# lorillard

# Eat 'em, Drink 'em, Smoke 'em The Berkshire Anne Hathaway's

By: CMO Tasha Phillips, CNO Nathan Ramos, CAO Jacob Bravo, CIO Ernie Stephenson, CFO April Estes, CEO Phil Bauch, and CPO Eli Von Berg



- Lorillard was founded in 1760 by Pierre Lorillard, making it the first tobacco company in New York City
- In 2008, spun off from Loews Corporation
- In 2010, Lorillard celebrated its 250<sup>th</sup> anniversary, making it the oldest publicly traded company listed on the New York Stock Exchange



- Nation's third largest tobacco company
- Lorillard Tobacco Company does business in all 50 states, the District of Columbia, Puerto Rico, and other outlying U.S. possessions
- Oldest continuously operating tobacco company in the United States

#### Brands



### Industry



### Newport

- Lorillard's premium cigarette brand
- Top selling menthol cigarette in the United States
- Accounted for 88% of sales revenue for 2012

### Competitors

- Reynolds American (RAI)
- Altria Group (MO)
- NJOY
- eSmoke
- ♦ 21<sup>st</sup> Century

#### **E-Cigarettes**

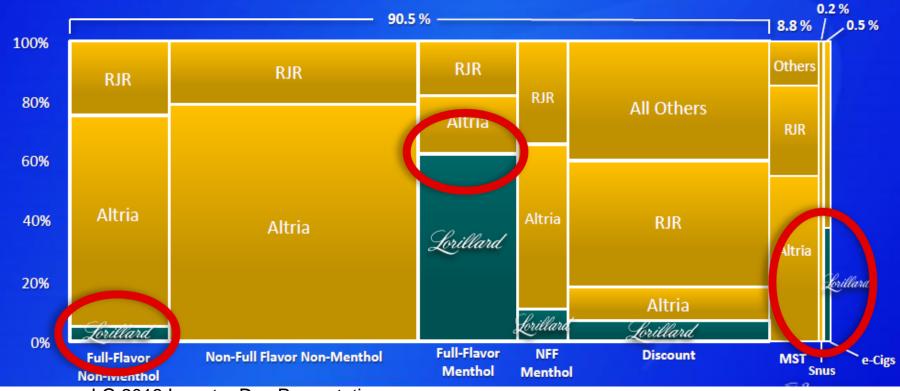


LO 2013 Investor Day Presentation

### **Market Share**

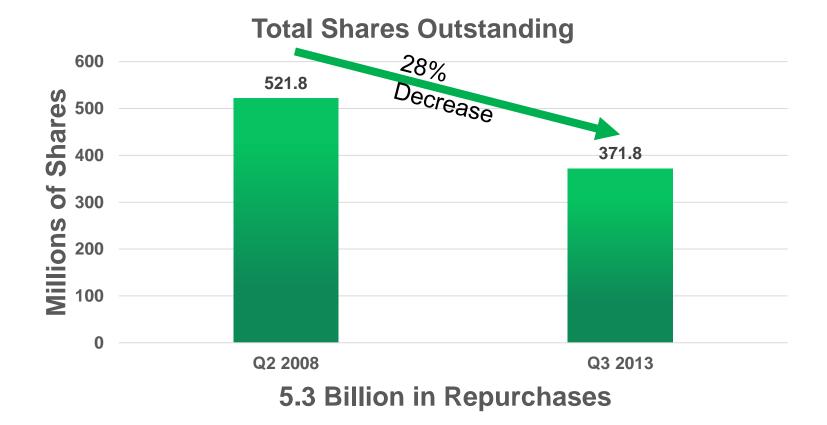
#### 2012 U.S. Tobacco Market Segmentation

