# Organon & Co. (OGN)

*Updated August 14th, 2021 by Nathan Parsh*

## Key Metrics

| | | | | | |
|---|---|---|---|---|---|
| **Current Price:** | $34 | **5 Year CAGR Estimate:** | 10.0% | **Market Cap:** | $8.7 billion |
| **Fair Value Price:** | $42 | **5 Year Growth Estimate:** | 3.0% | **Ex-Dividend Date:** | 8/20/2021 |
| **% Fair Value:** | 81% | **5 Year Valuation Multiple Estimate:** | 4.2% | **Dividend Payment Date:** | 9/13/2021 |
| **Dividend Yield:** | 3.3% | **5 Year Price Target** | $49 | **Years Of Dividend Growth:** | N/A |
| **Dividend Risk Score:** | B | **Retirement Suitability Score:** | A | **Last Dividend Increase:** | N/A |

## Overview & Current Events

On 6/3/2021, Merck & Company (MKR) completed its spinoff of Organon & Co. Organon is a pharmaceutical company that develops and markets health solutions in a variety of areas. It's established brands portfolio consists of nearly 50 products that have lost patent exclusivity and are used for treatment in the areas of cardiovascular, respiratory and dermatology and non-opioid pain management. Organon's women's health portfolio includes fertility and contraception brands, such as Nexplanon/Implanon and Nuva Ring. The company also has a small portfolio of biosimilars which are used in immunology and oncology. The spinoff has resulted in 15% of revenue, 25% of manufacturing sites and 50% of products being transferred from Merck to Organon.

Organon released second quarter results on 8/13/2021. The company reported revenues of $1.59 billion, which was a 4.5% improvement from the prior year and $62 million ahead of estimates. Adjusted earnings-per-share totaled $1.72, $0.29 better than expected.

Established brands, which accounted for nearly two-thirds of revenue, was lower by 4% due to loss of exclusivity of *Zetia*, which is used to lower cholesterol in the blood, in Japan. Women's health, which contributed a quarter of sales, grew 19% due to an increased number of in-patient visits and strength in fertility. Biosimilars improved 43% due to higher demand for *Renflexis*, which treats certain types of arthritis, and *Ontruzant*, which is used to treat HER2-overexpressing metastatic breast cancer.

Organon is expected to earn $5.98 in 2021, up from $5.86 previously.

## Growth on a Per-Share Basis

| Year | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2026 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **EPS** | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | ***$5.98*** | ***$6.93*** |
| **DPS** | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | ***$1.12*** | ***$1.30*** |
| **Shares**[1] | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | ***253*** | ***253*** |

Organon's parent company experienced an earnings per share growth rate of more than 5% over the last decade and nearly 12% over the last five years. Given that much of this growth was due to accelerating pharmaceutical sales that remain with Merck, we believe a slightly lower growth rate for Organon is likely to take place. Given the unknowns of the company at this point, we are comfortable forecasting earnings-per-share growth of 3% through 2026.

Organon does have several factors working in its favor for future growth. The established brands business should provide Organon with strong cash flows as the off-patent products don't require much in the way of the research and development expenses. The women's healthcare business has long been a pioneer in its field since its founding in 1923. The company produced the first-ever hormonal oral contraceptive as well the first-ever lower dose estrogen combined oral contraceptive. More recently, Organon developed the first once-a-month contraceptive ring. Biosimilars are the smallest portion of the new company, but Organon does expect to expand its portfolio, including a biosimilar to Humira for the U.S. market starting in 2023. Organon operates a fairly diverse business. By revenue per geography for 2020,

[1] In millions of shares

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Europe accounted for 27%, Asia Pacific/Japan 24%, the U.S. 22%, China 14% and Latin America/Middle East/Russia and Africa 13%, which affords the company some cushion should a specific region encounter headwinds.

The company declared its first dividend of $0.28, which is payable 9/13/2021.

## Valuation Analysis

| Year | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | Now | 2026 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **Avg. P/E** | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | ***5.7*** | ***7.0*** |
| **Avg. Yld.** | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | ***3.3%*** | ***2.7%*** |

Shares of Organon have increased $2, or 5.9%, since our 6/7/2021 update. Using the current share price and expected earnings-per-share for 2021, Organon trades with a price-to-earnings ratio of 5.7. This is an incredibly low valuation given the current state of the market. However, we feel that this new company will likely see low, but stable, growth in future years. We believe a starting price-to-earnings ratio of 7 is appropriate for the time being. This valuation target might be too conservative in the long run, but we are not ready to make that prediction at this point. Reaching the target multiple would add 4.2% to annual returns through 2026.

Even at the targeted low payout ratio, Organon's dividend yield is quite substantial at 3.3% and compares very favorably to the average yield of 1.3% for the S&P 500 index. We believe that dividend growth will match earnings-per-share growth over the next five years.

