

The Hershey Company(HSY)

\$129.45 (As of 06/19/20)

Price Target (6-12 Months): **\$136.00**

Long Term: 6-12 Months

Zacks Recommendation:

Neutral

(Since: 11/21/19)

Prior Recommendation: Outperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

3-Hold

Zacks Style Scores:

VGM:C

Value: D

Growth: C

Momentum: A

Summary

Hershey has outpaced the industry in the past three months. The company has been gaining from its efficient pricing strategy, which has been aiding its top line. Also, the company has been benefiting from prudent buyouts and focus on innovation. Markedly, buyouts and divestitures had a net favorable impact of 0.8 point on the top line in first-quarter 2020, thanks to the ONE Brands' acquisition. However, both top and bottom lines missed the consensus mark in the quarter. Management said that Hershey's first-quarter show was modestly affected by coronavirus, with the company's food service and travel retail businesses bearing adverse impacts. Overall, management pointed that retail traffic and takeaways have been uncertain due to increased social distancing. Apart from this, Hershey has been seeing higher advertising and marketing costs.

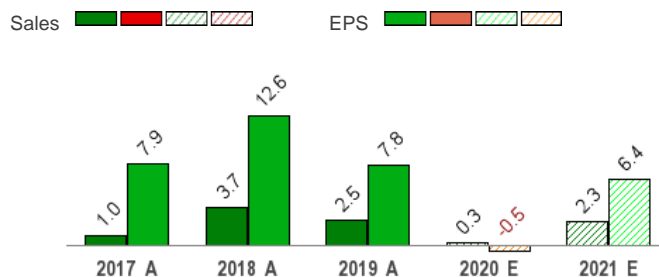
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$162.20 - \$109.88
20 Day Average Volume (sh)	1,247,082
Market Cap	\$26.9 B
YTD Price Change	-11.9%
Beta	0.17
Dividend / Div Yld	\$3.09 / 2.4%
Industry	Food - Confectionery
Zacks Industry Rank	Bottom 8% (231 out of 252)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	-4.1%
Last Sales Surprise	-2.1%
EPS F1 Est- 4 week change	-0.3%
Expected Report Date	07/23/2020
Earnings ESP	0.0%
P/E TTM	22.2
P/E F1	22.5
PEG F1	2.8
P/S TTM	3.4

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	2,089 E	1,806 E	2,200 E	2,110 E	8,192 E
2020	2,037 A	1,752 E	2,134 E	2,091 E	8,011 E
2019	2,016 A	1,767 A	2,134 A	2,068 A	7,986 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$1.76 E	\$1.33 E	\$1.77 E	\$1.39 E	\$6.12 E
2020	\$1.63 A	\$1.17 E	\$1.66 E	\$1.35 E	\$5.75 E
2019	\$1.59 A	\$1.31 A	\$1.61 A	\$1.28 A	\$5.78 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 06/19/2020. The reports text is as of 06/22/2020.

Overview

Founded in 1894 and based in Hershey, PA, **The Hershey Company** (HSY), is the largest chocolate manufacturer in North America as well as a global leader in chocolate and non-chocolate confectionery. In addition, Hershey manufactures pantry items like baking ingredients, toppings and beverages; and gum and mint refreshment products; snack bites and mixes, as well as spreads.

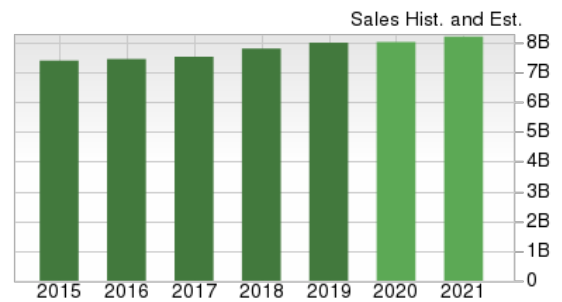
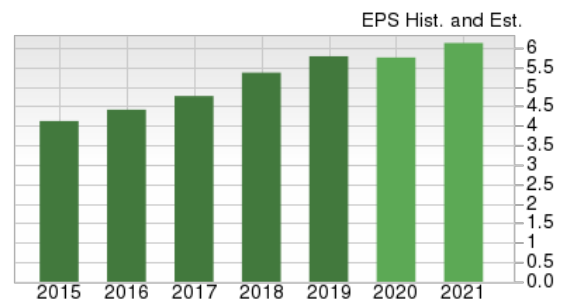
Hershey's operating segments comprise geographic regions — **North America** (contributed 88% to 2019 net sales) as well as **International and Other** (12%). International and Other segment includes operations in China, Mexico, Brazil, India and Malaysia, as well as export to markets in Asia, Latin America, Middle East, Europe, Africa and other regions).

