

## Central Garden & Pet (CENT)

**\$37.23** (As of 09/24/20)

Price Target (6-12 Months): **\$43.00**

Long Term: 6-12 Months

**Zacks Recommendation:**

**Outperform**

(Since: 08/06/20)

Prior Recommendation: Neutral

Short Term: 1-3 Months

**Zacks Rank:** (1-5)

**1-Strong Buy**

Zacks Style Scores:

VGM:B

Value: B

Growth: A

Momentum: D

### Summary

Shares of Central Garden & Pet have outperformed the industry in the past three months. Much of the stock's momentum is driven by a sturdy third-quarter fiscal 2020, wherein top and bottom lines beat the Zacks Consensus Estimate and grew year over year. Results primarily benefited from strong organic growth across both segments and gains from the C&S acquisition. Margins were also robust in the quarter driven by improved overhead leverage and reduced promotional activity, mainly related to the pandemic. Management informed that fiscal fourth quarter generally attracts smaller earnings, which coupled with increased investments in the period, is likely to result in delivering a slight loss in the quarter. Nevertheless, it envisions earnings per share at or above \$1.90 for fiscal 2020, suggesting growth of nearly 18% year over year.

### Data Overview

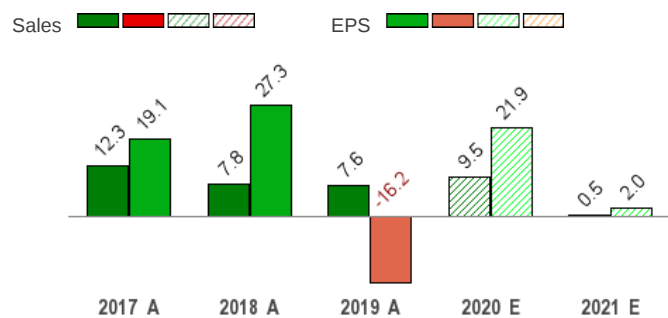
|                                |                                          |
|--------------------------------|------------------------------------------|
| 52-Week High-Low               | <b>\$44.80 - \$23.82</b>                 |
| 20-Day Average Volume (Shares) | <b>73,348</b>                            |
| Market Cap                     | <b>\$2.0 B</b>                           |
| Year-To-Date Price Change      | <b>19.8%</b>                             |
| Beta                           | <b>0.61</b>                              |
| Dividend / Dividend Yield      | <b>\$0.00 / 0.0%</b>                     |
| Industry                       | <b>Consumer Products - Discretionary</b> |
| Zacks Industry Rank            | <b>Top 15% (37 out of 250)</b>           |

|                               |                   |
|-------------------------------|-------------------|
| Last EPS Surprise             | <b>61.0%</b>      |
| Last Sales Surprise           | <b>14.5%</b>      |
| EPS F1 Estimate 4-Week Change | <b>0.0%</b>       |
| Expected Report Date          | <b>11/24/2020</b> |
| Earnings ESP                  | <b>0.0%</b>       |
| P/E TTM                       | <b>18.1</b>       |
| P/E F1                        | <b>19.1</b>       |
| PEG F1                        | <b>2.7</b>        |
| P/S TTM                       | <b>0.8</b>        |

### Price, Consensus & Surprise



### Sales and EPS Growth Rates (Y/Y %)



### Sales Estimates (millions of \$)

|      | Q1    | Q2    | Q3    | Q4    | Annual* |
|------|-------|-------|-------|-------|---------|
| 2021 | 500 E | 724 E | 767 E | 584 E | 2,622 E |
| 2020 | 483 A | 703 A | 833 A | 590 E | 2,610 E |
| 2019 | 462 A | 674 A | 707 A | 541 A | 2,383 A |

### EPS Estimates

|      | Q1        | Q2       | Q3       | Q4        | Annual*  |
|------|-----------|----------|----------|-----------|----------|
| 2021 | -\$0.08 E | \$0.85 E | \$0.93 E | \$0.18 E  | \$1.99 E |
| 2020 | -\$0.08 A | \$0.78 A | \$1.32 A | -\$0.06 E | \$1.95 E |
| 2019 | \$0.03 A  | \$0.72 A | \$0.80 A | \$0.04 A  | \$1.60 A |

\*Quarterly figures may not add up to annual.

The data in the charts and tables, including the Zacks Consensus EPS and Sales estimates, is as of 09/24/2020. The reports text is as of 09/25/2020.

## Overview

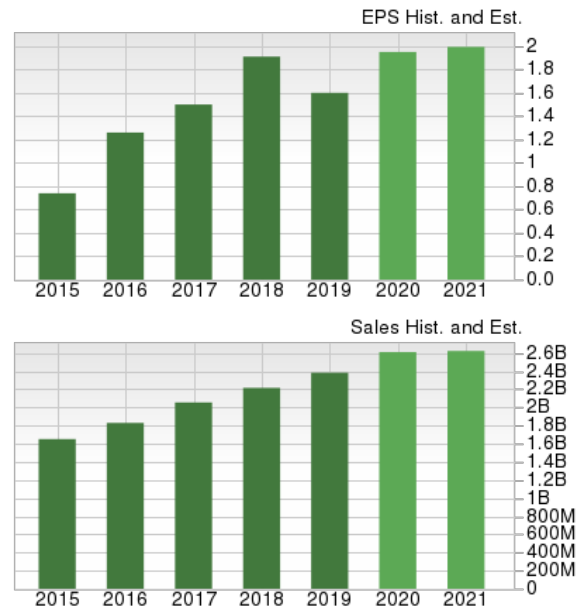
Committed to product innovation, Central Garden & Pet Co. is looking forward to strengthening its position as one of the leading companies in the U.S. pet supplies and lawn and garden supplies space. Unique packaging, point-of-sale displays, logistic capabilities and a high level of customer service are some of its key growth catalysts.

With such upsides, it boasts a wide repertoire of clients, including PetSmart, PETCO, Walmart, Home Depot and Lowe's. Further, the company actively engages in buyout activities to gain market share. In this regard, it acquired four new businesses in the last two years, including Arden and C&S.

