



# UnitedHealth Group, Inc. (UNH)

Updated January 19<sup>th</sup>, 2020 by Josh Arnold

## Key Metrics

<b>Current Price:</b>	\$298	<b>5 Year CAGR Estimate:</b>	7.8%	<b>Market Cap:</b>	\$283B
<b>Fair Value Price:</b>	\$264	<b>5 Year Growth Estimate:</b>	9.0%	<b>Ex-Dividend Date:</b>	03/09/20 <sup>1</sup>
<b>% Fair Value:</b>	113%	<b>5 Year Valuation Multiple Estimate:</b>	-2.4%	<b>Dividend Payment Date:</b>	03/19/20 <sup>2</sup>
<b>Dividend Yield:</b>	1.4%	<b>5 Year Price Target</b>	\$406	<b>Years Of Dividend Growth:</b>	10
<b>Dividend Risk Score:</b>	B	<b>Retirement Suitability Score:</b>	D	<b>Last Dividend Increase:</b>	20.0%

## Overview & Current Events

UnitedHealth dates back to 1974 when Charter Med was founded by a group of health care professionals looking for ways to expand healthcare options for consumers. UnitedHealth has certainly done that in the decades since and now offers global healthcare services to tens of millions of people via a wide array of products. The company has two major reporting segments: UnitedHealth and Optum. The former provides global healthcare benefits to individuals, employers and Medicare/Medicaid beneficiaries. The Optum segment is a services business that seeks to lower healthcare costs and optimize outcomes for its customers. UnitedHealth's market capitalization is \$283 billion and it produces about \$260 billion in revenue annually, making it one of the largest companies in America.

UnitedHealth reported Q4 and full-year earnings on January 15<sup>th</sup> and while results missed top line consensus, the bottom-line beat thanks to stronger margins. The UnitedHealthcare business saw full-year revenue of \$194 billion, up 5.6% from 2018, thanks to customer growth in Medicare Advantage and commercial benefits. Full-year operating earnings were up 13.3% to \$10.3 billion as margins improved.

Optum saw full-year revenue growth of 11.5% to \$113 billion, with OptumHealth being the primary driver. Full-year earnings from operations grew 13.7% to \$9.4 billion, again thanks to operating margin expansion. Interestingly, each segment within Optum produced double-digit operating earnings growth for 2019, so strength was broad-based.

The consolidated UnitedHealth Group produced 7% revenue growth in 2019 to \$242 billion on strong growth across the portfolio. Earnings from operations were up 13.5% to \$19.7 billion thanks to rising revenue and expanding margins. Earnings-per-share rose to \$15.11 from \$12.19 in 2018 and for Q4, earnings-per-share rose 19% year-over-year.

The company's full-year medical care ratio came to 82.5%, up from 81.6% in 2018, as the impact of the health insurance tax deferral was partially offset by cost efficiency improvements. The full-year operating cost ratio of 14.5% was down from 15.1% in the prior year as cost savings more than offset growth investment spending.

UnitedHealth guided for adjusted earnings-per-share of \$16.25 to \$16.55 for 2020, so our initial estimate is \$16.50.

## Growth on a Per-Share Basis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
<b>EPS</b>	\$4.10	\$4.73	\$5.28	\$5.50	\$5.70	\$6.01	\$8.05	\$10.07	\$12.19	\$15.11	<b>\$16.50</b>	<b>\$25.39</b>
<b>DPS</b>	\$0.41	\$0.61	\$0.80	\$1.05	\$1.41	\$1.88	\$2.38	\$2.88	\$3.45	\$4.14	<b>\$4.32</b>	<b>\$7.00</b>
<b>Shares<sup>3</sup></b>	1,086	1,070	1,019	988	954	953	952	969	968	962	<b>955</b>	<b>930</b>

We see forward earnings-per-share growth of 9% annually as UnitedHealth continues to buy back stock and generate strong revenue growth. However, this would mean that growth is slowing somewhat from more recent rates as the buyback loses some of its effectiveness due to a higher stock price, and as sheer size makes it more difficult to grow. We do not believe the company's very impressive run of earnings-per-share growth is ending by any means, but a slight

<sup>1</sup> Estimated date

<sup>2</sup> Estimated date

<sup>3</sup> Share count in millions

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reduction in growth expectations over the next five years seems prudent. Margin expansion is also playing a meaningful part in the earnings growth story, as evidenced again in 2019.