The company's portfolio in North America includes a wide range of products, which are marketed and sold under brands like Hershey's, Reese's and Kisses, along with other popular chocolate and non-chocolate confectionery brands like Jolly Rancher, Almond Joy, Brookside, barkTHINS, Cadbury, Good & Plenty, Heath, Kit Kat, Lancaster, Payday, Rolo, Twizzlers, Whoppers and York.

In North America, the company also provides premium chocolates through Scharffen Berger and Dagoba brands. Further, it offers Ice Breakers mints and chewing gum, Breathsavers mints and Bubble Yum bubble gum as part of gum and mint products. Hershey's pantry and snack items include baking products, toppings and sundae syrups sold under the Hershey's, Reese's and Heath brands, as well as Hershey's and Reese's chocolate spreads, snack bites and mixes, Popwell half-popped corn snacks, baked and trans fat free Pirate's Booty snacks and other better-for-you snack brands such as Oatmega among others.

In the International and Other regions, Hershey produces and sells the same brands. It also provides other brands, which are marketed regionally. These include Pelon Pelo Rico confectionery products in Mexico, IO-IO snack products in Brazil, and Nutrino and Maha Lacto confectionery products and Jumpin and Sofit beverage products in India.

The company manufactures and markets several products through licensing agreements with Kraft Foods Ireland (York, Peter Paul Almond Joy and Peter Paul Mounds), Cadbury U.K. (Cadbury and Caramello) and Nestle (Kit-Kat and Rolo).



Reasons To Buy:

▲ **Gains From Buyouts:** Shares of Hershey have rallied 16.2% in the past three months, compared with the industry's gain of 15.1%. The company has been undertaking buyouts to augment portfolio strength as well as boost revenues. Buyouts and divestitures had a net favorable impact of 0.8 point on the top line, thanks to the acquisition of ONE Brands (concluded in September 2019). Prior to this, the company acquired Pirate Brands in September 2018 to bolster its snacking business. Additionally, the company has been gaining from Amplify Snack Brands, which was acquired in January 2018, to expand in the snacking category. In earlier developments, the acquisition of New York-based barkTHINS (April 2016) premium chocolate snacking brand has been aiding the company's better-for-you snacks portfolio. The SkinnyPop buyout has also been driving growth in the ready-to-eat popcorn category.

Hershey has been undertaking buyouts to augment portfolio strength as well as boost revenues. Also, the company regularly brings innovation to its core brands to meet consumer demand.

▲ **Strong Brand Portfolio & Focus on Innovation:** Hershey is the largest producer of quality chocolate products in the United States. It markets some of the world's leading brands which enjoy widespread consumer acceptance. The company is also a global leader in sugar confectionery products, which is attractive category as confectionery products are easily available, affordable and highly indulgent, thus making the industry almost recession resistant. Hershey's core brands — Hershey's, Reese's, Hershey's Kisses, Jolly Rancher, Brookside, Sofit and Ice Breakers — have been growing strongly on the back of advertising investments, in-store merchandising, and programming and innovation.

In fact, Hershey regularly brings innovation to its core brands to meet consumer demand and needs that are not addressed by its current portfolio. In this respect, its Kit Kat Duos innovation and expansion to THiNS platform are noteworthy. Further, the company relaunched the Take5 brand under the Reese's banner. The launch of Kisses brand in India is also reaping benefits. An important strategy of the company is to create a unique and holistic portfolio for every season, which can meet consumers' seasonal shopping needs.

