



Philip Morris International Inc.

PM: Marlboro Prices Going Up In Japan

Outperform/\$140

Tobacco
Overweight

Company Note

- PM Wins Approval to Raise Marlboro Retail Prices by 2.2% in Japan Effective October 1 - Should Be A Positive for Margins and Should Help To Accelerate Smoker Conversion to IQOS** - We just learned that Japan's Finance Ministry approved PM's application on 9/6 to increase retail pricing by ¥10/pack on Marlboro combustible cigs effective 10/1. This price increase is particularly notable because it will occur in absence of an increase in cig excise taxes - a rare event. The price hike will effectively raise the retail price of a pack of Marlboro to ¥470 from ¥460 (+2.2% increase) while leaving the price of a 20-stick pack of IQOS HeatSticks unchanged at ¥460 (and ¥10,000/kit). This compares to Mevius, which retails for ¥440/pack. The key implication, in our view, is this could further accelerate smoker conversion (namely Marlboro smokers) to IQOS, while also helping to protect the profitability of the Marlboro brand family as combustible cig volumes continue their secular decline. For comparative purposes, BAT's glo product sells for ¥420/pack (Neostiks) and ¥8,000/kit and JT's Ploom Tech product sells for ¥460/pack (refills) and ¥4,000/kit. **Bottom line** - We believe this is a positive development and could potentially enhance PM's net price realization target going forward (+6% for FY17) as well as drive even faster share gains for IQOS in Japan (13.7% offtake share as of the last week of August vs 12.5% as of July 2). **We reiterate our Outperform rating on PM, our top stock pick**, driven by PM's pricing power, strong global brands and incrementality of its reduced risk product (RRP) platform under the IQOS umbrella, which we believe should create long term shareholder value and upside in the stock.
- Q3 Outlook - Expect A -1% Decline in Combustible Cig Volumes** - We also note comments by PM's CFO Jacek Olczak at a recent conference guiding to a -1% decline in total company cig/Heatstick volumes in Q3 given ongoing pressures in Russia (lack of pricing), the Gulf Cooperation Council (GCC) (prices basically doubled as a result of tax hike at end of June) & Indonesia (macro weakness). The company's guidance for FY17 volume remains unchanged at "closer to down 3%" for overall cig/Heatstick volumes.

USD EPS	2016A		2017E		2018E	
			Curr.	Prior	Curr.	Prior
Q1 (Mar.)	\$0.98		\$0.98 A	NC	NE	
Q2 (June)	1.15		1.14 A	NC	NE	
Q3 (Sep.)	1.25		1.42	NC	NE	
Q4 (Dec.)	1.10		1.31	NC	NE	
FY	\$4.48		\$4.85	NC	\$5.50	NC
CY	\$4.48		\$4.85		\$5.50	
FY P/EPS	26.1x		24.1x		21.3x	
Rev.(MM)	\$26,685		\$28,343		\$31,034	

Source: Company Data, Wells Fargo Securities, LLC estimates, and Reuters
 NA = Not Available, NC = No Change, NE = No Estimate, NM = Not Meaningful
 V = Volatile, * = Company is on the Priority Stock List

Ticker	PM
Price Target/Prior:	\$140/NC
Price (09/08/2017)	\$117.06
52-Week Range:	\$86-124
Shares Outstanding: (MM)	1,554.0
Market Cap.: (MM)	\$181,911.0
S&P 500:	2,367.34
Avg. Daily Vol.:	3,216,530
Dividend/Yield:	\$3.50/3.0%
LT Debt: (MM)	\$26,595.0
LT Debt/Total Cap.:	139.4%
ROE:	NM
3-5 Yr. Est. Growth Rate:	12.0%
CY 2017 Est. P/EPS-to-Growth:	2.0x
Last Reporting Date:	07/20/2017

NC = No Change
 Source: Company Data, Wells Fargo Securities, LLC estimates, and Reuters

Bonnie Herzog
 Senior Analyst | 212-214-5051
 bonnie.herzog@wellsfargo.com

Patty Kanada, CFA
 Associate Analyst | 212-214-5029
 patty.kanada@wellsfargo.com

Adam Scott
 Associate Analyst | 212-214-8064
 adam.scott@wellsfargo.com

Please see page 3 for rating definitions, important disclosures and required analyst certifications. All estimates/forecasts are as of 09/08/17 unless otherwise stated. 09/08/17 18:21:08 ET

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Price Target

Price Target: \$140 from NC

Our \$140 price target is based on a 17.5x forward EV/EBITDA multiple and a 25.4x forward P/E multiple, both slightly above its avg. historical multiples. Risks include f/x headwinds and a broad-based pullback in consumer spending.

