
Confectionery & Snacks

Unwrapping the Potential and Digging into the Chocolate Numbers: A Delicious Analysis of The Hershey Company



This report was prepared by Adebowale Atere.

July 2023



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The Company and Industry Overview

The Hershey Company is a leading American multinational chocolate manufacturer that also produces baked goods, beverages, and other products. Operating under 80 brands in 70 countries, Hershey’s is a global leader in chocolate, sugar confectionery, and chocolate-related grocery products. The company prides itself on its values-driven approach to snacking, offering moments of goodness through its more than 90 brands and products. Hershey’s values include togetherness, integrity, making a difference, and excellence.

Hershey’s offers a wide variety of flavours, sizes, and variations of its products. Popular items include Hershey’s Milk Chocolate Bar, Hershey’s Special Dark Mildly Sweet Chocolate Bar, Hershey’s Air Delight Chocolate Bar, Hershey’s Milk Chocolate with Almonds Bar, Hershey’s Cookies ‘N’ Creme Bar, Hershey’s Drops, and Hershey’s Miniatures. The company sells its products to a diverse range of customers through various channels, including its own retail stores and online. With a wide range of products catering to different income and age groups, Hershey’s target market is essentially everyone.

The company manufactures and sells confectionery products and pantry items both domestically and internationally through three segments: North America Confectionery, North America Salty Snacks, and International (see figures 1 and 2).

The confectionery industry is highly competitive with major players such as Mars, Nestle, Mondelez International, Ferrero, Lindt & Sprüngli among others. In addition to its own brands, Hershey’s also distributes KitKat in the USA through a partnership with Nestle. Data shown below is using current exchange rates and reflects market impacts of the Russia-Ukraine war (see figures 3 -6).

