# Group 37 – Philip Morris International (PM)

## Financial Analysis- FIN42030

**Trimester 1 – Autumn - 2025**

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## *Work Breakdown*

**Raw Data Collection:**
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**DCF Model:**
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**KVD and Economic Profit Model:**
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**Hypotheses and Scenario Analyses, and Sensitivity Analyses:**
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**Report:**
Basis for Conclusion (Robert), Company Background (Siddhi), Investor Perception (Rory), Industry and Stock Analysis (Rory), Accounting Analysis (Robert), Financial Analysis (Harshil), Model and Valuation (Robert, Rory), Key Value Drivers (Siddhi), Economic Profit Model (Navjot), Hypotheses, Scenario analyses, and sensitivity analyses (Harshil, Pavan) Conclusion (Robert).

**Meeting Minutes:**
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**Recommendation**: **Buy**

## *1. Basis For Conclusion*

Philip Morris International (PMI) is currently trading at $157.91 (3rd October 2025). Based on our $173.65 fair value estimate, our valuation implies the stock is undervalued, with an approximate 10% upside (Yahoo Finance, 2025). Our report supports a defensible downside due PMI's steady cashflows, healthy ROIC, and its mature risk profile. While historically a cigarette manufacturer, PMI are actively transforming to deliver a 'smoke-free future', expanding their portfolio to include products that provide a long-term solution to reduce the harm caused by smoking (*Annual Report Philip Morris International, 2024).* The acquisition of Swedish Match in 2022, has accelerated the company's smoke-free product shipment growth, which is currently the main driver of Phillip Morris International's organic revenue. (*Annual Report Philip Morris International, 2024)*.

## *2. Company Background*

PMI is one of the largest multinational tobacco and nicotine companies, distributed across 180 countries worldwide. Unlike Altria Group, which oversees the U.S. market, PMI operates independently and is responsible solely for international markets.

While it is headquartered in Stamford, Connecticut, its central operational and scientific hubs are based in Switzerland, highlighting its global orientation. The company operated 51 production sites across several continents, including 16 facilities dedicated exclusively to smoke-free products. Listed on the New York Stock Exchange under the symbol PM, the company is part of the S&P 100 index. PMI is particularly valued by investors for its consistent dividends, which remain among the highest in the sector *(Annual Report Philip Morris International, 2024, Corporate Profile, PMI, 2024)*.

### *2.1. Historical Development*

***Philip Morris International (PMI) Timeline***

| Year | Event |
|---|---|
| **1847** | Philip Morris opened his first tobacco store in London. |
| **1880s–1900s** | Expanded into U.S. market and began producing branded cigarettes. |
| **20th century** | Marlboro introduced, becoming the most recognized international cigarette brand. |
| **2003** | Parent entity rebranded as Altria Group to reflect diversification beyond tobacco. |
| **2008** | PMI separated from Altria, focusing solely on global operations outside the U.S. |
| **2010s** | Invested in Reduced-Risk Products (RRPs), such as heated tobacco devices. |
| **2020s** | Accelerated global launch of IQOS and expanded into wellness and oral nicotine products. |

Figure 1: PMI Historical Development

This timeline illustrates PMI's transformation from a traditional cigarette company to a broader nicotine and wellness enterprise centred on "smoke-free" alternatives. (Annual Report, PMI, 2008)

## *2.2. Product Portfolio*

### *2.2.1. Traditional Cigarettes*

- **Marlboro**: PMI's flagship brand, the most widely sold international cigarette brand.
- **Other global and regional brands**: L&M, Chesterfield, Parliament, Bond Street, and locally tailored labels.

Although cigarette consumption has declined worldwide, this segment remains highly profitable due to the strong pricing power of premium brands. (Annual Report, Philip Morris International, 2024, Product Portfolio Report, Philip Morris International, 2024)

### *2.2.2. Smoke-Free Alternatives (RRPs)*

- **IQOS Heated Tobacco**: The company's most important smoke-free product, launched in 2014; available in more than 70 countries.
- **Heets and Terea**: Tobacco consumables designed for use with the IQOS device.
- **Oral Nicotine Products**: Zyn, acquired via PMI's purchase of Swedish Match in 2022.
- **E-vapor Systems**: Pilot launches in selected markets to compete against rivals like British American Tobacco's Vuse. (IQOS Progress Report, Philip Morris International, 2024, Innovation Overview, Philip Morris International, 2024)

### *2.2.3. Diversification into Wellness*

PMI has expressed its ambition to expand into adjacent consumer health and wellness categories by leveraging its R&D capabilities and extensive distribution network. (Strategic Outlook Report, Philip Morris International, 2024)

## *2.3. Operations and Global Reach*

- **Regional Markets**: A significant portion of revenue comes from the European Union and Eastern Europe, with notable contributions from Asia, the Middle East, Africa, and Latin America. (Annual Report, Philip Morris International, 2024)
- **Production**: The company runs 51 manufacturing plants worldwide, 16 of which are exclusively for smoke-free products.
- **Research and Development**: Core facilities are located in Neuchâtel and Lausanne (Switzerland), supplemented by research sites in Italy, Hong Kong, and Armenia.

- **Distribution**: PMI relies on wholesalers, retailers, and direct-to-consumer digital platforms to expand its customer reach.(Market Access Report, Philip Morris International, 2024)

## *2.4. Financial Overview (2022–2024)*

| Year | Net Revenues | Operating Income | Net Earnings | EPS (Diluted) | % of Revenue from Smoke-Free | Dividend per Share |
|---|---|---|---|---|---|---|
| **2022** | ~$31.8B | ~$12.0B | ~$9.0B | $5.83 | ~30% | $5.04 |
| **2023** | ~$34.1B | ~$13.3B | ~$9.7B | $6.06 | ~36% | $5.20 |
| **2024** | ~$36.2B | ~$14.1B | ~$10.1B | $6.45 | ~40% | $5.40 |

*Figure 2: Financial Overview (2022-2024)*

**2.4 Key Insights-** Financial Overview (2022–2024)

- Net revenues grew approximately 7% CAGR from 2022-2024, led by smoke-free products.
- Strong profit margins supported by premium cigarette pricing and higher-margin IQOS.
- Dividend payout remains high, above 80%.
- Smoke-free products now account for 38% of revenues, reflecting successful business transformation. *(*Sustainability & Transformation Report, Philip Morris International, 2024)
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## *2.5. Strategic Priorities*

PMI’s overarching mission is to transition to a smoke-free future. Its strategy rests on five pillars:

1. **Accelerating RRPs**: Targeting smoke-free products to comprise the majority of net revenue by 2030.
2. **Scientific Credibility**: Heavy investments in clinical trials, toxicology studies, and product testing to secure regulatory acceptance.
3. **Geographic Expansion**: Rapid deployment of IQOS in high-potential regions such as Asia and Eastern Europe.
4. **Acquisitions and Partnerships**: The 2022 acquisition of Swedish Match strengthened PMI’s leadership in nicotine pouches and enhanced its U.S. footprint.

