Verizon Communications (VZ)

Updated July 24th, 2018 by Nate Parsh

Key Metrics

Current Price:	$52	**5 Year CAGR Estimate:**	12.7%	**Volatility Percentile:**	32.8%
Fair Value Price:	$61	**5 Year Growth Estimate:**	5.0%	**Momentum Percentile:**	74.7%
% Fair Value:	85%	**5 Year Valuation Multiple Estimate:**	3.1%	**Valuation Percentile:**	85.5%
Dividend Yield:	4.6%	**5 Year Price Target**	$78	**Total Return Percentile:**	84.1%

Overview & Current Events

Verizon Communications was created by a merger between Bell Atlantic Corp and GTE Corp in June, 2000. Verizon operates in the Telecommunications Services sector of the economy and is the largest wireless carrier in the country. Wireless contributes three-quarters of all revenues for the company. Verizon also offers broadband and cable services, which account for about a quarter of sales. The company's network covers ~298 million people and covers 98% of the U.S. Verizon has a market cap of almost $213 billion.

Verizon reported 2nd quarter earnings on July 24th. The company earned $1.20 per share, $0.06 above estimates and 26% higher from the same period last year. Revenue grew 5.4% to $32.2 billion, $420 million above estimates.

Growth on a Per-Share Basis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
EPS	$2.34	$2.40	$2.21	$2.15	$2.32	$4.00	$3.35	$3.99	$3.87	$3.75	***$4.35***	***$5.55***
DPS	$1.78	$1.87	$1.93	$1.96	$2.02	$2.08	$2.16	$2.23	$2.29	$2.32	***$2.36***	***$3.01***

Verizon has seen its earnings per share grow at a rate of almost 5% per year for the past 10 years. The company's guidance calls for a midpoint of $4.35 per share for 2018. This EPS gain from will come directly from tax reform as the company's effective tax rate should be ~25% going forward. Applying the historical earnings growth rate to the company's guidance for 2018 means that shares of Verizon could earn $5.55 per share by 2023.

After adding 260,000 retail postpaid net adds in the 1st quarter, Verizon added 531,000 net additions in the 2nd quarter. The company had almost 400,000 smartphone net adds. Wireless service revenue inched up almost 1%, due in part because unsubsidized phones make up 82% of Verizon's customer base, up from 75% in the 2nd quarter of 2017. Verizon is viewed as having the best wireless network, as seen by the company's postpaid phone churn rate of just 0.75% in the quarter. This is the fifth consecutive quarter that wireless retail postpaid churn was below 0.80%.

Verizon has increased its dividend for the past 13 years and has a 10-year average growth rate of 3.5%. If the company sticks to its historical pattern, the next increase should be announced in September. Verizon expects tax reform savings to lift cash flow by as much as $4 billion. This additional savings could result in higher dividend growth going forward. If dividend growth were to match earnings growth, then shares of Verizon could produce $3.01 in dividends per share.

Valuation Analysis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	Now	2023
Avg. P/E	13.7	12.7	13.8	17.1	18.1	12.2	14.5	11.8	13.3	12.3	***12.0***	***14.0***
Avg. Yld.	5.1%	6.1%	6.3%	5.3%	4.8%	4.3%	4.4%	4.7%	4.5%	4.8%	***4.7%***	***3.9%***

Shares of Verizon are trading at the same price as they were at the time of our April 28th update. Based off the current share price and projected 2018 EPS, Verizon has a forward P/E of 12. This is below the decade long average P/E of 14. If shares were to return to their average multiple over the past decade, then the stock's multiple could expand 3.1% per year through 2023.

Disclosure: This analyst has a long position in the security discussed in this research report

With a 4.6% dividend yield, Verizon offers investors a yield that is more than double that of the S&P 500 and is well above the yield of the 10-year Treasury Bond.

