

## WestRock Company (WRK)

**\$29.84** (As of 08/05/20)

Price Target (6-12 Months): **\$34.00**

Long Term: 6-12 Months

**Zacks Recommendation:** **Outperform**

(Since: 08/04/20)

Prior Recommendation: Neutral

Short Term: 1-3 Months

**Zacks Rank:** (1-5)

**3-Hold**

Zacks Style Scores:

VGM:A

Value: A

Growth: C

Momentum: B

### Summary

WestRock's third-quarter fiscal 2020 earnings beat the Zacks Consensus Estimate, while sales missed the same. Both bottom- and top-line figures declined year on year. Strong demand for e-commerce amid the coronavirus-induced crisis is aiding the company. WestRock's consumer packaging business is gaining from sustainable packaging options as well as significant demand in food, food service, and beverage packaging categories. Corrugated packaging business is poised to gain from improved box shipment as well as increased demand from distribution, industrial and agricultural customers as the economy gradually recovers. Moreover, the company is taking steps to align supply with demand and framed a Pandemic Action Plan to drive savings. Acquisitions and investments backed by a solid balance sheet will aid growth.

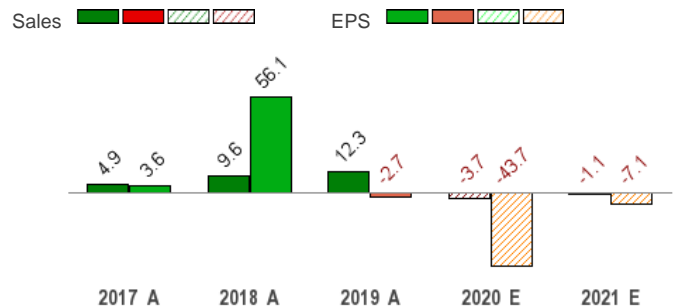
### Price, Consensus & Surprise



### Data Overview

|                            |  |
|----------------------------|--|
| 52 Week High-Low           | \$44.39 - \$21.50                          |
| 20 Day Average Volume (sh) | 2,596,014                                  |
| Market Cap                 | \$7.7 B                                    |
| YTD Price Change           | -30.5%                                     |
| Beta                       | 1.44                                       |
| Dividend / Div Yld         | \$0.80 / 2.7%                              |
| Industry                   | <a href="#">Paper and Related Products</a> |
| Zacks Industry Rank        | Bottom 16% (213 out of 253)                |

### Sales and EPS Growth Rates (Y/Y %)



|                           |            |
|---------------------------|------------|
| Last EPS Surprise         | 72.7%      |
| Last Sales Surprise       | -2.8%      |
| EPS F1 Est- 4 week change | 0.6%       |
| Expected Report Date      | 11/05/2020 |
| Earnings ESP              | 10.7%      |

### Sales Estimates (millions of \$)

|      | Q1      | Q2      | Q3      | Q4      | Annual*  |
|------|---------|---------|---------|---------|----------|
| 2021 | 4,308 E |         |         |         | 17,416 E |
| 2020 | 4,424 A | 4,447 A | 4,236 A | 4,427 E | 17,612 E |
| 2019 | 4,327 A | 4,620 A | 4,690 A | 4,652 A | 18,289 A |

### EPS Estimates

|      | Q1       | Q2       | Q3       | Q4       | Annual*  |
|------|----------|----------|----------|----------|----------|
| 2021 | \$0.38 E |          |          |          | \$2.08 E |
| 2020 | \$0.58 A | \$0.67 A | \$0.76 A | \$0.62 E | \$2.24 E |
| 2019 | \$0.83 A | \$0.80 A | \$1.11 A | \$1.24 A | \$3.98 A |

\*Quarterly figures may not add up to annual.

|         |      |
|---------|------|
| P/E TTM | 9.2  |
| P/E F1  | 13.3 |
| PEG F1  | 3.0  |
| P/S TTM | 0.4  |

The data in the charts and tables, including the Zacks Consensus EPS and Sales estimates, is as of 08/05/2020. The reports text is as of 08/06/2020.

