

McCormick & Company (MKC)

\$165.51 (As of 01/30/20)

Price Target (6-12 Months): **\$140.00**

Long Term: 6-12 Months

Zacks Recommendation: Underperform

(Since: 01/29/20)

Prior Recommendation: Neutral

Short Term: 1-3 Months

Zacks Rank: (1-5)

5-Strong Sell

Zacks Style Scores:

VGM:D

Value: F

Growth: B

Momentum: C

Summary

McCormick's shares have lagged the industry in the past three months. The stock came under pressure after the company posted fourth-quarter fiscal 2019 results, wherein both top and bottom lines missed the Zacks Consensus Estimate and management issued a not so impressive view for fiscal 2020. Earnings were hurt by higher taxes. These along with increased investments related to business transformation are likely to weigh on the bottom line in fiscal 2020. Moreover, the company anticipates mid-single-digit cost inflation in fiscal 2020, likely to be somewhat cushioned by pricing and cost-saving efforts. Speaking of saving efforts, gains from the CCI program have been yielding results. Also, focus on product launches and marketing efforts bodes well. However, volatile currency movements are concerning.

Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$174.58 - \$120.49
20 Day Average Volume (sh)	827,828
Market Cap	\$22.0 B
YTD Price Change	-2.5%
Beta	0.13
Dividend / Div Yld	\$2.48 / 1.5%
Industry	Food - Miscellaneous
Zacks Industry Rank	Top 43% (109 out of 255)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	-1.2%
Last Sales Surprise	-1.8%
EPS F1 Est- 4 week change	-4.6%
Expected Report Date	03/24/2020
Earnings ESP	0.0%
P/E TTM	30.9
P/E F1	31.3
PEG F1	3.9
P/S TTM	4.1

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	1,297 E	1,375 E	1,407 E	1,579 E	5,637 E
2020	1,253 E	1,333 E	1,366 E	1,537 E	5,489 E
2019	1,232 A	1,302 A	1,329 A	1,485 A	5,347 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$1.14 E	\$1.24 E	\$1.50 E	\$1.79 E	\$5.67 E
2020	\$1.07 E	\$1.12 E	\$1.40 E	\$1.68 E	\$5.29 E
2019	\$1.12 A	\$1.16 A	\$1.46 A	\$1.61 A	\$5.35 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 01/30/2020. The reports text is as of 01/31/2020.

Overview

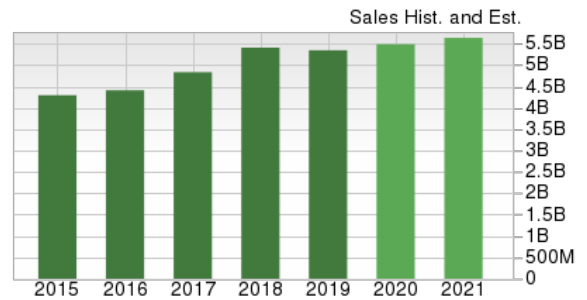
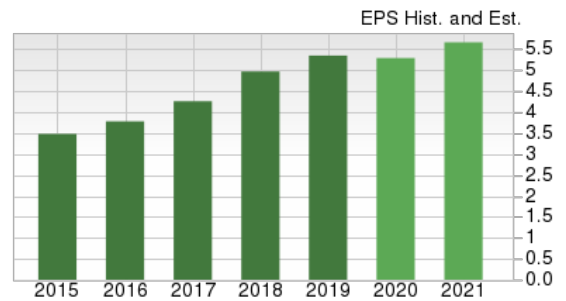
Founded in 1889 and based in Sparks, MD, McCormick & Company, Inc. is a leading manufacturer, marketer and distributor of spices, seasonings, specialty foods and flavors to the entire food industry across the globe.

The company's key sales, distribution and production facilities are located in North America and Europe. Furthermore, the company has facilities in China, Australia, Mexico, India, Singapore, Central America, Thailand and South Africa.

McCormick conducts its business through two segments – Consumer and Flavor Solutions.

The **Consumer Business** segment offers spices, herbs, extracts, seasoning blends, sauces, marinades, and specialty foods to the consumer food market. This segment primarily caters to retail outlets like grocery, mass merchandise, warehouse clubs and discount and drug stores.