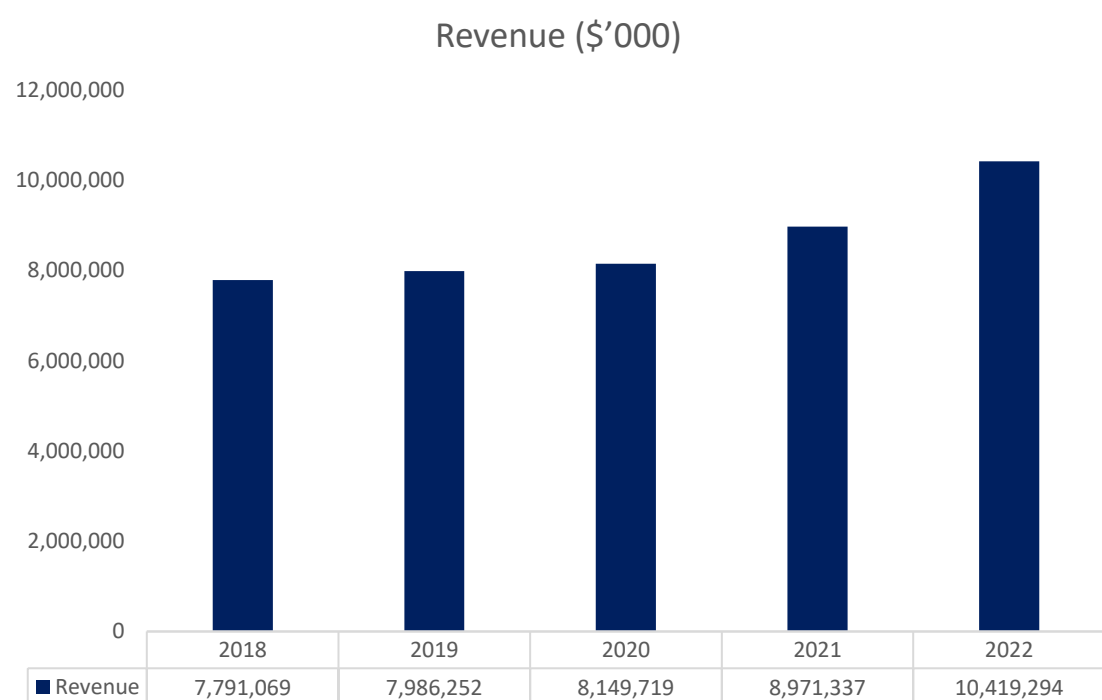


Figure 1 - Source: The Hershey Company Financial Statement

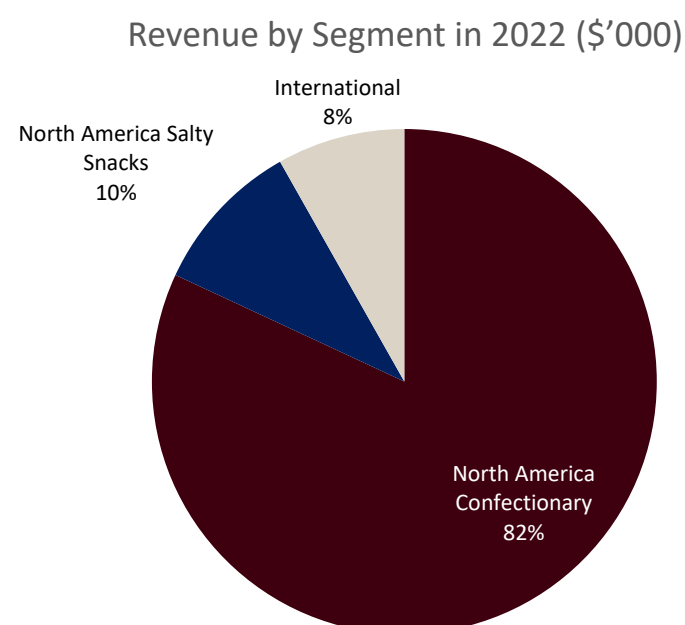


Figure 2 - Source: The Hershey Company Financial Statement

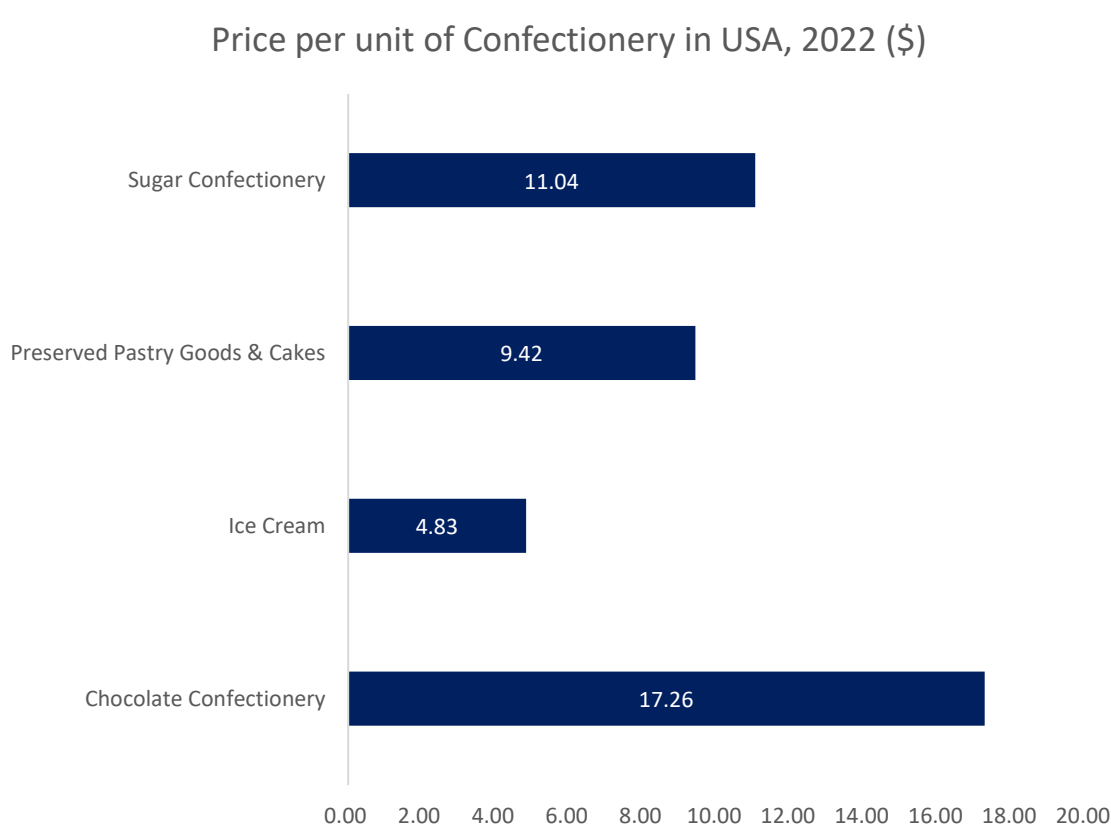


Figure 3 -Source: Statista

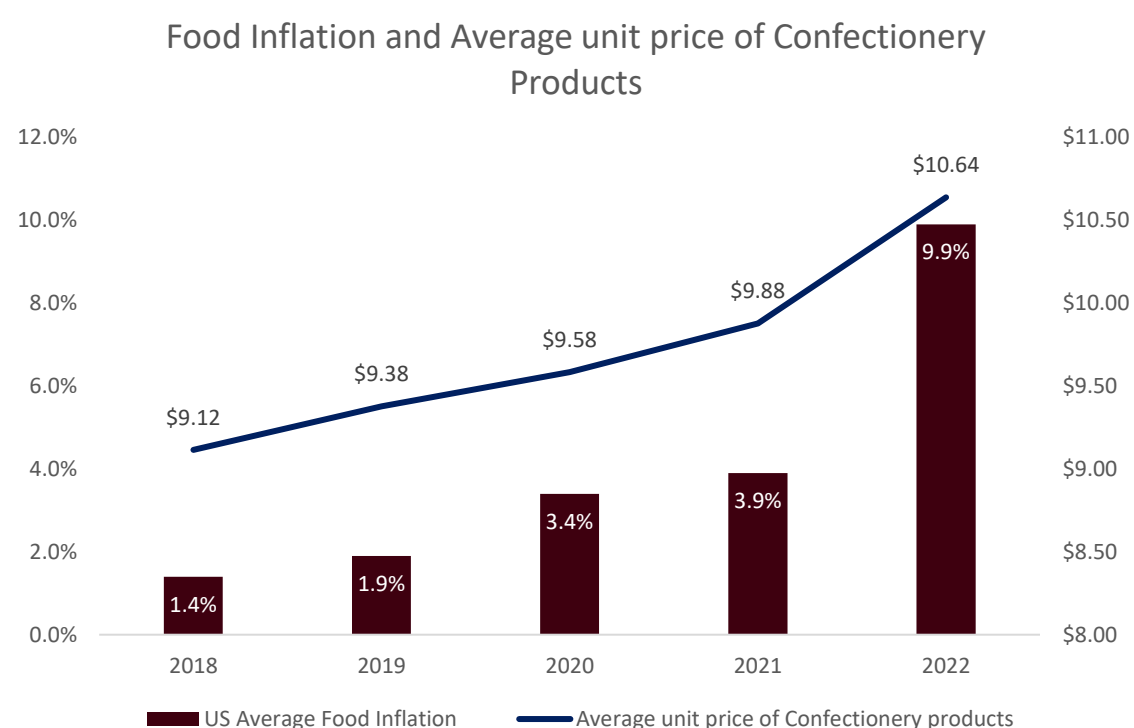


Figure 4 - Source: Statista (Average price of Confectionery products in the US), US inflation calculator (Average food Inflation)

