

WestRock Company (WRK)

\$26.61 (As of 03/09/20)

Price Target (6-12 Months): **\$29.00**

Long Term: 6-12 Months

Zacks Recommendation:

Neutral

(Since: 09/02/19)

Prior Recommendation: Underperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

3-Hold

Zacks Style Scores:

VGM:B

Value: A

Growth: C

Momentum: B

Summary

For fiscal 2020, WestRock expects adjusted EBITDA at \$3-\$3.2 billion. The mid-point reflects a year-over-year fall of 4% thanks to the impact of pricing declines, and ongoing inflation in wages and other cost categories. Consumer Packaging volumes are expected to rise 1% in fiscal 2020. However, this will be offset by lower prices and scheduled maintenance downtime. Earnings estimates for the current quarter and fiscal year have undergone negative revisions lately. Nevertheless, the acquisition of KapStone is likely to generate significant cost synergies and expand paper packaging product offerings in the days ahead. Productivity and performance improvement programs and cost-saving actions will likely continue to boost WestRock's margins. Focus on lowering debt levels and investment in growth will also drive results, going forward.

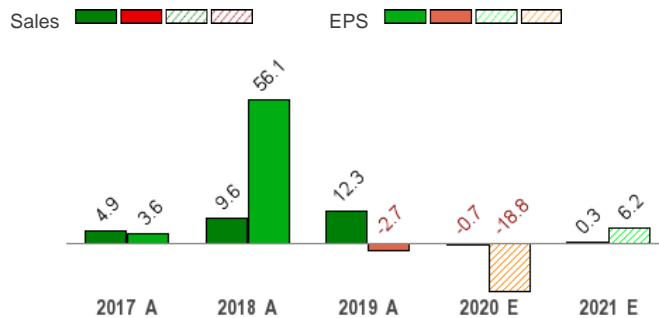
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$44.39 - \$26.32
20 Day Average Volume (sh)	2,935,506
Market Cap	\$6.9 B
YTD Price Change	-38.0%
Beta	1.75
Dividend / Div Yld	\$1.86 / 7.0%
Industry	Paper and Related Products
Zacks Industry Rank	Bottom 8% (234 out of 253)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	1.8%
Last Sales Surprise	2.2%
EPS F1 Est- 4 week change	-0.8%
Expected Report Date	05/05/2020
Earnings ESP	-6.9%

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	4,448 E				18,218 E
2020	4,424 A	4,485 E	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				\$3.43 E
2020	\$0.58 A	\$0.61 E	\$0.88 E	\$1.06 E	\$3.23 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	7.1
P/E F1	8.3
PEG F1	1.8
P/S TTM	0.4

The data in the charts and tables, including the Zacks Consensus EPS and Sales estimates, is as of 03/09/2020. The reports text is as of 03/10/2020.

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.

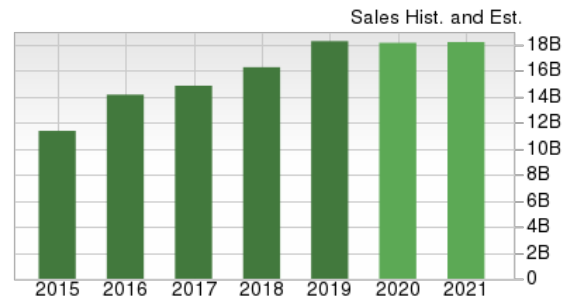
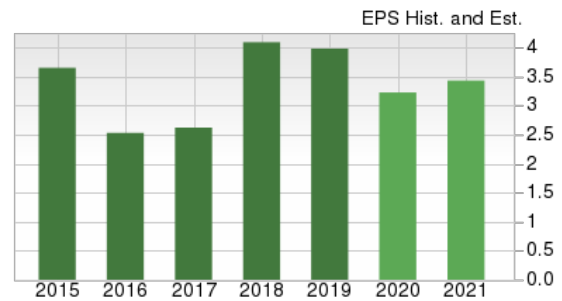
The company's operations outside the United States are conducted through subsidiaries located in Canada, Mexico, South America, Europe, Asia and Australia. Sales from non-U.S. operations accounted for 18.2% of net sales in fiscal 2019.

