adjusted earnings-per-share of \$2.70. Note that excluding this year's forecast, which indicates an adjusted figure, all other earnings-per-share figures in the table below depict GAAP metrics.

Growth on a Per-Share Basis

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2029
EPS	\$2.70	\$2.62	\$5.16	\$3.68	\$1.13	\$8.30	\$6.96	\$9.2	-\$7.88	-\$6.79	\$2.70	\$5.67
DPS	\$1.76	\$1.82	\$1.91	\$2.03	\$2.14	\$2.23	\$2.36	\$2.52	\$2.64	\$2.64	\$2.64	\$3.06
Shares	61.6	61.1	61.1	59.4	56.2	55.5	55.7	55.7	55.5	56.2	56.2	58.0

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 the company to focus on executing its Springboard strategy to cut costs and get the business back on track for profitable growth. Starting off of a low base for fiscal 2024, we expect earnings-per-share growth of 16%, estimating the company will gradually regain its lost ground. Assuming improvements in the bottom line go as planned, we expect acquisitions to resume as the industry remains highly fragmented.

Regarding the company's dividend, its 12-year dividend growth streak ended in fiscal 2023. We retain our DPS growth estimate at a rather modest 3%, though the dividend could remain stable until the company gets back on track.

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	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	Now	2029
Avg. P/E	22.2	25.0	17.1	26.1	---	12.0	11.9	19.1	---	---	19.4	13.0
Avg. Yld.	2.9%	2.8%	2.2%	2.1%	2.7%	2.2%	1.7%	1.4%	1.3%	4.0%	5.0%	4.2%

Over the past decade, Scotts Miracle-Gro's valuation has averaged around 19.1 times its underlying net income. Based on our projections for fiscal 2024, the P/E currently stands at 19.4. While this is a rich multiple, it reflects the market's expectations for a rapid earnings-per-share recovery over the medium-term. We have set our fair P/E at 13X adjusted EPS, expecting that the stock's valuation will normalize over time as its earnings hopefully rebound.

Safety, Quality, Competitive Advantage, & Recession Resiliency

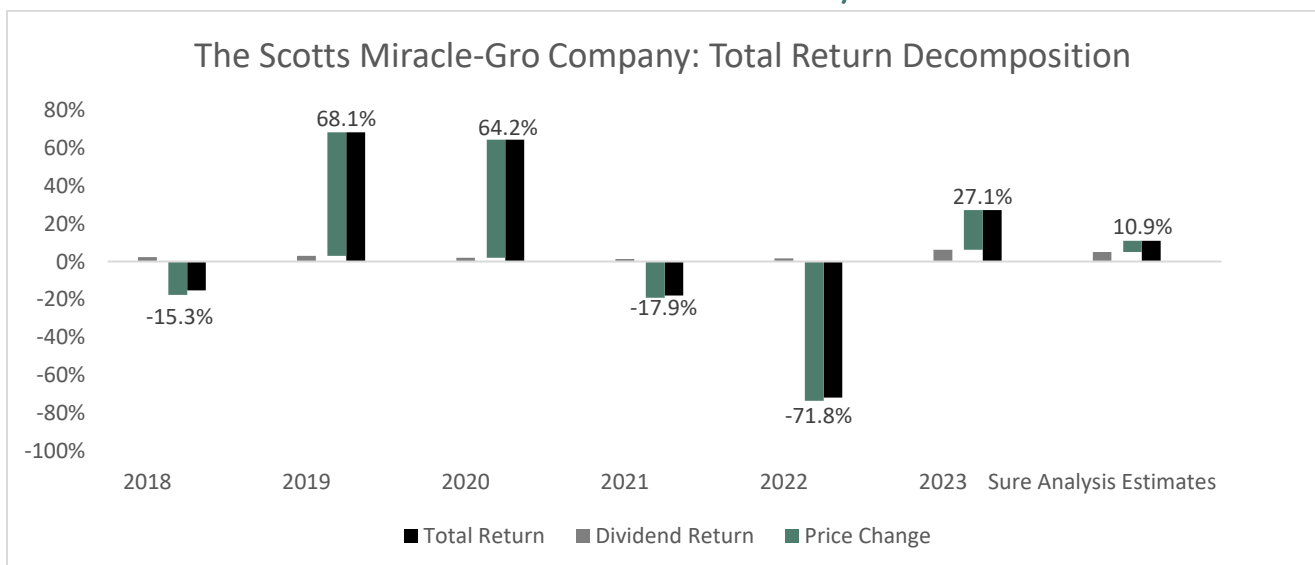
Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2029
Payout	65%	69%	37%	55%	189%	27%	34%	27%	---	---	98%	54%

