



Philip Morris International (PM)

Updated April 18th, 2019 by Eli Inkrot

Key Metrics

Current Price:	\$85	5 Year CAGR Estimate:	10.2%	Volatility Percentile:	67.2%
Fair Value Price:	\$84	5 Year Growth Estimate:	5.0%	Momentum Percentile:	17.9%
% Fair Value:	101%	5 Year Valuation Multiple Estimate:	-0.2%	Growth Percentile:	35.4%
Dividend Yield:	5.4%	5 Year Price Target	\$107	Valuation Percentile:	54.3%
Dividend Risk Score:	C	Retirement Suitability Score:	B	Total Return Percentile:	61.3%

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. Its sister company Altria sells the Marlboro brand (again, among others) in the U.S. Philip Morris has a market capitalization of \$132 billion.

On April 18th, 2019 Philip Morris reported Q1 2019 results for the period ending March 31st, 2019. For the quarter the company generated revenue of \$6.8 billion, which was down 2.1% as reported and up 3.2% excluding unfavorable currency fluctuations. Shipment volumes were largely flat for cigarettes, while heated tobacco units – a much smaller portion of the business – were up 20.2% year-over-year. Adjusted earnings-per-share totaled \$1.09 against \$1.00 in Q1 of 2018. The company's total international market share was up 1.0% to 28.4%, while its total international heated tobacco unit market share was up 0.5% to 2.0%.

Philip Morris also provided an updated 2019 full-year forecast. The company expects reported earnings-per-share to come in \$4.87 or greater, with adjusted earnings-per-share excluding currency fluctuations reaching \$5.09 or more per share. This is a marked decline of the company's previous \$5.37 per share or greater forecast provided last quarter, due primarily to the company's deconsolidation of the Canadian RBH subsidiary.

Growth on a Per-Share Basis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
EPS	\$3.24	\$3.92	\$4.85	\$5.17	\$5.26	\$4.76	\$4.42	\$4.48	\$4.72	\$5.10	\$5.09	\$6.50
DPS	\$2.24	\$2.44	\$2.84	\$3.24	\$3.58	\$3.88	\$4.04	\$4.12	\$4.22	\$4.49	\$4.68	\$5.52
Shares	1,887	1,802	1,726	1,654	1,589	1,547	1,549	1,551	1,553	1,554	1,550	1,450

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 International, the non-US business, would be the high-growth company. It looked like this would come true through 2013, as Philip Morris recorded near double-digit earnings-per-share growth through the first five years of its existence. This changed in the following years, as Philip Morris' profits declined and stagnated. Even during 2018, earnings-per-share remained 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 outside of the US.

Philip Morris' weak profit growth over the last couple of years was partially due to 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 stabilize its business.

Valuation Analysis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	Now	2024
Avg. P/E	13.4	13.2	13.8	16.7	17.0	17.7	18.8	21.5	23.4	17.3	16.7	16.5

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Avg. Yld.	5.1%	4.7%	4.2%	3.8%	4.0%	4.6%	4.9%	4.3%	3.8%	5.1%	5.5%	5.2%
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Shares of Philip Morris traded at an elevated valuation in the 2015 through 2017 stretch, but otherwise a mid-teens multiple has been fairly typical. At the current mark of 16.7 times anticipated earnings, we believe shares are more or less fairly valued – indicating neither a significant headwind or tailwind from the valuation component. However, with the elevated and consistent payout ratio, Philip Morris’ dividend ought to add meaningfully to shareholder returns.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
Payout	69%	62%	59%	63%	68%	82%	91%	92%	89%	88%	92%	85%