The division markets its products under brand names like McCormick, Lawry's, Zatarain's, Thai Kitchen, Simply Asia and Club House in the U.S.; and Ducros, Vahine, Schwartz and Kamis in Europe; and the Middle East and Africa (EMEA). In Asia-Pacific, the primary brand is McCormick, while in India the company has a joint venture with Kohinoor.



Sales from the Consumer Business segment formed nearly 65% of the company's top line in fiscal 2019.

The **Flavor Solutions** segment sells seasoning blends, natural spices and herbs, wet flavors, coating systems, and compound flavors to food manufacturers and food service customers. The products are sold through distributors.

Sales from the Flavor Solutions segment formed nearly 35% of the company's top line in fiscal 2019.



Reasons To Sell:

▼ **Stock Underperforms, Looks Overvalued:** McCormick's shares have underperformed the industry in the past three months. The stock came under pressure after the company posted fourth-quarter fiscal 2019 results, wherein both top and bottom lines missed the Zacks Consensus Estimate and management issued a not so impressive view for fiscal 2020. Consequently, shares of the company have lost 2.5% in a month. Although the stock has gained 3% in the past three months, it has underperformed the industry's rise of 3.5%. Further, considering price-to-earnings (P/E) ratio, McCormick looks pretty overvalued when compared with the industry as well as the S&P 500 over a year. The stock has a trailing 12-month P/E ratio of 30.59X. The trailing 12-month P/E ratio for the industry and the S&P 500 is 18.97X and 20.49X, respectively.

Currency volatility is a headwind for McCormick. This, along with higher taxes put pressure on the company's results in the fourth quarter of fiscal 2019.

▼ **Soft Q4 Earnings & Guidance:** McCormick posted fourth-quarter fiscal 2019 results, wherein both top and bottom lines came below the Zacks Consensus Estimate, with earnings breaking its three-quarter long positive surprise trend. Also, the bottom line declined year over year. Adjusted earnings of \$1.61 per share dropped 3.6% on a year-over-year basis and missed the Zacks Consensus Estimate of \$1.63. The decline was accountable to the unfavorable tax rate.

For fiscal 2020, though management expects sales to drive the underlying business' performance, the same is likely to be negatively impacted by increased investments related to business transformation and higher expected tax rate. Also, the company anticipates mid-single-digit cost inflation in fiscal 2020, though it is likely to be cushioned by pricing and cost-saving efforts. Adjusted earnings for fiscal 2020 are projected to be \$5.20-\$5.30 per share compared with \$5.24 reported in fiscal 2019.

▼ **Currency Volatility a Worry:** The company remains exposed to volatile foreign currency translations, as it has a widespread global business and undertakes business expansion efforts frequently. Evidently, adverse currency movements were a drag on McCormick's top line in all quarters of fiscal 2019. Clearly, volatility in exchange rates is a threat to the company's performance.

▼ **Intense Competition:** McCormick operates in the highly competitive food industry. The company mainly competed 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.

Risks

- **CCI Program Boosts Margins:** McCormick focuses on saving costs and enhancing productivity through its ongoing Comprehensive Continuous Improvement (CCI) program. Started in 2009, McCormick's CCI program has helped the company to focus on reducing costs and enhancing productivity. It has used CCI savings to increase investments, thereby leading to higher sales and profits. Notably, McCormick achieved cost-savings of \$119 million in fiscal 2019, courtesy of the CCI program. Taking this into account, the company has realized savings of \$463 million since fiscal 2016, exceeding its four-year goal of \$400 million.

Notably, cost savings from CCI boosted adjusted operating income in all quarters of fiscal 2019. During the fourth quarter, the metric advanced 3% year on year (up 4% at constant currency). Further, adjusted operating income margin expanded 40 basis points (bps) in the said quarter. Moreover, the CCI program also supported gross-margin growth in the quarter, which expanded 120 bps. To top it, adjusted operating margin increased 80 bps in fiscal 2019. The company expects to achieve cost savings of nearly \$105 million in fiscal 2020, which will be utilized for enhancing margins, sponsoring growth-oriented investments and offsetting high costs.