▲ **Efforts to Boost Efficiency & Pricing Strategies:** Hershey focuses on optimizing its portfolio in order to deliver increased profitability. In this respect, the company's SKU rationalizing efforts have been fruitful. In addition, the company gained from its Margin for Growth multi-year program. This program is intended to improve overall operating margin through supply chain optimization, streamlining the operating model and reduction of administrative expenses. These moves are anticipated to boost efficiency, leverage global shared services and common processes and increase capacity utilization. Additionally, the company has undertaken strategic pricing initiatives to improve mix. Notably, price realization benefited Hershey's top line by 2.8 points in the quarter under review.

▲ **E-Commerce Growth:** Hershey has been undertaking efforts to enhance e-commerce capabilities. Over the past years, the company's e-commerce growth has accelerated considerably, given the increased number of consumers buying groceries online. Also, the company has witnessed similar trends in the confectionery category. Markedly, Hershey's overall e-commerce business more than doubled in March compared with 60% growth seen in January and February each. The company remains well placed to capitalize on such trends, courtesy of its solid investments in elevating the e-commerce platform.

▲ **Financial Position:** Hershey's long-term debt of \$3,453.5 million as of the end of the first quarter of 2020 (Mar 31, 2020) declined 2.2% from the previous quarter level. Further, Hershey's times interest earned ratio of 10.2 is better than the industry's 8.9. 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. Further, Hershey looks well placed on the dividend-payout front. The company recently declared dividend of 77.3 cents per share on common stock and 70.2 cents a share on Class B stock. Notably, the company has a dividend payout of 53%, dividend yield of 2.3% and free cash flow yield of 4.9%. With an annual free cash flow return on investment of 28.2%, ahead of the industry's 21.2%; the dividend payment is likely to be sustainable.

Reasons To Sell:

- ▼ **COVID-19 Hurts Q1 Results:** Hershey released first-quarter 2020 results, wherein both top and bottom lines missed the Zacks Consensus Estimate. Management said that Hershey's first-quarter show was modestly impacted by coronavirus. Incidentally, in the International and Other segment, soft volumes hurt sales by 7.2 points mainly owing to the coronavirus impact in China.

The company has temporarily closed its retail locations, including its Chocolate World Store in Hershey, Pennsylvania; Times Square, New York; and Las Vegas. While these locations generate a small proportion of sales, several months of closure is likely to adversely impact performance. Apart from this, the company's food service and travel retail businesses are bearing adverse impacts of coronavirus-led disruptions. Overall, management pointed that retail traffic and takeaways have been uncertain due to increased social distancing, which is the only way to contain the deadly virus spread.

Owing to the uncertainty surrounding the duration and harshness of the pandemic and the resultant consumer behavior, management withdrew its previously-issued guidance for 2020.

- ▼ **High Advertising, Marketing & Selling Costs:** The company has been seeing higher advertising and related consumer marketing expenses as well as soft operating margin for the past few quarters now. In the first quarter of 2020, advertising and related consumer marketing expenses rose 4.5% due to increased advertising spending in North America. Further, selling, marketing and administrative costs escalated 4.8% during the quarter. Consequently, adjusted operating margin declined 20 basis points to 23.1% as gains from improved gross margin were offset by increased advertising costs and elevated business investments. A persistent rise in such expenses is likely to dent the company's performance.
 - ▼ **Currency Headwinds:** Hershey remains exposed to volatile currency movements despite a low international presence. Markedly, currency had an adverse impact of 0.3 point on the company's top line in the first quarter of 2020.
 - ▼ **Lower International Presence:** Approximately 88% of the company's revenues was generated in North America (U.S. and Canada) in 2019. Markets outside this region form a lower proportion of the company's top-line. Though the company is accelerating investments in the overseas markets, competitors like Mondelez International have a stronger presence outside North America.
 - ▼ **Stiff Competition:** Hershey operates in highly competitive markets, along with several global multinational, national, regional and local firms. The company has some competitors, which are big entities with considerable resources and significant international operations. Well, Hershey competes on the basis of product innovation, product quality, price, efficacy of marketing and promotional strategies and the ability to cater to consumer preferences among other things. Of late, the company also witnessed heightened competition from other snack items, which in turn puts pressure on the confectionery category.
-

