AmerisourceBergen (ABC)

Updated August 2nd, 2018 by Bob Ciura

Key Metrics

Current Price:	$79	**5 Year CAGR Estimate:**	16.1%	**Volatility Percentile:**	75.7%
Fair Value Price:	$98	**5 Year Growth Estimate:**	10%	**Momentum Percentile:**	12.7%
% Fair Value:	81%	**5 Year Valuation Multiple Estimate:**	4.2%	**Valuation Percentile:**	89.5%
Dividend Yield:	1.9%	**5 Year Price Target**	$156	**Total Return Percentile:**	93.7%

Overview & Current Events

AmerisourceBergen was formed in 2001, by the merger of AmeriSource and Bergen Brunswig. Today, AmerisourceBergen is one of the largest healthcare distributors in the U.S., along with Cardinal Health and McKesson. ABC provides pharmaceutical products and business solutions to a variety of customers, which include healthcare providers, veterinary practices, and livestock producers. ABC also services global manufacturers to improve supply chain efficiency. ABC generates annual revenue of $150 billion, with a presence in more than 50 countries around the world. More than 90% of ABC's revenue comes from its pharmaceutical segment.

On 8/2/18, the company reported strong 2018 fiscal-third-quarter financial results. Revenue of $43.14 billion increased 11.5% from the same quarter a year ago, and beat analyst expectations by $230 million. Growth was mostly due to an 11.6% increase in Pharmaceutical Distribution Services revenue. Adjusted earnings-per-share of $1.54 increased 7.7% for the quarter, and also beat expectations by $0.08 per share. This was a strong beat for the company on both the top and bottom line.

Per-Share Growth

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
EPS	$1.44	$1.72	$2.22	$2.52	$2.72	$3.14	$3.97	$4.96	$5.62	$5.88	***$6.45***	***$10.39***
DPS	$0.15	$0.24	$0.34	$0.46	$0.60	$0.83	$0.94	$1.16	$1.36	$1.46	***$1.52***	***$2.45***

The pharmaceutical distribution industry as a whole is under pressure right now. Increasing demand for generics has fueled drug price deflation in the U.S., which is eroding their margins. In addition, there is currently an elevated level of public and regulatory scrutiny over high drug prices. E-commerce giant Amazon is also making a big push into healthcare distribution with its acquisition of PillPack. Despite these headwinds, ABC continues to grow revenue and earnings each year, which can be attributed to the company's competitive advantages, specifically its industry position and major acquisitions. Last year, ABC acquired H. D. Smith, the largest independent pharmaceutical wholesaler in the U.S., for $815 million. The acquisition is expected to be boost earnings-per-share by $0.15 in fiscal 2020. This is a positive long-term catalyst for ABC shareholders, as it will strengthen the company's position in U.S. pharmaceutical distribution.

In 2018, ABC expects to generate earnings-per-share in a range of $6.45 to $6.65. The company has guided investors to expect earnings toward the bottom of the range. Still, this would represent a strong growth rate of 10% for the year, which is impressive given the challenges in pharmaceutical distribution right now. ABC is expected to grow earnings-per-share and dividends by 10% per year over the next five years.

Valuation Analysis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	Now	2023
Avg. P/E	14.7	12.4	10.7	14.7	14.0	16.0	17.6	20.4	15.7	14.4	***12.2***	***15.0***
Avg. Yld.	0.7%	1.3%	1.2%	1.2%	1.6%	1.7%	1.3%	1.1%	1.5%	1.7%	***1.9%***	***1.6%***

Even though ABC continues to generate strong results and expects 10% earnings growth this year, the stock valuation continues to decline. Based on 2018 earnings-per-share estimates of $6.45, the stock currently trades for a price-to-earnings ratio of 12.2, compared with over 20 as recently as 2015. As a result, the stock now trades well below our fair value estimate, which is a price-to-earnings ratio of 15. This is the average valuation multiple over the past 10 years, and seems easily achievable, given the company's continued earnings growth. If the stock valuation returns to our estimate of fair value, it would provide a 4.2% boost to annual shareholder returns.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
GP/A	16.8%	15.5%	16.1%	16.4%	17.1%	13.3%	13.9%	12.6%	12.7%	12.9%	***13.0%***	***13.0%***
Debt/A	77.8%	80.0%	79.5%	80.9%	84.1%	87.7%	90.9%	97.8%	93.7%	94.2%	***94.0%***	***94.0%***
Int. Cov.	12.8	15.2	15.1	15.7	14.2	12.2	9.0	12.2	11.0	7.3	***7.5***	***7.5***
Payout	10.4%	14.0%	15.3%	18.3%	22.1%	26.4%	23.7%	23.4%	23.4%	24.8%	***23.6%***	***23.6%***
Std. Dev.	29.4%	25.0%	18.6%	20.6%	14.3%	13.3%	20.4%	19.3%	27.3%	28.8%	***30.0%***	***30.0%***