15.1 B Packs/Cans



LO 2013 Investor Day Presentation

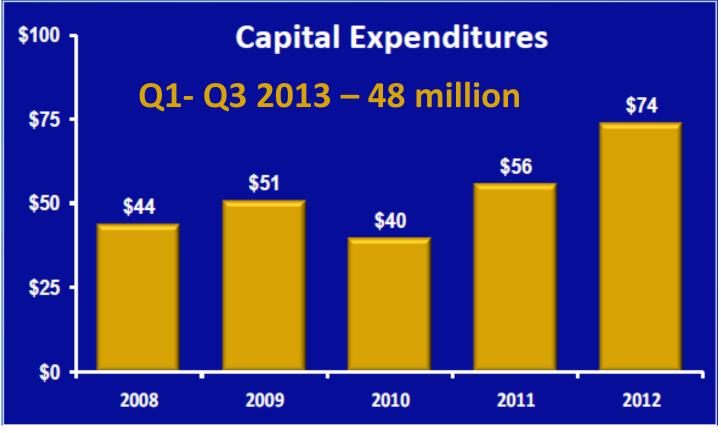
#### Share Buybacks



#### Effect of Buybacks

- 2008 2009 Bought back shares and put in Treasury Stock which creates negative balance in T.S. account
- 2010-2012 Continued to buy back shares until negative Treasury Stock balance exceeded remaining Shareholder's Equity accounts
- Q1 2013 Decide to retire all treasury stock which turns Retained Earnings balance negative and continue to buy back shares

#### **Capital Expenditures**



LO 2013 Investor Day Presentation

In millions

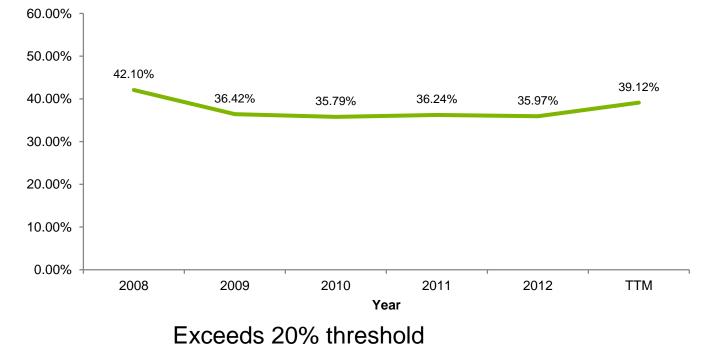
### Litigation

- Four types of litigation
  - Individual
    - Engle Progeny Suits
  - Class actions
  - Health-care reimbursement
  - Kent filter
- Other litigation
  - FDA related

#### **Risk Factors**

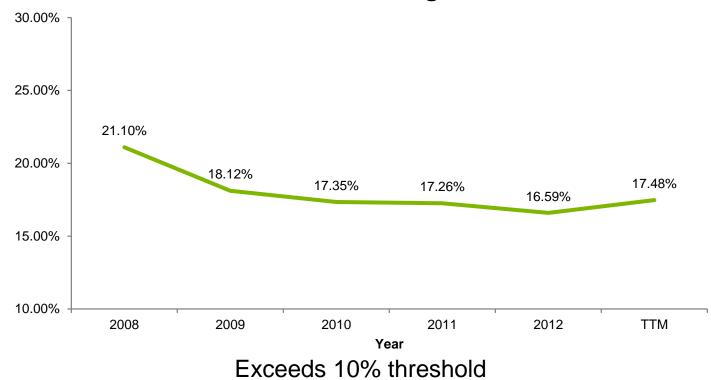
- Significant Litigation
- Derive majority of revenue from one brand
- Only one manufacturing facility
- Regulation of cigarettes by FDA
- Limitation on advertising and marketing
- Regulation of electronic cigarettes
- Sales of cigarettes are subject to hefty taxes
- Dependency on domestic cigarette business, which continues to contract
- Small number of suppliers for leaf tobacco

