

Cal-Maine Foods, Inc. (CALM)

Neutral: Upcoming Challenges and Opportunities

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We look to hold our position in CALM. If the stock drops below \$35.00 we look to add to our position. If the stock price surges to \$43.00, we look to sell off a portion of our position. We like Cal-Maine's dominance in the egg production industry due to medium and increasing barriers to entry. The industry in which Cal-Maine operates is also experiencing strong retail demand. However, we are still concerned with future feed prices and the low revenue growth the egg production industry experiences. We are also concerned with new cage free chicken regulations that will come into effect in the next few years.

Source: Bloomberg

Market Data	
Last Price	\$37.42
Shares O/S (mm)	44.1
52 wk High-Low	35.97-46.66
Market Cap. (mm)	\$1,828.7
Enterprise Value (mm)	\$1,650.6

Source: Bloomberg

Financial Summary			
Data	FY19A	FY20A	FY21E
Revenue	1,361.2	1,351.6	1,411.7
Adj. EBITDA	##	##	##
Adj. EPS	\$3.93	\$3.96	\$4.20
Consensus Revenue	1,375	1,353	1,412
Consensus Adj. EBITDA	132.5	79.93	93.9
Consensus Adj. EPS	\$1.30	\$50	\$0.60

Source: Bloomberg

Key Investment Highlights

Third quarter revenue went up by 3.4% compared to the previous year.

Net sales for the third fiscal quarter of 2021 were \$359.1 Million. The CEO Dolph Baker was satisfied with earnings results and attributed increased sales to strong retail demand for shell eggs. Earnings was also impacted by the recovery of the food service industry. As COVID-19 restrictions have been lifted, the demand from the Food Service and Hospitality industry have recovered.

The total number of eggs produced in the third quarter was 3.3% less compared to the previous year.

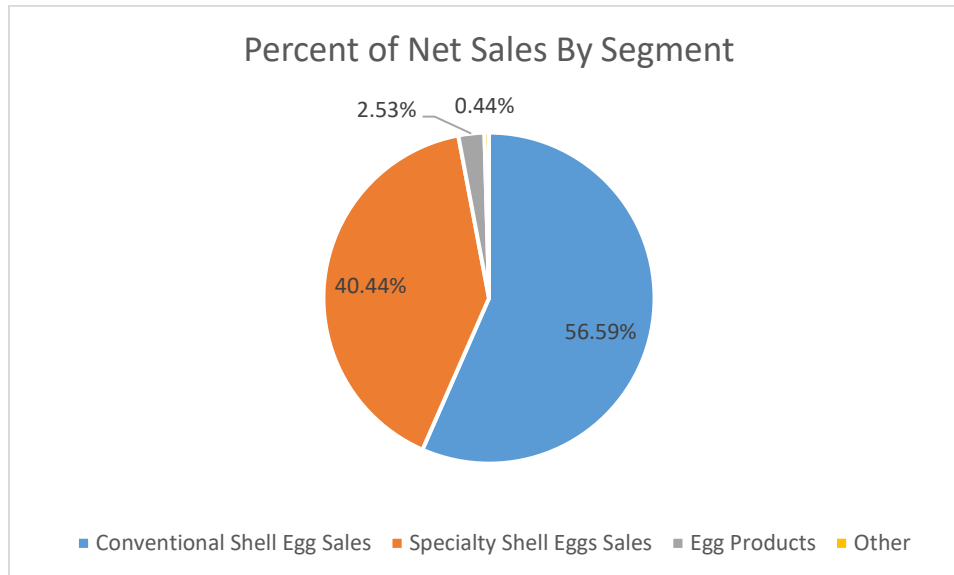
The USDA reported that Cal-Maine had 327.4 million hens on March 1st, 2021. Although this is three million hens fewer than the previous year, the hatch between October 2020 and February 2021 was 2.6 percent larger than the previous period. The number of eggs in incubators is also up 20% in February compared to last year. These growing supply indicators and returning demand from the Food Service segment will impact market prices for shell eggs in the near future.

