

Hofstra SMIF Research Report

Consumer Staples
Food Products

McCormick & Company Inc.

Ticker: MKC
Price: \$100.06

Recommendation: Buy
Price Target: \$113.31

Nicholas Nappi

		Q1	Q2	Q3	Q4	Year	P/E Ratio
November 21, 2017	2014A	\$0.62	\$0.64	\$0.95	\$1.16	\$3.37	22.54x
	2015A	0.70	0.75	0.85	1.18	3.48	24.88
	2016A	0.74	0.75	1.03	1.27	3.79	24.62
	2017E	0.76	0.82	1.12	1.60E	4.30	23.72E

Recent Highlights

- **Strategic Acquisitions:** Since 2015, McCormick has made six major acquisitions, ranging from herb companies to marinade and sauce companies. The firms that McCormick purchased span across the globe, which will further increase their global footprint in the industry.
- **High Industry Moat:** McCormick is the most dominant company in the Spices and Seasonings section of the Food Products industry, as they control 21% of the global market.
- **Defensive Qualities:** McCormick's five-year average beta of 0.643, which is almost 40% less than the average riskiness of the market as a whole, and the area of the market in which the company operates makes it a solid addition to any portfolio with the goal of mitigating risk.
- **Growth in Organic Sales:** McCormick is seeing increased sales and demand for their organic product lineup, as consumer preferences have been shifting to incorporating healthier foods into their diets.

Market Profile	
52 Week Price Range	\$88.64 - \$106.50
Average Daily Volume	1,100,000.00
Beta	0.643
Dividend Yield (Estimated)	1.93%
Shares Outstanding	128,000,000.00
Market Capitalization	\$11,900,000.00
Institutional Holdings	88.27%
Insider Holdings	0.09%
Book Value per Share (12/31/16)	\$94.66
Debt to Total Capital	46.91%
Return on Equity	28.65%

Source: Bloomberg



Important disclosures appear at the back of this report

Investment Summary

McCormick's dominant presence in the Food Products industry, specifically the Spices and Seasonings industry, combined with the firm's ability to generate excess free cash flow and value from expanding product lines and strategic acquisitions, makes it a solid investment with almost certain capital appreciation, regardless of the state of the markets or economy.

Acquisitions Contributing to Widening Industry Moat and Profitability

Over the past two and a half years, McCormick has acquired multiple companies from different parts of the world that have and will continue to provide value to the company, while expanding its presence and industry moat on an international scale.

In March of 2015, McCormick purchased Brand Aromatics, a private company based out of New Jersey for \$62.4 million.⁶ Brand Aromatics is a U.S. supplier of natural savory flavors, broth and stock concentrates, and marinades to the packaged food industry.⁶ The acquisition will continue to directly benefit and expand the offerings of McCormick's industrial segment.

A few months later, in May of 2015, McCormick acquired Italian branded and private label spice and seasoning company Drogheria & Alimentari (D&A) for \$49.0 million. D&A holds approximately one-third of the spice and seasoning category in Italy, and exports its products to over 60 other countries.⁸ The acquisition further expands McCormick's European presence, while also growing the firm's portfolio of spices and seasonings.⁸ The purchase will expand offerings in McCormick's consumer segment.

During the month of August later that year, McCormick acquired One World Foods Inc., the parent company of Stubb's brand of barbecue products, for \$99.4 million.⁶ Stubb's is based in Texas and is one of the leading brands of barbecue sauce in the United States. In addition to barbecue sauce, Stubb's also offers products such as marinades, rubs, and skillet sauces.⁸ The acquisition has and will continue to add value to the consumer segment of McCormick's business.

In April of 2016, McCormick bought Botanical Food Company, a packaged herb and seasoning company that owns Gourmet Garden brand, for \$116.2 million.⁶ This purchase assisted McCormick in breaking into the market in Australia, as that was the country of domicile for Gourmet Garden brands. This acquisition was made with the intent of adding value to the firm's consumer segment, due to the strong consumer following that Gourmet Garden has developed within Millennials and Generation X people.²

During November of 2016, McCormick acquired Giotti, an Italian based flavor, juice, and extract manufacturer for \$127 million.¹ This purchase will add value to the company's industrial segment due to the fact that Giotti supplies flavors and extracts to food companies and multi-national restaurants.¹ Giotti will also add expertise in the high growth segment of health and nutritional products, and will accelerate sales growth in the EMEA region.²

In July of this year, McCormick made their largest acquisition in the company's history, purchasing British consumer goods conglomerate Reckitt Benckiser Group for \$4.2 billion.⁴ RB Foods is the owner of brands such as French's Mustard, Cattlemen's BBQ Sauce, and Frank's RedHot Hot Sauce, and has a prodigious footprint in the global food products market. The acquisition will increase McCormick's branded foodservice sales by over 50% in the United States and Canada, and will dramatically escalate the company's potential for global growth.²

The addition of RB Foods to McCormick's portfolio of food products will be the most value-added acquisition that the company has made due to both the popularity and dominance of RB Foods' brand names. For example, Frank's RedHot has double the market share of the next closest competing hot sauce brand, while French's Mustard has four times the market share as the next closest mustard brand.⁵

Expanding Innovation and Research & Development

McCormick has been devoted to researching consumer preferences and developing new products to keep control of the industry that they operate in. The firm has over 20 product innovation centers around the world, and in the last three years, new products that have been launched have accounted for around 9% of sales growth in the most recent fiscal year (FY 2016).² What is interesting to note is that although a large amount of the new products that are being released are food based, a portion of the goods are non-food. The company has been introducing non-food items to further diversify their product lineup, including items such as Grill

¹Thomson Reuters²Bloomberg³Morningstar⁴McCormick & Company Inc. 10K⁵SeekingAlpha⁶CFRA S&P Global⁷CFRA Industry Report⁸Zacks Investment Research

Mates, Grinders, and Slow Cookers, as well as McCormick’s “Recipe Inspirations”.⁶ The “Recipe Inspirations” are recipe cards that come with premeasured packets of the herbs and spices that are required to make the meal detailed in the recipe.⁶

An Effective Way to Lower Portfolio Beta

McCormick & Company Inc. operates in the Consumer Staples industry, which is historically has low volatility when compared to the market as a whole. Furthermore, being that McCormick delivers food products to both consumer and industrial clients, the demand for its items is not as sensitive in the case of an economic downturn. Regardless of the state of the national or foreign economy or markets, people need to eat, and therefore need spices, seasonings, and/or condiments to cook or eat with.

McCormick currently has a five-year average beta of 0.643, which means that the stock is more than 35% less risky than the market as a whole. As per the requirements of the SMIF Portfolio Construction, analysts need to work in conjunction with one another to keep the overall portfolio beta below 1.0. The addition of McCormick to the SMIF Portfolio will indefinitely lower the portfolio’s beta, while also providing extraordinary growth potential for a company operating in the sector that McCormick does.

In looking at the historical pricing for McCormick, and comparing that data with the historical prices of the S&P 50 Index (SPX) and the Dow Jones Industrial Average Index (INDU), we can see that during periods of market turmoil, McCormick is able to power through those tough times, while the same cannot be said for the entire market. An example of this can be seen in the image below, where the black circle highlights McCormick’s reaction to the 2008 financial crisis, along with the reactions of the S&P 500 Index (orange) and the Dow Jones Industrial Average Index (blue). As per the data, the SPX fell by around 52% during the one-year period from the start of the crisis, and the INDU fell around 49% during that same time. On the other hand, McCormick suffered losses of only around 27% during that same period. Even with that fall in the stock price, McCormick was still able to deliver positive and growing EPS in the years following the financial crisis, posting an EPS of \$1.92 in 2008, and an EPS of \$2.14 in 2009 (11.46% increase), and an EPS of \$2.34 in 2010 (9.35% increase).⁵

With the extensive bull run of the domestic and global equity markets since the election of President Donald Trump, adding a stock that is defensive in nature, such as McCormick, would be a great protective measure to take by any portfolio manager or fund to combat the effect of a market pullback on the return of the portfolio.

