



Philips Electronics NV (PHG)

Updated October 26th, 2022 by Aristofanis Papadatos

Key Metrics

Current Price:	\$13	5 Year CAGR Estimate:	23.1%	Market Cap:	\$11.3 B
Fair Value Price:	\$19	5 Year Growth Estimate:	11.0%	Ex-Dividend Date:	5/11/2023 ¹
% Fair Value:	69%	5 Year Valuation Multiple Estimate:	7.8%	Dividend Payment Date:	6/7/2023
Dividend Yield:	7.0%	5 Year Price Target	\$32	Years Of Dividend Growth:	0
Dividend Risk Score:	F	Retirement Suitability Score:	C	Rating:	Buy

Overview & Current Events

Philips Electronics NV is a global manufacturer of electronic products for healthcare, lighting, and other consumer products. The company used to generate about half of its sales from lighting, TV and lifestyle entertainment products but has gone through a major transformation in recent years and has become a health tech leader. It now has four operating segments: Diagnosis & Treatment (42% of total sales), Personal Health (28% of sales), Connected Care & Health Informatics (29% of sales) and Legacy Items (1% of sales). The company is headquartered in The Netherlands. United States investors can initiate a stake in Philips Electronics through American Depository Receipts that trade on the New York Stock Exchange with a market capitalization of US\$11.3 billion under the ticker PHG.

In late October, Philips Electronics reported (10/24/22) financial results for the third quarter of fiscal 2022. Its comparable sales decreased -6% due to supply chain issues and the sustained effect of the recall of respiratory devices. As a result, adjusted EBITDA margin shrank from 12.3% to 4.8%.

The poor performance resulted primarily from the sustained effect of the recall of 4 million respiratory devices in 2021. Over 100 injuries have been reported from a foam part of the devices, which can degrade and cause cancer. The FDA has categorized the recall as “the most serious type.” The company recently changed its CEO in an effort to turn around. While this headwind is non-recurring, it may cost many billions of dollars and hence it has increased the risk of the stock. On the other hand, we believe that the company will recover from this downturn thanks to its leading position in its markets. Nevertheless, due to the short-term impact of this headwind, we have lowered our forecast for earnings-per-share in 2022 from \$1.30 to \$1.05. We also note that it is taking much longer to the company to recover from this crisis while management is blaming macro headwinds, such as supply chain disruptions and the war in Ukraine, for the poor results. This is a red flag for the stock. We are also cautious of the recently announced ~4,000 layoffs, as it will be hard for the company to increase the safety of its devices with a much lower head count (currently ~79,000 employees).

Growth on a Per-Share Basis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
EPS	\$0.37	\$1.75	\$0.29	\$0.47	\$1.22	\$1.31	\$1.37	\$2.22	\$2.28	\$1.23	\$1.05	\$1.77
DPS	\$0.94	\$0.98	\$1.09	\$0.89	\$0.90	\$0.90	\$0.94	\$0.96	\$0.96	\$1.03	\$0.91	\$1.00
Shares²	914.6	913.3	914.4	917.1	922.4	926.2	931.4	902.9	915.2	917.0	885	850

Philips Electronics has a markedly volatile performance record. However, it grew strongly between 2018 and 2021, until the aforementioned recall of respiratory devices. We view this headwind as temporary and expect the company to return to strong growth mode thanks to favorable business factors, such as a growing population, an increase in average age and rising consumer spending on healthcare. Management expects 4%-6% annual comparable sales growth until 2025, with all the segments within this range, annual improvement in EBITDA margin of 60-80 basis points and 10%

¹ Estimated date for annual dividend.

² 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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average annual earnings-per-share growth. We have assumed 11% average annual earnings-per-share growth over the next five years due to the low comparison base formed this year.

Valuation Analysis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	Now	2027
Avg. P/E	---	17.7	---	---	22.5	27.3	29.7	19.1	20.7	40.5	12.4	18.0
Avg. Yld.	4.3%	3.2%	3.4%	3.3%	3.3%	2.5%	2.3%	2.3%	2.0%	2.1%	7.0%	3.2%

During the years in which Philips Electronics' price-to-earnings ratio has been meaningful over the last decade, the stock has traded at an average earnings multiple of 22.8. We believe that this is a rich valuation multiple for a company like Philips Electronics and assume a fair price-to-earnings ratio of 18.0. The stock is currently trading at a 10-year low price-to-earnings ratio of 12.4 due to the aforementioned issue with the problematic devices. If the stock reaches our assumed fair price-to-earnings ratio of 18.0 over the next five years, it will enjoy a 7.8% annualized gain in its returns.

Income investors should note that the Netherlands applies a 15% withholding tax on dividends paid to international investors. This reduces the company's net dividend yield to 6.0% (from 7.0% before the withholding tax).

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
Payout	254%	56.0%	376%	189%	73.8%	68.7%	68.6%	43.2%	42.1%	83.7%	86.7%	56.8%

