Apr 14, 2020

Lamb Weston (LW)

$58.26 (As of 04/13/20)

Price Target (6-12 Months): **$49.00**

Long Term: 6-12 Months	**Zacks Recommendation:** (Since: 04/14/20) Prior Recommendation: Neutral	**Underperform**
Short Term: 1-3 Months	**Zacks Rank:** (1-5)	**5-Strong Sell**
	Zacks Style Scores:	VGM:F
	Value: F | Growth: D	Momentum: F

Summary

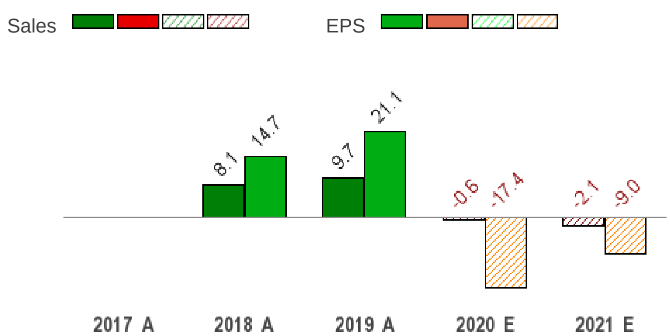
Shares of Lamb Weston have lagged the industry in the past three months. The stock took a hit following third-quarter fiscal 2020 results, wherein the top and bottom lines missed the Zacks Consensus Estimate. Also, earnings fell year over year, affected by continued rise in input and SG&A costs. Moreover, management withdrew its view due to the apprehended impact of the spread of coronavirus. Coronavirus-led social distancing has led to lower traffic at U.S. restaurants and QSRs, leading to slow orders for Lamb Weston. Though operators are coming up with takeout and delivery options, this can only compensate for part of the lost sales. Also, operations in Europe are likely to take a hit. Nonetheless, the company is seeing better trends in the Retail segment. Also, improved price/mix and LTOs have been a driver.

Price, Consensus & Surprise

Data Overview

52 Week High-Low	**$96.32 - $39.06**
20 Day Average Volume (sh)	**2,194,515**
Market Cap	**$8.5 B**
YTD Price Change	**-32.3%**
Beta	**0.92**
Dividend / Div Yld	**$0.92 / 1.6%**
Industry	**Food - Miscellaneous**
Zacks Industry Rank	**Top 34% (85 out of 253)**
Last EPS Surprise	**-16.3%**
Last Sales Surprise	**-1.7%**
EPS F1 Est- 4 week change	**-23.7%**
Expected Report Date	**07/28/2020**
Earnings ESP	**0.0%**
P/E TTM	**17.9**
P/E F1	**21.9**
PEG F1	**2.9**
P/S TTM	**2.2**

Sales and EPS Growth Rates (Y/Y %)



Sales Estimates (millions of $)

	Q1	Q2	Q3	Q4	Annual*
2021	908 E	1,000 E	984 E	944 E	3,654 E
2020	989 A	1,019 A	937 A	788 E	3,734 E
2019	915 A	911 A	927 A	1,003 A	3,757 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	$0.56 E	$0.79 E	$0.85 E	$0.53 E	$2.42 E
2020	$0.79 A	$0.95 A	$0.77 A	$0.15 E	$2.66 E
2019	$0.73 A	$0.80 A	$0.95 A	$0.74 A	$3.22 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 04/13/2020. The reports text is as of 04/14/2020.

