Weis Markets: Potential for Groundbreaking Gains?

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Executive Summary:

Weis Markets, Inc. (NYSE: WMK) is a supermarket chain with 197 stores in Pennsylvania, Maryland, New Jersey, Delaware, and West Virginia. The company has been in business for over 100 years and is headquartered in Sunbury, Pennsylvania. Weis Markets employs over 23,000 people and is a significant employer in the Mid-Atlantic region. Weis Markets operates a creamery, meat processing facility, and a large distribution center. The distribution center distributes products to Weis Markets stores throughout the Mid-Atlantic region.

Weis Markets is a well-managed company with a strong track record of profitability. The company has a loyal customer base and a strong brand reputation. Weis Markets is also well-positioned for future growth. The company is expanding its store base and investing in new technologies.

Weis Markets maintained strong margins throughout the lockdowns and inflation and increased its profit throughout the pandemic. Weis Markets has an impressive ROIC of 7.51% for the fiscal year 2022. Weis Markets' strong presence in the Mid-Atlantic states and its robust distribution network allow the company to maintain superior margins and profitability compared with larger chains such as Kroger.

Weis Markets trades at a discount relative to its intrinsic value. This is based on a DCF with outlined assumptions. The gap between intrinsic and market value exists due to decisions and actions (or lack thereof) the company has made that discourage investment and analysis.

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Introduction

Weis Markets is a small supermarket chain headquartered in Sunbury, Pennsylvania. Weis Markets was founded in 1912 by Harry and Sigmund Weis. Weis Markets is a regional business with 197 locations in seven states. Weis Markets is a publicly traded company on the New York Stock Exchange (NYSE) under the WMK ticker.

History

Weis Markets was founded in Sunbury, Pennsylvania, in 1912 by brothers Harry and Sigmund Weis. Weis Markets started as a local corner grocery store and was revolutionary in that it only accepted cash in exchange for goods. The adoption of cash-based sales allowed Weis Markets to offer lower prices than its competitors. Weis Markets' second location opened in Harrisburg, Pennsylvania, in 1915. The Weis brothers rapidly expanded throughout Pennsylvania and, by 1933, had 115 stores in 15 central Pennsylvania counties. By 1955, Weis Markets had consolidated all its corner grocery stores into 35 supermarkets. Over the next few decades, Weis

Markets expanded into regions outside of central Pennsylvania, including areas such as northeast Pennsylvania and eastern Pennsylvania. Weis Markets expanded via acquisitions of other local supermarket chains and new store openings. Today, Weis Markets operates 197 stores in seven Mid-Atlantic states.

Management

Top Executives

CEO: Jonathan Weis

Beginning date: February 2014

Jonathan Weis is the grandson of cofounder Harry Weis. Jonathan Weis holds a B.A. from Yale University. Mr. Weis started with the company in 1989 and worked in several roles, including produce merchandising, grocery procurement, and store operations. In 2004, Mr Weis became vice chairman and corporate secretary Mr. Weis was elected company chairman in 2015. Mr. Weis serves as an advisor for Pearl Holdings Acquisition Corp, an investment holding company. He also serves as a board member for Food Marketplace, Inc (FMI), a trade association that represents the food retail and wholesale industry in the United States. FMI lobbies on behalf of the food industry as well as supports innovation and research in the food industry. Mr. Weis currently holds a 27% stake in the company

CFO: Michael T. Lockard

Beginning date: January 2021

Michael Lockard graduated from Bellarmine University with a Bachelor’s in Accounting & Business Administration and a Master's in Business Administration. Mr. Lockard began his career at UPS, spending nearly twenty years with the global delivery service, including serving as VP of Finance/CFO of the Central U.S. District. Mr. Lockard then transitioned to Walmart, spending almost five years in Walmart’s financial shared services. After Walmart, Mr. Lockard transitioned to K-VA-T Food Stores, Inc. K-VA-T Food Stores is the parent company of Food City and Super Dollar. Mr. Lockard served as CFO and senior vice president (SVP) of K-VA-T Food Stores, Inc for nine years. In January 2021, Mr. Lockard transitioned to CFO, SVP, and treasurer of Weis Markets.