Figure 1: McCormick & Co Inc. vs SPX and DJIA since 1995

Reference the black circle, which highlights MKC’s reaction compared with the market indexes post 2008



Source: Bloomberg

Rising Growth and Demand for Organic Products

McCormick has been successfully adjusting to the growing consumer preferences and demand for healthier food options, as 75% of their gourmet product range is organic.³ This change has not only pleased their customers, but has also awarded the firm the opportunity to expand their shelf space for the offering of these

¹Thomson Reuters

²Bloomberg

³Morningstar

⁴McCormick & Company Inc. 10K

⁵SeekingAlpha

⁶CFRA S&P Global

⁷CFRA Industry Report

⁸Zacks Investment Research

new organic options at four out of ten of the top United States' retailers.³ Their organic product lineup is aimed at accommodating not only people who are eating healthier, but also to people who have dietary restrictions, such as Celiac Disease, by offering gluten-free items. By labeling almost 70% of their U.S. spices and seasonings as non-GMO (genetically modified organisms) and upgrading its gourmet line to hold 80% organic products, the firm saw sales surge by 5.6%.² Furthermore, in the company's recent 3Q17 earnings release, they reported sales growth in organic products by 4.4%.³

Valuation

During the valuation of McCormick & Company Inc., both a Free Cash Flow to Equity Model and a Two-Stage Dividend Discount Model were used. Both models showed a potential large upside in the stock, offering at least a 13% possible gain from the current trading price of \$100.06 (as of November 21, 2017). In the calculations, the yield on the 10-Year U.S. Treasury Bond was used for the risk-free rate. The lower price target from both valuation models will be used as the target price for McCormick. The results from the valuation solidify the "buy" recommendation on the stock.

Free Cash Flow to Equity Valuation

In using the FCFE valuation model, the valuation has produced a projected price target of \$193.13 per share, representing just about a 93% upside from the trading price at market close on 11/21/2017 (\$100.06). The valuation process began with taking the average Free Cash Flow of McCormick for the last ten years, and calculating the percent year over year increase or decrease for those ten years. Initially, we intended to use the five-year average free cash flow for the firm, but that number was much too high in our opinion to sustain (over 16%), therefore, in order to arrive at a more realistic number, we used the ten-year average. After computing this, we took the average percentage of the ten years and used that number (9.66%) as the average growth rate in computing the projected values for all of the elements of the financial model. This growth rate is very high, especially for a company that is operating in the Food Products industry, but McCormick has an exceptional business model in which the company historically has operated with an abundance of free cash flow. Next, the Cash Flow Statement for FY 2016 was used to take the totals for net income and other components of the model, and dividing that by the number of outstanding shares to arrive at per share results. The growth rate of 9.66% was then applied to these results, and started generating predictions for the components of the model. The rate of 9.66% was used for the estimation of the 2017 and 2018-year end projections, but for 2019 we used a late stage growth rate of 4.50% due to accommodate the possible risk to free cash flow from the rise in commodity prices. After applying these growth rates to per share estimates, the final prediction for the FCFE per share estimates were reached.

It is important to state that during the calculations performed for the projection of the Total Change in Net Debt, we assumed a higher growth rate (11.18%), because due to the firm's history of frequent acquisitions, we wanted to project a more realistic level of debt that the company would be operating with. We arrived at the growth rate of 11.18% by looking at the historical levels of both short-term and long-term debt, and pooling the total cost together and then computing the year over year percentage change (for ten years) in the total amount of short-term and long-term debt. Finally, we took the average of the percentage change in total debt for the last ten years, and reached our assumed expected growth rate of debt.

From here, we achieved a terminal value after the three-year period of \$215.83 by taking the 2019 FCFE estimate and dividing it by the required return on equity minus the late stage growth rate. A discount rate of 7.05% was used because that was the yielded result from the CAPM formula when using the stock's five-year weekly average beta (.643), the risk-free rate (2.36%), and the projected return of the S&P (9.66%). The FCFE estimate for FY 2018 was added to this terminal value to arrive at a value of \$221.33 for total cash flows to equity over the period of 2017 to 2019. Lastly, the value \$221.33 was discounted back to present value by taking the total cash flows to equity and dividing it by one plus the discount rate and raising the denominator to 2. From calculating this, the discounted value came out to \$193.01.

The results from this model represent an enormous potential upside for the stock, and although the calculations point to almost an 100% upside, this movement in the stock price is not unattainable. The company has been focused on operating efficiently to effectively return free cash flow both back to shareholders through buyback plans and dividend hikes, as well as back into the company to extend their R&D programs.

Two-Stage Dividend Discount Model

In using a Two-Stage Dividend Discount Model, the valuation has engendered a projected price target of \$113.31 per share, representing over a 13% upside from the closing price of \$100.06 on November 21, 2017.

¹Thomson Reuters

²Bloomberg

³Morningstar

⁴McCormick & Company Inc. 10K

⁵SeekingAlpha

⁶CFRA S&P Global

⁷CFRA Industry Report

⁸Zacks Investment Research

The estimate process began with first looking at the EPS, Dividends, and ROE of McCormick for the past five years. After gathering this data, the five-year average of each component was computed. By using taking the average dividend and dividing that by the average EPS, we arrive at the average payout ratio of the firm. We then take this number and subtract from one to compute the average plowback ratio of McCormick.

Taking the average plowback ratio, we can multiply this by the average ROE to arrive at the average growth over the last five years (12.91%). Taking this growth rate, the projected dividend values for 2018 and 2019 were computed. During the concluding calculations, a late stage growth rate of 5% was used due to the fact that historically, companies who operate in the Consumer Staples sector tend to grow at slower rates and that the company is mature.

After arriving at the terminal value and discounting this result to present value, the end result was a target price of \$113.31 with a potential upside of 13.24%.

Risks to McCormick's Target Price

There are a couple potential risks that could lower the price target of McCormick. One risk would be that due to the worldwide tensions, foreign exchange rates could be negatively affected, which in return, would hurt the profitability of McCormick. McCormick operates in copious countries around the world and sources around 45% of the revenue from international buyers.

In addition, if the prices of McCormick's most frequently purchased commodities (vanilla, pepper, garlic, and capsicums)³ keep rising due to inflation, this will directly raise their cost of production of their products, which will inevitably lower their profits.

Lastly, the potential rise of interest rates by the Federal Reserve later this year and next year could harm the price target of McCormick. By raising rates, investors will demand a higher required rate of return, which will have a negative effect on the final price target prediction that was calculated for McCormick & Company Inc.

Business Description

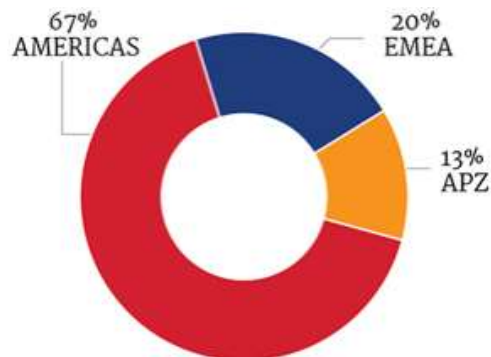
McCormick & Company Inc. was founded in 1889 by Willoughby M. McCormick and is headquartered in Sparks, Maryland. The company is a global leader in flavor and sells products in over 150 countries around the world. McCormick employs over 10,500 employees worldwide, and their current Chairman, CEO, and President is Lawrence Erik Kurzius. The company operates through two segments, its consumer segment and its industrial segment.

McCormick has a very dominant presence in the packaged foods industry, being that the company is four times as large as its next biggest competitor.⁵ The firm holds 21% of the market share in the global \$12 billion seasoning and spices industry, and roughly half of the market share in North America.

The company's largest area of business is conducted in the Americas, which represented around 67% of their record \$4.4 billion in sales during FY 2016.⁴ The EMEA region totaled 20% of McCormick's sales, and the Asia/Pacific region accounted for the remaining 13% of sales.

