



Johnson & Johnson (JNJ)

Updated July 4th, 2018 by Nate Parsh

Key Metrics

Current Price: \$123	5 Year CAGR Estimate: 8.6%	Volatility Percentile: 5.0%
Fair Value Price: \$129	5 Year Growth Estimate: 4.8%	Momentum Percentile: 24.5%
% Fair Value: 95%	5 Year Valuation Multiple Estimate: 0.9%	Valuation Percentile: 68.6%
Dividend Yield: 2.9%	5 Year Price Target: \$162	Total Return Percentile: 54.7%

Overview & Current Events

Johnson & Johnson is a diversified health care company and a leader in the area of pharmaceuticals, medical devices and consumer products. JNJ was founded in 1886 and employs more than 125,000 people around the world. The company generated more than \$76 billion in revenues in 2017, half of which came from outside the United States.

JNJ has spent heavily on acquiring companies that fit with its business model. One such is example is the company's \$30 billion all cash purchase of Actelion, which closed on June 16th of 2017. Actelion brings to JNJ a line-up of high margin medicines for rare diseases and should be accretive to earnings this year.

JNJ reported 1st quarter earnings on April 17th. The company earned \$2.06 per share, topping estimates by \$0.05 and growing 12.6% year over year. The company reported sales of \$20 billion, also a 12.6% increase from Q1 2017. This was \$630 million above what analysts had expected.

Growth on a Per-Share Basis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
EPS	\$4.57	\$4.63	\$4.76	\$5.00	\$5.10	\$5.52	\$5.70	\$5.48	\$5.93	\$7.30	\$8.10	\$10.24
DPS	\$1.80	\$1.93	\$2.11	\$2.25	\$2.40	\$2.59	\$2.76	\$2.95	\$3.15	\$3.32	\$3.54	\$5.06

JNJ has grown earnings over the past 10 years at a rate of 4.8%. The company managed to grow earnings before, during and after the last recession, showing that JNJ's products are in demand regardless of market conditions. Because of improving business performance and tax reform, the company forecasts that earnings per share will grow by 11% in 2018. To create a margin of safety, we calculate 2023's earnings estimate at by applying the company's historical growth rate (4.8%) to 2018's earnings per share midpoint (\$8.10). This gives an estimate of \$10.24 per share for 2023.

During Q1, each business unit showed impressive growth. Consumer (~17% of sales) grew revenues by 5.3% thanks to Beauty and Oral Care products. The Pharma division (~49% of sales) grew 19.4% year over year. Losses from *Remicade* were offset by gains in *Simponi*, *Stelara*, *Xarleto* and others. Medical Devices (34% of sales) had revenues growth of more than 19%.

With 55 years of growth, JNJ has one of the most impressive dividend growth streaks available in the market. The average dividend increase over the past 10 years is 7.4%. JNJ gave shareholders a 7.1% increase on April 26th. Based off of the current annualized dividend, investors could see the dividend become \$5.06 per share by 2023. At these estimates, the company would be paying out just 49.4% of earnings in the form of dividends. This would allow the company to potentially offer higher dividend growth in future years.

Valuation Analysis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	Now	2023
Avg. P/E	14.3	12.5	13.1	12.7	13.1	15.6	17.7	18.2	19.1	20.9	15.1	15.8
Avg. Yld.	2.8%	3.3%	3.4%	3.5%	3.6%	3.0%	2.7%	3.0%	2.8%	2.6%	2.9%	3.1%

JNJ's stock has dropped about 5 points since our April 8th update, presenting investors with an even cheaper valuation. Based off of 2018's EPS guidance, shares trade with a multiple of just 15.1, down from 15.8. JNJ has an average price to earnings multiple of almost 15.8 per year over the past decade. If JNJ's stock were to see its price-to-earnings ratio rise to the decade long average by 2023, then shares would see multiple expansion of about 0.9% per year.

JNJ has often paid shareholders a generous dividend. The stock's current yield is above the S&P 500's and very close to that of the 10-year Treasury Bond. The company offers a solid combination of price appreciation and dividend income.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
GP/A	53.4%	45.9%	41.6%	39.3%	37.6%	36.9%	39.6%	36.4%	35.6%	32.5%	34%	39.9%
Debt/A	49.9%	46.6%	45%	49.8%	46.6%	44.2%	46.5%	46.7%	50.1%	61.8%	59.2%	48.7%
Int. Cov.	234.6	44.9	50	26.9	30.6	39.1	45.3	46.6	57.3	33.9	39.3	60.9
Payout	39.4%	41.7%	44.3%	45%	47.1%	46.9%	48.4%	53.8%	53.1%	45.5%	43.7%	49.4%
Std. Dev.	30.4%	17.8%	13%	17.5%	9.8%	12.8%	14.7%	16.4%	13.3%	11.5%	12.3%	15.7%

Based on the company's ability to improve earnings in 2008 and 2009, JNJ can be considered a recession proof company. By having a diversified business model of drugs, devices and consumer products, JNJ is insulated to a certain degree from business slowdowns in any one division.

Even with more than 5 decades of dividend growth, JNJ has a reasonably low dividend payout ratio. After the most recent increase, the company has a payout ratio of less than 44%. This gives JNJ ample room to raise its dividend even in a prolonged recession. If EPS grows at a faster than historical rate, the dividend could grow at a much higher rate.

Final Thoughts & Recommendation

We forecast that Johnson & Johnson can offer a total return of 8.6% per year through 2023, up from our earlier estimate of 7.4%. This is largely due to a decline in share price, making shares attractively valued relative to its history. Our estimate is a combination of earnings growth (4.8%), dividends (2.8%) and multiple expansion (0.9%). Given the company's leadership in the healthcare sector, impressive dividend growth history and relatively recession proof business, we continue to think JNJ is one of the safest investments available to investors. Johnson & Johnson is one of only 2 companies to receive a AAA rating from Standard & Poor's (Microsoft is the other), which speaks to its safety. We recommend investors who don't already own JNJ consider adding the name to their portfolio. The recent price decline offers even more upside potential. We maintain our 2023 price target of \$162.

Total Return Breakdown by Year