COO: Kurt Schertle

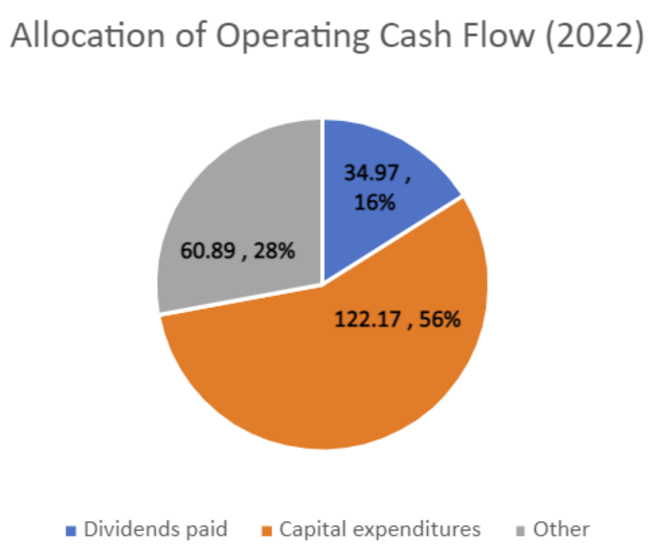
Beginning date: March 2014

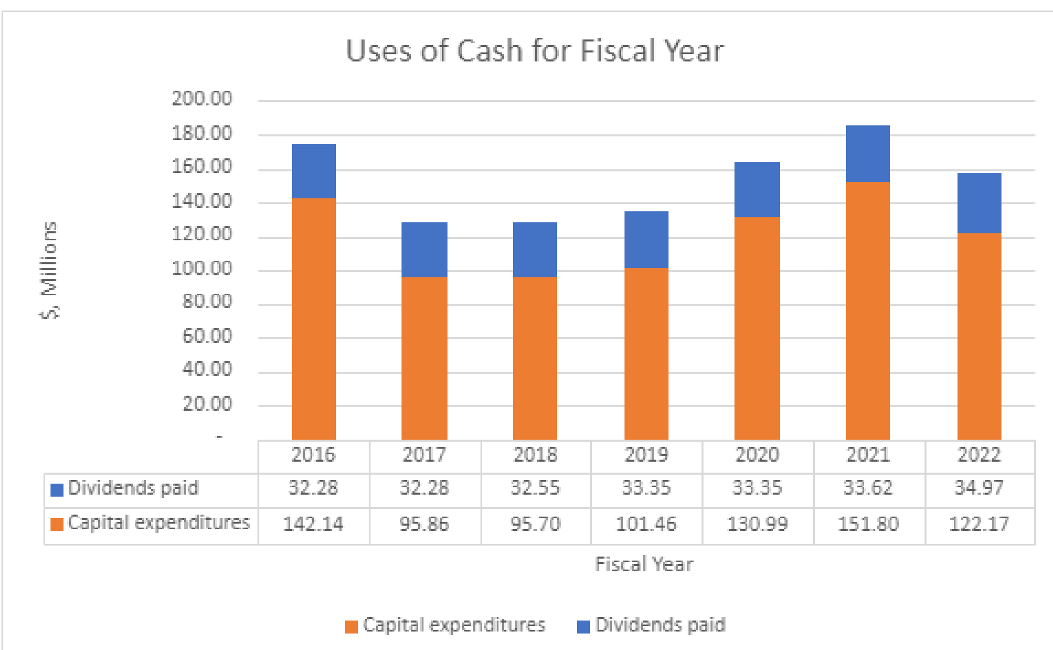
Kurt Schertle graduated with a bachelor's from Towson University. Kurt Schertle has worked at Weis Markets since 2009, when he joined as the VP of sales and merchandising. Mr. Schertle was promoted to senior VP of sales and merchandising in 2010 before being promoted to executive VP of sales and merchandising in 2012. Mr. Schertle was promoted to COO in 2014 and has served as COO since.

Capital Allocation

Weis Markets has a balanced capital allocation approach. The company has no interest-bearing liabilities and finances its operations entirely through equity and non-interest-bearing liabilities. Weis Markets wholly owns 101 of its stores and leases the remaining 96. The company utilizes its free cash flow for two primary uses.

1. Distributions to shareholders via dividends
2. Growth Capital expenditures
3. Maintenance capital expenditures
4. Acquisitions





	2016	2017	2018	2019	2020	2021	2022
Dividends paid	32.28	32.28	32.55	33.35	33.35	33.62	34.97
Capital expenditures	142.14	95.86	95.70	101.46	130.99	151.80	122.17

Weis Markets' dividend comprises 16% of its cash flow from operations and 36.5% of its free cash flow. The sustainable nature of the dividend further supplements Weis Markets' prudent capital allocation by removing much of the economic profit from market volatility. Weis Markets' aggressive swings in capital expenditures display the company's opportunistic approach to asset allocation.

Acquisitions:

Food Lion, 2016

In 2016, Weis Markets purchased 38 Food Lion supermarkets in Maryland, VA, and Delaware for $29.4 million. Weis Markets purchased 38 stores due to Food Lion's divestment of supermarkets. Food Lion had recently merged with European grocery companies Ahold and Delhaize Group, and regulators had Antitrust concerns for the new conglomerate. Weis described the purchase as below fair market value, citing that these stores were divestments to quell antitrust concerns.

Mars Super Markets, 2017

In 2017, Weis Markets acquired 5 Mars Super Markets stores in Baltimore County, MD, for $10 million. In the first quarter of 2017, these locations contributed $23.2 million to sales. Weis Markets was looking to build out its geographic foothold in Maryland further.

Nell's Family Market, 2018

In 2018, Weis Markets purchased a Nell's Family Market in East Berlin, PA, for $13 million. The new store contributed $4.1 million to Weis Markets' first quarter in 2017.

Martin's Food Markets, 2023

On January 25, 2023, Weis Markets announced it has entered a definitive agreement to acquire 16 Martin's Food Markets stores in Pennsylvania's Lehigh Valley and Poconos regions.

The transaction is expected to close in the second quarter of 2023 and further bolster Weis Markets' position in East Pennsylvania.

These transactions give us a clear picture of Weis Markets' acquisition strategy. Weis acquires stores with proven sales to expand its reach. Weis Markets combines its robust distribution network and innovative position to drive efficiency. The increase in efficiency allows Weis Markets to continue to acquire stores from medium-sized stores and drive accretive value for shareholders. In other words, Weis Markets' superior efficiency allows for a higher chance of positive outcomes than its less efficient competitors in acquisitions.