Last Earnings Report

Hershey's Q1 Earnings Lag Estimates, Guidance Withdrawn

Hershey reported first-quarter 2020 results. Adjusted earnings per share (EPS) of \$1.63 fell short of the Zacks Consensus Estimate of \$1.70, while it rose 2.5% year over year. The year-over-year upside can be attributed to higher sales and a lower tax rate.

Consolidated net sales of \$2,037.3 million rose 1% year over year, lagging the Zacks Consensus Estimate of \$2,080 million. Price realization drove sales by a 2.8 point. Buyouts and divestitures had a net favorable impact of 0.8 point on the top line, thanks to the acquisition of ONE Brands. However, currency translations and volumes had a negative impact of 0.3 and 2.3 points, respectively, on sales. Further, COVID-19 had a modest impact on net sales.

Quarter Ending **03/2020**

Report Date	Apr 23, 2020
Sales Surprise	-2.07%
EPS Surprise	-4.12%
Quarterly EPS	1.63
Annual EPS (TTM)	5.83

Margins in Detail

Adjusted gross margin expanded 90 bps to 46.6%, backed by net price realization as well as plant efficiencies stemming from actively building inventory to lower coronavirus-related risks.

Selling, marketing and administrative costs escalated 4.8% during the quarter. Advertising and related consumer marketing expenses rose 4.5% due to increased advertising spending in North America.

Adjusted operating profit amounted to \$471.5 million, up 0.2% from the prior-year quarter's figure. However, adjusted operating margin declined 20 basis points to 23.1% as gains from improved gross margin were offset by increased advertising costs and elevated business investments.

Segmental Update

North America (the United States and Canada) net sales improved 2.1% year over year to \$1,844.8 million. Markedly, price realization and net impact of acquisitions and divestitures boosted the unit's sales by 2.9 points and 0.9 point, respectively. However, volumes dented the unit by 1.7 points.

Net sales in the **International and Other** segment declined 8.1% to \$192.5 million. On a constant-currency or cc basis, net sales dropped 5.8%. Volumes hit sales by 7.2 points mainly owing to the coronavirus impact in China. This was somewhat compensated by a favorable net price realization of 1.4 points. Combined net sales in the company's focus markets, which include Mexico, Brazil, China and India, dropped nearly 13.1%. Excluding currency headwinds, combined organic sales from these markets decreased about 8.4%.

Financials

Hershey ended the quarter with cash and cash equivalents of nearly \$1,094.8 million, long-term debt of \$3,453.5 million and total shareholders' equity of \$1,674.5 million.

In a separate press release, Hershey declared quarterly a dividend payout of 77.3 cents per share for its common stock and 70.2 cents for Class B shares. These are payable on Jun 15 to shareholders of record as of May 22.

Recent News

Hershey to Make Face Masks Amid Coronavirus – Apr 24, 2020

Hershey informed that the company is pledging \$1 million to acquire and set up a new manufacturing line for the production of facemasks. The new line, operational toward the end of May will be capable of making up to 45,000 masks per day.

Hershey Temporarily Shuts 2 Locations Due to Coronavirus - Mar 15, 2020

The outbreak of the novel coronavirus Hershey to temporarily close its Chocolate World locations in Hershey, Pa., and Times Square, New York City. The shutdown, which is scheduled to last for two weeks, took effect from the closing time on Mar 15.

Though Hershey has not witnessed any confirmed coronavirus case among its workers, it made this decision as part of its precautionary and safety measures. The company's Chocolate World locations will continue to operate in Niagara, Canada and Las Vegas, as of now. Also, management did not talk about any impact of the aforementioned closure on its financial performance.

