CCL Industries

Materials
TSX: CCL.B
Market Outperform | Hold

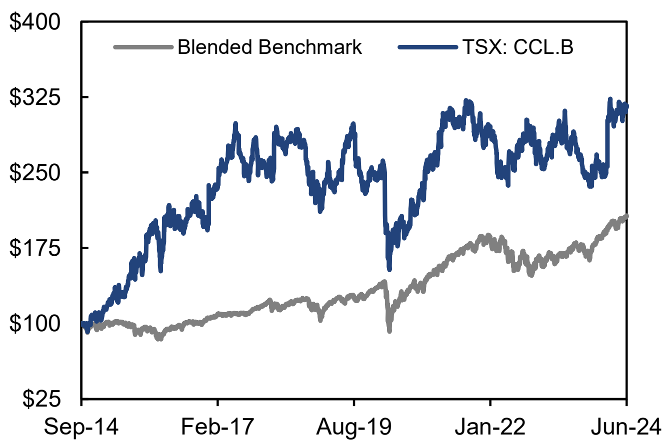
June 30, 2024
Joshua Olson, Investment Analyst

Return on Investment	
Current Share Price	$71.94
Target Price	$82.00
Dividend Yield	1.60%
Implied Return	16%
Conviction Rating	1

Market Profile	
52-Week Range	$52.82 - $74.49
Market Capitalization ($mm)	$12,914
Net Debt ($mm)	$1,608
Enterprise Value ($mm)	$14,522
Beta (5-Year Monthly)	0.56

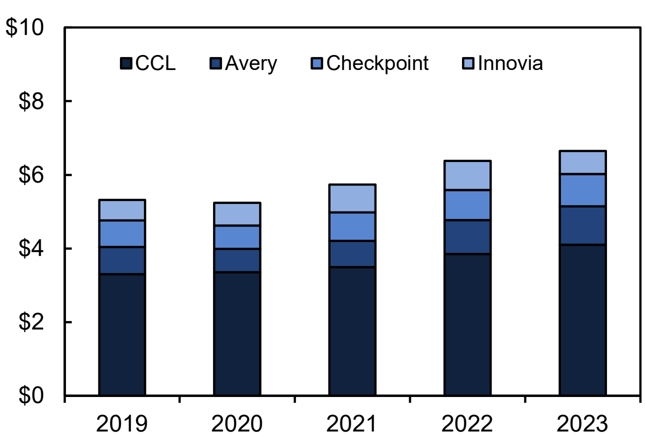
Metrics	2024E	2025E	2026E
Revenue ($mm)	$7,031	$7,276	$7,439
EBITDA ($mm)	$1,459	$1,517	$1,601
EPS	$4.16	$4.38	$4.67
EV/EBITDA	10.0x	9.6x	9.1x

Holding Period Trading Performance (Indexed to $100)



Source: S&P Capital IQ

Figure 1: Annual Revenue by Segment ($B)



Source: S&P Capital IQ

Business Description

CCL Industries (TSX: CCL.B) manufactures and sells labels, consumer printable media products, technology-driven label solutions, polymer banknote substrates, and specialty films. The Company operates globally under four segments: (1) CCL, (2) Avery, (3) Checkpoint, and (4) Innovia.

CCL: The CCL segment is the world's largest converter of pressure-sensitive and extruded film materials for a range of decorative, instructional, security, and functional applications for government institutions and large global customers. Its largest global customers consist of packaging, healthcare, chemical, consumer durable, and automotive companies. Specific end-use products are sold in parallel to the aforementioned companies.

Avery: The Avery segment is the world's largest supplier of labels, specialty converted media, and software solutions to enable short-run digital printing in businesses and homes alongside complementary end-use products. These end-use products include labels for marketing and shipping use, binders, sheet protectors, and writing instruments. These products are sold through distributors, mass-market stores, and e-commerce retailers.

Checkpoint: The Checkpoint segment is a leading developer in Radio Frequency and RFID-based technology systems for loss prevention and inventory management applications.

Innovia: The Innovia segment is a global producer of specialty high-performance, multi-layer, surface-engineered polypropylene films such as cavitated and metallised films for label, packaging, and security applications.