## Safety, Quality, Competitive Advantage, & Recession Resiliency

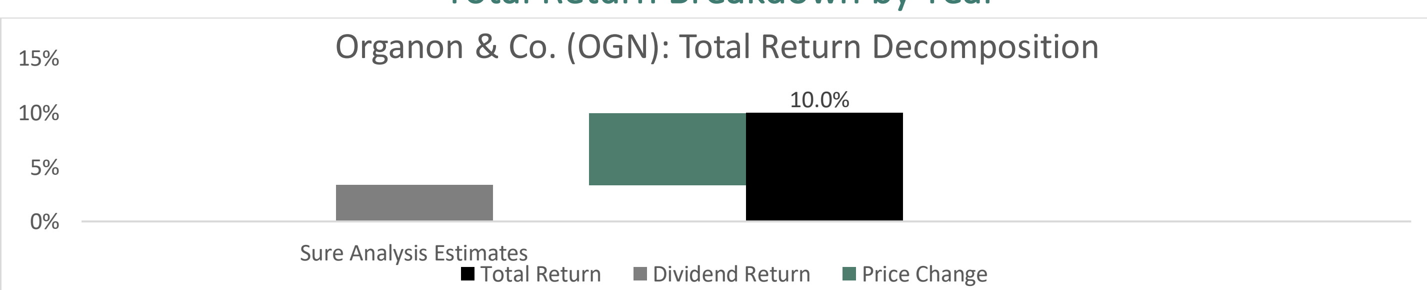
| Year | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2026 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **Payout** | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | ***19%*** | ***19%*** |

Organon has not yet been tested during a recession. It's parent company generated of earnings-per-share growth of 33% from 2007 through 2009. Including 2006 is this calculation actually results an earnings-per-share decrease of nearly 11% for this period of time, showing that Merck's business was more unpredictable than its healthcare peers. However, Merck is a vastly different company now then it was during that period of time, thanks to the explosive growth of its key product *Keytruda*. Nevertheless, we believe that Organon would perform well during a recession as its product portfolio can largely be considered recession resistant. Healthcare companies tend to hold up much better than more cyclical companies in economic downturns as their products are in demand regardless of economic conditions.

## Final Thoughts & Recommendation

Organon is projected to return 10% annually through 2026, down from our prior estimate of 11%. Our projected return stems from an earnings growth rate of 3%, a 3.3% starting dividend yield and a mid-single-digit contribution from multiple expansion. Organon delivered a solid quarter despite a weak showing from its largest business. Established brands showed a slight year-over-year decrease, but the other segments were quite strong. We have raised our 2026 price target $1 to $49 due to higher EPS estimates and continue to rate shares of Organon as a buy.

## Total Return Breakdown by Year

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## Income Statement Metrics

| Year | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 |
|---|---|---|---|---|---|---|---|---|---|---|
| Revenue | --- | --- | --- | --- | --- | --- | --- | 9,777 | 9,530 | 8,096 |
| Gross Profit | --- | --- | --- | --- | --- | --- | --- | 5,084 | 5,909 | 4,749 |
| Gross Margin | --- | --- | --- | --- | --- | --- | --- | 52.0% | 62.0% | 58.7% |
| SG&A Exp. | --- | --- | --- | --- | --- | --- | --- | 2,013 | 1,922 | 1,666 |
| D&A Exp. | --- | --- | --- | --- | --- | --- | --- | 1,673 | 354 | 157 |
| Operating Profit | --- | --- | --- | --- | --- | --- | --- | 2,706 | 3,655 | 2,779 |
| Op. Margin | --- | --- | --- | --- | --- | --- | --- | 27.7% | 38.4% | 34.3% |
| Net Profit | --- | --- | --- | --- | --- | --- | --- | 2,153 | 3,218 | 2,160 |
| Net Margin | --- | --- | --- | --- | --- | --- | --- | 22.0% | 33.8% | 26.7% |
| Free Cash Flow | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
| Income Tax | --- | --- | --- | --- | --- | --- | --- | 576 | 337 | 520 |

## Balance Sheet Metrics

| Year | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 |
|---|---|---|---|---|---|---|---|---|---|---|
| Total Assets ($B) | --- | --- | --- | --- | --- | --- | --- | --- | 10,548 | 10,434 |
| Cash & Equivalents | --- | --- | --- | --- | --- | --- | --- | --- | 319 | 500 |
| Acc. Receivable | --- | --- | --- | --- | --- | --- | --- | --- | 1,474 | 1,092 |
| Inventories | --- | --- | --- | --- | --- | --- | --- | --- | 1,071 | 913 |
| Goodwill & Int. | --- | --- | --- | --- | --- | --- | --- | --- | 5,172 | 5,106 |
| Total Liabilities | --- | --- | --- | --- | --- | --- | --- | --- | 3,513 | 11,254 |
| Accounts Payable | --- | --- | --- | --- | --- | --- | --- | --- | 258 | 259 |
| Long-Term Debt | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
| Total Equity | --- | --- | --- | --- | --- | --- | --- | --- | 7,035 | (820) |
| D/E Ratio | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |

## Profitability & Per Share Metrics

| Year | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 |
|---|---|---|---|---|---|---|---|---|---|---|
| Return on Assets | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
| Return on Equity | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
| ROIC | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
| Shares Out. | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
| Revenue/Share | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
| FCF/Share | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |

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