

Procter & Gamble Co. (PG)

\$121.63 (As of 03/05/20)

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

Long Term: 6-12 Months

Zacks Recommendation:

Outperform

(Since: 10/24/19)

Prior Recommendation: Neutral

Short Term: 1-3 Months

Zacks Rank: (1-5)

2-Buy

Zacks Style Scores:

VGM:D

Value: D

Growth: B

Momentum: F

Summary

Shares of Procter & Gamble have outpaced the industry in the past year. The company's solid second-quarter fiscal 2020 earnings mark the continuation of its positive surprise trend. Further, earnings and sales improved year over year in the reported quarter on gains from productivity efforts, robust volume, favorable mix and pricing. Total productivity cost savings aided core currency-neutral gross and operating margin by 120 bps and 220 bps, respectively. Further, it delivered adjusted free cash flow productivity of 100%. Backed by strong organic sales growth, core earnings and returns to shareholders in the fiscal second quarter, the company raised its view for fiscal 2020. However, currency fluctuations remain concerning. Nevertheless, gains from acquisitions and divestitures are likely to partly offset the currency headwinds.

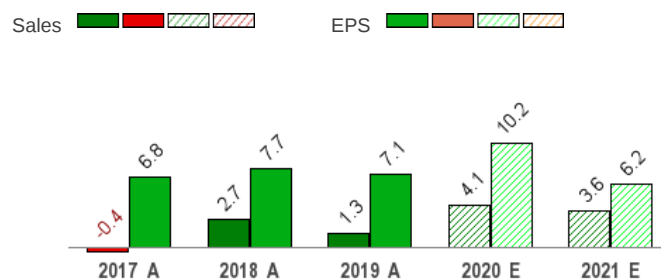
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$128.09 - \$97.75
20 Day Average Volume (sh)	8,289,439
Market Cap	\$300.4 B
YTD Price Change	-2.6%
Beta	0.45
Dividend / Div Yld	\$2.98 / 2.5%
Industry	Soap and Cleaning Materials
Zacks Industry Rank	Top 32% (82 out of 255)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	3.7%
Last Sales Surprise	-0.5%
EPS F1 Est- 4 week change	-0.2%
Expected Report Date	04/28/2020
Earnings ESP	-2.8%
P/E TTM	24.6
P/E F1	24.4
PEG F1	3.5
P/S TTM	4.3

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	18,374 E	18,854 E	17,467 E	18,050 E	72,965 E
2020	17,798 A	18,240 A	16,933 E	17,451 E	70,455 E
2019	16,690 A	17,438 A	16,462 A	17,094 A	67,684 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$1.43 E	\$1.48 E	\$1.20 E	\$1.20 E	\$5.29 E
2020	\$1.37 A	\$1.42 A	\$1.10 E	\$1.09 E	\$4.98 E
2019	\$1.12 A	\$1.25 A	\$1.06 A	\$1.10 A	\$4.52 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 03/05/2020. The reports text is as of 03/06/2020.

Overview

Headquartered in Cincinnati, OH, The Procter & Gamble Company, also referred to as Procter & Gamble or P&G, is a branded consumer products company which markets its products in more than 180 countries primarily through mass merchandisers, grocery stores, membership club stores, drug stores, department stores, distributors, baby stores, specialty beauty stores, e-commerce, high frequency stores and pharmacies. It has operations in approximately 70 countries. The company has five reportable segments:

