



Medtronic plc (MDT)

Updated August 20th, 2019 by Eli Inkrot

Key Metrics

Current Price:	\$109	5 Year CAGR Estimate:	2.8%	Volatility Percentile:	22.2%
Fair Value Price:	\$84	5 Year Growth Estimate:	6.0%	Momentum Percentile:	72.1%
% Fair Value:	131%	5 Year Valuation Multiple Estimate:	-5.2%	Growth Percentile:	54.2%
Dividend Yield:	2.0%	5 Year Price Target	\$112	Valuation Percentile:	18.4%
Dividend Risk Score:	A	Retirement Suitability Score:	B	Total Return Percentile:	16.4%

Overview & Current Events

Medtronic PLC is the largest manufacturer of biomedical devices and implantable technologies in the world. The company serves physicians, hospitals and patients in more than 150 countries and has over 90,000 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 42 consecutive years. The \$147 billion market cap company generates \$30 billion in revenue and \$7 billion in annual profits.

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](#).

On August 20th, 2019 Medtronic reported Q1 fiscal 2020 results for the period ending July 26th, 2019. (Medtronic's fiscal year ends on the Friday closest to April 30th). For the quarter Medtronic reported sales of \$7.49 billion, representing a 1.5% increase (+3.5% on a constant currency basis), compared to Q1 fiscal year 2019. The Cardiac and Vascular Group saw revenue decline 0.7% to \$2.79 billion. Meanwhile, the MITG, Restorative Therapies and Diabetes segments recorded increases of 2.3%, 3.2% and 3.5% to \$2.10 billion, \$2.01 billion and \$592 million, respectively. Net income equaled \$877 million or \$0.64 per share compared to \$1.08 billion or \$0.79 per share in the year ago period. On an adjusted basis, net income equaled \$1.7 billion or \$1.26 per share compared to \$1.6 billion or \$1.17 per share in Q1 2019.

Medtronic also updated its fiscal year 2020 guidance. The company now expects revenue growth of 4% on an organic basis (unchanged, but 0.8% to 1.2% less on a reported basis if current currency rates hold) and adjusted earnings-per-share of \$5.54 to \$5.60 (from \$5.44 to \$5.50 previously). We have increased our forecast accordingly.

Growth on a Per-Share Basis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
EPS	\$3.22	\$3.37	\$3.46	\$3.75	\$3.82	\$4.28	\$4.34	\$4.60	\$4.77	\$5.23	\$5.57	\$7.45
DPS	\$0.82	\$0.90	\$0.97	\$1.04	\$1.12	\$1.22	\$1.52	\$1.72	\$1.84	\$2.00	\$2.16	\$3.12
Shares¹	1,097	1,070	1,037	1,016	999	1,422	1,399	1,369	1,354	1,341	1,350	1,325

Note that Medtronic has already completed fiscal year 2019 (ending in April) but we have elected to show the information above closer to the actual calendar year. Over the past decade Medtronic has been able to grow earnings-per-share by about 6% per annum. With current guidance for 5.9% to 7.1% improvement this year, we believe 6% growth over the intermediate-term is a reasonable starting point as Medtronic's pipeline in new treatments could lead to further market share gains.

The dividend is a storied topic at Medtronic, having not only been paid but also increased for over four decades. Still, the payout ratio remains more than reasonable, allowing for dividend growth (10%+ annually for the last decade) to continue outpacing earnings-per-share growth. Note that the significant jump in outstanding shares in 2014 was a result of Medtronic's \$42.9 billion cash and stock acquisition of Covidien. Moving forward we anticipate that share repurchase activity will aid bottom line growth to a small degree.

1: In millions.

Disclosure: This analyst has no position in the security discussed in this research report, and no plans to initiate one in the next 72 hours.



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Valuation Analysis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	Now	2025
Avg. P/E	12.3	11.0	10.7	11.3	14.6	16.1	17.3	17.7	17.3	17.3	19.6	15.0
Avg. Yld.	2.1%	2.4%	2.6%	2.5%	2.0%	1.8%	2.0%	2.1%	2.2%	2.2%	2.0%	2.8%

From 2008 through 2012 shares routinely traded in the 10 to 14 times earnings range. Then from 2013 through today, it has been typical to see the security trade hands in the 15 to 18 times earnings range, even bumping up to 20 times earnings a couple of times; this despite the idea that the firm has been exceptionally consistent through that entire period. Our expectation splits the difference and assumes a “fair” multiple of 15 times earnings. With shares now trading near 20 times earnings, this implies the potential for a meaningful valuation headwind. This could be too conservative considering the quality of the firm, but it is in-line with the average valuation over the last decade.

