



West Pharmaceutical Services (WST)

Updated October 24th, 2019 by Jonathan Weber

Key Metrics

Current Price:	\$138	5 Year CAGR Estimate:	-10.0%	Volatility Percentile:	66.2%
Fair Value Price:	\$56	5 Year Growth Estimate:	7.0%	Momentum Percentile:	90.4%
% Fair Value:	248%	5 Year Valuation Multiple Estimate:	-16.6%	Growth Percentile:	71.4%
Dividend Yield:	0.5%	5 Year Price Target	\$79	Valuation Percentile:	1.1%
Dividend Risk Score:	A	Retirement Suitability Score:	C	Total Return Percentile:	0.8%

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 \$10 billion. The company has increased its dividend for 25 consecutive years, which qualifies it to be a Dividend Champion.

West Pharmaceutical Services reported its third quarter earnings results on October 24. The company reported that its revenues totaled \$456 million during the quarter, which represents a revenue growth rate of 5.7% compared to the prior year's quarter. West Pharmaceutical Services' revenues were slightly higher than what the analyst community had expected. Revenues were negatively impacted by adverse currency rate movements. Adjusted for that, West Pharmaceutical Services' organic revenues were up by a strong 7.9% year over year.

West Pharmaceutical Services generated adjusted earnings-per-share of \$0.79 during the third quarter, which represents an increase of 4% compared to the prior year's third quarter earnings-per-share of \$0.76. West Pharmaceutical Services raised its revenue guidance to ~\$1.82 billion for 2019, while the earnings-per-share forecast has been lifted as well, to a new range of \$3.10 - \$3.15. We have adjusted our estimates accordingly.

Growth on a Per-Share Basis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
EPS	\$1.06	\$1.05	\$1.17	\$1.38	\$1.57	\$1.75	\$1.30	\$1.91	\$2.78	\$2.81	\$3.13	\$4.39
DPS	\$0.31	\$0.33	\$0.35	\$0.37	\$0.39	\$0.41	\$0.46	\$0.50	\$0.54	\$0.57	\$0.64	\$0.86
Shares¹	66	67	67	67	70	71	72	73	74	74	74	75

West Pharmaceutical grew its earnings-per-share at an attractive pace of 11.4% annually between 2009 and 2018. This included the recovery from the last financial crisis, though, when West Pharmaceutical Services' earnings-per-share growth rate was at an above-average level, during 2010 – 2014. During the last financial crisis, West Pharmaceutical Services' earnings-per-share declined by roughly 15%, which was a solid performance versus most other companies. West Pharmaceutical's earnings-per-share growth has been a bit uneven during the last couple of years.

West Pharmaceutical projects a long-term organic sales growth rate in a range of 6% to 8%. We believe that this could be too optimistic, as West Pharmaceutical's revenues have grown at a slower pace of slightly less than 5% over the last 9 years, which is why we believe that this is a more realistic long-term organic sales growth estimate. West Pharmaceutical Services' organic revenue growth rate during 2018 was also slightly lower than management's revenue growth target range. Thanks to tailwinds for the industry, such as rising healthcare spending, we believe that the company should not have any problems in growing its revenues. Revenue growth will be one source for higher earnings, but a more favorable product mix will positively impact West Pharmaceutical's earnings growth as well. The company seeks to increase its revenues in the Proprietary Products segment, which has significantly higher margins than the Contract-Manufactured Products equivalent. We forecast a long-term earnings-per-share growth rate of 7%.

¹ In Millions

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	17.1	18.1	17.8	17.2	23.7	26.1	43.8	38.1	36.0	34.9	44.7	18.0
Avg. Yld.	1.7%	1.7%	1.7%	1.6%	1.0%	0.9%	0.8%	0.7%	0.6%	0.6%	0.5%	1.1%

West Pharmaceutical Services has never been valued at an especially low valuation throughout the last decade, but in the 2009-2012 time frame, its valuation was at least reasonable, although shares still traded at a premium valuation relative to the broad market. More recently, West Pharmaceutical Services' valuation has risen to a very high level, which is neither justified by the company's earnings growth record during the last couple of years, nor by the company's growth outlook over the coming years. We forecast huge downside potential for the company's share price.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
Payout	29.2%	31.4%	29.9%	26.8%	24.8%	23.4%	35.4%	26.2%	19.4%	20.3%	20.4%	19.5%

