



CVS Health Corporation (CVS)

Updated August 5th, 2020 by Nathan Parsh

Key Metrics

Current Price:	\$65	5 Year CAGR Estimate:	11.7%	Market Cap:	\$84.8 billion
Fair Value Price:	\$79	5 Year Growth Estimate:	5.0%	Ex-Dividend Date:	10/23/2020 ¹
% Fair Value:	82%	5 Year Valuation Multiple Estimate:	4.1%	Dividend Payment Date:	11/3/2020 ²
Dividend Yield:	3.1%	5 Year Price Target	\$101	Years Of Dividend Growth:	0
Dividend Risk Score:	B	Retirement Suitability Score:	B	Last Dividend Increase:	17.6% (2017)

Overview & Current Events

CVS Health Corporation is an integrated healthcare services provider that operates a pharmaceutical services business, along with the country's largest chain of pharmacies. The company operates more than 9,900 retail locations, 1,100 medical clinics, and services more than 102 million plan members. CVS Health Corporation generates annual revenues of about \$265 billion. On 11/11/18, 2018, CVS Health Corporation completed its acquisition of Aetna. The company expects \$750 million of cost synergies in 2020.

CVS Health Corporation released earnings results for the second quarter on 8/4/2020. Revenue improved 3% to \$65.3 billion, \$1.1 billion above estimates. Adjusted earnings-per-share increased \$0.75, or 40%, to \$2.64, which was \$0.72 higher than expected.

The COVID-19 pandemic added an estimated \$0.70 to \$0.80 to adjusted earnings-per-share and \$1.8 to \$2.1 billion to revenue results during the quarter. Pharmacy Services revenues inched higher by 0.1%. Specialty pharmacy sales and brand inflation were nearly offset by price compression and commercial membership losses. Retail/LTC revenues increased 1% due to pharmacy drug mix and 0.6% growth in retail pharmacy prescription volumes. Reimbursement pressure, generic introductions and a 1.1% decrease in prescriptions filled were all headwinds during the quarter. Front of store sales declined 4.5%, which was attributed to less customer traffic due to shelter-in-place directives, but was partially offset with higher average basket size. Retail pharmacy script share did increase nearly 40 basis points to 26.9%. Same store sales improved 2.4% from the previous year, but were higher by 7.1% in June alone. Health Care Benefit sales increased 6.1% due to government product memberships, which were up more than 22%. Medical memberships overall increased 3.3% to 23.6 million members. CVS Health Corp provided a business update for July as well. Same store sales have increased 4.6%, with growth in all areas. Prescription volumes were higher by more than 5% for the month with Pharmacy and front of store sales growing 4.5% and 4.7%, respectively. The company ended the quarter with \$7 billion in cash and investments and \$6 billion in borrowing capacity. CVS Health Corp expects adjusted earnings-per-share of \$7.14 to \$7.27 for the year, up from \$7.04 to \$7.17 previously. Cash flow from operations is now expected to be between \$11 billion and \$11.5 billion, up from \$10.5 billion to \$11 billion previously.

Growth on a Per-Share Basis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
EPS	\$2.69	\$2.80	\$3.43	\$4.00	\$4.51	\$5.16	\$5.84	\$5.90	\$7.08	\$7.08	\$7.21	\$9.20
DPS	\$0.35	\$0.50	\$0.65	\$0.90	\$1.10	\$1.40	\$1.70	\$2.00	\$2.00	\$2.00	\$2.00	\$2.55
Shares³	1363	1298	1231	1180	1140	1101	1061	1014	1126	1301	1314	1250

CVS Health Corporation's historical growth has been remarkable. The company has compounded its earnings and dividends at annualized rate of 10.3% and 25.4%, respectively, over the last decade. The acquisition of Aetna, which had nearly 40 million members at the time of purchase, offered CVS Health Corporation a significant increase in the number

¹ Estimated ex-dividend date

² Estimated date

³ In millions of shares

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of potential customers. It is also a positive that the company was able to pay down a sizeable amount of debt in recent quarters. We are forecasting 5% earnings-per-share growth for CVS over the medium term due to revenue increases and cost synergies from the Aetna transaction. Dividend growth during this time period is likely to underwhelm as CVS has frozen its dividend, instead focusing on reducing debt.

Valuation Analysis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	Now	2025
Avg. P/E	12.1	12.9	13.2	14.7	17.4	19.7	15.9	13.2	11.1	10.5	9.0	11.0
Avg. Yld.	1.1%	1.4%	1.4%	1.5%	1.4%	1.4%	1.8%	2.6%	2.9%	2.7%	3.1%	2.5%

Shares of CVS Health Corporation have increased \$3, or 4.8%, since our 5/6/2020 report. Using the midpoint of company's updated guidance for 2020, the stock is trading at a price-to-earnings ratio of 9.0, which compares favorably to its 10-year average of 14.6. We maintain our 2025 target P/E of 11 due to a projected slight increase in earnings for 2020. Our target P/E might be increased if CVS Health Corporation continues to show strong growth rates. Still, if our current target valuation is achieved, investors would see an additional 4.1% added to annual returns over this time.