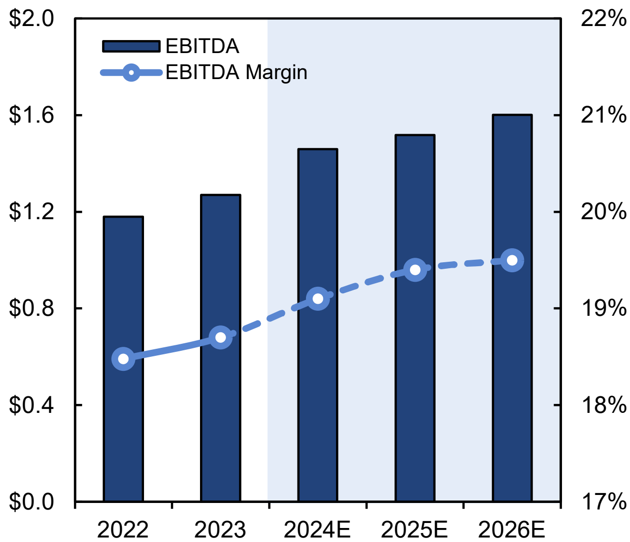
Recent Acquisitions

In Q3 2023, CCL acquired all of Imprint Energy's (IEI) intellectual property for $26.6mm. IEI was a start-up proprietary technology company with expertise in ultrathin, non-hazardous, and non-toxic printed batteries for devices, sensors, and wearables. In Q3 2023, CCL acquired Faubel, a global specialist in labels for pharmaceutical clinical trials for $169.7mm, as well as Creaprint for ~$37.7mm, which was a leader in producing labels for food and beverage packaging. CCL's focus on acquisitions supports its competitive advantage as it enters new markets and gains access to proprietary manufacturing technology. Since the market is fragmented with small private players, it has the balance sheet strength to be opportunistic.

Industry Overview

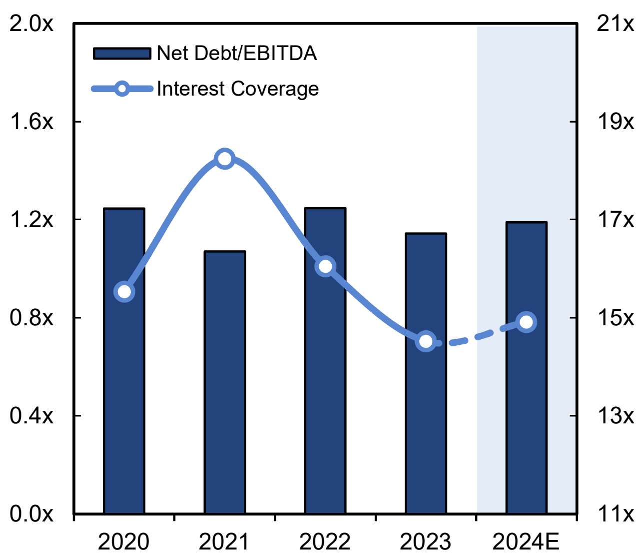
The packaging and label industry is mature, with the majority of growth coming from acquisitions of businesses or specific expertise. Many end-market users have experienced steady pressure to optimize supply chains after the COVID-19 pandemic. This has driven companies to focus on cutting costs, which has led to consolidation within the industry. Many end-market plastics are dependent on commodity pricing, such as petrochemicals, oil and gas, and base metals. The correlation between raw commodity input costs and end-market pricing is mitigated by long-term relationships with both suppliers and customers, reducing volatility and passing through costs to the end market. Competitors within the industry (consists of NYSE: ATR, CCK: TSX: WPK) have started to (cont.)

Figure 2: LHS EBITDA ($B) vs RHS EBITDA Margin



Source: CPMT Estimates, S&P Capital IQ

Figure 3: LHS Net Debt/EBITDA vs RHS Int. Coverage



Source: CPMT Estimates, S&P Capital IQ

Figure 4: Operating Segment EBIT ($mm) & EBIT Margin

	EBIT ($mm)		**EBIT Margin (%)**	
Operating Segment	**2023**	**2024E**	**2023**	**2024E**
CCL	***$633***	***$697***	***15.4%***	***15.9%***
AVERY	***$199***	***$205***	***19.2%***	***19.5%***
INNOVIA	***$132***	***$149***	***15.1%***	***16.2%***
Checkpoint	***$45***	***$78***	***7.2%***	***12.1%***

Source: Street Research

focus on specialized manufacturing equipment to satisfy customer requirements and maintain a competitive edge. An emerging theme with technology use within the industry includes software that manages plastic waste and exhibits more sustainable manufacturing practices. Plastic film, sheet and label manufacturing in Canada has experienced uneven results over the five years to 2023 as a result of extreme volatility in commodity prices and the pandemic. Growth has been limited despite strong economic conditions prior to the pandemic, stifled by increasing import competition from U.S. manufacturers that have competitive advantages, such as shared borders and economies of scale. Imports are anticipated to increase an annualized 1.2% to $4.7B over the five years to 2028 while satisfying 62.4% of domestic demand in 2028. Plastic products produced by the industry are not environmentally friendly, necessitating innovation for substitute products that are better for the environment. This trend is expected to have a negative effect on the industry, though industrial consumption will likely persist at steadily increasing rates and offset this negative effect.