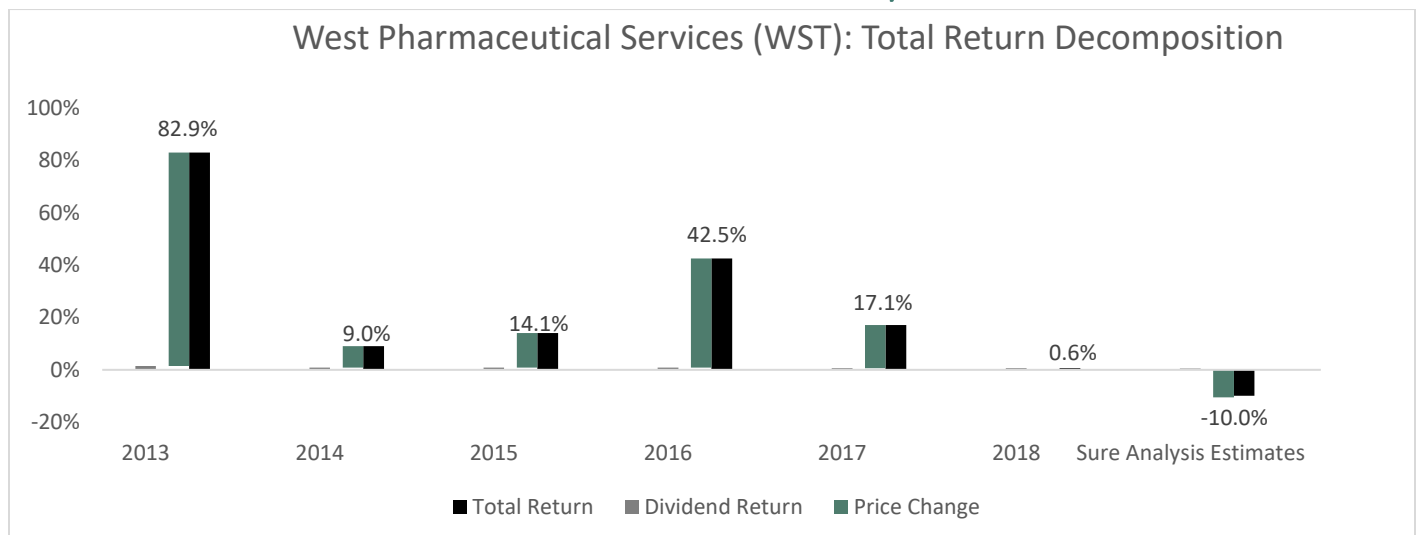
West Pharmaceutical Services' dividend payout ratio has never been high – the company has paid out less than one third of its net profits in the form of dividends during each year of the last decade. Coupled with the fact that the company continued to raise its dividend during the last financial crisis, the payout appears to be very safe. The yield is, however, so low that the stock is still uninteresting for income investors.

West Pharmaceutical is not active in a cyclical industry, as demand for medical items and pharmacologic products is not dependent upon economic conditions. This explains why West Pharmaceutical was not impacted by the last financial crisis to a large degree, showcased by the fact that earnings-per-share declined by just 15% peak-to-trough.

Final Thoughts & Recommendation

West Pharmaceutical Services is active in an industry that is poised to generate solid growth rates over the coming years, and which is also largely invulnerable to recessions. West Pharmaceutical Services has a solid dividend growth track record. We still do not think that the company is attractive for income investors due to the very low dividend yield. Due to an almost absurdly high valuation, West Pharmaceutical Services earns a strong sell recommendation from us at the current price, although we would like the company around fair value.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Revenue	1055.7	1104.7	1192.3	1266.4	1368.4	1421.4	1399.8	1509.1	1599.1	1717.4
Gross Profit	303.6	318.1	339.3	387.7	434.7	447.8	455.8	501.1	512.6	545.4
Gross Margin	28.8%	28.8%	28.5%	30.6%	31.8%	31.5%	32.6%	33.2%	32.1%	31.8%
SG&A Exp.	177.7	187.7	191.1	218.1	0	0	61.3	2.1	0	262.9
D&A Exp.	68.1	73.2	75.7	76.9	85.2	90	89.9	90.7	96.7	104.4
Operating Profit	106	106.5	119.1	142.9	398.8	411.7	362.7	468	480.2	240.3
Op. Margin	10.0%	9.6%	10.0%	11.3%	29.1%	29.0%	25.9%	31.0%	30.0%	14.0%
Net Profit	72.6	65.3	75.5	80.7	112.3	127.1	95.6	143.6	150.7	206.9
Net Margin	6.9%	5.9%	6.3%	6.4%	8.2%	8.9%	6.8%	9.5%	9.4%	12.0%
Free Cash Flow	29.9	64.5	33.9	55.4	64.7	70.8	80.8	49.2	132.5	288.6
Income Tax	13.5	13.6	23.5	32.7	40.2	47.2	26.3	54.4	80.9	41.4

Balance Sheet Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Total Assets	1271	1294.3	1399.1	1564	1671.6	1669.7	1695.1	1716.7	1862.8	337.4
Cash & Equivalents	83.1	110.2	91.8	161.9	230	255.3	274.6	203	235.9	337.4
Accounts Receivable	138.7	126.4	147.2	175	185.7	179	181.4	200.5	253.2	N/A
Inventories	129.2	147	151.8	162.2	176.9	181.5	181.1	199.3	215.2	N/A
Goodwill & Int. Ass.	169.8	167.6	163.5	163.1	162.5	150.6	142.2	126.3	129.4	N/A
Total Liabilities	691.9	668.6	744.2	835.1	765.2	712.8	671.2	599.2	582.9	-1059
Accounts Payable	68.4	63.2	89.8	102.9	108	103.1	119.8	122	138.1	N/A
Long-Term Debt	379.6	358.4	349.4	411.5	373.5	335.5	298.2	228.6	197	0
Shareholder's Equity	579.1	625.7	654.9	728.9	906.4	956.9	1023.9	1117.5	1279.9	1396.3
D/E Ratio	0.66	0.57	0.53	0.56	0.41	0.35	0.29	0.20	0.15	0.00

Profitability & Per Share Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Return on Assets	6.0%	5.1%	5.6%	5.4%	6.9%	7.6%	5.7%	8.4%	8.4%	18.8%
Return on Equity	13.6%	10.8%	11.8%	11.7%	13.7%	13.6%	9.7%	13.4%	12.6%	15.5%
ROIC	7.9%	6.7%	7.6%	7.5%	9.3%	9.9%	7.3%	10.8%	10.7%	14.4%
Shares Out.	66	67	67	67	70	71	72	73	74	74
Revenue/Share	14.54	15.05	16.11	17.64	19.17	19.52	18.97	20.12	21.10	22.78
FCF/Share	0.41	0.88	0.46	0.77	0.91	0.97	1.09	0.66	1.75	3.83

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

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