

Philip Morris International Inc. (PM)

Updated October 20th, 2020 by Eli Inkrot

Key Metrics

Current Price:	\$77	5 Year CAGR Estimate:	9.0%	Market Cap:	\$120 B
Fair Value Price:	\$76	5 Year Growth Estimate:	4.0%	Ex-Dividend Date¹:	12/18/20
% Fair Value:	101%	5 Year Valuation Multiple Estimate:	-0.3%	Dividend Payment Date¹:	01/10/20
Dividend Yield:	6.2%	5 Year Price Target	\$93	Years Of Dividend Growth:	13
Dividend Risk Score:	C	Retirement Suitability Score:	B	Last Dividend Increase:	2.6%

Overview & Current Events

Philip Morris International is a tobacco company that came into being when its parent company Altria (MO) spun off its international operations. Philip Morris sells cigarettes under the Marlboro brand, among others, internationally. Its sister company Altria sells the Marlboro brand (among others) in the U.S. Philip Morris has a \$120 billion market cap.

On October 20th, 2020 Philip Morris reported Q3 2020 results for the period ending September 30th, 2020. For the quarter the company generated net revenue of \$7.45 billion, which was down -2.6% as reported and down -1.5% on an organic basis. Shipment volume was down -7.6% collectively, with cigarette shipment volume down -9.8% and heated tobacco, a much smaller portion of the business, up 18.7%. Adjusted earnings-per-share equaled \$1.42, down from \$1.43 in the year ago period.

In the beginning of the year Philip Morris provided a 2020 full-year forecast of \$5.50 or greater in earnings-per-share and then withdrew this guidance due to the uncertainty surrounding the COVID-19 pandemic. Last quarter the company reinstated guidance of \$4.92 to \$5.07. This has since been updated to \$5.05 to \$5.10 in adjusted EPS this year.

Growth on a Per-Share Basis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
EPS	\$3.92	\$4.85	\$5.17	\$5.26	\$4.76	\$4.42	\$4.48	\$4.72	\$5.10	\$5.19	\$5.07	\$6.17
DPS	\$2.44	\$2.84	\$3.24	\$3.58	\$3.88	\$4.04	\$4.12	\$4.22	\$4.49	\$4.62	\$4.80	\$5.54
Shares²	1,802	1,726	1,654	1,589	1,547	1,549	1,551	1,553	1,554	1,555	1,560	1,500

When the spin-off of Philip Morris was announced, the market assumed that Altria, the U.S. business, would be the low-growth company, and that Philip Morris International, the non-U.S. business, would be the high-growth company. It looked like this would come true through 2013, as Philip Morris recorded near double-digit earnings-per-share growth through the first five years of its existence. This changed in the following years, as Philip Morris' profits declined and stagnated. Even during 2019, earnings-per-share remained below the peak set in 2013. Currency rates are a major factor for Philip Morris' profitability, as all of the company's revenues are generated outside of the US.

Philip Morris' weak profit growth over the last couple of years was partially due to the company's investments into the iQOS/Heatsticks technology. The investment in the development of this device and the manufacturing equipment needed to produce this reduced-risk product on a massive scale were costly, but Philip Morris is hoping that those investments will pay off in the long run. Ramp-up of iQOS in international markets has taken hold and the product is one of the reasons why Philip Morris has been able to stabilize its business.

The COVID-19 pandemic is a concern for the global economy, but Philip Morris is in an industry with inelastic demand. As such, despite declining shipment volumes in its cigarette business, the company has fortitude and even pricing power in lesser times. Still, given the reduced 2020 forecast, it's clear that the business will be affected to some degree. Taking these items collectively we are anticipating growth of 4% per annum over the intermediate term using the midpoint of recent guidance as a beginning baseline.

¹ Estimate

² In millions.

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Valuation Analysis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	Now	2025
Avg. P/E	13.2	13.8	16.7	17.0	17.7	18.8	21.5	23.4	17.3	15.7	15.2	15.0
Avg. Yld.	4.7%	4.2%	3.8%	4.0%	4.6%	4.9%	4.3%	3.8%	5.1%	5.7%	6.2%	6.0%

Shares of Philip Morris traded at an elevated valuation in the 2015 through 2017 stretch, but otherwise a mid-teens multiple has been fairly typical. At the current mark of 15.2 times anticipated earnings, we believe shares are more or less fairly valued. Moreover, with the elevated and consistent payout ratio, Philip Morris' dividend ought to add meaningfully to shareholder returns.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
Payout	62%	59%	63%	68%	82%	91%	92%	89%	88%	89%	95%	90%