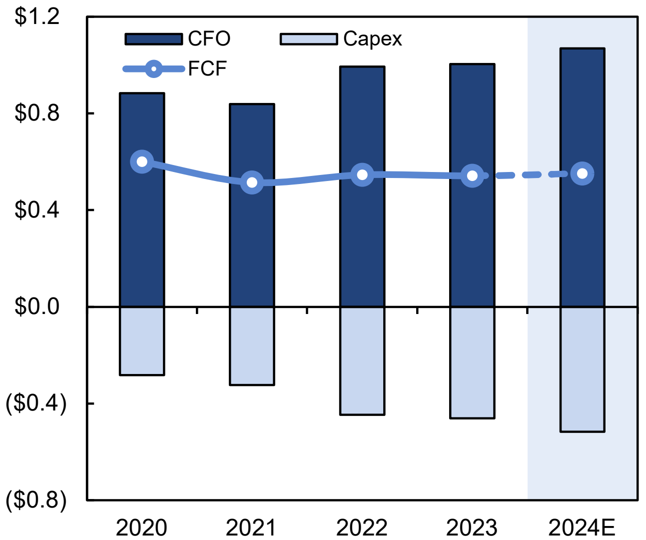
Mandate Fit

Quality Management: CCL is led by its CEO and President, Geoffrey Martin, who joined the Company in 2001 and assumed the role of CEO in 2008. Before joining CCL, Martin was the SVP of Worldwide Converting Graphic and Specialty Tapes within CCL's business segment, Avery. During his tenure, Martin has overseen numerous acquisitions, including Innovia for $1.1B. CCL's management team is separated into business segment leaders, strengthening niche industry and customer knowledge, and increasing efficiency and speed. CEO compensation consists of 32% base salary, while the remaining 68% is at-risk. Executive performance-based compensation is tied to EPS and Operating Income targets to maximize shareholder value and alignment.

Competitive Advantage: The Company's main competitive advantage stems from its strong customer service, process technology, market-leading brands, and ability to develop proprietary technologies and manufacturing techniques. CCL's global footprint of sales in North America, Europe, and Emerging Markets of 41%, 31%, and 28%, respectively, highlighting CCL's global presence. With 213 manufacturing facilities worldwide, CCL has a broader geographical reach compared to its peers. This enables the Company to enter a diverse range of markets and attract many new customers. With the plastic labelling industry highly fragmented, CCL has the advantage of acquiring smaller companies with niche technologies accessing new markets as evidenced by its eight acquisitions in 2023. These acquisitions in conjunction with the building of new plants around the world, have positioned CCL as a leader in home & personal care, healthcare, security, consumer durables, and food and beverage categories. The Company also benefits from a strong organic growth algorithm through its internal capacity additions and embedded margin expansion opportunities.

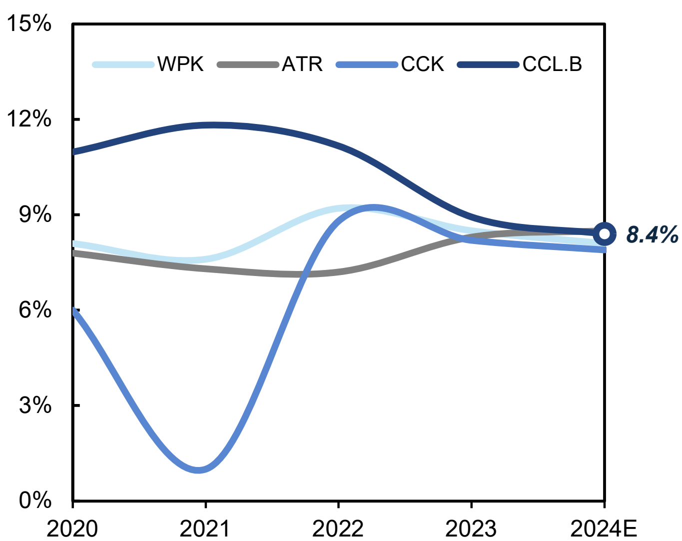
Strong Balance Sheet: CCL has consistently maintained BBB and Baa2 balance sheet ratings from S&P and Moody's, respectively. The Company holds a 1.2x Net Debt/EBITDA ratio compared to the peer average of 3.0x. CCL can maintain low interest expenses in an inflationary environment with long-term senior bonds at a weighted average term of four years and a coupon rate of 3.26%. The Company has adequate liquidity with $748mm of cash on hand and $944mm of undrawn revolving credit facilities. CCL's management has a disciplined approach to capital structure, with a current and quick ratio of 2.0x and 1.4x, respectively, and a Debt/Equity ratio of 0.3, with a weighted average interest rate on total debt of 2.8%.