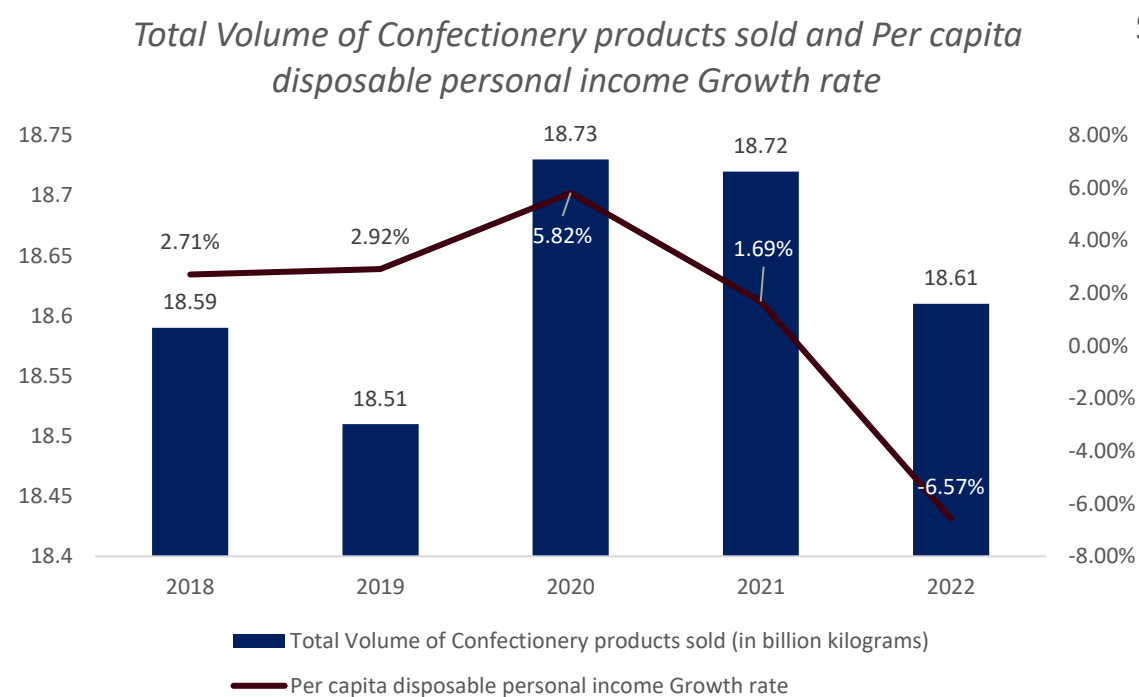


Figure 5 - Source: Statista (Total Volume of Confectionery products sold (in billion kilograms)), Federal Reserve Economic Data (Per capita disposable personal income Growth rate)

Segment share of Volume of Confectionery products sold in the USA in 2022

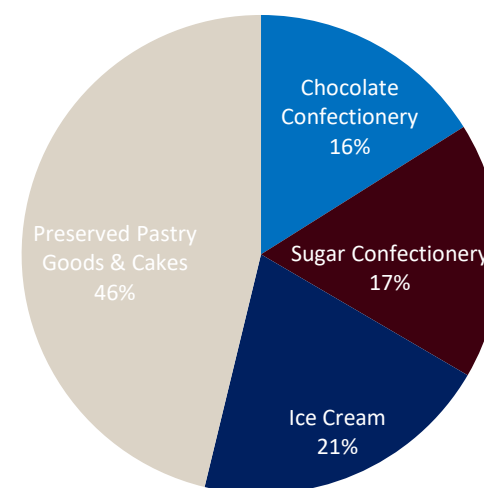


Figure 6 - Source: Statista

Porter's Five Forces analysis

A Porter's Five Forces analysis can help to evaluate the level of competition in the market and its potential impact on the Hershey Company. The analysis measures a company's position based on five forces: threat of new entrants, threat of substitutes, bargaining power of buyers, bargaining power of suppliers, and competitive rivalry.

When evaluating The Hershey Company through Porter's Five Forces analysis, **the threat of new entrants** is low due to factors such as economies of scale, product differentiation, large capital requirements, switching costs, limited access to distribution channels, and regulations for food manufacturers. Hershey's is a leading chocolate manufacturer, and it would be difficult for new entrants to maintain competitive prices due to the economies of scale that favour Hershey's and other larger players in the market.

The threat of substitutes is moderate within the industry. While other sweets and baked goods are close substitutes for chocolate products, they are not true replacements. Customers do not face any switching costs in shifting to a substitute product.

The bargaining power of customers is moderate. Hershey's target market is broad, and the company offers a wide range of products catering to different income and age groups in more than 70 countries worldwide.

The bargaining power of suppliers is low. Hershey's has a well-established supply chain with multiple suppliers for its raw materials, reducing the bargaining power of any single supplier.

The competitive rivalry is high within the confectionery market. Several large players such as Mars Inc., Nestle SA, Mondelez International Inc., Ferrero Group, etc. compete on price, quality, product differentiation, and marketing.

SWOT analysis

A SWOT analysis is a tool used to evaluate the Strengths, Weaknesses, Opportunities, and Threats of an organization by identifying internal and external factors that can affect its success or failure. Here is a summary of the SWOT analysis for The Hershey Company:

Strengths:

Hershey's is one of the largest chocolate manufacturers in the world with wide distribution in more than 70 countries.

The company is known for being an innovative and creative chocolate brand.

Hershey's has a large product portfolio with more than 50 product variants and huge annual sales.

The company is highly regarded and has strong brand equity.

Hershey's is involved in philanthropy efforts, such as education initiatives and basic nutrition programs.

Weaknesses:

The company has limited expansion and faces competition from many small and regional players.

Counterfeit Hershey's products are a problem in developing nations.

Opportunities:

Hershey’s can expand its product portfolio, strengthen its core brands, and pursue growth through strategic acquisitions and global expansion.

There is a growing trend towards healthier eating and reducing sugar intake. Hershey’s low/zero sugar chocolate products provide an opportunity for health enthusiasts to enjoy chocolate without added sugar. By offering these products, Hershey’s can tap into the growing market of health-conscious consumers, potentially increasing its customer base and driving sales growth while improving its brand image and reputation among health enthusiasts.

Threats:

The confectionery market is highly competitive with several large players such as Mars Inc., Nestle SA, Mondelez International Inc., Ferrero Group, etc. These companies have well-established brands and compete on price, quality, product differentiation, and marketing.

