



# Apple Inc. (AAPL)

Updated May 1<sup>st</sup>, 2019 by Eli Inkrot

## Key Metrics

<b>Current Price:</b>	\$212	<b>5 Year CAGR Estimate:</b>	5.1%	<b>Volatility Percentile:</b>	68.9%
<b>Fair Value Price:</b>	\$179	<b>5 Year Growth Estimate:</b>	7.0%	<b>Momentum Percentile:</b>	70.4%
<b>% Fair Value:</b>	119%	<b>5 Year Valuation Multiple Estimate:</b>	-3.4%	<b>Growth Percentile:</b>	66.4%
<b>Dividend Yield:</b>	1.5%	<b>5 Year Price Target</b>	\$251	<b>Valuation Percentile:</b>	27.5%
<b>Dividend Risk Score:</b>	B	<b>Retirement Suitability Score:</b>	C	<b>Total Return Percentile:</b>	26.2%

## Overview & Current Events

Apple is a technology company that designs, manufactures and sells products such as smartphones, personal computers and portable digital music players. Apple also has a thriving services business that sells music, apps, and subscriptions. The company was founded in 1976, is headquartered in Cupertino, CA and is currently valued at \$996 billion.

On April 30<sup>th</sup>, 2019 Apple reported Q2 2019 results for the period ending March 30<sup>th</sup>, 2019. For the quarter Apple recorded revenue of \$58.0 billion, down 5.1% compared to Q2 2018, as gains of 16.2%, 30.0% and 21.6% in the Services, Wearables and iPad segments were more than offset by a 17.3% decline in iPhones, which made up 53.5% of total sales. International sales accounted for 61% of the quarter's revenue. Net income fell 16.4%, from \$13.82 billion to \$11.56 billion, while earnings-per-share dropped 9.9% from \$2.73 in Q2 2018 to \$2.46 in Q2 2019, partially helped by a lower share count.

Apple announced an additional \$75 billion share repurchase program, along with a 5% dividend increase to \$0.77 per quarter. In addition, Apple provided guidance for Q3 2019. The company anticipates revenue of between \$52.5 billion and \$54.5 billion, with a 37% to 38% gross margin and \$8.7 billion to \$8.8 billion in operating expenses.

## Growth on a Per-Share Basis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
<b>EPS</b>	\$0.90	\$2.16	\$3.95	\$6.31	\$5.68	\$6.45	\$9.22	\$8.31	\$9.21	\$11.91	<b>\$11.90</b>	<b>\$16.70</b>
<b>DPS</b>	---	---	---	\$0.38	\$1.63	\$1.81	\$1.98	\$2.18	\$2.40	\$2.72	<b>\$3.08</b>	<b>\$4.40</b>
<b>Shares</b>	6,299	6,412	6,505	6,575	6,295	5,866	5,579	5,336	5,126	4,755	<b>4,600</b>	<b>4,000</b>

Apple is among the largest publicly traded corporations in the world. Since 2012 Apple's earnings-per-share have grown by 11.2% annually, which is an attractive growth rate, although it is substantially lower than the growth rates Apple produced in the years prior to 2012. The bigger the bottom line gets, the harder it becomes to grow at a very high pace.

Going forward Apple's earnings growth will be driven by several factors. One of these is the ongoing cycle of iPhone releases, which saw a significant decline in Q2 2019. However, in the long run Apple should be able to grow its iPhone sales again, albeit in an irregular fashion. Moreover, in emerging countries where consumers have rising disposable incomes, Apple should be able to increase the amount of smartphones it is selling over the coming years. Apple also has been increasing the selling prices of its phones over the last couple of years, which is a tailwind for revenues.

Another avenue for growth is Apple's services segment. This business unit, which consists of iTunes, Apple Music, the App Store, iCloud, Apple Pay, etc., has recorded significant revenue growth rate during the last couple of quarters. Services revenues are growing substantially faster than other segments, and at the same time this business produces high-margin recurring revenues and is not cyclical.

