



Verizon Communications (VZ)

Updated October 24th, 2018 by Nate Parsh

Key Metrics

Current Price:	\$57	5 Year CAGR Estimate:	10.4%	Volatility Percentile:	35.9%
Fair Value Price:	\$61	5 Year Growth Estimate:	5.0%	Momentum Percentile:	84.4%
% Fair Value:	93 %	5 Year Valuation Multiple Estimate:	1.3%	Growth Percentile:	30.1%
Dividend Yield:	4.1%	5 Year Price Target	\$78	Valuation Percentile:	60.0%
Dividend Risk Score:	A	Retirement Suitability Score:	A	Total Return Percentile:	58.0%

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 98% of the U.S. Verizon has a market cap of more than \$236 billion.

Verizon reported 3rd quarter earnings on October 23rd. The company earned \$1.22 per share, \$0.03 above estimates and growing more than 24% higher from the same period last year. Revenue grew 2.8% to \$32.61 billion, \$110 million above estimates.

Monthly phone subscribers increased by a net 295K, well above the market's expectation of 161K net adds. This includes more than 500K smartphone adds. Total revenue for the wireless segment grew 6.5% year over year. Wireline revenues decreased 3.8% from the same time last year. Verizon is considered to have the best wireless network amongst consumers, which helps explain their postpaid churn rate of just 0.80%. This is the sixth consecutive quarter where the churn rate was 0.80% or below. Fios video subscribers declined by 63K, leading to a 2.1% decline in revenues.

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
Shares	2840.6	2835.7	2828.1	2835.5	2858.3	4141.1	4155.4	4073.2	4076.7	4079.5	4050	3950

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.

Verizon gave shareholders a 2.12% dividend increase for the upcoming November payment. The company has now increased its dividend for the past 14 years and has a 10-year average growth rate of 3.5%. Cash flow was above \$5.2 billion for the quarter and \$14.2 billion year to date.

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	13.1	14.0
Avg. Yld.	5.1%	6.1%	6.3%	5.3%	4.8%	4.3%	4.4%	4.7%	4.5%	4.8%	4.1%	3.9%

Shares of Verizon have increased \$5, or 9.6%, since our July 24th update. Based off the current share price and projected 2018 EPS, Verizon has a forward P/E of 13.1. 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 1.3% per year through 2023. With a 4.1% 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. The stock's current multiple is well below that of the S&P 500.

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



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Safety, Quality, Competitive Advantage, & Recession Resiliency

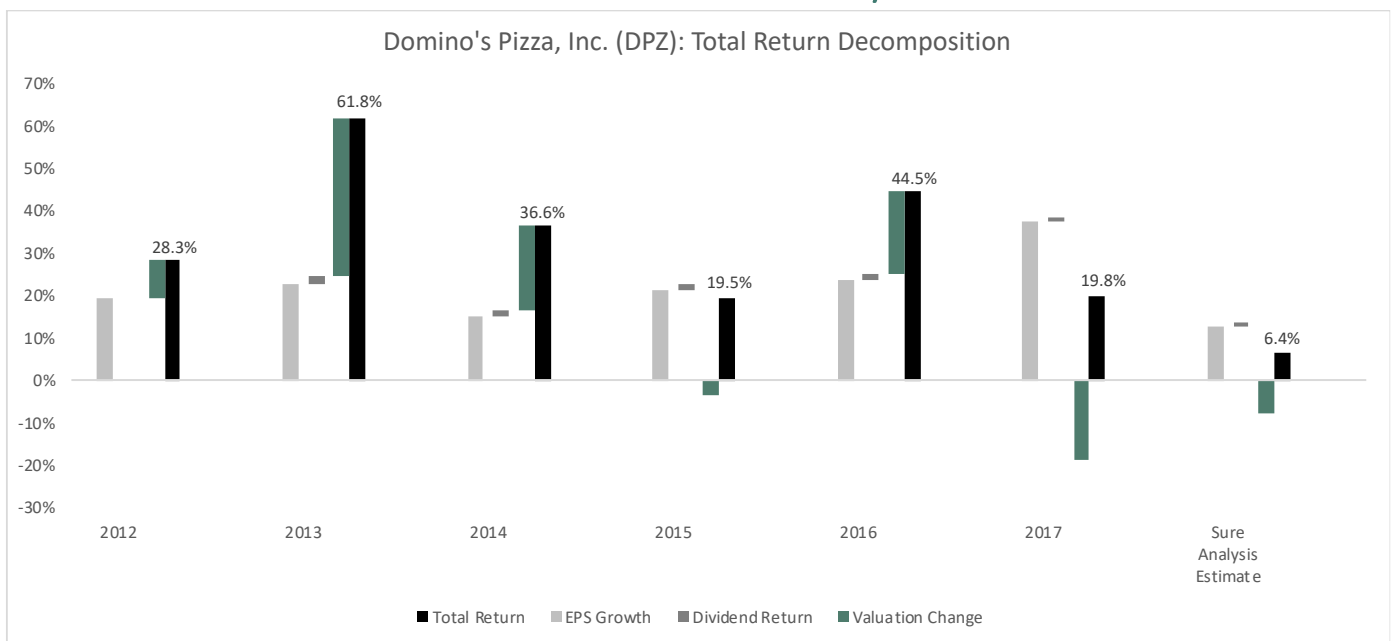
Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
GP/A	29%	27.9%	28.4%	28.2%	30.9%	27.6%	33.2%	32.4%	30.5%	29%	29.1%	29.7%
Debt/A	61%	62.9%	60.5%	32.7%	62%	65.2%	94.1%	92.7%	90.2%	82.6%	80.8%	73.4%
Int. Cov.	2.4	5.5	6.3	4.8	5	12.3	4.2	6.9	5.9	5.4	5.5	5.9
Payout	70.1%	77.9%	87.3%	91.2%	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 has not 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 low 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