## Overview

WestRock was formed as a result of the merger between MeadWestvaco Company and Rock-Tenn Company on Jul 1, 2015. Headquartered in Norcross, GA, WestRock is a multinational provider of paper and packaging solutions for consumer and corrugated packaging markets. The company is one of the largest integrated producers of containerboard by tons produced, and one of the largest producers of high-graphics preprinted linerboard on the basis of net sales in North America. It is also one of the largest paper recyclers in North America.

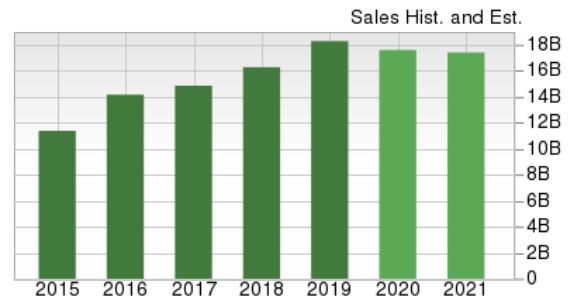
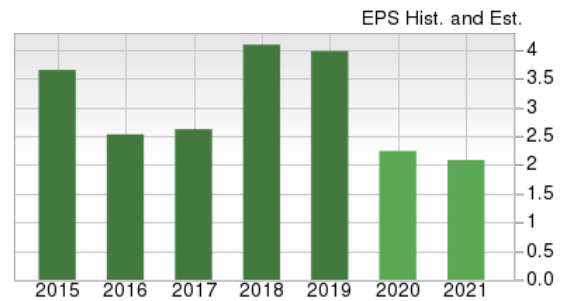
The company's operations outside the United States are conducted through subsidiaries located in Canada, Mexico, South America, Europe, Asia and Australia. Sales from non-U.S. operations accounted for 18.2% of net sales in fiscal 2019.

WestRock reports financial results in the following reportable segments:

**Corrugated Packaging Segment** (64.2% of total sales in fiscal 2019) operates an integrated corrugated packaging system that manufactures primarily containerboard, corrugated sheets, corrugated packaging and preprinted linerboard for sale to consumer, and industrial products manufacturers and corrugated box manufacturers. The full range of high-quality corrugated containers is designed to protect, ship, store and display products in accordance to customers' merchandising and distribution specifications. It converts corrugated sheets into corrugated products ranging from one-color protective cartons to graphically brilliant point-of-purchase packaging.

**Consumer Packaging Segment** (35.7% of total sales in fiscal 2019) operates integrated virgin and recycled fiber paperboard mills along with operations which convert items such as folding and beverage cartons, displays and interior partitions. The folding and beverage cartons are used to package items such as food, paper, beverages, dairy products, tobacco, confectionery, health and beauty and other household consumer, commercial and industrial products primarily for retail sale.

**Land and Development Segment** (0.1% of total sales in fiscal 2019) is responsible for maximizing the value of the various real estate holdings concentrated in the Charleston, SC region. The company expects the monetization of these holdings to be completed by fiscal 2020.



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## Reasons To Buy:

