



British American Tobacco (BTI)

Updated June 24th, 2022 by Jonathan Weber

Key Metrics

Current Price:	\$43	5 Year CAGR Estimate:	9.8%	Market Cap:	\$97B
Fair Value Price:	\$46	5 Year Growth Estimate:	3.0%	Ex-Dividend Date:	07/21/22
% Fair Value:	94%	5 Year Valuation Multiple Estimate:	1.2%	Dividend Payment Date:	08/05/22
Dividend Yield:	6.8%	5 Year Price Target	\$53	Years Of Dividend Growth:	2
Dividend Risk Score:	C	Retirement Suitability Score:	A	Rating:	Hold

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 H1 pre-close trading update, which is its equivalent of its first quarter earnings announcement, on June 9. In the report, British American Tobacco stated that revenue growth performance was in line with expectations so far this year, driven, among other factors, by a strong performance of the non-combustible product portfolio. During the first three months of the year, those products reached around 20 million consumers. British American Tobacco stated that profitability in the New Categories group improved markedly compared to the previous year's period, thanks to improving scale which allows for operating leverage. For the current year, British American Tobacco is forecasting revenue growth of 2% to 4% at constant currencies, which is solid for a tobacco company.

British American Tobacco generated adjusted earnings-per-share of 3.30 Pound Sterling in 2021, which equates to \$4.45 at then-current interest rates. For 2022, analysts are currently predicting meaningfully higher profits, due to higher revenues, debt reduction, and a lower share count.

Growth on a Per-Share Basis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
EPS	\$3.46	\$3.65	\$3.71	\$3.18	\$3.08	\$3.96	\$3.89	\$4.38	\$4.58	\$4.45	\$4.80	\$5.56
DPS	\$1.93	\$2.11	\$2.35	\$2.42	\$2.28	\$2.84	\$2.66	\$2.71	\$2.74	\$2.94	\$2.94	\$3.33
Shares¹	1940	1900	1860	1860	1860	2290	2290	2290	2300	2300	2250	2150

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

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Valuation Analysis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	Now	2027
Avg. P/E	14.7	14.6	15.3	17.6	19.2	16.4	8.5	9.6	8.1	8.3	9.0	9.5
Avg. Yld.	4.2%	4.4%	4.3%	4.1%	3.7%	4.1%	8.1%	6.5%	7.4%	7.9%	6.8%	6.3%

British American Tobacco's shares have declined slightly since our last update. Its valuation remains low on an absolute basis, but is higher than it was over the last two years. British American Tobacco trades for 9 times this year's expected net earnings, which is slightly below our fair value estimate. Due to uncertainties for the industry, such as increasing menthol regulation in the US, we believe that the valuation will not expand to the double digits. Investors get an attractive 6%+ dividend yield at current prices.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
Payout	55.8%	57.8%	63.3%	76.1%	74.0%	55.1%	68.4%	61.9%	59.8%	66.1%	61.3%	59.8%

