



Freeport-McMoRan Inc. (FCX)

Updated July 27th, 2020 by Josh Arnold

Key Metrics

Current Price:	\$13	5 Year CAGR Estimate:	-0.7%	Market Cap:	\$19.1 B
Fair Value Price:	\$8.00	5 Year Growth Estimate:	8.5%	Ex-Dividend Date:	N/A
% Fair Value:	164%	5 Year Valuation Multiple Estimate:	-9.4%	Dividend Payment Date:	N/A
Dividend Yield:	0.4%	5 Year Price Target	\$12	Years Of Dividend Growth:	0
Dividend Risk Score:	N/A	Retirement Suitability Score:	N/A	Last Dividend Increase:	N/A

Overview & Current Events

Freeport-McMoRan is a leading global mining company that is headquartered in Arizona. The company operates large, long-lived, geographically diverse mines with significant reserves of copper, gold, and molybdenum. The geographical footprint includes Indonesia, North America, South America, and Africa. It produces roughly four billion pounds of copper annually, and more than 2 million ounces of gold. Freeport-McMoRan should generate nearly \$13 billion in revenue this year, and has a market capitalization of \$19.1 billion.

Freeport reported second quarter earnings on July 23rd, with revenue coming in slightly weaker than expectations, but earnings beating consensus. Total revenue was just over \$3 billion, down more than -14% year-over-year.

Copper production was off -1.2% to 767 million pounds, while gold production soared 19% to 191 thousand ounces. Average realized prices were \$2.55 per pound for copper and \$1,749 per ounce for gold. Copper sales volume fell -5.9% year-over-year to 759 million pounds, so the company built inventory slightly, while gold sales declined -2.6% to 184 thousand ounces.

The company saw a strong reduction of -22% in operating costs as it took drastic measures to try and cut costs in unprecedented operating conditions. It did cut full-year volume forecasts for copper – from 3.5 billion pounds to 3.15 billion pounds – while maintaining its forecast of 800 thousand ounces for gold.

The company also forecast net cash costs of \$1.53 per pound for copper, slightly lower than previous guidance. The guidance for 2021, however, is just \$1.20 per pound, which should meaningfully reflate margins into next year.

We've boosted our estimate of earnings-per-share for this year from a small loss to a profit of 15 cents. We see higher gold and copper prices as helping Freeport get earnings back to where they were, and we will use an adjusted earnings power value of \$1 per share for our valuation and fair value calculations, to account for unusual conditions in 2020.

Growth on a Per-Share Basis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
EPS	\$4.57	\$4.78	\$3.19	\$2.64	-\$1.26	-\$11.31	-\$3.16	\$1.25	\$1.78	-\$0.17	\$0.15	\$1.50
DPS	\$0.63	\$1.00	\$1.19	\$1.25	\$1.25	\$0.46	---	---	\$0.20	\$0.20	\$0.05	\$0.20
Shares¹	945	948	949	1038	1039	1246	1445	1448	1449	1451	1450	1450

We expect Freeport to report a very small profit for this year, but our assumptions for future growth include a return to some state of normalcy in 2021 and beyond. Given this, we've assigned Freeport a forward growth rate of 8.5% on what is a low base. Since earnings are expected to be very small this year, we're using an earnings power estimate of \$1.00 per share for our valuation and fair value metric calculations. This is the amount we'd expect Freeport to earn on a normalized basis, rather than what should be temporarily depressed earnings from the COVID-19 crisis. This produces estimated 2025 earnings of \$1.50 per share.

Freeport's future growth will be heavily dependent upon copper pricing, as that is where it derives most of its revenue from. With copper volume being highly dependent upon global economic activity, Freeport will suffer until the current

¹ Share count in millions

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global recession has passed. However, once there is a return to normal activity, copper demand should pick up and with it, pricing. With the company saving money on every line item of cost, margins should reflate rather quickly. Still, we note that as with any commodity company, Freeport's revenue and margins have significant volatility from year to year, so this forecast has significant upside and downside risk due to factors outside of Freeport's control.

Valuation Analysis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	Now	2025
Avg. P/E	8.9	10.0	11.8	12.4	16.4	---	45.6	11.9	10.3	---	13.1	8.0
Avg. Yld.	1.5%	2.1%	3.2%	3.8%	3.8%	3.0%	---	---	1.3%	1.8%	0.4%	1.7%

Perhaps unsurprisingly, Freeport's price-to-earnings multiple has been quite erratic in the past decade. The company's wild swings in earnings have produced some very large and very small P/E multiples in the past, and shares trade for 13.1 times our earnings power estimate after a huge rally. We assign fair value at 8 times earnings given this volatility, and the fact that commodity companies tend to see lower valuations during times of economic stress. We don't see Freeport with a sustainable low double-digit P/E multiple in the foreseeable future due to this.