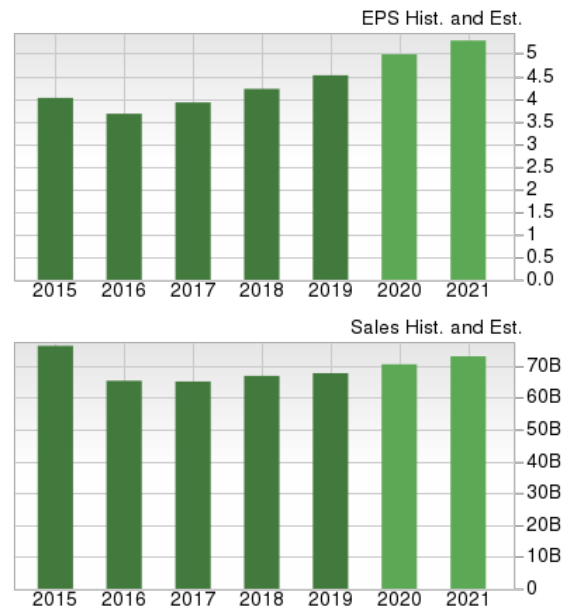
Beauty (18.7% of Q4 fiscal 2019 revenues): The segment includes hair care products (conditioner, shampoo, styling aids treatments) antiperspirants and deodorants as well as products for personal cleansing and skin care. Billion Dollar Brands include Head & Shoulders, Olay, Pantene, Old Spice, Safeguard, and SK-II. In Oct 2016, P&G completed its last major step in portfolio transformation with the Beauty Brands divestiture to Coty Inc.

Grooming (9.3%): The segment includes Shave Care products like female and male blades & razors and pre- and post-shave products as well as appliances. Billion Dollar Brands under this segment include Fusion, Gillette, Prestobarba and Mach3.

Health Care (11.9%): The segment includes gastrointestinal, rapid diagnostics, respiratory, vitamins/minerals/supplements and other personal health care product categories along with toothbrush, toothpaste and other oral care, product categories. Billion Dollar Brands include Crest, Oral-B and Vicks.

Fabric and Home Care (33.1%): The segment includes air care, dish care, fabric enhancers, laundry additives and detergents, P&G Professional and surface care product categories. Billion Dollar Brands under this segment are Ariel, Dawn, Downy, Febreze, Gain and Tide. P&G completed sale of its Duracell (Batteries) business to Berkshire Hathaway in exchange for Berkshire's equity stake in P&G in Feb 2016.

Baby, Feminine and Family Care (26.3%): The segment includes baby wipes, diapers and pants, paper towels, tissues, toilet paper, adult incontinence and feminine care products. Billion Dollar Brands include Always, Bounty, Charmin and Pampers.



Reasons To Buy:

▲ **Q2 Performance Strong, Outlook Upbeat:** Shares of Procter & Gamble have gained 23.5% in the past year, compared with the industry's growth of 17.5%. The outperformance is mainly attributed to the company's robust earnings trend and a raised view for fiscal 2020. The company reported bottom-line beat in second-quarter fiscal 2020, marking the continuation of its positive surprise trend for more than a couple of years. Moreover, earnings and sales improved on a year-over-year basis. Results primarily gained from productivity efforts, robust shipment volume, favorable mix and pricing. Organic sales benefited 1% each from increased pricing and favorable mix. The company's mix benefited from strong organic sales growth in the Health Care segment as well as Skin and Personal Care categories, which have higher than company average selling prices. Notably, all of the company's segments contributed to organic sales growth.

Driven by strong organic sales growth, core earnings and returns to shareholders, the company raised its view for fiscal 2020. It now expects growth of 4-5% in organic sales and 8-11% in core EPS.

Backed by strong organic sales growth, core earnings and returns to shareholders in the fiscal second quarter, the company raised its view for fiscal 2020. It now projects all-in and organic sales growth of 4-5% compared with 3-5% mentioned earlier. Moreover, it now projects core EPS growth of 8-11% for fiscal 2020 compared with 5-10% mentioned earlier.

▲ **Cost Savings and Productivity Program Aid Margins:** Procter & Gamble remains focused on productivity and cost-saving plans to boost margins. The company's continued investment in business alongside efforts to offset macro cost headwinds and balance top and bottom-line growth underscores its productivity efforts. With cost savings and efficiency improvements across all facets of business, it has crossed the mid-point of its second five-year (fiscal 2017-2021) cost-saving target of \$10 billion. The second five-year restructuring plan targets cutting costs in areas including supply chain and cost of goods sold (COGS), marketing and digitization and promotional spend effectiveness. This plan comprises \$7 billion in COGS savings (\$4.5 billion from raw and packaging materials, \$1.5 billion in manufacturing savings and \$1 billion from transportation/warehousing/other); \$2 billion of marketing cost reductions; \$1.5 billion of trade spending savings (10% efficiency); and \$1-\$2 billion of additional overhead reductions. This brings the total potential savings to \$12-\$13 billion, higher than the \$10 billion level. However, P&G adjusted the level down to up to \$10 billion to take into account the uncertainty associated with operations, especially when projecting out several years.