Business

Industry

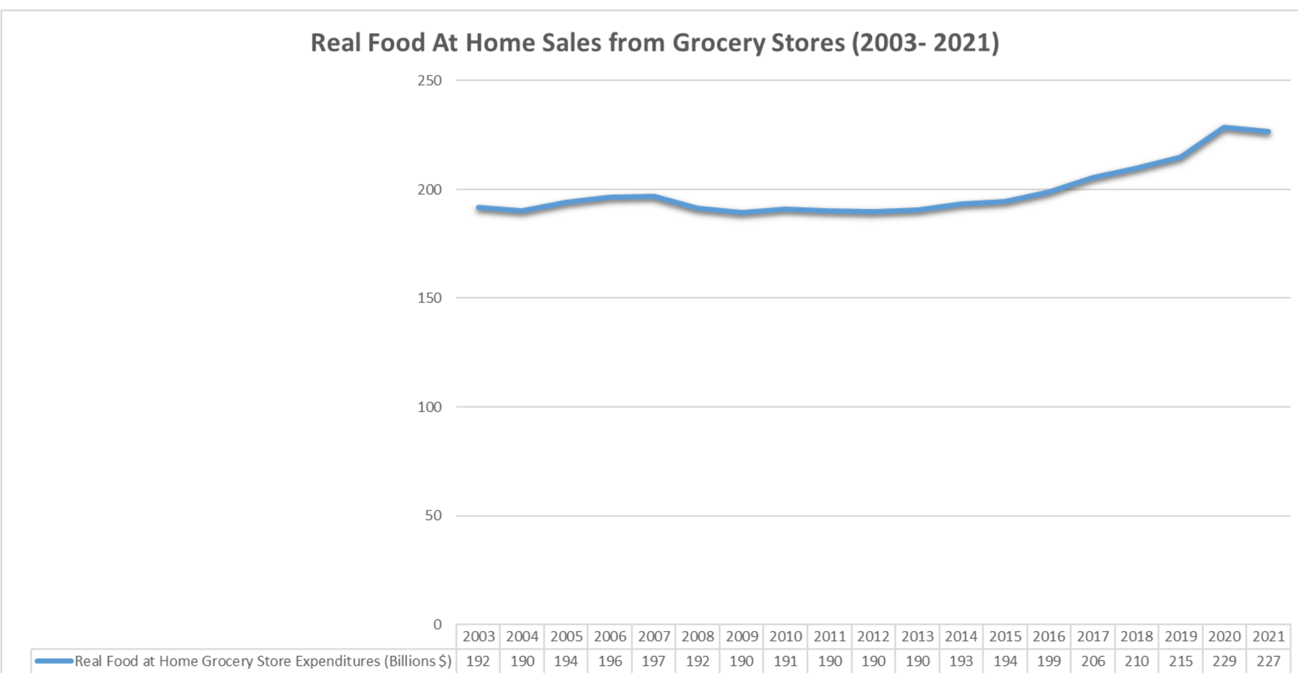
Supermarkets are physical stores that sell food products to consumers living in surrounding areas. There are four main subsegments of grocery stores.

- Traditional Supermarket
  - Grocery
  - Meat
  - Seafood
  - Deli
  - Beauty Products
- Limited assortment
  - Low-priced
  - Smaller quantities
  - Often franchise groceries
- Fresh Format
  - Organic
  - Whole Foods (product)
  - Ethnic foods
- Warehouse
  - Wholesale items
  - Large amount of few products
  - Large Quantity discounts

Each one of these four types of supermarkets comes with its respective pros and cons.

The supermarket industry is one of the most competitive businesses in the United States. The industry's margins are tight and dragged by high employment costs and inflation. Operating margins are typically below five percent. Inflation and supply chain disruptions can have unpredictable effects on the business.

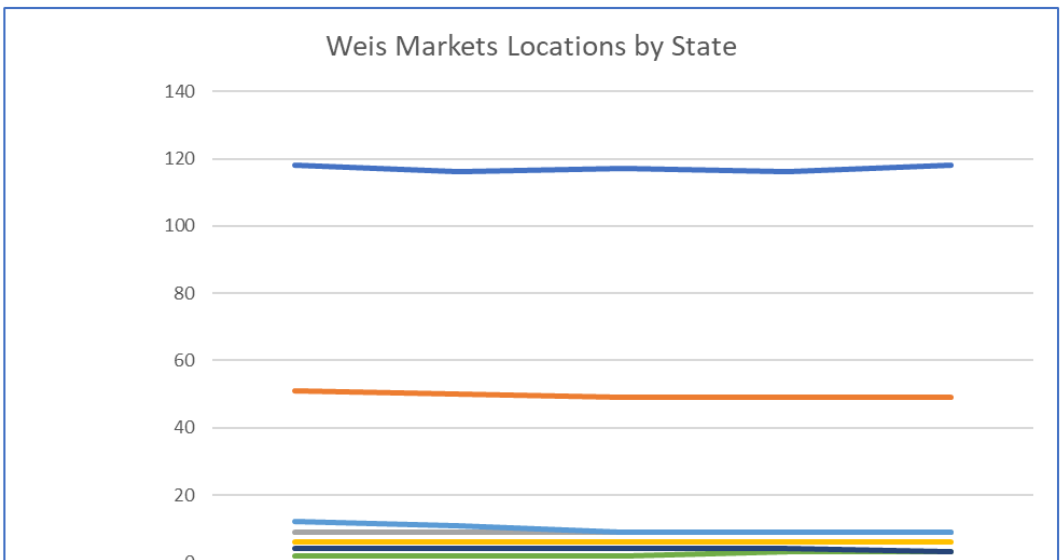
Due to the tight margins and competitive landscape, supermarkets build up robust distribution channels that allow them to distribute food among their various locations efficiently. To boost profits, larger supermarket chains often create their products, known as white-label products, outsourcing the production of store-branded goods. These white labels directly compete with mainstream name-brand items such as Kraft and Coca-Cola and host the supermarket’s brand. These products sell for significantly less money than the name-brand equivalent and have higher margins for the supermarket.



Source: Economic Research Service

The CAGR of Real food at home (FAH) in the United States is around .93%. This means that food consumption from grocery stores has been growing faster than inflation. If the last five years are considered solely, it sits around 2.65%, meaning that grocery stores have seen an increase in sales in the previous five years when inflation is considered. The long-term impacts of Covid are still unknown and further metrics are needed to determine if the grocery stores' resurgence is a long-term trend.

Market



	2018	2019	2020	2021	2022
Pennsylvania	118	116	117	116	118
Maryland	51	50	49	49	49
New York	9	9	9	9	9
New Jersey	6	6	6	6	6
Virginia	12	11	9	9	9
West Virginia	2	2	2	3	3
Delaware	4	4	4	4	3

Weis Markets operates supermarkets in the Mid-Atlantic region with an intense concentration in Central and Northeastern Pennsylvania. Weis Markets has three primary services that it aggregates its revenue into (Center Store, Fuel, and Pharmacy). Grocery consists of inventory sold within a Weis Markets supermarket, with Fuel and Pharmacy typically representing distinct areas inside and outside the store. Within grocery, Weis Markets sells food and everyday products that a consumer needs daily. Pharmacy consists of revenues on pharmacy services that Weis offers inside of its stores. Fuel consists of revenues generated on Weis Markets' gas stations.

