



Walgreens Boots Alliance (WBA)

Updated July 5th, 2019 by Eli Inkrot

Key Metrics

Current Price:	\$55	5 Year CAGR Estimate:	15.9%	Volatility Percentile:	53.1%
Fair Value Price:	\$75	5 Year Growth Estimate:	6.0%	Momentum Percentile:	26.1%
% Fair Value:	73%	5 Year Valuation Multiple Estimate:	6.6%	Growth Percentile:	52.4%
Dividend Yield:	3.3%	5 Year Price Target	\$101	Valuation Percentile:	95.0%
Dividend Risk Score:	A	Retirement Suitability Score:	A	Total Return Percentile:	92.0%

Overview & Current Events

Walgreens Boots Alliance is the largest retail pharmacy in both the United States and Europe. Through its flagship *Walgreens* business and other business ventures (including equity investments), Walgreens has a presence in more than 25 countries and employs more than 415,000 people. In its leading retail pharmacy business, Walgreens operates approximately 18,500 stores in 11 countries. The \$50 billion market cap company also operates one of the largest global pharmaceutical wholesale and distribution networks, with more than 390 centers that deliver to upwards of 230,000 pharmacies, doctors, health centers and hospitals each year.

On June 27th, 2019 Walgreens reported Q3 fiscal year 2019 results for the period ending May 31st, 2019. Sales increased 0.7% (2.9% on a constant currency basis) to \$34.6 billion compared to Q3 2018, due to growth in the Retail Pharmacy USA division (up 2.3%). Adjusted net earnings decreased 12.1% to \$1.3 billion and adjusted earnings-per-share fell 4.0% to \$1.47, as the decline in net earnings was partially offset by a substantially lower share count.

Walgreens also reiterated its fiscal year 2019 outlook, indicating that adjusted earnings-per-share are anticipated to be roughly flat year-over-year. This is consistent with what the company said last quarter, but down from previous guidance of 7% to 12% to start the year. Walgreens CEO Stefano Pessina said that progress was being made on the cost management program after a difficult second quarter. Over the long-term the company still believes it can grow the bottom line in the mid-to-high single digits.

Growth on a Per-Share Basis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
EPS	\$2.02	\$2.16	\$2.64	\$2.53	\$2.61	\$2.90	\$3.88	\$4.59	\$5.10	\$6.02	\$6.02	\$8.06
DPS	\$0.48	\$0.59	\$0.80	\$0.95	\$1.14	\$1.28	\$1.37	\$1.46	\$1.53	\$1.64	\$1.80	\$2.82
Shares	989	939	889	944	947	950	1,090	1,083	1,024	952	925	850

In our last update, as a result of the surprise change in management's guidance, along with headwinds that have begun to accelerate, we significantly reduced our earnings expectations for this year and also our growth expectation over the intermediate-term. Moving forward we expect flat earnings-per-share results this year, followed by 6% annual growth thereafter.

From 2009 through 2018, Walgreens grew earnings-per-share by 12.9% per annum. This was driven by a combination of factors including solid top-line growth (\$63 billion to \$132 billion), net profit margin expansion (3.7% to 4.6%) and a reduction in the number of shares outstanding. Given Walgreens much higher base from which to grow, we anticipate the company's growth rate slowing from the low double-digits to the mid-single-digits. Share repurchases and an aging population tailwind will continue to help, but Walgreens' core business is becoming more challenged.

Valuation Analysis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	Now	2024
Avg. P/E	13.9	15.9	14.8	13.2	16.3	21.8	20.2	18.0	16.2	11.5	9.1	12.5
Avg. Yld.	1.7%	1.7%	2.1%	2.8%	2.7%	2.0%	1.8%	1.8%	1.9%	2.3%	3.3%	2.8%

Disclosure: This analyst is long the security discussed in this research report.



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During the past decade shares of Walgreens have traded with an average price-to-earnings ratio of 16.2. However, this was during a time when the company's growth rate was much more robust. We have reduced this fair value multiple to better reflect a slower anticipated growth rate moving forward. Still, shares are trading at a compelling valuation.

Moreover, the dividend ought to add meaningfully in the years to come. Walgreens has a storied track record of increasing its dividend every year. With a modest payout ratio, and an expectation of reasonable earnings growth, there is ample room for the dividend to continue to grow moving forward.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
Payout	22%	25%	27%	35%	42%	43%	34%	31%	31%	27%	30%	35%

Walgreens' competitive advantage lies in its vast scale and network in an important and growing industry. However, lately a variety of headwinds have surfaced including reimbursement pressure, lower generic deflation and consumer market challenges that have called this advantage into question to a degree.

Meanwhile, the payout ratio remains reasonable and should continue to add an income ballast for investors.