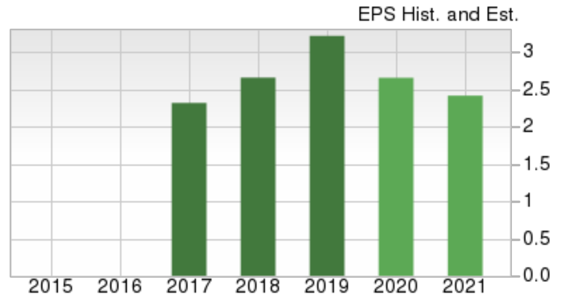
Overview

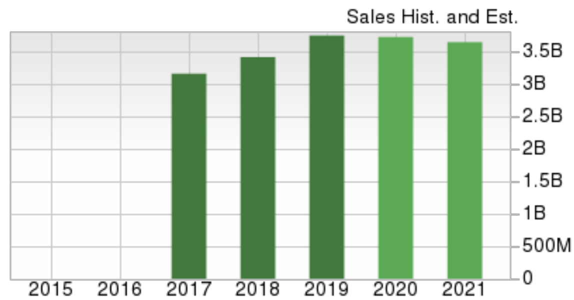
Based in Eagle, ID, Lamb Weston Holdings, Inc. is a leading global manufacturer, marketer and distributor of value-added frozen potato products, particularly French fries, and also provides a range of appetizers.

Lamb Weston was formed in July 2016 as a wholly owned subsidiary of Conagra Brands, while it was spun off from the latter in November 2016 when it began operating independently. Lamb Weston, along with its joint venture allies, is the top frozen potato products supplier in North America, while it also operates internationally, with a robust and growing presence in emerging markets. The company mainly serves retail and foodservices customers.

Lamb Weston operates through the following segments:

Global (52.2% of FY19 Sales): This includes the top 100 North American restaurant chains and international customers such as global and regional restaurant chains, foodservice distributors, and retailers. The segment also incorporates non-U.S. and non-Canadian retail and foodservice customers. Global segment products include frozen potatoes, sweet potatoes and appetizers sold under the Lamb Weston brand, alongside other customer labels.





Foodservice (30.8% of FY19 Sales): This includes products sold all over the United States and Canada, mainly to commercial distributors and restaurant chains, other than the top 100 North American restaurants. Foodservice, which also caters to non-commercial networks, sells frozen potatoes, sweet potatoes, commercial ingredients and appetizers.

Retail (13.3% of FY19 Sales): This includes customer-facing products sold mainly to grocery, mass merchants, clubs and specialty retailers. Main products of this segment include frozen potatoes and sweet potato items sold under the company's owned or licensed brands like Grown in Idaho and Alexia, among other selling channels.

Other (3.7% of FY19 Sales): This mainly includes the company's vegetable and dairy operations.

Also, Lamb Weston operates through two unconsolidated joint ventures ("JVs") and incorporates its share of earnings from these as equity method earnings. Lamb Weston has 50% stake in its JV with Meijer Frozen Foods and an equal stake in potato processing venture with RDO Frozen Co.

Reasons To Sell:

> Management is unable to foresee frozen potato products demand in the near term – considering the uncertainty related to COVID-19. The company withdrew its guidance for fiscal 2020.

- **COVID-19 Impact, Guidance Withdrawn:** Shares of Lamb Weston have slumped 36% in the past three months compared with the industry's decline of 15.2%. The stock got a hit following the company's third-quarter fiscal 2020 results, wherein both top and bottom lines fell short of the Zacks Consensus Estimate. Also, earnings declined year over year. Moreover, management withdrew its fiscal 2020 sales and adjusted EBITDA view owing to the apprehended impact of the rapid spread of coronavirus.

  During the quarter, earnings were marred by lower gross profit, higher tax rate and a rise in SG&A costs. Further, volumes were negatively impacted by declines in the Global segment, wherein the initial impact of coronavirus on restaurant traffic was a deterrent. Notably, the company largely caters to quick-serve restaurants or QSRs as well as full service restaurants and outlets. Apart from this, it sells through retail outlets. The growing spread of coronavirus and increased social distancing have led to lower traffic at restaurants and QSRs, especially in the United States, leading to slower orders for Lamb Weston. Though these operators are coming up with takeout and delivery options, this can only compensate for part of the lost sales. In fact, management expects traffic at full service restaurants to fall more sharply than QSRs. However, the company is seeing better trends in the Retail segment, given the increased demand for frozen fries stemming from stock-piling during quarantine.

  However, management is unable to foresee frozen potato products' demand in the near term, considering the uncertainty related to COVID-19. Management is particularly unsure about the impact of the pandemic on restaurant traffic in North America. Thus, the company withdrew its sales and adjusted EBITDA guidance for fiscal 2020.