Figure 2: McCormick & Company Inc. Sales Breakdown by Geographic Location

Data based off FY2016 net sales amount; EMEA – Europe, Middle East, and Africa, APZ – Asia/Pacific Zone



¹Thomson Reuters

²Bloomberg

³Morningstar

⁴McCormick & Company Inc. 10K

⁵SeekingAlpha

⁶CFRA S&P Global

⁷CFRA Industry Report

⁸Zacks Investment Research



Source: McCormick & Company Investor Relations

Consumer Segment

McCormick's consumer segment is built around delivering products, under a diverse number of brands, to consumers through grocery stores, warehouse clubs, discount and drug stores, and e-commerce retailers, served both directly and indirectly through distributors or wholesalers.⁴

McCormick's leading brands in the Americas include McCormick, Lawry's, and Club House, with their niche brands being Gourmet Garden and OLD BAY.⁴ In the EMEA region, the company's major brands include Ducros, Schwartz, Kamis, and Drogheria & Alimentari, and offer an extensive line of Vahiné brand dessert items.⁴ In the Asia/Pacific region, the company markets their products under major brands in China, Australia, and India. In China, the company markets their products under the McCormick brand and the DaQuio brand. Moving to Australia, the firm markets spices and seasonings under the McCormick brand name, their dessert products under the Aeroplane brand, and packaged chilled herbs under the Gourmet Garden brand.⁴ In India, the firm's majority owned joint venture operates under the Kohinoor brand.⁴ McCormick also markets different authentic regional and ethnic brands including Stubb's, Zatarain's, Thai Kitchen, and Simply Asia.⁴

As a whole, the consumer segment of McCormick has historically generated around 60% of sales and around 75% of operating income for the firm.⁶ Wal-Mart Stores Inc. has been McCormick's largest consumer segment customer, representing 11% of consolidated sales in the years 2014, 2015, and 2016.⁴

Industrial Segment

McCormick's industrial segment provides a large range of products to multi-national food manufacturers and foodservice customers. The foodservice customers are supplied with branded, packaged products both directly and indirectly through distributors.⁴ McCormick strives to supply its foodservice customers and food manufacturers with customized flavor solutions, in addition to offering its customers one of the broadest selection of seasoning blends, spices and herbs, condiments, coating systems, and compound flavors.⁴

The products purchased by foodservice customers in the industrial segment are used as ingredients for menu items to enhance the flavor of their foods, while food manufacturers use the products as ingredients for their finished goods.

The industrial segment has traditionally represented 40% of sales and 25% of operating income.⁶ PepsiCo Inc. has been McCormick's largest industrial segment customer, accounting for 11% of consolidated sales in the years 2014, 2015, and 2016.⁴ The company's top three customers in the industrial segment represented around 53% of its total industrial sales.⁴

¹Thomson Reuters

²Bloomberg

³Morningstar

⁴McCormick & Company Inc. 10K

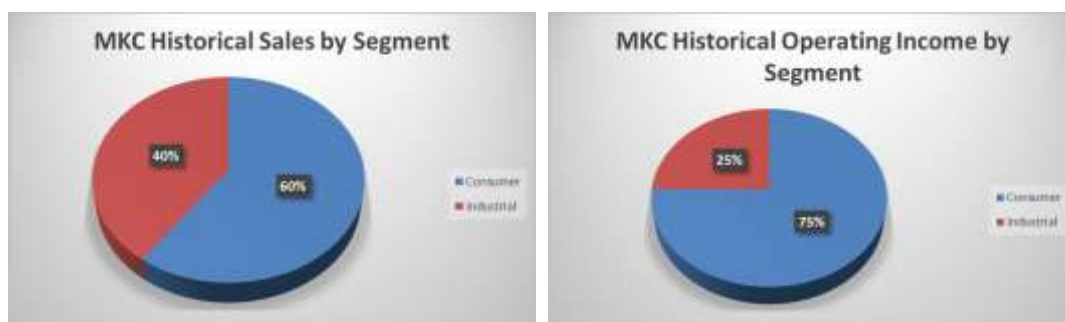
⁵SeekingAlpha

⁶CFRA S&P Global

⁷CFRA Industry Report

⁸Zacks Investment Research

Figure 3: McCormick & Company Inc. Sales and Operating Income Breakdown by Segment
Approximated Values, Yearly Averages



Source: McCormick & Company Inc. 10K

Additional Highlights

Institutional Transactions

During 3Q17, investment manager Clearbridge Investments LLC initiated a \$323.5 million position in McCormick, purchasing 3.15 million shares. In addition to Clearbridge, Vanguard Group Inc. opened a position worth over \$700,000 within the company during the same quarter.²

Growing Demand from Emerging Markets

McCormick is seeing rapid growth in various emerging markets within the Asia/Pacific Zone region, especially the firm's markets in China and India. McCormick's sales growth in the APZ region was around 3% during the last quarter.⁵

Over the last five years, the firm's sales in China have grown at an annual compounded growth rate of 39%.⁵ The growth in the Chinese market can be attributed to McCormick's effort to infiltrate the e-commerce market in the region, which has helped the firm increase sales in their newly released squeeze pouch condiments, in addition to the firm's sales in liquid products, such as sauces and cooking wines.⁴

Over the previous summer, McCormick started commercial production of different Indian spice mixes and condiments in an effort to appeal to more consumers in the region and to boost sales growth.⁴ In addition to the spices and condiments, the company has started manufacturing Indian ready-to-cook recipes, like Biryani, a popular Indian mixed rice dish, and various ready-to-eat products as well.⁵

Strength in Private Label Brand Sales

In addition to offering copious brand name items in its product lineup, McCormick is also a large producer of private label items, also known as store brand products. As expected, the core strength of the firm's private label item sales is through the spices and seasonings category. McCormick has effectively used their dominant position in this industry to augment its relationships with retailers, which has in return solidified their wide economic and industry moat.

An example of this would be how the firm has successfully gained a position in two of the leading dollar store chains, Dollar General and Family Dollar, and currently supplies them with brand store spices and seasoning mixes.³ By infiltrating this newly acquired customer base, McCormick is now able to offer products on the cheaper end of the spectrum, as opposed to their brand name options. The company's private label sales make up around 10% of their consumer segment revenue.³

Management & Governance

Lawrence Erik Kurzius was promoted to McCormick's CEO in February of 2016, and was elected as Chairman of the Board in February of this year.² Kurzius has been with McCormick for almost 15 years, and has held several executive leadership positions with the firm in his history of employment, including President and Chief Operating Officer (COO) and President and Chief Administrative Officer (CAO).² Kurzius, along with the rest of McCormick's executive management, have not given investors any reason to believe that the company's structure, strategy, or objectives will be altered.

¹Thomson Reuters

²Bloomberg

³Morningstar

⁴McCormick & Company Inc. 10K

⁵SeekingAlpha

⁶CFRA S&P Global

⁷CFRA Industry Report

⁸Zacks Investment Research

Decision Making with Long Term Vision

Historically, the management at McCormick has shied away from acquisitions or purchases that in any way would inhibit the firm's ability to perform as a top tier company in the industry. This was seen during April of 2016, when McCormick walked away from a proposed merger with Premier Foods, a packaged food company based in the United Kingdom.³ A large reason for the fall through of the deal was McCormick's distaste for Premier's heavily leveraged balance sheet, specifically the firm's net debt/EBITDA, which was around 4x.³

This decision by the management of McCormick illustrates how the company's goal regarding acquisitions is not to "plant flags around the world", but rather, is focused on the potential value added that the action will result for both the company and their shareholders.

