

Kraft Heinz(KHC)

\$34.38 (As of 07/31/20)

Price Target (6-12 Months): **\$41.00**

Long Term: 6-12 Months

Zacks Recommendation:
Outperform

(Since: 07/31/20)

Prior Recommendation: Neutral

Short Term: 1-3 Months

Zacks Rank: (1-5)

1-Strong Buy

Zacks Style Scores:

VGM:B

Value: B

Growth: C

Momentum: A

Summary

Shares of Kraft Heinz have increased and outperformed the industry in the past three months. The company posted robust second-quarter 2020 results, wherein both the top and the bottom lines not only surpassed the Zacks Consensus Estimate but also improved year over year. Notably, the company has been witnessing a surge in demand for its products. This can be attributed to higher at-home consumptions amid the coronavirus outbreak. Additionally, organic revenues increased 7.4% on the back of strong demand from retail customers amid the pandemic. Quite apparent, Kraft Heinz's efficient pricing strategy, robust product development and strategic investments have been aiding results. However, escalated SG&A expenses and unfavorable foreign currency translation are headwinds. Moreover, sluggish performance in the Canada region has been a concern.

Data Overview

52 Week High-Low	\$35.87 - \$19.99
20 Day Average Volume (sh)	5,762,332
Market Cap	\$42.0 B
YTD Price Change	7.0%
Beta	1.01
Dividend / Div Yld	\$1.60 / 4.7%
Industry	Food - Miscellaneous
Zacks Industry Rank	Bottom 35% (164 out of 253)

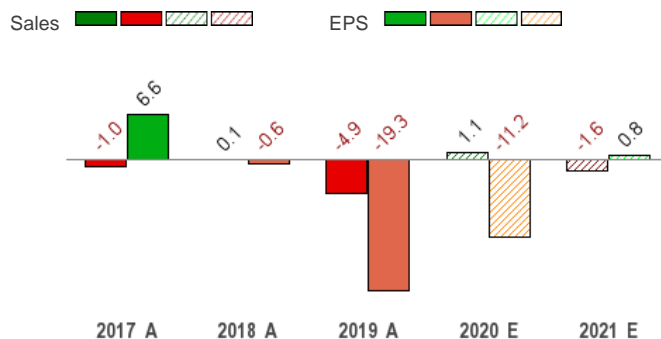
Last EPS Surprise	25.0%
Last Sales Surprise	1.9%
EPS F1 Est- 4 week change	1.3%
Expected Report Date	NA
Earnings ESP	-0.2%

P/E TTM	12.3
P/E F1	13.6
PEG F1	3.7
P/S TTM	1.7

Price, Consensus & Surprise



Sales and EPS Growth Rates (Y/Y %)



Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	5,797 E	6,225 E	6,188 E	6,660 E	24,838 E
2020	6,157 A	6,648 A	6,067 E	6,507 E	25,245 E
2019	5,959 A	6,406 A	6,076 A	6,536 A	24,977 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$0.56 E	\$0.69 E	\$0.61 E	\$0.67 E	\$2.55 E
2020	\$0.58 A	\$0.80 A	\$0.56 E	\$0.63 E	\$2.53 E
2019	\$0.66 A	\$0.78 A	\$0.69 A	\$0.72 A	\$2.85 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 07/31/2020. The reports text is as of 08/03/2020.

Overview

Headquartered in Pittsburgh, PA, The Kraft Heinz Company (KHC) is one of the largest consumer packaged food and beverage companies in North America. It manufactures and markets food and beverage products like condiments and sauces, cheese as well as dairy, meals, meats, refreshment beverages, coffee, and other grocery products.

Its popular brands include Heinz, Kraft, Oscar Mayer, Planters, Philadelphia, Velveeta, Lunchables, Maxwell House, Capri Sun, and Ore-Ida. Notably, the company generates sales across roughly 190 countries and territories.

Well, the merger of Kraft Foods Group, Inc. ("Kraft") with and into a wholly-owned subsidiary of H.J. Heinz Holding Corporation ("Heinz") was concluded in July 2015. Upon the merger, Heinz was rechristened as The Kraft Heinz Company and H.J. Heinz Holding Corporation was renamed to Kraft Heinz Foods Company. Kraft and Heinz were both pioneers in the food space for more than 100 years.

