Philip Morris International (PM)

Updated April 30th, 2018 by Jonathan Weber

Key Metrics

Current Price:	$83	**5 Year CAGR Estimate:**	11.1%	**Quality Percentile:**	N/A
Fair Value Price:	$88	**5 Year Growth Estimate:**	4.8%	**Momentum Percentile:**	N/A
% Fair Value:	95%	**5 Year Valuation Multiple Estimate:**	1.1%	**Total Return Percentile:**	N/A
Dividend Yield:	5.2%	**5 Year Price Target**	$111	**Valuation Percentile:**	N/A

Overview & Current Events

Philip Morris International is a tobacco company that came into being when its parent company Altria (MO) spun off its international operations. Philip Morris sells cigarettes under the Marlboro brand, among others, internationally. Altria uses the Marlboro brand (again, among others) in the U.S. Philip Morris has a market capitalization of $128 billon.

The company reported its Q1 earnings on April 19, showing that the company earned $1.00 per share (up two percent year over year) and revenues of $6.9 billion, up 14% year over year. The market reacted very negatively to these results (revenues were $100 million lower than the analyst consensus), sending shares to the low $80s, a new 52-week low.

Growth on a Per-Share Basis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
EPS	$3.32	$3.24	$3.92	$4.85	$5.17	$5.26	$4.76	$4.42	$4.48	$4.72	***$5.33***	***$6.75***
DPS	$1.54	$2.24	$2.44	$2.84	$3.24	$3.58	$3.88	$4.04	$4.12	$4.22	***$4.32***	***$5.38***

When the spin-off of Philip Morris was announced, the market assumed that Altria (the US business) would be the low-growth company, and that Philip Morris (the non-US business) would be the high-growth company. It looked like this would come true through 2013, as Philip Morris recorded a 9.6% EPS growth rate through the first five years of its existence. This changed in the following years, as Philip Morris' profits declined and stagnated – Philip Morris will only regain its 2013 EPS in 2018, according to Philip Morris' guidance for EPS of $5.25 to $5.40 for the current year.

Both the mediocre results in 2014 to 2017 as well as the big profit increase that is forecasted for the current year are, at least partially, based on the impact of currency rates on the company's results. Since Philip Morris generates all of its revenues outside of the US, forex movements widely impact the company's recorded sales as well as its recoded profits. When the dollar gets stronger versus other currencies, Philip Morris' recorded earnings decline (this was the case during the last couple of years), when we dollar gets weaker Philip Morris' results get a boost.

Another reason for Philip Morris' weak profit growth over the last couple of years was the company's investments into the iQOS / Heatsticks technology. This is a heat-not-burn product Philip Morris developed and which it has been rolling out in several markets around the globe. The investment in the development of this device and the manufacturing equipment needed to produce this reduced-risk product on a massive scale were costly, but Philip Morris is hoping that those investments will pay off in the long run. Ramp-up of iQOS in markets such as Japan and South Korea has been a success, and the product is one of the reasons why Philip Morris has been able to grow its revenues by a very sizeable 14% during the first quarter of 2018 despite cigarette volumes declining by 5%. With currency rates being more of a tailwind going forward and with the positive impact of iQOS, Philip Morris should be able to grow at a compelling pace over the coming years.

Valuation Analysis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	Now	2023
Avg. P/E	14.7	13.4	13.2	13.8	16.7	17.0	17.7	18.8	21.5	23.4	***15.6***	***16.5***
Avg. Yld.	3.1%	5.1%	4.7%	4.2%	3.8%	4.0%	4.6%	4.9%	4.3%	3.8%	***5.2%***	***4.8%***

Philip Morris' valuation has steadily risen starting in 2010, which can be partially explained by the fact that the market got more expensive overall, and partially by the fact that the market has been anticipating higher growth rates over the last couple of years (as it was clear that currency rates would at one point not be a headwind any longer and that iQOS investments would start to pay off). As earnings will rise significantly this year its P/E ratio (based on 2018's earnings) has come down and is now slightly lower than the median P/E and average P/E ratios over the last decade.

Philip Morris' dividend yield is currently over 5%. The stock's high yield and stable earnings make it a compelling choice for investors looking for high yields.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
GP/A	49.7%	46.2%	50.1%	57.5%	55.7%	54.5%	54.8%	51.2%	46.9%	42.6%	***44.0%***	***47.0%***
Debt/A	76.1%	82.1%	85.2%	98.3%	108%	116%	132%	134%	130%	124%	***120%***	***100%***
Int. Cov.	33.0	12.7	12.9	16.8	16.3	14.0	11.2	10.7	12.3	12.8	***13.0***	***13.0***
Payout	46.4%	69.1%	62.2%	58.6%	62.7%	68.1%	81.5%	91.4%	92.0%	89.4%	***81.1%***	***79.7%***
Std. Dev.	28.8%	27.7%	21.8%	17.3%	16.5%	13.4%	12.9%	18.0%	14.2%	18.9%	***19.0%***	***21.0%***

Philip Morris' gross profits relative to its assets are high, even though the ratio took a hit starting in 2016. This can, however, be explained by the increased asset base due to the investments into iQOS manufacturing, which will result in higher profits down the road. This should cause GP/A expansion in the future. Philip Morris' balance sheet is highly leveraged. The company has negative equity, which is why total debt is higher than all assets. This is due to the company's share repurchases in the past, which lowered equity levels (and which were partially funded via debt). The interest coverage ratio is still quite high though, as Philip Morris' long term debt is inexpensive. The company therefore is not in a dangerous situation financially.

Philip Morris has one of the best cigarette brands in the world (Marlboro) and is a leader in the reduced-risk product segment (with iQOS). At the same time the company's massive scale allows for cost advantages, and in the cigarette industry there are no up-and-coming competitors trying to get into the market. This means that Philip Morris generally is a low-risk business, with regulation being the exception. Smoking bans can affect the company's results, although Philip Morris is safer in this regard than many other tobacco companies due to its geographic diversification.

Final Thoughts & Recommendation

Philip Morris' offers decent growth prospects. There is a chance that iQOS sales could cause EPS growth well ahead of our estimates. Additionally, the stock appears a bit undervalued. The 5%+ dividend yield and high levels of safety are the real draws for investing in Philip Morris. This is one of the safest 5%+ yielding stocks available today. We recommend Philip Morris as a buy for investors looking for current income.

Total Return Breakdown by Year