

Taking Stock: Pfizer might be good for what ails you

by Malcolm_Berko

Dear Mr. Berko: Please tell me what you think of Pfizer Pharmaceutical. My broker wants me to buy 300 shares (\$7,500) for my joint account, which has an income orientation. We are in our early 70s and we do not want to expose ourselves to risks, as a result about 70 percent of our money is in bonds, CDs and annuities. Please tell me about Pfizer and if you think it's a conservative investment.

G.J.

Kankee, Ill.

Dear G.J.: If you are a couch potato, like most Americans, you can thank Pfizer Inc. (PFE-\$24.24) for sponsoring so many of those mindless TV programs I call "bubble gum for the brain." You've seen those ubiquitous ads for Zithromax (antibiotic), Lipitor (cholesterol), Zoloft (antidepressant), Aricept (Alzheimer's), Zyrtec (antihistamine), Viagra (impotence), Cardura (cardiovascular) and Diflucan (antifungal). It seems that the majority of TV advertisements are sponsored by drug companies and every so often you catch yourself looking for a matching illness so you too can try Zoloft or Zithromax or Zyrtec. Sometimes, I find myself pining for those old cigarette ads and the Marlboro man.

But I think you'll like the company.

The drug industry has been in the doldrums for the past few years but there's good evidence of improvement as better than expected earnings have begun to attract investors. That earnings improvement is expected to continue into 2008 and 2009. Resultantly, the shares of a number of long-depressed companies have revived of late. Worth noting are the mid-sized specialty drug companies which are often cited as take over targets by their growth-starved larger brethren. Also worth noting is the new Medicare Part D that provides drug access to millions of older Americans who, in the past, could not afford to purchase many medications.

The drug industry is beginning to gain favor once again and PFE shares, which have traded in a narrow range for the last three years, looks like a stellar "long-term buy!" While it may be another 18 to 24 months for PFE to break out of its low trading range, PFE's impressive 4.7 percent dividend yield makes that wait easy and worthwhile. And PFE's dividend record is a dandy - this company has increased its dividend for 40 consecutive years. You'll like that too!

Revenues have been flat as a flapjack and management must replace nearly \$12 billion in revenues, which will be lost when Lipitor comes off patent in 2011. As a result, new management is maximizing revenues from its current drug portfolio, as evidenced by TV ads and an aggressive marketing campaign.

Management has been eliminating redundant costs, reducing expenses, buying back shares and forming small operating divisions that will improve innovation and accountability.

But PFE's drug pipeline is PFE's lifeline. There are 180 new drugs/compounds in development stages, 39 of which are in Phase II trials and six of which are in Phase III trials. PFE's research and development pipeline has never been larger or more fecund and management believes its pipeline will aggressively drive revenue growth in 2011, when Lipitor with \$12 billion in revenues comes off patent. Don't worry!

PFE has a strong cash position and management will probably use that cash to acquire a competitor as it did with Warner Lambert in 2000 and Pharmacia (Upjohn) in 2003. However, I think that small to mid-sized acquisitions are more likely as they would add new products without increasing administration and infrastructure costs, which new management is in the process of streamlining. And that's good.

PFE's gross margins of 85 percent exceed the industry average of 67 percent and operating margins of 30 percent compare favorably to Merck's 24.4 percent. PFE's price-earnings ratio of just under 11 is compelling and so is its 22 percent return on equity and its phenomenal net profit margin of 33 cents on each dollar of revenue.

However, Bear Stearns, Prudential, JP Morgan and HSBC recently downgraded the stock to neutral. But those people are idiots. I think PFE could be a \$40 to \$45 stock in the next three years and the high dividend will certainly put a floor on the stock if the market falters.

So give your broker a hug and a gold star for recognizing and undervalued and classy issue. This stock will make an excellent addition to your portfolio.

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