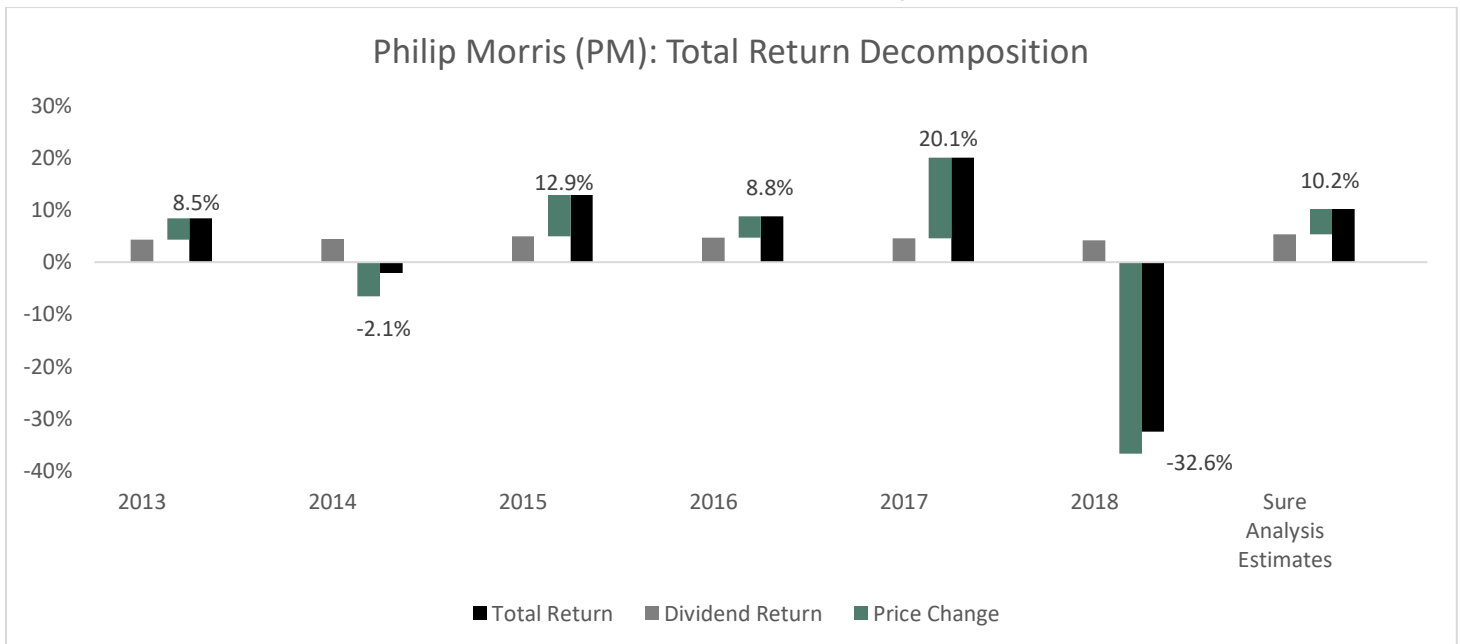
Philip Morris’ dividend payout ratio has never been especially low, and the ratio increased further during the last decade. At the peak, Philip Morris has paid out more than 90% of its net profits to its owners. The dividend payout ratio has come down slightly but remains at a high level. Due to strong cash generation, low capex requirements and the stability of Philip Morris’ business model during recessions the dividend still appears to be relatively well-covered.

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 is generally 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.

Final Thoughts & Recommendation

Shares are up about 6% since our last update, and indeed up over 25% year-to-date, while earnings expectations have been reduced. Philip Morris is an international tobacco giant that is heavily impacted by currency rate movements. The payout ratio is elevated, but thus far the company has proven more than capable of sustaining its lofty dividend. However, growth expectations are more or less average and the valuation has drifted upward. While the security is suitable for income investors, we are more cautious today, and have reduced our rating from buy to hold.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Revenue	25035	27208	31097	31377	31217	29767	26794	26685	28748	29625
Gross Profit	16013	17495	20419	21004	20807	19331	17429	17294	18316	18867
Gross Margin	64.0%	64.3%	65.7%	66.9%	66.7%	64.9%	65.0%	64.8%	63.7%	63.7%
SG&A Exp.	5870	6160	6870	6961	6890	7001	6656	6405	6725	7449
D&A Exp.	853	932	993	898	882	889	754	743	875	989
Operating Profit	10069	11247	13451	13946	13824	12237	10691	10815	11503	11336
Op. Margin	40.2%	41.3%	43.3%	44.4%	44.3%	41.1%	39.9%	40.5%	40.0%	38.3%
Net Profit	6342	7259	8591	8800	8576	7493	6873	6967	6035	7911
Net Margin	25.3%	26.7%	27.6%	28.0%	27.5%	25.2%	25.7%	26.1%	21.0%	26.7%
Free Cash Flow	7169	8724	9632	8365	8935	6586	6905	6905	7364	8042
Income Tax	2691	2826	3653	3833	3670	3097	2688	2768	4307	2445

Balance Sheet Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Total Assets	34552	35050	35488	37670	38168	35187	33956	36851	42968	39801
Cash & Equivalents	1540	1703	2550	2983	2154	1682	3417	4239	8447	6593
Acc. Receivable	3131	3065	3201	3589	3853	4004	2778	3499	3194	2950
Inventories	9207	8317	8120	8949	9846	8592	8473	9017	8806	8804
Goodwill & Int.	12658	14034	13625	13519	12086	11373	10038	9794	10098	9467
Total Liabilities	28407	29929	34937	40824	44442	46390	45432	47751	53198	50540
Accounts Payable	670	835	1031	1103	1274	1242	1289	1666	2242	2068
Long-Term Debt	15416	16502	18545	22839	27678	29455	28480	29067	34339	31759
Total Equity	5716	3506	229	-3476	-7766	-12.6B	-13.2B	-12.7B	-12.1B	-12.5B
D/E Ratio	2.70	4.71	80.98	-6.57	-3.56	-2.33	-2.15	-2.29	-2.84	-2.55

Profitability & Per Share Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Return on Assets	18.8%	20.9%	24.4%	24.1%	22.6%	20.4%	19.9%	19.7%	15.1%	19.1%
Return on Equity	96.0%	157.4%	460%	-542%	-153%	-73.5%	-53.1%	-53.7%	-48.7%	-64.5%
ROIC	30.6%	33.6%	42.2%	45.4%	41.7%	37.8%	39.0%	39.6%	28.6%	35.1%
Shares Out.	1950	1842	1762	1692	1622	1566	1549	1551	1553	1555
Revenue/Share	12.84	14.77	17.65	18.54	19.25	19.01	17.30	17.21	18.51	19.05
FCF/Share	3.68	4.74	5.47	4.94	5.51	4.21	4.46	4.45	4.74	5.17

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

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