ResMed Inc. (RMD)

Updated January 31st, 2020 by Jonathan Weber

Key Metrics

Current Price:	$165	**5 Year CAGR Estimate:**	-0.8%	**Market Cap:**	$23.0B
Fair Value Price:	$84	**5 Year Growth Estimate:**	12.0%	**Ex-Dividend Date:**	02/06/20
% Fair Value:	196%	**5 Year Valuation Multiple Estimate:**	-12.6%	**Dividend Payment Date:**	03/14/20
Dividend Yield:	0.9%	**5 Year Price Target**	$148	**Years Of Dividend Growth:**	7
Dividend Risk Score:	C	**Retirement Suitability Score:**	F	**Last Dividend Increase:**	5.4%

Overview & Current Events

ResMed is a medical devices company that engages in the development, manufacturing and marketing of devices that diagnose, treat and manage respiratory disorders. The company was founded in 1989, is headquartered in San Diego, CA, and is currently valued at $23 billion.

ResMed reported its second quarter (fiscal 2020) earnings results on January 30. The company reported revenues of $736 million for the quarter, which represents an increase of 13.1% compared to the prior year's quarter. At constant currency rates, ResMed would have been able to grow its revenues even quicker, by 14%. Sales growth for ResMed's software as a service business grew at a fast pace of 37% year-over-year, although the business unit is still not very large, which is why the majority of company-wide revenue growth is generated in other business units. ResMed was able to grow its margins further, the company boosted its gross margin by 60 basis points, to 59.7%.

ResMed generated earnings-per-share of $1.21 during the second quarter, which beat analyst estimates easily, by $0.18. ResMed's earnings-per-share were up 21% compared to the prior year's quarter. ResMed also was able to boost its cash flows from operations by 31% year over year, to $232 million for the first half of 2020.

Growth on a Per-Share Basis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
EPS	$1.23	$1.44	$1.71	$2.10	$2.39	$2.47	$2.49	$2.82	$3.53	$3.64	***$4.00***	***$7.05***
DPS	---	---	---	$0.68	$1.00	$1.12	$1.20	$1.32	$1.40	$1.48	***$1.56***	***$2.51***
Shares[1]	151	152	142	142	140	141	141	142	143	143	***142***	***140***

ResMed has been a reliable growth investment over the last several years. The company produced a very compelling 15% earnings-per-share growth rate through the last decade and was not impacted by the last financial crisis.

This growth rate was possible through a combination of revenue increases, some margin expansion, and a declining share count. Revenue growth was the most important factor, which ResMed achieved through growing its product portfolio, as well as via geographic expansion. Through focused R&D, ResMed was able to establish itself as the global leader in sleep apnea management, an indication with a large market that is still severely underpenetrated.

Studies show that up to one-fourth of adults have sleep apnea. In many major markets market penetration is still below 10%, which is why ResMed has a lot of potential to grow its revenues going forward, even without expanding its product lineup. All that is required will be investments into sales & marketing and additional manufacturing capacity. Chronic obstructive pulmonary disease (COPD) is another indication with need for treatment where ResMed is establishing itself.

ResMed is also actively working at the intermixture between medtech and information technology. ResMed is investing heavily into connected health solutions, as this is deemed a major growth market over the coming decades. ResMed's offerings include end-to-end systems for sleep and respiratory care and cloud-based diagnostic testing.

ResMed is active in attractive markets, the company remains hungry, and growth is unlikely to slow down going forward. Revenue increases and possible margin expansion due to improving economics of scale should drive profits rapidly.

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[1] In Millions

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Valuation Analysis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	Now	2025
Avg. P/E	21.8	22.3	17.2	20.0	20.3	23.4	22.7	26.1	29.2	34.1	***41.3***	***21.0***
Avg. Yld.	---	---	---	1.6%	2.1%	1.9%	2.1%	2.0%	1.3%	1.2%	***0.9%***	***1.7%***

ResMed is a high-quality company with a compelling earnings growth track record, and the earnings growth outlook over the coming years is positive as well. This justifies an above-average valuation multiple, which is why shares were valued at more than 20 times profits throughout most of the last decade. We see a fair value of 21 times net profits, but shares trade massively above that level right now, which is why the stock looks severely overvalued today.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
Payout	---	---	---	32.4%	41.8%	45.3%	48.2%	46.8%	39.7%	38.5%	***39.0%***	***35.6%***

