



# British American Tobacco (BTI)

Updated February 9<sup>th</sup>, 2023 by Jonathan Weber

## Key Metrics

<b>Current Price:</b>	\$37	<b>5 Year CAGR Estimate:</b>	11.7%	<b>Market Cap:</b>	\$83B
<b>Fair Value Price:</b>	\$42	<b>5 Year Growth Estimate:</b>	3.0%	<b>Ex-Dividend Date:</b>	03/29/23
<b>% Fair Value:</b>	87%	<b>5 Year Valuation Multiple Estimate:</b>	2.7%	<b>Dividend Payment Date:</b>	05/15/23
<b>Dividend Yield:</b>	7.7%	<b>5 Year Price Target</b>	\$49	<b>Years Of Dividend Growth:</b>	1
<b>Dividend Risk Score:</b>	C	<b>Retirement Suitability Score:</b>	A	<b>Rating:</b>	Buy

## 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 was able to generate 8% group-wide revenue growth during fiscal 2022. This revenue growth was driven, among other factors, by a strong performance of the non-combustible product portfolio the company has been investing heavily in, and which now generates 11% of the company's overall revenue, and which has grown at a rate of 41% over the last year.

British American Tobacco generated adjusted earnings-per-share growth of 13% during the period, which was quite attractive. The weakening Pound Sterling had a negative impact on British American Tobacco's results once denominated in US Dollars, however. For the current year, fiscal 2023, British American Tobacco expects that its revenue will grow by 3% to 5% at constant currency rates, mostly driven by growth in its New Categories business. Earnings-per-share are forecasted to grow by around 5% at constant currency rates, but in US Dollars the company's earnings-per-share growth could be different, depending on the exchange rate between GBP and USD over the year.

## Growth on a Per-Share Basis

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
<b>EPS</b>	\$3.65	\$3.71	\$3.18	\$3.08	\$3.96	\$3.89	\$4.38	\$4.58	\$4.45	\$4.49	<b>\$4.70</b>	<b>\$5.45</b>
<b>DPS</b>	\$2.11	\$2.35	\$2.42	\$2.28	\$2.84	\$2.66	\$2.71	\$2.74	\$2.94	\$2.81	<b>\$2.84</b>	<b>\$3.21</b>
<b>Shares<sup>1</sup></b>	1900	1860	1860	1860	2290	2290	2290	2300	2300	2270	<b>2270</b>	<b>2200</b>

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.

<sup>1</sup> In Millions

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## Valuation Analysis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	Now	2028
Avg. P/E	14.7	14.6	15.3	17.6	19.2	16.4	8.5	9.6	8.1	8.9	<b>7.9</b>	<b>9.0</b>
Avg. Yld.	4.2%	4.4%	4.3%	4.1%	3.7%	4.1%	8.1%	6.5%	7.4%	7.0%	<b>7.7%</b>	<b>6.6%</b>

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 a little less than 8 times this year's expected net earnings, which is 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 dividend yield at current prices.

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

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
Payout	57.8%	63.3%	76.1%	74.0%	55.1%	68.4%	61.9%	59.8%	66.1%	62.6%	<b>60.4%</b>	<b>59.0%</b>

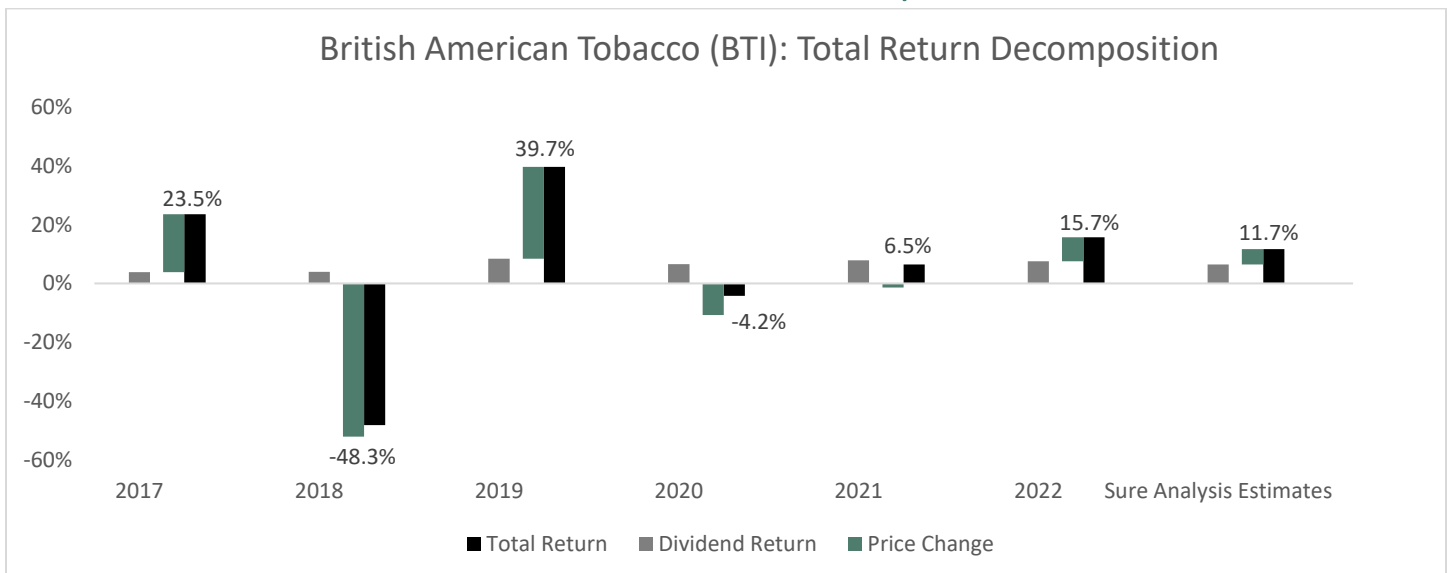
British American Tobacco has kept its dividend payout ratio in a range of 55%-75% throughout the last decade. Compared to other tobacco stocks, this is not a high payout ratio. Some competitors, such as Altria, pay out ~80% of their profits in the form of dividends. We believe that the dividend is safe 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. 2022 was a solid year for the company as it saw rapid growth in the New Categories space while continuing to deleverage. The operational outlook for 2023 is solid as well, and the company has increased its dividend by 6% in Pound Sterling, although the growth rate in USD was lower. We rate British American Tobacco a buy at current prices as the total return outlook is compelling.