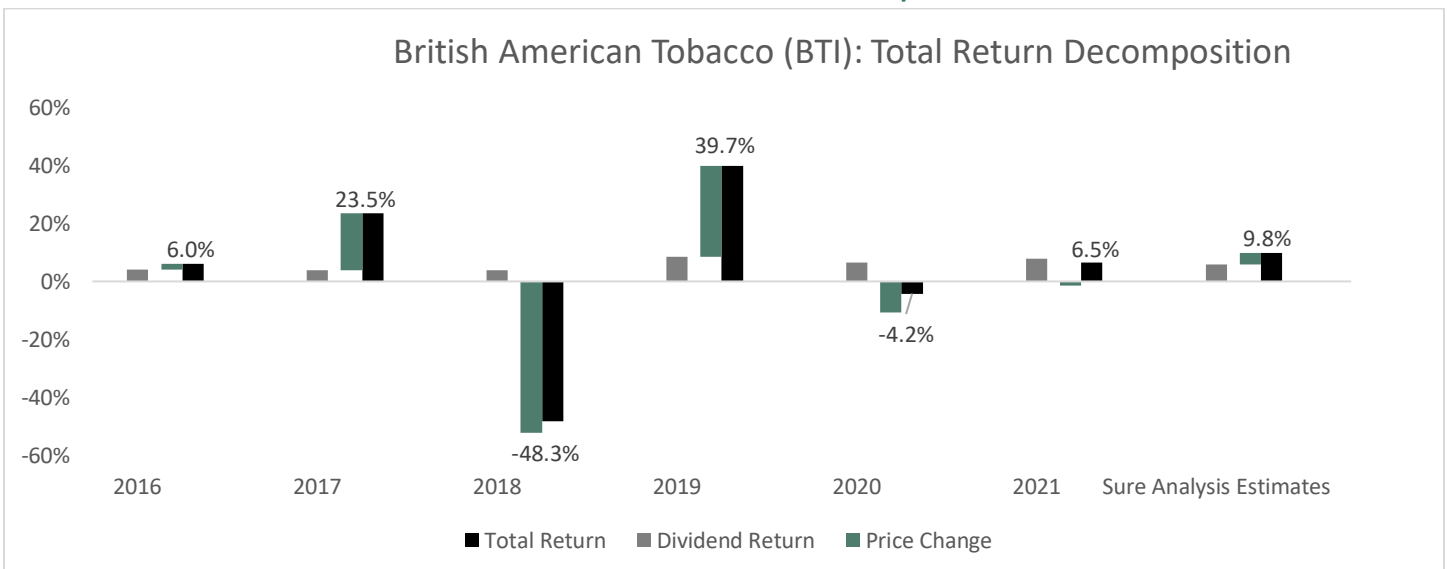
British American Tobacco has kept its dividend payout ratio in a range of 55%-75% throughout the last decade. Compared to other tobacco stocks, this is not a high payout ratio. Some competitors, such as Altria, pay out ~80% of their profits in the form of dividends. We believe that the dividend is safe 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 an attractive level of more than 6%. 2021 was a very solid year for the company as it saw rapid growth in the New Categories space while continuing to deleverage. The outlook for 2022 is solid as well, as revenue and profit should improve further. We rate British American Tobacco a hold at current prices as the total return outlook is solid but not great and since shares trade close to fair value.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Revenue	24,070	23,875	23,029	20,026	19,145	25,260	32,678	33,041	33,082	35,335
Gross Profit	18,822	18,802	18,035	15,391	14,087	18,762	26,608	27,376	27,771	29,306
Gross Margin	78.2%	78.7%	78.3%	76.9%	73.6%	74.3%	81.4%	82.9%	83.9%	82.9%
SG&A Exp.	24	23	25	19	15	39	34	32		
D&A Exp.	753	746	862	654	822	1,165	1,385	1,931	1,861	1,480
Operating Profit	8,611	8,716	7,670	6,979	6,745	8,697	12,592	11,785	12,790	14,083
Op. Margin	35.8%	36.5%	33.3%	34.9%	35.2%	34.4%	38.5%	35.7%	38.7%	39.9%
Net Profit	6,017	6,108	5,135	6,556	6,298	48,400	8,048	7,283	8,214	9,356
Net Margin	25.0%	25.6%	22.3%	32.7%	32.9%	191.6%	24.6%	22.0%	24.8%	26.5%
Free Cash Flow	5,741	5,812	4,985	6,295	5,333	5,641	12,478	10,446	11,591	12,343
Income Tax	2,402	2,503	2,398	2,037	1,905	-10,496	2,857	2,634	2,706	3,011

Balance Sheet Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Total Assets (\$B)	44.16	44.33	40.73	46.69	48.86	190.62	185.69	184.88	187.65	185.39
Cash & Equivalents	3,119	3,212	2,534	2,658	2,515	4,231	2,927	2,490	2,461	3,791
Acc. Receivable	4,429	4,743	4,308	4,839	4,772	5,477	4,553	5,367	5,071	5,332
Inventories	6,506	6,665	6,433	6,292	7,117	7,925	7,650	7,990	8,174	7,125
Goodwill/Int. (\$B)	18.92	18.48	16.82	15.46	14.89	159.17	157.36	155.75	157.19	156.05
Total Liab. (\$B)	31.59	32.89	31.68	39.23	38.53	108.21	102.34	100.76	101.85	94.43
Accounts Payable	9,416	9,467	8,598	8,796	9,011	12,038	13,490	12,754	13,210	12,926
Long-Term Debt	17,322	19,287	19,079	25,187	23,950	66,827	60,284	59,483	59,921	53,524
Total Equity	12,075	10,939	8,576	7,250	10,052	82,110	83,042	83,786	85,413	90,562
LTD/E Ratio	1.43	1.76	2.22	3.47	2.38	0.81	0.73	0.71	0.70	0.59

Profitability & Per Share Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Return on Assets	14.0%	13.8%	12.1%	15.0%	13.2%	40.4%	4.3%	3.9%	4.4%	5.0%
Return on Equity	48.8%	53.1%	52.6%	82.8%	72.8%	105%	9.7%	8.7%	9.7%	10.6%
ROIC	20.5%	20.2%	17.4%	21.6%	18.8%	52.7%	5.5%	5.1%	5.7%	6.4%
Shares Out.	1940	1900	1860	1860	1860	2290	2290	2290	2300	2300
Revenue/Share	12.35	12.51	12.32	10.75	10.27	12.32	14.26	14.42	14.42	15.38
FCF/Share	2.95	3.05	2.67	3.38	2.86	2.75	5.44	4.56	5.05	5.37

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

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