Financial Analysis

Short-term stability

The current ratio, which measures a company’s ability to pay short-term obligations, has decreased from 0.93x in 2018 to 0.80x in 2022. The cash ratio, which measures a company’s ability to pay off its current liabilities with only cash and cash equivalents, has decreased from 0.24x in 2018 to 0.14x in 2022. (See figure 7). The quick ratio, which measures a company’s ability to meet its short-term obligations with its most liquid assets, has decreased from 0.60x in 2018 to 0.44x in 2022.

Long-term solvency

The interest coverage ratio (EBIT/Interest expense), which measures how easily a company can pay interest on outstanding debt, has increased from 11.69x in 2018 to 16.44x in 2022. The interest coverage ratio (EBITDA/Interest expense), which measures how easily a company can pay interest on outstanding debt using its earnings before interest, taxes, depreciation, and amortization, has increased from 13.28x in 2018 to 17.69x in 2022 (Figure 8).

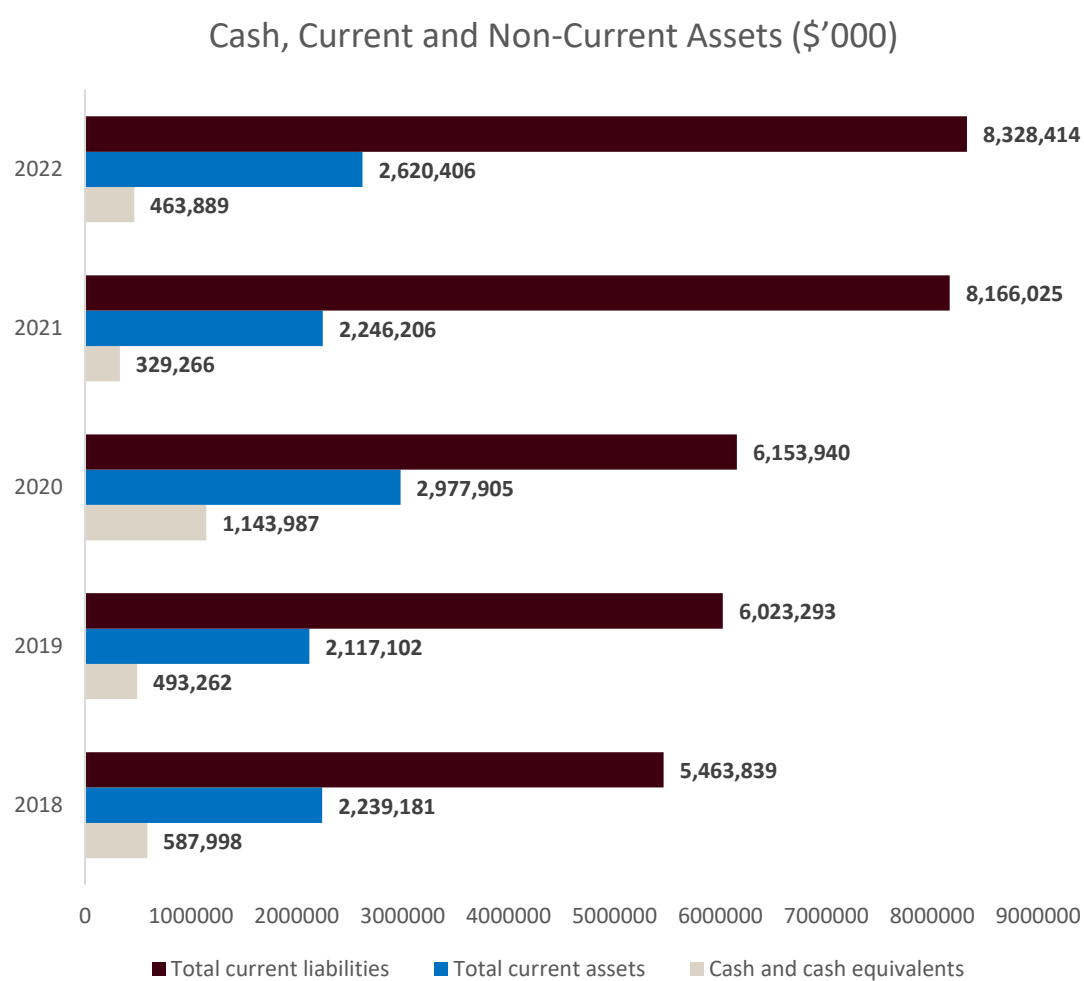


Figure 7 - Source: The Hershey Company Financial Statement

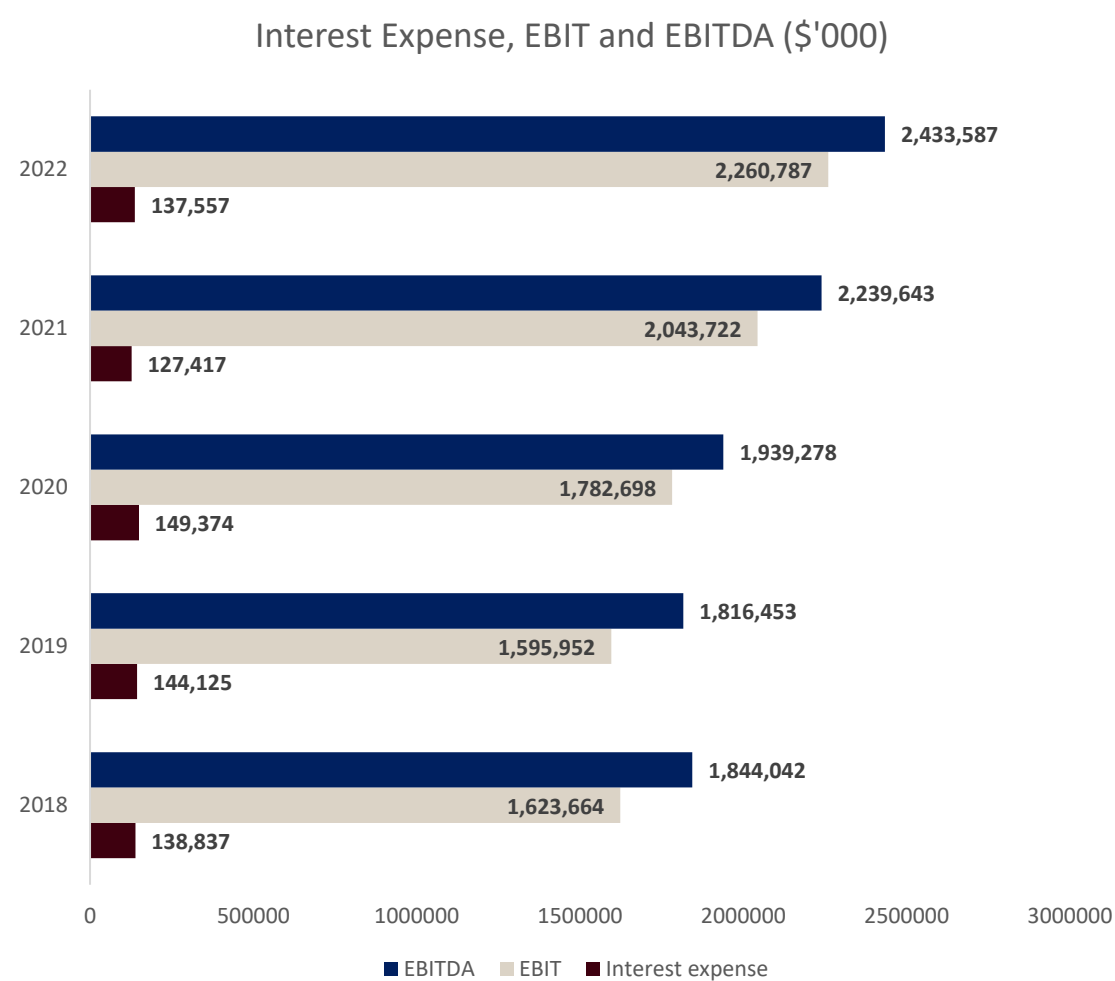


Figure 8 - Source: The Hershey Company Financial Statement

The debt-to-equity ratio, which measures how much debt a company is using to finance its assets relative to the value of shareholders’ equity, has decreased from 3.17x in 2018 to 1.45x in 2022. The debt to capital ratio, which measures a company’s financial leverage by comparing its total debt to its total capital, has decreased from 0.76x in 2018 to 0.59x in 2022. The debt to total assets ratio, which measures the extent of a company’s leverage by comparing its total debt to its total assets, has decreased from 0.58x in 2018 to 0.44x in 2022. (Figure 9).

The net debt to EBITDA ratio, which measures a company’s ability to pay off its debt using its earnings before interest, taxes, depreciation, and amortization, has decreased from 2.10x in 2018 to 1.78x in 2022.