Notably, the company's core currency-neutral gross and operating margins reflected significant gains from productivity savings and pricing in second-quarter fiscal 2020. In the reported quarter, core gross margin (on a currency-neutral basis) expanded 210 basis points (bps), backed by 120-bps gain from productivity savings, 40 bps of pricing gains, 70 bps from commodity cost declines and 20 bps of other benefits. The uptick was partly offset by unfavorable product mix. Core currency-neutral operating margin expanded 190 bps in the quarter, including 220 bps of total productivity cost savings.

▲ **Improving Product Portfolio:** P&G focuses on improving its product portfolio through strategic initiatives, which enable it to concentrate on its fast-growing businesses. For this, the company relies on its strategy of acquiring complementary businesses. In a bid to boost its women's care portfolio, it recently agreed to acquire a growing female body care company – Billie Inc. The transaction is likely to be complementary to P&G's existing female grooming portfolio, which includes the Venus, Braun and Joy brands. The company expects to benefit by combining its strong digital and direct-to-consumer marketing capabilities and a growing range of personal care products with the fresh, digitally-native brand, which appeals to Millennial and Gen Z consumers. Further, P&G expects Billie's high-quality, naturals-focused razors and body care products to make its portfolio more dynamic. Some of its other acquisitions include the beauty brand – First Aid Beauty, producer of period products with natural ingredients – This is L., the consumer health business of Germany-based Merck KGaA and Walker & Company Brands. These acquisitions should bolster the company's product portfolio in various categories.

The company also follows a systematic divestiture plan to streamline its portfolio. It has divested several assets over the years as part of portfolio reshaping plan. The most prominent divestitures are sale of four product categories comprising 41 beauty brands to Coty, its snacks unit – Pringles; the bleach business in Italy and Portugal and the Braun household appliances business; and sale of the remaining global bleach businesses.

▲ **Strong Free Cash Flows & Shareholder Returns:** Procter & Gamble generates strong free cash flow annually. Cash flow provides management the opportunity to invest in product innovations, acquisitions and brand development in addition to regularly paying dividends and repurchasing shares. Notably, the company generated operating cash flow of \$4.4 billion in the fiscal second quarter, while adjusted free cash flow productivity was 100%. Furthermore, the company returned nearly \$5.4 billion of cash to its shareholders. This included dividend payments worth \$1.9 billion and share buybacks of \$3.5 billion. For fiscal 2020, the company increased its view for adjusted free cash flow productivity to 100% from 95% stated earlier. It anticipates paying out more than \$7.5 billion in dividends and repurchasing \$7-\$8 billion of common shares in fiscal 2020. Earlier, the company had anticipated repurchasing shares worth \$6-\$8 billion.

Risks

- **Valuation Looks Stretched:** Considering price-to-earnings (P/E) ratio, Procter & Gamble looks overvalued when compared with the industry and the S&P 500. The stock has a trailing 12-month P/E ratio of 24.6x, which is below the median level of 25.2x and the high level of 27.5x scaled in the past year. On the contrary, the trailing 12-month P/E ratio for the industry is 20.8x and the S&P 500 is 19.5x. Given these factors, we believe that the stock is stretched from the P/E aspect.
 - **Currency Headwinds:** Procter & Gamble's significant international presence exposes it to foreign currency risks, which have been weighing on the company's performance. Apparently, currency fluctuations hurt net sales and core earnings per share to the tune of about 1% each and core gross margin by 10 bps in second-quarter fiscal 2020. For fiscal 2020, management projects witnessing modest impact of adverse foreign currency on all-in sales growth.
 - **Slowdown of Global Economies:** Procter & Gamble remains vulnerable to global economic challenges, which may impact its revenues, profits and cash flows. A global economic slowdown can reduce the personal disposable income of consumers, which in turn, will decrease the company's sales volumes as consumers move toward cheaper alternatives. Further, it may force the company to shift its product mix to lower-margin products, thereby impacting margins. Management stated that it is likely to continue facing challenges from a volatile macro and geopolitical environment.
 - **Competitive Pressure:** Procter & Gamble faces intense competition from other well-established players in the consumer products industry, such as Colgate-Palmolive, Clorox, and Church & Dwight on the basis of pricing, promotional activities and new product introductions. The failure to offer exclusive high-quality products at competitive prices may hamper the company's market share.
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Last Earnings Report