- **Product Innovation & Shift toward Healthy Products:** McCormick regularly enhances products through innovation to remain competitive and tap the evolving demand for new flavors, spices and herbs. Aided by a sturdy brand image, McCormick enjoys strong retail acceptance for its new products. Notably, the company's performance in fiscal 2019 gained from new products along with advancement in the base business. In fact, new products are boosting the company's performance across some key market locations of the company, such as the Americas and Asia-Pacific regions.

Further, McCormick focusses on product launches to boost revenue prospects. We note that in February 2019, McCormick entered into a partnership with IBM to boost artificial intelligence capabilities surrounding new product development. Additionally, the company is on track to augment marketing support for the new array of products. Apart from this, the company remains well aligned with consumer demand for flavorful healthy eating and has developed a range of natural and organic offerings. Moreover, the company has relaunched the Flavor Real platform to introduce organic, non-GMO and better-for-you products.

- **Expansion through Acquisitions:** McCormick has strategically increased its presence through acquisitions to grow its spices and seasonings portfolio. McCormick's acquisition of the food division of RB Foods, a British consumer products company, in August 2017, is the largest deal for the company till date. With iconic brands like Frank's RedHot Hot Sauce and French's Mustard, French's Crispy Vegetables and Cattlemen's BBQ Sauce, RB Foods is likely to continue being a profitable asset for McCormick's spices portfolio. Notably, Frank's RedHot and French's Mustard hold noteworthy positions in the United States and Canada. As a result, these brands position the company in the leading U.S. condiments category and place it well for international expansion. Moreover, the company's new products under these banners have been doing well.

Some of the other noteworthy acquisitions of the company are Italy-based Enrico Giotti SpA (Dec 2016) as well as Australia-based Botanical Food Company (April 2016). These takeovers have led to augmenting portfolio strength. Management expects to continue exploring acquisition opportunities as such moves are a vital part of the company's long-term growth strategies.

- **Strong Cash Flows & Shareholder-friendly Moves:** McCormick generated cash flow from operations of \$946.8 million in fiscal 2019, which marked a 15% rise from the previous year. Also, fiscal 2019 represented McCormick's eighth consecutive year of record cash flow from operations. The company's robust cash flow has been helping it lower debt burden and reward shareholders. Notably, the company announced a 9% hike in its quarterly dividend at the end of fiscal 2019, which marked its 34th straight year of dividend hike.
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Last Earnings Report

McCormick Q4 Earnings & Sales Miss Estimates

McCormick posted fourth-quarter fiscal 2019 results. Adjusted earnings of \$1.61 per share dropped 3.6% on a year-over-year basis and missed the Zacks Consensus Estimate of \$1.63. The decline was accountable to the unfavorable tax rate. A rise in adjusted operating profit failed to compensate for the decline.

This global leader of flavors and spices generated sales of \$1,484.8 million that inched up roughly 1% year over year, including currency headwinds of roughly 1%. On a constant-currency (or cc) basis, sales rose 2%. McCormick's top-line growth was driven by improvements in both segments. However, sales fell short of the Zacks Consensus Estimate of \$1,511 million.

Gross margin expanded 120 basis points (bps) to 42.4% on savings from the Comprehensive Continuous Improvement (CCI) program.

Adjusted operating income increased 3% to \$303 million and rose 4% at cc. Further, the adjusted operating margin expanded 40 bps to 20.4%. The upside can be attributable to improved sales and gross margin. This was somewhat countered by a planned increase in investments toward brand marketing.

Notably, McCormick achieved cost-savings of \$119 million in fiscal 2019, courtesy of the CCI program. This also helped the company see adjusted operating margin growth of 80 bps in the fiscal. Taking this into account, the company has realized savings of \$463 million since fiscal 2016, exceeding its four-year goal of \$400 million.

Segment Details

Consumer Business: Sales grew 1% to \$966.6 million and rose 2% at cc on the back of strength in the Americas and the Asia Pacific. Sales in the Americas rose 2% at cc. This was mainly driven by solid U.S. branded improvements. Sales in the Asia-Pacific region rose 3% at cc, courtesy of efficient pricing and holiday-season promotions. In the EMEA region, sales dipped 1% at cc mainly due to soft sales of private-label products.

