



Medtronic PLC (MDT)

Updated August 22nd, 2018 by Nick McCullum

Key Metrics

Current Price: \$95	5 Year CAGR Estimate: 4.8%	Volatility Percentile: 14.9%
Fair Value Price: \$80	5 Year Growth Estimate: 6.0%	Momentum Percentile: 54.2%
% Fair Value: 119%	5 Year Valuation Multiple Estimate: -3.3%	Valuation Percentile: 32.7%
Dividend Yield: 2.1%	5 Year Price Target \$107	Total Return Percentile: 27.1%

Overview & Current Events

Medtronic is the largest manufacturer of biomedical devices and implantable technologies in the world. The company operates in more than 140 countries and has over 84,000 employees. Medtronic currently has four operating segments: Cardiac and Vascular Group, Minimally Invasive Therapies Group (MITG), Diabetes Group, and Restorative Therapies Group. Medtronic has increased its dividend for 40 consecutive years and is a member of the Dividend Aristocrats Index.

Prospective Medtronic investors should note that the company has established tax residence in Ireland. Dividends are considered Irish source income and Irish dividend withholding tax may automatically be applied to Medtronic's dividend payments. Many investors will qualify for an exemption from this withholding tax. You can read more information about the tax treatment of Medtronic's dividends [here](#).

In late August, Medtronic reported financial results for the first quarter of fiscal 2019 (which ended on July 27th, 2018). In the quarter, the company reported worldwide revenue of \$7.4 billion, which represents a reported decrease of 0.1% over the same period a year ago. With that said, this revenue decline is attributable completely to the divestiture of Medtronic's Patient Care, Deep Vein Thrombosis, and Nutritional Insufficiency businesses, which were sold to fellow Dividend Aristocrat Cardinal Health (CAH). Excluding this divestiture, Medtronic generated organic revenue growth of 6.8%. On the bottom line, Medtronic generated GAAP net income and GAAP earnings-per-share of \$1.1 billion and \$0.79, respectively, while adjusted net income and adjusted earnings-per-share were \$1.6 billion and \$1.17. On an adjusted basis, Medtronic's earnings-per-share increased 9% over the same period a year ago.

Medtronic also updated its fiscal 2019 financial guidance with the publication of its third quarter earnings release. More specifically, the company increased its organic revenue growth guidance from 4.0%-4.5% to 4.5%-5.0%. On the bottom line, Medtronic now expects adjusted diluted earnings-per-share to increase by 9%-10% versus 8%-9% previously.

Growth on a Per-Share Basis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
EPS	\$2.60	\$2.92	\$3.22	\$3.36	\$3.02	\$3.37	\$3.41	\$4.28	\$4.37	\$4.60	\$4.77	\$5.20	\$6.96
DPS	\$0.63	\$0.82	\$0.90	\$0.97	\$1.04	\$1.12	\$1.22	\$1.52	\$1.72	\$1.81	\$1.84	\$2.07	\$3.05

After reading Medtronic's revised financial guidance, we now believe the company is likely to deliver adjusted earnings-per-share of around \$5.20 in fiscal 2019. Our long-term growth estimate of 6.0% has remain unchanged for the company. Applying a 6% growth rate to our new 2019 earnings-per-share estimate allows us to calculate a new 2024 earnings-per-share estimate of \$6.96. Our dividend estimates remain unchanged, and we continue to believe that Medtronic's dividend growth will outpace its earnings growth for the foreseeable future.

Valuation Analysis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	Now	2023
Avg. P/E	18.0	12.0	12.1	11.0	13.2	15.3	18.5	17.6	18.4	17.7	18.2	15.4
Avg. Yld.	1.5%	2.1%	2.4%	2.6%	2.5%	2.0%	1.8%	2.0%	2.1%	2.1%	2.3%	2.5%

Disclosure: This analyst has a long position in the security discussed in this research report.

Medtronic's stock price has risen noticeably since the publication of our last quarterly research report. The company is now trading at a price-to-earnings ratio of 18.2 using our new 2019 earnings-per-share estimate. For context, Medtronic has traded at an average price-to-earnings ratio of 15.4 over the last decade. Valuation contraction is likely to impair Medtronic's future returns at its current price. A 5-year period of earnings multiple mean reversion would introduce a 3.3% headwind to this company's returns during that time period.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2023
GP/A	47.0%	42.7%	38.8%	37.5%	35.8%	33.4%	13.1%	19.8%	20.5%	22.9%	20.0%	25.0%
Debt/A	44.1%	47.9%	47.5%	47.9%	46.4%	48.8%	50.1%	47.8%	49.6%	44.4%	45.0%	45.0%
Int. Cov.	15.4	17.8	14.2	30.2	30.7	37.8	14.8	6.0	7.8	9.1	9.0	10.0
Payout	28.1%	28.0%	28.9%	34.4%	33.2%	35.8%	35.5%	39.4%	39.3%	40.4%	40.4%	45.0%
Std. Dev.	31.9%	23.6%	28.3%	18.2%	16.0%	18.3%	20.6%	19.0%	15.0%	15.0%	18.0%	18.0%