CCI Program

McCormick started its Comprehensive Continuous Improvement program (CCI) in 2009 as an effort to improve productivity across the organization.⁸ The program places a heavy emphasis on reducing costs and enhancing productivity and efficiency, and as a result, the firm has seen increased cash flow throughout the organization. The firm reported that over the last five years, a total savings of \$400 million was achieved due to the initiatives put forth by the program.⁴

Shareholder Value

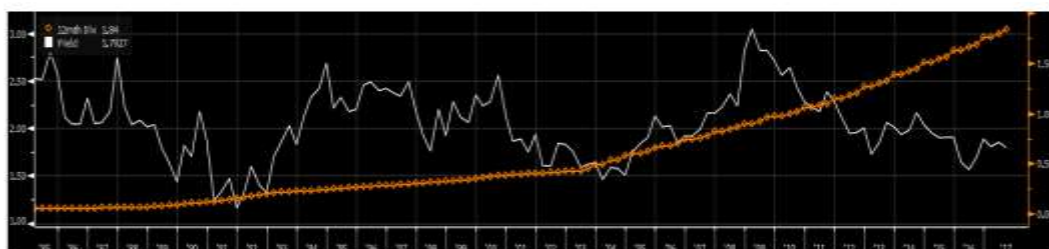
McCormick is one of 51 companies in the S&P 500 known as Dividend Aristocrats. In order to become a Dividend Aristocrat, a company must have consecutively increased their dividend for 25+ years, while also having a strong brand name and holding a dominant position in the industry that they operate in.⁵ McCormick has increased their dividend for the last 31 years, and the company has been paying a cash dividend for 90 consecutive years.⁵

Keeping the status of Dividend Aristocrat and providing its shareholders with value remains a top priority for the management of McCormick and the company as a whole. During the Q317 earnings conference call, while discussing shareholder concerns over the recent large acquisition of RB Foods, management was quoted as saying,

"By curtailing our share repurchase program and M&A activities, and utilizing the expected strong cash flow from the combined businesses, we will pay down prepayable debt. We're committed to returning to our historic credit profile over time. We have paid a dividend for 90 consecutive years with annual increases in the past 31 consecutive years. We are a dividend aristocrat and plan to maintain that status."

Figure 4: McCormick & Company Inc. Dividend Growth Since 1985

Reference the orange studded line for cash dividend per share for the last 31 years



Source: Bloomberg

Industry Overview and Competitive Positioning

McCormick operates in the Food Products industry within the Consumer Staples sector. The Food Products industry is comprised of 42 companies with a market capitalization over \$1 billion. The Food Products industry has severely underperformed both the Consumer Staples sector and the S&P index by around 10% and 15%, respectively (as of November 21, 2017). The industry's underperformance demonstrates how the Food Products industry is mostly uncorrelated to the market as a whole, which provides both safety to the investor when the market faces periods of pullbacks, but also lags the returns of other industries in the case of a bull market.

¹Thomson Reuters

²Bloomberg

³Morningstar

⁴McCormick & Company Inc. 10K

⁵SeekingAlpha

⁶CFRA S&P Global

⁷CFRA Industry Report

⁸Zacks Investment Research

Figure 5: Food Products Industry Return vs. Consumer Staples Sector and the S&P 500

Graph depicts YTD returns



Source: Bloomberg

Industry Analysis

The Food Products industry is composed of many large companies, all which specialize in manufacturing and distributing different types of food products. The largest companies operating in the Food Products industry by market capitalization are Kraft Heinz Co., Mondelez International Inc., Danone SA, General Mills Inc., and Tyson Foods Inc., respectively.² These companies produce a large amount of various food products, but do not directly compete within the market and sub industry that McCormick operates in.

In analyzing McCormick's competitors, we find that there is really no company that directly competes with the firm due to McCormick's wide industry moat. No company is able to provide the vast product lineup that McCormick does while simultaneously serving its customer base in over 150 countries across the world.

The closest competitors to McCormick are ConAgra Brands Inc., Ingredion Inc., Darling Ingredients Inc., and B&G Foods Inc.¹ All of these companies offer items such as hot sauces, spices, and seasonings through their product lines, but those items are not in the top revenue generating part of their businesses.

The barriers to entry of the Food Products industry are high. Smaller firms struggle to compete with larger companies due to their inability to keep up with the large capital requirements needed to establish manufacturing facilities.⁷ In addition, the high costs of marketing the products and forming distribution channels also inhibit smaller firms from gaining traction in the industry. Moreover, due to the mature nature of this industry, one popular way for companies to increase sales is by acquiring other smaller companies, adding yet another threat to undersized firms in the industry.⁷

There is a moderate threat of substitutes to companies operating in the Food Products industry. This threat generally depends on what sub category of the industry a company is operating in. For example, a company like General Mills has a great amount of threat of substitute products to their cereal brands from companies like Kellogg's. Mondelez has tough competition gaining an edge over Kraft Heinz with regards to their snack products, as the two firms are the largest global Food Products companies in the world. On the contrary, some sub categories of this industry face little threat due to the niche market that they operate in. A few of these industries include the organic food products market and the spices and seasonings market.

Firms like Whole Foods Market have a solid grasp on the organic foods market due to a strong product offering and a nationally recognized brand name. The company's threats of substitute products are mitigated due to the firm's distinguished place in the industry and their high-quality products, and this is seen through the fact that although the prices are higher than normal grocery store prices, people are still willing to pay more to have the company's higher-grade products.

A company operating in the spices and seasonings market do not have a large threat of substitute products, due to the fact that there are not many producers of those products, and that there is no substitute for certain spices and seasonings because most of those products are commodities. One of the largest threats that firms

¹Thomson Reuters²Bloomberg³Morningstar⁴McCormick & Company Inc. 10K⁵SeekingAlpha⁶CFRA S&P Global⁷CFRA Industry Report⁸Zacks Investment Research

in this industry face is the loss of customers to private label brands because of the lower cost of those products. As previously mentioned, McCormick has made an effort to alleviate this threat by successfully penetrating that segment of the market.

Financial Analysis

In assessing and forecasting McCormick's financial statements, it is clear that the company will continue to grow and be extremely profitable due to its ability to generate excess free cash while simultaneously cutting costs.

Comparison of Important Industry Related Financial Ratios

In comparing key financial ratios between McCormick and its competitors, McCormick stands out as the most profitable company among its peers and demonstrates great financial health. McCormick's ROE is around 29%, compared to the average of 17.71% among the five companies. This further illustrates how McCormick is generating plentiful cash, and is providing shareholders with an excellent return on their invested money. In addition, the ROE for McCormick is impressive when comparing it with the ROE of its peers because three out of four of the peer companies are operating with similar levels of debt, so this illustrates how McCormick is beating its competition without the use of financial leverage. We are forecasting McCormick's ROE to continue growing steadily as their acquisitions and global presence will accelerate its global growth, and are expecting the firm to earn around 34% return on equity at the end of FY 2019.

The same impressive results can be seen when comparing ROA percentages among the compared companies. McCormick has by far the highest amount of ROA, which displays how the company is more efficient in using its assets to create excess earnings than other firms in the industry. The ability of the firm to expand its business both vertically and horizontally by buying different companies around the world has added valuable assets and production facilities to their repertoire, which has in return resulted in greater profitability. Due to the rampant historical growth of assets within McCormick, we are projecting by the end of FY 2019 that the firm's ROA will be around 11%.

Operating margins are key in measuring a company's profitability. McCormick has an operating margin of around 14.50%, compared with an average between the five companies of 12.65%. This is a notable statistic, and demonstrates how McCormick has a surplus of revenue left over after paying for various costs of production. The company's operating high operating margin solidifies the fact that McCormick is conducting business very efficiently and producing large amounts of profits.

McCormick's current ratio is lower than its peers, and this can be credited to the firm's history of making frequent acquisitions. Although having a current ratio of 1.00 represents the firm's ability to exactly pay off all current liabilities with all current assets, investors usually like to see a ratio showing more of a cushion for the company. In McCormick's defense, the firm is a global leader in their industry and has a worldwide footprint in numerous food products markets. The company has a very wide industry moat and is a mature company that has a loyal customer base, and therefore, there is little threat that the company will have to cover large amounts of their debt on short notice. Furthermore, the acquisitions that add to the firm's debt level have provided and will continue to provide value added resources to McCormick, which will allow the firm to prosper and further expand their presence as a worldwide leader in the Food Products industry.

