



West Pharmaceutical Services (WST)

Updated November 8th, 2018 by Jonathan Weber

Key Metrics

Current Price:	\$113	5 Year CAGR Estimate:	-8.1%	Volatility Percentile:	65.6%
Fair Value Price:	\$51	5 Year Growth Estimate:	7.0%	Momentum Percentile:	64.0%
% Fair Value:	220%	5 Year Valuation Multiple Estimate:	-15.6%	Growth Percentile:	62.5%
Dividend Yield:	0.5%	5 Year Price Target	\$72	Valuation Percentile:	0.2%
Dividend Risk Score:	A	Retirement Suitability Score:	C	Total Return Percentile:	0.4%

Overview & Current Events

West Pharmaceutical Services manufactures packaging and components involved in the distribution and application of pharmaceuticals. The company's products include *Zenith Crystal*, a medical glass alternative, and *SmartDose*, an automatic medication delivery system. West Pharmaceutical was founded in 1923, is headquartered in Exton, Pennsylvania, and trades with a market capitalization of \$8.3 billion. The company has increased its dividend for 25 consecutive years, which qualifies it to be a Dividend Champion.

West Pharmaceutical reported its third quarter earnings results on October 25. The company reported revenues of \$432 million, which represents an increase of 8.4% compared to the previous year's quarter. West Pharmaceutical's organic sales growth rate was even better than its reported sales growth rate, at 9.6%. The reason for the difference was an adverse movement in currency rates. Both the Pharma segment as well as the Contract Manufacturing segment generated revenue growth rates in the double-digit, which propelled West Pharmaceutical's organic revenue growth rate to the highest level over the last couple of quarters. West Pharmaceutical introduced a new version of SmartDose, SelfDose, which allows patients to control injections.

West Pharmaceutical generated earnings-per-share of \$0.76 during the third quarter, which represents an increase of 13.4% compared to the previous year's quarter. West Pharmaceutical also reaffirmed its revenue guidance for 2018 (\$1.725 billion), its earnings-per-share guidance for 2018 (\$2.85) while lowering its capex guidance to ~\$115 million.

Growth on a Per-Share Basis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
EPS	\$1.19	\$1.06	\$1.05	\$1.17	\$1.38	\$1.57	\$1.75	\$1.30	\$1.91	\$2.78	\$2.85	\$4.00
DPS	\$0.29	\$0.31	\$0.33	\$0.35	\$0.37	\$0.39	\$0.41	\$0.46	\$0.50	\$0.54	\$0.58	\$0.95
Shares	65	66	67	67	67	70	71	72	73	74	74	76

West Pharmaceutical has grown its earnings-per-share at an attractive pace of 9.9% annually between 2008 and 2017. West Pharmaceutical's earnings-per-share growth has been a bit uneven, as earnings-per-share rose by 46% during 2017. West Pharmaceutical projects a long-term organic sales growth of 6% to 8%. We believe that this could be too optimistic, as West Pharmaceutical's revenues have grown at a slower pace of 4.8% over the last 9 years.

Revenue growth and a more favorable product mix will be the source of West Pharmaceutical's growth. The company seeks to increase its revenues in the Proprietary Products segment, which has significantly higher margins than the Contract-Manufactured Products equivalent. West Pharmaceutical's organic sales growth rate during 2018 looks promising, but the company forecasts that its earnings-per-share will grow by only 2.5% this year. In the long run it is likely that West Pharmaceutical will deliver earnings-per-share growth that is higher than its revenue growth rate.

Valuation Analysis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	Now	2023
Avg. P/E	18.0	17.1	18.1	17.8	17.2	23.7	26.1	43.8	38.1	18.3	39.6	18.0
Avg. Yld.	1.4%	1.7%	1.7%	1.7%	1.6%	1.0%	0.9%	0.8%	0.7%	0.6%	0.5%	1.0%

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West Pharmaceutical is a company that has delivered compelling earnings-per-share growth during the last decade, and that has a long and successful dividend growth history. The company nevertheless looks tremendously overvalued at its current price, as it trades at close to 40 times this year's net profits. Even if earnings-per-share rise by a faster pace compared to how the company grew in the past, this valuation would not be justified. West Pharmaceutical's median price to earnings multiple of 18 seems more justified, which means that shares have a lot of downside potential. The multiple compression tailwind is in the double digits, on an annual basis. The dividend yield is very low at current prices.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
GP/A	25.9%	23.9%	24.6%	24.3%	24.8%	26.0%	26.8%	26.9%	29.2%	27.5%	28.0%	28.5%
Debt/A	58.3%	54.4%	51.7%	53.2%	53.4%	45.8%	42.7%	39.6%	34.9%	31.3%	30.0%	30.0%
Int. Cov.	8.6	6.8	5.6	6.6	8.4	10.9	14.3	10.4	28.3	35.4	38	40
Payout	24.4%	29.2%	31.4%	29.9%	26.8%	24.8%	23.4%	35.4%	26.2%	19.4%	20.4%	25.0%
Std. Dev.	43.3%	29.6%	24.4%	27.6%	22.8%	18.9%	23.0%	21.9%	22.2%	22.3%	22.0%	22.0%