**Gross Profit Margin** 

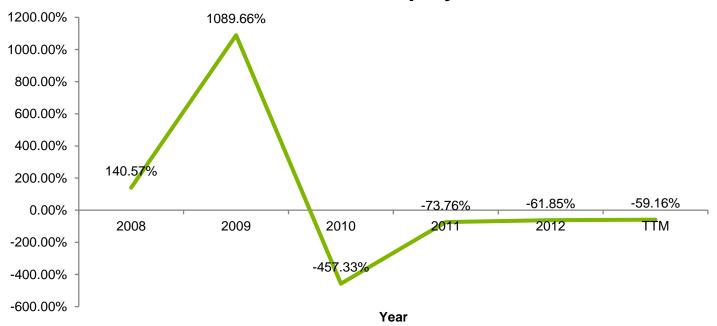




**Net Profit Margin** 



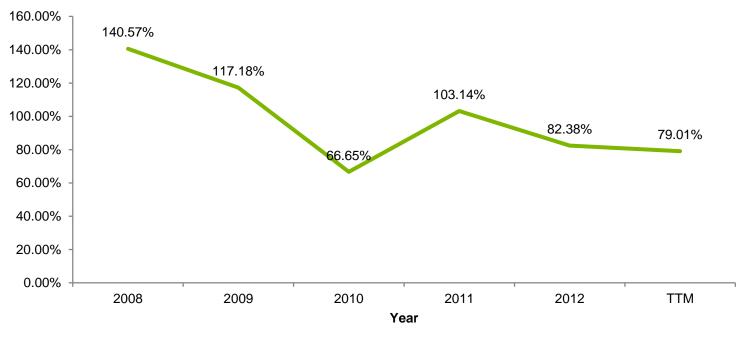




**Return on Equity** 

Doesn't exceed 15% threshold

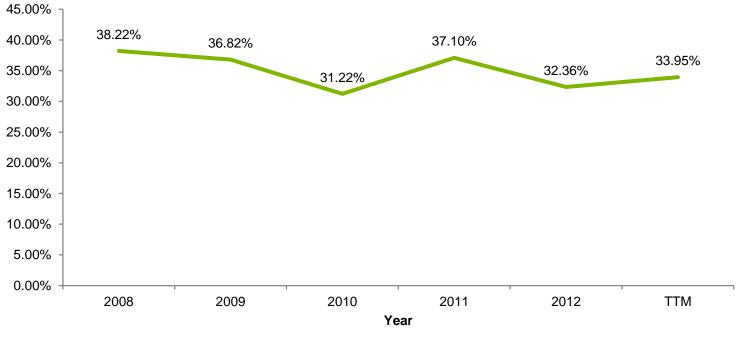
#### **Return on Capital**



Exceeds 15% threshold



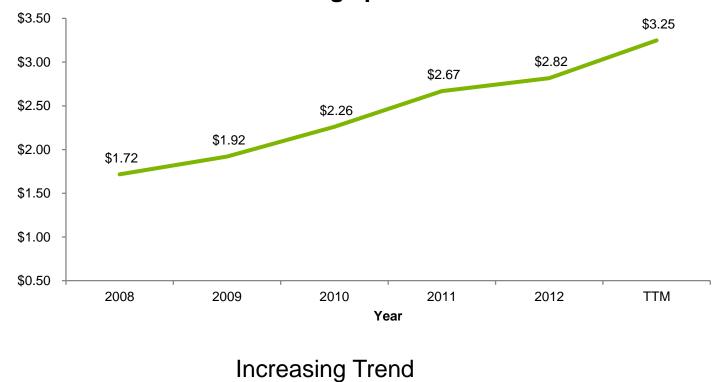
**Return on Assets** 



Exceeds 15% threshold



**Earnings per Share** 



### Interpretation of Financial Statements

Balance Sheet		Criteria	Pass?
Current Ratio:	1.828225	> 1	Yes
Obligation Ratio:	3.11	< 5 years	Yes
DD&A % of GP:	1.55%	≤ 10%	Yes
Interest % of OP:	8.02%	≤ 15%	Yes
Net Profit Margin:	<u></u> 17.48%	X ≥ 10%	Yes
	100	> 80	Yes
Earnings Predictability:	100	> 00	162

### Buffettology

#### **Qualitative Review**

What type of bu	Net Profit Ma	rgin	Deci	reasing		ompetitive
advantage?	Working Cap	Statistical Array Analysis				•
	Shareholder's					
		Sales per Share	ľ	Yes		
	Return on To	Cashflows per Share	Y	Yes		
		Earnings per Share	Ņ	Yes		
Can you easily o	6	Dividends Declared per Sha	are `	Yes		garette Producer
ls it heavily unio		Capital Spending per Share		Yes		
Does it require l	ł	Book Value per Share	I	No		
		Revenues (Sales)	ľ	Yes	ybacks	
Can inventory b	Common Sha	Gross Profit Margin		Fairly Stable		
Are there chron	<sup>I</sup> I ong-Term D			Faility Stable		
Is the company		Operating Profit Margin	F	Fairly Stable		
Will the compar	LT Debt Paya	Operating Profit Margin Number of Stores	I	None		
	All Dividends	Net Profit		Yes		
If I gave you \$1			_			
"no" your busin	Annual Grow	th Rate Analysis	Roo	m for Growth		

