



Organon & Co. (OGN)

Updated February 18th, 2023 by Nathan Parsh

Key Metrics

Current Price:	\$26	5 Year CAGR Estimate:	9.5%	Market Cap:	\$6.6 B
Fair Value Price:	\$30	5 Year Growth Estimate:	3.0%	Ex-Dividend Date:	02/24/23
% Fair Value:	86%	5 Year Valuation Multiple Estimate:	3.0%	Dividend Payment Date:	03/16/23
Dividend Yield:	4.3%	5 Year Price Target	\$35	Years Of Dividend Growth:	1
Dividend Risk Score:	B	Retirement Suitability Score:	A	Rating:	Hold

Overview & Current Events

On June 3rd, 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.

On February 16th, 2023, Organon released fourth quarter and full year results for the period ending December 31st, 2022. For the quarter, revenue of \$1.49 billion was down 6.9% from the prior year and was \$10 million less than expected. Adjusted earnings-per-share of \$10.81 compared unfavorably to \$1.13 in the prior year and was \$0.10 below estimates. For the year, revenue increased 4% to \$6.2 billion while adjusted earnings-per-share of \$5.03 was down from \$6.20 in 2021. Currency exchange was an 8% and 6% headwind to quarterly and full year revenue results, respectively.

For the quarter, Established Brands, which contributed 60% of quarterly revenue, fell 14%. The decrease was mostly due to currency exchange. Women's health, which contributed ~29% of sales, was up 4% due to strength in Nexplanon. Sales for Biosimilars were higher by 13% due to double-digit growth in Renflexis, Ontruzant, Hadlima, and Aybinto.

Organon offered guidance for 2023 as well, with the company expecting revenue of \$6.15 billion to \$6.45 billion. The company is projected to earn \$4.30 per year 2023. We have initiated our forecast accordingly.

Growth on a Per-Share Basis

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
EPS	---	---	---	---	---	---	---	---	\$6.20	\$5.03	\$4.30	\$4.98
DPS	---	---	---	---	---	---	---	---	\$0.56	\$1.12	\$1.12	\$1.30
Shares¹	---	---	---	---	---	---	---	---	253	255	255	255

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 2028.

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

¹ In millions of shares

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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, including geographically.

Valuation Analysis

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	Now	2028
Avg. P/E	---	---	---	---	---	---	---	---	4.7	5.6	6.0	7.0
Avg. Yld.	---	---	---	---	---	---	---	---	1.8%	4.0%	4.3%	3.7%

Shares of Organon have increased \$2, or 7.7%, since our November 7th, 2022 report. Using the current share price and expected earnings-per-share for 2023, Organon trades with a price-to-earnings ratio of 6.0. This is an incredibly low valuation relative to other healthcare companies. 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, implying a 3.0% contribution from multiple expansion to annual returns over the next five years.

Even at the targeted low payout ratio, Organon's dividend yield is quite substantial at 4.3%. We believe that dividend growth will match earnings-per-share growth over the next five years.