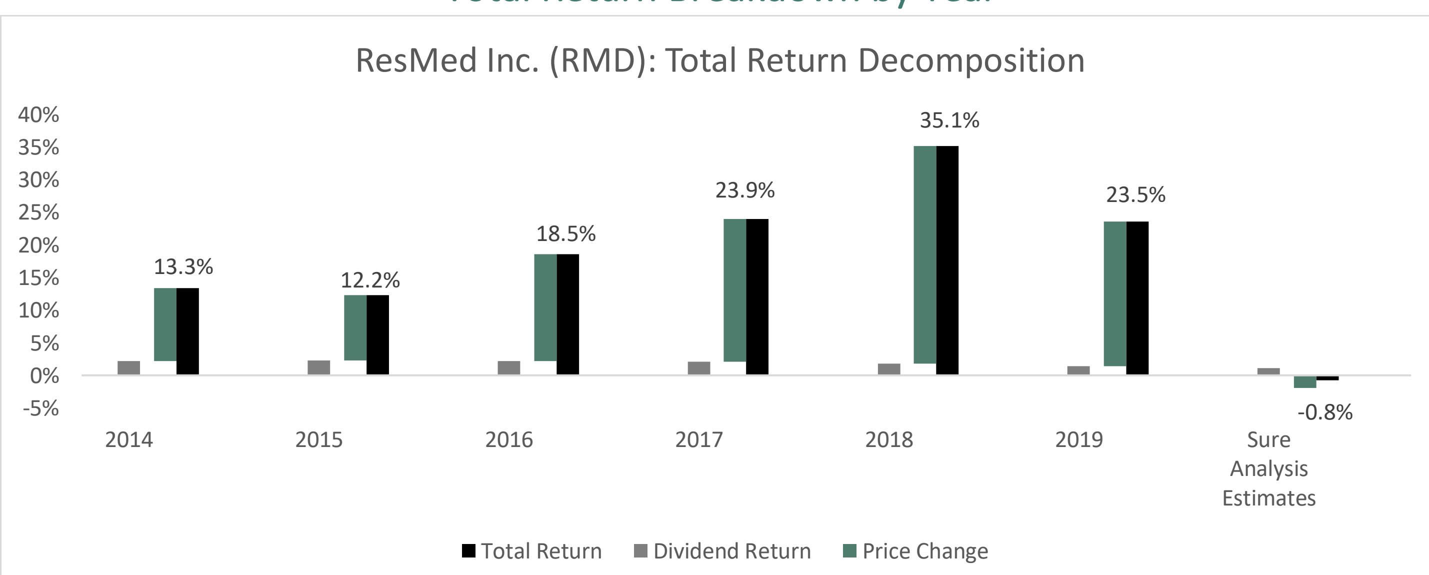
ResMed only started paying dividends in 2013, but since then the dividend has grown consistently. The most recent dividend increase of 5% was below the average dividend growth rate over the last couple of years. Due to a relatively low dividend payout ratio of ~40%, the dividend looks quite safe. The low yield makes the dividend unattractive, though.

ResMed is smaller than many of its medtech peers, but it is very well positioned in the niche it addresses, and it owns strong products and a respectable IP portfolio. We believe that ResMed will continue to be a dominant player in the markets that it targets; competition does not seem to be a problem. The company's products are needed whether the economy is doing well or not, which is why ResMed is not a cyclical company. The company's earnings-per-share continued to grow through the Great Recession, and this will most likely be the case during future recessions as well.

Final Thoughts & Recommendation

ResMed is a high-quality medtech company that targets an attractive market and that has achieved compelling earnings growth rates in the past. We believe that ResMed will be able to grow profitably during the coming years as well, and the company will also continue to grow its dividend. Shares trade significantly above our fair value estimate, though, which is why we rate ResMed a sell, even though the company looks strong on a fundamental basis.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Revenue	1092	1243	1369	1514	1555	1679	1839	2067	2340	2607
Gross Profit	655	741	821	941	990	1011	1066	1202	1362	1537
Gross Margin	60.0%	59.6%	60.0%	62.1%	63.7%	60.2%	58.0%	58.1%	58.2%	59.0%
SG&A Exp.	329	372	403	431	450	479	488	554	600	645
D&A Exp.	62	71	86	78	73	73	87	112	120	151
Operating Profit	243	267	294	355	411	409	436	457	560	636
Operating Margin	22.3%	21.5%	21.5%	23.4%	26.5%	24.4%	23.7%	22.1%	23.9%	24.4%
Net Profit	190	227	255	307	345	353	352	342	316	405
Net Margin	17.4%	18.3%	18.6%	20.3%	22.2%	21.0%	19.2%	16.6%	13.5%	15.5%
Free Cash Flow	127	210	322	331	310	311	480	343	434	382
Income Tax	71	77	77	78	86	83	87	76	206	114

Balance Sheet Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Total Assets	1626	2069	2138	2211	2361	2182	3257	3468	3064	4108
Cash & Equivalents	489	735	810	876	906	717	731	822	189	147
Accounts Receivable	227	274	283	318	360	363	382	451	484	528
Inventories	186	201	174	146	165	247	224	268	269	350
Goodwill & Int. Ass.	230	283	311	324	335	311	1359	1327	1284	2378
Total Liabilities	339	338	530	600	603	594	1562	1508	1005	2035
Accounts Payable	58	55	55	61	85	81	93	93	93	116
Long-Term Debt	122	100	251	301	301	301	1173	1079	281	1271
Shareholder's Equity	1288	1731	1608	1611	1758	1587	1695	1960	2059	2072
D/E Ratio	0.09	0.06	0.16	0.19	0.17	0.19	0.69	0.55	0.14	0.61

Profitability & Per Share Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Return on Assets	12.1%	12.3%	12.1%	14.1%	15.1%	15.5%	13.0%	10.2%	9.7%	11.3%
Return on Equity	15.8%	15.0%	15.3%	19.1%	20.5%	21.1%	21.5%	18.7%	15.7%	19.6%
ROIC	14.2%	14.0%	13.8%	16.3%	17.4%	17.9%	14.8%	11.6%	11.7%	14.2%
Shares Out.	151	152	142	142	140	141	141	142	143	143
Revenue/Share	7.04	7.91	9.17	10.34	10.77	11.77	12.98	14.51	16.25	18.04
FCF/Share	0.82	1.34	2.16	2.26	2.15	2.18	3.39	2.40	3.01	2.64

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