5. **Sustainability Goals**: Commitments to carbon neutrality, sustainable tobacco sourcing, and reduced environmental waste. (Regional Strategy report, science & innovation report, acquisition report sustainability Report, Philip Morris International, 2024)

### *2.6. Industry Environment*

PMI's operations are influenced by multiple external pressures:

- Regulation
- Public Health Concerns
- Competitive Rivalry
- Innovation Dynamics
- Global Uncertainty
  (World Health Organization Tobacco Report, 2024)

## *3. Investor Perception*

Philip Morris International has had a bullish investor sentiment in 2025. The company's strategic pivot to reduced risk products and its strong financial results have made it a strong performer. PM's stock price has repeatedly surpassed benchmarks, reflecting optimism about its growth prospects. However, some analysts worry that the recent rally has stretched valuations. Overall, investors view PMI with optimism. They are enthusiastic about its smoke-free vision and earnings momentum, but wary of regulatory risks.

### *3.1. Analyst Sentiment and Ratings*

Wall Street's view on Philip Morris is largely positive. The stock has a 'Moderate Buy' rating, with no sell ratings as of September 2025. Out of 13 analysts tracked, 12 have a buy recommendation and only 1 rate it a hold (MarketBeat, 2025), a strong bullish outlook on the stock. The average 12-month price target stands around $184, implying roughly 20% upside from its current price of $153 (MarketBeat, 2025). It has a high price target of $220, showing a strong confidence in PMI's smoke-free product growth. The low-price target of $135 does show that there exists a small minority of analysts who remain wary of the stock (MarketBeat, 2025). Overall, the main sentiment among analysts is that Philip Morris's risk to reward is favourable due to its growth, trajectory and dividend profile.

Recent commentary from analysts and investors show this optimism. For example, after PMI issued upbeat forecasts early in the year, Gaurav Jain, analyst at Barclays praised the company for over-delivering saying that investors believed management was being "conservative" and saying that investors were asking whether they would "beat and raise (expectations) throughout the year" (Reuters, 2025). In line with that view, PMI raised its earnings outlook again mid-year, due to the strong demand for smoke-free products like IQOS and ZYN, further reinforcing bullish sentiment (Reuters2, 2025). Some market observers expect the company to continue outperforming in the second half of 2025, saying that the expanding production capacity and ZYN's dominant ~61% U.S. market share in oral nicotine are reasons that it can continue to grow (Seeking Alpha Contributor, 2025).

### *3.2. Key Drivers of Market Sentiment*

There are several factors that are driving investors bullish perceptions of PMI. A major driver of positive sentiment is PMI's success in non-combustible products. The company's heated-tobacco device IQOS and nicotine pouch ZYN are experiencing rapid growth. Investors see this as securing the company's future in a declining cigarette market. In Q1 2025, "smoke-free net revenues jumped 20.4% in first-quarter 2025, and gross profit rose by a striking 33.1%" (Mohta, 2025). ZYN has been a standout. U.S. shipments jumped 53% year-on-year in early 2025 up to 202 million cans. This resulted in PMI raising its 2025 forecast to 800-840 million cans, up from 780-820 (Mohta, 2025). This smoke-free vision gives investors optimism that Philip Morris can transition toward its goal of two-thirds revenue from smoke-free products by 2030 (Hasson, 2025).

Despite declines in cigarette smoking, PMI has shown good pricing power and cost control in its business, increasing investor confidence. The company has consistently managed to grow revenue and earnings through higher pricing and operating efficiency. It beat consensus expectations in recent quarters and has raised its EPS guidance multiple times in 2025 (Reuters, 2025). 2024 Q4 had EPS of $1.55, and this has been raised in the first two quarters of 2025 which EPS of $1.69 (beating estimates of $1.61) and $1.91 (beating estimates of $1.86) respectively. (Yahoo Finance, 2025). This 'beat-and-raise' pattern has reinforced a bullish narrative that PMI can deliver on growth and profitability, even as it invests heavily in new products. In short, strong execution and earnings momentum have been key in driving the stock's rally.

Economic trends have also played a role in boosting PMI's stock. 2025 has had rising market volatility due to tariff worries, recession fears, and a tech sector pullback. This has resulted in investors choosing to invest in more high-dividend stocks (Hasson, 2025). PMI has a reliable dividend and thus benefited from investors who are looking for more stability. By April, the S&P 500 was down ~5%, yet PM's stock was up over 40% YTD (Hasson, 2025). Its 3%+ yield and status as a dividend growth stock made it attractive when bond yields and interest rates were rising.

Finally, there are also the risks of regulation and legal challenges in the tobacco industry. Investors remain aware that new regulations could change the outlook for PMI. An example of this is that Chuck Schumer, the US Senate minority leader, has expressed his desire to regulate ZYN more strongly in the United States. This would deter against the long-term vision of PMI (Politico Staff, 2024). At the same time, some regulatory developments are welcomed by investors. In January 2025, the FDA authorised the marketing of 20 ZYN nicotine pouch products, stating that they contain "substantially lower amounts of harmful constituents than cigarettes". This shows that government regulation is in line with Philip Morris' vision for the future. Philip Morris themselves acknowledge the risks on their website. They speak of "excise tax increases and discriminatory tax structures, increasing marketing and regulatory restrictions" (Philip Morris International, 2025). While no major new laws have passed in 2025, the health concerns around tobacco remain an issue that investors factor into their valuation.

## ***4. Industry and Stock Analysis***

PMI's recent stock performance is in line with the bullish investor perception. Year-to-date in 2025, PM shares have increased by over ~50% by June and have fallen slightly to a total gain of 37% on the year, making it one of the top performers in the S&P 500 (Mohta, 2025; Hasson, 2025). In April 2025 the stock had risen about 41% YTD which was the fourth-best return in the entire index, even with the S&P 500 down roughly 5% over the same period amid broad market uncertainty (Hasson, 2025). This rally has turned PMI into a market leader in a year when defensive, dividend-paying stocks came back in favour (Hasson, 2025).