- ▲ During fiscal 2018 and 2019, the company completed acquisitions of Schlüter, Plymouth Packaging and rival KapStone Paper and Packaging Corp that expanded its product offerings and geographic presence. The integration of KapStone Paper, the most notable acquisition among these, is on track. The company anticipates cost synergies and performance improvements of more than \$200 million by the end of fiscal 2021. WestRock has already achieved \$150 million of cumulative KapStone run-rate synergies and performance improvements through Jun 30, 2020. KapStone's corrugated packaging operations will enhance WestRock's North American corrugated packaging business and provide complementary products. The acquisition will help the company strengthen presence in Western United States and to compete better in the growing agricultural markets in the region. It also fast-tracks its target to improve margins of its North American corrugated packaging business. The company continues to evaluate potential acquisitions in the future.
- ▲ E-commerce demand remains strong across all channels and momentum will continue, particularly on account of the restrictions imposed to stem the spread of the coronavirus pandemic. WestRock's corrugated packaging business is poised to gain from improved box shipment, as well as increased demand from distribution, industrial and agricultural customers as the economy gradually recovers. Consumer packaging business is gaining from sustainable packaging options as well as significant demand in food, food service, and beverage packaging categories owing to the pandemic. Notably, this category represents 59% consumer packaging revenue.
- ▲ As of Jun 30, 2020, the company had more than \$3.2 billion of availability under its long-term committed credit facilities and cash and cash equivalents. Total debt was \$10.1 billion at Jun 30, 2020. Debt payable within a year is around \$213 million and the company has around \$505 million of bonds payable until 2022. Further, in June, the company issued \$600 million in 13-year bonds to boost liquidity. In the fiscal third quarter, the company generated more than \$500 million of adjusted free cash flow while investing in strategic capital projects. Moreover, WestRock's Pandemic Action Plan is expected to generate around \$1 billion in cash, which will be utilized toward debt reduction through fiscal 2021. The company is on track to generate more than \$350 million from this plan in the current fiscal. It is also well positioned to fulfill its debt obligations.
- ▲ During first-half fiscal 2020, WestRock invested \$616 million in capital expenditures. The company has reduced fiscal 2020 capital expenditures to \$950 million from the prior guidance of \$1.1 billion. This includes \$350 million for strategic capital projects at Florence, SC and TresBarras, Brazil mills. The company expects to start the Florence paper mill later this year and complete the TresBarras mill upgrade in the first half of fiscal 2021. Once completed, these projects are expected to contribute to the company's EBITDA. WestRock had announced that it is reconfiguring its North Charleston, SC, paper mill to improve the long-term competitiveness of the mill. The move is expected to increase the company's annual EBITDA by approximately \$40 million, primarily owing to the reduction in operating costs from the shutdown of the paper machine and its associated infrastructure. It will also reduce linerboard capacity by approximately 288,000 tons and help balance supply with customer demand.
- ▲ In the wake of the uncertainty imposed by the coronavirus outbreak, WestRock is taking steps to align supply with demand and formulated a Pandemic Action Plan. The company has decreased salaries and retainers up to 25% for its senior executive team and board of directors. It is also trimming discretionary expenses. The company expects to use company stock to pay its annual incentive and company funded 401(k) contributions in 2020. It plans to lower capital investments. Further, per the recently enacted Coronavirus Aid, Relief, and Economic Security ("CARES") Act, employers can postpone paying their share of employment taxes incurred through the end of calendar year 2020. WestRock expects to postpone an estimated \$120 million of such payments over the next three quarters and will be required to pay 50% of these amounts in December 2021 and the remaining 50% in December 2022. WestRock has also slashed annual dividend payout to 80 cents per share from the prior \$1.86 per share. These actions will likely help contribute an additional \$1 billion in cash.

WestRock is poised well on strong demand for food, beverage, household cleaning and e-commerce. A solid balance sheet, investment in growth projects and KapStone acquisition will drive growth.