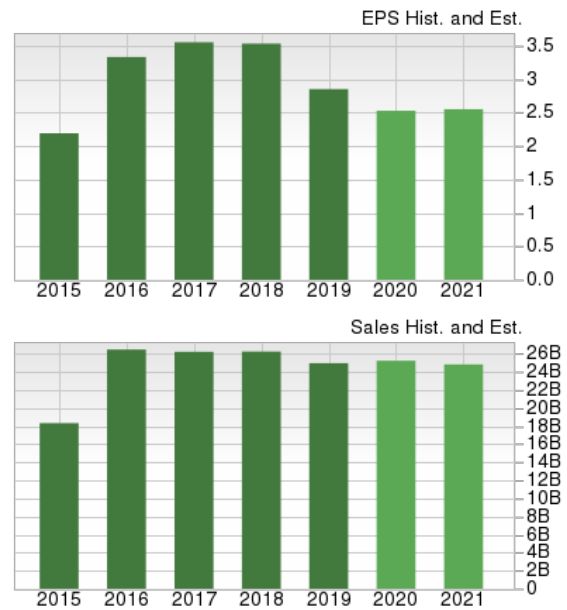
We note that during the third quarter of 2017, management revealed plans to reorganize some of its international businesses for better geographic alignment. These plans included shifting the Middle East and Africa businesses from AMEA segment to Europe, which in turn will form the Europe, Middle East, and Africa (EMEA) segment. The remaining AMEA unit will form the Asia Pacific or APAC segment, which will be a part of the Rest of the World.

Effective first-quarter 2018, Kraft Heinz has three reportable segments defined by geographic region:

United States (71.1% of the total revenues in FY19), Canada (7.5% of the total revenues in FY19), and Europe, Middle East, and Africa or EMEA (10.2% of the total revenues in FY19). The remaining businesses are combined and disclosed as "Rest of World" or ROW.

Rest of World (11.2% of the total revenues in FY19) comprises two operating segments: Latin America, and Asia-Pacific (APAC).

On Jan 30, 2019, Kraft Heinz announces the completion of sales of Indian brands namely Glucon-D, Nycil, Complan and Sampriti to Zydus Wellness Limited.



Reasons To Buy:

- ▲ **Impressive Q2 Results:** Kraft Heinz reported robust second-quarter 2020 with the top and the bottom line surpassing the Zacks Consensus Estimate. Moreover, sales and earnings increased year over year. Results gained from solid retail demand in all business segments.

Notably, adjusted earnings per share of 80 cents surpassed the Zacks Consensus Estimate of 64 cents. Also, the metric increased 2.6% courtesy of higher adjusted EBITDA. Net sales increased 3.8% and surpassed the consensus mark. Organic sales rose 7.4% on the back of higher demand from retail customers owing to greater in-at-home consumption amid the outbreak. During the quarter, volume/mix increased 5.2 percentage points on the back of higher demand in the retail segment as well as improved retail inventory. We note that shares of Kraft Heinz have increased 20.4% in the past three months compared with the industry's growth of 10%.

Kraft Heinz is gaining from strong consumer demand in retail business stemming from the coronavirus pandemic.

- ▲ **Pricing Strategies Bode Well:** Solid pricing initiatives have been aiding Kraft Heinz for a while now. In the second quarter of 2020, overall pricing was up 2.2 percentage points, driven by reduced promotional activities. During the quarter, pricing in the United States moved up 2.3 percentage points. In Canada pricing rose 1.3 percentage points due to higher list price in several categories as well as reduced promotional activities. Within International markets pricing improved 2.6 percentage points. We believe that Kraft Heinz's robust pricing actions are likely to help the company mitigate adverse impacts of cost inflation.

- ▲ **Efficiency Building Plans on Track:** In order to ramp up overall business, management laid down certain enterprise transformation strategies. In this context, the company is on track to improve efficiency across its supply chain, with particular emphasis on procurement, manufacturing and distribution. During third-quarter 2019, the company had implemented nine transformational projects to strengthen some of the core areas of the business. Among them, five projects are directed toward bolstering the top line, two for enhancing operational efficiencies and the remaining for increasing effectiveness. Another important focus-area of the company is its workforce. Management believes that strength in its people plays a key role in realizing the company's strategic goals. As a result, management has undertaken several moves to strengthen the company's leadership.

In terms of cost savings, the company has been increasing visibility and control of its cost components, especially in areas such as marketing and e-commerce. It is also keeping a close watch on investments made for enhancing sales and customer services. Further, the company is on track with examining its SKU's to remove complexities and boost mix. Other productivity improvement initiatives include programs such as zero-based budgeting; modernization and capability building within the manufacturing footprint and building a performance driven culture in the company. A portion of the gains from such initiatives are re-invested in the business for innovation, brand building and advertising to stimulate top-line growth.