The debt service coverage ratio (EBITDA/P+R), which measures a company’s ability to service its current debts by comparing its EBITDA to its total debt service obligations (principal and interest), has increased from -7.41x in 2021 to 6.27x in 2022.

Profitability

The gross margin, which measures the percentage of revenue that exceeds the cost of goods sold (COGS), has decreased from 46% in 2018 to 43% in 2022. The EBITDA margin, which measures a company’s operating profitability as a percentage of its total revenue, has decreased from 24% in 2018 to 23% in 2022.

The EBIT margin, which measures a company’s operating profitability as a percentage of its total revenue, has increased from 21% in 2018 to 22% in 2022. The net profit margin, which measures how much of each dollar of revenues is left over after all expenses are paid, has increased from 15% in 2018 to 16% in 2022.

The return on invested capital (ROIC), which measures how well a company is using its capital to generate returns, has remained stable at around 26-28% from 2018 to 2022.

The return on shareholders’ equity (ROE), which measures how much profit a company generates with the money shareholders have invested, has decreased from 73% in 2019 to 54% in 2022. The return on assets (ROA), which measures how profitable a company is relative to its total assets, has remained stable at around 15% from 2019 to 2022 (Figure 10).

Activity

Trade receivables days, which measures the average number of days it takes for a company to collect payment after a sale has been made, has decreased from 28 days in 2018 to 25 days in 2022.

Inventory holding days, which measures the average number of days it takes for a company to sell its inventory, has increased from 68 days in 2018 to 72 days in 2022.

Trade payables days, which measures the average number of days it takes for a company to pay its suppliers, has increased from 43 days in 2018 to 60 days in 2022.

The cash conversion cycle (CCC), which measures the time it takes for a company to convert its investments in inventory and other resources into cash flows from sales, has decreased from 52 days in 2018 to 37 days in 2022 (Figure 11).