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## Risks

- The pandemic has disrupted demand patterns across few of WestRock's businesses. Demand in foodservice impacted by uncertainty in timing of reopening of restaurants, schools and other services. Commercial print demand is also likely to be restrained due to limited public events and reduced retail and direct mail advertising. Luxury goods and industrial products have also been hit hard. This will continue until the situation stabilizes. Further, resurgence of COVID-19 cases in many markets has created uncertainties. Based on these current market trends, WestRock expects fourth fiscal quarter's adjusted segment EBITDA to be slightly lower than the fiscal third quarter.
  - WestRock noted that end markets are changing quickly and recycled fiber costs have gone up dramatically. Recycled fiber costs have gone up more than \$50 per ton since December while other input costs have gone down. However, the company expects recycled fiber cost to be approximately \$25 per ton lower than the average in the fiscal third quarter. In the fiscal fourth quarter, the company plans to take 112,000 tons of maintenance downtime. This will impact margins in the quarter.
  - The folding carton markets remain challenged by weak primary demand for processed, frozen, and dry foods. This is in line with the ongoing consumer preference for fresh foods and the shrinking center of the supermarket. Moreover, demand for carbonated drinks continues to remain weak, particularly in North America.
  - In the consumer packaging segment, Specialty SBS paperboard for tobacco, commercial print and liquid packaging accounts for about 10% of the segment sales. The segment is bearing the brunt of bleak demand in commercial print business. Volume declines in commercial print and tobacco have declined more than 20% since fiscal 2016. Also, pulp and other business which accounts for 4% of the segment sales continue to be negatively impacted by low global pulp prices. These factors continue to impact the segment.
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## Last Earnings Report

### WestRock's Earnings Beat Estimates in Q3, Down Y/Y

WestRock delivered third-quarter fiscal 2020 adjusted earnings of 76 cents per share, surpassing the Zacks Consensus Estimate of 44 cents. However, earnings plunged 31.5% from the prior-year quarter.

Including one-time items, the company reported earnings per share of 69 cents in the reported quarter, down 29.6% from the prior-year quarter.

Quarter Ending **06/2020**

| Report Date      | Aug 04, 2020 |
|------------------|--------------|
| Sales Surprise   | -2.77%       |
| EPS Surprise     | 72.73%       |
| Quarterly EPS    | 0.76         |
| Annual EPS (TTM) | 3.25         |

### Operational Update

WestRock's total revenues slid 9.7% year over year to \$4,236 million. Moreover, the revenue figure missed the Zacks Consensus Estimate of \$4,357 million.

Cost of sales was down 6.3% year over year to \$3,466 million in the fiscal third quarter. Gross profit declined 22.1% year over year to \$770 million. Gross margin came in at 18% compared with the 21% reported in the prior-year period. Adjusted segment EBITDA was \$708 million compared with the \$858 million witnessed in the year-earlier quarter. Total segment income was around \$323 million, down from the year-ago quarter's \$485 million.

### Segmental Performance

Corrugated Packaging: Sales in the segment dipped 11.2% year over year to \$2,729 million in the June-end quarter primarily on lower corrugated selling price/mix, lower volumes, and unfavorable impact of the coronavirus pandemic and foreign currency. Adjusted segment EBITDA decreased 25.2% year over year to \$482 million.

Consumer Packaging: Sales in the segment were down 5.8% year over year to \$1,553 million. This downside resulted from lower selling price/mix, dismal volumes, and unfavorable impact of the pandemic and foreign-currency translation. Adjusted segment EBITDA climbed 4.3% year over year to \$243 million.

### Financial Position

As of Jun 30, 2020, cash and cash equivalents were \$292 million, significantly up from \$152 million as of Sep 30, 2019. As of Jun 30, 2020, total debt was \$10.1 billion, unchanged compared with total debt as of Sep 30, 2019. Cash flow from operations was \$740 million during the fiscal third quarter compared with the year-earlier quarter's \$735 million. WestRock invested \$244 million in capital expenditure and paid out \$52 million in dividends in the reported quarter.

WestRock is focused on meeting customer demand and executing strategies for financial strength and substantial liquidity to counter the pandemic-related setbacks.

## Valuation

WestRock's shares are down 30.4% in the year-to-date period and 14.2% over the trailing 12-month period. Stocks in the Zacks Paper and Related Products industry and the Zacks Basic Materials sector are down 22.5% and up 1.5% in the year-to-date period, respectively. Over the past year, the Zacks sub-industry are down 8.1% while the sector are up 10.8%.

The S&P 500 index is up 3.3% in the year-to-date period and 15.7% in the past year.

The stock is currently trading at 14.41X forward 12-month earnings, which compares with 9.33X for the Zacks sub-industry, 16.02X for the Zacks sector and 22.58X for the S&P 500 index.