- ▲ **Product Development Efforts:** Kraft Heinz remains focused on improving the performance of key brands — Heinz, Kraft and Planters — and major product categories like condiments and sauces, cheese, meals, nuts and baby food. Management earlier outlined that the company will make significant investments in marketing, go-to-market capabilities and product development. These capabilities and platforms are expected to further add to the company's gains. The company is on track with identifying areas that hold significant growth opportunities and is accordingly undertaking product development efforts. It is also undertaking efforts to boost the e-commerce channel. Such well-chalked efforts have been aiding growth across several business categories.

Additionally, with growing awareness of the nutritional value of food products, responsible and sustainable sourcing of raw materials has become an important issue for food companies. The importance of using real ingredients and minimal processing in packaged food products is also being emphasized increasingly. As a result, a large number of companies in the food industry are switching or have already switched to the use of cage-free eggs. Kraft Heinz had stated earlier that it plans to switch to 100% cage-free eggs for its North American operations by 2025. Kraft Heinz uses eggs for its sauces portfolio.

- ▲ **Debt Analysis:** Kraft Heinz's cash position remains sufficient to meet current portion of long-term debt of \$757 million as of Jun 27, 2020. Further, its long-term debt of \$28,097 million declined 10.9% on a quarter-on-quarter basis. Moreover, at the end of the second quarter, the company's debt-to-capitalization ratio was a respectable 0.37 compared with 0.39 at the end of the first quarter. Additionally, the company has a decent "times interest earned" ratio of 1.2. 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.

- ▲ **Strong Brand Portfolio:** Kraft Heinz is the fifth-largest branded food and beverage company in the world and the third-largest food and beverage company in North America. Globally, the company markets more than \$1 billion brands. The company boasts many iconic brands which enjoy long-standing consumer recognition. Eight of its brands generate more than \$1 billion in sales including Oscar Mayer, Planters, Philadelphia, Velveeta, and Smart Ones.

Risks

- **Soft Canada Business:** Sales in Kraft Heinz's Canada segment has been declining year over year in the past few quarters. During second-quarter 2020, net sales fell 23.9%, which included unfavorable impact of divestitures to the tune of 23.1 percentage points and an unfavorable currency impact of 2.8 percentage points. Also, segment adjusted EBITDA declined 23.2% to \$110 million, due to unfavorable currency rates and adverse divestiture impacts. Persistence of the trend may continue exerting pressure on the company's top line.
 - **Rising SG&A a Concern:** Kraft Heinz is seeing a rise in selling, general and administrative expenses. Excluding impairment losses, SG&A expense increased 22.4% to \$918 million during the second quarter of 2020. As a percentage of sales, SG&A expense excluding impairment losses expanded 210 basis points to 13.8%. Apart from this, the company is incurring higher expenses related to the coronavirus pandemic. These include incremental costs for providing personal protective gear to workers as well as incorporating work from home policy. We believe that persistence of such trends is a threat to the company's performance in the future.
 - **Currency Headwinds:** Kraft Heinz's cross-border presence exposes it to unfavorable currency movements due to the strengthening of the U.S. dollar. During the second quarter, currency movements had an adverse impact of 1.5 percentage points on the top line. Moreover, unfavorable currency rates had an adverse impact of 6.2 and 2.8 percentage points across the company's International and Canada segments sales, respectively.
 - **Intense Competition:** Kraft Heinz operates in the highly competitive food industry. The company competes with other major players on grounds of pricing, product innovation, brand recognition and loyalty, product quality, effectiveness of marketing and promotional activity, and responsiveness to consumers' changing preferences. Such competitive pressures may compel the company to lower prices, which remains a threat to its profits.
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Last Earnings Report

Kraft Heinz Q2 Earnings Surpass Estimates, Sales Up

Kraft Heinz reported robust second-quarter 2020 results, with the top and the bottom line surpassing the Zacks Consensus Estimate. Moreover, sales and earnings increased year over year. Results gained from solid retail demand in all business segments.

Q2 in Detail

Adjusted earnings per share of 80 cents surpassed the consensus mark of 64 cents. Moreover, the bottom line increased 2.6% year over year on the back of higher adjusted EBITDA.

Net sales increased 3.8% year over year to \$6,648 million. Also, the figure surpassed the Zacks Consensus Estimate of \$6,521.7 million. Net sales growth included 1.5 and 2.1 percentage point impact from unfavorable impacts of currency and divestitures, respectively. Organic sales rose 7.4% on the back of solid consumer demand in the retail category stemming from the coronavirus pandemic. However, reduced sales from foodservice channels were a deterrent.

