Apple Stock Hits an All-Time High: Buy, Sell, or Hold?

Description

Thanks to a nice 2.7% increase on Friday, **Apple** (NASDAQ: AAPL) stock finished the trading day at a new all-time high. Zooming out further, shares are up 50% year to date and more than 100% over the past three years. It's been a great run for Apple shareholders to say the least.

But with shares trading sharply higher, what should investors think of the stock at this level? Is it still a compelling buy? Or has Apple's valuation become too rich, making the stock a hold or — even worse — a sell?

While the tech stock certainly isn't the bargain it was earlier this year, a close look at some of the company's key catalysts and the stock's valuation relative to its underlying cash flow suggest shares remain attractive — even at a new all-time high of $236.

What about declining iPhone revenue?

Of course, any investment thesis for Apple stock has to address the elephant in the room: declining iPhone sales. After all, the iPhone continues to account for the bulk of Apple's business; the smartphone segment accounted for 56% of trailing-12-month revenue.

But investors should realize that the iPhone segment is up against tough comparisons in fiscal 2018, when the company's new iPhone X and iPhone 8 helped drive double-digit revenue growth in the segment. Further, declines in the segment have moderated recently, lessening the segment's negative impact on Apple's consolidated results and implying that the decline could eventually come to a halt; iPhone revenue was down 12% year over year in fiscal Q3, compared with a 17% decline in fiscal Q2.

Also worth noting, Apple saw great signs of improvement in iPhone sales in the last month of its third quarter of fiscal 2019. iPhone sales in Apple's retail and online stores, for instance, returned to year-over-year growth during the month of June.

Apple’s next big growth drivers

Fortunately, however, Apple’s iPhone segment doesn’t need to return to growth in order for the company’s total revenue and profits to rise in the coming years. A growing iPhone business, therefore, would just be icing on the cake.

Apple is becoming less dependent on iPhone thanks to its rapidly growing services business — the company’s second-largest segment. In the nine months ended Jun. 29, 2019, services accounted for 17.2% of revenue — up from 14.3% of revenue in the same period in 2018.Â Going forward, services will likely grow to represent an even larger portion of total sales, as Apple’s services business is firing on all cylinders. In the tech company’s most recent quarterly conference call, management said the segment benefited from double-digit revenue growth in the app store, Apple Music, cloud services, and AppleCare. Even more, Apple Pay and the company’s App Store advertising business grew by triple-digit rates year over year.

Then there’s Apple’s wearables business, which is included in the company’s wearables, home, and accessories segment. This segment is just half the size of Apple’s services business, but it’s growing at an impressive rate. Wearables, home, and accessories revenue increased 37% year over year in the trailing nine months. Furthermore, revenue from the company’s wearables products (Apple Watch, AirPods, and Beats headphones), increased at a rate greater than 50% year over year in Apple’s fiscal third quarter.

Gobs of free cash flow

But the best bull case for Apple stock is simply its conservative valuation. The company brought in $58.2 billion in free cash flow in the trailing-12-month period ending June 29. This means Apple currently trades at just 18 times its annual free cash flow. Comparatively, **Microsoft** and **Alphabet** trade at 28 and 31 times free cash flow, respectively.

Further supporting its valuation, of course, is Apple’s mountain of cash on its balance sheet. The company ended its most recent quarter with $102 billion of net cash.

Sure, Apple may now have a $1.067 trillion valuation. But recent improvement in iPhone sales trends, strong growth in services and wearables, and a conservative valuation make Apple stock worth considering even after its 50% gain this year.

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