



British American Tobacco (BTI)

Updated September 23rd, 2021 by Jonathan Weber

Key Metrics

Current Price:	\$37	5 Year CAGR Estimate:	11.6%	Market Cap:	\$84B
Fair Value Price:	\$42	5 Year Growth Estimate:	3.0%	Ex-Dividend Date:	10/08/21
% Fair Value:	89%	5 Year Valuation Multiple Estimate:	2.5%	Dividend Payment Date:	11/24/21
Dividend Yield:	7.8%	5 Year Price Target	\$48	Years Of Dividend Growth:	2
Dividend Risk Score:	C	Retirement Suitability Score:	A	Last Dividend Increase:	3.9%

Overview & Current Events

British American Tobacco is one of the world's largest tobacco companies. British American Tobacco owns many tobacco brands, including *Kool*, *Benson & Hedges*, *Dunhill*, *Kent*, and *Lucky Strike*. The company also acquired the remaining 48% stake in Reynolds American Tobacco that it did not already own in July of 2017. Although the company is incorporated in the United Kingdom and headquartered in London, American investors can purchase its stock through American Depository Receipts that trade on the New York Stock Exchange under the ticker BTI. Despite being headquartered in the United Kingdom, British American Tobacco triggers no dividend withholding tax for United States investors. All numbers in this report are in US\$ unless noted otherwise.

British American Tobacco announced its first half earnings results for the current year on July 28. In the report, British American Tobacco stated that revenue came in at 12.2 billion Pound Sterling during the first half, which equates to an attractive 8.1% growth rate versus the previous year's period on an adjusted basis. This was, to a large extent, driven by strong growth for the *New Categories* business (reduced-risk products, such as non-combustible tobacco), which saw revenues rise 50% year over year. Due to some operating margin compression, British American Tobacco was not able to translate the high-single-digit revenue growth rate into a similar bottom line growth rate, however.

British American Tobacco generated adjusted earnings-per-share of 1.54 Pound Sterling in the first half of the current year, which equates to \$2.11. Earnings-per-share were up 6.1% year over year, which is not an outstanding, but a very solid growth rate for a tobacco company. British American Tobacco also showed that its net debt had declined to 40.5 billion Pound Sterling, down 8% year over year, which shows the company's balance sheet progress.

Growth on a Per-Share Basis

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
EPS	\$3.04	\$3.46	\$3.65	\$3.71	\$3.18	\$3.08	\$3.96	\$3.89	\$4.38	\$4.58	\$4.40	\$5.10
DPS	\$1.59	\$1.93	\$2.11	\$2.35	\$2.42	\$2.28	\$2.84	\$2.66	\$2.71	\$2.74	\$2.90	\$3.28
Shares¹	1970	1940	1900	1860	1860	1860	2290	2290	2290	2300	2310	2350

British American Tobacco's earnings-per-share grew by ~90% between 2009 and 2020, which equates to an annual earnings-per-share growth rate of ~6%. The company's growth has been uneven, though, as there were several years where British American Tobacco's profits declined. The company reports its results in Pound Sterling, whereas the results in the above table are in USD. Depending on the exchange rate between these two currencies, growth rates in USD can differ from British American Tobacco's reported growth rates. In 2018, for example, results in Pound Sterling were up, whereas results in USD declined. Currency rate changes also impact dividend payments.

Cost savings following the integration of Reynolds American will be a driver for British American Tobacco's earnings in the future. Other factors include ongoing organic growth due to rising cigarette prices and the rise of vaping products, and declining interest expenses as long as British American Tobacco is able to lower its debt load due to ongoing debt pay downs. Interest rates at all-time lows, especially in Europe, should help drive further interest savings. We see a low-single-digit earnings-per-share growth rate in the future, although management has a more positive growth goal.