Pricing was up 2.2 percentage points, driven by reduced promotional activities. Volume/mix increased 5.2 percentage points on the back of higher demand in the retail segment as well as improved retail inventory.

Operating Highlights

Gross profit of \$2,452 million increased 17.8% year over year and gross margin came in at 36.9% in the reported quarter.

Adjusted EBITDA was up 12.4% to \$1,799 million in the quarter. The upside can be attributed to robust organic net sales growth.

Segment Discussion

United States: Net sales of \$4,917 million increased 8.5% year over year. During the quarter, pricing moved up 2.3 percentage points owing to lower promotional activities. Volume/mix increased 6.2 percentage points on growth in various retail categories as well as increase in retail inventory.

The segment's adjusted EBITDA increased 17.6% to \$1,478 million. The upside was caused by volume leverage along with favorable channel and product mix. Favorable pricing and reduced costs of packaging were also a reason.

Canada: Net sales of \$426 million declined 23.9% year over year, which included unfavorable impact of divestitures to the tune of 23.1 percentage points and an unfavorable currency impact of 2.8 percentage points. Nevertheless, organic sales increased 2% year over year. Pricing increased 1.3 percentage points due to higher list price in several categories as well as reduced promotional activities. Volume/mix moved up slightly owing to higher consumption in the retail unit.

Segment adjusted EBITDA declined 23.2% to \$110 million, due to unfavorable currency rates and adverse divestiture impacts.

International: Net sales of \$1,305 million inched down 0.7% year over year, which included unfavorable currency impact of 6.2 percentage points. Organic sales rose 5.5% year on year. Pricing improved 2.6 percentage points owing to reduced promotional expenses and better prices in various markets. Volume/mix was up 2.9 percentage points on growth of consumption in condiments, sauces and meal-oriented categories. Also, improvement in retail inventory levels was a reason.

Adjusted EBITDA increased 3.2% to \$275 million on higher organic net sales.

Financials

Kraft Heinz ended the quarter with cash and cash equivalents of \$2,812 million, long-term debt of \$28,097 million as well as total shareholders' equity of \$49,040 million. Further, the company generated \$2,216 million as cash from operating activities for six months ended Jun 27, 2020.

In a separate press release, the company announced a quarterly dividend of 40 cents per share, which is payable on Sep 25 to shareholders of record as of Aug 28.

Quarter Ending **06/2020**

Report Date	Jul 30, 2020
Sales Surprise	1.94%
EPS Surprise	25.00%
Quarterly EPS	0.80
Annual EPS (TTM)	2.79

Recent News

Kraft Heinz Declares Dividend - Jul 30, 2020

The company announced a quarterly dividend of 40 cents per share, which is payable on Sep 25 to shareholders of record as of Aug 28.

Valuation

Kraft Heinz shares are up 10.6% in the year-to-date period and 16.3% over the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Consumer Staples sector are down 4.1% and 6.7%, respectively in the year-to-date period. Over the past year, the Zacks sub-industry is up 6.3%, while the sector declined 6.3%.

The S&P 500 index is up 2.7% in the year-to-date period and 17.7% in the past year.

The stock is currently trading at 13.47X forward 12-month earnings, which compares to 18.79X for the Zacks sub-industry, 20.04X for the Zacks sector and 22.64X for the S&P 500 index.

Over the past five years, the stock has traded as high as 27.34X and as low as 8.58X, with a 5-year median of 19.49X. Our Outperform recommendation indicates that the stock will perform better than the market. Our \$41 price target reflects 16.06X forward 12-month earnings.

The table below shows summary valuation data for KHC

Valuation Multiples - KHC					
		Stock	Sub-Industry	Sector	S&P 500
P/E F12M	Current	13.47	18.79	20.04	22.64
	5-Year High	27.34	22.9	22.37	22.64
	5-Year Low	8.58	14.82	16.63	15.25
	5-Year Median	19.49	18.54	19.57	17.55
P/S F12M	Current	1.67	1.68	9.46	3.59
	5-Year High	4.41	2.05	11.15	3.59
	5-Year Low	1	1.41	8.1	2.53
	5-Year Median	3.18	1.76	9.89	3.04
EV/EBITDA F12M	Current	11.33	13.15	32.76	13.21
	5-Year High	20.75	14.68	37.28	14.2
	5-Year Low	9.68	10.95	25.89	9.15
	5-Year Median	14.24	13.17	33.7	11

