Jeff Middleswart
jmiddleswart@btnresearch.com

Bill Whiteside, CFA
bwhiteside@btnresearch.com

August 1, 2019 | www.btnresearch.com

# Mondelez International 2Q19 Update
# Maintain NEUTRAL

We remain far from impressed with MDLZ's results. We are keeping it Neutral for now, but it is evident that the organic growth figures are likely being overstated by hyperinflation in Argentina. The company is not projecting that it will hit its $3 billion goal in free cash flow even with lower capital spending as some of the working capital stretching is now snapping back to consume cash flow.

- **We seriously question the 4.6% organic growth rate in 2Q for MDLZ** and the company boosted its annual forecast above 3% for sales growth after the quarter. All this growth is coming from hyperinflation in Argentina. Investors would have to believe that the smallest and weakest segment – Latin America at only 12% of total sales – is actually the rocket booster driving up results. The 4.6% organic growth is broken down as 3.0% higher pricing and 1.6% stronger volume.
-

| MDLZ 2Q | Pricing | Vol/Mix | Organic | FX | Acq/Divest | Real |
|---|---|---|---|---|---|---|
| Latin America | 11.5% | -0.6% | 10.9% | -15.7% | 0.0% | -4.8% |
| Asia/ME/Africa | 1.9% | 2.8% | 4.7% | -4.5% | -0.8% | -0.6% |
| Europe | 0.3% | 3.6% | 3.9% | -6.3% | 0.0% | -2.4% |
| North America | 3.5% | -1.0% | 2.5% | -0.4% | 0.9% | 3.0% |
| Total | 3.0% | 1.6% | 4.6% | | | 0.8% |

- **All the pricing is coming from Latin America, which is being done ahead of huge FX losses there.** If Latin America is so strong, why is volume negative? This is even worse because in 2018, this unit was suffering from a Brazilian trucking strike. Simply having that resolved boosted volumes in Brazil – yet the segment still posted negative volume growth. We think this picture of 10.9% organic growth in Latin America is very misleading.

- **If we pull Latin America out of the mix – as it actually posted the worst result on GAAP results as opposed to the highest on the company's organic definition – the organic growth rate here is 3.7% - not 4.6%. What does it say about the company's definition of organic growth when pulling the laggard division out of the mix makes results decline?**

| MDLZ 2Q | 2018 2Q | 2019 2Q | Org. Growth $ | Organic Growth |
|---|---|---|---|---|
| Asia/ME/Africa | $1,328 | $1,391 | $63 | 4.7% |
| Europe | $2,303 | $2,392 | $89 | 3.9% |
| North America | $1,675 | $1,717 | $42 | 2.5% |
| Total | $5,306 | $5,500 | $194 | 3.7% |

This makes much more sense to us. As seen in the first table, the company is taking FX losses in every unit. Where the FX losses are greatest, because the dollar is stronger – MDLZ has trouble taking pricing. Except, when there is hyperinflation and pricing is high but that doesn't translate into volume gains and FX losses exceed the organic growth.

- **We would still point out that FX losses are a way of life for MDLZ. It is not a case where there are good years and bad. This is why the company's 3% organic growth is never seen in actual sales changes.** It is also why sales since 2014 are down about 12% instead of being up 14% if 3% was compounded over the same period.

| Sales Growth | 1H19 | 2018 | 2017 | 2016 | 2015 |
|---|---|---|---|---|---|
| Actual | -0.8% | 1.0% | 1.2% | -3.3% | -11.6% |
| Organic | 4.6% | 2.4% | 0.9% | 1.3% | 1.4% |

- **We also noted that the company's forecast for Free Cash Flow is only $2.8 billion for 2019 vs. the goal of $3.0 billion.** This is with lower capital spending so far in 2019 by $67 million. The reason is the company's past efforts of stretching working capital is now reversing and they are consuming cash.

| W/C Cash Flow | 1H19 | 1H18 |
|---|---|---|
| Receivables | $135 | $112 |
| Inventory | -$145 | -$240 |
| Accts Payable | -$430 | -$325 |

There is some seasonality here, but we had been warning that MDLZ had been stretching payables and selling receivables into factoring deals to generate cash. In 2Q19, payables were down considerably even as inventory still rose albeit at a slower rate than last year. The company noted that factored receivables also fell just over $100 million along with declining figure on the balance sheet.

- **We still question that MDLZ continues to borrow money to plug its cash flow shortfall and debt is up to $18.0 billion.** It just raised the dividend to an annualized $1.65 billion against free cash flow of $2.8 billion for a 60% payout ratio. That is rising quickly, and MDLZ still likes to repurchase its shares at over 22x EPS even though EPS is only growing at its forecast adjusted rate of 5%, which includes about 3% growth as a result of spending considerable sums buying back stock. So 2% growth for 22x EPS with rising debt.

# Disclosure

*BTN Research is a research publication structured to provide analytical research to the financial community. Behind the Numbers, LLC is not rendering investment advice based on investment portfolios and is not registered as an investment adviser in any jurisdiction. Information included in this report is derived from many sources believed to be reliable (including SEC filings and other public records), but no representation is made that it is accurate or complete, or that errors, if discovered, will be corrected.*

*The authors of this report have not audited the financial statements of the companies discussed and do not represent that they are serving as independent public accountants with respect to them. They have not audited the statements and therefore do not express an opinion on them. Other CPAs, unaffiliated with Mr. Middleswart, may or may not have audited the financial statements. The authors also have not conducted a thorough "review" of the financial statements as defined by standards established by the AICPA.*

*This report is not intended, and shall not constitute, and nothing contained herein shall be construed as, an offer to sell or a solicitation of an offer to buy any securities referred to in this report, or a "BUY" or "SELL" recommendation. Rather, this research is intended to identify issues that investors should be aware of for them to assess their own opinion of positive or negative potential.*

*Behind the Numbers, LLC, its employees, its affiliated entities, and the accounts managed by them may have a position in, and from time-to-time purchase or sell any of the securities mentioned in this report. Initial positions will not be taken by any of the aforementioned parties until after the report is distributed to clients, unless otherwise disclosed. It is possible that a position could be held by Behind the Numbers, LLC, its employees, its affiliated entities, and the accounts managed by them for stocks that are mentioned in an update, or a BTN Thursday Thoughts.*