Figure 6: Comparison of Financial Ratios

Competitors of McCormick & Company Inc.

	Current Ratio	Debt/Capital	Operating Margin	PEG	ROE	ROA
Averages	1.82	49.29%	12.65%	2.52	17.71%	6.17%
\$MKC	1.00	46.91%	14.53%	2.45	28.65%	10.37%
\$BGS	2.67	68.72%	18.26%	2.13	17.60%	3.92%
\$CAG	1.17	42.36%	11.82%	2.70	16.60%	5.44%
\$DAR	1.98	45.75%	4.48%	-	5.32%	2.16%
\$INGR	2.30	42.70%	14.17%	2.81	20.37%	8.94%

Source: Bloomberg

¹Thomson Reuters

²Bloomberg

³Morningstar

⁴McCormick & Company Inc. 10K

⁵SeekingAlpha

⁶CFRA S&P Global

⁷CFRA Industry Report

⁸Zacks Investment Research

Earnings

McCormick's earnings history has been very solid and dependable over the last few years. In the last year, three out of four quarterly earnings results were positive surprises by greater than 2%, with the greatest surprise coming in the most recent quarter, 3Q17, which beat consensus estimates by 7.1%.¹ The other earnings release was in line with the consensus estimates. Furthermore, when looking at McCormick's earnings history over the last three years, seven out of twelve quarterly earnings results (roughly 58%) were positive surprises by greater than 2%, with the biggest surprise being over 9% in 3Q16.¹ We are estimating EPS for 2017 to be around \$4.30 per share, an increase of 13.50% from 4Q16, due to the positive effect that the RB Foods acquisition will have on McCormick's 4Q17 sales and revenues.

Cash Flow

McCormick's free cash flow has been growing at an average rate of over 16% over the past five years, and a rate of over 9% during the last 10 years, indicating that the company is operating very efficiently. The ability of McCormick to have continuous free cash flow growth year after year is a main reason why the firm has had the ability to raise their dividend for 31 consecutive years and achieve and maintain the status of Dividend Aristocrat. Using the computed future growth rates, the predicted amount of free cash flow to equity for McCormick at the end of FY 2019 will break \$800 million, offering \$5.51 per share of FCFE based off the current number of outstanding shares. McCormick's ability to generate excess free cash flow can be attributed in some part to the firm's cost cutting CCI program.

Balance Sheet

In forecasting McCormick's balance sheet, we see that the company moving forward will be operating with more debt than in previous years due to the large price that was paid for RB Foods (\$4.2 billion). Although this may be daunting at first glance, the company and management has been adamant about expressing their plans to pay down the debt as soon as possible. Also, in examining the RB Foods acquisition in greater detail, we see that McCormick used 4% debt to finance the purchase, which was a lower interest rate than expected when they originally planned the deal.⁵ The Reckitt Benckiser business is currently yielding 6.5%, so in fact, McCormick is using "cheap" debt to finance this acquisition.⁵ In addition, the firm's current ratio will stay in safe areas, remaining right around 1.00, with projections showing 0.97 for the end of this year, 0.93 for FY 2018, and 0.90 for FY 2019. Overall, the projection of the balance sheet for McCormick illustrates that the company will continue to operate resourcefully and with low risk, even after taking into account the firm's most recent acquisition and its history of making frequent acquisitions.

Investment Risks

Volatile Commodity Costs

The potential volatility of commodity prices remains one of the biggest threats to McCormick. There has been continued inflation in the prices of vanilla and garlic, which have increased by two or three times their previous price levels in the last year¹. The firm has anticipated continued inflation in the prices of the aforementioned commodities, as well as the prices of pepper and capsicums, through the end of 2017. Over the past five years, the cost of pepper has climbed by five times its value in 2012.¹

In order to combat the risk of fluctuating commodity prices, McCormick is exploring alternative ways to offset this rising cost (instead of just raising their prices). The company's management has discussed solutions such as adjusting packaging to cut costs or removing additional costs from its underlying business.¹

Foreign Currency Risk

McCormick generates around 45% of its sales from international customers across the globe, and thus is exposed to risk through foreign exchange rates and currencies. The decrease in the value of the U.S. Dollar throughout this year has eaten away at some of the company's profits, and the political turmoil in some parts of the world could end up losing the firm money as well.

Unfavorable View on Acquisition Activity

Some shareholders of McCormick believe that the \$4.2 billion price that the firm paid to acquire RB Foods was too large of a cost. McCormick had to take a large debt position to go through with the purchase, and this initially frightened investors and shareholders. The concern came from uncertainty about if this acquisition would force the company to shift away from prioritizing the creation shareholder value, as the firm has done for decades. As previously mentioned in the management section of this report, the management of McCormick stated that they will be committed to paying down debt and will honor their shareholder-friendly dividend policy.⁵

¹Thomson Reuters²Bloomberg³Morningstar⁴McCormick & Company Inc. 10K⁵SeekingAlpha⁶CFRA S&P Global⁷CFRA Industry Report⁸Zacks Investment Research