Procter & Gamble Beats on Q2 Earnings, Sales Miss

Procter & Gamble reported second-quarter fiscal 2020 results, wherein earnings per share surpassed the Zacks Consensus Estimate. However, sales missed the consensus mark. Nonetheless, earnings and sales improved on a year-over-year basis. Moreover, the company raised its guidance for fiscal 2020.

Procter & Gamble's core earnings of \$1.42 per share improved 14% year over year and outpaced the Zacks Consensus Estimate of \$1.37. Meanwhile, currency-neutral core earnings per share (EPS) grew 15%.

The company reported net sales of \$18,240 million, improving 4.6% year over year. However, sales missed the Zacks Consensus Estimate of \$18,339 million. Currency fluctuations hurt the top line by one percentage point.

Quarter Ending **12/2019**

Report Date	Jan 23, 2020
Sales Surprise	-0.54%
EPS Surprise	3.65%
Quarterly EPS	1.42
Annual EPS (TTM)	4.95

Sales in Detail

On an organic basis (excluding the impact of acquisitions, divestitures and foreign exchange), revenues grew 5% based on 3% rise in organic shipment volume. Further, organic sales benefited 1% each from increased pricing and favorable mix. The company mix benefited from strong organic sales growth in the Health Care segment as well as Skin and Personal Care categories, which have higher than company average selling prices.

Moreover, all of the company's business segments reported organic sales growth. Organic sales improved 8% for the Beauty segment, 4% for Grooming, 7% for Health Care, 5% for Fabric & Home Care, and 1% for the Baby, Feminine and Family Care segment.

Net sales at Beauty, Grooming, Health Care, Fabric & Home Care, and Baby, Feminine and Family Care segments grew 7%, 2%, 14%, 4% and 1%, respectively.

Margins

In the reported quarter, core gross margin increased 200 basis points (bps) year over year to 51.6%, including nearly 10 bps of adverse impact of foreign currency. On a currency-neutral basis, core gross margin expanded 210 bps, backed by gains from productivity savings, higher pricing, commodity cost declines and other benefits. This uptick was partly offset by unfavorable product mix.

Core and currency-neutral selling, general and administrative expenses (SG&A), as a percentage of sales, increased 20 bps to 26.9%. The increase was driven by higher marketing investments, inflation, digital investments, incentive compensation costs and other impacts. However, these were partly negated by savings from overhead and marketing expenses, and sales leverage benefit.

Moreover, core and currency-neutral operating margin expanded 190 bps to 24.7%, driven by 220 bps of total productivity cost savings.

Financials

Procter & Gamble ended the reported quarter with cash and cash equivalents of \$6,279 million, long-term debt of \$18,985 million, and total shareholders' equity of \$45,908 million.

Cash flow from operating activities amounted to \$8,533 million for the first half of fiscal 2020, with operating cash flow of \$4.4 billion in the fiscal second quarter. Moreover, adjusted free cash flow productivity was 100%.

Furthermore, the company returned \$5.4 billion of cash to its shareholders in the fiscal second quarter. This included dividend payments worth \$1.9 billion and share buybacks of \$3.5 billion.

For fiscal 2020, the company increased its view for adjusted free cash flow productivity to 100% from 95% stated earlier. It anticipates paying out more than \$7.5 billion in dividends and repurchasing \$7-\$8 billion of common shares in fiscal 2020. Earlier, the company had anticipated repurchasing shares worth \$6-\$8 billion.