Flavor Solutions: Sales in the segment climbed 2% from the prior-year quarter's \$518.2 million. At cc, sales rose 3% year over year, backed by strength in all regions. Sales in the Americas advanced 3% at cc, owing to growth in the base business, contributions from new products and sustained momentum in the snacks seasoning and branded foodservice categories. Sales in the EMEA region improved 5% at cc, driven by volume growth and favorable product mix. Sales in the Asia-Pacific region improved 2% at cc, owing to sales to quick-service restaurants.

Financial Update

McCormick exited the quarter with cash and cash equivalents of \$155.4 million, long-term debt of \$3,625.8 million and shareholders' equity of \$3,456.7 million. For fiscal 2019, net cash provided by operating activities was \$946.8 million. McCormick's net debt-to-adjusted EBITDA ratio stood at 3.4x at the end of fiscal 2019.

Fiscal 2020 Guidance

For fiscal 2020, McCormick anticipates consumer demand to continue witnessing global growth. Management is focused on catering to consumers' demands through effective brand marketing, product launches and extended distribution. While management expects sales to drive the underlying business performance, the same is likely to be negatively impacted by increased investments related to business transformation and higher expected tax rate. Excluding the impact of these factors, underlying growth is expected to be strong in fiscal 2020.

The company expects sales growth of 2-4%. It anticipates achieving top-line growth completely on an organic basis, as it envisions no benefits from acquisitions. That said, sales are likely to be driven by product launches, and expanded distribution and marketing. Also, strong pricing is expected to drive sales.

In fact, management anticipates pricing and cost-saving efforts to help the company counter an expected mid-single-digit cost inflation in fiscal 2020. Incidentally, the company expects to achieve cost savings of nearly \$105 million in fiscal 2020, which will be utilized for enhancing margins, sponsoring growth-oriented investments and offsetting high costs.

Quarter Ending **11/2019**

Report Date	Jan 28, 2020
Sales Surprise	-1.76%
EPS Surprise	-1.23%
Quarterly EPS	1.61
Annual EPS (TTM)	5.35

Recent News

McCormick Announces Dividends – Sep 24, 2019

McCormick's board announced quarterly dividend of 57 cents per share, payable on Oct 21 to shareholders of record as of Oct 7.

Valuation

McCormick shares are up 33.9% over the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Consumer Staples sector are up 9.1% and 11.2%, respectively in the past year.

The S&P 500 index is up 20.1% in the past year.

The stock is currently trading at 29.53X forward 12-month earnings, which compares to 18.17X for the Zacks sub-industry, 19.39X for the Zacks sector and 18.8X for the S&P 500 index.

Over the past five years, the stock has traded as high as 31.98X and as low as 19.38X, with a 5-year median of 23.32X. Our Underperform recommendation indicates that the stock will perform worse than the market. Our \$140 price target reflects 24.98X forward 12-month earnings.

The table below shows summary valuation data for MKC

Valuation Multiples - MKC					
		Stock	Sub-Industry	Sector	S&P 500
P/E F12M	Current	29.53	18.17	19.39	18.8
	5-Year High	31.98	22.9	22.38	19.34
	5-Year Low	19.38	14.82	16.66	15.18
	5-Year Median	23.32	19.28	19.71	17.45
P/S F12M	Current	3.98	1.72	9.89	3.49
	5-Year High	4.26	2.05	11.13	3.49
	5-Year Low	2.11	1.44	8.09	2.54
	5-Year Median	2.67	1.81	9.88	3
EV/EBITDA F12M	Current	21.86	14.08	34.39	12.66
	5-Year High	22.49	16.59	37.23	12.66
	5-Year Low	11.54	11.67	29.38	9.08
	5-Year Median	15.71	13.27	33.54	10.78

As of 01/30/2020

Industry Analysis Zacks Industry Rank: Top 43% (109 out of 255)



