



Organon & Co. (OGN)

Updated August 10th, 2024 by Nathan Parsh

Key Metrics

| | | | | | |
|-----------------------------|---------|--|------|----------------------------------|----------|
| Current Price: | \$20.15 | 5 Year CAGR Estimate: | 8.9% | Market Cap: | \$5.2 B |
| Fair Value Price: | \$21.85 | 5 Year Growth Estimate: | 3.0% | Ex-Dividend Date: | 08/16/24 |
| % Fair Value: | 92% | 5 Year Valuation Multiple Estimate: | 1.6% | Dividend Payment Date: | 09/12/24 |
| Dividend Yield: | 5.6% | 5 Year Price Target | \$25 | Years Of Dividend Growth: | N/A |
| 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. The company'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 August 6th, 2024, Organon announced second quarter results for the period ending June 30th, 2024. For the quarter, revenue of \$1.61 billion was unchanged from the prior year, but was \$10 million below expectations. Adjusted earnings-per-share of \$1.12 compared unfavorably to \$1.31 in the prior year, but was \$0.04 ahead of estimates.

Excluding the impact of currency exchange, revenue grew 2% for the year. For the quarter, revenue for Established Brands, which contributed 60% of the total, fell 1% as gains from recent licensing agreements and a recovery in certain injectable steroid products was offset by weaker volumes in China and price revisions in Japan. Women's Health, which contributed 28% of sales, continued to see a return to growth, with sales higher by 3% year-over-year. Growth continues to be driven by the ongoing higher demand for fertility products, offset by generic competition in some contraceptive items. Sales for Biosimilars increased 22% due to high uptake rates for Hadlima and continued demand for Ontruzant.

Organon provided updated guidance for 2024 as well, with the company now expecting revenue in a range of \$6.25 billion to \$6.45 billion, compared to its prior forecast of \$6.2 billion to \$6.5 billion. We project that the company will earn \$4.37 per share in 2024, compared to \$4.44 and \$4.22 previously. We have updated our forecast accordingly.

Growth on a Per-Share Basis

| Year | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 | 2023 | 2024 | 2029 |
|---------------------------|------|------|------|------|------|------|------|--------|--------|--------|---------------|---------------|
| EPS | --- | --- | --- | --- | --- | --- | --- | \$6.20 | \$5.03 | \$4.14 | \$4.37 | \$5.07 |
| DPS | --- | --- | --- | --- | --- | --- | --- | \$0.56 | \$1.12 | \$1.12 | \$1.12 | \$1.12 |
| Shares¹ | --- | --- | --- | --- | --- | --- | --- | 253 | 255 | 257 | 259 | 258 |

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 2029.

The company announced its 13th consecutive quarterly dividend of \$0.28 per share. We now expect a constant distribution through 2029 given that Organon has yet to raise its dividend since becoming a standalone company.

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 do not require much in the way of the research and

¹ In millions of shares

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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 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 | 2023 | Now | 2029 |
|-----------|------|------|------|------|------|------|------|------|------|------|------|------|
| Avg. P/E | --- | --- | --- | --- | --- | --- | --- | 4.7 | 5.6 | 3.5 | 4.6 | 5.0 |
| Avg. Yld. | --- | --- | --- | --- | --- | --- | --- | 1.8% | 4.0% | 7.8% | 5.6% | 4.4% |

Shares of Organon have gained 0.5% since our May 6th, 2024 report. Using the current share price and expected earnings-per-share for 2024, Organon trades with a price-to-earnings ratio of 4.6. 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 reaffirm our target price-to-earnings ratio of 5 from 7 given the weakness in one of the company's key businesses, but this still implies a 1.6% annual tailwind to returns due to multiple expansion. Organon's dividend yield is quite substantial at 5.6%. The high yield could be a warning sign, but the dividend looks very safe.

Safety, Quality, Competitive Advantage, & Recession Resiliency

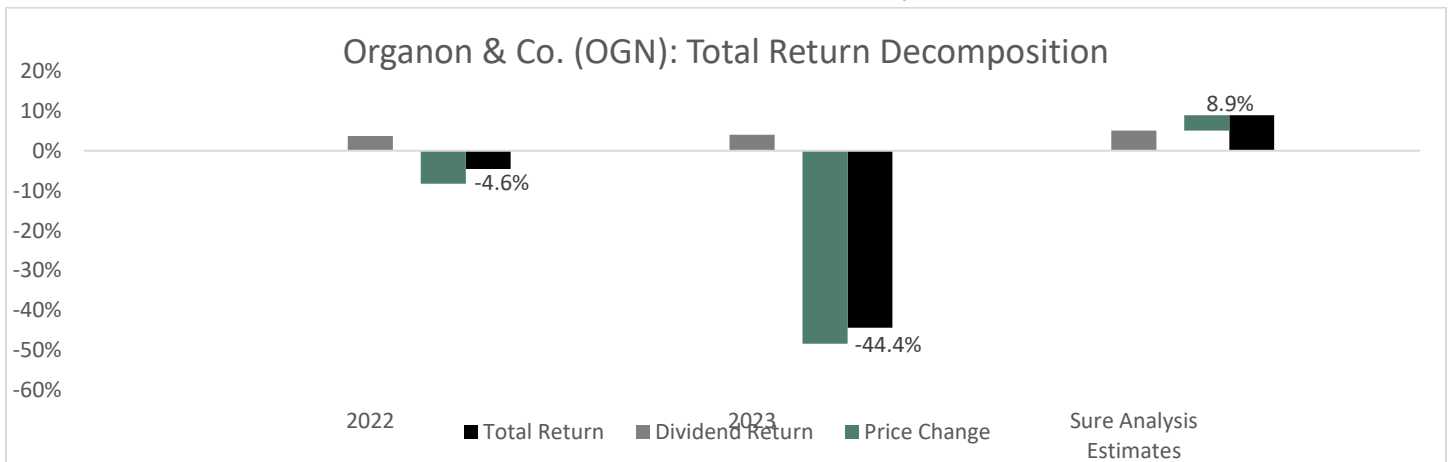
| Year | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 | 2023 | 2024 | 2029 |
|--------|------|------|------|------|------|------|------|------|------|------|------|------|
| Payout | --- | --- | --- | --- | --- | --- | --- | 9% | 22% | 27% | 26% | 22% |