Fiscal 2020 Guidance

Backed by strong organic sales growth, core earnings and returns to shareholders in the fiscal second quarter, Procter & Gamble raised its view for fiscal 2020. The company now projects all-in and organic sales growth of 4-5% compared with 3-5% mentioned earlier. The guidance includes a modest impact of adverse foreign currency, which is likely to be mostly offset by slight gain from acquisitions and divestitures.

Moreover, the company now projects core EPS growth of 8-11% for fiscal 2020 compared with 5-10% mentioned earlier. In fiscal 2019, it reported core earnings of \$4.52 per share.

Recent News

Procter & Gamble Announces Dividend – Jan 15, 2020

Procter & Gamble announced a quarterly dividend of 74.59 cents per share, which is payable on Feb 18, 2020, to shareholders of record on Jan 24.

Procter & Gamble's Billie Buyout to Boost Grooming Portfolio – Jan 9, 2020

Procter & Gamble remains keen on boosting its women's care portfolio. In sync with this, the company intends to buy a growing female body care company – Billie Inc. – for an undisclosed amount. Billie is a subscription-oriented direct-to-consumer brand, catering to women's beauty and grooming needs. The company offers quality shaving products and a premium body care range. Its portfolio comprises razors, shaving cream, body wash and body lotion.

The transaction is likely to be complementary to P&G's existing female grooming portfolio, which includes the Venus, Braun and Joy brands. The company expects to benefit by combining its strong digital and direct-to-consumer marketing capabilities and a growing range of personal care products with the fresh, digitally-native brand, which appeals to Millennial and Gen Z consumers. Further, P&G expects Billie's high-quality, naturals-focused razors and body care products to make its portfolio more dynamic.

Following the acquisition, Billie's co-founders, Georgina Gooley and Jason Bravman, will continue to lead the brand's operations.

As for Billie, the brand will benefit from P&G's strong presence and ability to create global household brands. It expects P&G's strong brand-building capabilities to help create a stronger brand for women.

In all, this combination is expected to further strengthen P&G's grooming business and boost Billie.

Valuation

Procter & Gamble shares are down 2.3% in the year-to-date period but up 23.4% for the trailing 12-month period. Stocks in the Zacks sub-industry are up 1.7% but the Zacks Consumer Staples sector is down 4% in the year-to-date period. Over the past year, the Zacks sub-industry and sector are up 17.5% and 6.6%, respectively.

The S&P 500 index is down 3% in the year-to-date period but up 12.6% in the past year.

The stock is currently trading at 23.43X forward 12-month earnings, which compares to 22.57X for the Zacks sub-industry, 19.03X for the Zacks sector and 17.89X for the S&P 500 index.

Over the past five years, the stock has traded as high as 25.46X and as low as 16.02X, with a 5-year median of 21.09X. Our Outperform recommendation indicates that the stock will perform better than the market. Our \$140 price target reflects 26.97X forward 12-month earnings.

The table below shows summary valuation data for PG

Valuation Multiples - PG					
		Stock	Sub-Industry	Sector	S&P 500
P/E F12M	Current	23.43	22.57	19.03	17.89
	5-Year High	25.46	23.53	22.38	19.34
	5-Year Low	16.02	17.89	16.66	15.18
	5-Year Median	21.09	21.07	19.68	17.46
P/S F12M	Current	4.16	2.69	9.55	3.3
	5-Year High	4.41	2.72	11.13	3.43
	5-Year Low	2.6	1.94	8.09	2.54
	5-Year Median	3.38	2.33	9.88	3.01
EV/EBITDA TTM	Current	16.9	12.41	35.87	10.93
	5-Year High	20.54	14.61	45.75	12.88
	5-Year Low	11.41	9.26	31.94	8.49
	5-Year Median	14.28	10.97	38.84	10.79

As of 03/05/2020

Industry Analysis Zacks Industry Rank: Top 32% (82 out of 255)