As of 07/31/2020

Industry Analysis Zacks Industry Rank: Bottom 35% (164 out of 253)



Top Peers

Company (Ticker)	Rec	Rank
BG Foods, Inc. (BGS)	Neutral	3
Conagra Brands Inc. (CAG)	Neutral	3
Campbell Soup Company (CPB)	Neutral	3
Flowers Foods, Inc. (FLO)	Neutral	2
General Mills, Inc. (GIS)	Neutral	3
Kellogg Company (K)	Neutral	2
Mondelez International, Inc. (MDLZ)	Neutral	3
Sysco Corporation (SYI)	Underperform	5

Industry Comparison Industry: Food - Miscellaneous				Industry Peers		
	KHC	X Industry	S&P 500	CAG	CPB	MDLZ
Zacks Recommendation (Long Term)	Outperform	-	-	Neutral	Neutral	Neutral
Zacks Rank (Short Term)	1	-	-	3	3	3
VGM Score	B	-	-	A	A	B
Market Cap	42.01 B	3.87 B	22.59 B	18.25 B	14.98 B	79.51 B
# of Analysts	7	3	14	8		9
Dividend Yield	4.65%	0.00%	1.83%	2.27%	2.82%	2.05%
Value Score	B	-	-	B	B	B
Cash/Price	0.13	0.07	0.07	0.03	0.08	0.02
EV/EBITDA	13.74	12.76	12.94	14.41	13.26	19.00
PEG Ratio	3.70	3.92	3.04	2.24	2.04	3.19
Price/Book (P/B)	0.85	2.41	3.17	2.30	5.80	3.05
Price/Cash Flow (P/CF)	10.05	11.13	12.51	12.13	13.07	17.14
P/E (F1)	13.59	17.87	21.87	15.65	16.89	21.26
Price/Sales (P/S)	1.65	1.23	2.44	1.65	1.79	3.07
Earnings Yield	7.36%	4.97%	4.31%	6.38%	5.91%	4.70%
Debt/Equity	0.57	0.63	0.75	1.12	2.01	0.63
Cash Flow (\$/share)	3.42	2.81	6.94	3.09	3.79	3.24
Growth Score	C	-	-	A	B	B
Hist. EPS Growth (3-5 yrs)	0.09%	5.41%	10.85%	-2.26%	-2.14%	9.10%
Proj. EPS Growth (F1/F0)	-11.38%	5.30%	-7.75%	4.99%	27.58%	5.67%
Curr. Cash Flow Growth	-15.53%	4.39%	5.39%	22.57%	-12.42%	4.99%
Hist. Cash Flow Growth (3-5 yrs)	11.14%	6.08%	8.55%	4.34%	0.50%	2.73%
Current Ratio	1.09	1.59	1.31	0.88	0.84	0.55
Debt/Capital	36.37%	39.16%	44.32%	52.82%	66.79%	38.71%
Net Margin	-0.76%	2.44%	10.44%	7.60%	18.34%	13.31%
Return on Equity	6.68%	12.01%	14.73%	14.38%	46.05%	14.02%
Sales/Assets	0.25	1.08	0.52	0.49	0.66	0.40
Proj. Sales Growth (F1/F0)	1.07%	0.00%	-1.95%	-2.92%	-8.00%	0.57%
Momentum Score	A	-	-	C	C	B
Daily Price Chg	-3.32%	-0.62%	-0.92%	-0.69%	-1.77%	-1.80%
1 Week Price Chg	-0.94%	0.00%	0.37%	0.08%	-0.40%	1.48%
4 Week Price Chg	8.08%	2.91%	3.81%	5.76%	0.51%	7.77%
12 Week Price Chg	19.25%	8.03%	11.93%	12.90%	-1.33%	10.63%
52 Week Price Chg	5.69%	-1.91%	-1.92%	28.52%	17.72%	3.47%
20 Day Average Volume	5,762,332	160,444	1,887,986	2,471,717	1,670,405	5,568,431
(F1) EPS Est 1 week change	1.15%	0.00%	0.00%	0.00%	0.00%	1.72%
(F1) EPS Est 4 week change	1.30%	0.00%	0.38%	1.92%	0.00%	1.77%
(F1) EPS Est 12 week change	1.52%	1.31%	-0.07%	3.68%	5.06%	2.07%
(Q1) EPS Est Mthly Chg	2.94%	0.00%	0.16%	0.69%	0.00%	0.86%

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	B
Growth Score	C
Momentum Score	A
VGM Score	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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