- **Input Cost Inflation:** Lamb Weston is witnessing cost increases for input materials as well as manufacturing. In third-quarter fiscal 2020, gross profit tumbled 8.4% to $250.4 million due to increased manufacturing costs stemming from input and fixed-cost inflation as well as unfavorable customer mix. Further, gross profit was hurt by higher transportation costs and depreciation expenses related to the company's french fry production line in Oregon. Also, costs resulting from COVID-19-related production interruptions in China were a reason. Rising costs were also a drag on product contribution margins in the Global, Retail and Foodservice units during the said period.

- **Increased SG&A Costs a Worry:** Lamb Weston's SG&A expenses have been rising year over year for the past few quarters. In third-quarter fiscal 2020, SG&A expenses increased 10.4% to $87.9 million due to investments in the company's sales, operating and systems capabilities. Also, unfavorable currency movements impacted SG&A expenses. Continuation of these factors may be a burden on the bottom line.

- **Challenges in Europe:** Poor potato crop scenario in Europe has been a headwind for Lamb Weston for a while. The company serves the European market through its Lamb Weston Meijer joint venture. Most of the consumption in the region is through dine-in, and takeaways through walk-in traffic. The adverse impact of coronavirus on demand in the region has been highest in Italy. Other countries are also seeing lower demand due to several restrictions on social movement. Management also expects the decrease in demand to accelerate in these countries, which is likely to hurt Lamb Weston Meijer's performance.

- **Stiff Competition:** Lamb Weston Holdings operates in a highly competitive frozen potato-products industry. The company competes with big national and international firms, along with regional and local companies. Lamb Weston competes with these firms on the basis of sales and marketing, financial resources, customer service, product innovation, food safety, product quality, pricing and brand recognition, among others. This may hamper market share and hinder top and bottom-line growth.

Risks

- **Robust Price/Mix:** Lamb Weston's top line has been gaining from robust price/mix, as also witnessed during the third quarter of fiscal 2020. During the quarter, price/mix rose 1% and aided sales growth, which was otherwise negatively impacted by flat volumes. Price/mix rose 4% and 2% at the Foodservice and Retail segments, respectively. The rise could be attributable to actions to enhance mix and pricing. Continuity of such trends is likely to augment sales growth.

- **Efforts to Boost Offerings & Expand Capacity:** Lamb Weston has been undertaking initiatives to boost offerings and operating capacity. These efforts enable the company to effectively meet rising demand conditions for snacks and fries. Markedly, it completed the acquisition of joint venture interests in Lamb Weston BSW sometime around mid-fiscal 2019. During the third quarter of fiscal 2020, acquisitions drove volumes by more than a point. Among other moves, the company acquired Australia-based companies Ready Meals and Marvel Packers in 2019 and 2018, respectively. These buyouts have bolstered Lamb Weston's market share in Australia.

  Speaking on capacity expansion endeavors, the company completed the expansion of a facility located at Hermiston, Oregon on Jun 18, 2019. The expansion has facilitated the addition of a new processing line for increasing the production of frozen french fries. This is expected to cater to demand in North America and key export markets as well as support production needs emerging from, innovation and LTO's.

- **LTO's a Major Sales Driver:** Lamb Weston has been benefitting from its limited time offering products or LTO innovations, which form key part in the company's long-term prospects. Incidentally, LTOs helped drive growth and market share gains in fiscal 2018 and in fiscal 2019. More specifically, LTOs are aiding volumes in the company's Global segment. Management has been optimistic about prospects from new LTOs.

- **Strong Top-line Growth Trend:** Lamb Weston boasts a solid top-line trend. Markedly, the company's sales have been rising year over year for a while. The trend continued in third-quarter fiscal 2020, wherein net sales climbed 1% to $937.3 million on the back of improved price/mix. For volumes, growth in the Foodservice segment was offset by weak Global segment volumes. Acquisitions also drove volumes to an extent.