## Valuation Analysis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	Now	2025
Avg. P/E	8.0	9.8	10.4	11.9	14.7	19.4	16.8	18.4	20.4	16.5	<b>18.1</b>	<b>16.0</b>
Avg. Yld.	1.2%	1.3%	1.5%	1.6%	1.7%	1.6%	1.8%	1.5%	1.4%	1.7%	<b>1.4%</b>	<b>1.7%</b>

UnitedHealth's price-to-earnings multiple has moved significantly higher since our last update and today, stands at 18.1. The business has posted continuously strong earnings growth rates and as such, investors have assigned a high-teens multiple in recent years. With shares trading above our fair value estimate of 16 times earnings, this could drive a modest headwind to annual total returns. We see the yield remaining about where it is over time as dividend increases consume a slightly greater proportion of earnings, but the yield should remain comfortably below 2%.

## Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
Payout	10%	13%	15%	19%	24%	31%	29%	28%	28%	27%	<b>26%</b>	<b>28%</b>

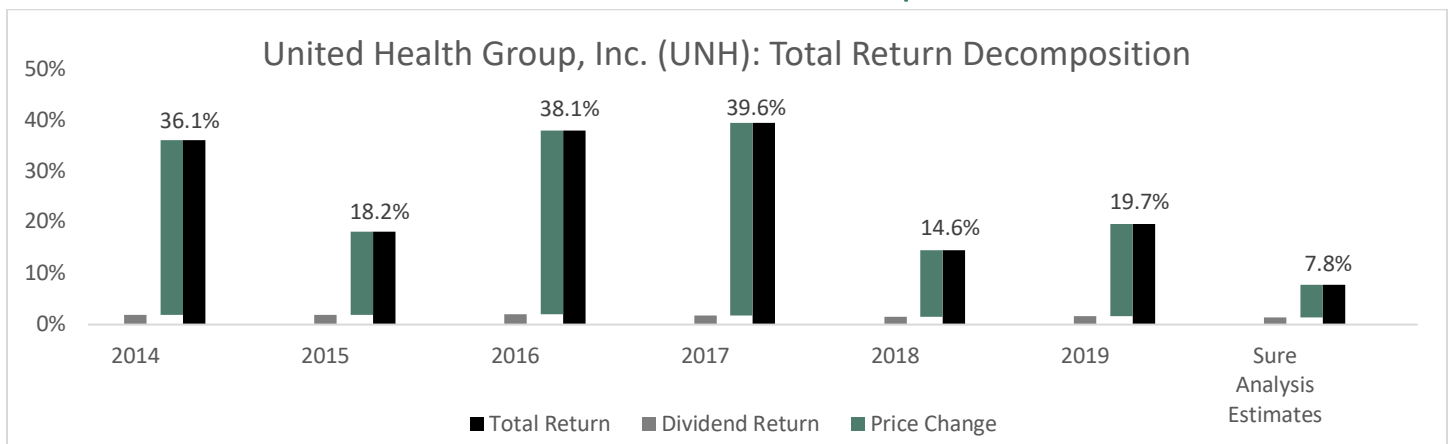
As mentioned, we see the payout ratio rising over time, as UnitedHealth's dividend is ultra-safe today. At less than one-third of earnings, UnitedHealth has tremendous flexibility in terms of returning capital to shareholders. Its outstanding earnings growth should only strengthen this over time.

UnitedHealth's competitive advantage is in its gargantuan scale as well as its deeply entrenched customers with high switching costs. Like a utility, health and wellness providers have high switching costs, accruing significant benefits to incumbents like UnitedHealth. It is also quite resistant to recessions as its services are necessities in most cases.