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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Valuation Analysis

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	Now	2026
Avg. P/E	14.3	14.7	14.6	15.3	17.6	19.2	16.4	8.5	9.6	8.1	8.4	9.5
Avg. Yld.	4.4%	4.2%	4.4%	4.3%	4.1%	3.7%	4.1%	8.1%	6.5%	7.4%	7.8%	6.8%

British American Tobacco's shares have not moved much since our last update. Its valuation remains pretty low on an absolute basis. Share prices of other tobacco companies have declined substantially throughout the last couple of years, which has resulted in big declines in these companies' valuations. British American Tobacco trades for just 8.4 times this year's expected net earnings. Due to uncertainties for the industry, such as increasing menthol regulation in the US, we believe that the valuation will not expand to double digits, but we still see upside potential from the current level.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
Payout	52.3%	55.8%	57.8%	63.3%	76.1%	74.0%	55.1%	68.4%	61.9%	59.8%	65.9%	64.3%

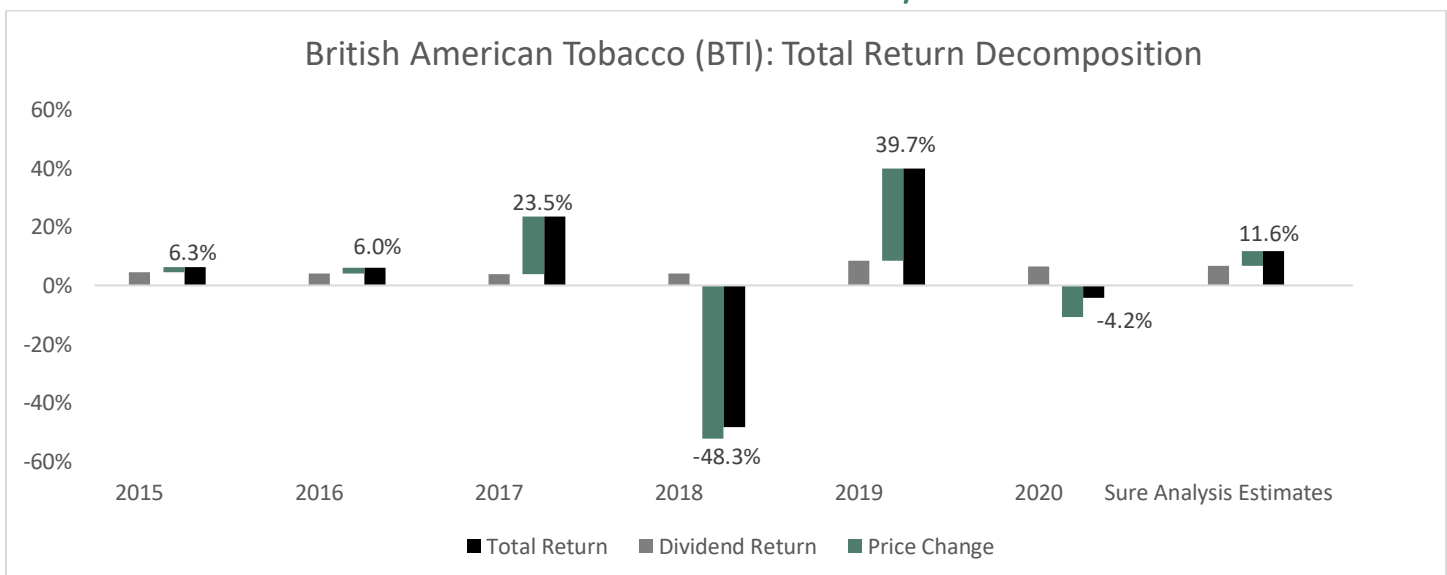
British American Tobacco has kept its dividend payout ratio in a range of 55%-75% throughout the last decade. Compared to other tobacco stocks, this is not a high payout ratio. Some competitors, such as Altria, pay out ~80% of their profits in the form of dividends. We believe that the dividend is safe for the foreseeable future.