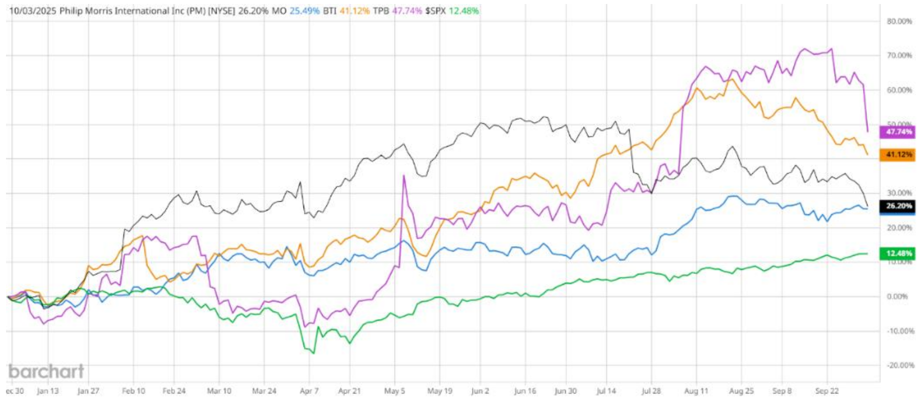

*Figure 3: PM and Competitors YTD (Barchart.com)*

As observed, Philip Morrus has performed well alongside its peers in the tobacco industry. YTD, PMI's share price gain 26% is a strong increase and the same can be said for other cigarette makers such as Altria (MO), which is up about 25%, British American Tobacco (BTI) about 41%, and smaller peer Turning Point Brands which is up 47% in the same period (Mohta, 2025).

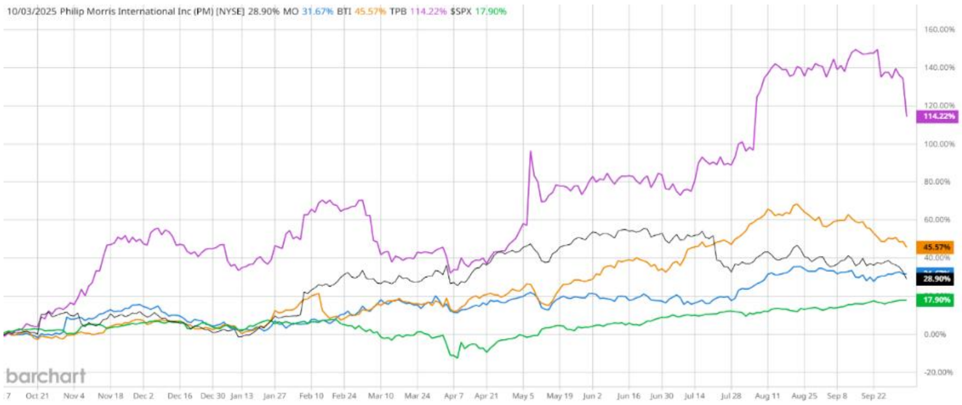

*Figure 4: PM and Competitors Oct 2024 to Oct 2025 (Barchart.com)*

The company's total 12-month return of around 28% is almost double the S&P 500's +17.9% return. (Seeking Alpha Contributor, 2025). Even after a pullback from its record highs of $186.69 (MarketWatch, 2025) in June 2025 back to the $160s, the stock has remained well ahead of the index. This relative strength shows investors' confidence in Philip Morris's earnings resilience and growth strategy compared to the average company. However, high expectations are now built into PMI's stock, which can mean large reactions to any news.

An example of this came after the 2025 Q2 results. Philip Morris dropped 8.4% in one day on July 22 after their total revenue of $10.14 billion was under the analysts' estimates of $10.32 billion (Kilgore, 2025). "ZYN shipments of 190 million cans were behind the 203 million expected by analysts" (Reuters2, 2025). Bernstein's Callum Elliot wrote that "These numbers risk being not quite 'good enough' for the higher bar that PMI is likely to be held to today", so even solid growth numbers are at risk of being judged not quite good enough for PM's high expectations. This clearly shows that the general sentiment is bullish, however the market is quick to punish any signs of underperformance.

# ***5. Accounting Analysis***

## *5.1. Revenue Recognition*

PMI recognises revenue net of excise taxes when control transfers upon shipment or delivery of goods. Accounting for variable considerations (discounts, rebates, trade promos) is estimated at the time of sale, updated as required as a revenue, and deducted after transfers are fulfilled. Warranty costs for IQOS and other devices are accrued in cost of sales (*Annual Report Philip Morris International, 2024)*.

2024 Net revenue increased by 7.7%, driven primarily by the company's smoke-free portfolio growth. In addition, Operating cashflow rose 32.7% to $12.2bn, supporting reinvestment into their SFP portfolio as well as higher shareholder returns through consistent dividend growth (*Annual Report Philip Morris International, 2024)*.

In 2021, PMI reorganised revenue reporting into four geographical segments categorized as; Europe Region; South and Southeast Asia, Commonwealth of Independent States (CIS), Middle east and Africa Region; Americas Region; East Asia, Australia and PMI Duty Free Region. PMI's largest distributors are located in the Europe Region and East Asia, Australia and PMI Duty Free Region; each individually accounting for more than 10% of total consolidated net revenues, indicating concentration risk. Disrupting any of these relationships may temporarily affect shipments and market share in these regions (*Annual Report Philip Morris International, 2024)*.

## *5.2. Special Items*

PMI's non-recurring items consist of a $199m pre-tax loss on the Vectura sale, the $45m Egypt sales-tax charge on 2014-2016 cut filler, $180m restructuring relating to U.S. IQOS sourcing, a $77m tax charge from Megapolis forced-localization in Russia, and a $27m impairment of non-amortizable intangibles (*Annual Report Philip Morris International, 2024)*.

## *5.3. Leases*

PMI rents offices, warehouses, retail space, Machinery, equipment and vehicles under operating and finance leases. Most leases are recognised as right-of-use (ROU) assets and lease liabilities; short term leases are expensed. PMI combines lease and non-lease components, except for vehicles. In 2024, PMI's ROU assets were $585m (operating) and $126m (finance), with lease obligations of $604m (operating) and $67m (finance). These commitments are manageable relative to the company's capital structure; therefore, they are not material to PMI's profitability and financial position (*Annual Report Philip Morris International, 2024)*.

## *5.4. Off Balance Sheet Issues and Investment*

PMI reports no off-balance-sheet arrangements other than guarantees. These guarantees are a minor implication in valuation and relate to excise tax obligations; there is no recorded liability, and they are not expected affect liquidity. PMI sells trade receivables to banks; 11.9bn sold in 2024 with $0.9bn outstanding at 2024 year-end, therefore boosting operating cash flow while outstanding. Notably, PMI sponsors a supply-chain financing program for suppliers, where a bank pays suppliers in advance and later pays an invoice amount. Therefore, this liability from buying the purchase of goods remains a trade payable. Furthermore, trade payables is a component of operating activities and is included in Cash Flow from Operations. PMI also uses Account Receivable sales to manage cash and credit exposure. (*Annual Report Philip Morris International, 2024)*.