Valuation

Hershey's shares are down 11.9% in the year-to-date period and 5.8% over the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Consumer Staples sector are down 13.2% and 11.8% in the year-to-date period, respectively. Over the past year, the Zacks sub-industry and the sector declined 9% and 9.1%, respectively.

The S&P 500 index is down 3.8% in the year-to-date period and up 5.2% in the past year.

The stock is currently trading at 21.85X forward 12-month earnings, which compares to 19.95X for the Zacks sub-industry, 19.74X for the Zacks sector and 22.24X for the S&P 500 index.

Over the past five years, the stock has traded as high as 27.02X and as low as 16.46X, with a 5-year median of 21.2X. Our Neutral recommendation indicates that the stock will perform in line with the market. Our \$136 price target reflects 22.96X forward 12-month earnings.

The table below shows summary valuation data for HSY

Valuation Multiples - HSY					
		Stock	Sub-Industry	Sector	S&P 500
P/E F12M	Current	21.85	19.95	19.74	22.24
	5-Year High	27.02	24.52	22.37	22.24
	5-Year Low	16.46	15.67	16.65	15.23
	5-Year Median	21.2	18.19	19.66	17.49
P/S F12M	Current	3.33	2.19	9.54	3.47
	5-Year High	4.2	2.74	11.16	3.47
	5-Year Low	2.35	1.63	8.1	2.53
	5-Year Median	2.91	2.09	9.89	3.02
EV/EBITDA F12M	Current	15.26	11.64	34.16	12.28
	5-Year High	18.02	12.5	37.75	12.62
	5-Year Low	11.28	7.36	29.77	9.03
	5-Year Median	13.38	9.4	34.1	10.79

As of 06/19/2020

Industry Analysis Zacks Industry Rank: Bottom 8% (231 out of 252)



Top Peers

Company (Ticker)	Rec	Rank
Conagra Brands Inc. (CAG)	Neutral	3
Campbell Soup Company (CPB)	Neutral	3
General Mills, Inc. (GIS)	Neutral	3
Kellogg Company (K)	Neutral	3
Mondelez International, Inc. (MDLZ)	Neutral	3
TreeHouse Foods, Inc. (THS)	Neutral	3
HOSTESS BRANDS (TWNK)	Neutral	3
The Simply Good Foods Company (SMPL)	Underperform	5