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:

- ▲ WestRock was formed by the merger of MeadWestvaco and Rock-Tenn in Jul 2015. WestRock is realizing the strategic benefits of the merger. The company has achieved its \$1 billion target for synergy and performance improvements which it had set at the inception of WestRock. This was achieved by the productivity and performance improvement programs across its manufacturing footprint, as well as cost savings from capital investments. Further, manufacturing optimization and reductions from the elimination of duplicate corporate costs and support functions will aid results.
- ▲ 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 \$110 million of cumulative KapStone run-rate synergies and performance improvements through Dec 31, 2019. 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.
- ▲ WestRock reported per-day organic box shipment growth of 2.5% in fiscal 2019, ahead of the industry's 0.5%. For fiscal 2020, box volumes are expected to be up 1-2% on a per day basis. In first-quarter fiscal 2020, North American Corrugated Packaging box shipment growth was noted at 4.5% on a per day basis aided by growth in e-commerce, processed food and protein. Consumer Packaging volumes are expected to be up 1% for the fiscal 2020.
- ▲ WestRock generated \$1.044 billion of adjusted free cash flow in fiscal 2019 — the fourth consecutive year of more than \$1 billion. The company projects adjusted free cash flow to be more than \$1 billion for the fifth consecutive year. The company paid out \$120 million in dividends in first-quarter fiscal 2020. As of Dec 31, 2019, the company had approximately 19.1 million shares available for repurchase under the program. In November 2019, WestRock announced an annual dividend hike of 2.2% to \$1.86 per share. The company ended the year with net leverage ratio of 3.0. WestRock retains target to lower its net leverage ratio to 2.25-2.50.
- ▲ During first-quarter fiscal 2020, WestRock invested \$375 million in capital expenditures. This includes \$132 million for strategic projects, including a new paper machine at its mill in Florence, SC and an upgrade of its mill in Brazil. The company has a capital expenditure target of \$1.1 billion in fiscal 2020 and \$900 million-\$1 billion in fiscal 2021. In fiscal 2019, WestRock completed strategic capital projects at its Porto Feliz corrugated box plant in Sao Paulo, Brazil, Cottonton, AL and Covington, VA mills. The projects to be completed this fiscal year include the Florence paper machine in the North Charleston mill. As these projects ramp up, they are expected to contribute an additional \$85 million in EBITDA at the end of the fiscal fourth quarter and a total of \$175 million in EBITDA by the end of fiscal 2021. The estimates are expected to go up once the Tres Barras upgrade is fully operational in fiscal 2022.
- ▲ WestRock 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.

Execution of its capital allocation strategy and investment in growth projects will aid growth. The KapStone acquisition will enhance corrugated packaging business and add complementary products.

Reasons To Sell:

- ▼ WestRock expects net sales at \$18.0-\$18.5 billion for fiscal 2020. The mid-point of the range reflects a year-over-year decline of 0.2%. The guidance reflects declines in North American container board and craft paper index pricing, and the full year impact of market pricing declines that have been witnessed in export container board, craft paper and market pulp. Adjusted EBITDA for the fiscal is anticipated in the range of \$3 billion to \$3.2 billion. Compared with the adjusted EBITDA of \$3.23 billion in fiscal 2018, the mid-point of the range reflects a year-over-year decline of 4%. This can be attributable to impact of pricing declines and ongoing inflation in wages, benefits and other non-commodity cost categories. Earnings in the first half of fiscal 2020 will be lower than the second half, owing to seasonal factors, the timing of scheduled mill maintenance outages and impact of strategic capital projects.
- ▼ For second-quarter fiscal 2020, the company has scheduled 118,000 tons of maintenance downtime in the Corrugated Packaging segment compared with 94,000 tons in the prior-year quarter. For the Consumer Packaging segment, maintenance downtime is estimated at 17,000 tons compared with the prior-year quarter figure of 54,000 tons. For second-quarter fiscal 2020, WestRock expects adjusted segment EBITDA between \$680 million and \$710 million. The company had reported adjusted EBITDA of \$757 million in second-quarter fiscal 2019. Seasonal volume increases across the Corrugated Packaging and Consumer Packaging segments will be offset by price reductions of \$10 per ton for domestic linerboard and \$15 per ton for domestic medium. Productivity improvements and lower sequential healthcare costs will be offset by higher sequential wage costs and the payroll tax reset that occurs at the beginning of each calendar year.
- ▼ 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.
- ▼ Energy is one of the primary costs of WestRock's mill operations. The cost of natural gas, coal, oil, electricity, diesel and wood by-products (biomass) at times have fluctuated significantly. WestRock spent around \$879 million on all energy sources in fiscal 2019 to operate facilities. Natural gas and electricity each accounted for approximately a third of its total energy purchases in fiscal 2019. In fiscal 2020, WestRock expects to consume approximately 84 million MMBtu of natural gas. Inbound and outbound freight is also a significant expenditure. The company experienced significantly higher freight costs in fiscal 2019, as transportation companies hiked prices to address shortage of drivers and strong demand. Higher energy and freight costs are likely to limit the company's margins.