## *5.5. Goodwill & Intangibles*

Year-end goodwill was $16.6bn, driven by the Swedish Match acquisition. Other intangibles totalled $11.3bn, approximately $4.45bn indefinite-lived, and $6.88bn amortizable (trademarks, technology, customer relationships, and the IQOS U.S. reacquired commercialisation rights, amortized straight-line over five years). At acquisition Swedish Match's identifiable intangibles were $7.9bn, including the $3.133bn ZYN trademark. 2024 amortization was $835m, and management is guiding roughly $1bn per year over the next five years. Intangibles are central to PMI's value, while goodwill risk is mostly concentrated in Wellness & Healthcare (*Annual Report Philip Morris International, 2024)*.

## *5.6. Liquidity and Solvency*

At 2024 year close, PMI attained $4.25bn in cash against $45.7bn of predominantly fixed rate debt, with manageable near-term maturities (2025: $3.4bn; 2026: $5bn). Liquidity is supported by $6.2bn of undrawn revolving credit, and a new €1.5bn revolver effective Jan 29, 2025, keeps total committed capacity at roughly $6.1bn. These credit lines have no ratings triggers and no collateral requirements, making this funding reliable. Capital allocation remains income focused, with dividends prioritised, and investment tilted toward smoke-free capacity *(Annual Report Philip Morris International, 2024)*.

## ***6. Financial Analysis***

### ***6.1. Income Statement and Profit and Loss account***

Net revenues increased by 7.68% in 2024, driven by smoke- free product shipment volume growth, positive product mix and favourable pricing. PMIs' Operating Income rose 16% (21.5% excluding currency and acquisitions) due to higher product earnings and the absence of 2023 one-time costs like a $665M goodwill impairment, a $204M South Korea tax, a $140M pledge termination, and $53M from the Ukraine war. These gains were partially offset by higher 2024 costs, including amortization, restructuring, a $199M loss on the sale of Vectura Group, a $45M Egypt tax, increased marketing, administration, and research expenses due to inflation and higher wages, higher manufacturing costs from tobacco leaf, EU plastics rules, partly balanced by productivity improvements. The adjusted Diluted EPS increased by 15%, due to strong operational performance. SSEA, CIS & MEA saw gains from favourable pricing and higher volumes, Europe benefited from higher prices and smoke-free product growth, East Asia, Australia & PMI GTR from improved volume/mix and lower manufacturing costs, and the Americas from improved volume/mix and pricing. These operational improvements added approximately +$1.04 per share. Additional contributions came from fair value gains on equity investments in India and Sri Lanka (+$0.27 per share) and a U.S. tax deduction (+$0.03 per share). (Annual Report Philip Morris International, 2024).

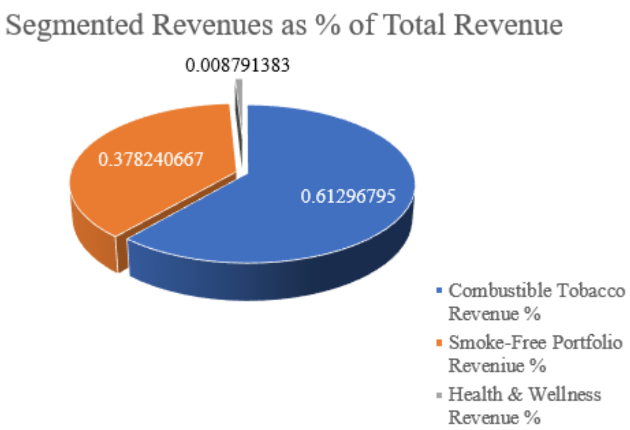


*Figure 5: Segmented Revenues*

### *6.2. Cashflow Statement*

Operating cashflow increased by 32.73%. This increase was driven by higher net earnings, improved receivables and payables. Investing cashflow decreased by $2,506 million but remained negative. The improvement mainly reflects PMI's termination of the IQOS U.S. agreement with Altria and reacquisition of the rights, ending ongoing payments to Altria. Partially offsetting this, capital expenditures rose to $1,444 million from $1,321 million. Financing activities are low, with a negative value of $9481 million. A major reason for this was the short and long-term repayments. This debt was acquired when PMI decided to acquire Swedish match (2022) and to reacquire the IQOS U.S. rights (2022-2023). (*Annual Report Philip Morris International, 2024)*.

### *6.3. Balance Sheet*

PMI's total assets fell in 2024 due to debt repayments, amortization of intangibles, and currency effects. The company used cash to repay short and long-term debt, reducing cash, while regular amortization and depreciation lowered the value of intangible and fixed assets. A stronger U.S. dollar also reduced the USD value of foreign assets. PMI's total liabilities and equity slightly decreased in 2024 compared with 2023, reflecting a mix of debt repayments, operational performance, and retained earnings changes. The company repaid a significant portion of short-term and long-term debt, reducing total liabilities. Equity was affected by net income and dividends paid. (*Annual Report Philip Morris International, 2024)*.

### *6.4. Ratios*

PMI's current ratio in 2024 was 0.88 since short-term debts exceeded short-term assets. At year-end, it held approximately $2,0170 million in current assets yet held $22,915 million in current liabilities. The gap came mainly from near-term bills like $6,904 million in taxes payable, $2120 million in dividends payable, and over $3392 million in current debt. Furthermore, cash was relatively small at $4216 million. A debt-assets ratio of 1.16 means PMI has $1.16 in liabilities for every $1 of assets. This indicated negative equity because liabilities exceed assets (*Annual Report Philip Morris International, 2024)*.

## *7. Valuation and Model*

Using a WACC of 5.90% (Bloomberg, 2025), our FCFF model values PMI at $173.65 per share, a 13% increase of its current share price (04/10/2025) of $153.27. Our FCFE model yields $193.36 per share, using the PMI's cost of equity of 6.3% (Bloomberg, 2025) to discount FCFE. This figure of $193.36 is much closer to the average 12-month price target which stands around $184 (MarketBeat, 2025), an 26% increase from current share price of 153.27.

Historically, PMI's FCFE exceeds FCFF because FCFE = FCFF – after-tax interest each year. PMI's net Borrowing raised significantly in 2023 and 2024, partially due to the financing of the Swedish Match deal, which exceed after tax interest, therefore making FCFE greater than

FCFF during these years. Since our equity level forecasts were assumed constant from 2024 onwards (Koller, Goedhart and Wessels, 2015), net borrowing is equal to zero for forecast years (2025-2039). We predict a decrease of 0.9% in debt yearly from 2025 onwards. The FCFE figure is dominated by the large yearly changes in debt. PMI's debt in 2022 surged due to the acquisition of Swedish Match through cash on hand and debt proceeds. The report's MD&A section documents cash used in investing to acquire Swedish Match and the offsetting net cash provided by financing activities, linking the transaction to surges in debt (*Annual Report Philip Morris International, 2024)*. Therefore 2022's debt surge is treated as an outlier and excluded from estimating the future growth rate. Using this assumption results a slightly negative debt growth rate across the forecasted years.