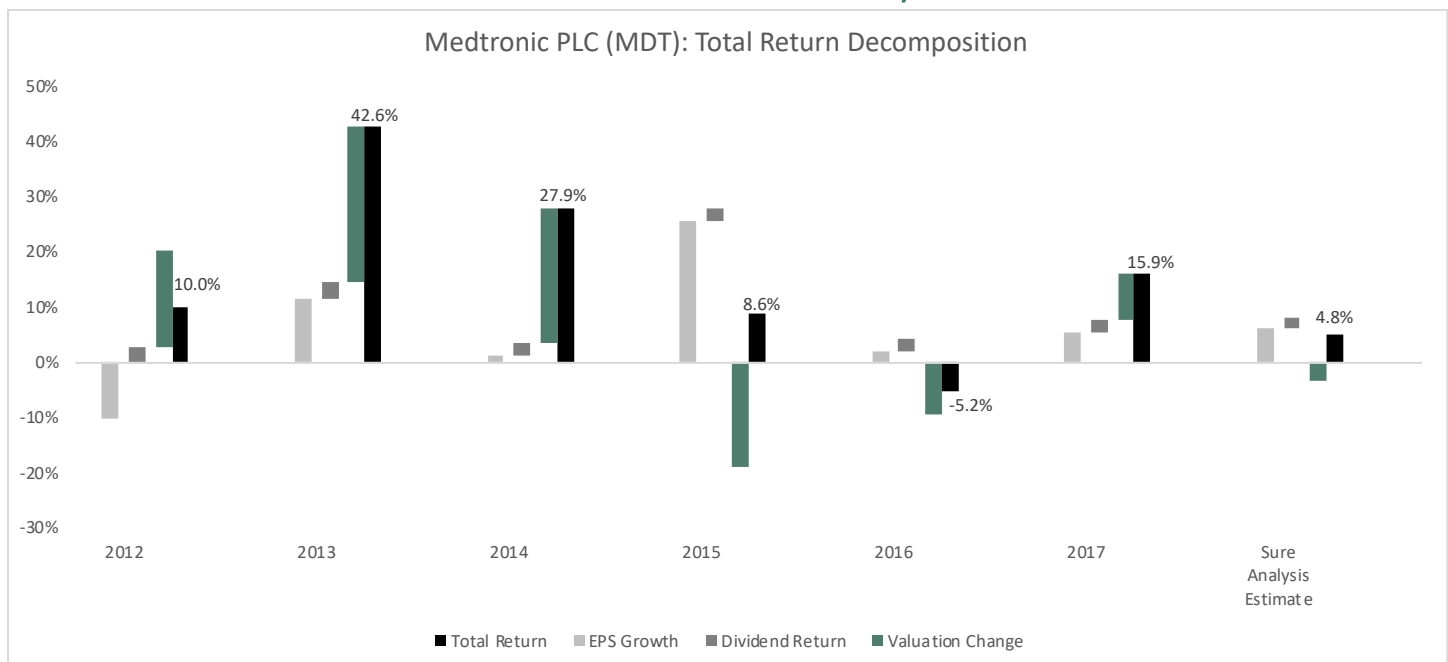
Medtronic's most compelling competitive advantage is its intellectual leadership in a complicated industry within the healthcare sector. It has filed more than 53,000 patents and spends more than \$2 billion per year on research and development. Medtronic also has a strong product pipeline that should drive its growth for the foreseeable future.

Medtronic's gross profits as a percent of its assets have declined over time, primarily due to margin compression. Debt to total assets remains firmly below the 50% mark, while the dividend payout ratio has slowly increased and its interest coverage remains adequate. Medtronic's financial house is in order. We believe the company's financial positioning combined with the recession-resistant nature of the healthcare industry make it appealing for conservative investors.

Final Thoughts & Recommendation

The recent increase in Medtronic's stock price has dramatically reduced its expected total returns. The company is not attractive at current prices. Investors who hold the stock at a cost basis that is significantly below its current market price in a taxable investment account may want to continue holding the shares, simply due to Medtronic's unquestionable business quality. Otherwise, our recommendation is to sell Medtronic and reinvest the proceeds into more attractively-valued opportunities within the healthcare space.

Total Return Breakdown by Year



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