Apple Inc. (AAPL)

Updated October 31st, 2020 by Eli Inkrot

Key Metrics

Current Price:	$109	**5 Year CAGR Estimate:**	-0.2%	**Market Cap:**	$1.9 T
Fair Value Price:	$66	**5 Year Growth Estimate:**	9.0%	**Ex-Dividend Date:**	11/06/20
% Fair Value:	164%	**5 Year Valuation Multiple Estimate:**	-9.4%	**Dividend Payment Date:**	11/12/20
Dividend Yield:	0.8%	**5 Year Price Target**	$102	**Years Of Dividend Growth:**	8
Dividend Risk Score:	A	**Retirement Suitability Score:**	D	**Last Dividend Increase:**	6.5%

Overview & Current Events

Apple is a technology company that designs, manufactures and sells products such as smartphones, personal computers and portable digital music players. Apple also has a thriving services business that sells music, apps, and subscriptions. The company was founded in 1976, is headquartered in Cupertino, CA and is valued at $1.9 trillion.

On August 31st, 2020 Apple completed a 4-for-1 stock split; which we have adjusted for in this report.

On October 29th, Apple reported Q4 and fiscal year 2020 results for the period ending September 26th, 2020 (Apple's fiscal year ends the last Saturday in September). For the quarter Apple generated revenue of $64.7 billion, representing a 1.0% increase compared to Q4 2019. Product sales were down 2.7%, as gains in Mac, iPad and Wearables were more than offset by a 20.7% decline in iPhone sales, which made up about 41% of total sales. Service sales increased 16.3% and made up 22% of all sales in the quarter. Net income equaled $12.67 billion, a 7.4% decline, while earnings-per-share equaled $0.73 versus $0.76 prior. The slower decline was attributable to a materially lower share count.

For the year Apple generated revenue of $274.5 billion, representing a 5.5% increase compared to fiscal year 2019. Product sales were up 3.2%, as gains in Mac, iPad and Wearables offset by a 3.2% decline in iPhone sales, which fell from 55% of total sales in 2019 to 50% in 2020. Service sales increased 16.2% year-over-year and went from 18% of total sales in 2019 to 20% in 2020. Net income equaled $57.4 billion, representing a 3.9% increase, while earnings-per-share equaled $3.28 compared to $2.97 in 2019, a 10.4% increase due to a much lower share count.

Growth on a Per-Share Basis

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
EPS	$0.99	$1.58	$1.42	$1.61	$2.31	$2.08	$2.30	$2.98	$2.97	$3.28	***$3.90***	***$6.00***
DPS	---	$0.09	$0.41	$0.45	$0.50	$0.55	$0.60	$0.68	$0.75	$0.80	***$0.82***	***$1.50***
Shares[1]	26,020	26,298	25,178	23,465	22,315	21,345	20,505	19,020	17,773	17,528	***17,000***	***15,000***

In the 2012 through 2020 stretch, Apple has grown its earnings-per-share by 9.6% annually. Naturally this is an attractive growth rate, although it is substantially lower than the growth rates Apple produced in the years prior to 2012. The bigger the bottom line gets, the harder it becomes to grow at a very high pace.

Going forward Apple's earnings growth will be driven by several factors. One of these is the ongoing cycle of iPhone releases, despite the significant decline last year. In the long run Apple should be able to grow its iPhone sales, albeit in an irregular fashion. Moreover, in emerging countries where consumers have rising disposable incomes, Apple should be able to increase the number of smartphones it is selling in the coming years. Increasing the selling prices of its phones could be a tailwind for revenue as well. In addition, Apple's Services unit which consists of iTunes, Apple Music, the App Store, iCloud, Apple Pay, etc., has recorded a significant revenue growth rate during the last couple of quarters. Services revenues grow substantially faster than other segments and produce high-margin recurring revenues.

Another factor that has played a role in the past is the shrinking share count. Due to its immense cash flows Apple is able to repurchase hundreds of millions of shares. Apple should continue to lower its share count, further boosting EPS.

[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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The ongoing COVID-19 pandemic does not appear to be materially impairing the company's underlying earnings power. Over the intermediate term we believe Apple could generate 9% annual growth from its strong "cash cow" legacy business, growing Services revenue, and a shrinking share count.

Valuation Analysis

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	Now	2026
Avg. P/E	12.4	12.0	12.3	13.0	12.8	12.6	14.9	15.3	16.1	29.2	***27.9***	***17.0***
Avg. Yld.	---	0.5%	2.3%	2.2%	1.7%	2.1%	1.8%	1.5%	1.6%	0.8%	***0.8%***	***1.5%***

In the 2011 through 2016 stretch shares of Apple routinely traded with an average price-to-earnings multiple between 12- and 13-times earnings. In the years since the earnings multiple has expanded tremendously, but the company is not growing significantly faster. With shares now trading at 28 times expected earnings, we believe there is the potential for a significant valuation headwind in the years to come. This view could be too conservative if the valuation remains elevated, but we are not yet ready to make that leap and instead forecast a high-teens multiple. While the dividend yield is not spectacular, it is very well covered with the propensity to grow over time.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
Payout	---	6%	29%	28%	22%	26%	26%	23%	25%	24%	***21%***	***25%***

Apple started paying a dividend in 2012. Since then, the dividend has been increased regularly, but more or less in-line with the company's earnings-per-share growth, which is why the dividend payout ratio has remained in the 20% range. This, coupled with the company's enviable balance sheet, makes Apple's dividend look quite safe.