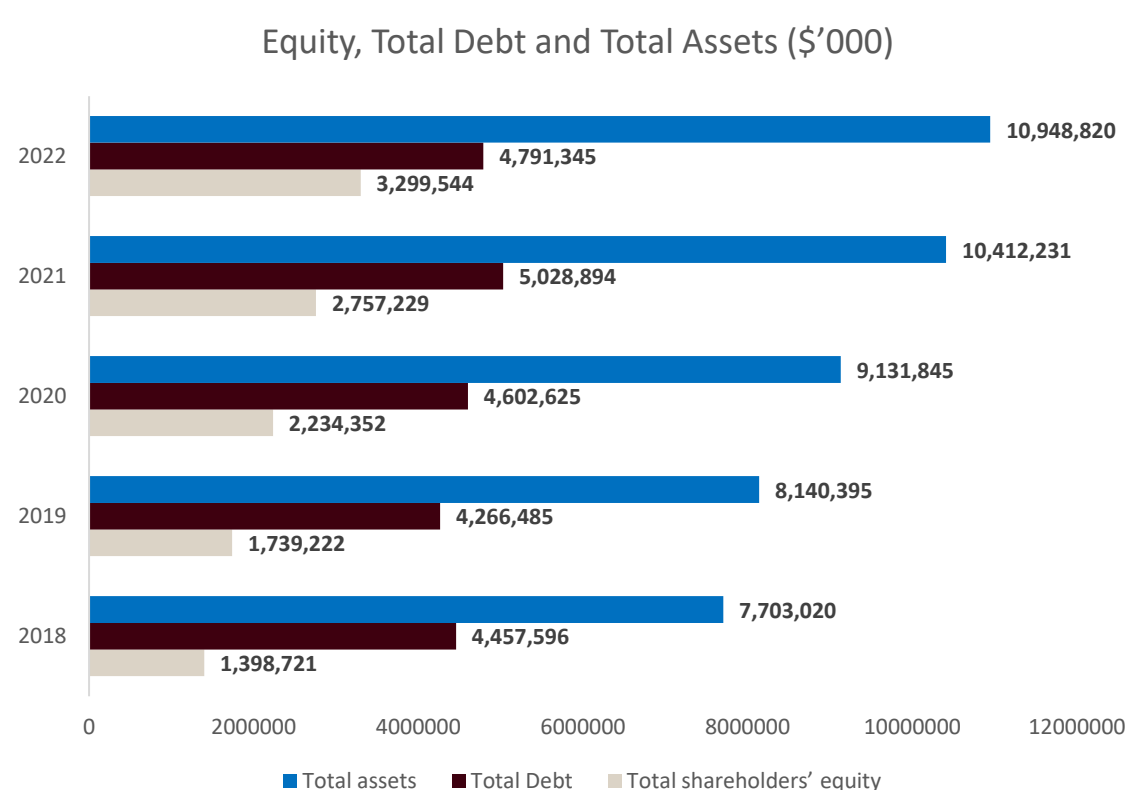


Figure 9 - Source: The Hershey Company Financial Statement

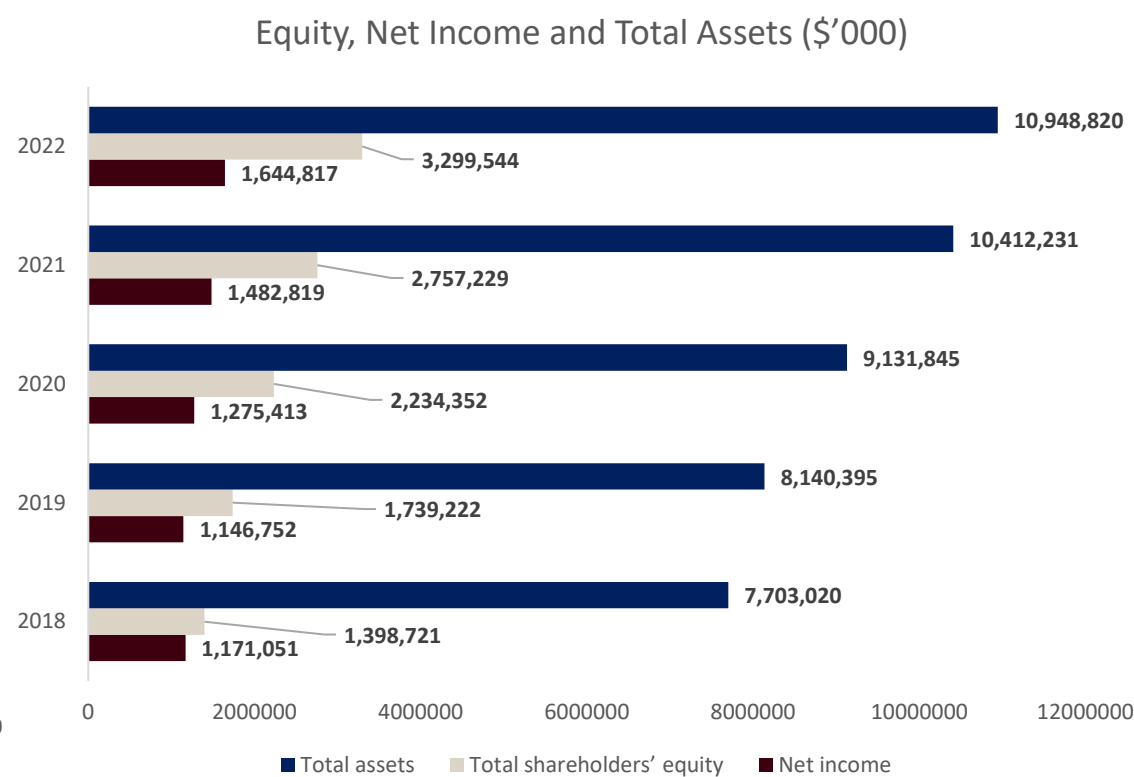


Figure 10 - Source: The Hershey Company Financial Statement

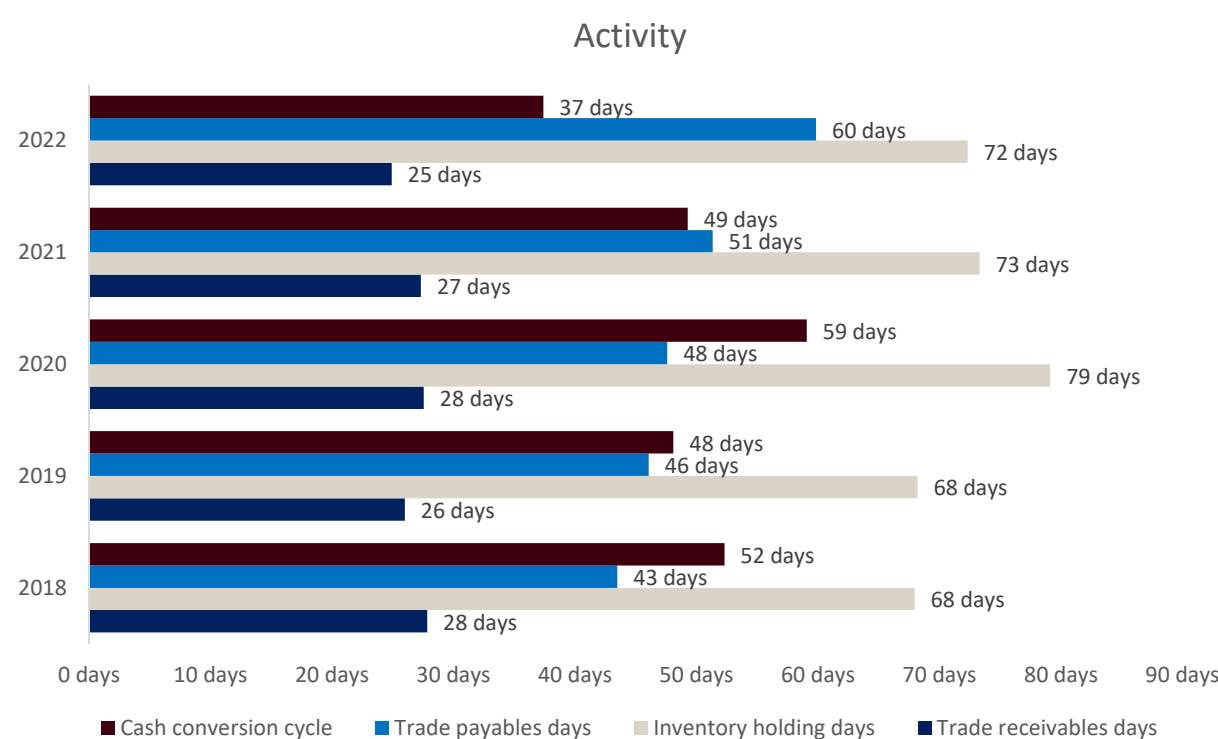


Figure 11 - Source: The Hershey Company Financial Statement

Summary

The Hershey Company has seen a decrease in its short-term stability ratios, indicating that its ability to meet short-term obligations has decreased. However, its long-term solvency ratios have improved, indicating that the company's ability to meet its long-term obligations has improved. The company's profitability ratios have remained relatively stable, with some slight fluctuations. Its activity ratios show a decrease in trade receivables days and an increase in trade payables days, indicating that the company is taking longer to pay its suppliers and is collecting payment from customers faster.

Financial Modelling and Valuation

To project The Hershey's Company expected revenue from 2023 to 2027, there were certain macro-economic factors to consider, like the US Population Growth rate, Per capita disposable personal income Growth rate and the US Average Food Inflation.

Total Volume of Confectionery products sold in the US and Average price of Confectionery products in the US projections were used to estimate the expected sales from 2023 to 2027. The risk-free rate was based on the US 10-year Bond Yield while the gross cost of debt was derived from the yield of Hershey US\$400 million of 4.50% debt due February 15, 2033.

The perpetuity growth rate was calculated using the CAGR of The Hershey's Company actual revenue from 2022 to the projected 2027 revenue. The Discounted Free Cash Flow Method and the Dividend Discount Model Method was used to arrive at the Intrinsic Equity Value (see Table 1 and the Appendix pages for more information).

Valuation Metrics	
Perpetuity Growth Rate	3.71%
Weight Average Cost of Capital (WACC)	5.50%

Valuation Methodology	Weight	Price
Discounted Free Cash Flow Method	50%	\$403.01
Dividend Discount Model Method	50%	\$240.97
Target Price	100%	\$321.99

Upside/Downside	
Current share price	\$241.22
Potential Gain/Loss	33.49%

Table 1

Income Statement (\$'000)	2018A	2019A	2020A	2021A	2022A	2023P	2024P	2025P	2026P	2027P
Net sales	7,791,069	7,986,252	8,149,719	8,971,337	10,419,294	10,884,458	11,370,389	11,878,014	12,408,301	12,962,263
Cost of sales	4,215,744	4,363,774	4,448,450	4,922,739	5,920,509	5,987,095	6,274,760	6,567,817	6,878,649	7,200,364
Gross profit	3,575,325	3,622,478	3,701,269	4,048,598	4,498,785	4,897,363	5,095,629	5,310,197	5,529,652	5,761,899
Selling, marketing and administrative expense	1,874,829	1,905,929	1,890,925	2,001,351	2,236,009	2,282,949	2,330,874	2,379,805	2,429,764	2,480,771
Long-lived asset impairment charges	57,729	112,485	9,143	0	0	0	0	0	0	0
Business realignment costs	19,103	8,112	18,503	3,525	1,989	10,246	8,475	8,548	6,557	7,163
Operating profit	1,623,664	1,595,952	1,782,698	2,043,722	2,260,787	2,604,168	2,756,280	2,921,843	3,093,332	3,273,965
Interest expense, net	138,837	144,125	149,374	127,417	137,557	218,608	216,007	219,433	212,282	203,977