Industry Comparison Industry: Food - Confectionery				Industry Peers		
	HSY	X Industry	S&P 500	MDLZ	SMPL	TWNK
Zacks Recommendation (Long Term)	Neutral	-	-	Neutral	Underperform	Neutral
Zacks Rank (Short Term)	3	-	-	3	5	3
VGM Score	C	-	-	D	D	C
Market Cap	26.93 B	2.02 B	21.51 B	75.32 B	1.69 B	1.61 B
# of Analysts	8	5	14	8	3	5
Dividend Yield	2.39%	0.00%	1.92%	2.17%	0.00%	0.00%
Value Score	D	-	-	D	C	C
Cash/Price	0.04	0.05	0.06	0.03	0.03	0.06
EV/EBITDA	15.18	17.74	12.62	17.61	26.08	14.77
PEG Ratio	2.84	2.94	2.90	3.16	NA	NA
Price/Book (P/B)	16.09	2.28	2.99	2.92	1.41	1.02
Price/Cash Flow (P/CF)	16.66	21.16	11.39	16.23	25.66	13.88
P/E (F1)	22.68	21.41	21.20	20.58	21.41	18.54
Price/Sales (P/S)	3.36	2.97	2.29	2.89	2.57	1.73
Earnings Yield	4.44%	4.69%	4.42%	4.85%	4.69%	5.36%
Debt/Equity	2.06	0.61	0.77	0.54	0.52	0.71
Cash Flow (\$/share)	7.77	1.10	7.01	3.24	0.69	0.89
Growth Score	C	-	-	D	C	C
Hist. EPS Growth (3-5 yrs)	9.08%	9.08%	10.87%	9.10%	NA	NA
Proj. EPS Growth (F1/F0)	-0.56%	9.21%	-10.65%	3.39%	47.62%	8.85%
Curr. Cash Flow Growth	9.40%	10.15%	5.46%	4.99%	10.26%	19.10%
Hist. Cash Flow Growth (3-5 yrs)	7.63%	5.50%	8.55%	2.73%	NA	5.50%
Current Ratio	0.99	2.42	1.29	0.53	3.17	1.66
Debt/Capital	67.35%	37.86%	45.14%	34.87%	34.27%	41.45%
Net Margin	13.94%	8.86%	10.53%	14.24%	3.86%	4.78%
Return on Equity	71.52%	7.46%	16.06%	13.73%	5.90%	4.71%
Sales/Assets	0.96	0.48	0.55	0.41	0.42	0.30
Proj. Sales Growth (F1/F0)	0.31%	5.00%	-2.61%	-0.31%	60.55%	9.69%
Momentum Score	A	-	-	A	F	D
Daily Price Chg	-2.33%	1.67%	-1.02%	-1.00%	1.67%	1.74%
1 Week Price Chg	-4.67%	-5.00%	-7.25%	-3.43%	-5.00%	-8.10%
4 Week Price Chg	1.11%	4.32%	5.73%	6.66%	7.27%	4.32%
12 Week Price Chg	-2.27%	4.92%	15.89%	7.48%	4.92%	20.57%
52 Week Price Chg	-5.95%	-5.95%	-6.79%	-5.23%	-28.28%	-10.93%
20 Day Average Volume	1,247,082	1,018,101	2,574,456	6,840,594	1,113,640	1,018,101
(F1) EPS Est 1 week change	0.00%	0.00%	0.00%	0.10%	-3.13%	0.00%
(F1) EPS Est 4 week change	-0.28%	-0.28%	0.00%	0.29%	-4.62%	0.00%
(F1) EPS Est 12 week change	-5.80%	-5.80%	-14.21%	-3.77%	-9.82%	-5.68%
(Q1) EPS Est Mthly Chg	-0.24%	-0.24%	0.00%	0.26%	-9.84%	0.00%

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 have an excellent 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.

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	D
Growth Score	C
Momentum Score	A
VGM Score	C

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.

Disclosures

This report contains independent commentary to be used for informational purposes only. The analysts contributing to this report do not hold any shares of this stock. The analysts contributing to this report do not serve on the board of the company that issued this stock. The EPS and revenue forecasts are the Zacks Consensus estimates, unless indicated otherwise on the reports first page. Additionally, the analysts contributing to this report certify that the views expressed herein accurately reflect the analysts personal views as to the subject securities and issuers. ZIR certifies that no part of the analysts compensation was, is, or will be, directly or indirectly, related to the specific recommendation or views expressed by the analyst in the report.

Additional information on the securities mentioned in this report is available upon request. This report is based on data obtained from sources we believe to be reliable, but is not guaranteed as to accuracy and does not purport to be complete. Any opinions expressed herein are subject to change.

ZIR is not an investment advisor and the report should not be construed as advice designed to meet the particular investment needs of any investor. Prior to making any investment decision, you are advised to consult with your broker, investment advisor, or other appropriate tax or financial professional to determine the suitability of any investment. This report and others like it are published regularly and not in response to episodic market activity or events affecting the securities industry.

This report is not to be construed as an offer or the solicitation of an offer to buy or sell the securities herein mentioned. ZIR or its officers, employees or customers may have a position long or short in the securities mentioned and buy or sell the securities from time to time. ZIR is not a broker-dealer. ZIR may enter into arms-length agreements with broker-dealers to provide this research to their clients. Zacks and its staff are not involved in investment banking activities for the stock issuer covered in this report.

ZIR uses the following rating system for the securities it covers. **Outperform-** ZIR expects that the subject company will outperform the broader U.S. equities markets over the next six to twelve months. **Neutral-** ZIR expects that the company will perform in line with the broader U.S. equities markets over the next six to twelve months. **Underperform-** ZIR expects the company will underperform the broader U.S. equities markets over the next six to twelve months.

No part of this report can be reprinted, republished or transmitted electronically without the prior written authorization of ZIR.