

WestRock Company (WRK)

\$24.70 (As of 05/06/20)

Price Target (6-12 Months): **\$26.00**

Long Term: 6-12 Months

Zacks Recommendation:

Neutral

(Since: 09/02/19)

Prior Recommendation: Underperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

4-Sell

Zacks Style Scores:

VGM:A

Value: A

Growth: C

Momentum: A

Summary

WestRock's second-quarter fiscal 2020 adjusted earnings and revenues were both down year over year. However, the bottom line beat the Zacks Consensus Estimate while the top line missed the same. Amid the coronavirus pandemic, the company has witnessed strong growth in e-commerce and food, beverage, household cleaning and liquid packaging. However, demand in foodservice, commercial print, luxury goods and industrial products have been impacted. This is likely continue until the situation stabilizes. The acquisition of KapStone is likely to generate significant cost synergies and expand paper packaging product offerings in the days ahead. The company's pandemic action plan will help generate around \$1 billion in cash thorough fiscal 2021 and will be utilized to repay debt. Investment in growth will also drive results, going forward.

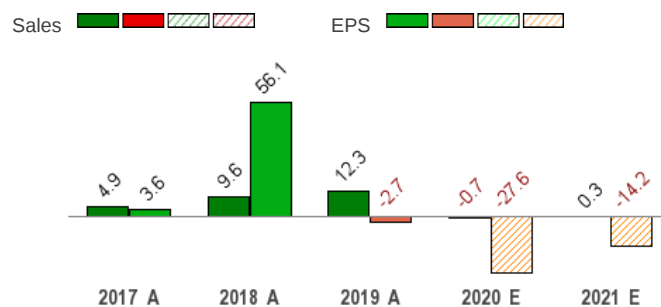
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$44.39 - \$21.50
20 Day Average Volume (sh)	2,802,983
Market Cap	\$6.4 B
YTD Price Change	-42.4%
Beta	1.56
Dividend / Div Yld	\$0.80 / 7.5%
Industry	Paper and Related Products
Zacks Industry Rank	Bottom 41% (149 out of 253)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	11.7%
Last Sales Surprise	-0.8%
EPS F1 Est- 4 week change	0.0%
Expected Report Date	08/06/2020
Earnings ESP	-28.8%
P/E TTM	6.9
P/E F1	8.6
PEG F1	1.9
P/S TTM	0.4

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	4,448 E				18,218 E
2020	4,424 A	4,447 A	4,618 E	4,635 E	18,162 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	\$0.48 E				\$2.47 E
2020	\$0.58 A	\$0.67 A	\$0.80 E	\$1.06 E	\$2.88 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.

The data in the charts and tables, including the Zacks Consensus EPS and Sales estimates, is as of 05/06/2020. The reports text is as of 05/07/2020.

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.

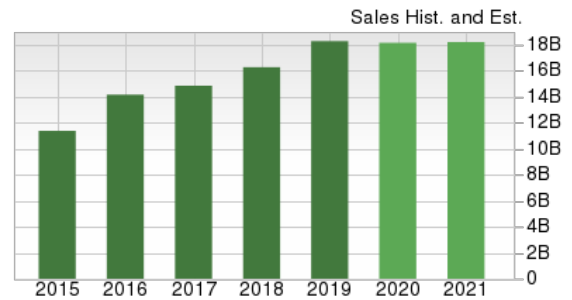
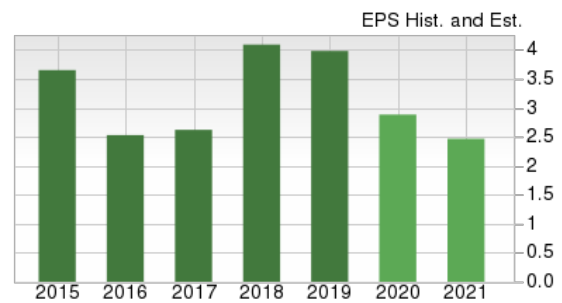
The company's operations outside the United States are conducted through subsidiaries located in Canada, Mexico, South America, Europe, Asia and Australia. Sales from non-U.S. operations accounted for 18.2% of net sales in fiscal 2019.