Moving on, the company offers products to mass merchants, home improvement centers, lawn and garden nurseries, grocery stores, specialty pet stores, veterinarians' municipalities, and other individual animal buyers. It also produces both branded products and private-label products along with distributing third-party brands. With such a wide array of products in its portfolio, Central Garden & Pet operates under two segments as discussed below.

**Pet Segment** (58% of Fiscal 2019 total sales): This segment offers food and accessories for dogs, cats, birds, small animals, fishes, horses and livestock under brands, such as Adams, Aqueon, Avoderm, Cadet, Farnam, Four Paws, Kaytee, K&H Pet Products, Nylabone, Pinnacle, TFH, Zilla, Comfort Zone and Coralife.

**Garden Segment** (42% of Fiscal 2019 total sales): This segment offers both proprietary and nonproprietary grass seeds, herbicides, insecticides, pesticides, decorative outdoor lifestyle and lighting products. The segment markets its products under brands such as AMDRO, Ironite, Pennington, Sevin, Over-N-Out and The Rebels.



Source: Zacks Investment Research

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## Reasons To Buy:

▲ **Robust Q3 Performance Aids Stock:** We note that shares of Central Garden & Pet have gained 7.2% in the past three months, outperforming the industry's 15% decline. Much of this stock's momentum is driven by better-than-expected third-quarter fiscal 2020 results, wherein the top and bottom lines also improved on a year-over-year basis. Results primarily benefited from strong organic growth across segments as well as gains from recent acquisitions. Notably, adjusted earnings of \$1.32 per share rose substantially from 80 cents earned in the year-ago period. Strong sales growth as well as operating-margin expansion drove the bottom line. Operating margin expanded 290 basis points to 12.6%, primarily attributed to gross-margin expansion coupled with improved overhead leverage and reduced promotional activity, mainly related to the pandemic.

Central Garden & Pet's impressive third-quarter fiscal 2020 results gained from the acquisition of C&S and robust organic sales growth across both the company's segments.

Additionally, the company has been experiencing a sturdy top-line performance. In third-quarter fiscal 2020, sales increased 18%, following hikes of 4.4%, 4.5%, 7.7% and 7.4% in the preceding four quarters. While net sales at the Pet segment grew 18% on gains from the acquisition of C&S, the metric advanced 17.9% at the Garden segment. Robust portfolio strength, gains in garden distribution, controls and fertilizers, wild-bird feed, and grass seed aided the Garden unit. Driven by strong year-to-date performance and anticipated investments in the fiscal fourth quarter, earnings per share are envisioned at or above \$1.90 for fiscal 2020. This suggests growth of nearly 18% from the year-ago quarter's earnings of \$1.61. Management expects robust business momentum witnessed in fiscal third quarter to continue ahead.

▲ **Acquisitions Playing a Key Role:** Central Garden & Pet company has been a disciplined buyer in the garden and pet areas and has concluded more than 50 acquisitions since 1992. The company through buyouts also looks to enhance manufacturing capabilities, operating synergies, or developing distribution network. In the last two years, the company has bought four new businesses including entering into the live plant and outdoor seat cushion businesses. In this regard, Central Garden & Pet acquired C&S Products in May 2019, which has been complementing its existing wild bird feed business. This buyout has been boosting the company's top line. During the third quarter of fiscal 2020, acquisitions contributed about \$10 million of sales.

Prior to this, the company acquired the remaining 55% stake at Arden Companies in February 2019. Earlier, the company bought Bell Nursery, a leading grower and distributor of live flowers and plants in March 2018, while the same year in April, it acquired General Pet Supply, a supplier of pet food and supplies.

▲ **Financial Status:** Central Garden's cash and cash equivalents at the end of third-quarter fiscal 2020 was \$495.3 million, which rose 49.4% sequentially and is sufficient to fund its short-term obligations of \$31.7 million (includes current lease liabilities and current portion of long-term debt). As of Jun 27, 2020, the company's long-term debt (including operating lease liabilities) of \$765.4 million inched up 0.1% sequentially. However, its debt-to-capitalization of 0.42 shows a decline from 0.45 at the end of fiscal second quarter. Also, the company's times interest earned ratio of 4.2 as of Jun 27, 2020 has increased from 3.6 as of Mar 28. The times-interest-earned ratio is very important for some companies, as it measures a company's ability to meet its debt obligations based on its current income.

▲ **Healthy Commercial Relationship:** Being the leading producer of garden and pet supplies products in the U.S. with a diversified portfolio of brands has aided Central Garden & Pet in developing healthy commercial relationships with giant retailers such as PetSmart, PETCO, Walmart, Home Depot and Lowe's. We believe this provides the company significant opportunity to drive growth. Walmart, the company's largest customer, accounted about. Sales to Walmart represented approximately 28%, 29% and 31%, sales to Lowe's represented about 22%, 21% and 21%, and sales to Home Depot represented roughly 29%, 27% and 20% of Garden segment's net sales in fiscal 2019, 2018 and 2017, respectively.

Walmart, the company's largest customer, accounted about 16% of total company net sales in each of the fiscal years 2019, 2018 and 2017. Home Depot, the second largest customer, reflected approximately 12%, 11% and 8% of our total company net sales in fiscal 2019, 2018 and 2017, respectively. Moreover, other prominent customers include Lowe's, Costco and PetSmart, and together with Walmart and Home Depot, represented for approximately 49% of net sales in fiscal 2019, 48% in fiscal 2018 and 44% in fiscal 2017.

▲ **A Complete Metamorphosis:** Central Garden & Pet's effective inventory management is helping it to optimize merchandise levels in accordance with sales trends and is also facilitating in optimum utilization of its working capital. Further, the company intends to evolve into an integrated, multi-brand company by restructuring and reorganizing operating units and consolidating facilities. The company is steadily making strides in advancing its digital capabilities to focus on e-commerce and optimizing supply chain. The company is also expanding its data analytics capability to improve and accelerate business insight. Management revealed plans to lower cost of goods sold and administrative spending by 1-2% annually via cost-containment efforts.