Safety, Quality, Competitive Advantage, & Recession Resiliency

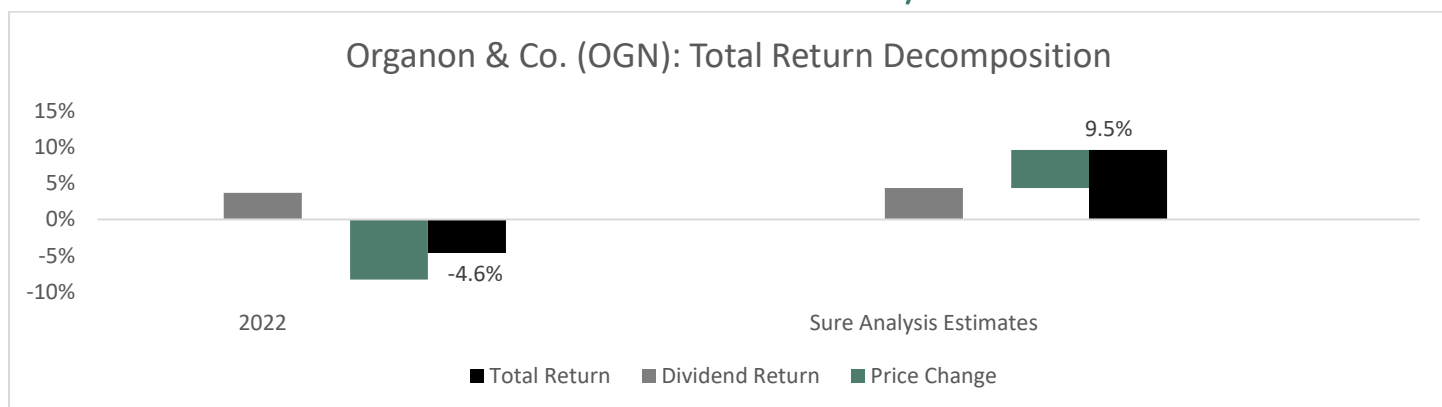
Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
Payout	---	---	---	---	---	---	---	---	9%	22%	26%	26%

Organon has not yet been tested during a recession. Its former parent company generated of earnings-per-share growth of 33% from 2007 through 2009. Including 2006 in this calculation actually results in 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 than 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 9.5% annually through 2028, down from our prior estimate of 14.0%. Our projected return stems from an earnings growth rate of 3%, a 4.3% starting dividend yield, and a low single-digit contribution from multiple expansion. Organon had a mixed quarter among its businesses and currency exchange remains a headwind. We have lowered our five-year price target \$5 to \$35 due to earnings estimates for the year. We now rate shares of Organon as a hold due to projected returns.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Revenue	---	---	---	---	---	---	9,777	9,530	8,096	6,304
Gross Profit	---	---	---	---	---	---	5,084	5,909	4,749	3,922
Gross Margin	---	---	---	---	---	---	52.0%	62.0%	58.7%	62.2%
SG&A Exp.	---	---	---	---	---	---	2,013	1,922	1,666	1,668
D&A Exp.	---	---	---	---	---	---	1,673	354	157	195
Operating Profit	---	---	---	---	---	---	2,706	3,655	2,779	1,811
Op. Margin	---	---	---	---	---	---	27.7%	38.4%	34.3%	28.7%
Net Profit	---	---	---	---	---	---	2,153	3,218	2,160	1,351
Net Margin	---	---	---	---	---	---	22.0%	33.8%	26.7%	21.4%
Free Cash Flow	---	---	---	---	---	---	3,586	2,658	1,909	1,970
Income Tax	---	---	---	---	---	---	576	337	520	178

Balance Sheet Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Total Assets (\$B)	---	---	---	---	---	---	10,548	10,548	10,109	10,681
Cash & Equivalents	---	---	---	---	---	---	319	319	12	737
Acc. Receivable	---	---	---	---	---	---	1,474	1,474	1,038	1,382
Inventories	---	---	---	---	---	---	1,071	1,071	913	915
Goodwill & Int.	---	---	---	---	---	---	5,172	5,172	5,106	5,254
Total Liabilities	---	---	---	---	---	---	3,513	3,513	4,623	12,189
Accounts Payable	---	---	---	---	---	---	258	258	259	1,382
Long-Term Debt	---	---	---	---	---	---	---	104	1,339	9,134
Total Equity	---	---	---	---	---	---	7,035	7,035	5,486	(1,508)
LTD/E Ratio	---	---	---	---	---	---	---	0.01	0.24	(6.06)

Profitability & Per Share Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Return on Assets	---	---	---	---	---	---	---	---	20.6%	13.0%
Return on Equity	---	---	---	---	---	---	---	---	69.5%	67.9%
ROIC	---	---	---	---	---	---	---	---	68.4%	18.7%
Shares Out.	---	---	---	---	---	---	---	---	---	253
Revenue/Share	---	---	---	---	---	---	38.62	37.65	31.98	24.80
FCF/Share	---	---	---	---	---	---	14.17	10.50	7.54	7.75

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

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