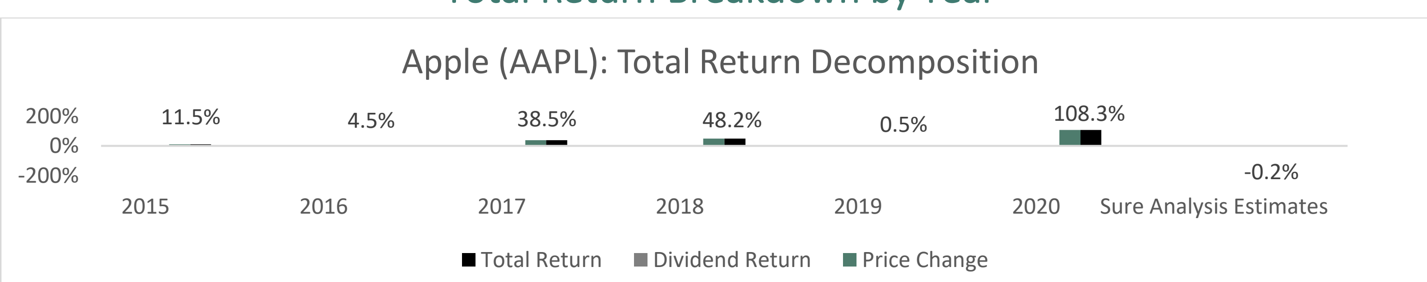
Apple's brand is admired around the globe, and together with Samsung the company basically earns all the profits in the top end smartphone market. In addition, Apple's Services will bring in an increasing stream of recurring revenues. During the last financial crisis Apple's profits rose, but that was during the hyper-growth phase. Since Apple is still highly dependent on sales of relatively high-cost smartphones, a major economic crisis could hurt its profits.

As of the most recent report Apple held $90.9 billion in cash and securities, $143.7 billion in current assets and $323.9 billion in total assets (of which an additional $100.9 billion are non-current securities) against $105.4 billion in current liabilities and $258.5 billion in total liabilities. Apple is in excellent financial shape.

Final Thoughts & Recommendation

Shares are up 6% in the last three months but have more than doubled in the last year. We are enthused on a number of fronts, including an extraordinary business story, a growing Services segment and a balance sheet that provides significant safety. However, in our view, the current valuation remains a major hindrance. We are forecasting -0.2% annual total return potential, stemming from 9% growth and a 0.8% starting yield, offset by a significant valuation headwind. Due to the materially higher valuation shares earn a sell rating.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Revenue ($B)	108.2	156.5	170.91	182.8	233.7	215.64	229.2	265.6	260.2	---
Gross Profit	43818	68662	64304	70537	93626	84263	88186	102B	98392	---
Gross Margin	40.5%	43.9%	37.6%	38.6%	40.1%	39.1%	38.5%	38.3%	37.8%	---
SG&A Exp.	7599	10040	10830	11993	14329	14194	15261	16705	18245	---
D&A Exp.	1814	3277	6757	7946	11257	10505	10157	10903	12547	---
Operating Profit	33790	55241	48999	52503	71230	60024	61344	70898	63930	---
Op. Margin	31.2%	35.3%	28.7%	28.7%	30.5%	27.8%	26.8%	26.7%	24.6%	---
Net Profit	25922	41733	37037	39510	53394	45687	48351	59531	55256	---
Net Margin	23.9%	26.7%	21.7%	21.6%	22.8%	21.2%	21.1%	22.4%	21.2%	---
Free Cash Flow	30077	41454	44590	49900	69778	52276	50803	64121	58896	---
Income Tax	8283	14030	13118	13973	19121	15685	15738	13372	10481	---

Balance Sheet Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Total Assets ($B)	116.37	176.06	207.00	231.84	290.35	321.69	375.32	365.73	338.52	---
Cash & Equivalents	9815	10746	14259	13844	21120	20484	20289	25913	48844	---
Accounts Receivable	5369	10930	13102	17460	16849	15754	17874	23186	22926	---
Inventories	776	791	1764	2111	2349	2132	4855	3956	4106	---
Goodwill & Int. Ass.	4432	5359	5756	8758	9009	8620	8015	---	---	---
Total Liab. ($B)	39.76	57.85	83.45	120.29	170.99	193.44	241.27	258.58	248.03	---
Accounts Payable	14632	21175	22367	30196	35490	37294	49049	55888	46236	---
Long-Term Debt ($B)	0	0	16.96	35.30	64.33	87.03	115.68	114.48	108.05	---
Total Equity ($B)	76.62	118.21	123.55	111.55	119.36	128.25	134.05	107.15	904.88	---
D/E Ratio	0	0	0.1373	0.3164	0.539	0.6786	0.863	1.0685	1.19	---

Profitability & Per Share Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Return on Assets	27.1%	28.5%	19.3%	18.0%	20.5%	14.9%	13.9%	16.1%	15.7%	---
Return on Equity	41.7%	42.8%	30.6%	33.6%	46.2%	36.9%	36.9%	49.4%	55.9%	---
ROIC	41.7%	42.8%	28.6%	27.5%	32.3%	22.9%	20.8%	25.3%	26.3%	---
Shares Out.	26,020	26,298	25,178	23,465	22,315	21,345	20,505	19,020	17,773	17,528
Revenue/Share	4.13	5.91	6.55	7.46	10.09	9.80	10.91	13.28	13.99	---
FCF/Share	1.15	1.57	1.71	2.04	3.01	2.43	2.46	3.21	3.17	---

Note: All figures in millions of U.S. Dollars unless per share or indicated otherwise. Apple's fiscal 2020 table numbers will be available in our next update.