Over the past five years, the stock has traded as high as 22.17X and as low as 6.66X, with a five-year median of 13.46X. Our Outperform recommendation indicates that the stock will perform better than the market. Our \$34 price target reflects 16.41X Forward 12-month earnings.

The table below shows summary valuation data for WRK:

| Valuation Multiples - WRK |               |       |              |        |         |
|---------------------------|---------------|-------|--------------|--------|---------|
|                           |               | Stock | Sub-Industry | Sector | S&P 500 |
| P/E F12M                  | Current       | 14.41 | 9.33         | 16.02  | 22.58   |
|                           | 5-Year High   | 22.17 | 13.89        | 21.05  | 22.58   |
|                           | 5-Year Low    | 6.66  | 4.15         | 9.86   | 15.25   |
|                           | 5-Year Median | 13.46 | 10.61        | 13.51  | 17.55   |
| EV/EBITDA TTM             | Current       | 5.89  | 4.93         | 10.19  | 12.8    |
|                           | 5-Year High   | 33.59 | 14.57        | 17.94  | 12.85   |
|                           | 5-Year Low    | 5.07  | 4.49         | 6.55   | 8.24    |
|                           | 5-Year Median | 8.79  | 7.61         | 10.72  | 10.89   |
| P/B TTM                   | Current       | 0.67  | 4.46         | 2.77   | 4.54    |
|                           | 5-Year High   | 3.64  | 6.73         | 3.07   | 4.56    |
|                           | 5-Year Low    | 0.48  | 1.5          | 1.23   | 2.83    |
|                           | 5-Year Median | 1.1   | 2.31         | 2.2    | 3.73    |

As of 08/05/2020

## Industry Analysis Zacks Industry Rank: Bottom 16% (213 out of 253)



## Top Peers

| Company (Ticker)                       | Rec          | Rank |
|--|--------------|------|
| Clearwater Paper Corporation (CLW)     | Outperform   | 2    |
| International Paper Company (IP)       | Neutral      | 3    |
| Packaging Corporation of America (PKG) | Neutral      | 3    |
| Domtar Corporation (UFS)               | Neutral      | 3    |
| Veritiv Corporation (VRTV)             | Neutral      | 4    |
| Mercer International Inc. (MERC)       | Underperform | 5    |
| Neenah Paper, Inc. (NP)                | Underperform | 5    |
| Verso Corporation (VRS)                | Underperform | 5    |