Safety, Quality, Competitive Advantage, & Recession Resiliency

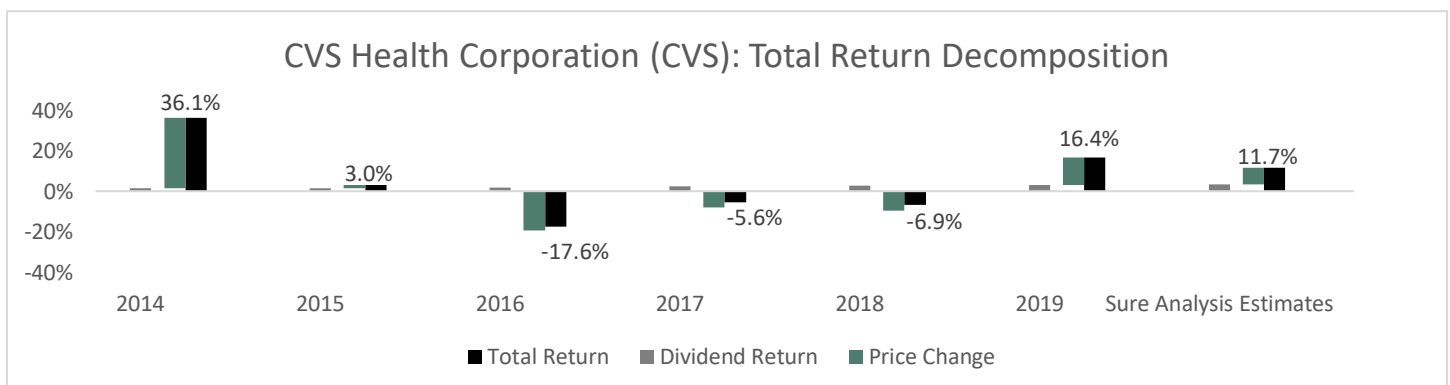
Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
Payout	13%	18%	19%	23%	24%	27%	29%	34%	28%	28%	28%	28%

CVS Health Corporation's most compelling competitive advantage is its entrenched position in the pharmaceutical retail industry. The industry is highly regulated, which makes it difficult for new competitors to enter into the industry and gain market share. In addition, the company is one of the largest pharmacies in the United States (along with Walgreens Boots Alliance), which allows it to capture economies of scale and pressure its suppliers into delivering better prices. CVS Health Corp controlled 26.9% of the retail pharmacy market share as of the end of the second quarter of 2020.

Final Thoughts & Recommendation

Following second quarter earnings results, CVS Health Corporation is projected to offer an annual return of 11.7% through 2025, down from 12.4% previously. While certain areas of the business were impacted by the COVID-19 pandemic, CVS Health Corporation saw an overall benefit during the quarter. The company has also seen fairly strong growth rates in June and July as stay-at-home directives were eased. This shows that demand for products and pharmacy services remains high among consumers. The company also increased its script market share once again. We maintain our buy rating on CVS Health Corporation due to business performance and raise our 2025 price target \$1 to \$101 due to revised EPS estimates.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Revenue (\$B)	95,778	107,080	123,120	126,761	139,367	153,290	177,546	184,786	194,579	256,776
Gross Profit	20,219	20,562	22,488	23,783	25,367	26,528	28,834	28,528	31,538	45,528
Gross Margin	21.1%	19.2%	18.3%	18.8%	18.2%	17.3%	16.2%	15.4%	16.2%	17.7%
D&A Exp.	1,469	1,568	1,753	1,870	1,931	2,092	2,475	2,479	2,718	4,371
Operating Profit	6,137	6,331	7,210	8,037	8,799	9,475	10,386	9,719	10,170	11,987
Op. Margin	6.4%	5.9%	5.9%	6.3%	6.3%	6.2%	5.8%	5.3%	5.2%	4.7%
Net Profit	3,427	3,462	3,864	4,592	4,644	5,237	5,317	6,622	(594)	6,634
Net Margin	3.6%	3.2%	3.1%	3.6%	3.3%	3.4%	3.0%	3.6%	-0.3%	2.6%
Free Cash Flow	2,774	3,984	4,641	3,799	6,001	6,172	7,917	6,089	6,828	10,391
Income Tax	2,179	2,258	2,436	2,928	3,033	3,386	3,317	1,637	2,002	2,366

Balance Sheet Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Total Assets	62,169	64,543	66,221	71,526	74,187	92,437	94,462	95,131	196,456	222,449
Cash & Equivalents	1,427	1,413	1,375	4,089	2,481	2,459	3,371	1,696	4,059	5,683
Acc. Receivable	4,925	6,047	6,479	8,729	9,687	11,888	12,164	7,895	6,896	19,617
Inventories	10,695	10,046	11,032	11,045	11,930	14,001	14,760	15,296	16,450	17,516
Goodwill & Int.	35,453	36,327	36,148	36,071	37,916	51,984	51,760	52,081	115,202	112,870
Total Liabilities	24,435	26,492	28,568	33,588	36,224	55,234	57,628	57,436	137,913	158,279
Accounts Payable	4,026	4,370	5,070	5,548	6,547	7,490	7,946	8,863	8,925	10,492
Long-Term Debt	10,057	10,014	9,828	13,402	12,890	27,464	27,531	27,002	73,429	68,480
Total Equity	37,700	38,051	37,653	37,938	37,958	37,196	36,830	37,691	58,225	63,864
D/E Ratio	0.27	0.26	0.26	0.35	0.34	0.74	0.75	0.72	1.26	1.07

Profitability & Per Share Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Return on Assets	5.5%	5.5%	5.9%	6.7%	6.4%	6.3%	5.7%	7.0%	-0.4%	3.2%
Return on Equity	9.3%	9.1%	10.2%	12.1%	12.2%	13.9%	14.4%	17.8%	-1.2%	10.9%
ROIC	7.2%	7.2%	8.1%	9.3%	9.1%	9.1%	8.2%	10.3%	-0.6%	5.0%
Shares Out.	1363	1298	1231	1180	1140	1101	1061	1014	1126	1301
Revenue/Share	69.56	79.50	96.19	103.39	119.22	136.14	164.55	180.46	186.38	196.76
FCF/Share	2.01	2.96	3.63	3.10	5.13	5.48	7.34	5.95	6.54	7.96

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

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