

# Apple Inc.

(NASDAQ: AAPL)

## Q2 Will be Tough to Beat

**BUY**

**Current Price: \$133.79**

**Fair Value: \$144.27**

**Risk\*: 2**

**Sector/Industry: Technology**

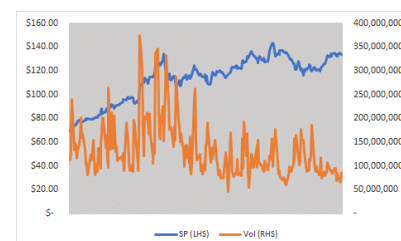
[Click here for more research on the company and to share your views](#)

### Highlights

- Q2 (quarter ended March 2021) revenue beat market estimates by 16%, and our estimate by 7%. Earnings beat market estimates by 42%, and our estimate by 11%. Declared a cash dividend of \$0.22 per share (payable in May), up 7% QoQ.
- **Reported revenue growth across all product types and geographic segments.**
- Growth primarily came from strong sales of the new iPhone 12, and Mac/iPad sales due to work-from-home and remote learning environments caused by the pandemic.
- **We believe one of the strongest points of Q2 was a significant increase in the adoption of Apple products.** First-time buyers accounted for close to 50% of global Mac sales, and two-thirds in China.
- Service revenue grew 27% YoY. Apple has over 660M paid subscriptions, up 6% QoQ.
- Despite the stellar performance in Q2, **Apple expects a relatively weaker Q3** due to slower iPhone sales (as initial sales taper off), and a supply-chain crunch caused by the ongoing semiconductor shortage.
- **Based on the strong Q2, we are raising our 2021 revenue and EPS forecasts by 7% and 11%, respectively.** However, we are lowering our fair value estimate by 3% due to declines in sector multiples since our previous report in January.
- **We feel that Q2 will be a tough quarter to beat, which will impact investors' sentiment/excitement towards the stock.** Apple has already warned investors that Q3 will be relatively weak. In addition, a potential reduction in work-from-home/remote learning from the vaccine rollout means that Apple is unlikely to report similar growth in the coming quarters.

**Sid Rajeev, B.Tech, CFA, MBA**  
Head of Research

### AAPL Price and Volume (1-year)



	YTD	12M
Ret.	1%	92%
NASDAQ	11%	58%

52-Week Range	\$71 - \$145
Shares O/S	16.7B
Market Cap.	\$2.3T
Current Yield	0.9%
P/E (forward)	28.2

Key Financial Data (YE Sept 30, \$M)	2017	2018	2019	2020	2021E	2022E
Cash, cash equivalent and marketable securities	268,895	237,100	205,898	191,830	167,823	146,184
Working Capital	27,831	15,410	57,101	38,321	36,336	34,838
Total Assets	375,319	365,725	338,516	323,888	311,259	297,399
Revenue	229,234	265,595	260,174	274,515	354,075	375,478
Net Income	48,351	59,531	55,256	57,411	75,923	78,111
EPS Diluted (\$)	2.32	3.00	2.99	3.28	4.74	4.88

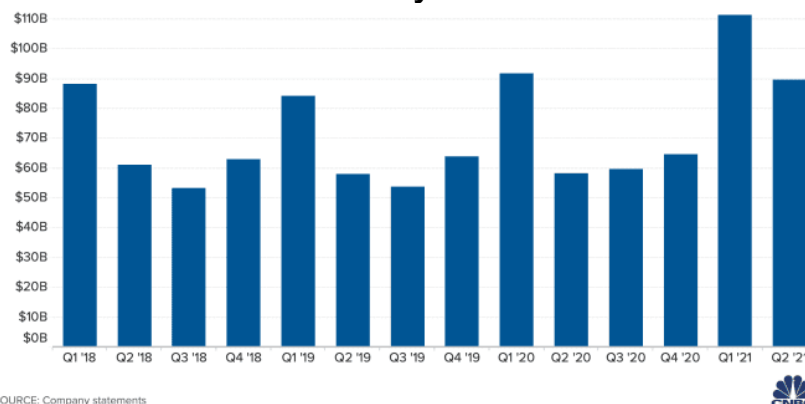
See last page for important disclosures, rating, and risk definitions. All figures in US\$ unless otherwise specified.