Another factor that has played a role in the past is the shrinking share count. Due to its immense cash flows Apple is able to repurchase hundreds of millions of shares. The resulting lower share count means that each remaining share's portion of all profits rises. Apple should continue to lower its share count further through 2019 and beyond. Taking these items collectively – a strong "cash cow" legacy business, growing Service revenue and a shrinking share count – we are forecasting 7% annual growth over the intermediate-term.

*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.*



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## Valuation Analysis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	Now	2024
Avg. P/E	19.2	15.2	12.4	12.0	12.3	13.0	12.8	12.6	14.9	15.3	17.8	15.0
Avg. Yld.	---	---	---	0.5%	2.3%	2.2%	1.7%	2.1%	1.8%	1.5%	1.5%	1.8%

Absent the last recession, shares of Apple have routinely traded with an average price-to-earnings multiple of just over 13 times earnings. We believe a multiple closer to 15 times earnings is a fair starting point, considering the growth possibilities of the firm to go along with an exceptional balance sheet. Given the current valuation of 17.8 times expected earnings, this could imply the potential for a valuation headwind in the years to come.

While the dividend yield is not spectacular, it is very well covered with the propensity to grow over time.

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

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
Payout	---	---	---	6%	29%	28%	22%	26%	26%	23%	26%	26%

Apple started paying a dividend in 2012. Since then, the dividend has been increased regularly, but more or less in line with the company's earnings-per-share growth, which is why the dividend payout ratio has remained in the 20% range throughout the last couple of years. This, coupled with the company's enviable balance sheet, makes Apple's dividend look quite safe.

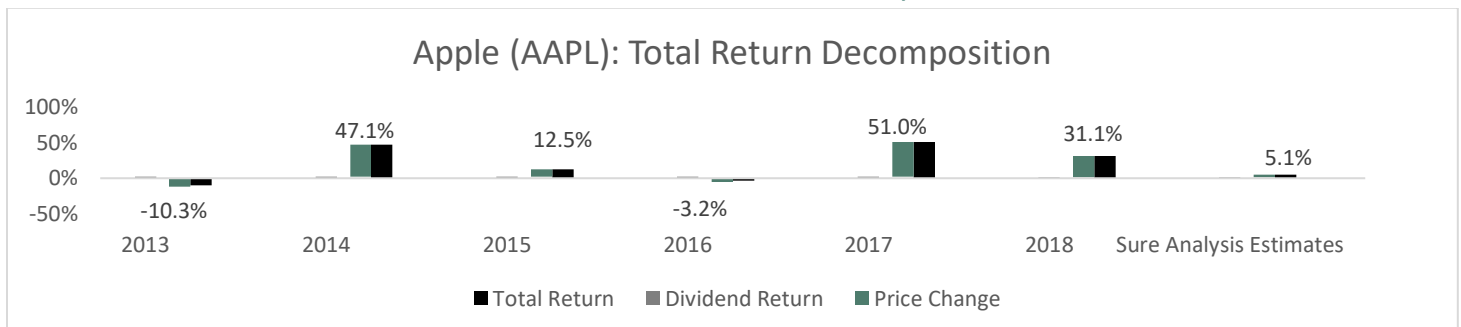
Apple's brand is admired around the globe, and together with Samsung the company basically earns all the profits in the top end smartphone market. That is unlikely to change soon, and with Apple's service business becoming larger the company will be able to benefit from an increasing stream of recurring revenues. During the last financial crisis Apple's profits rose, but that was during the hyper-growth phase. Since Apple is still highly dependent on sales of relatively high-cost smartphones, a major economic crisis could hurt its profits considerably.

As of the most recent report Apple held \$80.1 billion in cash and securities, \$123.3 billion in current assets and \$342 billion in total assets (of which an additional \$145 billion are non-current marketable securities) against \$93.7 billion in current liabilities and \$236.1 billion in total liabilities.