Other (income) expense, net	74,766	71,043	138,327	119,081	206,159	252,524	309,315	378,880	464,089	568,461
Income before income taxes	1,410,061	1,380,784	1,494,997	1,797,224	1,917,071	2,133,036	2,230,958	2,323,531	2,416,961	2,501,527
Provision for income taxes	239,010	234,032	219,584	314,405	272,254	342,493	354,228	363,948	383,299	388,528
Net income	1,171,051	1,146,752	1,275,413	1,482,819	1,644,817	1,790,543	1,876,730	1,959,583	2,033,663	2,112,998
Balance Sheet (\$'000)	2018A	2019A	2020A	2021A	2022A	2023P	2024P	2025P	2026P	2027P
Total current assets	2,239,181	2,117,102	2,977,905	2,246,206	2,620,406	2,650,536	3,408,074	3,808,977	4,151,020	4,502,083
Total non-current assets	5,463,839	6,023,293	6,153,940	8,166,025	8,328,414	8,755,447	9,293,301	9,975,702	10,808,000	11,828,045
Total assets	7,703,020	8,140,395	9,131,845	10,412,231	10,948,820	11,405,983	12,701,374	13,784,679	14,959,019	16,330,128
Total current liabilities	2,418,566	2,008,793	1,891,745	2,493,313	3,257,154	3,129,346	3,775,595	4,238,050	4,702,885	5,336,443
Total non-current liabilities	3,877,188	4,386,608	5,002,217	5,161,689	4,392,122	4,454,788	4,527,505	4,611,594	4,708,537	4,820,002
Total liabilities	6,295,754	6,395,401	6,893,962	7,655,002	7,649,276	7,584,134	8,303,100	8,849,644	9,411,422	10,156,445
Total—The Hershey Company stockholders' equity	1,398,721	1,739,222	2,234,352	2,757,229	3,299,544	3,821,849	4,398,274	4,935,036	5,547,597	6,173,683
Noncontrolling interest in subsidiary	8,545	5,772	3,531	0	0	0	0	0	0	0
Total stockholders' equity	1,407,266	1,744,994	2,237,883	2,757,229	3,299,544	3,821,849	4,398,274	4,935,036	5,547,597	6,173,683
Total liabilities and equities	7,703,020	8,140,395	9,131,845	10,412,231	10,948,820	11,405,983	12,701,374	13,784,679	14,959,019	16,330,128
Check 1 =====>>> Assets - (Liabilities + Equity) = 0	0	0	0	0	0	0	0	0	0	0
Check 2 =====>>> Assets = Liabilities + Equity	TRUE	TRUE	TRUE	TRUE	TRUE	TRUE	TRUE	TRUE	TRUE	TRUE
Cash Flow (\$'000)	2018A	2019A	2020A	2021A	2022A	2023P	2024P	2025P	2026P	2027P
Net cash provided by operating activities	1,599,993	1,763,873	1,699,657	2,082,884	2,327,837	2,487,798	2,446,074	2,448,981	2,473,953	2,406,411
Net cash flow from investing activities	(1,502,894)	(780,480)	(531,280)	(2,222,828)	(787,376)	(525,369)	(562,676)	(610,706)	(631,086)	(647,819)
Net cash flow from financing activities	116,108	(1,081,455)	(499,228)	(681,136)	(1,415,725)	(2,015,678)	(1,223,291)	(1,556,884)	(1,577,745)	(1,504,950)
Effect of exchange rate changes on cash and cash equivalents	(5,388)	3,326	(6,990)	(5,075)	9,887	0	0	0	0	0
Increase (decrease) in cash and cash equivalents, including cash classified as held for sale	207,819	(94,736)	662,159	(826,155)	134,623	(53,250)	660,107	281,391	265,122	253,642
Less: Decrease (increase) in cash and cash equivalents classified as held for sale	0	0	(11,434)	11,434	0	0	0	0	0	0
Increase (decrease) in cash and cash equivalents	207,819	(94,736)	650,725	(814,721)	134,623	(53,250)	660,107	281,391	265,122	253,642
Cash and cash equivalents, beginning of period	380,179	587,998	493,262	1,143,987	329,266	463,889	410,639	1,070,746	1,352,137	1,617,259
Cash and cash equivalents, end of period	587,998	493,262	1,143,987	329,266	463,889	410,639	1,070,746	1,352,137	1,617,259	1,870,902