Last Earnings Report

Lamb Weston's Q3 Earnings Lag Estimates, View Withdrawn

Quarter Ending	02/2020
Report Date	Apr 01, 2020
Sales Surprise	-1.71%
EPS Surprise	-16.30%
Quarterly EPS	0.77
Annual EPS (TTM)	3.25

Lamb Weston delivered dismal third-quarter fiscal 2020 results, wherein both top and the bottom lines fell short of the Zacks Consensus Estimate. In fiscal third quarter, the company delivered adjusted earnings of 77 cents per share, down 19% year over year. The downside can be attributable to lower gross profit, higher tax rate and a rise in SG&A expenses. Moreover, the bottom line lagged the Zacks Consensus Estimate of 92 cents.

Net sales came in at $937.3 million, up 1% year on year, though it missed the consensus mark of $954 million. While volumes were flat, price/mix rose 1%. For volumes, growth in the Foodservice segment was offset by weak Global segment volumes. Further, fewer shipping days this year was a drag on volumes, though acquisitions were a driver.

Gross profit tumbled 8.4% to $250.4 million due to increased manufacturing costs stemming from input and fixed cost inflation as well as unfavorable customer mix. Further, gross profit was hurt by higher transportation cost and depreciation expenses related to the company's french fry production line in Oregon. Also, costs resulting from COVID-19-related production interruptions in China were a reason.

SG&A expenses increased 10.4% to $87.9 million due to investments in the company's sales, operating as well as systems capabilities. Also, unfavorable currency movements impacted SG&A expenses. Adjusted EBITDA (including unconsolidated joint ventures) declined10% to $227.7 million due to lower operating income.

Segment Analysis

Sales in the **Global** segment dipped 2% to $487.1 million. Volumes and price/mix dropped 1% each, bearing adverse impacts of lower sale of customized products and LTOs. Volumes were also hurt by initial impact of coronavirus on restaurant traffic. Product contribution margin in the segment tumbled 15% to $109.3 million due to elevated production costs, reduced sales volumes and adverse product and customer mix.

Foodservice sales rose 7% to $283 million. Price/mix and volumes improved 4% and 3%, respectively. Product contribution margin rose 5% million to reach $99.8 million, owing to improved price/mix and volumes. This was partly offset by inflated input and fixed costs along with high transportation costs.

In the **Retail** segment, sales moved up 2% to $132.2 million. Volumes in the category were flat whereas price/mix improved 2%. Product contribution margin inched down 1% to $28.8 million due to inflation of input and fixed costs along with greater transportation costs. This was somewhat compensated by reduced advertising and promotional costs and improved price/mix.

Other Financial Details & Guidance

The company ended the quarter with cash and cash equivalents of $30.1 million, long-term debt and financing obligations (excluding current portion) of $2,195.3 million as well as total shareholders' equity of $270.4 million. Lamb Weston generated $435.7 million as net cash from operating activities during the first three quarters of fiscal 2020.

Considering the uncertainty related to COVID-19, management is unable to foresee frozen potato products demand in the near term. Management is particularly unsure about the impact of the pandemic on restaurant traffic in North America. Thus, the company withdrew its sales and adjusted EBITDA guidance for fiscal 2020. Also, management lowered its capital expenditure guidance from roughly $300 million to nearly $200 million for the fiscal.

Recent News

Lamb Announces Dividend – Dec 19, 2019

Lamb Weston announced a quarterly dividend of 23 cents per share, an increase of nearly 15% from the last quarter's dividend. This is payable on Feb 28, 2020 to shareholders of record as on Jan 31, 2020.

Valuation

Lamb Weston's shares are down 32.3% in the year-to-date period and 18.2% over the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Consumer Staples sector are down 16% and 16.5%, respectively in the year-to-date period. Over the past year, the Zacks sub-industry and the sector went down 9.2% and 11.2%, respectively.

The S&P 500 index is down 13.7% in the year-to-date period and 4.6% in the past year.

The stock is currently trading at 15.79X forward 12-month earnings, which compares to 16.54X for the Zacks sub-industry, 18X for the Zacks sector and 18.1X for the S&P 500 index.

Our Underperform recommendation indicates that the stock will perform worse than the market. Our $49 price target reflects 13.28X forward 12-month earnings.