Revenues from  
iPhone, Mac, and  
iPad were up 68%  
YoY

Services and Mac  
revenue hit record  
highs

Revenue by Product (YE Sept 30, \$M)	Q1-2020	Q1-2021	YoY	Q2-2020	Q2-2021	YoY
iPhone	55,957	65,597	17%	28,962	47,938	66%
Mac	7,160	8,675	21%	5,351	9,102	70%
iPad	5,977	8,435	41%	4,368	7,807	79%
Wearables, Home and Accessories	10,010	12,971	30%	6,284	7,836	25%
Services	12,715	15,761	24%	13,348	16,901	27%
<b>Total Revenue</b>	<b>91,819</b>	<b>111,439</b>	<b>21.4%</b>	<b>58,313</b>	<b>89,584</b>	<b>53.6%</b>

### Revenue by Quarter



Growth across every  
geographic segment

Strongest growth in  
China and the rest  
of Asia

Revenue by Region (YE Sept 30, \$M)	Q1-2020	Q1-2021	YoY	Q2-2020	Q2-2021	YoY
Americas	41,367	46,310	11.9%	25,473	34,306	34.7%
Europe	23,273	27,306	17.3%	14,294	22,264	55.8%
Greater China	13,578	21,313	57.0%	9,455	17,728	87.5%
Japan	6,223	8,285	33.1%	5,206	7,742	48.7%
Rest of Asia Pacific	7,378	8,225	11.5%	3,885	7,544	94.2%
<b>Total Revenue</b>	<b>91,819</b>	<b>111,439</b>	<b>21.4%</b>	<b>58,313</b>	<b>89,584</b>	<b>53.6%</b>

Margins improved  
across the board

Margins	Q1-2020	Q1-2021	YoY	Q2-2020	Q2-2021	YoY
Gross	38.4%	39.8%	142 bps	38.4%	42.5%	414 bps
EBITDA	30.9%	32.5%	157 bps	26.8%	33.8%	700 bps
EBIT	27.8%	30.1%	224 bps	22.0%	30.7%	866 bps
Net	24.2%	25.8%	159 bps	19.3%	26.4%	709 bps

Expenses as % of Revenue	Q1-2020	Q1-2021	YoY	Q1-2021	Q2-2021	YoY
Research and development	4.8%	4.6%	-21 bps	7.8%	5.9%	-195 bps
Selling, general and administrative	5.7%	5.1%	-61 bps	8.5%	5.9%	-256 bps

FCF up 92% YoY

Summary of Cash Flows (YE Sept 30, \$M)	Q1-2020	Q1-2021	YoY	Q2-2020	Q2-2021	YoY
Cash Flows from Operations	30,516	38,763	27%	13,311	23,981	80%
Cash Flows from Investing	-13,668	-8,584	-37%	9,013	-10,368	-215%
Cash Flows from Financing	-25,407	-32,249	27%	-20,940	-11,326	-46%
Net Change	-8,559	-2,070	-76%	1,384	2,287	65%
<b>Free Cash Flows</b>	<b>27,451</b>	<b>35,254</b>	<b>28%</b>	<b>11,282</b>	<b>21,712</b>	<b>92%</b>

Strong balance  
sheet, with \$204B in  
cash equivalents

Liquidity and Capital Structure (YE Sept 30, \$M)	Q1-2021	Q2-2021
Cash, cash equivalent and marketable securities	195,571	204,373
Working Capital	21,599	15,080
Current Ratio	1.2	1.1
LT Debt	99,281	108,642
Total Debt	112,043	121,645
Total Debt/Capital	63%	64%
Long Term Debt/Capital	56%	57%

Source: FRC / Apple

## Projections and Valuation

Line Items	Old Forecasts		New Forecasts	
	2021	2022	2021	2022
Revenue (\$ mn)	\$329,609	\$346,855	\$354,075	\$375,478
EBITDA (\$ mn)	\$93,547	\$97,211	\$99,716	\$104,448
Net Income (\$mn)	\$69,476	\$72,208	\$75,923	\$78,111
EPS (\$)	\$4.28	\$4.45	\$4.74	\$4.88