Scotts Miracle-Gro's dividend should remain covered despite the recent challenges. The company has recovered rather swiftly from past hurdles, which should bolster investors' confidence in the stock. During the last recession, for instance, 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, unfavorable trading periods and industry trends can easily harm sales, as is the current situation. It's also 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 last-twelve-month long-term debt/equity ratio of nearly 2100%.

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. While the company's performance has been disastrous in recent years, we do expect gradual improvements. We forecast annualized returns of 10.9% over the medium-term, powered by a strong recovery in earnings-per-share, the 5.0% yield, and a 7.7% annual valuation adjustment. Shares earn a buy rating. We remind there are multiple risks to SMG's investment case, including ultra-thin margins and high indebtedness.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2015	2016	2017	2018	2019	2020	2021	2022
Revenue	2,371	2,506	2,642	2,663	3,156	4,132	4,925	3,924
Gross Profit	811	900	973	865	1,020	1,347	1,469	873
Gross Margin	34.2%	35.9%	36.8%	32.5%	32.3%	32.6%	29.8%	22.2%
SG&A Exp.	444	468	489	469	529	687	669	537
D&A Exp.	69	74	80	83	89	95	94	105
Operating Profit	326	393	422	325	418	585	726	259
Op. Margin	13.7%	15.7%	16.0%	12.2%	13.3%	14.2%	14.7%	6.6%
Net Profit	160	315	218	64	461	387	513	-438
Net Margin	6.7%	12.6%	8.3%	2.4%	14.6%	9.4%	10.4%	-11.2%
Free Cash Flow	(115)	186	294	274	184	495	165	-243
Income Tax	76	138	117	(12)	145	124	160	-121

Balance Sheet Metrics

Year	2015	2016	2017	2018	2019	2020	2021	2022
Total Assets	2,527	2,756	2,747	3,055	3,029	3,381	4,800	4,297
Cash & Equivalents	71	29	121	34	19	17	244	87
Acc. Receivable	158	127	198	226	224	475	483	299
Inventories	396	395	408	481	540	622	1,127	1,344
Goodwill & Int.	939	1,062	1,191	1,400	1,246	1,223	1,315	834
Total Liabilities	1,894	2,022	2,085	2,695	2,306	2,678	3,787	4,149
Accounts Payable	193	131	153	151	214	391	609	423
Long-Term Debt	1,158	1,216	1,401	2,016	1,652	1,522	2,294	2,970
Total Equity	621	715	649	355	719	697	1,013	148
LTD/E Ratio	1.87	1.70	2.16	5.69	2.30	2.18	2.26	20.11

Profitability & Per Share Metrics

Year	2015	2016	2017	2018	2019	2020	2021	2022
Return on Assets	7.0%	11.9%	7.9%	2.2%	15.1%	12.1%	12.5%	-9.6%
Return on Equity	27.2%	47.2%	32.0%	12.7%	85.8%	54.7%	59.9%	-75.4%
ROIC	10.2%	16.9%	10.9%	2.9%	19.4%	16.8%	18.5%	-13.6%
Shares Out.	61.1	61.1	59.4	56.2	55.5	55.7	55.7	55.5
Revenue/Share	38.12	40.42	43.89	46.64	56.06	72.61	88.42	70.70
FCF/Share	(1.85)	3.00	4.88	4.80	3.28	8.70	2.96	-4.37

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

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