The dividend yield is not spectacular, but income investors should be encouraged by the safety of the payout and its ability to grow significantly over time.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
Payout	26%	27%	26%	28%	29%	29%	35%	37%	39%	38%	39%	42%

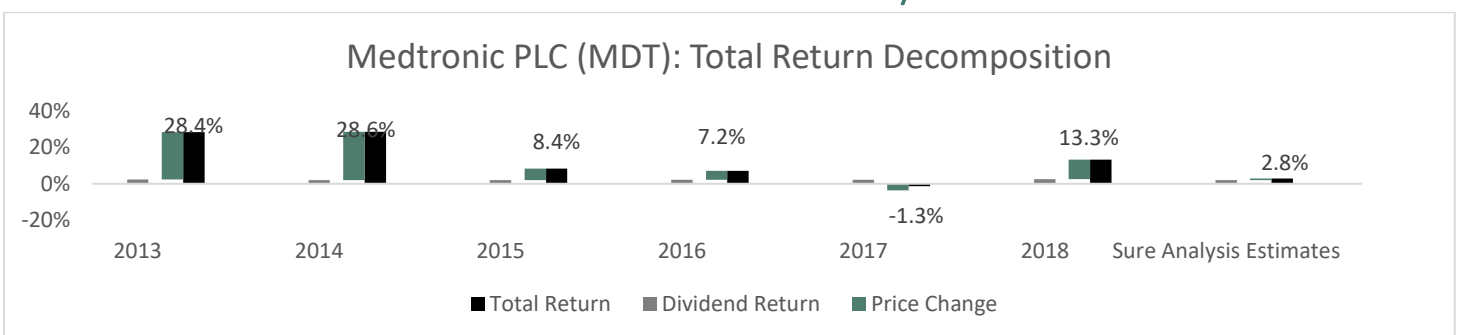
Medtronic’s most compelling competitive advantage is its intellectual leadership in a complicated industry within the healthcare sector. It has filed more than 53,000 patents and spends more than \$2 billion per year on research and development. Medtronic also has a strong product pipeline that should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

During the last recession Medtronic posted earnings-per-share of \$2.61, \$2.92, \$3.22, \$3.37 and \$3.46 during the 2007 through 2011 stretch. In addition, the dividend kept on increasing every year as well. While the payout ratio has been climbing from 26% in 2009 to nearly 40% today, this still leaves ample room for dividend growth combined with share repurchases. Moreover, the balance sheet is good shape as current assets cover current liabilities by a wide margin and the debt load is well serviced by the ~\$7 billion underlying profit machine.

Final Thoughts & Recommendation

Shares are up 17% since our last report, while earnings expectations have improved moderately. From a quality, earnings and dividend growth standpoint, Medtronic is attractive. However, our total annual return expectation is just 2.8%, stemming from 6% growth and the 2.0% dividend yield offset by a potential -5.2% valuation headwind. If Medtronic were to continue trading at ~19+ times earnings, the security is set up to offer high single-digit returns. Alternatively, if the price returns to a lower valuation, as had been the case in prior years, the total returns do not look compelling. Collectively, we continue to rate Medtronic as a hold.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Revenue	15817	15508	16184	16590	17005	20261	28833	29710	29953	30557
Gross Profit	12005	11808	12295	12464	12672	13952	19691	20416	20886	21402
Gross Margin	75.9%	76.1%	76.0%	75.1%	74.5%	68.9%	68.3%	68.7%	69.7%	70.0%
SG&A Exp.	5415	5427	5623	5698	5847	6904	9469	10018	10238	10418
D&A Exp.	772	804	833	819	850	1306	2820	2917	2644	2659
Operating Profit	4662	4460	4483	4770	4818	4557	5960	5986	6034	6632
Operating Margin	29.5%	28.8%	27.7%	28.8%	28.3%	22.5%	20.7%	20.1%	20.1%	21.7%
Net Profit	3099	3096	3617	3467	3065	2675	3538	4028	3104	4631
Net Margin	19.6%	20.0%	22.3%	20.9%	18.0%	13.2%	12.3%	13.6%	10.4%	15.2%
Free Cash Flow	3496	3240	3986	4485	4563	4331	4172	5626	3616	5873
Income Tax	870	609	730	784	640	811	798	578	2580	547

Balance Sheet Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Total Assets	28090	30424	32818	34900	37943	106685	99644	99857	91393	89694
Cash & Equivalents	1400	1382	1172	919	1403	4843	2876	4967	3669	4393
Accounts Receivable	3335	3822	3808	3727	3811	5112	5562	5591	5987	6222
Inventories	1481	1695	1800	1712	1725	3463	3473	3338	3579	3753
Goodwill & Int. Ass.	10950	12314	12581	13002	12879	68631	68399	61922	61266	60519
Total Liabilities	13461	14456	15705	16229	18500	53455	47581	49527	40571	39482
Accounts Payable	420	511	565	681	742	1610	1709	1555	1628	1953
Long-Term Debt	9519	9835	10454	10499	11775	36041	30970	33413	25731	25308
Shareholder's Equity	14629	15968	17113	18671	19443	53230	52063	50208	50720	50091
D/E Ratio	0.65	0.62	0.61	0.56	0.61	0.68	0.59	0.67	0.51	0.51

Profitability & Per Share Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Return on Assets	12.0%	10.6%	11.4%	10.2%	8.4%	3.7%	3.4%	4.0%	3.2%	5.1%
Return on Equity	22.3%	20.2%	21.9%	19.4%	16.1%	7.4%	6.7%	7.9%	6.2%	9.2%
ROIC	14.1%	12.4%	13.6%	12.2%	10.2%	4.4%	4.1%	4.8%	3.9%	6.1%
Shares Out.	1,097	1,070	1,037	1,016	999	1,422	1,399	1,369	1,354	1,341
Revenue/Share	14.26	14.34	15.27	16.15	16.78	18.27	20.22	21.35	21.89	22.51
FCF/Share	3.15	3.00	3.76	4.37	4.50	3.91	2.93	4.04	2.64	4.33

Note: All figures in millions of U.S. Dollars unless per share or indicated otherwise.

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