Demand for specialty egg sales remained favorable in the third fiscal quarter of 2021.

Sales for specialty eggs totaled \$145.2 million dollars in the third fiscal quarter of 2021. Net sales for specialty eggs grew 16.2% compared to the same quarter last year. This growth in sales follows a trend of increased demand for specialty shell eggs by health-conscious consumers looking for inexpensive sources of protein.

Company Overview

Cal-Maine Foods primarily produces, grades, packages, and markets fresh shell eggs, including cage-free, nutritionally enhanced, and conventional eggs. Cal-Maine is headquartered in Jackson, Mississippi and is the largest producer of fresh shell eggs in the United States. Most of its eggs are sold in the Southwestern, southeastern, mid-western, and mid-Atlantic regions of the United States. Their segments have performed as seen below.



Industry Overview

Cal-Maine Foods participates in the chicken egg production industry. Companies in this industry raise chickens for egg production. 70% of eggs produced in this industry are sold as shell eggs to grocery stores (60%), food service customers (7%), and to foreign customers (3%).

Company Competitors

Major competitors for Cal-Maine foods include Rose Acres Farms, Versova Holdings L.L.P., Hillandale Farms, Daybreak farms, and dozens of other smaller egg producers. These companies raise hens and mainly engage in the production of fresh shell eggs.

Segment Analysis

Historical revenue for the third fiscal quarter of 2020 is below. Conventional Shell Eggs 56.59% (\$203), Specialty Shell Eggs 40.44% (\$145), Egg Products 2.53% (\$9.1), Other 0.44% (\$1.6).

Recent Earnings Commentary

Cal-Maine beat analyst revenue estimates this past quarter. This is because specialty egg sales were up 16.2 percent compared to the previous year. More eggs were produced this quarter and 8 thousand more egg dozens were sold in the third fiscal quarter compared to the same period last year. Higher egg prices also contributed to earnings and increased over the quarter.

Sell-Side Viewpoint

The sell side thesis is that the egg production industry has historically had low revenue growth and new regulations surrounding caged chickens pose a threat. California, Colorado, Washington, Oregon, Massachusetts, Rhode Island, and Michigan have all passed laws that regulate the amount of space given to chickens. These regulations will come into effect over the next few years and Cal-Maine could be excluded from large markets if they are too slow to shift to cage free production of eggs.

Positive & Negative Catalysts

The next positive catalyst for this stock is fourth quarter earnings. Next quarters earnings will be reported on July 19th. This stock has seen a slight increase and decrease in price but has mostly traded sideways over the previous quarter. Another catalyst is egg prices. In the press release for third quarter earnings, it was mentioned that egg prices have increased towards the end of the previous quarter. An increase in egg prices will have a positive impact on this stock.

Risks associated with the stock include an increase in feed costs. Feed costs make up 55-60% of production costs. A dramatic increase in feed costs could eat away at the already small gross profit margin and could lead to major losses. Additionally, if revenue decreases for the 4th quarter the stock price could drop \$1.00-3.00 dollars.

What to Watch – Next Earnings

Current street estimates expect the revenue of Cal-Maine foods to surpass \$409 Million this upcoming quarter. We believe that this estimate is attainable due to the cyclical nature of Cal-Maine and recent demand trends. Historically, this upcoming quarter experiences the most revenue compared to the rest of the year. This has to do with the fluctuations in egg demand throughout the year. Because of strong retail demand and historical trends, Cal-Maine should be able to easily attain this revenue estimate. If revenue expectations are met, the stock price will only see a slight increase (\$1.00-\$3.00).

Final Take

Recommendation: Hold on Cal-Maine Foods shares unless the price drops below \$35.00 (buy) or if the stock price rises above \$43.00 (sell). I believe that this decision will add value to the portfolio. As strong retail demand for eggs continues and Cal-Maine acquires more cage free producers, the stock price of Cal-Maine will increase. Lastly, if Cal-Maine fails to meet new regulations surrounding cage free egg production, we should look to sell off most of our position in Cal-Maine Foods.