## Total Return Breakdown by Year



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## Income Statement Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
<b>Revenue</b>	23,875	23,029	20,026	19,145	25,260	32,678	33,041	33,082	35,335	34,246
<b>Gross Profit</b>	18,802	18,035	15,391	14,087	18,762	26,608	27,376	27,771	29,306	28,607
<b>Gross Margin</b>	78.7%	78.3%	76.9%	73.6%	74.3%	81.4%	82.9%	83.9%	82.9%	83.5%
<b>SG&amp;A Exp.</b>	23	25	19	15	39	34	32			1,472
<b>D&amp;A Exp.</b>	746	862	654	822	1,165	1,385	1,931	1,861	1,480	1,616
<b>Operating Profit</b>	8,716	7,670	6,979	6,745	8,697	12,592	11,785	12,790	14,083	18,921
<b>Op. Margin</b>	36.5%	33.3%	34.9%	35.2%	34.4%	38.5%	35.7%	38.7%	39.9%	55.2%
<b>Net Profit</b>	6,108	5,135	6,556	6,298	48,400	8,048	7,283	8,214	9,356	8,255
<b>Net Margin</b>	25.6%	22.3%	32.7%	32.9%	191.6%	24.6%	22.0%	24.8%	26.5%	24.1%
<b>Free Cash Flow</b>	5,812	4,985	6,295	5,333	5,641	12,478	10,446	11,591	12,343	12,059
<b>Income Tax</b>	2,503	2,398	2,037	1,905	-10,496	2,857	2,634	2,706	3,011	3,069

## Balance Sheet Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
<b>Total Assets (\$B)</b>	44.33	40.73	46.69	48.86	190.62	185.69	184.88	187.65	185.39	185.8
<b>Cash &amp; Equivalents</b>	3,212	2,534	2,658	2,515	4,231	2,927	2,490	2,461	3,791	4,170
<b>Acc. Receivable</b>	4,743	4,308	4,839	4,772	5,477	4,553	5,367	5,071	5,332	5,285
<b>Inventories</b>	6,665	6,433	6,292	7,117	7,925	7,650	7,990	8,174	7,125	6,863
<b>Goodwill/Int. (\$B)</b>	18.48	16.82	15.46	14.89	159.17	157.36	155.75	157.19	156.05	156.2
<b>Total Liab. (\$B)</b>	32.89	31.68	39.23	38.53	108.21	102.34	100.76	101.85	94.43	94.19
<b>Accounts Payable</b>	9,467	8,598	8,796	9,011	12,038	13,490	12,754	13,210	12,926	12,645
<b>Long-Term Debt</b>	19,287	19,079	25,187	23,950	66,827	60,284	59,483	59,921	53,524	51,581
<b>Total Equity</b>	10,939	8,576	7,250	10,052	82,110	83,042	83,786	85,413	90,562	91,210
<b>LTD/E Ratio</b>	1.76	2.22	3.47	2.38	0.81	0.73	0.71	0.70	0.59	0.57

## Profitability & Per Share Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
<b>Return on Assets</b>	13.8%	12.1%	15.0%	13.2%	40.4%	4.3%	3.9%	4.4%	5.0%	4.4%
<b>Return on Equity</b>	53.1%	52.6%	82.8%	72.8%	105%	9.7%	8.7%	9.7%	10.6%	9.1%
<b>ROIC</b>	20.2%	17.4%	21.6%	18.8%	52.7%	5.5%	5.1%	5.7%	6.4%	5.8%
<b>Shares Out.</b>	1900	1860	1860	1860	2290	2290	2290	2300	2300	2270
<b>Revenue/Share</b>	12.51	12.32	10.75	10.27	12.32	14.26	14.42	14.42	15.38	15.11
<b>FCF/Share</b>	3.05	2.67	3.38	2.86	2.75	5.44	4.56	5.05	5.37	5.32

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

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