The Discounted Cashflow (DCF) model is a valuation technique that estimates a company's intrinsic value through explicit, evidence-based assumptions regarding the business's operating performance and how it translates to cashflows generated by a company. The DCF model was selected to value PMI due to its theoretical underpinnings and ability to be applied to various scenarios. However, DCF is assumption-sensitive; errors in key inputs (both historical and forecasted), can vary results significantly. To Mitigate this, throughout our model we have justified and referenced forecasted inputs (Harvard Business School, 2025)

## *7.1. Assumptions and Segment growth*

For our DCF model we applied a WACC of 5.90% to discount FCF from years 2025 onwards (Bloomberg, 2025). Separate year-over year growth rates by revenue segments (Combustible Tobacco, Smoke-Free products, Health & wellness) from 2024-2034. Firstly, Management's Q2'25 guidance calls for 12-14% SFP volume growth and roughly flat combustibles. With H1'25 combustible volume down 1.5% YoY and pricing up 7.7%, Considering CAGR for the previous 4-years is equal to 1.67%, we assumed a conservative 3% combustibles revenue growth for 2025, and 13% for the smoke-free portfolio (*Philip Morris International, 2025a; Philip Morris International, 2025b; Philip Morris International, 2024c*). A 2.85% growth rate for PMI's combustible revenue stream was assumed for the remaining detailed forecasted years (2026-2029). Two SkyQuest articles reported an average 2.85% CAGR global combustible tobacco revenue for the years 2025-2033, assumed to be driven primarily by favourable pricing considering the company's guidance on declining overall cigarette industry volume (SkyQuest, 2025; SkyQuest, 2025; *Annual Report Philip Morris International, 2024*). For SFPs beyond 2025, we reference category growth of approximately 15.2% CAGR (2026–2033) *(Verified Market Research, 2025)*. The Health & Wellness segment grows 10.9% (average 2023–2024) but remains immaterial to the mix. The weighted blend across combustibles, SFP, and H&W yields 6.65% total revenue growth, is consistent with management's 6 - 8% organic net revenue growth guidance *(Philip Morris International, 2024; Philip Morris International, 2025b).*

## *7.2. Economic Profit Model*

This analysis applies the Economic Profit (EP) method to calculate the real value created by PMI for the years 2015-2034. Economic Profit approximates the difference between Net

Operating Profit After Tax (NOPAT) and the cost of capital employed (Invested Capital WACC), thus reflecting the profit earned over the expected return from shareholders.

### *7.2.1 Key Findings*

The model illustrates PMI in order to consistently produce positive and rising Economic Profit, ensuring that the company is, in fact, building value for owners:

- **Strong Value Creation:** PMI Economic Profit is positive over the entire period of 10 years i.e., the return on capital employed of the company is greater than its WACC.
- **Accelerating Growth:** The calculated EP shows higher growth, increasing from approximately 6,471.67 in 2016 to a forecasted 17,826 by 2034. This suggests expansion of PMI's core operating profitability.
- **Capital Efficiency:** The positive and growing EP shows the management is taking right capital allocation decisions ensuring higher returns with more debt/capital.

The Economic Profit model also verifies that PMI is a powerful driver of value, effectively allocating capital at rates of return substantially above the cost required by the market. The rapid growth in EP reflects that strategic initiatives seemingly linked to the shift away from smoke-containing products and growth outside the US are propelling underlying, value-driven growth (*Annual Report Philip Morris International, 2024; Philip Morris International, 2025d; Copenhagen Business School, 2019*).

## *7.3. Key Value Drivers*

### *7.3.1. Overview*

This report reviews the company's performance from 2015 to 2034, focusing on key drivers such as NOPLAT, Invested Capital, ROIC, and Enterprise Value (EV). The purpose is to understand how effectively the business has created value and maintained growth.

### *7.3.2. Assumptions*

**Growth Rate (g):** 5.88%
**WACC:** 5.90%
**Capital Spread (WACC – g):** 0.02%

The small difference between the cost of capital and growth rate indicates that the company operates as a mature, low-risk business that continues to generate stable value.

### *7.3.3. Performance Summary*

- NOPLAT grew steadily from $7,653 million in 2015 to $19,618 million in 2034, showing consistent operational improvement.

- Invested Capital increased from $30,908 million to $103,442 million, reflecting ongoing reinvestment to support expansion.

- ROIC reached a peak of 40 percent in 2020 before stabilizing around 19 percent in later years, signalling a transition from a rapid growth phase to maturity.

- The Growth Efficiency Factor remained between 68 percent and 85 percent, highlighting effective capital management.

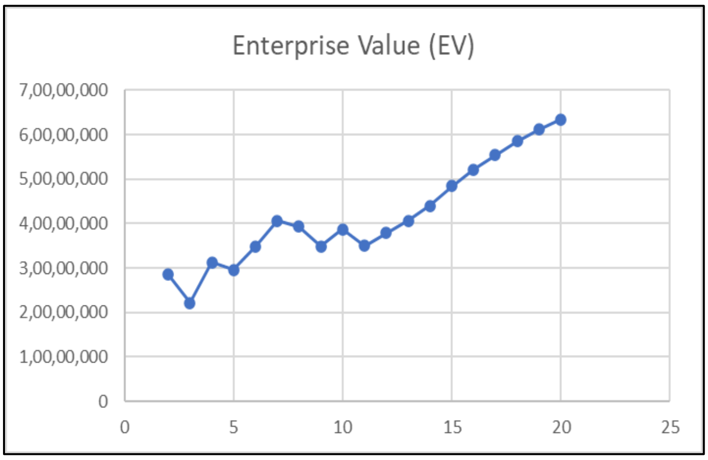


Figure 6: Enterprise Value

### *7.3.4. Key Insights*

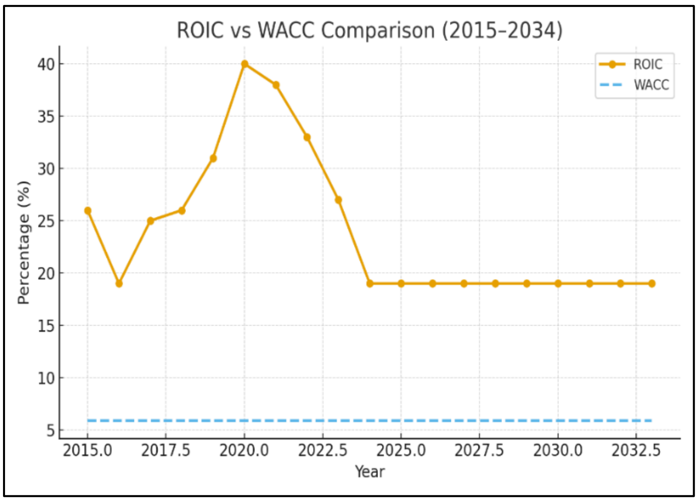


Figure 7: ROIC vs WACC Comparison (2015-2034)

**Consistent Value Creation:** ROIC has remained above WACC throughout the period, confirming ongoing value creation.

**High Operational Efficiency:** The strong ROIC during 2018 to 2020 demonstrates excellent reinvestment efficiency.

**Stability and Predictability:** After 2024, the company's performance becomes more stable, resulting in predictable cash flows and steady growth in enterprise value.