| Industry Comparison Industry: Paper And Related Products |            |            |           | Industry Peers |         |          |
|--|------------|------------|-----------|----------------|---------|----------|
|  | WRK        | X Industry | S&P 500   | IP             | PKG     | UFS      |
| Zacks Recommendation (Long Term)                         | Outperform | -          | -         | Neutral        | Neutral | Neutral  |
| Zacks Rank (Short Term)                                  | 3          | -          | -         | 3              | 3       | 3        |
| VGM Score  | A          | -          | -         | A              | B       | B        |
| Market Cap   | 7.74 B     | 765.19 M   | 22.93 B   | 13.99 B        | 9.09 B  | 1.20 B   |
| # of Analysts  | 7          | 1          | 14        | 6              | 7       | 4        |
| Dividend Yield   | 2.68%      | 0.00%      | 1.76%     | 5.76%          | 3.30%   | 8.38%    |
| Value Score  | A          | -          | -         | A              | B       | B        |
| Cash/Price   | 0.09       | 0.11       | 0.07      | 0.06           | 0.09    | 0.13     |
| EV/EBITDA  | 5.49       | 6.23       | 13.16     | 6.72           | 7.49    | 5.11     |
| PEG Ratio  | 2.95       | 10.13      | 2.99      | NA             | 3.69    | NA       |
| Price/Book (P/B)   | 0.66       | 1.17       | 3.20      | 1.98           | 2.89    | 0.55     |
| Price/Cash Flow (P/CF)                                   | 3.02       | 5.74       | 12.45     | 4.54           | 7.98    | 2.59     |
| P/E (F1)   | 13.32      | 15.34      | 21.78     | 15.34          | 18.45   | NA       |
| Price/Sales (P/S)  | 0.44       | 0.66       | 2.47      | 0.66           | 1.35    | 0.23     |
| Earnings Yield   | 7.51%      | 3.93%      | 4.33%     | 6.52%          | 5.41%   | -2.03%   |
| Debt/Equity  | 0.84       | 0.81       | 0.77      | 1.38           | 0.85    | 0.54     |
| Cash Flow (\$/share)                                     | 9.89       | 1.65       | 6.94      | 7.84           | 12.01   | 8.39     |
| Growth Score   | C          | -          | -         | B              | B       | B        |
| Hist. EPS Growth (3-5 yrs)                               | 10.46%     | 1.27%      | 10.46%    | 8.39%          | 14.75%  | 1.27%    |
| Proj. EPS Growth (F1/F0)                                 | -43.68%    | -36.97%    | -7.14%    | -47.63%        | -32.10% | -114.50% |
| Curr. Cash Flow Growth                                   | 9.85%      | -12.25%    | 5.47%     | -13.00%        | -3.69%  | -20.37%  |
| Hist. Cash Flow Growth (3-5 yrs)                         | 23.04%     | -1.80%     | 8.55%     | 2.55%          | 5.99%   | -5.05%   |
| Current Ratio  | 1.80       | 1.60       | 1.32      | 0.79           | 3.51    | 2.06     |
| Debt/Capital   | 45.62%     | 45.25%     | 44.59%    | 57.94%         | 45.88%  | 34.86%   |
| Net Margin   | 4.37%      | 0.06%      | 10.15%    | 2.98%          | 7.65%   | 0.18%    |
| Return on Equity   | 7.24%      | 4.50%      | 14.46%    | 19.18%         | 20.07%  | 4.08%    |
| Sales/Assets   | 0.58       | 0.71       | 0.51      | 0.64           | 0.93    | 1.04     |
| Proj. Sales Growth (F1/F0)                               | -3.70%     | 0.00%      | -1.68%    | -8.20%         | -6.11%  | -11.78%  |
| Momentum Score   | B          | -          | -         | A              | D       | D        |
| Daily Price Chg  | 1.95%      | 0.41%      | 0.59%     | 0.85%          | 0.51%   | 1.92%    |
| 1 Week Price Chg   | -11.09%    | -0.99%     | 0.14%     | -4.21%         | -6.49%  | -4.29%   |
| 4 Week Price Chg   | 8.63%      | 4.22%      | 5.31%     | 4.22%          | -0.47%  | 11.28%   |
| 12 Week Price Chg  | 23.51%     | 11.86%     | 19.84%    | 15.33%         | 6.75%   | 9.26%    |
| 52 Week Price Chg  | -14.23%    | -9.37%     | 2.73%     | -11.45%        | -4.62%  | -39.58%  |
| 20 Day Average Volume                                    | 2,596,014  | 119,616    | 2,098,555 | 2,658,739      | 726,569 | 870,761  |
| (F1) EPS Est 1 week change                               | 0.00%      | 0.00%      | 0.00%     | 13.68%         | -0.71%  | 0.00%    |
| (F1) EPS Est 4 week change                               | 0.64%      | 0.00%      | 1.10%     | 15.76%         | -1.38%  | 10.31%   |
| (F1) EPS Est 12 week change                              | -6.74%     | -6.74%     | 1.04%     | 8.22%          | -6.91%  | -825.00% |
| (Q1) EPS Est Mthly Chg                                   | 17.46%     | 0.00%      | 0.39%     | 12.03%         | 1.17%   | -3.57%   |

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## 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.

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### 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    | A |
| Growth Score   | C |
| Momentum Score | B |
| VGM Score      | A |

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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