Lower prices are likely to impact WestRock's results in fiscal 2020. Weak folding cartons market owing to lower consumer preference for processed & frozen food remains a headwind.

Last Earnings Report

WestRock Earnings and Revenues Surpass Estimates in Q1

WestRock Company has delivered first-quarter fiscal 2020 (ended Dec 31, 2019) adjusted earnings of 58 cents per share, surpassing the Zacks Consensus Estimate of 57 cents. However, earnings declined 30% from the prior-year quarter figure of 83 cents per share.

Including one-time items, the company reported earnings per share of 53 cents in the reported quarter, down 1.9% from the prior-year quarter's 54 cents.

Quarter Ending **12/2019**

Report Date	Jan 30, 2020
Sales Surprise	2.20%
EPS Surprise	1.75%
Quarterly EPS	0.58
Annual EPS (TTM)	3.73

Operational Update

WestRock's total revenues jumped 2.2% year over year to \$4,423.7 million. Moreover, the metric surpassed the Zacks Consensus Estimate of \$4,328.5 million.

The year-over-year improvement in total sales can primarily be attributed to an additional month of KapStone ownership in fiscal 2020, partially offset by lower corrugated and pulp prices, and lower consumer paperboard volumes.

Cost of sales improved 1.9% year over year to \$3,614.7 million in the first quarter of fiscal 2020. Gross profit advanced 1.5% year over year to \$1,081 million. Gross margin came in at 24.4% compared with 24.6% reported in the prior-year period. Adjusted segment EBITDA was \$675.3 million compared with the \$733.2 million reported in the prior-year quarter.

Total segment income was \$331 million, up from \$324 million witnessed in the year-ago quarter.

Segmental Performance

Corrugated Packaging: Sales in the segment improved 6.4% year over year to \$2,909.5 million in the reported quarter, backed by the KapStone acquisition, partly offset by lower volumes and prices. Adjusted segment EBITDA declined 4.8% year over year to \$507.6 million.

Consumer Packaging: Sales in the segment declined 5.1% year over year to \$1,536.9 million. The downside resulted from lower volumes and selling prices, and unfavorable foreign currency impact. Adjusted segment EBITDA was down 14.7% year over year to \$184.3 million.

Land and Development: The segment's sales were \$18.9 million compared with the year-earlier quarter's figure of \$13.9 million.

Financial Position

As of Dec 31, 2019, cash and cash equivalents were \$156.4 million, significantly down from \$260.7 million as of Dec 31, 2018. As of Dec 31, 2019, total debt was \$10.2 billion, up from \$10.1 billion as of Sep 30, 2019. Cash flow from operations was \$431 million in the reported quarter compared with \$303 million reported in the prior-year quarter.

WestRock invested \$375 million in capital expenditure and paid out \$120 million in dividends in the reported quarter.

WestRock has so far achieved more than \$110 million of its \$200-million targeted synergies from the acquisition of KapStone. WestRock remains focused on organic growth, productivity improvement, cash-flow generations and debt reduction.

Valuation

WestRock's shares are down 27.4% over the trailing 12-month period. Stocks in the Zacks Paper and Related Products industry and the Zacks Basic Materials sector are down 39.1% and 28.5% over the past year.

The S&P 500 index has declined 2.3% in the past year.

The stock is currently trading at 8.03X forward 12-month earnings, which compares with 5.41X for the Zacks sub-industry, 10.26X for the Zacks sector and 15.75X for the S&P 500 index.

Over the past five years, the stock has traded as high as 24.70X and as low as 7.59X, with a five-year median of 14.06X. Our Neutral recommendation indicates that the stock will perform in-line with the market. Our \$29 price target reflects 8.75X 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	8.03	5.41	10.26	15.75
	5-Year High	24.70	14.82	21.15	19.34
	5-Year Low	7.59	4.15	9.82	15.18
	5-Year Median	14.06	11.39	13.51	17.42
EV/EBITDA TTM	Current	5.74	11.16	8.05	11.04
	5-Year High	33.59	15.14	17.92	12.87
	5-Year Low	5.38	4.69	7.44	8.49
	5-Year Median	10.86	7.72	10.93	10.79
P/B TTM	Current	0.58	2.33	1.38	3.69
	5-Year High	3.74	6.73	3.54	4.56
	5-Year Low	0.58	1.5	1.34	2.85
	5-Year Median	1.22	2.32	2.17	3.63

