



# Philip Morris International (PM)

Updated October 18<sup>th</sup>, 2018 by Jonathan Weber

## Key Metrics

<b>Current Price:</b>	\$88	<b>5 Year CAGR Estimate:</b>	9.8%	<b>Volatility Percentile:</b>	39.9%
<b>Fair Value Price:</b>	\$83	<b>5 Year Growth Estimate:</b>	5.9%	<b>Momentum Percentile:</b>	7.9%
<b>% Fair Value:</b>	107%	<b>5 Year Valuation Multiple Estimate:</b>	-1.3%	<b>Growth Percentile:</b>	47.0%
<b>Dividend Yield:</b>	5.2%	<b>5 Year Price Target</b>	\$110	<b>Valuation Percentile:</b>	41.6%
<b>Dividend Risk Score:</b>	D	<b>Retirement Suitability Score:</b>	D	<b>Total Return Percentile:</b>	59.2%

## 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 sells the Marlboro brand (again, among others) in the U.S. Philip Morris has a market capitalization of \$131 billion.

Philip Morris reported its most recent quarterly results on October 18. The company grossed revenues of \$7.5 billion, up marginally (0.4%) from the prior year's quarter. The revenue growth rate was negatively impacted by adverse currency movements. At constant currencies revenues would have been up by 3.3%. Despite a weak revenue growth rate Philip Morris has still been able to grow its earnings per share to \$1.44 during Q3, a 13% increase year over year, and a 21% increase from the prior year's level when adjusted for currency. Due to the negative impact of a stronger dollar Philip Morris has lowered its earnings guidance to \$4.97 to \$5.02 per share. We have adjusted our estimate accordingly.

## Growth on a Per-Share Basis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
<b>EPS</b>	\$3.32	\$3.24	\$3.92	\$4.85	\$5.17	\$5.26	\$4.76	\$4.42	\$4.48	\$4.72	<b>\$5.00</b>	<b>\$6.65</b>
<b>DPS</b>	\$1.54	\$2.24	\$2.44	\$2.84	\$3.24	\$3.58	\$3.88	\$4.04	\$4.12	\$4.22	<b>\$4.49</b>	<b>\$5.38</b>
<b>Shares</b>	2.00	1.88	1.80	1.73	1.65	1.59	1.55	1.55	1.55	1.55	<b>1.55</b>	<b>1.50</b>

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, and even during 2018 earnings per share will remain below the peak set in 2013. Currency rates are a major factor for Philip Morris' profitability, as all of the company's revenues are generated out of the US. The advance of the US dollar has led to a reduction in Philip Morris' guidance for 2018. The company forecasts a \$0.12 headwind from currency in 2018.

Another reason for Philip Morris' weak profit growth over the last couple of years were the company's investments into the IQOS/Heatsticks technology. 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 8% during the first three quarters of 2018 despite cigarette volumes declining by 3% during these nine months.

Cigarette volume declines have decelerated through the first nine months of 2018, and with the added benefit of rising Heatsticks sales Philip Morris has ample potential to grow its revenues and earnings over the coming years.

## Valuation Analysis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	Now	2023
<b>Avg. P/E</b>	14.7	13.4	13.2	13.8	16.7	17.0	17.7	18.8	21.5	23.4	<b>17.6</b>	<b>16.5</b>
<b>Avg. Yld.</b>	3.1%	5.1%	4.7%	4.2%	3.8%	4.0%	4.6%	4.9%	4.3%	3.8%	<b>5.2%</b>	<b>5.0%</b>

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



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Philip Morris' share price is still substantially lower than it was at the beginning of the year, but share prices nevertheless have recovered solidly over the last couple of months. PM is up more than 15% from the 52-week low. Philip Morris' valuation has thus expanded, and due to the lower profit estimate for 2018 shares are now trading slightly above our fair value estimate. Shares of Philip Morris still offer a high dividend yield of more than 5%, which means that they are an attractive hold for income focused investors.

## Safety, Quality, Competitive Advantage, & Recession Resiliency

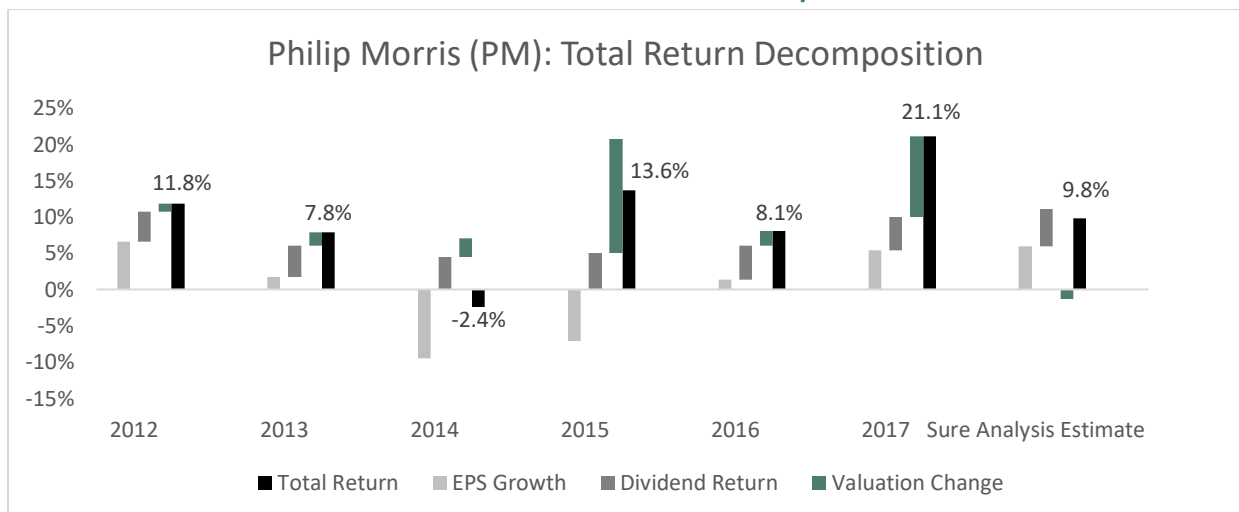
Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
<b>GP/A</b>	49.7%	46.2%	50.1%	57.5%	55.7%	54.5%	54.8%	51.2%	46.9%	42.6%	<b>44.0%</b>	<b>47.0%</b>
<b>Debt/A</b>	76.1%	82.1%	85.2%	98.3%	108%	116%	132%	134%	130%	124%	<b>120%</b>	<b>100%</b>
<b>Int. Cov.</b>	33.0	12.7	12.9	16.8	16.3	14.0	11.2	10.7	12.3	12.8	<b>13.0</b>	<b>13.0</b>
<b>Payout</b>	46.4%	69.1%	62.2%	58.6%	62.7%	68.1%	81.5%	91.4%	92.0%	89.4%	<b>89.8%</b>	<b>80.9%</b>
<b>Std. Dev.</b>	28.8%	27.7%	21.8%	17.3%	16.5%	13.4%	12.9%	18.0%	14.2%	18.9%	<b>19.0%</b>	<b>21.0%</b>