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## Risks

- **Higher SG&A in Q3:** Although margins were robust in third-quarter fiscal 2020, the company's SG&A expense increased 5% year over year in the quarter. Various factors such as increased variable-compensation accruals and logistics costs along with inorganic spend from the C&S acquisition and PPE costs led to this increase in SG&A. Higher SG&A expense remains a deterrent to the company's profits.
- **Soft Q4 View:** Management informed that the fiscal fourth quarter generally attracts smaller earnings, which coupled with increased investments in the period, is likely to result in delivering a slight loss in fourth-quarter fiscal 2020. Central Garden & Pet delivered adjusted earnings of 4 cents in the same quarter a year ago.
- **Tough competition:** Central Garden & Pet operates in highly-competitive markets. It faces intense competition from regional and national firms on grounds of price, product quality, number of products offered, brand awareness and customer service. The company's growth and success depend on its ability to offer high-quality distinguished products at a competitive price.

In fact, the company's lawn and garden products compete against national and regional products and private label products produced by various suppliers. The company turf and forage grass seed products, fertilizers, pesticides and combination products compete primarily against products marketed by The Scotts Miracle-Gro Company ("Scotts"). Additionally, Spectrum Brands is a strong competitor in yard and household insecticides. The company's branded pet products compete against national and regional branded products and private label products produced by various suppliers. The company's largest competitors in the product categories are Spectrum Brands and Hartz Mountain. The segment's sales and logistics operations compete with Animal Supply Co., Phillips Pet Food & Supplies and a number of smaller local and regional distributors.

- **Seasonality of Garden Segment:** Gardening is generally limited to the period between spring to summer, which makes the garden business highly seasonal in nature. A major part of the sales occurs during the second and third fiscal quarters. Failure to perform during the season is likely to have a significant impact on the company's yearly financials. In fiscal 2019, approximately 69% of Garden segment's net sales and 58% of total net sales occurred during the second and third quarters.
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## Last Earnings Report

### Central Garden & Pet Beats Q3 Earnings & Sales

Central Garden & Pet reported better-than-expected results in third-quarter fiscal 2020, wherein both top and bottom lines improved on a year-over-year basis. Results primarily benefited from strong organic growth across segments as well as gains from recent acquisitions.

The company reported adjusted earnings of \$1.32 per share, substantially higher than 80 cents reported in the year-ago period. Moreover, the figure surpassed the Zacks Consensus Estimate of 82 cents.

The California-based company reported net sales of \$833.5 million, beating the Zacks Consensus Estimate of \$728 million. Further, the top line improved 18% from the year-ago period on organic gains in the Garden and Pet segments as well as contribution from the C&S acquisition. Total organic sales grew 16.5%.

Gross profit increased 19.5% to \$262.1 million, with gross margin expansion of 40 basis points (bps) to 31.4%.

Operating income was \$104.6 million, up 51.8% from the prior-year quarter, while operating margin expanded 290 bps to 12.6%. Operating margin growth was primarily attributed to gross margin expansion coupled with improved overhead leverage and reduced promotional activity, mainly related to the pandemic. SG&A expenses of \$157.4 million rose nearly 5% from the prior-year quarter.

### Segment in Detail

Net sales at the **Pet** segment grew 18% year over year to \$413.3 million, driven by the acquisition of C&S. Organic sales increased 15%, driven by strength in dog treats and chews, pet distribution, small animal food and supplies, and animal health categories. This was partly offset by weak live fish sales due to the exit of a major retailer in this category during fiscal 2019 as well as shipment and supply restrictions for live animals due to the COVID-19 outbreak.

The segment's operating income grew 44.8% year over year to \$50.8 million, backed by the C&S acquisition and organic sales growth. Operating margin expanded 230 basis points to 12.3%, while organic operating margin was up 220 bps to 12.2%.

At the **Garden** segment, net sales advanced 17.9% year over year to \$420.2 million, driven by robust portfolio strength, with gains in garden distribution, controls and fertilizers, wild bird feed, and grass seed. Organic sales for the segment improved 17.9%. The segment reported an operating income of \$77.8 million, up 46.5% from \$53.1 million in the year-ago quarter. Also, operating margin expanded 360 basis points to 18.5%.

### Financial Details

Central Garden & Pet ended the quarter with cash and cash equivalents of \$495.3 million and total debt of \$694 million compared with \$445.6 million and \$693.1 million, respectively, in the prior-year period. Shareholders' equity at the end of the quarter was \$1,059.4 million, excluding non-controlling interest.

Cash provided by operations during the quarter was \$181.6 million compared with \$172.1 million a year ago, driven by EBITDA gains, offset by changes in working capital mostly associated with robust demand trends in the reported quarter. Net interest expenses increased to \$11.5 million in the reported quarter, up from \$8.5 million in the prior-year period.

Moreover, the company bought back shares worth \$5.1 million during the fiscal third quarter. As of Jun 27, it had \$100 million remaining under its share repurchase program. Additionally, it has 600,000 shares remaining under the board's equity dilution authorization.

### Outlook

Driven by strong year-to-date performance and anticipated investments in the fiscal fourth quarter, the company projects earnings per share at or above \$1.90 for fiscal 2020. This suggests growth of nearly 18% from the year-ago quarter's earnings of \$1.61. However, the company informed that the fiscal fourth quarter generally attracts smaller earnings, which coupled with increased investments in the period, is likely to result in delivering a slight loss in fourth-quarter fiscal 2020.

Additionally, the company expects to provide its refreshed long-term strategy, called the Vision2025, at a virtual Investor Day to be held in conjunction with its fiscal 2020 earnings release in late November 2020.

| Quarter Ending   | 06/2020      |
|------------------|--------------|
| Report Date      | Aug 05, 2020 |
| Sales Surprise   | 14.54%       |
| EPS Surprise     | 60.98%       |
| Quarterly EPS    | 1.32         |
| Annual EPS (TTM) | 2.06         |

## Valuation

Central Garden & Pet Company shares are up 19.9% in the year-to-date period and 25.2% over the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Consumer Discretionary sector are down 10.8% and 4.9%, respectively, in the year-to-date period. Over the past year, the Zacks sub-industry is down 9.3% but the sector is 5.1%.