The yield is just 0.4% for 2020 given the one dividend payment, but we expect the company to reinstate its payout in the future, as it has at other times in the past, good for a 1.7% estimated yield for 2025.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
Payout	12%	21%	37%	48%	64%	---	---	---	10%	---	5%	13%

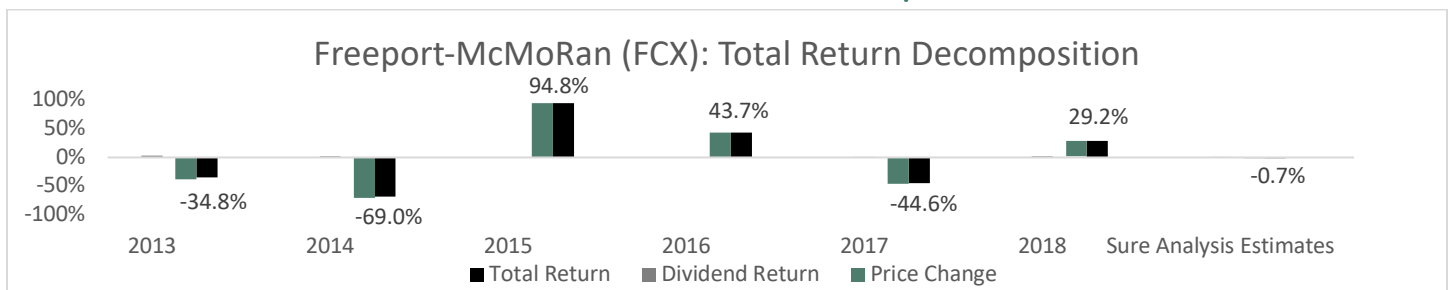
We see the payout ratio as manageable in the coming years as the company has ceased paying dividends until earnings recover - consistent with other periods of weak earnings - as Freeport will only reinstate when it is safe to do so.

The company's competitive advantage - if it has one - is in its scale. Freeport produces enormous volumes of copper and can therefore generally achieve lower product costs. However, it is still a mining company and advantages are difficult to come by. The company also suffers greatly during periods of economic weakness due to its exposure to copper, and it has more than \$8 billion in debt on its balance sheet. It pays more than \$500 million annually just in debt servicing costs, so its prospects for getting out of debt are quite dim given unpredictable earnings. We see the balance sheet as a significant negative for Freeport and note that it greatly increases risks for shareholders.

Final Thoughts & Recommendation

We see Freeport-McMoRan as a high-risk way to enter the commodity space. The company's exposure to copper is very profitable during times of strong economic activity, but devastating in weak periods, like we're seeing today. We see Freeport producing -0.7% annual returns from here. As a result, we rate the stock a sell given the significant uncertainty surrounding the recovery, and its highly leveraged balance sheet.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Revenue	18982	20880	18010	20921	20001	14607	14830	16403	18628	14402
Gross Profit	9611	9960	6449	6284	1507	-12808	-2704	4423	5183	1297
Gross Margin	50.6%	47.7%	35.8%	30.0%	7.5%	-87.7%	-18.2%	27.0%	27.8%	9.0%
SG&A Exp.	381	415	431	657	580	558	597	477	443	414
Operating Profit	9068	9140	5755	5351	702	-13551	-3378	3609	4546	674
Operating Margin	47.8%	43.8%	32.0%	25.6%	3.5%	-92.8%	-22.8%	22.0%	24.4%	4.7%
Net Profit	4336	4560	3041	2680	-1268	-12195	-4315	1817	2602	-239
Net Margin	22.8%	21.8%	16.9%	12.8%	-6.3%	-83.5%	-29.1%	11.1%	14.0%	-1.7%
Free Cash Flow	4861	4086	280	853	-1584	-3133	924	3256	1892	-1170
Income Tax	2983	3087	1510	1475	225	-1951	371	883	991	510

Balance Sheet Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Total Assets	29386	32070	35440	63473	58674	46577	37317	37302	42216	40809
Cash & Equivalents	3738	4822	3705	1985	464	177	4245	4526	4217	2020
Accounts Receivable	2327	892	927	1728	953	645	1126	1322	829	741
Inventories	3434	3869	4576	5018	5361	4075	3642	4149	4503	4073
Goodwill & Int. Ass.	328	325	334	2296	334	316	305	307	398	402
Total Liabilities	14826	13517	14129	38242	36200	34533	28060	26006	24324	23361
Accounts Payable	1272	1353	1568	2144	2439	2251	1540	1546	1661	1654
Long-Term Debt	4755	3537	3527	20706	18849	20324	16027	13229	11141	9826
Shareholder's Equity	12504	15642	17543	20934	18287	7828	6051	7977	9798	9298
D/E Ratio	0.38	0.23	0.20	0.99	1.03	2.60	2.65	1.66	1.14	1.06

Profitability & Per Share Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Return on Assets	15.7%	14.8%	9.0%	5.4%	-2.1%	-23.2%	-10.3%	4.9%	6.5%	-0.6%
Return on Equity	46.3%	32.4%	18.3%	13.9%	-6.5%	-93.4%	-62.2%	25.9%	29.3%	-2.5%
ROIC	23.8%	22.0%	13.0%	7.6%	-2.9%	-33.1%	-15.0%	7.3%	9.7%	-0.8%
Shares Out.	945	948	949	1038	1039	1246	1445	1448	1449	1451
Revenue/Share	20.00	21.86	18.88	20.80	19.25	13.50	11.25	11.28	12.78	9.93
FCF/Share	5.12	4.28	0.29	0.85	(1.52)	(2.90)	0.70	2.24	1.30	(0.81)

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

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