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, 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 8.9% annually through 2029, down from our prior estimate of 9.3%. Our projected return stems from an earnings growth rate of 3%, a 5.6% starting dividend yield, and a small contribution from multiple expansion. We rate Organon as a hold due to projected returns.

Total Return Breakdown by Year



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Income Statement Metrics

| Year | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 | 2023 |
|------------------|------|------|------|------|-------|-------|-------|-------|-------|-------|
| Revenue | --- | --- | --- | --- | 9,777 | 9,530 | 8,096 | 6,304 | 6,174 | 6,263 |
| Gross Profit | --- | --- | --- | --- | 5,084 | 5,909 | 4,749 | 3,922 | 3,880 | 3,748 |
| Gross Margin | --- | --- | --- | --- | 52.0% | 62.0% | 58.7% | 62.2% | 62.8% | 59.8% |
| SG&A Exp. | --- | --- | --- | --- | 2,013 | 1,922 | 1,666 | 1,668 | 1,704 | 1,893 |
| D&A Exp. | --- | --- | --- | --- | 1,673 | 354 | 157 | 195 | 212 | 236 |
| Operating Profit | --- | --- | --- | --- | 2,706 | 3,655 | 2,779 | 1,811 | 1,705 | 1,327 |
| Op. Margin | --- | --- | --- | --- | 27.7% | 38.4% | 34.3% | 28.7% | 27.6% | 21.2% |
| Net Profit | --- | --- | --- | --- | 2,153 | 3,218 | 2,160 | 1,351 | 917 | 1,023 |
| Net Margin | --- | --- | --- | --- | 22.0% | 33.8% | 26.7% | 21.4% | 14.9% | 16.3% |
| Free Cash Flow | --- | --- | --- | --- | 3,586 | 2,658 | 1,909 | 1,970 | 431 | 538 |
| Income Tax | --- | --- | --- | --- | 576 | 337 | 520 | 178 | 205 | (350) |

Balance Sheet Metrics

| Year | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 | 2023 |
|--------------------|------|------|------|------|--------|--------|--------|---------|--------|----------|
| Total Assets (\$B) | --- | --- | --- | --- | 10,548 | 10,548 | 10,109 | 10,681 | 10,955 | 12,058 |
| Cash & Equivalents | --- | --- | --- | --- | 319 | 319 | 12 | 737 | 706 | 693 |
| Acc. Receivable | --- | --- | --- | --- | 1,474 | 1,474 | 1,038 | 1,382 | 1,475 | 1,744 |
| Inventories | --- | --- | --- | --- | 1,071 | 1,071 | 913 | 915 | 1,003 | 1,315 |
| Goodwill & Int. | --- | --- | --- | --- | 5,172 | 5,172 | 5,106 | 5,254 | 5,252 | 5,136 |
| Total Liabilities | --- | --- | --- | --- | 3,513 | 3,513 | 4,623 | 12,189 | 11,847 | 12,128 |
| Accounts Payable | --- | --- | --- | --- | 258 | 258 | 259 | 1,382 | 1,132 | 1,314 |
| Long-Term Debt | --- | --- | --- | --- | --- | 104 | 1,339 | 9,134 | 8,913 | 8,760 |
| Total Equity | --- | --- | --- | --- | 7,035 | 7,035 | 5,486 | (1,508) | (892) | (70) |
| LTD/E Ratio | --- | --- | --- | --- | --- | 0.01 | 0.24 | (6.06) | (9.99) | (125.14) |

Profitability & Per Share Metrics

| Year | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 | 2023 |
|------------------|------|------|------|------|-------|-------|-------|-------|-------|-------|
| Return on Assets | --- | --- | --- | --- | --- | --- | 20.6% | 13.0% | 8.5% | 8.9% |
| Return on Equity | --- | --- | --- | --- | --- | --- | 69.5% | 67.9% | | |
| ROIC | --- | --- | --- | --- | --- | --- | 68.4% | 18.7% | 11.7% | 12.2% |
| Shares Out. | --- | --- | --- | --- | --- | --- | --- | 253 | 255 | 257 |
| Revenue/Share | --- | --- | --- | --- | 38.62 | 37.65 | 31.98 | 24.80 | 24.20 | 24.44 |
| FCF/Share | --- | --- | --- | --- | 14.17 | 10.50 | 7.54 | 7.75 | 1.69 | 2.10 |

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

Disclaimer

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