The S&P 500 index is up 0.8% in the year-to-date period and 9.4% in the past year.

The stock is currently trading at 18.68X forward 12-month earnings, which compares to 14.13X for the Zacks sub-industry, 31.99X for the Zacks sector and 21.31X for the S&P 500 index.

Over the past five years, the stock has traded as high as 26.29X and as low as 12.2X, with a 5-year median of 19.49X. Our Outperform recommendation indicates that the stock will perform better than the market. Our \$43 price target reflects 21.48X forward 12-month earnings.

The table below shows summary valuation data for CENT

| Valuation Multiples - CENT |               |       |              |        |         |
|----------------------------|---------------|-------|--------------|--------|---------|
|                            |               | Stock | Sub-Industry | Sector | S&P 500 |
| P/E F12M                   | Current       | 18.68 | 14.13        | 31.99  | 21.31   |
|                            | 5-Year High   | 26.29 | 26.7         | 34.65  | 23.44   |
|                            | 5-Year Low    | 12.2  | 10.31        | 16.13  | 15.26   |
|                            | 5-Year Median | 19.49 | 16.89        | 19.86  | 17.63   |
| P/S F12M                   | Current       | 0.78  | 1.09         | 2.36   | 3.95    |
|                            | 5-Year High   | 1.05  | 1.22         | 2.95   | 4.29    |
|                            | 5-Year Low    | 0.35  | 0.57         | 1.68   | 3.11    |
|                            | 5-Year Median | 0.77  | 0.92         | 2.47   | 3.66    |
| EV/EBITDA TTM              | Current       | 9.22  | 7.21         | 11.01  | 14      |
|                            | 5-Year High   | 14.99 | 23.03        | 17.8   | 15.61   |
|                            | 5-Year Low    | 6.87  | 5.03         | 8.29   | 9.51    |
|                            | 5-Year Median | 10.01 | 11.83        | 12.21  | 13.03   |

As of 09/24/2020

Source: Zacks Investment Research

## Industry Analysis Zacks Industry Rank: Top 15% (37 out of 250)



Source: Zacks Investment Research

## Top Peers

| Company (Ticker)                                             | Rec          | Rank |
|--------------------------------------------------------------|--------------|------|
| Prestige Consumer Healthcare Inc. (PBH)                      | Outperform   | 2    |
| Spectrum Brands Holdings Inc. (SPB)                          | Outperform   | 1    |
| Aphria Inc. (APHA)                                           | Neutral      | 3    |
| Chewy Inc. (CHWY)                                            | Neutral      | 3    |
| General Mills, Inc. (GIS)                                    | Neutral      | 3    |
| Hengan International Group Co., Ltd. Unsponsored ADR (HEGIY) | Neutral      | 2    |
| The J. M. Smucker Company (SJM)                              | Neutral      | 3    |
| Party City Holdco Inc. (PRTY)                                | Underperform | 4    |

The positions listed should not be deemed a recommendation to buy, hold or sell.

| Industry Comparison Industry: Consumer Products - Discretionary |            |            |           | Industry Peers |           |            |
|-----------------------------------------------------------------|------------|------------|-----------|----------------|-----------|------------|
|                                                                 | CENT       | X Industry | S&P 500   | CHWY           | GIS       | SPB        |
| Zacks Recommendation (Long Term)                                | Outperform | -          | -         | Neutral        | Neutral   | Outperform |
| Zacks Rank (Short Term)                                         | 1          | -          | -         | 3              | 3         | 1          |
| VGM Score                                                       | B          | -          | -         | B              | B         | C          |
| Market Cap                                                      | 2.04 B     | 254.48 M   | 22.77 B   | 22.35 B        | 35.89 B   | 2.46 B     |
| # of Analysts                                                   | 3          | 3          | 14        | 6              | 8         | 3          |
| Dividend Yield                                                  | 0.00%      | 0.00%      | 1.72%     | 0.00%          | 3.34%     | 2.94%      |
| Value Score                                                     | B          | -          | -         | F              | C         | D          |
| Cash/Price                                                      | 0.24       | 0.10       | 0.07      | 0.01           | 0.05      | 0.19       |
| EV/EBITDA                                                       | 10.36      | 8.52       | 12.78     | -100.10        | 12.30     | 12.61      |
| PEG F1                                                          | 2.66       | 2.74       | 2.82      | NA             | 2.19      | 0.86       |
| P/B                                                             | 1.92       | 1.77       | 3.12      | NA             | 4.10      | 1.77       |
| P/CF                                                            | 14.43      | 10.30      | 12.37     | NA             | 12.78     | 5.71       |
| P/E F1                                                          | 19.09      | 16.93      | 20.56     | NA             | 16.41     | 15.87      |
| P/S TTM                                                         | 0.80       | 0.67       | 2.34      | 3.78           | 1.99      | 0.65       |
| Earnings Yield                                                  | 5.24%      | 5.48%      | 4.60%     | -0.66%         | 6.10%     | 6.31%      |
| Debt/Equity                                                     | 0.65       | 0.54       | 0.70      | 0.00           | 1.24      | 1.93       |
| Cash Flow (\$/share)                                            | 2.58       | 0.72       | 6.93      | -0.55          | 4.59      | 9.99       |
| Growth Score                                                    | A          | -          | -         | A              | A         | C          |
| Historical EPS Growth (3-5 Years)                               | 15.07%     | 0.86%      | 10.41%    | NA             | 3.19%     | NA         |
| Projected EPS Growth (F1/F0)                                    | 21.88%     | 13.04%     | -4.56%    | -24.71%        | -0.90%    | 25.76%     |
| Current Cash Flow Growth                                        | -4.06%     | -4.06%     | 5.26%     | -5.57%         | 9.11%     | 64.31%     |
| Historical Cash Flow Growth (3-5 Years)                         | 21.71%     | 13.92%     | 8.49%     | NA             | 3.48%     | 16.24%     |
| Current Ratio                                                   | 3.81       | 1.55       | 1.35      | 0.61           | 0.70      | 2.08       |
| Debt/Capital                                                    | 39.56%     | 39.92%     | 42.92%    | NA             | 55.30%    | 65.90%     |
| Net Margin                                                      | 4.28%      | -1.51%     | 10.25%    | -3.74%         | 12.78%    | -1.86%     |
| Return on Equity                                                | 11.16%     | 1.26%      | 14.59%    | NA             | 28.46%    | 11.34%     |
| Sales/Assets                                                    | 1.19       | 0.99       | 0.50      | 5.82           | 0.59      | 0.74       |
| Projected Sales Growth (F1/F0)                                  | 9.52%      | 0.00%      | -1.44%    | 40.78%         | -0.53%    | 0.37%      |
| Momentum Score                                                  | D          | -          | -         | B              | D         | C          |
| Daily Price Change                                              | 2.73%      | 0.00%      | 0.21%     | -0.05%         | 1.70%     | 0.21%      |
| 1-Week Price Change                                             | -3.98%     | 0.00%      | 0.79%     | -1.51%         | -2.08%    | -3.43%     |
| 4-Week Price Change                                             | -10.85%    | -1.43%     | -5.64%    | -3.38%         | -9.29%    | -3.68%     |
| 12-Week Price Change                                            | 3.02%      | 0.53%      | 1.89%     | 16.74%         | -4.52%    | 22.99%     |
| 52-Week Price Change                                            | 25.18%     | -3.45%     | -2.71%    | 109.13%        | 6.75%     | 14.30%     |
| 20-Day Average Volume (Shares)                                  | 73,348     | 47,953     | 2,095,310 | 6,133,080      | 3,417,428 | 374,415    |
| EPS F1 Estimate 1-Week Change                                   | 0.00%      | 0.00%      | 0.00%     | 0.00%          | 1.45%     | 0.00%      |
| EPS F1 Estimate 4-Week Change                                   | 0.00%      | 0.00%      | 0.00%     | 27.42%         | 1.45%     | 0.28%      |
| EPS F1 Estimate 12-Week Change                                  | 20.87%     | 4.27%      | 4.08%     | 27.42%         | 2.21%     | 24.31%     |
| EPS Q1 Estimate Monthly Change                                  | 0.00%      | 0.00%      | 0.00%     | 20.00%         | -2.91%    | 0.85%      |

