Organon & Co. (OGN)

Updated November 12th, 2023 by Nathan Parsh

Key Metrics

Current Price:	$11.12	**5 Year CAGR Estimate:**	21.6%	**Market Cap:**	$2.8 B
Fair Value Price:	$20.20	**5 Year Growth Estimate:**	3.0%	**Ex-Dividend Date:**	11/10/23
% Fair Value:	55%	**5 Year Valuation Multiple Estimate:**	12.7%	**Dividend Payment Date:**	12/14/23
Dividend Yield:	10.1%	**5 Year Price Target**	$23	**Years Of Dividend Growth:**	1
Dividend Risk Score:	B	**Retirement Suitability Score:**	A	**Rating:**	Buy

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 November 2nd, 2023, Organon reported third quarter results for the period ending September 30th, 2023. For the quarter, revenue of $1.52 billion was 1.3% lower from the prior year and $50 million less than expected. Adjusted earnings-per-share of $0.87 compared unfavorably to $1.32 in the prior year and was $0.19 below estimates.

Excluding the impact of currency exchange, revenue was down 1% for the period. For the quarter, Established Brands, which contributed 62% of quarterly revenue, grew 3% as volume gains and favorable pricing in several products. Women's Health, which contributed ~28% of sales, declined 7%, primarily due to the negative impact of generic competition to the company's Nuva Ring product. Fertility products were lower by 10% for the period. Sales for Biosimilars grew 10% due to improvements in volume in the U.S. and Canada.

Organon provided updated guidance for 2023 as well, with the company now expecting revenue of $6.15 billion to $6.25 billion, compared to $6.25 billion to $6.45 billion and $6.15 billion to $6.45 billion previously. We now project that the company will earn $4.04 per share in 2023, down from $4.35 and $4.30 previously.

Growth on a Per-Share Basis

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
EPS	---	---	---	---	---	---	---	---	$6.20	$5.03	***$4.04***	***$4.68***
DPS	---	---	---	---	---	---	---	---	$0.56	$1.12	***$1.12***	***$1.30***
Shares[1]	---	---	---	---	---	---	---	---	253	255	***256***	***256***

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.

On August 16th, 2022, the Inflation Reduction Act of 2022 was signed into law. The law will, in part, require the federal government to negotiate prices for drugs covered under Medicare starting in 2026. This could reduce the profits pharmaceutical companies could collect, but these costs could be shifted to employer sponsored plans, reducing the negative impact on businesses. As such, we maintain our expected growth rates, but we will monitor the situation as we get closer to the implementation of the law.

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[1] In millions of shares

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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 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	***2.8***	***5.0***
Avg. Yld.	---	---	---	---	---	---	---	---	1.8%	4.0%	***10.1%***	***5.5%***

Shares of Organon have fallen almost 50% since our August 18th, 2023 report. Using the current share price and expected earnings-per-share for 2023, Organon trades with a price-to-earnings ratio of 2.8. 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 lowered our target price-to-earnings ratio to 5 from 7 given the weakness in one of the company's key businesses, but this still implies a 12.7% annual tailwind to returns due to multiple expansion. Organon's dividend yield is quite substantial at 10.1%. The high yield could be a warning sign, but the dividend looks safe.

Safety, Quality, Competitive Advantage, & Recession Resiliency

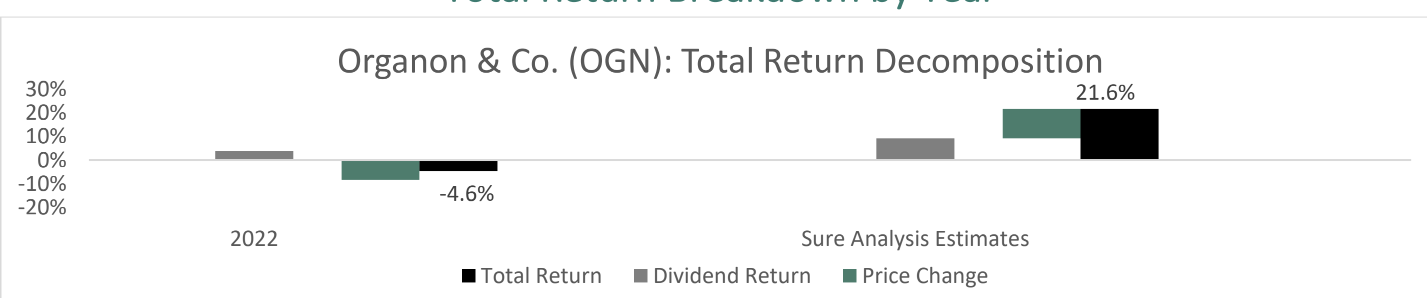
Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
Payout	---	---	---	---	---	---	---	---	9%	22%	***28%***	***28%***

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 is 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 then it was during that period, 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 21.6% annually through 2028, up from our prior estimate of 13.5%. Our projected return stems from an earnings growth rate of 3%, a 10.1% starting dividend yield, and a low double-digit contribution from multiple expansion. We believe that the selloff in the stock is overdone and rate shares of Organon as a buy due to projected returns.

Total Return Breakdown by Year



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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Income Statement Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Revenue	---	---	---	---	---	9,777	9,530	8,096	6,304	6,174
Gross Profit	---	---	---	---	---	5,084	5,909	4,749	3,922	3,880
Gross Margin	---	---	---	---	---	52.0%	62.0%	58.7%	62.2%	62.8%
SG&A Exp.	---	---	---	---	---	2,013	1,922	1,666	1,668	1,704
D&A Exp.	---	---	---	---	---	1,673	354	157	195	212
Operating Profit	---	---	---	---	---	2,706	3,655	2,779	1,811	1,705
Op. Margin	---	---	---	---	---	27.7%	38.4%	34.3%	28.7%	27.6%
Net Profit	---	---	---	---	---	2,153	3,218	2,160	1,351	917
Net Margin	---	---	---	---	---	22.0%	33.8%	26.7%	21.4%	14.9%
Free Cash Flow	---	---	---	---	---	3,586	2,658	1,909	1,970	431
Income Tax	---	---	---	---	---	576	337	520	178	205

Balance Sheet Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Total Assets ($B)	---	---	---	---	---	10,548	10,548	10,109	10,681	10,955
Cash & Equivalents	---	---	---	---	---	319	319	12	737	706
Acc. Receivable	---	---	---	---	---	1,474	1,474	1,038	1,382	1,475
Inventories	---	---	---	---	---	1,071	1,071	913	915	1,003
Goodwill & Int.	---	---	---	---	---	5,172	5,172	5,106	5,254	5,252
Total Liabilities	---	---	---	---	---	3,513	3,513	4,623	12,189	11,847
Accounts Payable	---	---	---	---	---	258	258	259	1,382	1,132
Long-Term Debt	---	---	---	---	---	---	104	1,339	9,134	8,913
Total Equity	---	---	---	---	---	7,035	7,035	5,486	(1,508)	(892)
LTD/E Ratio	---	---	---	---	---	---	0.01	0.24	(6.06)	(9.99)

Profitability & Per Share Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Return on Assets	---	---	---	---	---	---	---	20.6%	13.0%	8.5%
Return on Equity	---	---	---	---	---	---	---	69.5%	67.9%	
ROIC	---	---	---	---	---	---	---	68.4%	18.7%	11.7%
Shares Out.	---	---	---	---	---	---	---	---	253	255
Revenue/Share	---	---	---	---	---	38.62	37.65	31.98	24.80	24.20
FCF/Share	---	---	---	---	---	14.17	10.50	7.54	7.75	1.69

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