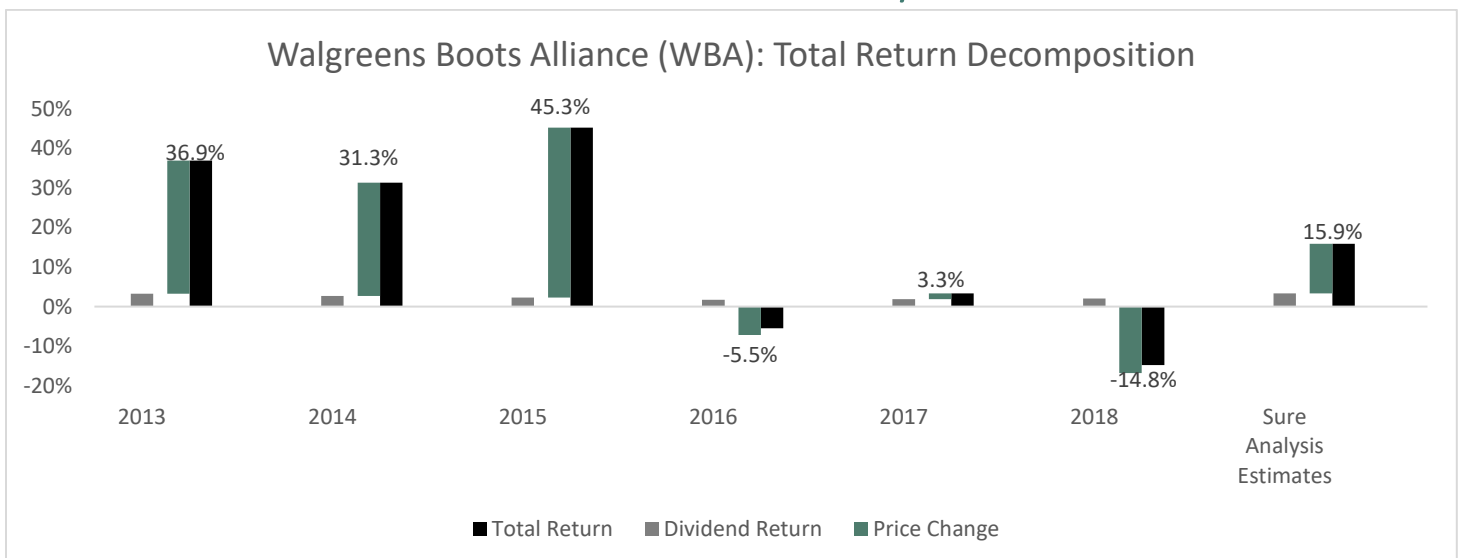
Furthermore, despite the lack of expected growth this year, it should be noted that Walgreens has put together a very strong record in good times or bad. Walgreens' earnings dipped just 6.9% in 2009, as an illustration.

As of the most recent quarter Walgreens held \$839 million in cash, \$19.0 billion in current assets (including \$9.9 billion in inventory) and \$68.6 billion in total assets (41% of which was goodwill and intangible assets) against \$25.1 billion in current liabilities and \$43.8 billion in total liabilities. Long-term debt stood at \$12.1 billion against underlying earnings power of ~\$5.5 billion.

Final Thoughts & Recommendation

Shares are more or less unchanged since our last update. Walgreens has proven to be an exceptional company over the years. The dividend track record is excellent, earnings growth had previously been robust and the company still maintains a relatively conservative stance even while digesting acquisitions. That being said, industry headwinds are starting to gain some momentum. Total return potential comes in at 15.9% per annum, stemming from 6.0% growth, a 3.3% starting yield and a 6.6% valuation tailwind. We continue to rate Walgreens as a buy at the current quotation.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Revenue (\$B)	63.34	67.42	72.18	71.63	72.22	76.39	103.44	117.35	118.2	131.54
Gross Profit	17613	18976	20492	20342	21119	21569	26753	29874	29162	30792
Gross Margin	27.8%	28.1%	28.4%	28.4%	29.2%	28.2%	25.9%	25.5%	24.7%	23.4%
SG&A Exp.	14366	15518	16561	16878	17543	17992	22400	23910	23740	24569
D&A Exp.	975	1030	1086	1166	1283	1316	1742	1718	1654	1770
Operating Profit	3247	3458	3931	3464	3576	3577	4353	5964	5422	6223
Op. Margin	5.1%	5.1%	5.4%	4.8%	5.0%	4.7%	4.2%	5.1%	4.6%	4.7%
Net Profit	2006	2091	2714	2127	2548	1932	4220	4173	4078	5024
Net Margin	3.2%	3.1%	3.8%	3.0%	3.5%	2.5%	4.1%	3.6%	3.4%	3.8%
Free Cash Flow	2184	2730	2430	2881	3089	2787	4413	6522	5900	6898
Income Tax	1158	1282	1580	1249	1499	1526	1056	997	760	998

Balance Sheet Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Total Assets	25142	26275	27454	33462	35481	37250	68782	72688	66009	68124
Cash & Equivalents	2087	1880	1556	1297	2106	2646	3000	9807	3301	785
Acc. Receivable	2496	2450	2497	2167	2632	3218	6849	6260	6528	6573
Inventories	6789	7378	8044	7036	6852	6076	8678	8956	8899	9565
Goodwill & Int.	2158	3001	3229	3447	3717	3539	28723	25829	25788	28697
Total Liabilities	10766	11875	12607	15226	16027	16633	37482	42407	37735	41435
Accounts Payable	4308	4585	4810	4384	4635	4315	10088	11000	12494	13566
Long-Term Debt	2351	2401	2409	5392	5047	4490	14383	19028	12935	14397
Total Equity	14376	14400	14847	18236	19454	20513	30861	29880	27466	26007
D/E Ratio	0.16	0.17	0.16	0.30	0.26	0.22	0.47	0.64	0.47	0.55

Profitability & Per Share Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Return on Assets	8.4%	8.1%	10.1%	7.0%	7.4%	5.3%	8.0%	5.9%	5.9%	7.5%
Return on Equity	14.7%	14.5%	18.6%	12.9%	13.5%	9.7%	16.4%	13.7%	14.2%	18.8%
ROIC	12.9%	12.5%	15.9%	10.4%	10.6%	7.8%	11.9%	8.8%	9.0%	12.2%
Shares Out.	989	939	889	944	947	950	1,090	1,083	1,024	952
Revenue/Share	63.89	68.25	78.08	81.39	75.60	79.15	98.15	107.55	109.61	132.20
FCF/Share	2.20	2.76	2.63	3.27	3.23	2.89	4.19	5.98	5.47	6.93

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

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