Source: FRC

## Comparables Valuation

Comparable Companies	P/E	
	FY21E	FY22E
Apple Inc	28.20	27.41
Samsung Electronics Co Ltd	14.67	11.35
Nokia Oyj	18.79	13.83
Microsoft Corp	32.76	31.03
Alphabet Inc	27.22	26.31
Amazon.com Inc	72.90	52.10
International Business Machines Corp	13.10	11.93
HP Inc	8.80	8.40
Dell Technologies Inc	12.51	11.96
Lenovo Group Ltd	15.46	13.79
<b>Average Market Multiples</b>	<b>26.2x</b>	<b>22.2x</b>
<b>Median Market Multiples</b>	<b>17.1x</b>	<b>13.8x</b>
<b>AAPL versus average</b>	<b>108%</b>	<b>124%</b>
<b>Relative Valuation - AAPL</b>		
EPS 2021e (\$)		\$4.74
EPS 2022e (\$)		\$4.88
Target P/E multiple for 2021E (x) - 20% premium to avg		31.4x
Target P/E Multiple for 2022E (x) - 20% premium to avg		26.6x
<b>Fair value per share (\$) - P/E Multiple (2021E)</b>		<b>149.04</b>
<b>Fair value per share (\$) - P/E Multiple (2022E)</b>		<b>129.97</b>

Valuation Method	Fair Value per share (\$)	Weight
Fair value per share (\$) - P/E Multiple (2021E)	\$149.04	75.0%
Fair value per share (\$) - P/E Multiple (2022E)	\$129.97	25.0%
<b>Fair Value Estimate (\$)</b>		<b>\$144.27</b>
Current Price (\$)		\$133.79
<b>Upside/(Downside)</b>		<b>7.8%</b>
Forward Dividend Yield 2021E		0.9%
<b>Total return including dividend</b>		<b>8.7%</b>

Source: FRC / S&P Capital IQ

**We are lowering our fair value estimate from \$148.12 to \$144.27 per share, suggesting a potential return (including dividends) of 8.7% this year. We are also maintaining our BUY rating.**

Raising 2021 and 2022 EPS estimates due to a stronger than expected Q2

APPL's 2022 forward P/E is 1.24x the comparables average

Sector multiples fell 4% since our previous report in January 2021

Valuing Apple at a 20% premium

Lowering our fair value estimate by 3% to \$144.27 per share

Higher forward P/E multiples were more than offset by lower sector multiples

## Risks

We believe the company is exposed to the following risks (list is non-exhaustive):

- Intense competition.
- Longer-term impact of COVID-19 is uncertain.
- Regulatory interventions in AAPL's business could have a negative impact on operations.
- Constant innovation is critical.

**We are maintaining a risk rating of 2 (Below Average Risk).**

### Appendix

Income Statement (YE Sept 30, \$ million)	2020	2021E	2022E
<b>Total Revenue</b>	<b>274,515</b>	<b>354,075</b>	<b>375,478</b>
COGS	169,559	215,986	230,168
<b>Gross Margin</b>	<b>104,956</b>	<b>138,089</b>	<b>145,310</b>
Research and development	18,752	23,015	24,406
Sales and marketing	19,916	26,556	28,161
<b>EBIT</b>	<b>66,288</b>	<b>88,519</b>	<b>92,743</b>
Depreciation and Amortization	11,056	11,197	11,705
<b>EBITDA (calculated)</b>	<b>77,344</b>	<b>99,716</b>	<b>104,448</b>
Other income (expense)	803	803	803
<b>EBT</b>	<b>67,091</b>	<b>89,322</b>	<b>93,546</b>
Provision for income taxes	9,680	13,398	15,435
<b>Net Income</b>	<b>57,411</b>	<b>75,923</b>	<b>78,111</b>
EPS	3.31	4.74	4.88

Balance Sheet (YE Sept 30, \$ million)	2020	2021E	2022E
<b>Assets</b>			
Cash, cash equivalents and markatable securities	191,830	167,823	146,184
Accounts receivable, net	16,120	23,282	25,718
Inventories	4,061	4,142	5,045
Property and equipment, net	36,766	40,794	45,235
Other assets	75,111	75,218	75,218
<b>Total assets</b>	<b>323,888</b>	<b>311,259</b>	<b>297,399</b>
<b>Liabilities and stockholders' equity</b>			
Accounts payable	42,296	48,781	51,978
Commercial paper and repurchase agreement	4,996	4,996	4,996
Short-term debt	8,773	7,509	7,509
Long-term debt	98,667	90,199	80,360
Other liabilities	103,817	103,817	103,817
<b>Total liabilities</b>	<b>258,549</b>	<b>255,302</b>	<b>248,660</b>
Common stock and paid-in capital	50,779	59,454	68,653
Retained earnings	14,966	-3,091	-19,508
Accumulated other comprehensive income/(loss)	-406	-406	-406
<b>Total stockholders' equity</b>	<b>65,339</b>	<b>55,956</b>	<b>48,739</b>
<b>Total liabilities and stockholders' equity</b>	<b>323,888</b>	<b>311,259</b>	<b>297,399</b>