Top Peers

Church & Dwight Co., Inc. (CHD)	Neutral
Colgate-Palmolive Company (CL)	Neutral
The Clorox Company (CLX)	Neutral
Coty Inc. (COTY)	Neutral
The Estee Lauder Companies Inc. (EL)	Neutral
Helen of Troy Limited (HELE)	Neutral
Henkel AG & Co. (HENKY)	Neutral
Unilever PLC (UL)	Neutral

Industry Comparison Industry: Soap And Cleaning Materials				Industry Peers		
	PG Outperform	X Industry	S&P 500	CHD Neutral	CL Neutral	UL Neutral
VGM Score	D	-	-	C	C	A
Market Cap	300.36 B	56.93 B	22.29 B	18.43 B	61.85 B	67.53 B
# of Analysts	9	7.5	13	11	8	3
Dividend Yield	2.45%	2.19%	1.97%	1.28%	2.38%	3.09%
Value Score	D	-	-	D	D	B
Cash/Price	0.02	0.04	0.05	0.01	0.02	0.09
EV/EBITDA	34.15	18.16	13.20	19.97	17.88	NA
PEG Ratio	3.52	3.42	1.94	3.35	4.05	2.66
Price/Book (P/B)	6.68	6.30	3.05	6.90	111.11	4.34
Price/Cash Flow (P/CF)	21.24	15.41	12.16	23.46	21.83	7.61
P/E (F1)	24.42	23.49	17.58	28.05	24.25	19.09
Price/Sales (P/S)	4.32	3.82	2.45	4.23	3.94	NA
Earnings Yield	4.09%	4.27%	5.69%	3.56%	4.12%	5.24%
Debt/Equity	0.42	0.68	0.70	0.68	13.14	NA
Cash Flow (\$/share)	5.86	3.45	7.01	3.26	3.45	7.68
Growth Score	B	-	-	B	C	A
Hist. EPS Growth (3-5 yrs)	3.75%	6.81%	10.85%	11.40%	0.54%	NA
Proj. EPS Growth (F1/F0)	10.27%	5.18%	6.26%	8.28%	5.39%	4.97%
Curr. Cash Flow Growth	4.72%	1.11%	6.03%	12.70%	-4.58%	-5.80%
Hist. Cash Flow Growth (3-5 yrs)	-0.93%	4.28%	8.52%	9.63%	-1.27%	4.28%
Current Ratio	0.63	0.87	1.23	0.88	1.03	0.78
Debt/Capital	29.26%	40.42%	42.57%	40.42%	92.93%	NA
Net Margin	6.92%	12.14%	11.69%	14.13%	15.08%	NA
Return on Equity	27.14%	25.65%	16.66%	24.16%	1,906.25%	NA
Sales/Assets	0.60	0.89	0.54	0.67	1.12	NA
Proj. Sales Growth (F1/F0)	4.09%	3.34%	3.94%	6.41%	4.60%	5.16%
Momentum Score	F	-	-	C	B	D
Daily Price Chg	5.36%	4.51%	3.75%	4.67%	5.00%	4.36%
1 Week Price Chg	-10.63%	-9.67%	-12.06%	-9.25%	-11.41%	-9.67%
4 Week Price Chg	-1.82%	-1.82%	-7.42%	2.98%	-0.48%	-3.09%
12 Week Price Chg	-0.13%	-0.13%	-4.61%	10.19%	11.73%	-2.10%
52 Week Price Chg	25.85%	10.00%	7.38%	17.00%	14.88%	9.20%
20 Day Average Volume	8,276,390	1,334,987	2,456,671	1,562,938	4,846,979	1,107,036
(F1) EPS Est 1 week change	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
(F1) EPS Est 4 week change	-0.18%	0.00%	-0.06%	0.00%	0.04%	0.00%
(F1) EPS Est 12 week change	0.83%	-0.91%	-0.41%	-0.61%	0.21%	-2.26%
(Q1) EPS Est Mthly Chg	-1.12%	-0.56%	-0.27%	0.00%	0.00%	NA

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	B
Momentum Score	F
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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