Philip Morris has negative equity, as total debt is higher than total assets. This is due to a strong historical trend of debt-funded share repurchases. Still, the interest coverage ratio is quite high, as Philip Morris' long term debt is inexpensive. 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 tremendous cost advantages. 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. Quantitatively, the company's high dividend payout ratio causes it to earn a D rating for both Dividend Safety and Retirement Suitability, although its long dividend history leads us to believe it may be safer than quantitative models would suggest.

## Final Thoughts & Recommendation

Philip Morris was a great investment during summer, when shares well traded below fair value. Philip Morris still is a solid, low-risk company which offers a high dividend yield and regular dividend increases, but the combination of a double-digit share price gain and a lowered profit guidance has made shares look more expensive. Overall, Philip Morris International earns a hold recommendation from Sure Dividend at current prices.

## Total Return Breakdown by Year



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## Income Statement Metrics

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Revenue	25705	25035	27208	31097	31377	31217	29767	26794	26685	28748
Gross Profit	16377	16013	17495	20419	21004	20807	19331	17429	17294	18316
Gross Margin	63.7%	64.0%	64.3%	65.7%	66.9%	66.7%	64.9%	65.0%	64.8%	63.7%
SG&A Exp.	6001	5870	6160	6870	6961	6890	7001	6656	6405	6725
D&A Exp.	842	853	932	993	898	882	889	754	743	875
Operating Profit	10332	10069	11247	13451	13946	13824	12237	10691	10815	11503
Op. Margin	40.2%	40.2%	41.3%	43.3%	44.4%	44.3%	41.1%	39.9%	40.5%	40.0%
Net Profit	6890	6342	7259	8591	8800	8576	7493	6873	6967	6035
Net Margin	26.8%	25.3%	26.7%	27.6%	28.0%	27.5%	25.2%	25.7%	26.1%	21.0%
Free Cash Flow	6836	7169	8724	9632	8365	8935	6586	6905	6905	7364
Income Tax	2787	2691	2826	3653	3833	3670	3097	2688	2768	4307

## Balance Sheet Metrics

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Total Assets	32972	34552	35050	35488	37670	38168	35187	33956	36851	42968
Cash & Equivalents	1531	1540	1703	2550	2983	2154	1682	3417	4239	8447
Acc. Receivable	2848	3131	3065	3201	3589	3853	4004	2778	3499	3738
Inventories	9664	9207	8317	8120	8949	9846	8592	8473	9017	8806
Goodwill & Int.	11099	12658	14034	13625	13519	12086	11373	10038	9794	10098
Total Liabilities	25068	28407	29929	34937	40824	44442	46390	45432	47751	53198
Accounts Payable	1013	670	835	1031	1103	1274	1242	1289	1666	2242
Long-Term Debt	11961	15416	16502	18545	22839	27678	29455	28480	29067	34339
Total Equity (\$B)	7.50	5.72	3.51	0.23	-3.48	-7.77	-12.63	-13.24	-12.69	-12.09
D/E Ratio	1.59	2.70	4.71	80.98	-6.57	-3.56	-2.33	-2.15	-2.29	-2.84

## Profitability & Per Share Metrics

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Return on Assets	21.3%	18.8%	20.9%	24.4%	24.1%	22.6%	20.4%	19.9%	19.7%	15.1%
Return on Equity	59.7%	96.0%	157%	460%	-542%	-153%	-73.5%	-53.1%	-53.7%	-48.7%
ROIC	33.2%	30.6%	33.6%	42.2%	45.4%	41.7%	37.8%	39.0%	39.6%	28.6%
Shares Out.	2.00	1.88	1.80	1.73	1.65	1.59	1.55	1.55	1.55	1.55
Revenue/Share	12.38	12.84	14.77	17.65	18.54	19.25	19.01	17.30	17.21	18.51
FCF/Share	3.29	3.68	4.74	5.47	4.94	5.51	4.21	4.46	4.45	4.74

Note: All figures in millions of U.S. Dollars unless per share or indicated otherwise.

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