Distribution

Weis Markets operates a single distribution center. The 1.3 million square foot distribution center is located in Milton, Pennsylvania. This location currently supports Weis Markets' seven-state operation and is instrumental in maintaining Weis Markets' above-average margins.

Weis Markets currently supplies 63% of its inventory from its distribution channel. The remaining 37% is distributed via vendors and wholesalers that stock shelves within Weis Markets' supermarkets. These products typically have lower margins for Weis than self-distributed products.

Structure

Weis Markets possesses no financing debt and operates its business through leases and equity. One hundred one of the stores' locations are owned, while the other ninety-six are under operating leases.

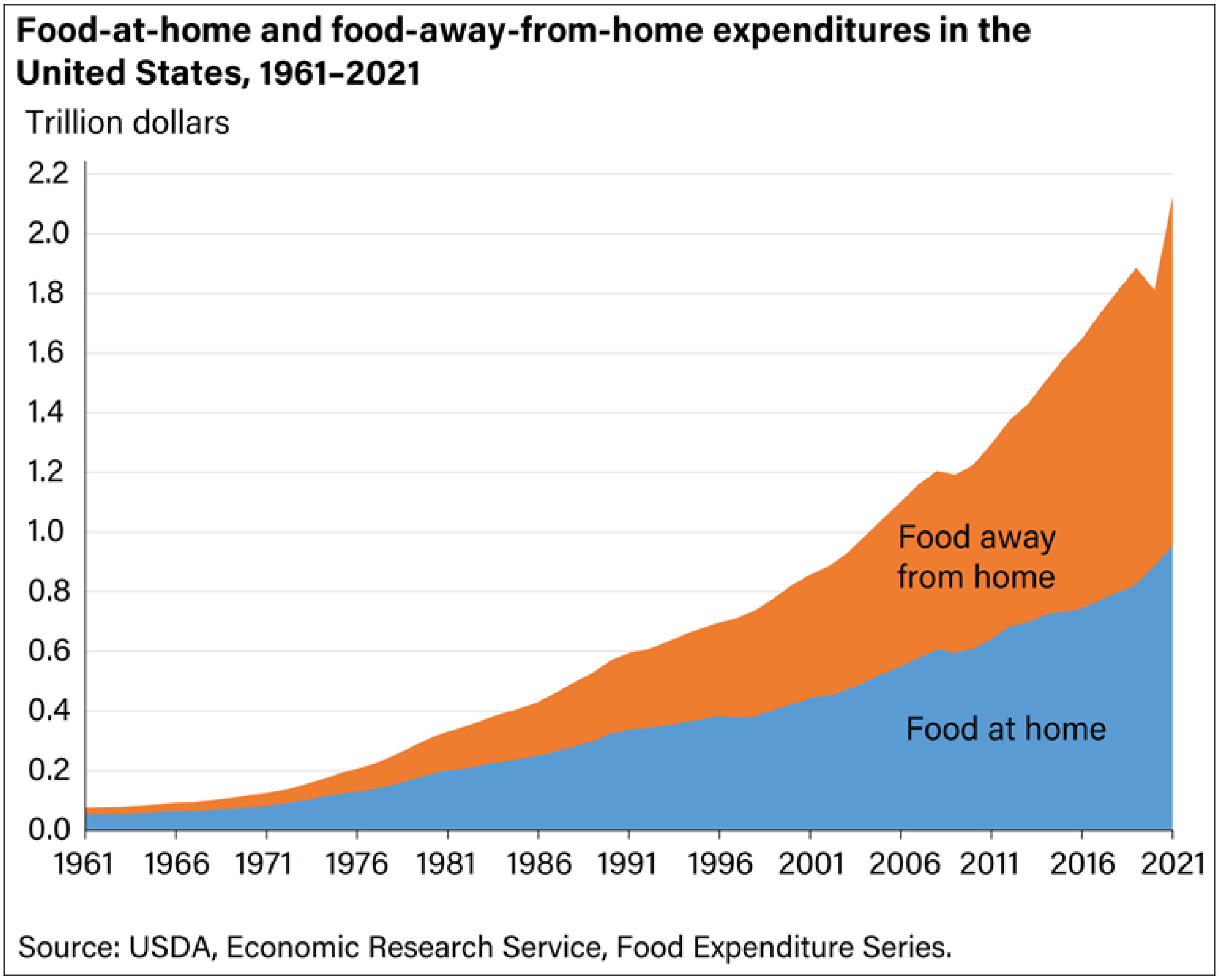
Of Weis Markets' 23,000 associates, 97% are hourly workers. Weis Markets depends on student workers to staff its stores after 4 P.M. and on weekends. Because of this model, Weis has access to an endless supply of workers and can sustain heavy turnover. However, the high turnover makes Weis Markets more susceptible to broader wage market shifts such as inflation and rising wages.

Technology

Weis Markets has invested heavily in modernizing its stores in the past few years. For example, Weis Markets has implemented self-checkout registers in its stores, lowering the need for cashiers and allowing for more checkouts during busier hours. Weis Markets has also implemented its online ordering service Weis 2 Go Online, which allows customers to have their groceries delivered straight to their car on arrival. Weis also offers a rewards program to its customers that allows its customers to turn grocery purchases into gas discounts. Finally, Weis Markets has an app that allows customers to claim in-app discounts on groceries and order them for pickup or delivery.

Weis continues to lean heavier into technology. The constant movement towards technology will result in higher operating efficiency and competitive advantage in the future. As Weis Markets acquires less efficient chains and retrofits them with the latest technology and business practices, it will be able to generate accretive value for the shareholders.