**Sustainable Valuation:** The close alignment between WACC and growth rate suggests a balanced and mature business model with minimal risk exposure.

### *7.3.5. Strategic Implications*

To maintain long-term value creation, the company needs to keep ROIC above WACC through operational efficiency. It should optimize capital allocation to achieve the right balance between reinvestment and shareholder returns. Enhancing growth efficiency through innovation and productivity improvements will further support enterprise value growth.

### *7.3.6 Methodology*

This analysis looks at how effectively the company turns its operations and investments into long-term value. It focuses on key financial indicators such as NOPLAT, Invested Capital, ROIC, WACC, Growth Rate, and Enterprise Value.

NOPLAT reflects the company's true operating profit after tax, while ROIC measures how efficiently that profit is generated from the capital invested in the business. WACC represents the overall cost of funding, combining both equity and debt. Comparing ROIC and WACC helps determine whether the company is creating value or simply covering its capital costs.

Enterprise Value is estimated by projecting future cash flows and discounting them at the company's cost of capital.

### *7.3.7 Value Creation Summary*

The analysis covers the period 2015-2034, combining historical performance with future projections to evaluate profitability, capital efficiency, and the company's ability to sustain growth. The Value Creation Summary pie chart shows how the company's enterprise value is created. Around 70% of the value comes from a strong ROIC, reflecting efficient use of invested capital. 20% comes from growth, showing the impact of revenue and profit increases. The remaining 10% is from the capital spread, highlighting the extra return earned over the cost of capital. The chart

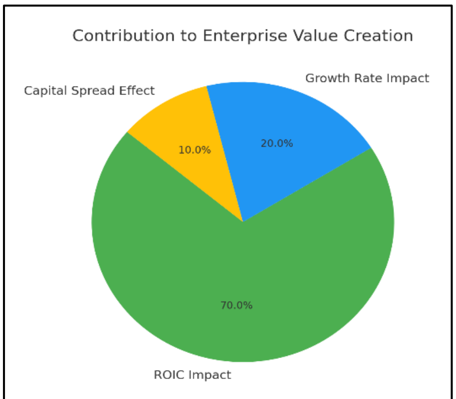


*Figure 8: Capital Spread, Growth Rate, ROIC Contribution to Value Creation*

emphasizes that maintaining high returns and steady growth are the main drivers of long-term value.

### *7.3.8 Key Value Driver Conclusion*

The company demonstrates strong financial fundamentals, efficient capital utilisation, and consistent growth in enterprise value. Despite entering a more mature stage, it continues to generate returns above its cost of capital, ensuring financial stability, long-term growth, and sustained confidence among shareholders.

## *7.4. Hypotheses for Scenario analyses*

### *7.4.1 Hypothesis 1 and Scenario Analysis 1*

<u>What would the financials of the company look like if they didn't buy back the IQOS rights from Altria.</u>

The re-acquiring of the US IQOS rights lifted PMI's debt ratio to approximately 1.16 (high), enabling a full U.S. rollout without self-cannibalization but increasing leverage and near-term balance-sheet pressure. The major downside of this acquisition an immediate balance-sheet strain despite the long-term profit potential.

Had PMI not reacquired the rights, the debt ratio would be lower, improving financial flexibility. The incremental debt taken to finance the obligation would create additional interest payments, which reduces the net income, this would have been avoided. With U.S. expansion, PMI would rely on Altria's marketing and execution team, regulatory efforts and decision speeds. From a valuation standpoint, investors typically reward firms that control core assets; PMI's move away from dependence on Altria enhances strategic control and can support a higher valuation.

### *7.4.2 Hypothesis 2 and Scenario Analysis 2*

<u>*A Smoke-Free Future*</u>

#### *7.4.2.1 Background*

ZYN nicotine pouches began early in 2010s in Sweden, where they were developed by Swedish Match as a "tobacco-free nicotine alternative".

#### *7.4.2.2 Testing*

*Test Logic:*

| Scenario | SF Rev CAGR | Comb Rev CAGR | First year SF ≥ 50% | Year-10 SF Mix | Year-10 Total Revenue | Year-10 Total EBIT |
|---|---|---|---|---|---|---|
| Bear | +10% | −1% | 2029 (Year 5) | 64.4% | $59,022m | $14,926m |
| Base | +15% | −3% | 2027 (Year 3) | 77.6% | $76,429m | $20,544m |
| Bull | +20% | −5% | 2026 (Year 2) | 86.7% | $104,672m | $30,290m |

*Figure 9: Bear, Base, Bull scenarios for Hypothesis 2*

1. *Smoke-free share ≥ 50% in any year of the forecasting period*
2. *Smoke-free CAGR > Combustible CAGR*

#### *7.4.2.3 Findings*

- **Bear:** SF share climbs from ~41% in Year 1 (2025) to 51.7% by 2029.
- **Base:** SF crosses 50% by 2027 and reaches ~78% by 2034; total EBIT margin trends up from ~25% to ~27%.
- **Bull:** SF crosses 50% as early as 2026 and reaches ~87% by 2034; total EBIT margin improves from ~25.5% to ~28.9%.

#### *7.4.2.4 Interpretation*

- *Resilience of the findings:* Under a conservative Bear estimate, (where: Smoke Free +10% CAGR & Combustible (Smoke) -1%), smoke free manages to overtake combustibles within 5 years. This supports the major thesis that PMI's revenue engine is tilting towards *smoke-free.*
- *Outcomes:* By Year-10, total revenue ranges from $59 billion to $105 billion across the Bear & Bull scenarios. With the total EBIT in the range of $15 billion to $30 billion. Highlighting how sensitive the long-run level is to smoke-free growth and combustibles decline.

#### *7.4.2.5 Limitations*

- *Constant Margins:* We used constant EBIT margins for clarity. Margins might end up varying, given the success of the brand there might be expansions which could increase the margins but could also lead to debt accumulation.
- *FX & Taxation:* Long duration results are sensitive to FX and taxes. Given the addictive nature of nicotine there is a possibility that ZYN gets taxed like tobacco products soon. This would increase taxes and selling restrictions that could hurt the growth.

#### *7.4.2.6 Scenario Conclusion*

Under all three scenarios we tested, smoke-free becomes the primary revenue driver for PMI within the forecasted period of 10 years. The consolidated finances improve along as the revenue-mix concentrates to smoke-free.