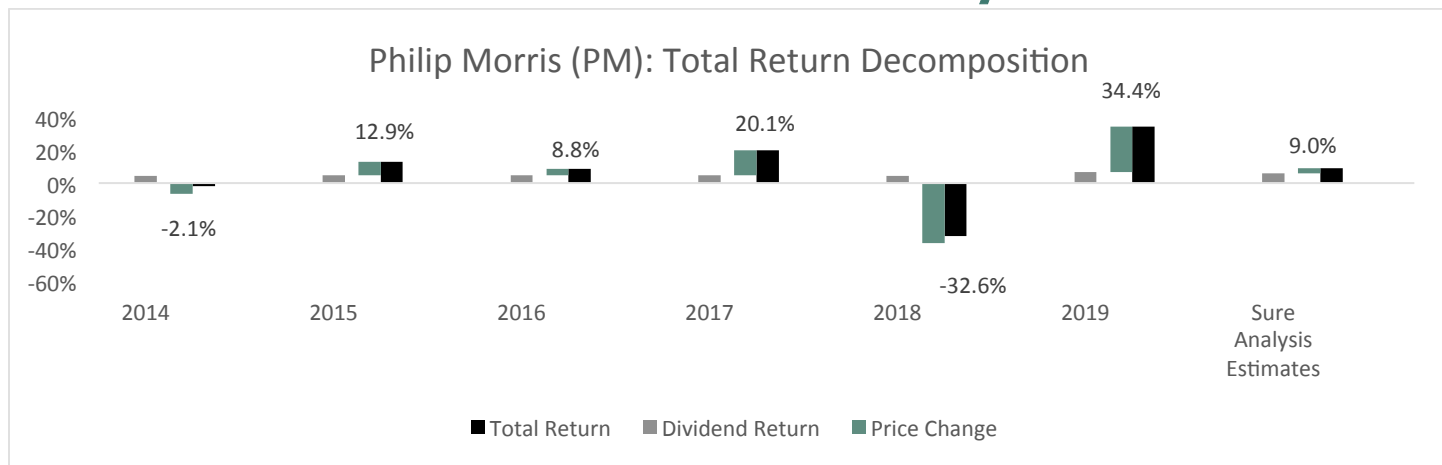
Philip Morris' dividend payout ratio has never been especially low, and the ratio increased further during the last decade. At the peak, Philip Morris has paid out more than 90% of its net profits to its owners and this year could approach 100% depending on business conditions. Due to strong cash generation, low capex requirements and the stability of Philip Morris' business model during recessions the dividend still appears to be relatively well-covered.

Philip Morris has one of the most valuable cigarette brands in the world, Marlboro, and is a leader in the reduced-risk product segment with IQOS. At the same time, the company's massive scale allows for tremendous cost advantages. This means that Philip Morris is generally a low-risk business, with regulation being the exception. Smoking bans can affect the company's results, although Philip Morris is safer in this regard than many other tobacco companies due to its geographic diversification.

Final Thoughts & Recommendation

Shares are up 4% since our last report, while earnings expectations have improved moderately. Philip Morris is an international tobacco giant that is heavily impacted by currency rate movements. The payout ratio is elevated, but thus far the company has proven more than capable of sustaining its lofty dividend. However, both growth expectations and the valuation are average. Total return potential comes in at 9% per annum, driven by a 4% growth rate and a 6.2% starting dividend yield. While the security is suitable for income investors, we continue to rate shares as a hold.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Revenue	27208	31097	31377	31217	29767	26794	26685	28748	29625	29805
Gross Profit	17495	20419	21004	20807	19331	17429	17294	18316	18867	19292
Gross Margin	64.3%	65.7%	66.9%	66.7%	64.9%	65.0%	64.8%	63.7%	63.7%	64.7%
SG&A Exp.	6160	6870	6961	6890	7001	6656	6405	6725	7449	8784
D&A Exp.	932	993	898	882	889	754	743	875	989	964
Operating Profit	11247	13451	13946	13824	12237	10691	10815	11503	11336	10442
Op. Margin	41.3%	43.3%	44.4%	44.3%	41.1%	39.9%	40.5%	40.0%	38.3%	35.0%
Net Profit	7259	8591	8800	8576	7493	6873	6967	6035	7911	7185
Net Margin	26.7%	27.6%	28.0%	27.5%	25.2%	25.7%	26.1%	21.0%	26.7%	24.1%
Free Cash Flow	8724	9632	8365	8935	6586	6905	6905	7364	8042	9238
Income Tax	2826	3653	3833	3670	3097	2688	2768	4307	2445	2293

Balance Sheet Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Total Assets	35050	35488	37670	38168	35187	33956	36851	42968	39801	42875
Cash & Equivalents	1703	2550	2983	2154	1682	3417	4239	8447	6593	6861
Acc. Receivable	3065	3201	3589	3853	4004	2778	3499	3194	2950	3080
Inventories	8317	8120	8949	9846	8592	8473	9017	8806	8804	9235
Goodwill & Int.	14034	13625	13519	12086	11373	10038	9794	10098	9467	7971
Total Liabilities	29929	34937	40824	44442	46390	45432	47751	53198	50540	52474
Accounts Payable	835	1031	1103	1274	1242	1289	1666	2242	2068	2299
Long-Term Debt	16502	18545	22839	27678	29455	28480	29067	34339	31759	31045
Total Equity	3506	229	-3476	-7766	-12.6B	-13.2B	-12.7B	-12.1B	-12.5B	-11.6B
D/E Ratio	4.71	80.98	-6.57	-3.56	-2.33	-2.15	-2.29	-2.84	-2.55	-2.68

Profitability & Per Share Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Return on Assets	20.9%	24.4%	24.1%	22.6%	20.4%	19.9%	19.7%	15.1%	19.1%	17.4%
Return on Equity	157%	460%	-542%	-153%	-73.5%	-53.1%	-53.7%	-48.7%	-64.5%	
ROIC	33.6%	42.2%	45.4%	41.7%	37.8%	39.0%	39.6%	28.6%	35.1%	33.8%
Shares Out.	1842	1762	1692	1622	1566	1549	1551	1553	1555	1555
Revenue/Share	14.77	17.65	18.54	19.25	19.01	17.30	17.21	18.51	19.05	19.15
FCF/Share	4.74	5.47	4.94	5.51	4.21	4.46	4.45	4.74	5.17	5.94

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

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