Industry Analysis **Zacks Industry Rank:** Top 34% (85 out of 253)

Top Peers

Flowers Foods, Inc. **(FLO)**	Outperform
The Hain Celestial Group, Inc. **(HAIN)**	Outperform
Darling Ingredients Inc. **(DAR)**	Neutral
General Mills, Inc. **(GIS)**	Neutral
McCormick & Company, Incorporated **(MKC)**	Neutral
Nomad Foods Limited **(NOMD)**	Neutral
Sysco Corporation **(SYY)**	Neutral
Tate & Lyle PLC **(TATYY)**	Neutral

Industry Comparison Industry: Food - Miscellaneous

Industry Peers

	LW Underperform	X Industry	S&P 500	DAR Neutral	FLO Outperform	MKC Neutral
VGM Score	F	-	-	B	A	F
Market Cap	8.51 B	3.37 B	19.08 B	3.37 B	4.66 B	19.76 B
# of Analysts	4	3	14	3	3	6
Dividend Yield	1.58%	0.27%	2.19%	0.00%	3.45%	1.67%
Value Score	F	-	-	A	C	F
Cash/Price	0.00	0.05	0.06	0.02	0.00	0.01
EV/EBITDA	12.85	12.21	11.58	6.26	14.83	20.31
PEG Ratio	2.92	2.80	2.06	NA	NA	5.85
Price/Book (P/B)	31.47	1.99	2.58	1.27	3.69	5.53
Price/Cash Flow (P/CF)	13.37	11.12	10.19	6.04	13.37	22.56
P/E (F1)	21.90	16.67	17.15	13.15	20.73	28.77
Price/Sales (P/S)	2.15	1.07	2.07	1.00	1.13	3.71
Earnings Yield	4.57%	5.96%	5.67%	7.59%	4.81%	3.48%
Debt/Equity	8.12	0.60	0.70	0.62	0.95	1.01
Cash Flow ($/share)	4.36	2.75	7.01	3.40	1.65	6.59
Growth Score	D	-	-	B	A	F
Hist. EPS Growth (3-5 yrs)	18.82%	6.16%	10.92%	-1.35%	0.73%	11.68%
Proj. EPS Growth (F1/F0)	-17.47%	0.36%	-1.91%	-15.95%	10.76%	-3.40%
Curr. Cash Flow Growth	18.57%	4.18%	5.93%	16.44%	1.85%	7.80%
Hist. Cash Flow Growth (3-5 yrs)	12.76%	5.35%	8.55%	3.58%	1.66%	9.99%
Current Ratio	1.85	1.59	1.24	1.33	1.05	0.74
Debt/Capital	89.03%	37.52%	42.36%	38.43%	48.84%	50.37%
Net Margin	12.12%	4.07%	11.64%	9.29%	3.99%	13.13%
Return on Equity	342.27%	11.20%	16.74%	9.24%	16.03%	20.53%
Sales/Assets	1.20	1.17	0.54	0.66	1.28	0.51
Proj. Sales Growth (F1/F0)	-0.59%	0.00%	0.45%	2.46%	4.39%	-1.05%
Momentum Score	F	-	-	F	A	B
Daily Price Chg	-0.24%	-0.55%	-2.62%	-0.53%	-0.59%	-3.64%
1 Week Price Chg	16.33%	5.37%	16.01%	18.60%	4.58%	5.05%
4 Week Price Chg	11.10%	13.48%	14.48%	21.53%	3.57%	23.53%
12 Week Price Chg	-35.62%	-18.02%	-21.69%	-29.79%	-0.32%	-11.85%
52 Week Price Chg	-18.17%	-14.07%	-14.14%	-7.22%	2.37%	-4.06%
20 Day Average Volume	2,194,515	294,718	3,634,618	1,586,405	1,885,216	1,296,760
(F1) EPS Est 1 week change	0.00%	0.00%	0.00%	-5.82%	0.00%	0.00%
(F1) EPS Est 4 week change	-23.75%	0.00%	-5.74%	-8.04%	1.92%	-1.71%
(F1) EPS Est 12 week change	-24.13%	-6.49%	-8.41%	11.40%	5.28%	-6.47%
(Q1) EPS Est Mthly Chg	-81.49%	0.00%	-10.28%	0.40%	2.60%	-1.08%

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.

Value Score	F
Growth Score	D
Momentum Score	F
VGM Score	F

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.

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.