Figure A: Income Statement

\$ in millions, FY 2017, 2018, and 2019 Projected

McCormick & Co Inc (MKC US) - Income Statement

In Millions of USD except Per Share 12 Months Ending	FY 2005 11/30/2005	FY 2006 11/30/2006	FY 2007 11/30/2007	FY 2008 11/30/2008	FY 2009 11/30/2009	FY 2010 11/30/2010	FY 2011 11/30/2011	FY 2012 11/30/2012	FY 2013 11/30/2013	FY 2014 11/30/2014	FY 2015 11/30/2015	FY 2016 11/30/2016	FY 2017 Est 11/30/2017	FY 2018 Est 11/30/2018	FY 2019 Est 11/30/2019
Revenue	2,592.0	2,716.4	2,916.2	3,176.6	3,192.1	3,336.8	3,637.6	4,014.2	4,123.4	4,243.2	4,296.3	4,411.5	4,620.0	5,410.5	5,992.2
+ Sales & Services Revenue	—	—	—	—	3,192.1	3,336.8	3,637.6	4,014.2	4,123.4	4,243.2	4,296.3	4,411.5	4,620.0	5,410.5	5,992.2
- Cost of Revenue	1,555.4	1,601.8	1,724.4	1,888.4	1,862.4	1,919.1	2,175.1	2,396.4	2,457.6	2,513.0	2,555.0	2,579.5	2,823.0	3,163.6	3,503.8
+ Cost of Goods & Services	—	—	—	—	1,662.4	1,919.1	2,175.1	2,396.4	2,457.6	2,510.0	2,555.0	2,579.5	2,823.0	3,163.6	3,503.8
Gross Profit	1,036.6	1,114.6	1,191.8	1,288.2	1,329.7	1,417.7	1,522.5	1,617.8	1,665.8	1,730.2	1,741.3	1,832.0	2,005.0	2,246.8	2,488.4
+ Other Operating Income	—	—	—	—	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
- Operating Expenses	651.3	772.6	806.3	870.6	846.6	907.3	962.2	1,037.9	1,061.0	1,122.0	1,125.8	1,166.1	1,276.2	1,430.2	1,584.0
+ Selling, General & Admin	—	—	—	—	797.7	855.2	924.1	980.0	1,009.4	1,060.0	1,063.0	1,108.3	1,213.2	1,359.3	1,505.7
+ Research & Development	—	—	—	—	40.9	52.7	50.1	57.8	61.5	62.0	60.8	61.0	66.0	74.0	82.3
+ Other Operating Expenses	—	—	—	—	0.0	0.0	0.0	0.0	-3.7	0.0	0.0	-3.4	-3.7	-4.2	-4.6
Operating Income (Loss)	354.7	342.0	384.9	417.6	483.1	509.8	540.3	580.0	604.8	608.2	617.5	665.9	728.8	816.7	904.5
- Non-Operating (Income) Loss	—	—	—	—	50.4	47.1	48.9	52.2	51.1	48.6	52.2	51.8	56.7	63.5	70.4
+ Interest Expense, Net	48.2	53.7	60.6	56.7	52.8	49.3	51.2	54.6	53.3	49.7	53.3	56.0	61.3	68.7	76.1
+ Interest Income	48.2	53.7	60.6	56.7	52.8	49.3	51.2	54.6	53.3	49.7	53.3	56.0	61.3	68.7	76.1
+ Foreign Exchange (Gain) Loss	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
+ Other Non-Op (Income) Loss	—	—	—	—	-2.4	-2.2	-2.3	-2.4	-2.2	-1.1	-1.1	-4.2	-4.6	-5.2	-5.7
Pretax Income (Loss), Adjusted	316.3	269.7	323.0	356.4	432.7	462.7	491.4	527.8	553.7	559.6	565.3	614.1	672.1	753.1	834.1
- Abnormal Losses (Gains)	11.2	57.9	34.8	35.8	16.2	0.0	0.0	1.7	54.3	5.8	69.1	24.9	27.9	30.5	33.8
+ Market/Acquisition Expenses	—	—	—	—	—	—	—	1.7	4.3	—	3.6	5.5	6.0	6.7	7.5
+ Asset Write-Down	—	—	—	28.0	—	—	—	—	—	—	10.7	—	—	—	—
+ Impairment of Goodwill	—	—	—	—	—	—	—	—	—	—	—	2.6	2.8	3.2	3.5
+ Impairment of Intangible	—	—	—	—	—	—	—	—	6.4	—	—	—	—	—	—
+ Restructuring	—	—	—	—	16.2	—	—	—	25.0	5.2	50.8	16.8	18.4	20.6	22.8
+ Other Abnormal Items	—	—	—	—	—	—	—	—	10.6	—	4.0	—	—	—	—
Pretax Income (Loss), GAAP	316.3	269.7	323.0	356.4	416.5	462.7	491.4	526.1	499.4	554.4	496.2	589.2	644.8	722.6	800.3
- Income Tax Expense (Benefit)	36.7	64.7	32.2	100.6	133.0	110.0	142.6	139.8	133.6	145.9	131.3	153.0	167.4	187.6	207.6
+ Current Income Tax	—	—	—	—	109.0	107.5	104.6	115.5	140.3	139.8	130.3	153.0	211.2	236.7	262.2
+ Deferred Income Tax	—	—	—	—	24.0	10.5	38.0	24.3	-15.3	6.1	1.0	-40.0	-43.8	-43.1	-54.3
+ Tax Allowance/Credit	—	—	—	—	0.0	0.0	0.0	—	—	—	—	—	—	—	—
- (Income) Loss from Affiliates	—	—	—	—	-16.3	-25.5	-25.4	-21.5	-23.2	-29.4	-36.7	-36.1	-39.5	-44.3	-43.0
Income (Loss) from Cont Ops	219.6	205.0	230.8	255.8	299.8	370.2	374.2	407.0	389.0	437.9	401.6	472.3	516.9	534.9	592.5
- Net Extraordinary Losses (Gains)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
- Discontinued Operations	—	—	—	—	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
+ XO & Accounting Changes	—	—	—	—	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Income (Loss) Incl. MI	219.6	205.0	230.8	255.8	299.8	370.2	374.2	407.0	389.0	437.9	401.6	472.3	516.9	534.9	592.5
- Minority Interest	4.7	2.8	0.7	0.0	—	—	—	—	—	—	—	0.0	0.0	0.0	0.0
Net Income, GAAP	214.9	202.2	230.1	255.8	299.8	370.2	374.2	407.0	389.0	437.9	401.6	472.3	516.9	534.9	592.5
- Preferred Dividends	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
+ Other Adjustments	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Net Income Available to Common, GAAP	214.9	202.2	230.1	255.8	299.8	370.2	374.2	407.0	389.0	437.9	401.6	472.3	516.9	534.9	592.5

Source: Bloomberg

¹Thomson Reuters²Bloomberg³Morningstar⁴McCormick & Company Inc. 10K⁵SeekingAlpha⁶CFRA S&P Global⁷CFRA Industry Report⁸Zacks Investment Research