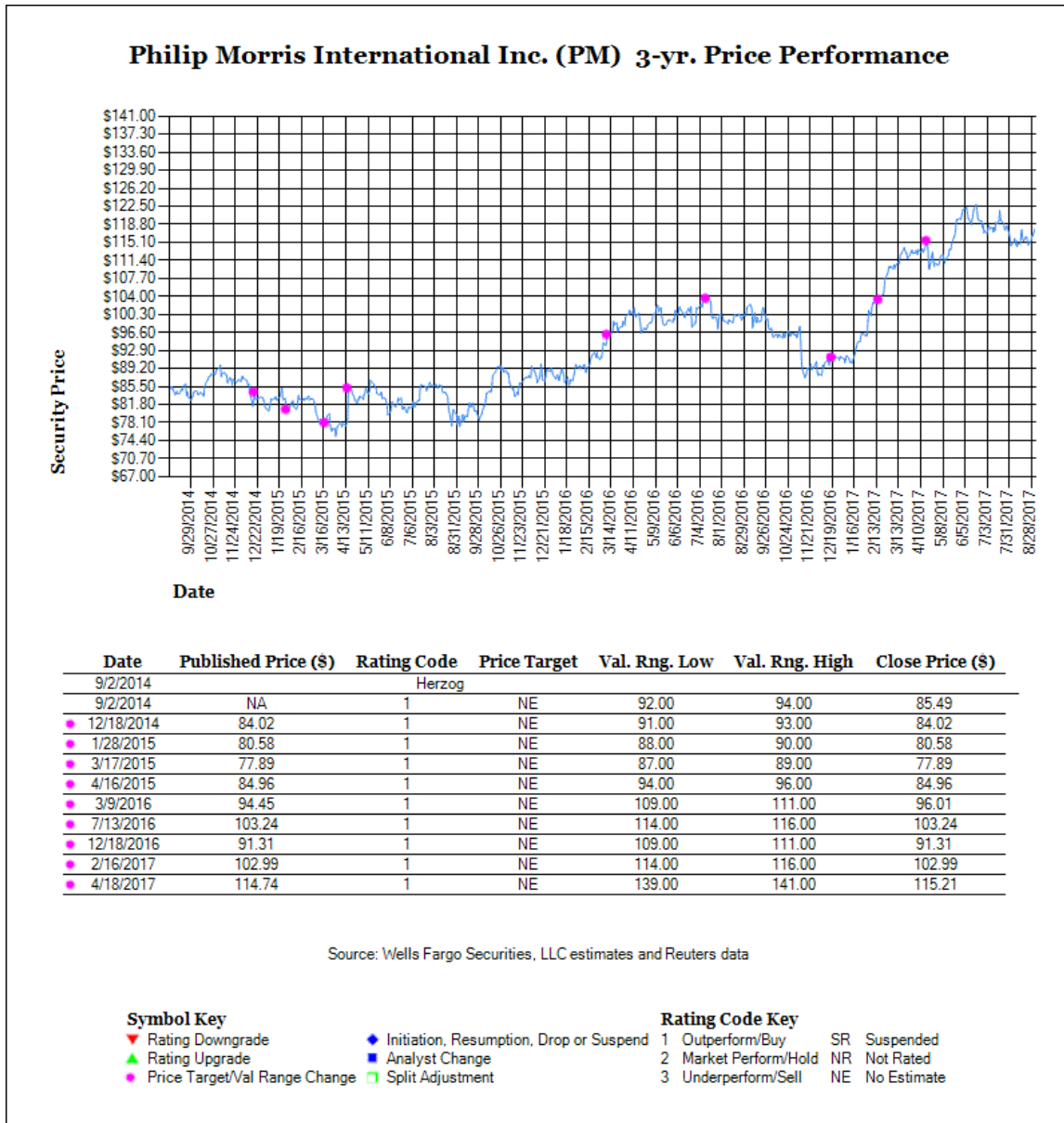
Investment Thesis

We expect PM to outperform over the long term given: (1) iQOS, (2) a re-invigorated Marlboro brand franchise, (3) an industry-leading, diverse brand portfolio, and (4) an improving ROIC & economic profit. PM has emerged in a class of its own and we believe it is poised for further growth.

Company Description

Philip Morris International is engaged in the manufacturing and marketing of cigarettes and other tobacco products outside of the United States. Headquartered in New York, the company has a wide range of premium, mid-price, and low-price brands, and its portfolio consists of both international and local brands. Philip Morris' leading brand Marlboro is the world's best-selling international cigarette. Philip Morris is also the leader in reduced risk products (RRPs) with its iQOS platform.

Required Disclosures



Additional Information Available Upon Request

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PM: Risks include f/x headwinds and a broad-based pullback in consumer spending.

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M=Market Weight: Industry expected to perform in-line with the relevant broad market benchmark over the next 12 months.

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V = A stock is defined as volatile if the stock price has fluctuated by +/-20% or greater in at least 8 of the past 24 months or if the analyst expects significant volatility. All IPO stocks are automatically rated volatile within the first 24 months of trading.

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