Consumer Defensive



As an industry, supermarkets provide more stable returns and less volatility than the broader market. This is the result of several factors working in the favor of supermarkets. First, most supermarkets offer a stable dividend that attracts less volatile investors and moves capital allocation away from the executives and towards the investors. This is also a result of the necessity for food regardless of the economic condition. However, adverse economic conditions harm supermarkets. For example, during economic booms, consumers may feel more inclined to eat out and consume more Food-away-from-home. The graph below displays total food spending by U.S. consumers, businesses, and government entities at 2.12 trillion in 2021.

When analyzed closely, it is apparent that Food-away-from-home tends to vary far more than Food-at-home spending. This intuitively makes sense, as restaurant spending aligns more with economic cycles than supermarket spending.

Another exciting trend on the graph is the rapid increase in Food-away-from-home spending relative to Food-at-home. In 1961 Food away from home spending accounted for 47% of food spending, while in 2021, it accounted for 55% of total food spending, indicating shifting consumer habits.

Moving forward, it is likely that supermarkets, and subsequently, Weis Markets, will offer less volatility than the broader market. This is backed up by the aforementioned fundamentals surrounding the supermarket industry.

Financials (For the Year Ending 12/31/22 & Quarter Ending 3/30/22)

For the following financial statements:

- ➢ Quarterly Figures are presented with Orange underlining.
- ➢ Analysis of quarterly financials are underlined.
- ➢ Full financial statements and disclosures can be found at sec.gov.

Income Statement

(amounts in thousands, except shares and per share amounts) For the Fiscal Years Ended December 31, 2022, December 25, 2021 and December 26, 2020	**2022 (53 weeks)**	2021 (52 weeks)	2020 (52 weeks)
Net sales	**$ 4,695,943**	$ 4,224,417	$ 4,112,601
Cost of sales, including advertising, warehousing and distribution expenses	**3,514,029**	3,108,710	3,012,167
Gross profit on sales	**1,181,914**	1,115,707	1,100,434
Operating, general and administrative expenses	**1,024,862**	968,996	937,256
Income from operations	**157,052**	146,711	163,178
Investment income (loss) and interest expense	**(82)**	5,007	3,817
Other income (expense)	**3,807**	(3,411)	(3,316)
Income before provision for income taxes	**160,777**	148,307	163,679
Provision for income taxes	**35,581**	39,458	44,762
Net income	**$ 125,196**	$ 108,849	$ 118,917
Weighted-average shares outstanding, basic and diluted	**26,898,443**	26,898,443	26,898,443
Cash dividends per share	**$ 1.30**	$ 1.25	$ 1.24
Basic and diluted earnings per share	**$ 4.65**	$ 4.05	$ 4.42

(amounts in thousands, except shares and per share amounts)	13 Weeks Ended April 1, 2023	13 Weeks Ended March 26, 2022
Net sales	$ 1,144,974	$ 1,104,069
Cost of sales, including advertising, warehousing and distribution expenses	859,185	810,384
Gross profit on sales	285,789	293,685
Operating, general and administrative expenses	253,171	252,271
Income from operations	32,618	41,414
Investment income (loss) and interest expense	3,798	(881)
Other income (expense)	(1,258)	1,505
Income before provision for income taxes	35,158	42,038
Provision for income taxes	9,344	10,649
Net income	$ 25,814	$ 31,389
Weighted-average shares outstanding, basic and diluted	26,898,443	26,898,443
Cash dividends per share	$ 0.34	$ 0.32
Basic and diluted earnings per share	$ 0.96	$ 1.17

For the fiscal year 2022, Weis Markets Net Sales grew 9.1% yoy when adjusting for the additional week in the fiscal year 2022. This represents an acceleration from the 2.7% yoy growth rate in 2021. Accelerated revenue growth in 2022 is primarily driven by passing rising prices across the United States onto the consumer. In 2022 Food-at-home prices increased by

11.4%, proving the previous statement. For the quarter ending April 1st, Weis Markets increased its Net Sales by 3.7% yoy. While inflation is subsiding, January and February 2023 saw substantial increases in Food-at-home prices.

The cost of sales for the fiscal year 2022 grew by 11% when adjusting for the additional week in fiscal year 2022. Weis Markets' increase in the cost of sales can primarily be explained by rising production costs attributable to broader inflation, particularly in food prices. As inflation subsides, Weis Markets will likely experience more stable margins. For the quarter ending April 1st, Weis Markets grew its cost of sales by 6%, indicating the firm may be having trouble passing on its increased costs to the consumer.

For the fiscal year 2022, Weis Markets increased its operating and general administrative expenses by 3.8% when adjusting for the additional week of fiscal year 2022. The increase in operating expenses is also heavily influenced by inflation. However, as inflation subsists, operating expenses should stabilize and align with revenue growth. Operating expenses remained flat for the quarter ending April 1st, indicating that inflation is subsiding in the wage market.

Balance Sheet

(amounts in thousands, except shares)		**December 31, 2022**		December 25, 2021
Assets				
Current:				
Cash and cash equivalents	$	**157,997**	$	86,048
Marketable securities		**186,419**		205,744
SERP investment		**22,696**		27,059
Accounts receivable, net		**50,863**		52,108
Inventories		**293,274**		269,587
Prepaid expenses and other current assets		**29,921**		31,112
Total current assets		**741,170**		671,658
Property and equipment, net		**970,913**		977,787
Operating lease right-to-use		**175,952**		191,175
Goodwill		**52,330**		52,330
Intangible and other assets, net		**18,785**		17,525
Total assets	$	**1,959,150**	$	1,910,475
Liabilities				
Current:				
Accounts payable	$	**206,849**	$	218,774
Accrued expenses		**57,431**		48,654
Operating leases		**43,527**		39,940
Accrued self-insurance		**19,416**		18,568
Deferred revenue, net		**11,774**		11,901
Income taxes payable		**6,354**		7,360
Total current liabilities		**345,351**		345,197
Postretirement benefit obligations		**25,270**		29,964
Accrued self-insurance		**23,712**		23,400
Operating leases		**142,424**		161,669
Deferred income taxes		**111,225**		115,087
Other		**9,334**		15,416
Total liabilities		**657,316**		690,733
Shareholders' Equity				
Common stock, no par value, 100,800,000 shares authorized, 33,047,807 shares issued, 26,898,443 shares outstanding		**9,949**		9,949
Retained earnings		**1,449,191**		1,358,963
Accumulated other comprehensive income (loss) (Net of deferred taxes of $2,342 in 2022 and $669 in 2021)		**(6,449)**		1,687
		1,452,691		1,370,599
Treasury stock at cost, 6,149,364 shares		**(150,857)**		(150,857)
Total shareholders' equity		**1,301,834**		1,219,742
Total liabilities and shareholders' equity	$	**1,959,150**	$	1,910,475

See accompanying notes to Consolidated Financial Statements.