Source: Zacks Investment Research

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## Zacks Stock Rating System

We offer two rating systems that take into account investors' holding horizons: Zacks Rank and Zacks Recommendation. Each provides valuable insights into the future profitability of the stock and can be used separately or in combination with each other depending on your investment style.

### Zacks Recommendation

The Zacks Recommendation aims to predict performance over the next 6 to 12 months. The foundation for the quantitatively determined Zacks Recommendation is trends in the company's estimate revisions and earnings outlook. The Zacks Recommendation is broken down into 3 Levels; Outperform, Neutral and Underperform. Unlike many Wall Street firms, we maintain a balance between the number of Outperform and Neutral recommendations. Our team of 70 analysts are fully versed in the benefits of earnings estimate revisions and how that is harnessed through the Zacks quantitative rating system. But we have given our analysts the ability to override the Zacks Recommendation for the 1200 stocks that they follow. The reason for the analyst over-rides is that there are often factors such as valuation, industry conditions and management effectiveness that a trained investment professional can spot better than a quantitative model.

### Zacks Rank

The Zacks Rank is our short-term rating system that is most effective over the one- to three-month holding horizon. The underlying driver for the quantitatively-determined Zacks Rank is the same as the Zacks Recommendation, and reflects trends in earnings estimate revisions.

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### Zacks Style Scores

The Zacks Style Score is as a complementary indicator to the Zacks rating system, giving investors a way to focus on the highest rated stocks that best fit their own stock picking preferences.

Academic research has proven that stocks with the best Value, Growth and Momentum characteristics outperform the market. The Zacks Style Scores rate stocks on each of these individual styles and assigns a rating of A, B, C, D and F. We also produce the VGM Score (V for Value, G for Growth and M for Momentum), which combines the weighted average of the individual Style Scores into one score. This is perfectly suited for those who want their stocks to have the best scores across the board.

|                |          |
|----------------|----------|
| Value Score    | <b>B</b> |
| Growth Score   | <b>A</b> |
| Momentum Score | <b>D</b> |
| VGM Score      | <b>B</b> |

As an investor, you want to buy stocks with the highest probability of success. That means buying stocks with a Zacks Recommendation of Outperform, which also has a Style Score of an A or a B.

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## Disclosures

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## Glossary of Terms and Definitions

**52-Week High-Low:** The range of the highest and lowest prices at which a stock has traded during the past year. This range is determined based on the stock's daily closing price which may differ from the intra-day high or low. Many investors use it as a technical indicator to determine a stock's current value and future price movement. The idea here is that if price breaks out from the 52-week range, in either direction, the momentum may continue in the same direction.

**20-Day Average Volume (Shares):** The average number of shares of a company traded in a day over the last 20 days. It is a direct indication of a security's overall liquidity. The higher the average daily trading volume, the easier it is to enter or exit the stock at a desired price with more buyers and sellers being available.

**Daily Price Change:** This is the percentage difference between a trading day's closing price and the prior trading day's closing price. This item is updated at 9 p.m. EST each day.

**1-Week Price Change:** This is the percentage change in a stock's closing price over the last 5 trading days. This change reflects the collective buying and selling sentiment over the 1-week period.

A strong weekly price increase for the stock, especially when accompanied by increased volume, is an indication of it gaining momentum.

**4-Week Price Change:** This is the percentage change in a stock's closing price over the last 20 trading days or past 4 weeks. This is a medium-term price change metric and an indication of the stock gaining momentum.

**12-Week Price Change:** This is the percentage change of a stock's closing price over the last 60 trading days or past 12 weeks. Similar to 4-week price change, this is a medium-term price change metric. It shows whether a stock has been enjoying strong investor demand, or if it has been in consolidation, or distress over this period.