As of 03/09/2020

Industry Analysis Zacks Industry Rank: Bottom 8% (234 out of 253)



Top Peers

Clearwater Paper Corporation (CLW)	Outperform
Neenah Paper, Inc. (NP)	Neutral
Verso Corporation (VRS)	Neutral
Veritiv Corporation (VRTV)	Neutral
International Paper Company (IP)	Underperform
Mercer International Inc. (MERC)	Underperform
Packaging Corporation of America (PKG)	Underperform
Domtar Corporation (UFS)	Underperform

Industry Comparison Industry: Paper And Related Products				Industry Peers		
	WRK Neutral	X Industry	S&P 500	IP Underperform	PKG Underperform	UFS Underperform
VGM Score	B	-	-	A	C	B
Market Cap	6.88 B	895.46 M	19.13 B	12.66 B	8.05 B	1.50 B
# of Analysts	6	1	13	6	5	5
Dividend Yield	6.99%	1.43%	2.26%	6.35%	3.72%	6.82%
Value Score	A	-	-	B	D	B
Cash/Price	0.02	0.06	0.05	0.04	0.09	0.04
EV/EBITDA	5.30	6.83	11.99	6.48	6.83	5.65
PEG Ratio	1.90	0.47	1.68	NA	2.80	NA
Price/Book (P/B)	0.58	0.98	2.64	1.64	2.62	0.64
Price/Cash Flow (P/CF)	2.69	4.37	10.70	4.12	7.08	3.20
P/E (F1)	8.57	11.43	15.44	10.48	14.01	20.98
Price/Sales (P/S)	0.37	0.47	2.05	0.57	1.16	0.29
Earnings Yield	12.10%	8.26%	6.47%	9.54%	7.14%	4.76%
Debt/Equity	0.81	0.81	0.70	1.28	0.87	0.42
Cash Flow (\$/share)	9.89	1.65	7.01	7.84	12.01	8.33
Growth Score	C	-	-	B	B	C
Hist. EPS Growth (3-5 yrs)	12.85%	5.23%	10.85%	11.46%	16.61%	5.23%
Proj. EPS Growth (F1/F0)	-18.97%	-13.41%	6.25%	-30.44%	-20.63%	-57.60%
Curr. Cash Flow Growth	9.85%	-13.89%	6.09%	-13.00%	-3.69%	-20.37%
Hist. Cash Flow Growth (3-5 yrs)	23.04%	-5.19%	8.52%	2.55%	5.99%	-5.05%
Current Ratio	1.44	1.66	1.24	0.77	3.42	1.98
Debt/Capital	44.91%	44.91%	42.57%	56.19%	46.51%	29.77%
Net Margin	4.69%	2.18%	11.69%	5.47%	10.00%	1.61%
Return on Equity	8.23%	7.21%	16.74%	23.49%	24.57%	7.33%
Sales/Assets	0.60	0.76	0.54	0.66	0.98	1.05
Proj. Sales Growth (F1/F0)	-0.70%	0.00%	3.76%	-3.54%	-2.90%	-3.70%
Momentum Score	B	-	-	B	C	D
Daily Price Chg	-11.54%	-8.63%	-7.65%	-9.61%	-6.32%	-7.10%
1 Week Price Chg	-9.53%	-1.80%	-0.67%	-3.38%	0.18%	-0.14%
4 Week Price Chg	-35.02%	-20.01%	-19.26%	-26.20%	-15.44%	-22.91%
12 Week Price Chg	-34.94%	-20.30%	-17.26%	-30.13%	-22.70%	-30.78%
52 Week Price Chg	-31.40%	-23.20%	-6.83%	-30.55%	-13.04%	-47.16%
20 Day Average Volume	2,935,506	91,480	2,684,709	2,947,377	911,178	1,047,514
(F1) EPS Est 1 week change	0.00%	0.00%	0.00%	0.00%	-2.48%	0.00%
(F1) EPS Est 4 week change	-0.77%	-3.33%	-0.06%	0.00%	-2.48%	-24.91%
(F1) EPS Est 12 week change	-3.87%	-5.28%	-0.46%	-16.41%	-11.44%	-48.00%
(Q1) EPS Est Mthly Chg	-1.92%	0.00%	-0.40%	0.00%	0.00%	16.67%

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	B

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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