(amounts in thousands, except shares)		April 1, 2023		December 31, 2022
Assets				
Current:				
Cash and cash equivalents	$	113,575	$	157,997
Marketable securities		214,229		186,419
SERP investment		23,806		22,696
Accounts receivable, net		49,947		50,863
Inventories		307,800		293,274
Prepaid expenses and other current assets		29,427		29,921
Total current assets		738,784		741,170
Property and equipment, net		961,728		970,913
Operating lease right-to-use		173,812		175,952
Goodwill		52,330		52,330
Intangible and other assets, net		18,051		18,785
Total assets	$	1,944,705	$	1,959,150
Liabilities				
Current:				
Accounts payable	$	198,907	$	206,849
Accrued expenses		32,560		57,431
Operating leases		43,233		43,527
Accrued self-insurance		18,299		19,416
Deferred revenue, net		9,445		11,774
Income taxes payable		12,970		6,354
Total current liabilities		315,414		345,351
Postretirement benefit obligations		25,582		25,270
Accrued self-insurance		23,562		23,712
Operating leases		140,293		142,424
Deferred income taxes		114,406		111,225
Other		5,237		9,334
Total liabilities		624,494		657,316
Shareholders' Equity				
Common stock, no par value, 100,800,000 shares authorized, 33,047,807 shares issued, 26,898,443 shares outstanding		9,949		9,949
Retained earnings		1,465,860		1,449,191
Accumulated other comprehensive income (loss) (Net of deferred taxes of $1,710 in 2023 and $2,342 in 2022)		(4,741)		(6,449)
		1,471,068		1,452,691
Treasury stock at cost, 6,149,364 shares		(150,857)		(150,857)
Total shareholders' equity		1,320,211		1,301,834
Total liabilities and shareholders' equity	$	1,944,705	$	1,959,150

Weis Markets boasts a strong capital position with a debt-to-equity ratio of .473 as of April 1, 2023. Weis Markets has a current ratio of 2.34, a quick ratio of 1.20, and a cash ratio of 1.04, demonstrating its ability to meet all of its obligations in the next year. Overall, Weis Markets possesses one of the most robust balance sheets in the supermarket industry.

Statement of Cash Flows

(amounts in thousands)	53 Weeks Ended December 31, 2022	52 Weeks Ended December 25, 2021	December 26, 2020
Cash flows from operating activities:			
Net income	$ **125,196**	$ 108,849	$ 118,917
Adjustments to reconcile net income to			
net cash provided by operating activities:			
Depreciation and amortization	**104,026**	102,804	99,370
(Gain) loss on disposition of fixed assets	**(2,407)**	1,026	3,914
Unrealized (gain) loss in value of equity securities	**1,325**	900	1,791
Deferred income taxes	**(852)**	12,313	5,657
Unrealized (gain) loss in SERP	**5,653**	(2,309)	(2,641)
Changes in operating assets and liabilities:			
Inventories	**(23,687)**	(563)	10,782
Accounts receivable and prepaid expenses	**2,436**	2,727	(6,804)
Accounts payable and other liabilities	**7,695**	174	54,658
Income taxes	**(1,005)**	2,302	(3,139)
Other	**(356)**	(514)	(4,515)
Net cash provided by operating activities	**218,024**	227,709	277,990
Cash flows from investing activities:			
Purchase of property and equipment	**(122,169)**	(151,800)	(130,991)
Proceeds from the sale of property and equipment	**6,691**	5,932	470
Purchase of marketable securities	**(355,757)**	(116,268)	(50,789)
Proceeds from the sale and maturities of marketable securities	**362,237**	19,680	7,730
Purchase of intangible assets	**(819)**	(208)	(127)
Change in SERP investment	**(1,290)**	(1,986)	(1,188)
Net cash used in investing activities	**(111,107)**	(244,650)	(174,895)
Cash flows from financing activities:			
Dividends paid	**(34,968)**	(33,623)	(33,354)
Net cash used in financing activities	**(34,968)**	(33,623)	(33,354)
Net increase (decrease) in cash and cash equivalents	**71,949**	(50,564)	69,741
Cash and cash equivalents at beginning of year	**86,048**	136,612	66,871
Cash and cash equivalents at end of period	$ **157,997**	$ 86,048	$ 136,612

See accompanying notes to Consolidated Financial Statements. Cash paid for income taxes was $37.4 million, $24.8 million and $42.3 million in 2022, 2021 and 2020, respectively. Cash paid for interest related to long-term debt was $40 thousand, $32 thousand and $34 thousand in 2022, 2021 and 2020, respectively.