Figure B: Balance Sheet

\$ in millions, FY 2017, 2018, and 2019 Projected

McCormick & Co. Inc (MCK US) - Balance Sheet																		
In Millions of USD except Per Share	FY 2002	FY 2003	FY 2004	FY 2005	FY 2006	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011	FY 2012	FY 2013	FY 2014	FY 2015	FY 2016	FY 2017 E.H.	FY 2018 E.H.	FY 2019 E.H.
12 Month Ending	11/30/2002	11/30/2003	11/30/2004	11/30/2005	11/30/2006	11/30/2007	11/30/2008	11/30/2009	11/30/2010	11/30/2011	11/30/2012	11/30/2013	11/30/2014	11/30/2015	11/30/2016	11/30/2017	11/30/2018	11/30/2019
Total Assets	413.0	251.0	393.0	393.0	430.0	455.0	385.0	395.0	505.0	559.0	790.0	650.0	712.0	824.0	884.0	925.0	1013.0	1013.0
+ Cash & Cash Equivalents	413.0	251.0	393.0	393.0	430.0	455.0	385.0	395.0	505.0	559.0	790.0	650.0	712.0	824.0	884.0	925.0	1013.0	1013.0
+ ST Investments	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
+ Accounts & Notes Receivable	303.0	347.0	401.0	383.0	379.0	456.5	414.7	385.0	396.7	427.0	483.0	436.1	430.6	452.0	465.3	432.1	522.0	531.0
+ Accounts Receivable, Net	303.0	347.0	401.0	383.0	379.0	456.5	414.7	385.0	396.7	427.0	483.0	436.1	430.6	452.0	465.3	432.1	522.0	531.0
+ Notes Receivable, Net	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
+ Prepaids	263.0	382.0	292.0	344.0	405.7	430.2	420.0	457.0	417.6	453.3	650.0	476.9	715.0	793.0	756.3	601.7	849.0	909.0
+ Prepaids, Net	263.0	382.0	292.0	344.0	405.7	430.2	420.0	457.0	417.6	453.3	650.0	476.9	715.0	793.0	756.3	601.7	849.0	909.0
+ Work in Progress	120.0	112.0	150.0	151.0	112.0	286.2	206.0	220.0	343.5	344.0	341.0	372.0	490.6	390.0	420.0	445.2	472.0	500.0
+ Finished Goods	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
+ Other Inventory	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
+ Other ST Assets	90.0	26.1	35.0	55.0	45.0	75.7	75.7	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
+ Derivatives & Hedging Assets	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
+ Misc ST Assets	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Total Current Assets	724.0	762.0	864.0	889.0	893.4	983.3	968.3	979.5	1,093.9	1,222.9	1,285.4	1,320.2	1,416.2	1,351.4	1,421.8	1,337.7	1,433.7	1,433.7
+ Property, Plant & Equip, Net	292.1	458.2	438.6	463.1	463.3	467.8	461.1	483.0	488.0	523.1	447.3	376.6	402.7	418.4	469.4	420.5	453.0	491.1
+ Property, Plant & Equip	292.1	458.2	438.6	463.1	463.3	467.8	461.1	483.0	488.0	523.1	447.3	376.6	402.7	418.4	469.4	420.5	453.0	491.1
+ Accumulated Depreciation	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
+ ST Investments	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
+ Other ST Assets	88.1	527.0	1,030.0	1,030.0	1,042.0	1,010.0	1,010.0	1,010.0	1,040.0	2,044.0	2,040.0	2,010.0	2,050.0	2,014.0	2,050.0	2,310.0	2,423.0	2,555.0
+ Total Intangible Assets	165.2	176.3	628.1	822.3	391.4	1,081.0	1,081.0	1,081.0	1,040.0	2,044.0	2,040.0	2,010.0	2,050.0	2,014.0	2,050.0	2,310.0	2,423.0	2,555.0
+ Goodwill	439.7	200.7	209.3	462.0	400.0	412.0	412.0	412.0	412.0	412.0	412.0	412.0	412.0	412.0	412.0	412.0	412.0	412.0
+ Other Intangible Assets	6.5	6.2	6.2	6.2	6.2	6.2	6.2	6.2	6.2	6.2	6.2	6.2	6.2	6.2	6.2	6.2	6.2	6.2
+ Derivatives & Hedging Assets	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
+ Prepaid Pension Costs	390.0	210.0	190.0	190.0	455.0	380.0	320.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
+ Misc ST Assets	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Total Noncurrent Assets	1,296.2	1,366.1	1,395.6	1,471.5	1,466.0	1,604.4	2,252.0	2,411.9	2,405.8	2,664.8	2,866.0	3,075.5	2,996.1	3,015.2	3,214.1	3,410.9	3,422.0	3,520.0
Total Assets	1,990.2	2,148.2	2,260.6	2,377.7	2,568.0	2,787.5	3,220.3	3,387.8	3,493.7	4,087.8	4,165.4	4,445.7	4,412.3	4,472.6	4,835.9	4,997.1	5,293.7	5,545.7
Liabilities & Shareholders' Equity																		
+ Payables & Accruals	175.1	193.8	195.1	198.2	224.4	243.2	266.1	686.6	721.6	783.5	750.0	847.4	843.0	836.3	1,023.3	1,123.8	1,220.4	1,264.4
+ Accounts Payable	175.1	193.8	195.1	198.2	224.4	243.2	266.1	686.6	721.6	783.5	750.0	847.4	843.0	836.3	1,023.3	1,123.8	1,220.4	1,264.4
+ Other Payables & Accruals	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
+ ST Debt	117.0	111.8	113.2	106.1	0.0	16.6	10.6	584.0	98.1	96.0	222.4	216.1	270.0	243.6	300.2	420.6	474.1	520.6
+ ST Borrowings	117.0	111.8	113.2	106.1	0.0	16.6	10.6	584.0	98.1	96.0	222.4	216.1	270.0	243.6	300.2	420.6	474.1	520.6
+ ST Capital Leases	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
+ Current Portion of LT Debt	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
+ Other LT Debt	360.0	382.9	494.4	354.7	474.7	465.4	414.0	414.0	414.0	414.0	414.0	414.0	414.0	414.0	414.0	414.0	414.0	414.0
+ Deferred Revenue	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
+ Derivatives & Hedging	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
+ Misc LT Liabilities	360.0	382.9	494.4	354.7	474.7	465.4	414.0	414.0	414.0	414.0	414.0	414.0	414.0	414.0	414.0	414.0	414.0	414.0
Total Current Liabilities	672.3	710.7	772.7	699.0	700.5	664.3	1,026.1	810.2	824.8	833.3	1,072.4	1,063.1	1,122.0	1,239.6	1,422.7	1,562.3	1,715.5	1,883.8
+ LT Debt	450.0	448.8	465.0	462.9	560.6	515.5	605.2	875.8	719.3	1,027.7	793.0	1,010.0	1,011.1	1,011.1	1,011.1	1,011.1	1,011.1	1,011.1
+ LT Borrowings	450.0	448.8	465.0	462.9	560.6	515.5	605.2	875.8	719.3	1,027.7	793.0	1,010.0	1,011.1	1,011.1	1,011.1	1,011.1	1,011.1	1,011.1
+ LT Capital Leases	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
+ Other LT Liabilities	185.4	200.5	292.0	290.7	281.0	251.7	245.1	250.0	344.0	446.0	456.4	418.0	466.0	465.7	521.0	500.6	500.0	602.1
+ Accrued Liabilities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
+ Pension Liabilities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
+ Deferred Revenue	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
+ Derivatives & Hedging	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
+ Misc LT Liabilities	185.4	200.5	292.0	290.7	281.0	251.7	245.1	250.0	344.0	446.0	456.4	418.0	466.0	465.7	521.0	500.6	500.0	602.1
Total Noncurrent Liabilities	646.3	658.1	678.2	744.6	650.6	631.2	1,130.9	1,226.1	1,122.2	1,476.0	1,277.6	1,438.3	1,482.3	1,547.3	1,751.3	1,673.9	1,791.6	1,910.3
+ Preferred Equity and Hybrid Capital	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
+ Share Capital & APIC	256.7	262.8	326.0	388.5	444.0	501.0	518.1	634.0	756.3	821.9	906.2	962.4	956.6	1,038.4	1,064.2	1,064.2	1,064.2	1,064.2
+ Common Stock	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
+ Treasury Stock	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
+ Retained Earnings	456.9	432.6	434.0	388.5	344.7													

Figure C: Statement of Cash Flows

\$ in millions, FY 2017, 2018, and 2019 Projected

McCormick & Co Inc (MKC US) - Free Cash Flow to Equity Valuation \$ 100.06				
Projected Free Cash Flow Statement				
In Millions of USD except Per Share	FY 2016	FY 2017 Est.	FY 2018 Est.	FY 2019 Est.
	12/31/2016	12/31/2017	12/31/2018	12/31/2019
Growth Rate		9.66%	9.66%	4.50%
Cash from Operating Activities				
+ Net Income	472,300	517,918	567,942	593,499
+ Depreciation & Amortization	108,700	119,193	130,712	136,534
+ Non-Cash Items	-4,400	-4,825	-5,291	-5,529
+ Stock-Based Compensation	25,600	28,073	30,784	32,163
+ Deferred Income Taxes	-40,000	-43,863	-48,100	-50,265
+ Other Non-Cash Adj	10,000	10,966	12,025	12,566
+ Chg in Non-Cash Work Cap	81,500	83,372	98,004	102,414
+ (Inc) Dec in Accts Receiv	-21,000	—	—	—
+ (Inc) Dec in Inventories	-33,000	-42,767	-46,838	-49,008
+ Inc (Dec) in Accts Payable	47,000	51,540	56,518	59,061
+ Inc (Dec) in Other	94,500	103,627	113,636	118,750
+ Net Cash From Disc Ops	0,000	0,000	0,000	0,000
+ Net Working Capital	119,70	131,261	143,939	157,842
Cash from Operating Activities	777,800	852,925	935,306	984,820
Cash from Investing Activities				
+ Change in Fixed & Intang	-152,100	-166,791	-182,901	-191,131
+ Disp in Fixed & Intang	1,700	1,864	2,044	2,136
+ Disp of Fixed Prod Assets	1,700	1,864	2,044	2,136
+ Disp of Intangible Assets	0,000	0,000	0,000	0,000
+ Acq of Fixed & Intang	-153,800	-168,655	-184,945	-193,267
+ Acq of Fixed Prod Assets	-153,800	-168,655	-184,945	-193,267
+ Acq of Intangible Assets	0,000	0,000	0,000	0,000
+ Net Change in LT Investment	0,000	0,000	0,000	0,000
+ Dec in LT Investment	0,000	0,000	0,000	0,000
+ Inc in LT Investment	0,000	0,000	0,000	0,000
+ Net Cash From Acq & Div	-116,400	-127,643	-133,971	-146,270
+ Cash from Divestitures	4,200	4,606	5,051	5,278
+ Cash for Acq of Subs	-120,600	-132,248	-145,022	-151,548
+ Cash for JVs	0,000	0,000	0,000	0,000
+ Other Investing Activities	1,400	1,535	1,684	1,759
+ Net Cash From Disc Ops	0,000	—	—	—
Cash from Investing Activities	-267,100	-292,898	-321,188	-335,642
Free Cash Flow to Firm	1,044,900	1,145,823	1,256,494	1,320,462
Cash from Financing Activities				
+ Dividends Paid	-217,800	-242,158	-269,241	-299,352
+ Cash From (Repayment) Debt	55,700	61,929	68,855	76,556
+ Cash From (Repay) ST Debt	251,700	279,850	311,147	345,945
+ Cash From LT Debt	6,000	6,671	7,417	8,247
+ Repayments of LT Debt	-202,000	-224,591	-249,709	-277,636
+ Cash (Repurchase) of Equity	-209,400	-232,819	-258,857	-287,807
+ Increase in Capital Stock	33,300	37,024	41,165	45,769
+ Decrease in Capital Stock	-242,700	-269,843	-300,022	-333,576
+ Other Financing Activities	0,000	0,000	0,000	0,000
+ Net Cash From Disc Ops	0,000	0,000	0,000	0,000
+ Effect of Foreign Exchange Rates	-13,700	-15,232	-16,936	-18,830
Total Change in Net Debt	-371,500	-413,048	-459,242	-510,603
Free Cash Flow to Equity	673,400	732,775	797,252	809,859