#### **DuPont Analysis**

Net Profit MarginTotal Asset TurnoverFinancial Leverage Multiplier

17.48% X 1.944 X -1.740

#### = Not Calculable

# Conscious Investor 3-year Default

71000		and the second	Per Share (EPS	The second s			-		HGROWT		TAEGR
12/05	12/06 1	2/07 1		12/1	0 12/11	12/12	EPStim	Years	Calc 11.51		8.21%
	current year		ST	RETD® 25 Oct	2013 P	rice	49.59	_	HGROWT	H 51	TAEGR™
6.835	Dividend Re				Red Contraction of the	PSttm	3.190		Calc 13.53 Current NPM		7.69%
19.79	Buy addi				P	ERatio	13.53		16.59 Current ROE		Chart
52.70					H	Growth	11.51	%	0.00		Chart
11.40	Note: PE an	d PR Rati	os are ave	of 4 yrs	P	ayout	67	%	Current PE	-	Chat
7.00					_				Current Price	_	Char.
9.49	Investment Pe	riod	5	years	Tax - divide Tax - capita	100	0	%	Current PR		
45	Calculat	e   13	.83%	_ per yea			c with TAR	g	74%		Char
current year	25 Oct 2013	Price	49.59						Req Return	15.0	96
Dividend Reinvestment Strate		EPSttm	3.190		Dividend Rein     Generation		itegy		EPStm	3.190	
Buy additional shares Invest at the rate below		PE Ratio	13.53		C invest at the				PE Ratio	13.53	_
Note: PE and PR Ratios are a	ve of 4 yrs	-IGrowth Payout	11.51		Note: PE and PR	Ratios are a	ive of 4 yrs		HGrowth Payout	11.51 67	- 55
		- apour	Per.	1							
Investment Period	years Tax -	dividends	0	- s	the sector of Party	va 15	years	Tax - di	idends	1	- %
Investment Period  5		capital gains	0	%	Investment Perio	10 Io	10010	Tax - ca	pital gains	0	5
Calculate 13.83%	per year	S	ync with TARG		Calculate	\$47.00			Sync	with STRE	ET

# **Conscious Investor 6-year Default**

		ST	RETD®	è.		125		ROWTH	STAE	EGR"
	ent year		25 00	12013	Price	49.59	T T	11.93%	96.1	4%
Divis	dend Reinvestmer	t Strategy		2003-2052	EPSttm	3.190		ROWTH		GR
<sup>6</sup>	Buy additional shar	es			PERatio	13.53	-	nt NPM	s laer	670
	nvest at the rate be	low					_	59		Chart
5 Note	an sala - ta ang ang ang ang	100-2007		2.6	HGrowth	11.93	%	nt ROE		Chart
Note	: PE and PR Ratio	s are ave	of 4 yrs		Payout	67	%		_	,nan
1						1		ent PE		Chart
7								00	-	man
G								t Price		
[9] Im un att	and the second second	5	-	Tax - div	idends	0	%	59	0	Char.
investi	mentPeriod	12	years	Tax - ca	pital gains	0	%	ent PR		
4			_	Tax - Ca	pital gains	1.	1.0	16		Chart
Irrent year	Calculate 14.	26%	per yea	ar	Sync	with TARG			15.0	96
vidend Reinvestment Strategy	20 00 2013 -1108	3.190	-	Dividend Rei	investment Strategy		EPSttr	um	3.190	- "
Buy additional shares	EPSttm PE Rati		- 1	Buy addit	ional shares he rate below		PE Rat	io	13.53	
Invest at the rate below	HGrowt		%		Same State		HGrow	S	11.93	96
ote: PE and PR Ratios are ave of	4 yrs Payout	67	.96	Note: PE and F	PR Ratios are ave of	4 yrs	Payout		67	%
		1977								
	Tax - dividends	0	- %		1	Tax-0	dividends	1	1	- %
estment Period 5	years Tax - capital gain:	s 0	%	Investment Per	riod 5	years Tax - 0	capital ga	ins	0	%
Calculate 14.26%	per year :	Sync with TARG		Calculate	\$47.89			Sync w	ith STRET	