Comprehensive Financial Performance Analysis - Q3 2023										
Financial Ratios	Historical Performance (Actuals)					Forecasted Performance (Projections)				
	2018A	2019A	2020A	2021A	2022A	2023P	2024P	2025P	2026P	2027P
Short-term stability										
Current ratio	0.93x	1.05x	1.57x	0.90x	0.80x	0.85x	0.90x	0.90x	0.88x	0.84x
Quick ratio	0.60x	0.65x	1.06x	0.50x	0.44x	0.47x	0.57x	0.58x	0.59x	0.57x
Cash ratio	0.24x	0.25x	0.60x	0.13x	0.14x	0.13x	0.28x	0.32x	0.34x	0.35x
Long-term solvency										
Interest coverage ratio (EBIT/Interest expense)	11.69x	11.07x	11.93x	16.04x	16.44x	11.91x	12.76x	13.32x	14.57x	16.05x
Interest coverage ratio (EBITDA/Interest expense)	13.28x	12.60x	12.98x	17.58x	17.69x	12.52x	13.17x	13.48x	14.41x	15.47x
Debt to equity	3.17x	2.44x	2.06x	1.82x	1.45x	1.06x	0.94x	0.81x	0.69x	0.62x
Debt to capital	0.76x	0.71x	0.67x	0.65x	0.59x	0.51x	0.48x	0.45x	0.41x	0.38x
Debt to total assets	0.58x	0.52x	0.50x	0.48x	0.44x	0.35x	0.32x	0.29x	0.26x	0.23x
Net debt to EBITDA	2.10x	2.08x	1.78x	2.10x	1.78x	1.33x	1.07x	0.89x	0.72x	0.62x
Debt service coverage ratio (EBITDA/P+R)	4.57x	1.38x	2.39x	-7.41x	6.27x	2.83x	20.47x	8.37x	8.29x	14.21x
Profitability										
Gross margin	46%	45%	45%	45%	43%	45%	45%	45%	45%	44%
EBITDA margin	24%	23%	24%	25%	23%	25%	25%	25%	25%	24%
EBIT margin	21%	20%	22%	23%	22%	24%	24%	25%	25%	25%
Return on invested capital	28%	27%	26%	26%	28%	33%	32%	33%	33%	33%
Net profit margin	15%	14%	16%	17%	16%	16%	17%	16%	16%	16%
Return on shareholders' equity (ROE)		73%	64%	59%	54%	50%	46%	42%	39%	36%
Return on assets (ROA)		14%	15%	15%	15%	16%	16%	15%	14%	14%
Activity										
Trade receivables days	28 days	26 days	28 days	27 days	25 days	27 days	26 days	27 days	26 days	26 days
Inventory holding days	68 days	68 days	79 days	73 days	72 days	72 days	73 days	74 days	73 days	73 days
Trade payables days	43 days	46 days	48 days	51 days	60 days	64 days	68 days	72 days	77 days	82 days
Cash conversion cycle	52 days	48 days	59 days	49 days	37 days	35 days	32 days	28 days	22 days	17 days
Growth										
Revenue Growth Rate		3%	2%	10%	16%	4%	4%	4%	4%	4%
EBITDA Growth Rate		-1%	7%	15%	9%	12%	4%	4%	3%	3%
EBIT Growth Rate		-2%	12%	15%	11%	15%	6%	6%	6%	6%
PAT Growth Rate		-2%	11%	16%	11%	9%	5%	4%	4%	4%