Figure 5: Annual FCF Generation ($B)



Source: CPMT Estimates, S&P Capital IQ

Figure 6: Return on Capital vs Peers



Source: Bloomberg

Growing Free Cash Flow: CFO increased 61% QoQ to $171.2mm due to high organic sales growth while capex increased by 46% to $179.0mm in the same respective period. The capex increase was mainly attributable to capacity additions to support the home & personal care segment. The Company is focused on increasing its capex spend to expand its business geographically and add capacity in its facilities. CCL's annualized run-rate dividend is $1.16, giving a yield of 2%. The Company has paid a quarterly dividend since 2004 and has increased it every year since.

Risks

Raw Material Costs: CCL may experience adverse headwinds in an inflationary environment due to the nature of raw materials used in its inputs. However, the Company can pass these costs on to the customer through price increases. Polypropylene is the most significant input cost and is traded in the market, with prices linked to the market price of natural gas and refining capacity.

Political and Economic Instability: CCL operates through 213 manufacturing facilities in 43 countries. The impact of political and economic events in countries will impact the Company's operations and ability to deliver its products to market.

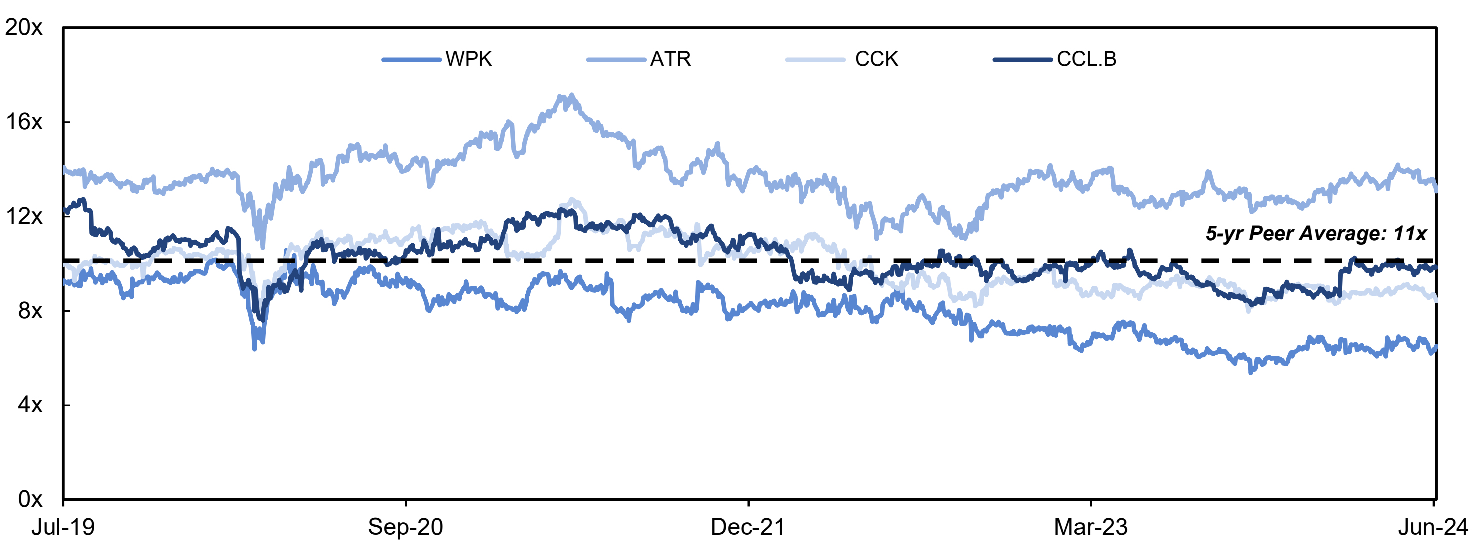
Acquisition Integration Risk: Finally, CCL's aggressive acquisition strategy poses a risk if accretive M&A opportunities become scarce. There can be no assurance that the Company will be able to identify attractive acquisition opportunities in the future or have the required resources to complete desired acquisitions. Poor integration of future acquired businesses can also have an adverse effect on the operational efficiency of CCL.

Investment Thesis and Valuation

CCL was valued at $82 using a five-year DCF with a WACC of 9.81%. The terminal value was derived using a 50/50 blend of (1) the Gordon growth method, using a terminal growth rate of 2.0%, and (2) an EV/EBITDA exit multiple of 11x.

The CPMT views CCL as a leader in the plastic labeling industry with operations spanning the globe. The Company's ability to acquire businesses with leading technology and enter new markets solidifies its competitive advantage. The Fund is confident in management's capital allocation track record and prudent discipline in consistently raising its dividend. The CPMT will continue to monitor CCL's performance and recommends a hold on the name.

Figure 7: NTM EV/EBITDA vs Peers



Source: S&P Capital IQ