# **Conscious Investor 8-year Default**

			Earnin	igs Per Shan	e (EPS)				_			_	_
	12/05	12/06	12/07	12/08	12/09	12/10	12/11	12/12	EPSttm	Years	HGROWI		TAEGR**
	1.350	1.580	1.720	1.720	1.920	2.260	2.660	2.810	3.190	8	- Calc 10.85	5% 9	6.07%
				Calae Der Ch				_			HGROWT	TH ST	TAEGR
	6.835		irrent year		STRE	TD®					- Calc   16.28	396 9	3.37%
			in ent year			25 Oct 20	13 Price	e	49.59	1	Current NPM		
	19.79		videndReinv	estment St	trategy		EPS	ttm	3.190		16.59	<u>.</u>	Charl
1944		E G	Buy addition	nal shares					43.53		Current ROB	- N	
	52.70		Invest at the	e rate below	1		PEF	Ratio	13.53		0.00		Chart
							HGr	owth	10.85	%			
	11.40	NO NO	ote: PE and F	R Ratios a	re ave of 4	l yrs	Payo	ut	67	%	Current PE	<u>.</u>	-
	7.00	-i -					r aye	, di	0.1		15.55 w		Chart
	1									2	2		
	15.35										oh Current Price	<u> </u>	
	9.49	14		-		-	Tax - dividends		0	% L0	49.59 w		Char
	le re	Inve	stment Perio	d 5	У	ears	lax - umuenus	>		201	Current PF		
	45	38					Tax - capital ga	ains	0	%	74%	<u>.</u>	Char
			Calculate	13.159	6	per year		SVDCW	ith TARG	1 -	1/470		Griat.
current year	ST	TRET _	di manananan		in the second se	per jea		Oylic w		-	Reg Return	15.0	96
		25 Oct :	COLORADO DE LA	e 1	59	2	Dividend Reinv	estment St	rateov		EPStm	3.190	
<ul> <li>Dividend Reinvest</li> <li>Buy additional</li> </ul>		0	EPS		190		· Buy addition				PERatio	13.53	-
C Invest at the rai			PEI	Ratio 13	.53		C Invest at the	rate below			10.200	10.85	<u> </u>
			HGI	owth 10	.85 %		lote: PE and PR	Define ere	min of Aliza		HGrowth	10000	55
Note: PE and PR P	Ratios are ave	of 4 yrs	Pay	out 67	96		IOIE. PE and PR	Rapos are	ave of 4 yrs		Payout	67	56
				eren de									
	10		Tax - dividend	s 0	%					Tax -	dividends	1	96
nvestment Period	5	years	Tax - capital g	-	94	In	westment Perio	d 5	years	9) ST	capital gains	0	96
	the second	-	rue - capital g				-	1 Internet		198.		10	
Calculate	13.15%	per year		Sync with	TARG		Calculate	\$45.63			Sync	with STR	6.E

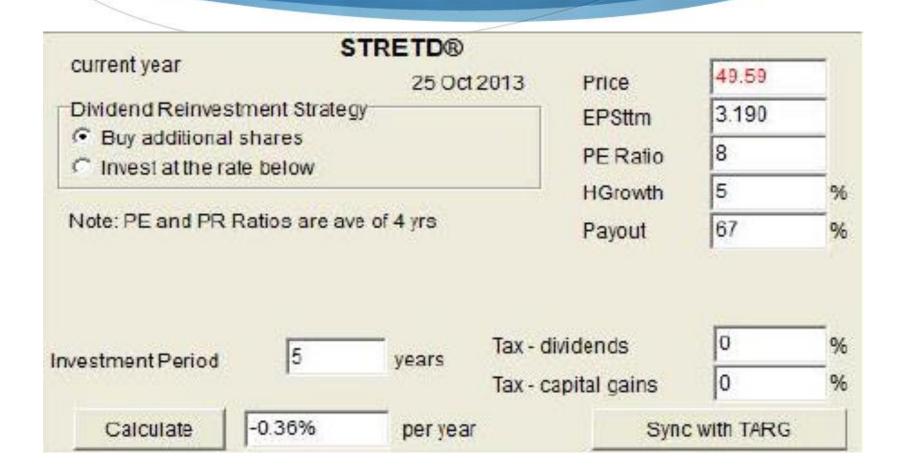
# **Conscious Investor Safety**

	STRETD®		100	
current year	25 Oct 2	2013 Price	49.59	11
Dividend Reinvestment \$	Strategy	EPSttm	3.190	
Buy additional shares		PERatio	12.63	
C Invest at the rate belo	vv	HGrowth	10.72	9
Note: PE and PR Ratios	are ave of 4 yrs	Payout	67	9
nvestment Period	years	Tax - dividends Tax - capital gains	0	9
		ion oopnal game	0.72	100