## *7.5. Sensitivity Analysis*

### *7.5.1 WACC Sensitivity*

Under the current assumption of WACC of 5.90%, the price per share is at $173.64, which is higher than the current price of $157 the stock is trading at. Therefore, the recommendation would be: **Buy**.

Under the sensitivity analysis we adjust the WACC lies between the lower and upper limit of **4% - 10%**:

- When considering the WACC to be at 4% - the lower extreme, the price per share was coming at $352.73, the recommendation here would be: **Buy**.
- When we consider the upper limit of the WACC which is at 10%. The share price falls to $63.16. This is a major drop compared to the market price of $157.91. Therefore, the recommendation would be to: **Sell**.

### *7.5.2 Cost of Equity Sensitivity*

Moving to the sensitivity analysis, we test the price in the following band for Cost of Equity: 5% - 9%

- At the lower limit of 5%, we see a significant rise in the price of the stock. It moves to $275.80. Where the recommendation would be: **Buy.**
- At the upper limit of 9%, the price of the share falls steeply to $115.00. Considering this drop, the recommendation would be to: **Sell.**

## ***8. Conclusion***

We recommend **buy** on Philip Morris International. Despite near-term regulation risks, PMI has demonstrated steady growth as it pivots toward a smoke-free portfolio. At $157.91, PMI trades below our base case intrinsic FCFF valuation of $173.65 at a 5.9% WACC, implying an approximate 10% upside, with a defensible downside given the company's stable cashflows, healthy ROIC, and mature risk profile. With the FCFE valuation cross-check at a cost of equity at 6.3% is $193.36, highlights a reasonable fair value range and implying an approximate 10%-22.4% upside from the current price. Fundamentally, PMI's future growth relies on a mix shift to smoke-free with the category growth outpacing combustibles, our scenario work shows smoke-free surpassing at least 50% of total revenue by 2029. Strong cash generation, disciplined capital allocation, and a transition to reduced-risk products positions PMI's share value to increase (*Bloomberg, 2025; Annual Report Philip Morris International, 2024)*.

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# *Appendices*

## *Appendix 1: Base Financial Forecast*

### *Appendix 1.1: Base Stock Valuation*

| FCFF Valuation Model | 2024 | 2025 | 2026 | 2027 | 2028 | 2029 | 2030 | 2031 | 2032 | 2033 | 2034 | CV |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| t | | 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 | 10 | 11 |
| g | | | | | | | | | | | | 1.50% |
| WACC | | | | | | | | | | | | 5.90% |
| FCFF | | 6,151 | 7,787 | 8,237 | 8,802 | 9,551 | 10,814 | 12,094 | 13,289 | 14,379 | 15,329 | 18,998 |
| **PV of FCFF$_{2022\text{-}2031}$** | | 5,809 | 6,944 | 6,936 | 6,999 | 7,171 | 7,666 | 8,096 | 8,401 | 8,583 | 8,641 | |
| Continuing Value | | | | | | | | | | | 431,763 | |
| **PV of CV** | | | | | | | | | | | 243,380 | |
| Enterprise (Firm) Value | 318,626 | | | | | | | | | | | |
| Total Debt (Book Value of Debt) | 48,635 | | | | | | | | | | | |
| Total Equity | 269,991 | | | | | | | | | | | |
| Number of outstanding shares | 1554.846 | | | | | | | | | | | |
| **Price per share** | 173.6449 | | | | | | | | | | | |
| Current price per share (Oct 3rd, 2025) | $157.91 | | | | | | | | | | | |