Cash Flow (YE Sept 30, \$ million)	2020	2021E	2022E
Operating activities:			
Net income	57,411	75,923	78,111
Adjustments to reconcile net income to net cash from operations:			
Depreciation and amortization	11,056	11,197	11,705
Share-based compensation expense	6,829	8,675	9,199
Other	-312	0	0
Changes in operating assets and liabilities:			
Accounts receivable, net	6,917	-7,162	-2,436
Inventories	-127	-81	-903
Accounts payable	-4,062	6,485	3,197
Other current and non-current liabilities	2,962	0	0
<b>Cash generated by operating activities</b>	<b>80,674</b>	<b>95,038</b>	<b>98,873</b>
Investing activities:			
Purchases of marketable securities	-114,938	0	0
Proceeds from maturities of marketable securities	69,918	10,000	10,000
Proceeds from sales of marketable securities	50,473	10,000	10,000
Payments for acquisition of property, plant and equipment	-7,309	-14,163	-15,019
Payments made in connection with business acquisitions, net	-1,524	-1,062	-1,126
Other	-909		
<b>Cash generated by/(used in) investing activities</b>	<b>-4,289</b>	<b>4,775</b>	<b>3,854</b>
Financing activities:			
Payments for dividends and dividend equivalents	-14,081	-18,981	-19,528
Repurchases of common stock	-72,358	-75,000	-75,000
Proceeds from issuance of term debt, net	16,091	0	0
Repayments of term debt	-12,629	-9,839	-9,839
Other	-3,843	0	0
<b>Cash used in financing activities</b>	<b>-86,820</b>	<b>-103,820</b>	<b>-104,367</b>
<b>Increase/(Decrease) in cash, cash equivalents and restricted cash</b>	<b>-10,435</b>	<b>-4,007</b>	<b>-1,639</b>
Cash, cash equivalents and restricted cash, beginning balances	50,224	39,789	35,782
<b>Cash, cash equivalents and restricted cash, ending balances</b>	<b>39,789</b>	<b>35,782</b>	<b>34,143</b>
Restricted cash included in other current assets	1,773	1,773	1,773
Restricted cash included in other non-current assets	0	0	0
<b>Cash and cash equivalents</b>	<b>38,016</b>	<b>34,009</b>	<b>32,370</b>



**Fundamental Research Corp. Equity Rating Scale:**

**Buy** – Annual expected rate of return exceeds 12% for micro / small cap companies, and 8% for mid / large cap companies.

**Hold** – Annual expected rate of return is between 5% and 12% for micro / small-cap companies, and 5% and 8% for mid / large-cap companies.

**Sell** – Annual expected rate of return is below 5%.

**Suspended or Rating N/A**— Coverage and ratings suspended until more information can be obtained from the company regarding recent events.

**Fundamental Research Corp. Risk Rating Scale:**

**1 (Low Risk)** - The company operates in an industry where it has a strong position (for example a monopoly, high market share etc.) or operates in a regulated industry. The future outlook is stable or positive for the industry. The company generates positive free cash flow and has a history of profitability. The capital structure is conservative with little or no debt.

**2 (Below Average Risk)** - The company operates in an industry where the fundamentals and outlook are positive. The industry and company are relatively less sensitive to systematic risk than companies with a Risk Rating of 3. The company has a history of profitability and has demonstrated its ability to generate positive free cash flows (though current free cash flow may be negative due to capital investment). The company's capital structure is conservative with little to modest use of debt.

**3 (Average Risk)** - The company operates in an industry that has average sensitivity to systematic risk. The industry may be cyclical. Profits and cash flow are sensitive to economic factors although the company has demonstrated its ability to generate positive earnings and cash flow. Debt use is in line with industry averages, and coverage ratios are sufficient.

**4 (Speculative)** - The company has little or no history of generating earnings or cash flow. Debt use is higher. These companies may be in start-up mode or in a turnaround situation. These companies should be considered speculative.