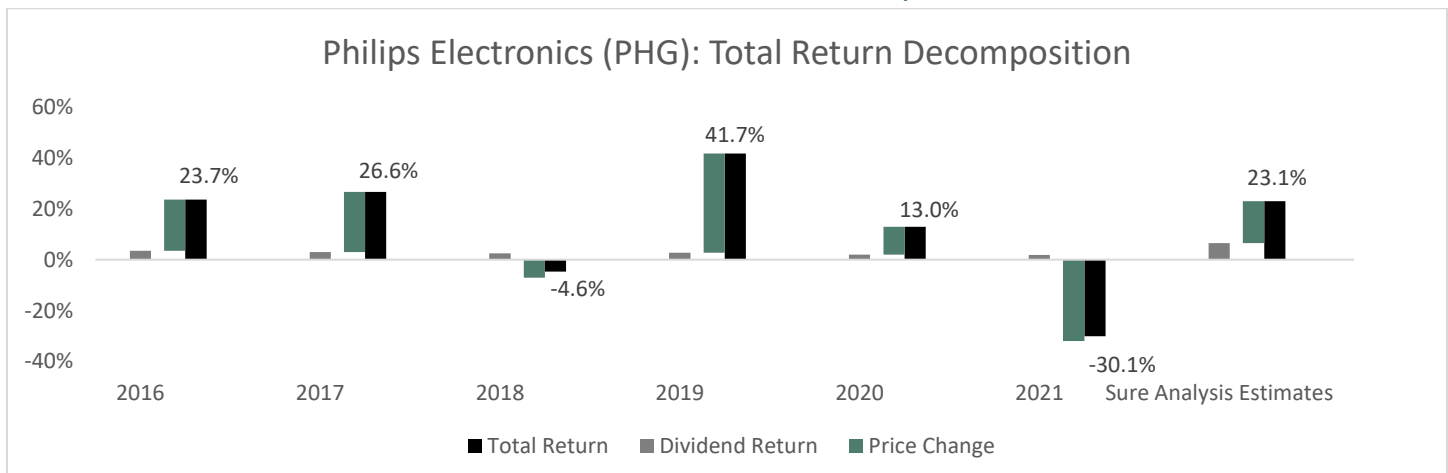
Philips Electronics has a strong brand name, which provides a competitive advantage in the current product categories of the company. Moreover, the company generates more than 60% of its sales from the #1 or #2 position based on market share for its respective products. This provides some pricing power to the company.

On the other hand, as Philips Electronics has a volatile performance record, it is not suitable for income-oriented investors. Moreover, the stock has previously underperformed the market during broad market corrections.

Final Thoughts & Recommendation

After its -79% decline off its peak in 2021, which has resulted from the aforementioned recall, Philips Electronics could offer a 23.1% average annual return over the next five years thanks to 11.0% growth, its 7.0% dividend and a 7.8% valuation tailwind. The recall has increased the risk of the stock, but we view it as a temporary headwind and thus we view the decline of the stock as an opportunity. Shares earn a buy rating.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Revenue	28,585	29,205	28,447	18,650	19,281	20,136	21,397	19,196	19,771	20,299
Gross Profit	11,222	12,400	10,913	8,003	8,787	9,265	10,101	8,843	8,931	8,481
Gross Margin	39.3%	42.5%	38.4%	42.9%	45.6%	46.0%	47.2%	46.1%	45.2%	41.8%
SG&A Exp.	7,826	7,812	7,807	5,605	5,312	5,634	6,059	5,274	5,349	5,747
D&A Exp.	1,597	1,563	1,579	1,079	1,080	1,161	1,286	1,503	1,670	1,565
Operating Profit	1,180	2,385	931	665	1,623	1,609	1,954	1,557	1,603	737
Op. Margin	4.1%	8.2%	3.3%	3.6%	8.4%	8.0%	9.1%	8.1%	8.1%	3.6%
Net Profit	(45)	1,553	552	692	1,603	1,877	1,287	1,306	1,356	3,927
Net Margin	-0.2%	5.3%	1.9%	3.7%	8.3%	9.3%	6.0%	6.8%	6.9%	19.3%
Free Cash Flow	1,367	73	608	(255)	458	1,145	1,106	965	1,846	1,025
Income Tax	280	619	35	188	225	395	228	289	242	(122)

Balance Sheet Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Total Assets	38,460	36,675	34,477	33,866	34,115	30,370	29,763	30,263	34,086	35,055
Cash & Equivalents	5,070	3,404	2,278	1,931	2,467	2,326	1,931	1,596	3,968	2,608
Acc. Receivable	5,732	6,103	5,443	5,168	5,631	4,330	4,353	5,101	4,831	4,030
Inventories	4,622	4,474	4,030	3,786	3,586	2,823	3,059	3,106	3,681	3,906
Goodwill & Int.	14,123	13,486	12,800	13,356	13,162	13,261	13,831	13,576	13,544	16,177
Total Liabilities	23,667	21,171	21,139	20,987	19,893	15,946	15,902	16,120	19,448	18,667
Accounts Payable	3,749	3,394	3,034	2,918	3,011	2,507	2,634	2,340	2,606	2,120
Long-Term Debt	5,996	5,387	4,991	6,297	5,926	4,674	4,113	4,343	5,823	5,465
Total Equity	14,747	15,485	13,214	12,750	13,263	14,395	13,827	14,111	14,600	16,347
LTD/E Ratio	0.41	0.35	0.38	0.49	0.45	0.32	0.30	0.31	0.40	0.33

Profitability & Per Share Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Return on Assets	-0.1%	4.1%	1.6%	2.0%	4.7%	5.8%	4.3%	4.4%	4.2%	11.4%
Return on Equity	-0.3%	10.3%	3.8%	5.3%	12.3%	13.6%	9.1%	9.4%	9.4%	25.4%
ROIC	-0.2%	7.5%	2.8%	3.7%	8.2%	9.6%	6.9%	7.2%	7.0%	18.6%
Shares Out.	914.6	913.3	914.4	917.1	922.4	926.2	931.4	902.9	915.2	917.0
Revenue/Share	30.22	31.04	30.22	19.79	20.35	20.88	22.43	20.62	21.57	22.31
FCF/Share	1.44	0.08	0.65	(0.27)	0.48	1.19	1.16	1.04	2.01	1.13

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

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