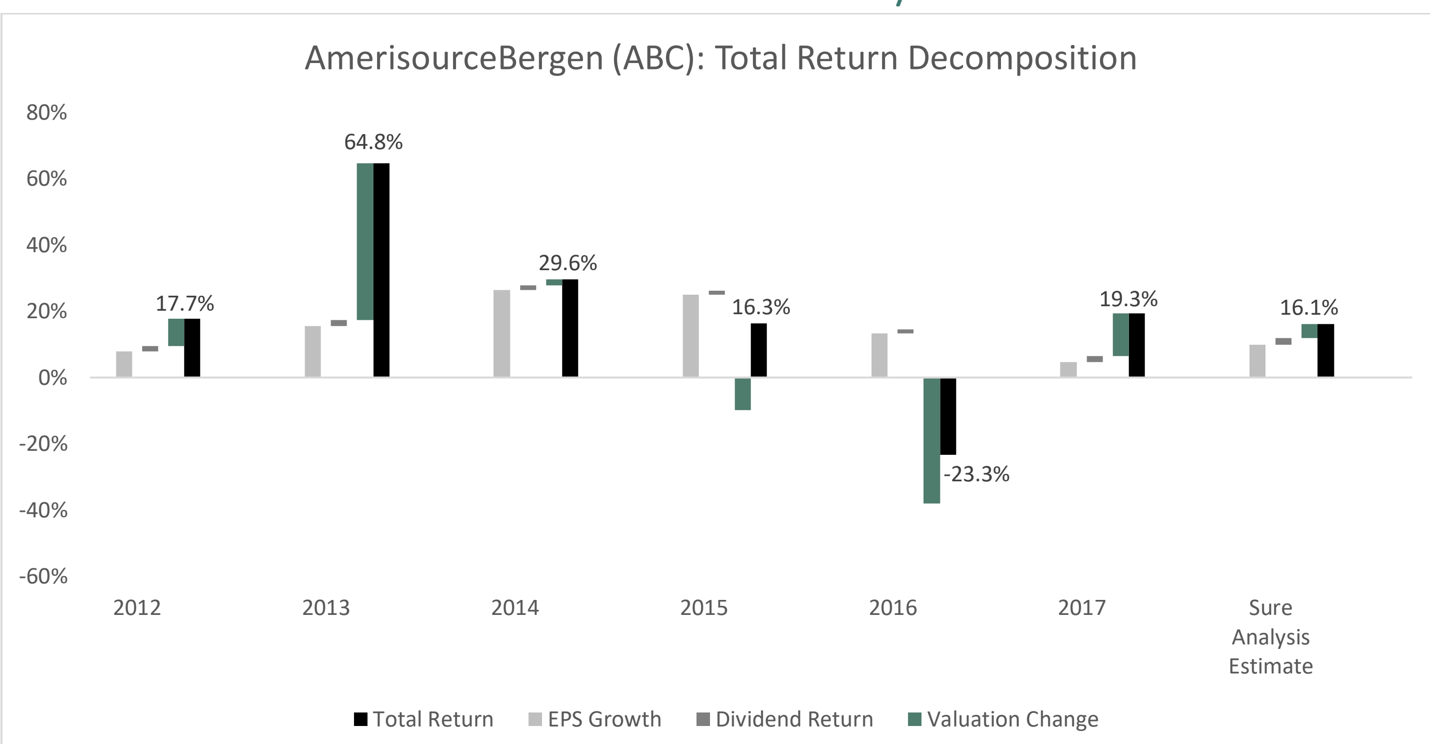
In terms of safety, ABC scores very well. The company's level of debt has increased, in relation to assets, and its interest coverage ratio has fallen in the past 10 years. However, its debt coverage is still more than sufficient, with plenty of financial flexibility to invest in growth, and reward shareholders with dividends. With a dividend payout ratio below 25%, the company should have little trouble continuing to increase the dividend each year.

ABC's main competitive advantage is its industry position. As one of the 'Big 3', ABC has a sizable economic moat that protects its market share. It is very difficult for a new competitor to enter the market. ABC sources over 1.5 million products, delivered from over 30 distribution centers, which is a major competitive advantage over smaller companies.

Final Thoughts & Recommendation

ABC's stock valuation has declined significantly in recent years, as the market has turned much more negative toward the major pharmaceutical distributors. However, we believe this is simply a matter of sentiment. The fundamentals are still strong. We expect 10% annual earnings growth for the company, as well as 4.2% annual returns from valuation changes. Adding the 1.9% dividend yield results in total expected returns of 16.1% per year over the next five years. This makes ABC a strong buy for value and dividend growth investors.

Total Return Breakdown by Year



Disclosure: This analyst has no position in the security discussed in this research report, and no plans to initiate one in the next 72 hours.