intelligent OPTION INVESTOR

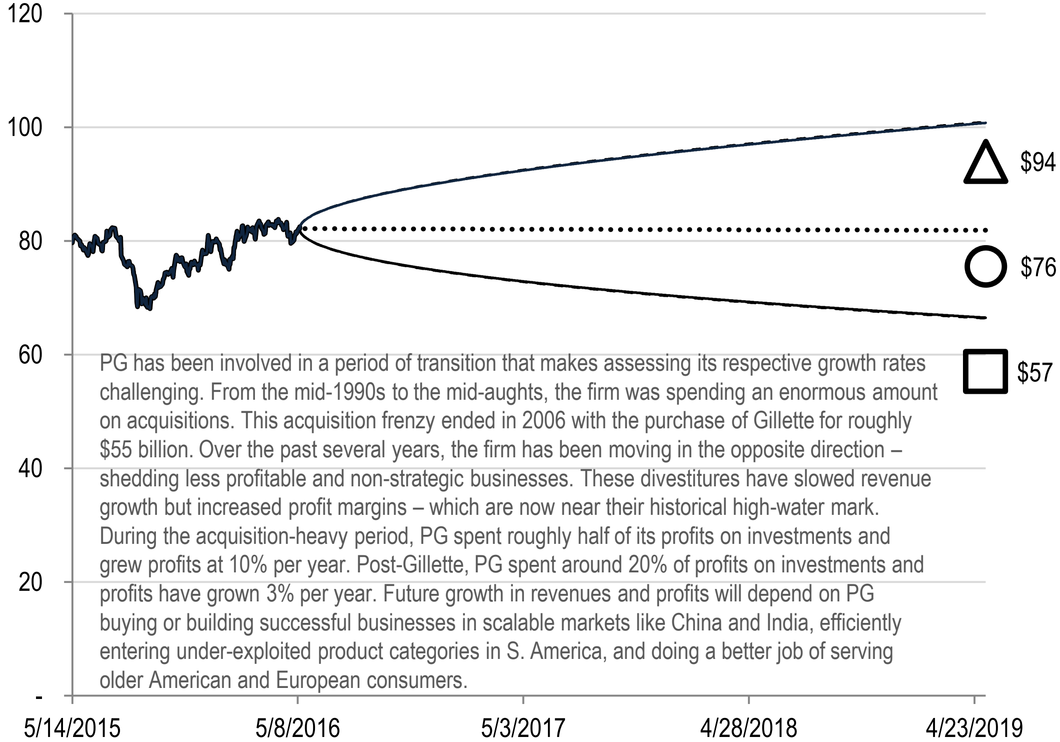
Valuation Only

IOI does not see the opportunity for an attractive risk / reward balance investment in PG at this time

IOI Tear Sheet : Procter & Gamble (PG)

Valuation Only

Data as of 9 June, 2016



PG has been involved in a period of transition that makes assessing its respective growth rates challenging. From the mid-1990s to the mid-aughts, the firm was spending an enormous amount on acquisitions. This acquisition frenzy ended in 2006 with the purchase of Gillette for roughly $55 billion. Over the past several years, the firm has been moving in the opposite direction – shedding less profitable and non-strategic businesses. These divestitures have slowed revenue growth but increased profit margins – which are now near their historical high-water mark. During the acquisition-heavy period, PG spent roughly half of its profits on investments and grew profits at 10% per year. Post-Gillette, PG spent around 20% of profits on investments and profits have grown 3% per year. Future growth in revenues and profits will depend on PG buying or building successful businesses in scalable markets like China and India, efficiently entering under-exploited product categories in S. America, and doing a better job of serving older American and European consumers.

IOI's Take

By shedding brands and headcount, P&G is undergoing the largest transformation in the Company's long history and the jury is still out on how it will turn out. Operationally, the Company has committed to returning $70Bn to shareholders by the end of FY19. This implies FCFO of roughly 13Bn or so annually going forward, a step change increase. To deliver this and not tap reserves or debt, PG has to increase profits by roughly $1.5Bn annually. They have a combination of Ad agency and supply chain rationalizations in place to deliver this. The question is can PG use it's focused brand portfolio and EM opportunities to restart meaningful revenue growth.