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.



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 more than \$125 million of cumulative KapStone run-rate synergies and performance improvements through Mar 31, 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 outbreak. Further, demand for packaging for food, beverage, household cleaning and liquid packaging will remain robust on the back of the coronavirus outbreak. This bodes well for WestRock.
- ▲ As of Mar 31, 2020, the company had more than \$2.5 billion of availability under its long-term committed credit facilities and cash and cash equivalents. Total debt was \$10.86 billion at Mar 31, 2020. Debt payable within a year is around \$432 million and the company has around \$505 million of bonds payable until 2022. Further, its U.S. qualified pension plan is overfunded and global cash contributions to its qualified plans in fiscal 2020 are \$10 million. 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 ended the quarter with net leverage ratio of 3.13x. WestRock's times interest earned ratio is 3.7, higher than the industry's 0.8. The company is 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 machine in second-half calendar 2020, and the TresBarras mill upgrade project should be concluded in second-quarter 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 is decreasing 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.

Reasons To Sell:

- ▼ The pandemic has disrupted demand patterns across few of WestRock's businesses. Demand in foodservice remains 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.
- ▼ WestRock has withdrawn fiscal 2020 guidance for net sales, adjusted EBITDA, adjusted cash flow and free cash flow citing the uncertainty associated with the COVID-19. The company noted that end markets are changing quickly and recycled fiber costs have gone up dramatically. The third-quarter fiscal 2020 results will reflect the flow-through of the published index reduction for liner board in January and the February reductions for SBS and recycled box board for grades. While other input costs have gone down, recycled fiber costs have gone up more than \$50 per ton since December. 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 13% of the segment sales. Volume declines in commercial print and tobacco have declined more than 20% since fiscal 2016. This continues to impact the segment.

Weak demand in some of its markets owing to the impact of the coronavirus pandemic is likely to impact WestRock's near-term results. Further, higher recycled fiber costs will dent margins.

Last Earnings Report

WestRock Beats on Q2 Earnings, Scraps '20 Guidance

WestRock delivered second-quarter fiscal 2020 adjusted earnings of 67 cents per share, surpassing the Zacks Consensus Estimate of 60 cents. However, earnings declined 16.2% from the prior-year quarter figure of 80 cents per share.

Including one-time items, the company reported earnings per share of 57 cents in the reported quarter, down 8% from the prior-year quarter's 62 cents.

Quarter Ending **03/2020**

Report Date	May 05, 2020
Sales Surprise	-0.84%
EPS Surprise	11.67%
Quarterly EPS	0.67
Annual EPS (TTM)	3.60

Operational Update

WestRock's total revenues slid 3.7% year over year to \$4,447 million. Moreover, the revenue figure missed the Zacks Consensus Estimate of \$4,485 million.

Cost of sales was down 2% year over year to \$3,643 million in the fiscal second quarter. Gross profit declined 10.5% year over year to \$805 million. Gross margin came in at 18.1% compared with the 19.5% reported in the prior-year period. Adjusted segment EBITDA was \$708 million compared with the \$757 million witnessed in the year-earlier quarter. Total segment income was around \$335 million, down from the year-ago quarter's \$396 million.

Segmental Performance

Corrugated Packaging: Sales in the segment dipped 3.6% year over year to \$2,883 million in the March-end quarter primarily due to lower corrugated selling price/mix and unfavorable impacts of foreign currency, partly offset by higher volumes. Adjusted segment EBITDA declined 9.2% year over year to \$502 million.

Consumer Packaging: Sales in the segment were down 3.1% year over year to \$1,616 million. This downside resulted from lower selling price/mix, dismal volumes and unfavorable foreign-currency translation impact. Adjusted segment EBITDA edged down 1.8% year over year to \$222 million.