Source: Bloomberg

¹Thomson Reuters²Bloomberg³Morningstar⁴McCormick & Company Inc. 10K⁵SeekingAlpha⁶CFRA S&P Global⁷CFRA Industry Report⁸Zacks Investment Research

Figure AA: Free Cash Flow to Equity Valuation Model

\$ in millions

McCormick & Co Inc (MKC US) - Free Cash Flow to Equity Valuation				
Projected Free Cash Flow per Share				\$ 100.06
	FY 2016 12/31/2016	FY 2017 Est. 12/31/2017	FY 2018 Est. 12/31/2018	FY 2019 Est. 12/31/2019
Growth Rate		9.66%	9.66%	4.50%
Net Income	\$ 3.69	\$ 4.05	\$ 4.44	\$ 4.64
Depreciation & Amortization	\$ 0.85	\$ 0.93	\$ 1.02	\$ 1.07
Change in Net Working Capital	\$ (0.94)	\$ (1.03)	\$ (1.12)	\$ (1.18)
Operating Cash Flow	\$ 5.47	\$ 6.00	\$ 6.58	\$ 6.88
Operating Cash Flow	\$ 5.47	\$ 6.00	\$ 6.58	\$ 6.88
Net Capital Expenditures	\$ (2.09)	\$ (2.29)	\$ (2.51)	\$ (2.62)
Free Cash Flow to Firm	\$ 7.56	\$ 8.29	\$ 9.09	\$ 9.50
Free Cash Flow to Firm	\$ 7.56	\$ 8.29	\$ 9.09	\$ 9.50
Change in Net Debt	\$ (2.90)	\$ (3.23)	\$ (3.59)	\$ (3.99)
Free Cash Flow to Equity	\$ 4.66	\$ 5.06	\$ 5.50	\$ 5.51
Free Cash Flow to Equity	\$ 4.66	\$ 5.06	\$ 5.50	\$ 5.51
Terminal Value	\$ 215.83			
Total Cash Flows to Equity	\$ 221.33			
Discounted Value	\$ 193.13			
Potential Upside	93.01%			

Relevant Information	
Shares outstanding:	128.00
Required return on equity (r):	7.05%
Avg. FCF growth last 5 years	9.66%

FCF Growth last 10 Years		
Year	FCF	Change
2016	\$504.00	9.09%
2015	\$462.00	24.53%
2014	\$371.00	1.64%
2013	\$365.00	5.80%
2012	\$345.00	41.98%
2011	\$243.00	-18.73%
2010	\$299.00	-10.21%
2009	\$333.00	45.41%
2008	\$229.00	56.85%
2007	\$146.00	-35.40%
2006	\$226.00	-14.72%
2005	\$265.00	
Average		9.66%

ST and LT Debt Growth last 10 Years		
Year	Total Debt	Change
2016	\$1,447.20	3.79%
2015	\$1,394.40	8.52%
2014	\$1,284.90	4.20%
2013	\$1,233.10	5.23%
2012	\$1,171.80	-6.41%
2011	\$1,252.10	42.24%
2010	\$880.30	-11.18%
2009	\$991.10	-20.02%
2008	\$1,239.20	71.37%
2007	\$723.10	11.08%
2006	\$651.00	14.21%
2005	\$570.00	
Average		11.18%

Change in NWC			
CA 2016	\$1,421.80	CL 2016	\$1,422.70
CA 2015	\$1,357.40	CL 2015	\$1,238.60
Change in CA	\$64.40	Change in CL	\$184.10
Change in NWC	(\$119.70)		

CAPM			
10 Yr Treasury	2.36%	r	7.05%
S&P Return	9.66%	MRP	7.30%
β	0.643		

¹Thomson Reuters²Bloomberg³Morningstar⁴McCormick & Company Inc. 10K⁵SeekingAlpha⁶CFRA S&P Global⁷CFRA Industry Report⁸Zacks Investment Research

Figure AB: Two-Stage Dividend Discount Valuation Model

\$ in millions

McCormick & Co Inc (MKC US) - Two Stage Dividend Discount Model \$ 100.06

12 Months Ending	FY 2012 12/31/2012	FY 2013 12/31/2013	FY 2014 12/31/2014	FY 2015 12/31/2015	FY 2016 12/31/2016
Earnings/Share	\$3.04	\$2.91	\$3.34	\$3.11	\$3.69
Average Earnings/Share					\$3.22
Dividends	\$1.27	\$1.39	\$1.51	\$1.63	\$1.76
Average Dividend					\$1.51
Return on Equity	24.83%	21.52%	23.51%	23.20%	28.65%
Average Return on Equity					24.34%
Payout Ratio	41.78%	47.77%	45.21%	52.41%	47.70%
Average Payout Ratio					46.99%
Plowback Ratio	58.22%	52.23%	54.79%	47.59%	52.30%
Average Plowback Ratio					53.03%
Average 5 Year Growth Rate	12.91%				
Late Stage Growth Rate	5.00%				
2017 Dividend	\$1.88				
2018 Projected Dividend	\$2.12				
2019 Projected Dividend	\$2.40				
Terminal Value	\$106.91				
Total Discounted Value	\$113.31				
Potential Upside	13.24%				

CAPM			
10 Yr Treasury	2.36%	k	7.05%
S&P Return	9.66%	MRP	7.30%
β	0.643		

¹Thomson Reuters²Bloomberg³Morningstar⁴McCormick & Company Inc. 10K⁵SeekingAlpha⁶CFRA S&P Global⁷CFRA Industry Report⁸Zacks Investment Research

Disclosures:

Ownership and material conflicts of interest:

The author(s), or a member of their household, of this report holds a financial interest in the securities of this company.

The author(s), or a member of their household, of this report knows of the existence of any conflicts of interest that might bias the content or publication of this report. The conflict of interest is...

Receipt of compensation:

Compensation of the author(s) of this report is not based on investment banking revenue.

Position as an officer or director:

The author(s), or a member of their household, does serves as an officer, director or advisory board member of the subject company.

Market making:

The author(s) does not act as a market maker in the subject company's securities.

Ratings key:

A security is rated as either a BUY, HOLD or SELL. A BUY rating is given when the security is expected to deliver positive returns that sufficiently compensate for the risks over the next twelve-month period. A SELL rating is given when the security is expected to deliver negative returns over the next twelve months, while a HOLD rating implies flat returns over the next twelve months.

Disclaimer:

The information set forth herein has been obtained or derived from sources generally available to the public and believed by the author(s) to be reliable, but the author(s) does not make any representation or warranty, express or implied, as to its accuracy or completeness. The information is not intended to be used as the basis of any investment decisions by any person or entity. This information does not constitute investment advice, nor is it an offer or a solicitation of an offer to buy or sell any security.

¹Thomson Reuters

²Bloomberg

³Morningstar

⁴McCormick & Company Inc. 10K

⁵SeekingAlpha

⁶CFRA S&P Global

⁷CFRA Industry Report

⁸Zacks Investment Research