## Final Thoughts & Recommendation

Shares are up an exceptional 37% since our last update. We are enthused on a number of fronts, including a business with an extraordinary story, a Services segment that is picking up steam and a balance sheet that provides significant safety in good times or bad. However, in our view, the current valuation leaves something to be desired. We are forecasting 5.1% annual total return potential, stemming from 7% growth and a 1.5% starting yield, offset by a 3.4% valuation headwind as a result of the much higher share price as of late. We 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
<b>Revenue (\$B)</b>	42.91	65.23	108.25	156.51	170.91	182.80	233.72	215.64	229.23	265.60
<b>Gross Profit</b>	17222	25684	43818	68662	64304	70537	93626	84263	88186	102B
<b>Gross Margin</b>	40.1%	39.4%	40.5%	43.9%	37.6%	38.6%	40.1%	39.1%	38.5%	38.3%
<b>SG&amp;A Exp.</b>	4149	5517	7599	10040	10830	11993	14329	14194	15261	16705
<b>D&amp;A Exp.</b>	734	1027	1814	3277	6757	7946	11257	10505	10157	10903
<b>Operating Profit</b>	11740	18385	33790	55241	48999	52503	71230	60024	61344	70898
<b>Op. Margin</b>	27.4%	28.2%	31.2%	35.3%	28.7%	28.7%	30.5%	27.8%	26.8%	26.7%
<b>Net Profit</b>	8235	14013	25922	41733	37037	39510	53394	45687	48351	59531
<b>Net Margin</b>	19.2%	21.5%	23.9%	26.7%	21.7%	21.6%	22.8%	21.2%	21.1%	22.4%
<b>Free Cash Flow</b>	8946	16474	30077	41454	44590	49900	69778	52276	50803	64121
<b>Income Tax</b>	3831	4527	8283	14030	13118	13973	19121	15685	15738	13372

## Balance Sheet Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
<b>Total Assets (\$B)</b>	47.50	75.18	116.37	176.06	207.00	231.84	290.35	321.69	375.32	365.73
<b>Cash &amp; Equivalents</b>	5263	11261	9815	10746	14259	13844	21120	20484	20289	25913
<b>Accounts Receivable</b>	3361	5510	5369	10930	13102	17460	16849	15754	17874	23186
<b>Inventories</b>	455	1051	776	791	1764	2111	2349	2132	4855	3956
<b>Goodwill &amp; Int. Ass.</b>	453	1083	4432	5359	5756	8758	9009	8620	8015	N/A
<b>Total Liab. (\$B)</b>	15.86	27.39	39.76	57.85	83.45	120.29	170.99	193.44	241.27	258.58
<b>Accounts Payable</b>	5601	12015	14632	21175	22367	30196	35490	37294	49049	55888
<b>Long-Term Debt (\$B)</b>	0	0	0	0	16.96	35.30	64.33	87.03	115.68	114.48
<b>Total Equity (\$B)</b>	31.64	47.79	76.62	118.21	123.55	111.55	119.36	128.25	134.05	107.15
<b>D/E Ratio</b>	0	0	0	0	0.1373	0.3164	0.539	0.6786	0.863	1.0685

## Profitability & Per Share Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
<b>Return on Assets</b>	19.7%	22.8%	27.1%	28.5%	19.3%	18.0%	20.5%	14.9%	13.9%	16.1%
<b>Return on Equity</b>	30.5%	35.3%	41.7%	42.8%	30.6%	33.6%	46.2%	36.9%	36.9%	49.4%
<b>ROIC</b>	30.5%	35.3%	41.7%	42.8%	28.6%	27.5%	32.3%	22.9%	20.8%	25.3%
<b>Shares Out.</b>	6300	6410	6500	6570	6290	5870	5580	5340	5130	4850
<b>Revenue/Share</b>	6.76	10.08	16.51	23.65	26.21	29.86	40.34	39.21	43.65	53.12
<b>FCF/Share</b>	1.41	2.55	4.59	6.26	6.84	8.15	12.05	9.50	9.67	12.82

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

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