### *Appendix 1.2: Income Statement in Base Valuation (Integrated Finance)*

| Income Statement for Year Ending: | 31-Dec-2015 | 31-Dec-2016 | 31-Dec-2017 | 31-Dec-2018 | 31-Dec-2019 | 31-Dec-2020 | 31-Dec-2021 | 31-Dec-2022 | 31-Dec-2023 | 31-Dec-2024 | 2025 | 2026 | 2027 | 2028 | 2029 | 2030 | 2031 | 2032 | 2033 | 2 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Revenue | 26,794.0 | 26,685.0 | 28,748.0 | 29,625.0 | 29,805.0 | 28,694.0 | 31,405.0 | 31,762.0 | 35,174.0 | 37,878.0 | 40,437 | 43,616 | 47,192 | 51,223 | 55,776 | 60,047 | 63,878 | 67,275 | 70,256 | |
| **Combustible tobacco products** | | | | | | | | | | | | | | | | | | | | |
| Europe | | | | | | | 8,767 | 7,694 | 8,037 | 8,599 | 8,873 | 9,126 | 9,386 | 9,654 | 9,929 | | | | | |
| SSEA, CIS | | | | | | | 8,734 | 9,173 | 9,321 | 9,848 | 9,940 | 10,223 | 10,514 | 10,814 | 11,122 | | | | | |
| EA, AU & PMI DF | | | | | | | 2,861 | 2,831 | 2,676 | 2,516 | 2,924 | 3,007 | 3,093 | 3,181 | 3,272 | | | | | |
| Americas | | | | | | | 1,706 | 1,874 | 2,299 | 2,255 | 2,178 | 2,240 | 2,304 | 2,369 | 2,437 | | | | | |
| Total combustible tobacco products | | 25952 | 25107 | 25529 | 24218 | 21747 | 22,068 | 21,572 | 22,333 | 23,218 | 23,915 | 24,596 | 25,297 | 26,018 | 26,760 | | | | | |
| **Smoke free products / reduced risk products** | | | | | | | | | | | | | | | | | | | | |
| Europe | | | | | | | 4388 | 5,278 | 6,194 | 6,758 | 7,986 | 9,199 | 10,598 | 12,209 | 14,064 | | | | | |
| SSEA, CIS | | | | | | | 1124 | 1,294 | 1,308 | 1,413 | 1,842 | 2,122 | 2,445 | 2,816 | 3,244 | | | | | |
| EA, AU & PMI DF | | | | | | | 3587 | 3,105 | 3,525 | 3,877 | 5,072 | 5,843 | 6,731 | 7,755 | 8,933 | | | | | |
| Americas | | | | | | | 137 | 242 | 1,508 | 2,279 | 1,290 | 1,486 | 1,711 | 1,971 | 2,271 | | | | | |
| Total smoke-free | | 733 | 3640 | 4096 | 5587 | 6947 | 9236 | 9919 | 12535 | 14327 | 16189.5 | 18650.3 | 21485.2 | 24750.9 | 28513.0 | | | | | |
| **Wellness & Healthcare** | | | | | | | | | | | | | | | | | | | | |
| Total Wellness & Healthcare | | | | | | | 101 | 271 | 306 | 333 | 333 | 369 | 409 | 454 | 503 | | | | | |
| Cost of Sales | 9365 | 9391 | 10432 | 10758 | 10513 | 9569 | 10030 | 11402 | 12893 | 13329 | 14195.32937 | 15311.15806 | 16566.49355 | 17981.6389 | 19579.95275 | 21079.22045 | 22424.27794 | 23616.6822 | 24663.19055 | 255 |
| **Gross Profit** | 17,429.0 | 17,294.0 | 18,316.0 | 18,867.0 | 19,292.0 | 19,125.0 | 21,375.0 | 20,360.0 | 22,281.0 | 24,549.0 | 26,242 | 28,305 | 30,625 | 33,241 | 36,196 | 38,968 | 41,454 | 43,658 | 45,593 | |
| Operating Expenses | 6806 | 6391 | 6735 | 7490 | 8761 | 7457 | 8400 | 8114 | 10725 | 11147 | 11174.18314 | 12052.5336 | 13040.70008 | 14154.66461 | 15412.81447 | 16592.99785 | 17651.79109 | 18590.4198 | 19414.20314 | 2 |
| **EBITDA** | 11,377 | 11,646 | 12,456 | 12,366 | 11,495 | 12,649 | 13,973 | 13,435 | 12,954 | 15,189 | 15,068 | 16,252 | 17,585 | 19,087 | 20,783 | 22,375 | 23,802 | 25,068 | 26,179 | |
| Depreciation | 672 | 669 | 787 | 907 | 898 | 908 | 902 | 918 | 901 | 952 | 1172.78 | 1264.969147 | 1368.681789 | 1485.597518 | 1617.646165 | 1741.51187 | 1852.637117 | 1951.150542 | 2037.610413 | 2112 |
| **EBITA** | 10,705.0 | 10,977.0 | 11,669.0 | 11,459.0 | 10,597.0 | 11,741.0 | 13,071.0 | 12,517.0 | 12,053.0 | 14,237.0 | 13,895 | 14,987 | 16,216 | 17,601 | 19,166 | 20,633 | 21,950 | 23,117 | 24,141 | |
| Amortization | 82.00 | 74.00 | 88.00 | 82.00 | 66.00 | 73.00 | 96.00 | 0.00 | 497.00 | 835.00 | | | | | | | | | | |
| **EBIT (operating income)** | 10,623.00 | 10,903.00 | 11,581.00 | 11,377.00 | 10,531.00 | 11,668.00 | 12,975.00 | 12,246.00 | 11,556.00 | 13,402.00 | 13,895 | 14,987 | 16,216 | 17,601 | 19,166 | 20,633 | 21,950 | 23,117 | 24,141 | |
| Non Operating income | 9,615.00 | 9,924.00 | 10,589.00 | 10,671.00 | 9,872.00 | 10,953.00 | 12,232.00 | 11,634.00 | 10,450.00 | 12,199.00 | | | | | | | | | | |
| Non Operating Expenses, net | 1008 | 891 | 914 | 665 | 570 | 618 | 628 | 588 | 1061 | 1143 | | | | | | | | | | |
| Other Non Operating Income/Expenses | — | 88 | 78 | 41 | 89 | 97 | 115 | 24 | 45 | 60 | | | | | | | | | | |
| Unrealized gain/loss from secs non-operating | | | | | | | | | | | | | | | | | | | | |
| EBIT | 10,623.00 | 10,903.00 | 11,581.00 | 11,377.00 | 10,531.00 | 11,668.00 | 12,975.00 | 12,246.00 | 11,556.00 | 13,402.00 | 13,895 | 14,987 | 16,216 | 17,601 | 19,166 | 20,633 | 21,950 | 23,117 | 24,141 | |

## *Appendix 2: Scenario Manager (Hypothesis 1)*

| Category | Buyback of IQOS (Standard) | Non-Buyback of IQOS | Assumptions |
|---|---|---|---|
| EBIT | $ 13,402 | $ 13,402 | Assuming this to be the same |
| Total assets | $ 72,848 | $ 70,148 | The acquisition amount would be deducted from the total asset |
| Total Debt | $ 48,635 | $ 45,935 | The acquisition amount would be deducted from the total liability |
| Incremental Interest | $ 98 | $ - | No additional interest would be paid on the for the debt taken |
| Interest | $ 1,861 | $ 1,763 | Exisitng debt |
| Acquisition cost | $ 2,700 | $ - | No acquisition cost in the assumed scenario |
| Pre- tax income | $ 11,541 | $ 11,639 | EBIT - Interest (exisitng interest + incremental interest) |
| Net income | $ 8,656 | $ 8,729 | Pre-tax income*(1- tax rate) |
| Ratio- without formula | 0.667622996 | 0.654829788 | Total debt / Total asset |
| Ratio- with formula | 0.667622996 | 0.654829788 | |

| Original Data (Used for reference) | |
|---|---|
| EBIT | 13,402.00 |
| Total assets | 72,848 |
| Total Debt | 48,635 |
| Acquisition cost | 2700 |
| Interest | 1763 |
| Interest rate | 3.6250% |
| Tax rate | 0.25 |

Scenario Manager

Scenarios:

Original IQOS rights buyback

Non buyback of IQOS rights

Add... | Delete | Edit... | Merge... | Summary...

Changing cells: $B$5:$B$7,Debt_asset_ratio

Comment: Created by HARSHIL on 05-10-2025

Show | Close

FCFF Valuation Model

| Categories | 2024 | 2025 | 2026 | 2027 | 2028 | 2029 | 2030 | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|
| T | | 1 | 2 | 3 | 4 | 5 | 6 | | | | 1 |
| G | | | | | | | | | | | 50 |
| WACC- | | | | | | | | | | | 90 |
| FCFF- | | $ 6,151.42 | $ 7,787.36 | $8,237.41 | $8,802.35 | $ 9,550.70 | $ 10,813.59 | $ | | | ,9 |
| PV of FCFF2022-2031 | | $ 5,808.70 | $ 6,943.82 | $6,935.90 | $6,998.66 | $ 7,170.60 | $ 7,666.45 | $ | | | |
| Continuing Value | | | | | | | | | | $4,31,762.74 | |
| PV of CV | | | | | | | | | | $2,43,380.38 | |
| Enterprise (Firm) Value | $ 3,18,626.05 | | | | | | | | | | |
| Total Debt (Book Value of Debt) | $ 48,635.00 | | | | | | | | | | |
| Total Equity | $ 2,69,991.05 | | | | | | | | | | |
| Number of outstanding shares | $ 1,554.85 | | | | | | | | | | |
| Price per share | $ 173.64 | | | | | | | | | | |
| Current price per share (Oct 3rd, 2025) | $ 157.91 | | | | | | | | | | |

The price per share changes as the scenario changes. All the scenarios have been made using scenario manager.