**5 (Highly Speculative)** - The company has no history of generating earnings or cash flow. They may operate in a new industry with new, and unproven products. Products may be at the development stage, testing, or seeking regulatory approval. These companies may run into liquidity issues and may rely on external funding. These stocks are considered highly speculative.

**Disclaimers and Disclosure**

The opinions expressed in this report are the true opinions of the analyst about this company and industry. Any "forward looking statements" are our best estimates and opinions based upon information that is publicly available and that we believe to be correct, but we have not independently verified with respect to truth or correctness. There is no guarantee that our forecasts will materialize. Actual results will likely vary. Fundamental Research Corp. "FRC" owns shares of the subject company, but does not make a market or offer shares for sale of the subject company, and does not have any investment banking business with the subject company. The Analyst does not own shares of the subject company. No fees were paid by AAPL to FRC. FRC takes steps to ensure independence including setting fees in advance and utilizing analysts who must abide by CFA Institute Code of Ethics and Standards of Professional Conduct. Additionally, analysts may not trade in any security under coverage. Our full editorial control of all research, timing of release of the reports, and release of liability for negative reports are protected contractually. Distribution procedure: our reports are distributed first to our web-based subscribers on the date shown on this report then made available to delayed access users through various other channels for a limited time.

The distribution of FRC's ratings are as follows: BUY (69%), HOLD (7%), SELL / SUSPEND (24%).

To subscribe for real-time access to research, visit <https://www.researchfrc.com/website/subscribe/> for subscription options.

This report contains "forward looking" statements. Forward-looking statements regarding the Company and/or stock's performance inherently involve risks and uncertainties that could cause actual results to differ from such forward-looking statements. Factors that would cause or contribute to such differences include, but are not limited to, continued acceptance of the Company's products/services in the marketplace; acceptance in the marketplace of the Company's new product lines/services; competitive factors; new product/service introductions by others; technological changes; dependence on suppliers; systematic market risks and other risks discussed in the Company's periodic report filings, including interim reports, annual reports, and annual information forms filed with the various securities regulators. By making these forward-looking statements, Fundamental Research Corp. and the analyst/author of this report undertakes no obligation to update these statements for revisions or changes after the date of this report. A report initiating coverage will most often be updated quarterly while a report issuing a rating may have no further or less frequent updates because the subject company is likely to be in earlier stages where nothing material may occur quarter to quarter.

Fundamental Research Corp DOES NOT MAKE ANY WARRANTIES, EXPRESSED OR IMPLIED, AS TO RESULTS TO BE OBTAINED FROM USING THIS INFORMATION AND MAKES NO EXPRESS OR IMPLIED WARRANTIES OR FITNESS FOR A PARTICULAR USE. ANYONE USING THIS REPORT ASSUMES FULL RESPONSIBILITY FOR WHATEVER RESULTS THEY OBTAIN FROM WHATEVER USE THE INFORMATION WAS PUT TO. ALWAYS TALK TO YOUR FINANCIAL ADVISOR BEFORE YOU INVEST. WHETHER A STOCK SHOULD BE INCLUDED IN A PORTFOLIO DEPENDS ON ONE'S RISK TOLERANCE, OBJECTIVES, SITUATION, RETURN ON OTHER ASSETS, ETC. ONLY YOUR INVESTMENT ADVISOR WHO KNOWS YOUR UNIQUE CIRCUMSTANCES CAN MAKE A PROPER RECOMMENDATION AS TO THE MERIT OF ANY PARTICULAR SECURITY FOR INCLUSION IN YOUR PORTFOLIO. This REPORT is solely for informative purposes and is not a solicitation or an offer to buy or sell any security. It is not intended as being a complete description of the company, industry, securities or developments referred to in the material. Any forecasts contained in this report were independently prepared unless otherwise stated and HAVE NOT BEEN endorsed by the Management of the company which is the subject of this report. Additional information is available upon request. THIS REPORT IS COPYRIGHT. YOU MAY NOT REDISTRIBUTE THIS REPORT WITHOUT OUR PERMISSION. Please give proper credit, including citing Fundamental Research Corp and/or the analyst, when quoting information from this report.

The information contained in this report is intended to be viewed only in jurisdictions where it may be legally viewed and is not intended for use by any person or entity in any jurisdiction where such use would be contrary to local regulations or which would require any registration requirement within such jurisdiction.