After 3rd quarter earnings and the recent share price increase, we forecast that Verizon's stock can offer a total annual return of 10.4% over the next five years, down from 12.7% previously. This return is a combination of earnings growth (5%), dividends (4.1%) and multiple expansion (1.3%). Verizon showed strong net add growth and continues to have a very low churn rate. The company also has demonstrated several quarters in a row of smartphone adds. While the stock has climbed almost 10%, we continue to feel that Verizon can offer a solid combination of earnings growth and dividends. 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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Income Statement Metrics

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Revenue (\$B)	97.35	107.81	106.57	110.88	115.85	120.55	127.08	131.62	125.98	126.03
Gross Profit	58739	63229	62416	65000	69571	75663	77148	79063	74556	74478
Gross Margin	60.3%	58.6%	58.6%	58.6%	60.1%	62.8%	60.7%	60.1%	59.2%	59.1%
SG&A Exp.	41517	30717	31366	35624	39951	27089	41016	29986	30562	28336
D&A Exp.	14610	16534	16405	16496	16460	16606	16533	16017	15928	16954
Operating Profit	2612	15978	14645	12880	13160	31968	19599	33060	28066	29188
Op. Margin	2.7%	14.8%	13.7%	11.6%	11.4%	26.5%	15.4%	25.1%	22.3%	23.2%
Net Profit	-2193	4894	2549	2404	875	11497	9625	17879	13127	30101
Net Margin	-2.3%	4.5%	2.4%	2.2%	0.8%	9.5%	7.6%	13.6%	10.4%	23.9%
Free Cash Flow	10319	14518	16119	13315	11013	21634	13086	11310	5217	7475
Income Tax	-2319	1919	2467	285	-660	5730	3314	9865	7378	-9956

Balance Sheet Metrics

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Total Assets (\$B)	202.35	226.91	220.01	230.46	225.22	274.10	232.62	244.18	244.18	257.14
Cash & Equivalents	9782	2009	6668	13362	3093	53528	10598	4470	2880	2079
Acc. Receivable	11703	12573	11781	11776	12576	12439	13993	13457	17513	23493
Inventories	2092	1426	1131	940	1075	1020	1153	1252	1202	1034
Goodwill/Int. (\$B)	73.21	101.30	100.81	102.49	107.82	106.18	105.71	119.50	122.78	127.84
Total Liab. (\$B)	123.45	142.76	133.09	144.55	139.69	178.68	218.94	226.33	220.15	212.46
Accounts Payable	3856	4337	3936	4194	4454	4954	5598	5700	7084	7063
LT Debt (\$B)	51.95	62.26	52.79	55.15	51.99	93.59	113.27	109.73	108.08	117.10
Total Equity	41706	41382	38569	35970	33157	38836	12298	16428	22524	43096
D/E Ratio	1.25	1.50	1.37	1.53	1.57	2.41	9.21	6.68	4.80	2.72

Profitability & Per Share Metrics

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Return on Assets	-1.1%	2.3%	1.1%	1.1%	0.4%	4.6%	3.8%	7.5%	5.4%	12.0%
Return on Equity	-4.8%	11.8%	6.4%	6.5%	2.5%	31.9%	37.6%	125%	67.4%	91.7%
ROIC	-1.8%	3.5%	1.8%	1.7%	0.6%	7.0%	6.1%	14.0%	10.1%	20.5%
Shares Out.	2841	2835.7	2828.1	2835.5	2858.3	4141.1	4155.4	4073.2	4076.7	4079.5
Revenue/Share	34.17	37.95	37.62	39.05	40.48	41.95	31.92	32.16	30.83	30.82
FCF/Share	3.62	5.11	5.69	4.69	3.85	7.53	3.29	2.76	1.28	1.83

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

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