British American Tobacco operates in an oligopoly that does not have a tendency to engage in price wars. The players in this industry have always focused on profits over market share gains, which is why the industry is not overly competitive, and why profits have been rising for all players. Demand for cigarettes is not cyclical, which is why British American Tobacco performed well during the last financial crisis, when profits continued to rise between 2008 and 2010.

Final Thoughts & Recommendation

British American Tobacco's dividend yield remains at a high level of more than 7%. 2020 was, despite pandemic-related headwinds, a very solid year for the company, as it was able to grow its profits while continuing to deleverage. Due to some currency rate headwinds, earnings-per-share will likely decline slightly this year. We rate British American Tobacco a buy at current prices thanks to an attractive total return outlook of more than 10% a year over the coming five years.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Revenue	24,693	24,070	23,875	23,029	20,026	19,145	25,260	32,678	33,041	33,082
Gross Profit	19,199	18,822	18,802	18,035	15,391	14,087	18,762	26,608	27,376	27,771
Gross Margin	77.8%	78.2%	78.7%	78.3%	76.9%	73.6%	74.3%	81.4%	82.9%	83.9%
SG&A Exp.	26	24	23	25	19	15	39	34	32	36
D&A Exp.	1,310	753	746	862	654	822	1,165	1,385	1,931	1,861
Operating Profit	7,676	8,611	8,716	7,670	6,979	6,745	8,697	12,592	11,785	13,060
Op. Margin	31.1%	35.8%	36.5%	33.3%	34.9%	35.2%	34.4%	38.5%	35.7%	39.5%
Net Profit	4,963	6,017	6,108	5,135	6,556	6,298	48,400	8,048	7,283	8,214
Net Margin	20.1%	25.0%	25.6%	22.3%	32.7%	32.9%	191.6%	24.6%	22.0%	24.8%
Free Cash Flow	6,332	5,741	5,812	4,985	6,295	5,333	5,641	12,478	10,446	11,591
Income Tax	2,495	2,402	2,503	2,398	2,037	1,905	-10496	2,857	2,634	2,706

Balance Sheet Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Total Assets (\$B)	41785	44160	44327	40728	46689	48862	190620	185693	184882	187648
Cash & Equivalents	3156	3119	3212	2534	2658	2515	4231	2927	2490	2461
Acc. Receivable	3733	4429	4743	4308	4839	4772	5477	4553	5367	5071
Inventories	5390	6506	6665	6433	6292	7117	7925	7650	7990	8174
Goodwill/Int. (\$B)	18477	18923	18477	16816	15461	14886	159175	157360	155750	157193
Total Liab. (\$B)	28728	31590	32891	31679	39235	38535	108211	102342	100757	101851
Accounts Payable	7972	9416	9467	8598	8796	9011	12038	13490	12754	13210
Long-Term Debt	15833	17322	19287	19079	25187	23950	66827	60284	59483	59921
Total Equity	12584	12075	10939	8576	7250	10052	82110	83042	83786	85413
D/E Ratio	1.26	1.43	1.76	2.22	3.47	2.38	0.81	0.73	0.71	0.70

Profitability & Per Share Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Return on Assets	11.7%	14.0%	13.8%	12.1%	15.0%	13.2%	40.4%	4.3%	3.9%	4.4%
Return on Equity	37.0%	48.8%	53.1%	52.6%	82.8%	72.8%	105%	9.7%	8.7%	9.7%
ROIC	16.7%	20.5%	20.2%	17.4%	21.6%	18.8%	52.7%	5.5%	5.1%	5.7%
Shares Out.	1970	1940	1900	1860	1860	1860	2290	2290	2290	2300
Revenue/Share	12.46	12.35	12.51	12.32	10.75	10.27	12.32	14.26	14.42	14.42
FCF/Share	3.19	2.95	3.05	2.67	3.38	2.86	2.75	5.44	4.56	5.05

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

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