(amounts in thousands)		April 1, 2023		March 26, 2022
Cash flows from operating activities:				
Net income	$	25,814	$	31,389
Adjustments to reconcile net income to net cash provided by operating activities:				
Depreciation and amortization		26,688		25,629
(Gain) loss on disposition of fixed assets		1		(3)
Unrealized (gain) loss in value of equity securities		(325)		214
Deferred income taxes		2,549		3,557
Unrealized (gain) loss in SERP		(1,196)		2,184
Changes in operating assets and liabilities:				
Inventories		(14,526)		(15,768)
Accounts receivable and prepaid expenses		1,410		6,297
Accounts payable and other liabilities		(40,190)		(26,316)
Income taxes		6,615		7,559
Other		1,104		(262)
Net cash provided by operating activities		7,944		34,480
Cash flows from investing activities:				
Purchase of property and equipment		(17,731)		(18,793)
Proceeds from the sale of property and equipment		16		13
Purchase of marketable securities		(35,958)		(25,965)
Proceeds from the sale and maturities of marketable securities		10,372		25,481
Purchase of intangible assets		(6)		(48)
Proceeds from sale of intangible assets		—		125
Change in SERP investment		86		359
Net cash used in investing activities		(43,221)		(18,828)
Cash flows from financing activities:				
Dividends paid		(9,145)		(8,608)
Net cash used in financing activities		(9,145)		(8,608)
Net increase (decrease) in cash and cash equivalents		(44,422)		7,044
Cash and cash equivalents at beginning of year		157,997		86,048
Cash and cash equivalents at end of period	$	113,575	$	93,092

See accompanying notes to Consolidated Financial Statements. In the first thirteen weeks of 2023, there was $179 thousand cash paid for income taxes compared to $233 thousand in 2022 for the same period. Cash paid for interest related to long-term debt was $8 thousand and $8 thousand in the first thirteen weeks of 2023 and 2022, respectively.

For the fiscal year 2022, Weis Markets reported $218,024,000 in operating cash flow and $122,169,000 in capital expenditures, bringing the free cash flow to $95,855,000. This represents a 26.3% increase in free cash flow yoy. This is primarily due to an increase in earnings quality and a decrease in capital expenditures. For the quarter ending April 1st, 2023, free cash flow was ($9,787,000) compared with $15,687,000 in Q1 2022. This was primarily due to a deterioration of earnings quality led by substantial declines in current liabilities, signaling potentially worse supplier terms.

Ratios

Fiscal year	2021	2022
Days inventory outstanding	31.62	29.23
Days sales outstanding	4.70	4.00
Days payable outstanding	25.85	22.10
Cash conversion cycle	10.47	11.13
Financial Ratios		
ROA	5.84%	6.47%
ROE	8.63%	9.37%
ROIC	6.73%	7.51%

Weis Markets' yearly calculated ratios tell a strong story about the company's overall operational efficiency. Most notably, ROIC quantifies the management's ability to invest in opportunities that create new shareholder value. An ROIC of 6.73% and 7.51% signifies that much of the company's investments are neutral when compared with the company's cost of capital. However, Weis Markets' management has performed better than many of its larger peers regarding capital allocation and efficiency.

Competition

Overview

Weis Markets competes with all food retailers in the United States but predominantly with traditional supermarkets. Supermarkets of this nature include Wegmans, Shoprite, Kroger, and Walmart's grocery section. All of these businesses offer similar services and products. Weis Markets' success is primarily a result of a robust and cost-effective distribution network and developed customer loyalty programs that create exit costs for consumers. For example, Weis Markets' pharmacies push customers into Weis' supermarkets. While customers pick up their prescriptions, they will likely buy some food. Similarly, the rewards card incentivizes customers to regularly shop at Weis to maximize their savings.

Another factor that governs many of Weis Markets' stores is economics. When Weis Markets opens a store in a smaller community, it is not economically viable for another supermarket to operate. In these areas, Weis Markets effectively holds a monopoly on nearby groceries.

In areas with more competition, Weis Markets has to rely on its technology and supply chain to outperform its rivals. According to Checkbook.org, Weis Markets rated 2nd in terms of pricing but nearly at the bottom in quality. Despite the poor quality ranking, Weis Markets matches well against competitors with similar business models.

Comps

Companies Chosen

- ➢ Ingles Markets (IMKTA)
- ➢ Grocery Outlet Holding (GO)
- ➢ Sprouts Farmers Markets (VLGEA)
- ➢ Natural Grocers (NGVC)
- ➢ Village Super Markets (VLGEA)
- ➢ Kroger (KR)

Finding publicly traded firms that operate businesses similar to Weis Markets was difficult. Most comparably sized supermarkets do not trade on the public market. Among some of the competitors selected substantially different business models persist that differentiate the businesses enough to change potential target markets radically.

Company Name	Ticker	Gross Margin (%)	Pretax Margin (%)	Net Margin (%)
Weis Markets	WMK	22.8	3.2	2.5
Ingles Markets	IMKTA	24.4	5.7	4.3
Grocery Outlet Holding	GO	29.2	2.2	1.8
Sprouts Farmers Market	SFM	34.9	5.1	3.8
Natural Grocers	NGVC	25.7	1.9	1.5
Village Super Markets	VLGEA	26.5	2.3	1.5
Kroger	KR	19.4	2	1.5
Average	N/A	26.1	3.2	2.4

Weis Markets currently boasts below average gross profit margins when compared with its competitors. However, Weis Markets has maintained gross profit margins superior to its peers in previous periods. Compared to Kroger, the largest supermarket in the United States, Weis Markets dominates in margins, outperforming Kroger in all three margins. Regional supermarkets possess stronger margins due to their more centralized and efficient distribution centers when compared to national chains.

Weis Markets' operational efficiency begins to show itself in the pretax margins. Weis Markets' 3.2% margin is substantially higher than the median 2.8% pretax margin. Sprouts Farmers Market, a whole foods-focused supermarket, and Ingles Markets, a regional North Carolina supermarket chain, only surpass Weis Markets' margins.

Valuation

Assumptions

Our Model assumptions are listed below:

Cost of equity	7.47%
Risk free rate	3.55%
Equity risk premium	8.00%
Beta*	0.88

For my 3-statement model, I assumed a long-term growth rate of 2.5%, approximately equal to the projected long-term GDP growth of the U.S.. For the next eight years, I projected a growth rate of 3%, slightly above the long-term growth rate of 2.5%. This is due to the projected expansion of stores over the next few years and a regression to the mean in real food spending growth to roughly 1%. Because it is impossible to project the impact of deals that have yet to be announced, this will need to be closely monitored. However, Weis Markets' management has done a commendable job in the past with its acquisitions.