Drivers

Revenues	A culling of brands means revenue growth has stalled. Future EM growth + elder focus in US best prospects for growth. Proj: 4% (Best), 2% (Worst)
Profitability	Current rationalization may succeed in boosting profits to the 20% OCP margin level. Proj: 19% (B), 15% (W)
Investment Level / Eff.	Smarter, smaller EM acquisitions and cutting operational fat drive best-case. Proj (med-term growth): 8% (B), 3% (W)
Balance Sheet	Net $14 billion of value for expected Coty transaction.

Valuation & Return

Valuation Uncertainty: MED

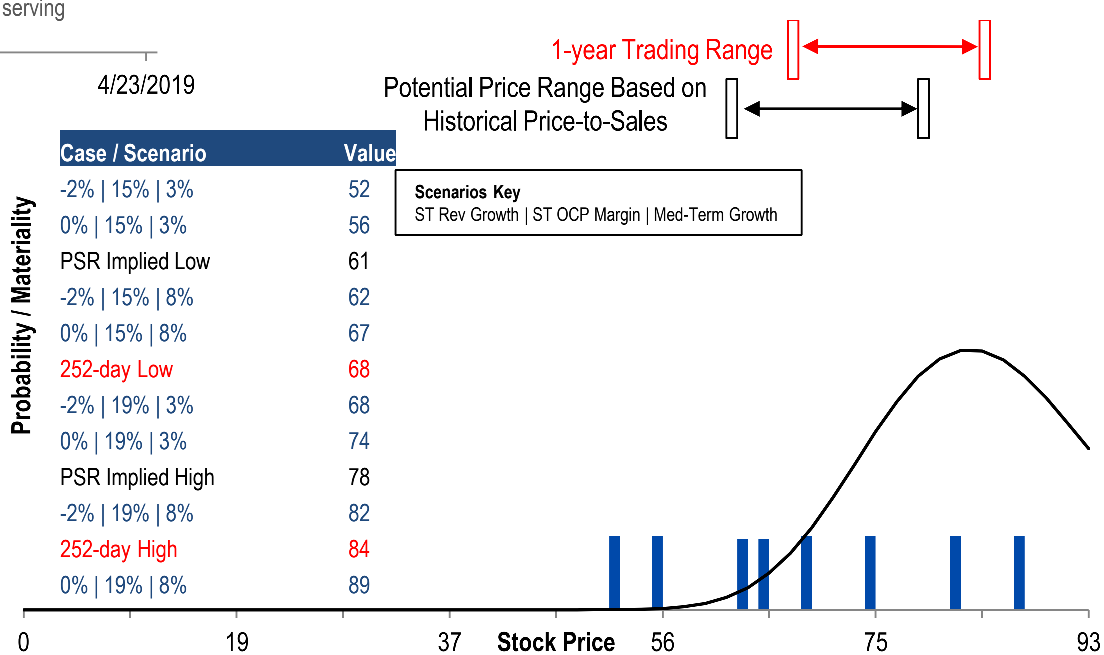
	Low	Likely	High
Stock Fair Value ($)	57	76	94
Stock Return (%)	-31	-9	13
Option Period Return (%)	NA	NA	NA
Option Annual Return (%)	NA	NA	NA

Historical Metrics

	Historical Median	
	5-year	10-year
Revenue Growth (%)	0	1
Profit Margin (%)	13	14
Med-term Growth	Neg	Flat

Market Risk

On a PS Ratio basis, we believe the market is giving PG the benefit of the doubt. Even best-case revenues generate an upper price range of $78/share. Top and bottom quartile of PSR used.



Case / Scenario	Value
-2% | 15% | 3%	52
0% | 15% | 3%	56
PSR Implied Low	61
-2% | 15% | 8%	62
0% | 15% | 8%	67
252-day Low	68
-2% | 19% | 3%	68
0% | 19% | 3%	74
PSR Implied High	78
-2% | 19% | 8%	82
252-day High	84
0% | 19% | 8%	89

Scenarios Key
ST Rev Growth | ST OCP Margin | Med-Term Growth