# **Conscious Investor Kill it**

current year	STRETD® 25 Oct 2013	8 Price	49.59	
Dividend Reinvestment S	strategy	EPSttm	3.190	_
Buy additional shares Invest at the rate belo		PE Ratio	11	_
s investature rate bero	w	HGrowth	7	%
Note: PE and PR Ratios	are ave of 4 yrs	Payout	67	%
vestment Period	years	- dividends - capital gains	0	%

# Conscious Investor Kill it again

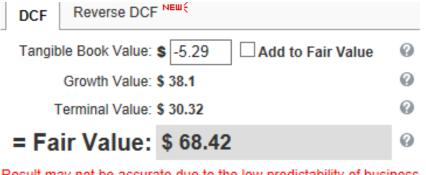


# Discounted Cash Flow-5-year EBITDA Growth

#### Financial Data of Lorillard, Inc.

Annual Rates (per share)	10 yrs	5 yrs	12 months
Revenue Growth (%)		20.30	8.10
EBITDA Growth (%)		16.10	18.10
Earning Growth (%)		14.00	18.40
Free Cash Flow Growth (%)		12.50	37.90





Result may not be accurate due to the low predictability of business Margin Of Safety: 26%

# Discounted Cash Flow-5-Year Earnings Growth

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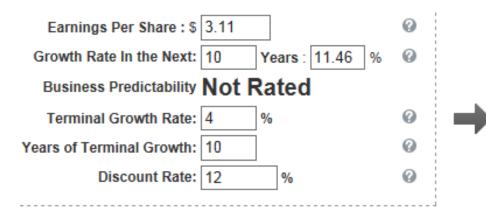


Margin Of Safety: 15%

# Discounted Cash Flow-Break Even

#### Financial Data of Lorillard, Inc.

Annual Rates (per share)	10 yrs	5 yrs	12 months
Revenue Growth (%)		20.30	8.10
EBITDA Growth (%)		16.10	18.10
Earning Growth (%)		14.00	18.40
Free Cash Flow Growth (%)		12.50	37.90



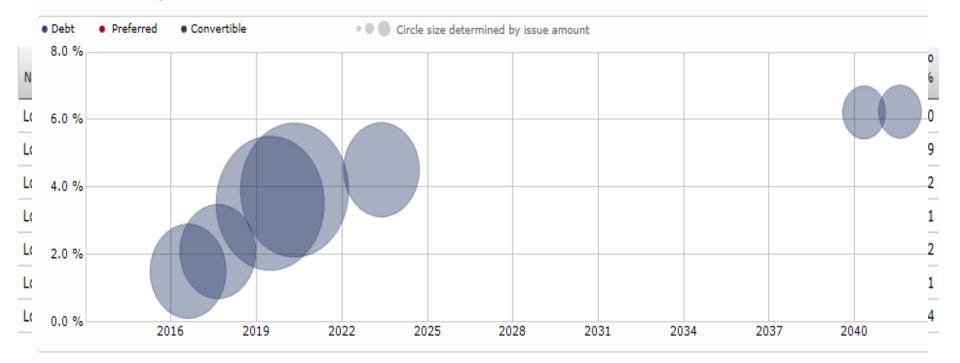
DCF Reverse DCF NEW	
Tangible Book Value: \$ -5.29 Add to Fair Value	0
Growth Value: \$ 30.29	0
Terminal Value: \$ 20.16	0
= Fair Value: \$ 50.45	0
Becult may not be accurate due to the low predictability of busi	noce

Result may not be accurate due to the low predictability of business

Margin Of Safety: 0%

# Morningstar Debt Analysis

**Yield to Maturity** 



# Van den Berg Metrics



# Comparison

	Ticker	Price /	EV /	Price /	▲ P
		Earnings	EBITDA	Book	Sales
Þ	LO 🗷	16.0	9.9	-	2.9
Þ	RAI 🗵	18.1	11.3	5.5	3.4
Þ	мо 🗵	17.0	10.2	21.0	4.3
	Summary	17.0	10.5	22.3	3.5

## **Recent News**

- Lawsuits continue over asbestos in Kent cigarette filters
- Blue E-Cigarettes help Lorillard Capture Half of the U.S. Market
- Acquired British-based SKYCIG

# Conclusion

- Tremendous share buybacks
- Shareholder oriented
- Low capital expenditures
- Poised for growth

#### Recommendation

Due to the recent appreciation of Lorillard, the Berkshire Anne Hathaway's would like to:

- Write a put with a strike price of 50, and a limit order on the premium of 1.50
- Annualized rate of return on premium of 21%