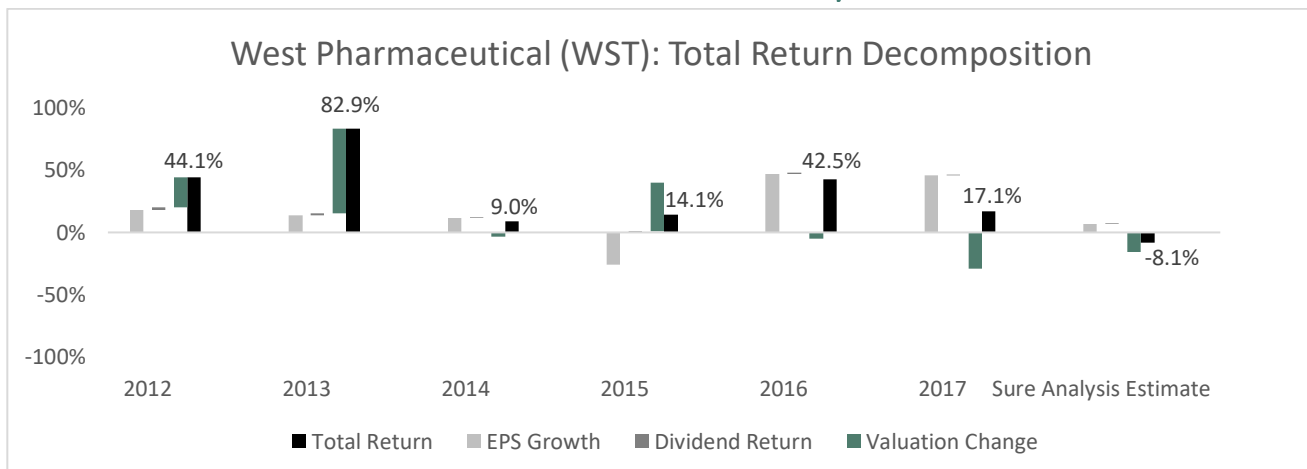
West Pharmaceutical produces a solid amount of gross profits with its assets, which is not atypical for medical technology companies. West Pharmaceutical has managed to clean up its balance sheet considerably over the last decade. The debt to asset ratio has almost been cut in half. West Pharmaceutical currently has a very strong balance sheet. Its cash position is, in fact, larger than its debt position (\$300 million versus \$200 million as of the end of Q3). This explains why West Pharmaceutical's interest coverage ratio is so high.

West Pharmaceutical is not active in a cyclical industry, as demand for medical items and pharmacologic products is not dependent on economic conditions. This explains why West Pharmaceutical was not impacted by the last financial crisis to a significant degree. Earnings-per-share declined by only 11% peak-to-trough.

Final Thoughts & Recommendation

West Pharmaceutical is a high-quality medical technology company that has generated compelling earnings-per-share growth during the last decade. The company is also relatively immune to recessions, and West Pharmaceutical has raised its dividend for 25 years in a row. Despite these compelling characteristics, the company is one of the most overvalued securities in our investment universe. Because of this, West Pharmaceutical earns a strong sell 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	1051	1056	1105	1192	1266	1368	1421	1400	1509	1599
Gross Profit	303	304	318	339	388	435	448	456	501	513
Gross Margin	28.8%	28.8%	28.8%	28.5%	30.6%	31.8%	31.5%	32.6%	33.2%	32.1%
SG&A Exp.	159	178	188	191	218	0	0	61	2	0
D&A Exp.	61	68	73	76	77	85	90	90	91	97
Operating Profit	125	106	107	119	143	399	412	363	468	480
Operating Margin	11.9%	10.0%	9.6%	10.0%	11.3%	29.1%	29.0%	25.9%	31.0%	30.0%
Net Profit	86	73	65	76	81	112	127	96	144	151
Net Margin	8.2%	6.9%	5.9%	6.3%	6.4%	8.2%	8.9%	6.8%	9.5%	9.4%
Free Cash Flow	-4	30	65	34	55	65	71	81	49	133
Income Tax	24	14	14	24	33	40	47	26	54	81

Balance Sheet Metrics

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Total Assets	1169	1271	1294	1399	1564	1672	1670	1695	1717	1863
Cash & Equivalents	87	83	110	92	162	230	255	275	203	236
Accounts Receivable	129	139	126	147	175	186	179	181	201	253
Inventories	116	129	147	152	162	177	182	181	199	215
Goodwill & Int. Ass.	155	170	168	164	163	163	151	142	126	129
Total Liabilities	682	692	669	744	835	765	713	671	599	583
Accounts Payable	68	68	63	90	103	108	103	120	122	138
Long-Term Debt	386	380	358	349	412	374	336	298	229	197
Shareholder's Equity	487	579	626	655	729	906	957	1024	1118	1280
D/E Ratio	0.79	0.66	0.57	0.53	0.56	0.41	0.35	0.29	0.20	0.15

Profitability & Per Share Metrics

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Return on Assets	7.3%	6.0%	5.1%	5.6%	5.4%	6.9%	7.6%	5.7%	8.4%	8.4%
Return on Equity	17.7%	13.6%	10.8%	11.8%	11.7%	13.7%	13.6%	9.7%	13.4%	12.6%
ROIC	9.8%	7.9%	6.7%	7.6%	7.5%	9.3%	9.9%	7.3%	10.8%	10.7%
Shares Out.	65	66	67	67	67	70	71	72	73	74
Revenue/Share	14.56	14.54	15.05	16.11	17.64	19.17	19.52	18.97	20.12	21.10
FCF/Share	-0.06	0.41	0.88	0.46	0.77	0.91	0.97	1.09	0.66	1.75

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

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