## Final Thoughts & Recommendation

We see UnitedHealth as a premier growth stock that is now trading somewhat above its fair value. Its strong growth forecast makes it attractive to growth investors, while its high rate of dividend growth makes it attractive for those seeking longer term income. We forecast total annual returns of 7.8%, consisting of the current 1.4% yield, 9% earnings growth and a small headwind from the valuation. UnitedHealth is an attractive long-term story offering high rates of earnings and dividend growth. However, the recent rally has pushed the valuation out of our comfort zone, so we are moving from buy to hold.

## Total Return Breakdown by Year



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## Income Statement Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
<b>Revenue (\$B)</b>	93.55	101.21	109.94	121.74	129.70	156.40	184.01	200.14	224.87	240.27
<b>Gross Profit</b>	22589	24491	27189	29194	32236	36316	42558	45988	52470	55712
<b>Gross Margin</b>	24.1%	24.2%	24.7%	24.0%	24.9%	23.2%	23.1%	23.0%	23.3%	23.2%
<b>SG&amp;A Exp.</b>	14270	15557	17306	18941	21263	24312	28401	29557	34074	
<b>D&amp;A Exp.</b>	1064	1124	1309	1375	1478	1693	2055	2245	2428	2720
<b>Operating Profit</b>	7255	7810	8574	8878	9495	10311	12102	14186	15968	17799
<b>Op. Margin</b>	7.8%	7.7%	7.8%	7.3%	7.3%	6.6%	6.6%	7.1%	7.1%	7.4%
<b>Net Profit</b>	4634	5142	5526	5625	5619	5813	7017	10558	11986	13839
<b>Net Margin</b>	5.0%	5.1%	5.0%	4.6%	4.3%	3.7%	3.8%	5.3%	5.3%	5.8%
<b>Free Cash Flow</b>	5395	5901	6085	5684	6526	8184	8090	11573	13650	16392
<b>Income Tax</b>	2749	2817	3096	3242	4037	4363	4790	3200	3562	3742

## Balance Sheet Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
<b>Total Assets (\$B)</b>	63.06	67.89	80.89	81.88	86.38	111.25	122.81	139.06	152.22	173.89
<b>Cash &amp; Equivalents</b>	9123	9429	8406	7276	7495	10923	10430	11981	10866	
<b>Acc. Receivable</b>	2061	2294	2709	3052	4252	6523	8152	9568	11388	11822
<b>Goodwill &amp; Int.</b>	25655	26770	35968	35448	36609	52844	56125	63045	68235	
<b>Total Liabilities</b>	37238	39597	49707	49733	53928	77529	84633	89225	97902	113453
<b>Accounts Payable</b>	9220	16652	17988	19033	21287	26324	29752	33051	36596	21690
<b>Long-Term Debt</b>	13503	11638	16754	16860	17406	31965	32970	31692	36554	40678
<b>Total Equity</b>	25825	28292	31178	32149	32454	33830	38274	47776	51696	60436
<b>D/E Ratio</b>	0.52	0.41	0.54	0.52	0.54	0.94	0.86	0.66	0.71	0.67

## Profitability & Per Share Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
<b>Return on Assets</b>	7.6%	7.9%	7.4%	6.9%	6.7%	5.9%	6.0%	8.1%	8.2%	8.5%
<b>Return on Equity</b>	18.7%	19.0%	18.6%	17.8%	17.4%	17.5%	19.5%	24.5%	24.1%	24.7%
<b>ROIC</b>	12.1%	13.0%	12.6%	11.6%	11.4%	10.1%	10.3%	13.8%	13.9%	14.4%
<b>Shares Out.</b>	1,086	1,070	1,019	988	954	953	952	969	968	962
<b>Revenue/Share</b>	82.71	93.11	105.10	119.01	131.54	161.73	190.10	203.18	228.76	248.73
<b>FCF/Share</b>	4.77	5.43	5.82	5.56	6.62	8.46	8.36	11.75	13.89	16.97

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

### Disclaimer

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