The discount was created with the cost of equity (COE) (CAPM). Because Weis pays no interest, the COE approach is acceptable. I calculated the cost of equity using a 3.55% Risk-free rate and an 8% equity risk premium. I adjusted Weis Markets' beta from .44 to .88 to offset many of the operational risks that Weis Markets possesses, such as low volume, low coverage, and small market capitalization.

Projected Metrics & Income Statement

Fiscal year	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030
Days inventory outstanding	31.62	29.23	29.75	31.30	31.36	31.49	31.49	31.49	31.49	31.49
Days sales outstanding	4.70	4.00	3.96	4.14	4.14	4.14	4.14	4.14	4.14	4.14
Days payable outstanding	25.85	22.10	22.82	25.33	25.28	25.18	25.18	25.18	25.18	25.18
Cash conversion cycle	10.47	11.13	10.90	10.11	10.22	10.45	10.45	10.45	10.45	10.45
Financial Ratios										
ROA	5.84%	6.47%	4.98%	6.39%	7.26%	7.01%	6.79%	6.58%	6.39%	6.22%
ROE	8.63%	9.37%	7.13%	8.99%	9.97%	9.47%	9.04%	8.65%	8.31%	8.27%
ROIC	6.73%	7.51%	5.56%	7.62%	8.96%	8.93%	8.89%	8.85%	8.81%	8.79%

Year	FY 2020	FY 2021	FY 2022	FY 2023	FY 2024	FY 2025	FY 2026	FY 2027	FY 2028	FY 2029	FY 2030
Net sales	4,112,601	4,224,417	4,695,943	4,836,821	4,981,926	5,131,384	5,285,325	5,443,885	5,607,202	5,775,418	5,948,680
Growth		2.72%	11.16%	3.00%	3.00%	3.00%	3.00%	3.00%	3.00%	3.00%	3.00%
Cost of sales	3,012,167	3,108,710	3,514,029	3,675,984	3,716,517	3,797,224	3,911,141	4,028,475	4,149,329	4,273,809	4,402,023
as a % of sales	73.24%	73.59%	74.83%	76.00%	74.60%	74.00%	74.00%	74.00%	74.00%	74.00%	74.00%
Gross profit on sales	1,100,434	1,115,707	1,181,914	1,160,837	1,265,409	1,334,160	1,374,185	1,415,410	1,457,872	1,501,609	1,546,657
Gross profit margin	26.8%	26.4%	25.2%	24.0%	25.4%	26.0%	26.0%	26.0%	26.0%	26.0%	26.0%
Operating, general and administrative expenses	937,256	968,996	1,024,862	1,064,101	1,096,024	1,128,904	1,162,772	1,197,655	1,233,584	1,270,592	1,308,710
% of revenues	22.79%	22.94%	21.82%	22.00%	22.00%	22.00%	22.00%	22.00%	22.00%	22.00%	22.00%
Income from operations	163,178	146,711	157,052	96,736	169,385	205,255	211,413	217,755	224,288	231,017	237,947
Operating margin	3.97%	3.47%	3.34%	2.00%	3.40%	4.00%	4.00%	4.00%	4.00%	4.00%	4.00%
Investment income (loss) and interest expense	3817	5,007	(82)	7,200	5,600	5,500	5,400	5,400	5,400	5,400	5,400
Other income	(3,316)	(3,411)	3,807	-	-	-	-	-	-	-	-
Income before provision for income taxes	163,679	148,307	160,777	103,936	174,985	210,755	216,813	223,155	229,688	236,417	243,347
EBT margin											
Provision for income taxes	44,762	39,458	35,581	23,905	40,247	48,474	49,867	51,326	52,828	54,376	55,970
Tax rate	27%	27%	22%	23%	23%	23%	23%	23%	23%	23%	23%
Net income	118,917	108,849	125,196	80,031	134,739	162,282	166,946	171,830	176,860	182,041	187,377

Discounted Cash Flow Analysis

Year	2023	2024	2025	2026	2027
Operating cash flow	222,265	245,181	274,604	281,186	288,136
Less: capital expenditures	(160,000)	(155,000)	(155,000)	(160,000)	(165,000)
Free Cash Flow	62,265	90,181	119,604	121,186	123,136
Present Value	57,940	78,086	96,368	90,859	85,907
Shares outstanding	26,898	26,898	26,898	26,898	26,898
Discounted FCF per share	2.15	2.90	3.58	3.38	3.19

Terminal Value	$60.34
Target Price	90.35
Market price (5/20/2023)	$65.06
Upside	38.9%

Areas of Concern:

The most concerning implication this model makes is that Weis markets will obtain a 4% operating margin in the fiscal year 2025 and onward. Historically, supermarkets are known to have margins between 1% and 3%. While I think this is a bold assumption, Inflation is subsiding in both the wage and food markets. Because of this, Weis Markets' margins will improve over the next few years rather than deteriorate.

Conclusion

It is my opinion that Weis Markets is trading below its intrinsic value. My research suggests multiple factors are at play in suppressing WMK's valuation. First, the company's market cap remains too small for many institutional investors to take notice seriously. Second, I believe that the small volume and overwhelming ownership of the Weis family over Weis Markets play against it. Most importantly, Weis Markets does a relatively poor job of marketing its company to Wall Street. For example, Weis Markets does not create investor presentations that would help analysts better understand the company. Weis Markets also does not have a readily visible investor relations contact. The company is also abnormally vague in its announcements of acquisitions and other corporate milestones. While I think Weis Markets is trading below its intrinsic value, without improvements to its investor relations, this value will likely remain unrealized. Finally, I concede that the market may be pricing in margin compression that would considerably lower the company's intrinsic value.