Top Peers

Post Holdings, Inc. (POST)	Outperform
Conagra Brands Inc. (CAG)	Neutral
Campbell Soup Company (CPB)	Neutral
Flowers Foods, Inc. (FLO)	Neutral
General Mills, Inc. (GIS)	Neutral
Ingredion Incorporated (INGR)	Neutral
The J. M. Smucker Company (SJM)	Neutral
TreeHouse Foods, Inc. (THS)	Neutral

Industry Comparison Industry: Food - Miscellaneous				Industry Peers		
	MKC Underperform	X Industry	S&P 500	CPB Neutral	POST Outperform	THS Neutral
VGM Score	D	-	-	C	B	B
Market Cap	22.00 B	4.36 B	23.91 B	14.79 B	7.52 B	2.51 B
# of Analysts	6	3	13	6	4	5
Dividend Yield	1.50%	0.12%	1.77%	2.86%	0.00%	0.00%
Value Score	F	-	-	C	B	A
Cash/Price	0.01	0.04	0.04	0.00	0.14	0.02
EV/EBITDA	23.87	13.31	14.07	15.02	15.72	16.62
PEG Ratio	3.91	2.26	2.00	3.25	3.05	1.70
Price/Book (P/B)	6.36	2.65	3.27	11.84	2.65	1.39
Price/Cash Flow (P/CF)	25.11	13.17	13.48	12.93	10.38	6.53
P/E (F1)	31.29	18.72	18.76	19.35	21.32	16.82
Price/Sales (P/S)	4.11	1.33	2.61	1.67	1.32	0.49
Earnings Yield	3.20%	5.14%	5.32%	5.16%	4.69%	5.94%
Debt/Equity	1.05	0.62	0.72	5.37	2.41	1.29
Cash Flow (\$/share)	6.59	2.72	6.88	3.79	10.24	6.83
Growth Score	B	-	-	C	A	C
Hist. EPS Growth (3-5 yrs)	11.05%	5.08%	10.68%	-0.30%	37.17%	-10.27%
Proj. EPS Growth (F1/F0)	-1.09%	6.88%	7.73%	10.14%	1.63%	11.67%
Curr. Cash Flow Growth	7.80%	2.50%	12.29%	-12.42%	5.71%	-61.72%
Hist. Cash Flow Growth (3-5 yrs)	9.17%	7.12%	8.78%	0.50%	34.52%	10.92%
Current Ratio	0.72	1.57	1.23	0.60	2.65	1.49
Debt/Capital	51.19%	38.38%	43.16%	84.30%	70.64%	56.27%
Net Margin	13.14%	2.79%	11.59%	2.07%	2.19%	-7.65%
Return on Equity	21.00%	11.54%	17.38%	64.48%	11.90%	5.80%
Sales/Assets	0.52	1.17	0.54	0.66	0.49	0.92
Proj. Sales Growth (F1/F0)	2.64%	2.41%	4.05%	-12.90%	4.95%	0.98%
Momentum Score	C	-	-	F	F	C
Daily Price Chg	-1.13%	0.00%	-0.21%	1.43%	0.99%	0.84%
1 Week Price Chg	2.37%	-0.50%	-1.09%	1.60%	-2.48%	-2.57%
4 Week Price Chg	-1.21%	-1.10%	-0.01%	1.11%	-2.31%	-5.88%
12 Week Price Chg	3.17%	2.17%	4.14%	5.62%	0.35%	-8.81%
52 Week Price Chg	33.86%	14.37%	17.24%	38.39%	14.59%	-23.53%
20 Day Average Volume	827,828	168,090	1,824,613	1,991,127	407,450	272,829
(F1) EPS Est 1 week change	-4.77%	0.00%	0.00%	0.00%	-0.25%	0.00%
(F1) EPS Est 4 week change	-4.57%	0.00%	0.00%	-0.11%	-2.67%	0.38%
(F1) EPS Est 12 week change	-6.29%	-1.21%	-0.11%	0.73%	-6.20%	-6.44%
(Q1) EPS Est Mthly Chg	-0.56%	0.00%	0.00%	1.62%	-4.19%	-5.06%

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	F
Growth Score	B
Momentum Score	C
VGM Score	D

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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