**52-Week Price Change:** This is the percentage change in a stock's closing price over the last 260 trading days or past 52 weeks. This long-term price change metric is a good reference point for investors. Some investors seek stocks with the best percentage price change over the last 52 weeks, expecting the momentum to continue.

**Market Cap:** The number of outstanding common shares of a company times its latest price per share. This figure represents a company's size, which indicates various characteristics, including price stability and risk, in which investors could be interested.

**Year-To-Date Price Change:** Change in a stock's daily closing price in the period of time beginning the first day of the current calendar year through to the previous trading day.

**# of Analysts:** Number of EPS estimates used in calculating the current-quarter consensus. These estimates come from the brokerage analysts tracking this stock. However, the number of such analysts tracking this stock may not match the number of estimates, as all brokerage analysts may not come up with an estimate or provide it to us.

**Beta:** A measure of risk commonly used to compare the volatility of a stock to the overall market. The S&P 500 Index is the base for calculating beta and carries a value of 1. A stock with beta below 1 is less risky than the market as a whole. And a stock with beta above 1 is riskier.

**Dividend:** The portion of earnings a company is expected to distribute to its common shareholders in the next 12 months for each share they own. Dividends are usually paid quarterly. Dividend payments reflect positively on a company and help maintain investors' trust. Investors typically find dividend-paying stocks appealing because the dividend adds to any market price appreciation to result in higher return on investment (ROI). Moreover, a steady or increasing dividend payment provides investors a cushion in a down market.

**Dividend Yield:** The ratio of a company's annual dividend to its share price. The annual dividend used in the ratio is calculated based on the most recent dividend paid by the company. Dividend yield is an estimate of the dividend-only return from a stock in the next 12 months. Since dividend itself doesn't change frequently, dividend yield usually changes with a stock's price movement. As a result, often an unusually high dividend yield is a result of weak stock price.

**S&P 500 Index:** The Standard & Poor's 500 (S&P 500) Index is an unmanaged group of securities considered to be representative of the stock market in general. It is a market-capitalization-weighted index of stocks of the 500 largest U.S. companies. Each stock's weight in the index is proportionate to its market value.

**Industry:** One of the 250+ groups that Zacks classifies all stocks into based on the nature of business. These groups are termed as expanded (aka "X") industries and map to their respective (economic) sectors; Zacks has 16 sectors.

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**Zacks Industry Rank:** The Zacks Industry Rank is determined by calculating the average Zacks Rank for all stocks in the industry and then assigning an ordinal rank to it. For example, an industry with an average Zacks Rank of 1.6 is better than an industry with an average Zacks Rank of 2.3. So, the industry with the better average Zacks Rank would get a better Zacks Industry Rank. If an industry has the best average Zacks Rank, it would be considered the top industry (1 out of 250+), which would place it at the top 1% of Zacks-ranked industries. Studies have shown that roughly half of a stock's price movement can be attributed to the industry group it belongs to. In fact, the top 50% of Zacks-ranked industries outperforms the bottom 50% by a factor of more than 2 to 1.

**Last EPS Surprise:** The percentage deviation of a company's last reported earnings per share from the Zacks Consensus Estimate. Companies with a positive earnings surprise are more likely to surprise again in the future (or miss again if they recently missed).

**Last Sales Surprise:** The percentage deviation of a company's last reported sales from the Zacks Consensus Estimate.

**Expected Report Date:** This is an estimated date of a company's next earnings release. The information originated or gathered by Zacks Investment Research from its information providers or publicly available sources is the basis of this estimate.

**Earnings ESP:** The Zacks Earnings ESP compares the Most Accurate Estimate to the Zacks Consensus Estimate for the yet-to-be reported quarter. The Most Accurate Estimate is the most recent version of the Zacks Consensus EPS Estimate. The idea here is that analysts revising their estimates closer to an earnings release have the latest information, which could potentially be more accurate than what they and others contributing to the consensus had predicted earlier. Thus, a positive or negative Earnings ESP reading theoretically indicates the likely deviation of the actual earnings from the consensus estimate. However, the model's predictive power is significant for positive ESP readings only. A positive Earnings ESP is a strong predictor of an earnings beat, particularly when combined with a Zacks Rank #1 (Strong Buy), #2 (Buy) or #3 (Hold). Our research shows that stocks with this combination produce a positive surprise nearly 70% of the time.

**Periods:**

**TTM:** Trailing 12 months. Using TTM figures is an effective way of analyzing the most-recent financial data in an annualized format that helps neutralize the effects of seasonality and other quarter-to-quarter variation.

**F1:** Current fiscal year. This period is used to analyze the estimates for the ongoing full fiscal year.

**F2:** Next fiscal year. This period is used to analyze the estimates for the next full fiscal year.

**F12M:** Forward 12 months. Using F12M figures is an effective way of analyzing the near-term (the following four unreported quarters) estimates in an annualized manner. Instead of typically representing estimates for the full fiscal year, which may not represent the nitty-gritty of each quarter, F12M figures suggest an all-inclusive annualized estimate for the following four quarters. The annualization helps neutralize the potential effects of seasonality and other quarter-to-quarter variations.

**P/E Ratio:** The price-to-earnings ratio measures a company's current market price per share relative to its earnings per share (EPS). Usually, the trailing-12-month (TTM) EPS, current-fiscal-year (F1) EPS estimate, or forward-12-month (F12M) EPS estimate is used as the denominator. In essence, this ratio shows what the market is willing to pay today for each dollar of EPS. In other words, this ratio gives a sense of what the relative value of the company is at the already reported level of earnings or at a future level of earnings.

It is one of the most widely-used multiples for determining the value of a company and helps comparing its valuation with that of a competitor, the industry group or a benchmark.

**PEG Ratio:** The price/earnings to growth ratio is a stock's P/E ratio using current fiscal year (F1) EPS estimate divided by its expected EPS growth rate over the coming 3 to 5 years. This ratio essentially determines a stock's value by factoring in the company's expected earnings growth and is thus believed to provide a more complete picture than just the P/E ratio, particularly for faster-growing companies.