Safety, Quality, Competitive Advantage, & Recession Resiliency

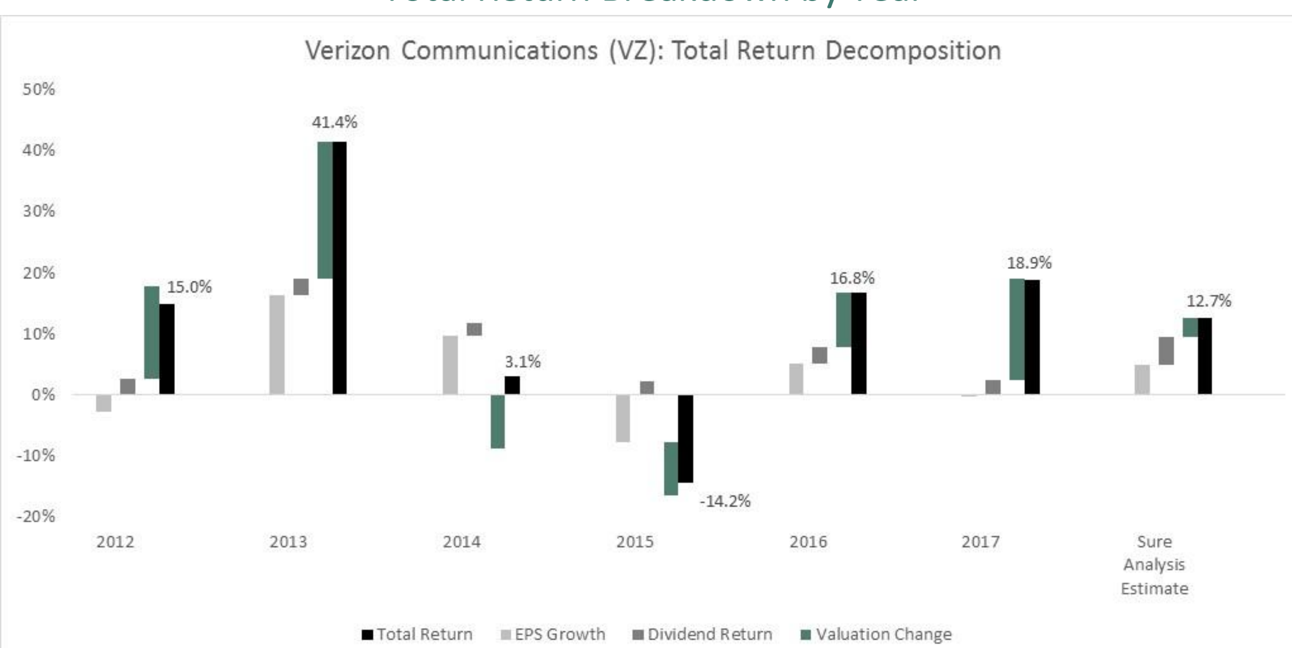
Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
GP/A	29%	27.9%	28.4%	28.2%	30.9%	27.6%	33.2%	32.4%	30.5%	29%	***29.1%***	***29.7%***
Debt/A	61%	62.9%	60.5%	32.7%	62%	65.2%	94.1%	92.7%	90.2%	82.6%	***80.8%***	***73.4%***
Int. Cov.	2.4	5.5	6.3	4.8	5	12.3	4.2	6.9	5.9	5.4	***5.5***	***5.9***
Payout	70.1%	77.9%	87.3%	91.2%	87%	52%	64.5%	55.9%	59.2%	62.1%	***54.3%***	***54.2%***
Std. Dev.	28.8%	23.6%	20.9%	14.2%	14.6%	17.6%	11.7%	11.6%	19.7%	22.2%	***21.4%***	***18.5%***

Verizon's earnings-per-share increased during the last recession, but the company hasn't always demonstrated EPS growth year in and year out. EPS declined 2015-2017. Verizon also has a large debt balance of more than $113 billion – but its interest coverage ratio is not overly high for a stable telecom. Earnings are expected to be much higher in 2018 and beyond thanks to tax reform. This will help to increase cash flow dramatically, which could be used pay down debt or increase the company's dividend at a higher than average rate. Verizon has also managed to decrease its dividend payout ratio over the past few years, which should give shareholders confidence that the company will be able to maintain and increase its dividend in future years.

Final Thoughts & Recommendation

As with our previous report, we see shares of Verizon returning 12.7% per year over the next five years. This return is a combination of earnings growth (5%), dividends (4.6%) and multiple expansion (3.1%). Shares continue to trade at a discount to their historical valuation. Low churn rates coupled with high net device adds show that Verizon is well respected by consumers. While telecommunications companies are often considered "defensive" in nature, we see Verizon offering solid growth going forward. This growth combined with a generous yield make the stock look very attractive here. While we consider peer AT&T (T) to be a buy as well, Verizon has shown revenue growth in recent quarters that AT&T hasn't. AT&T also has issues related to its acquisition of Time Warner (TWX) that Verizon doesn't have. Investors looking for consistent revenue growth without any regulatory issues might feel that Verizon is the safer choice between the two telco giants. We maintain our 2023 price target of $78 and encourage investors to consider adding Verizon to their portfolio.

Total Return Breakdown by Year



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