Financial Position

As of Mar 31, 2020, cash and cash equivalents were \$640 million, significantly up from \$152 million as of Sep 30, 2019. As of Mar 31, 2020, total debt was \$10.8 billion, up from \$10.1 billion as of Sep 30, 2019. Cash flow from operations was \$168 million in the fiscal second quarter compared with the \$362 million reported in the year-earlier quarter. WestRock invested \$241 million in capital expenditure and paid out \$121 million in dividends in the reported quarter.

The company is executing strategies for financial strength and substantial liquidity to counter the pandemic-related setbacks. WestRock is decreasing salaries and retainers by up to 25% for the company's senior executive team and board of directors as well as reducing its discretionary expenses. The company is lowering capital investments by approximately \$150 million to \$950 million for fiscal 2020 while reducing capital investments to \$600-\$800 million for fiscal 2021. It will pay a quarterly dividend of 20 cents per share for an annual rate of 80 cents per share. WestRock expects to have an additional \$1 billion in cash available for debt reduction through fiscal 2021.

Suspends Guidance

The company has withdrawn the fiscal 2020 guidance for net sales, adjusted segment EBITDA, adjusted operating cash flow and adjusted free cash on the coronavirus pandemic-related concerns.

Valuation

WestRock's shares are down 39.7% over the trailing 12-month period. Stocks in the Zacks Paper and Related Products industry and the Zacks Basic Materials sector are down 26.5% and 15.4% over the past year.

The S&P 500 index has gone down 14.9% in the past year.

The stock is currently trading at 9.23X forward 12-month earnings, which compares with 7.36X for the Zacks sub-industry, 14.39X for the Zacks sector and 20.52X for the S&P 500 index.

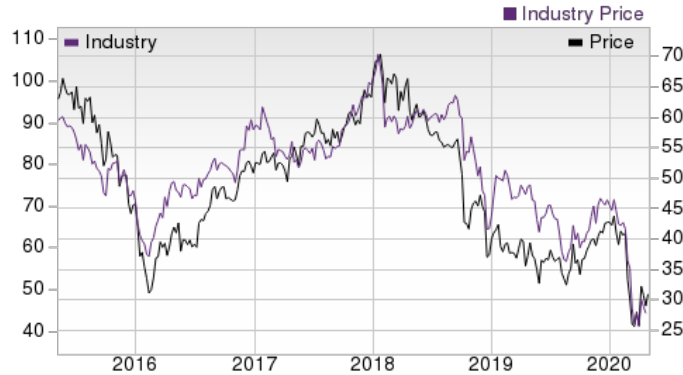
Over the past five years, the stock has traded as high as 24.70X and as low as 6.66X, with a five-year median of 13.63X. Our Neutral recommendation indicates that the stock will perform in-line with the market. Our \$26 price target reflects 9.72X Forward 12-month earnings.

The table below shows summary valuation data for WRK:

Valuation Multiples - WRK					
		Stock	Sub-Industry	Sector	S&P 500
P/E F12M	Current	9.23	7.36	14.39	20.52
	5-Year High	24.70	14.21	21.06	20.52
	5-Year Low	6.66	4.15	9.79	15.19
	5-Year Median	13.63	11.3	13.46	17.44
EV/EBITDA TTM	Current	5.37	8.38	8.4	10.44
	5-Year High	33.59	14.57	17.84	12.86
	5-Year Low	5.07	4.5	6.53	8.28
	5-Year Median	10.81	7.67	10.84	10.77
P/B TTM	Current	0.54	2.3	1.65	3.78
	5-Year High	3.74	6.73	3.57	4.55
	5-Year Low	0.48	1.5	1.22	2.84
	5-Year Median	1.19	2.3	2.17	3.64

As of 05/06/2020

Industry Analysis Zacks Industry Rank: Bottom 41% (149 out of 253)