**P/S Ratio:** The price-to-sales ratio is calculated as a company's current price per share divided by trailing 12 months (TTM) sales or revenues per share. This ratio shows what the market is willing to pay today for each dollar of TTM sales per share. The P/S ratio is at times the only valuation metric when the company has yet to become profitable.

**Cash/Price Ratio:** The cash-to-price ratio or Cash Yield is calculated as cash and marketable securities per share divided by the company's current share price. Like the earnings yield, which shows the anticipated yield (or return) on a stock from earnings for each dollar invested, the cash yield does the same, with cash being the source of return instead of earnings. For example, a cash/price ratio of 0.08 suggests a return of 8% or 8 cents for every \$1 investment.

**EV/EBITDA Ratio:** The EV/EBITDA ratio, also known as Enterprise Multiple, is calculated as a company's enterprise value (market capitalization + value of total long-term debt + book value of preferred shares - cash and marketable securities) divided by EBITDA (earnings before interest, taxes, depreciation and amortization). Usually, trailing-12-month (TTM) or forward-12-month (F12M) EBITDA is used as the denominator.

**EV/Sales Ratio:** The enterprise value-to-sales ratio is calculated as a company's enterprise value (market capitalization + value of total long-term debt + book value of preferred shares - cash and marketable securities) divided by annual sales. It is an expansion of the P/S valuation, which uses market value instead of enterprise value. The EV/Sales ratio is perceived as more accurate than P/S, in part, because the market capitalization does not take a company's debt into account when valuing it.

**EV/CF Ratio:** The enterprise value-to-cash flow ratio is calculated as a company's enterprise value (market capitalization + value of total long-term debt + book value of preferred shares - cash and marketable securities) divided by the trailing-12-month (TTM) operating cash flow. It's a measure of how long it would take to buy the entire business if you were able to use all the company's operating cash flow.

The EV/CF ratio is perceived as more accurate than the P/CF ratio, in part, because the market price does not take a company's debt into account when valuing it.

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**EV/FCF Ratio:** The enterprise value-to-free cash flow metric compares a company's enterprise value to its trailing-12-month (TTM) free cash flow (FCF). This metric is very similar to the EV/CF ratio, but is considered a more exact measure owing to the fact that it uses free cash flow, which subtracts capital expenditures (CAPEX) from a company's total operating cash flow, thereby reflecting the actual cash flow available for funding growth activities and payments to shareholders.

**P/EBITDA Ratio:** The P/EBITDA ratio is calculated as a company's per share market value divided by EBITDA (earnings before interest, taxes, depreciation, and amortization). This metric is very similar to the EV/EBITDA ratio, but is considered a little less exact measure as it uses market price, which does not take a company's debt into account. However, since EBITDA is often considered a proxy for cash income, the metric is used as a measure of what the market is willing to pay today for each dollar of the company's cash profitability in the trailing 12 months (TTM) or forward 12 months (F12M).

**P/B Ratio:** The price-to-book ratio is calculated as a company's current price per share divided by its book value (total assets – liabilities – preferred stocks) per share. In short, the book value is how much a company is worth. In other words, it reflects the total value of a company's assets that its common shareholders would receive if it were to be liquidated. So, the P/B ratio indicates whether you're paying higher or lower than what would remain if the company went bankrupt immediately. Investors typically use this metric to determine how a company's stock price stacks up to its intrinsic value.

**P/TB Ratio:** The price-to-tangible-book value ratio is calculated as a the per share market value of a company divided by the value of its tangible assets (total assets – liabilities – preferred stocks – intangible assets) per share. Tangible book value is the same thing as book value except it excludes the value of intangible assets to get a step closer to the baseline value of the company.

**P/CF Ratio:** The price-to-cash flow ratio measures a company's per share market price relative to its trailing-12-month (TTM) operating cash flow per share. This metric is used to determine whether a company is undervalued or overvalued relative to another stock, industry or sector. And like the P/E ratio, a lower number is typically considered better from the value perspective.

One of the reasons why P/CF ratio is often preferred over P/E ratio is the fact that operating cash flow adds back non-cash expenses such as depreciation and amortization to net income. This feature helps valuing stocks that have positive cash flow but are not profitable because of large noncash charges.

**P/FCF Ratio:** The price-to-free cash flow ratio is an extension of P/CF ratio, which uses trailing-12-month (TTM) free cash flow per share instead of operating cash flow per share. This metric is considered a more exact measure than P/CF ratio, as free cash flow subtracts capital expenditures (CAPEX) from a company's total operating cash flow, thereby reflecting the actual cash flow available for funding activities that generate additional revenues.

**Earnings Yield:** The earnings yield is calculated as current fiscal year (F1) EPS estimate divided by the company's current share price. The ratio, which is the inverse of the P/E ratio, measures the anticipated yield (or return) from earnings for each dollar invested in a stock today.

For example, earnings yield for a stock, which is trading at \$35 and expected to earn \$3 per share in the current fiscal year (F1), would be 0.0857 ( $3/35 = 0.0857$ ) or 8.57%. In other words, for \$1 invested in the stock today, the yield from earnings is anticipated to be 8.57 cents.

Investors most commonly compare the earnings yield of a stock to that of a broad market index (such as the S&P 500) and prevailing interest rates, such as the current 10-year Treasury yield. Since bonds and stocks compete for investors' dollars, stock investors typically demand a higher yield for the extra risk they assume compared to investors of U.S. Treasury-backed securities that offer virtually risk-free returns. This additional return is referred to as the risk premium.

**Debt/Equity Ratio:** The debt-to-equity ratio is calculated as a company's total liabilities divided by its shareholder equity. This metric is used to gauge a company's financial leverage. In other words, it is a measure of the degree to which a company is financing its operations through debt versus its own funds. The higher the ratio, the higher the risk for shareholders.

However, this ratio is difficult to compare across industry groups where ideal amounts of debt vary. Some businesses are more capital intensive than others and typically require higher debt to finance their operations. So, a company's debt-to-equity ratio should be compared with other companies in the same industry.