Top Peers

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

Industry Comparison Industry: Paper And Related Products				Industry Peers		
	WRK	X Industry	S&P 500	IP	PKG	UFS
Zacks Recommendation (Long Term)	Neutral	-	-	Neutral	Neutral	Neutral
Zacks Rank (Short Term)	4	-	-	4	3	3
VGM Score	A	-	-	C	A	B
Market Cap	6.38 B	768.68 M	19.11 B	12.64 B	8.87 B	1.16 B
# of Analysts	6	1.5	14	4	6	5
Dividend Yield	7.53%	0.00%	2.2%	6.37%	3.38%	8.64%
Value Score	A	-	-	A	B	A
Cash/Price	0.02	0.09	0.06	0.09	0.09	0.05
EV/EBITDA	5.39	6.25	11.69	6.25	7.39	4.87
PEG Ratio	1.98	0.48	2.48	NA	3.35	NA
Price/Book (P/B)	0.56	1.06	2.58	1.84	2.88	0.50
Price/Cash Flow (P/CF)	2.50	4.81	10.40	4.10	7.79	2.51
P/E (F1)	8.94	16.06	18.81	15.36	16.75	351.17
Price/Sales (P/S)	0.35	0.46	1.97	0.57	1.28	0.22
Earnings Yield	11.66%	6.23%	4.99%	6.53%	5.97%	0.28%
Debt/Equity	0.91	0.79	0.75	1.44	0.87	0.42
Cash Flow (\$/share)	9.89	1.65	7.01	7.84	12.01	8.39
Growth Score	C	-	-	C	B	C
Hist. EPS Growth (3-5 yrs)	12.85%	5.23%	10.87%	10.27%	16.14%	5.23%
Proj. EPS Growth (F1/F0)	-27.56%	-26.68%	-9.86%	-52.71%	-27.06%	-98.00%
Curr. Cash Flow Growth	9.85%	-12.25%	5.88%	-13.00%	-3.69%	-20.37%
Hist. Cash Flow Growth (3-5 yrs)	23.04%	-3.82%	8.55%	2.55%	5.99%	-5.05%
Current Ratio	1.75	1.75	1.25	0.77	3.42	1.98
Debt/Capital	47.56%	44.06%	44.23%	58.95%	46.51%	29.77%
Net Margin	4.67%	2.32%	10.87%	2.99%	9.39%	1.61%
Return on Equity	7.98%	6.73%	16.36%	20.98%	22.63%	7.33%
Sales/Assets	0.59	0.74	0.55	0.65	0.97	1.05
Proj. Sales Growth (F1/F0)	-0.70%	0.00%	-2.18%	-4.40%	-2.56%	-9.62%
Momentum Score	A	-	-	D	B	C
Daily Price Chg	-1.44%	-0.90%	-1.27%	-2.81%	0.00%	-2.90%
1 Week Price Chg	6.79%	6.79%	0.53%	8.93%	10.19%	7.23%
4 Week Price Chg	-19.52%	-1.02%	0.68%	-2.87%	6.42%	-7.67%
12 Week Price Chg	-41.11%	-27.71%	-22.30%	-27.71%	-8.13%	-41.54%
52 Week Price Chg	-35.21%	-29.48%	-11.55%	-29.48%	-5.05%	-54.17%
20 Day Average Volume	2,802,983	114,875	2,470,143	3,871,048	783,449	564,060
(F1) EPS Est 1 week change	0.00%	0.00%	0.00%	-13.61%	2.17%	0.00%
(F1) EPS Est 4 week change	0.00%	0.00%	-6.52%	-17.19%	0.36%	-91.48%
(F1) EPS Est 12 week change	-11.28%	-24.20%	-14.84%	-29.51%	-10.39%	-97.09%
(Q1) EPS Est Mthly Chg	-8.75%	-14.68%	-12.48%	-19.36%	-8.57%	-261.36%

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	A
Growth Score	C
Momentum Score	A
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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