**Cash Flow (\$/share):** Cash flow per share is calculated as operating cash flow (after-tax earnings + depreciation + other non-cash charges) divided by common shares outstanding. It is used by many investors as a measure of a company's financial strength. Since cash flow per share takes into consideration a company's ability to generate cash by adding back non-cash expenses, it is regarded by some as a more accurate measure of a company's financial situation than earnings per share, which could be artificially deflated.

**Current Ratio:** The current ratio or liquidity ratio is a company's current assets divided by its current liabilities. It measures a company's ability to pay short-term obligations. A current ratio that is in line with the industry average or slightly higher is generally considered acceptable. A current ratio that is lower than the industry average would indicate a higher risk of distress or default. A higher number is usually better. However, a very high current ratio compared to the industry average could be an indication of inefficient use of assets by management.

**Debt/Capital Ratio:** Debt-to-capital ratio is a company's total debt (interest-bearing debt + both short- and long-term liabilities) divided its total capital (interest-bearing debt + shareholders' equity). It is a measure of a company's financial leverage. All else being equal, the higher the debt-to-capital ratio, the riskier the stock.

However, this ratio can vary widely from industry to industry, the ideal amount of required debt being different. Some businesses are more capital intensive than others and typically require higher debt to finance their operations. So, a company's debt-to-capital ratio should be compared with the same for its industry.

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**Net Margin:** Net margin is calculated as net income divided by sales. It shows how much of each dollar in sales generated by a company translates into profit. For example, if a company's net margin is 15%, its net income is 15 cents for every \$1 of sales it makes.

A change in margin can reflect either a change in business conditions, or a company's cost controls, or both. If a company's expenses are growing faster than sales, its net margin will decline. However, different net margin rates are considered good for different industries, so it's better to compare net margin rates of companies in the same industry group.

**Return on Equity:** Return on equity (ROE) is calculated as trailing-12-month net income divided by trailing-12-month average shareholder equity (including reinvested earnings). This metric is considered a measure of how effectively management is using a company's assets to generate profits. For example, if a company's ROE is 10%, it creates 10 cents profits for every \$1 shareholder equity, which is basically the company's assets minus debt. A company's ROE deemed good or bad depends on what's normal for its peers or industry group.

**Sales/Assets Ratio:** The sales-to-assets ratio or asset utilization ratio or asset turnover ratio is calculated as a company's annual sales divided by average assets (average of assets at the beginning of the year and at the year's end). This metric helps investors understand how effectively a company is using its assets to generate sales. For example, a sales-to-assets ratio of 2.5 indicates that the company generated \$2.50 in sales for every \$1 of assets on its books.

The higher the sales-to-assets ratio, the better the company is performing. However, similar to many other ratios, the asset turnover ratio tends to be higher for companies in certain industries/sectors than in others. So, a company's sales-to-assets ratio should be compared with the same for its industry/sector.

**Historical EPS Growth (3-5 Years):** This is the average annual (trailing-12-month) EPS growth rate over the last 3-5 years. This metric helps investors see how a company's EPS has grown from a long-term perspective.

Note: There are many factors that can influence short-term numbers — a recession will reduce this number, while a recovery will inflate it. The longterm perspective helps smooth out short-term events.

**Projected EPS Growth (F1/F0):** This is the estimated EPS growth rate for the current financial year. It is calculated as the consensus estimate for the current fiscal year (F1) divided by the reported EPS for the last completed fiscal year (F0).

**Current Cash Flow Growth:** It measures the latest year-over-year change in operating cash flow. Cash flow growth tells an investor how quickly a company is generating inflows of cash from operations. A positive change in the cash flow is desired and shows that more 'cash' is coming in than going out.

**Historical Cash Flow Growth (3-5 Years):** This is the annualized change in cash flow over the last 3-5 years. The change in a longer period helps put the current reading into proper perspective. By looking at the rate, rather than the actual dollar value, the comparison across the industry and peers becomes easier.

**Projected Sales Growth (F1/F0):** This metric looks at the estimated sales growth for the current year. It is calculated as sales estimate for the current fiscal year (F1) divided by the reported sales for the last completed fiscal year (F0).

Like EPS growth, a higher rate is better for sales growth. A look at a company's projected sales growth instantly tells you what the outlook is for their products and services. However, different sales growth rates are considered good for different industries, so it's better to compare sales growth rates of companies in the same industry group.

**EPS F1 Estimate 1-Week Change:** The percentage change in the Zacks Consensus EPS estimate for the current fiscal year over the past week. The change in a company's consensus EPS estimate (or earnings estimate revision) has proven to be strongly correlated with the near-term price movement of its shares. It is an integral part of the Zacks Rank.

If a stock's consensus EPS estimate is \$1.10 now versus \$1.00 a week ago, that will be reflected as a 10% upward revision. If, on the other hand, it went from \$1.00 to 90 cents, that would be a 10% downward revision.

**EPS F1 Estimate 4-Week Change:** The percentage change in the Zacks Consensus EPS estimate for the current fiscal year over the past four weeks.

A stock's earnings estimate revision in a 1-week period is important. But it's more meaningful to look at the longer-term revision. And, of course, the 4-week change helps put the 1-week change into proper perspective.

**EPS F1 Estimate 12-Week Change:** The percentage change in the Zacks Consensus EPS estimate for the current fiscal year over the past 12 weeks.

This metric essentially shows how the consensus EPS estimate has changed over a period longer than 1 week or 4 weeks.

**EPS Q1 Estimate Monthly Change:** The percentage change in the Zacks Consensus EPS estimate for the current fiscal quarter over the past four weeks.

While the revision in consensus EPS estimate for the current fiscal year is strongly correlated with the near-term price movement of its shares, the estimate revision for the current fiscal quarter is an important metric as well, especially over the short term, and particularly as a stock approaches its earnings date. If a stock's Q1 EPS estimate decreases ahead of its earnings release, it's usually a negative sign, whereas an increase is a positive sign.