Stryker Corporation (SYK)

Updated July 31st, 2020 by Nathan Parsh

Key Metrics

Current Price:	$190	**5 Year CAGR Estimate:**	7.6%	**Market Cap:**	$75 billion
Fair Value Price:	$146	**5 Year Growth Estimate:**	12.0%	**Ex-Dividend Date:**	9/29/2020
% Fair Value:	130%	**5 Year Valuation Multiple Estimate:**	-5.1%	**Dividend Payment Date:**	10/30/2020
Dividend Yield:	1.2%	**5 Year Price Target**	$258	**Years Of Dividend Growth:**	26
Dividend Risk Score:	A	**Retirement Suitability Score:**	C	**Last Dividend Increase:**	10.6%

Overview & Current Events

Stryker is a global leader in the medical device sector. The company's product lines include surgical equipment, neurovascular products and orthopedic implants. The company was founded in 1941 by Dr. Homer Stryker because he felt that products that the medical device industry offered were not meeting the needs of his patients. Today, the company employs more than 33,000 people worldwide. The company completed its $1.4 billion purchase of K2M in November of 2018. This acquisition has helped Stryker take greater market share in the spinal surgery market.

Stryker released second quarter earnings on 7/30/2020. Revenue declined 24.4% to $2.8 billion. The company's adjusted earnings-per-share decreased $1.34, or 68%, to $0.64, though this was $0.07 higher than expected.

COVID-19 caused a severe decline on both the top and bottom-line during the second quarter as the health care system prioritized dealing with the pandemic over performing elective surgeries. Organic growth declined 24% in the quarter. Organic sales for Orthopedics declined 29.3% due to fewer hip, knee and trauma procedures. Mako was stable. MedSurg was down 17%, with a 22.2% decline in the U.S. Instruments were especially weak due to lower sales for power tools and waste management. Endoscopy sales decreased 34% on lower business for video general surgery, communications and sports medicine. Neurotechnology & Spine was lower by nearly 30% as all neurotech units suffered a severe slowdown. Adjusted gross margins declined 850 basis points to 57.3%. Stryker operated at 60% of capacity in the second quarter. Business improved in several regions as the quarter progressed. The U.S., China, Australia and Germany elective procedures returned to at least the 85% mark of pre-COVID levels by the end of the quarter. Latin America and India were still seeing declines. The company has guided towards average capacity of 85% in the third quarter. Consensus estimates have been raised to $6.36 from $6.33 previously.

Growth on a Per-Share Basis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
EPS	$3.33	$3.72	$3.39	$2.63	$2.36	$3.78	$4.35	$6.49	$7.28	$8.26	***$6.36***	***$11.21***
DPS	$0.63	$0.75	$0.90	$1.10	$1.26	$1.42	$1.57	$1.70	$1.93	$2.14	***$2.30***	***$4.05***
Shares[1]	390	381	381	378	379	373	375	374	373	380	***376***	***368***

Stryker has grown earnings-per-share at a rate of 14% per year since 2008. The company was very resilient during the last recession, only seeing a $0.01 decline in earnings in 2009. The company did see earnings declines in 2013 and 2014 as well, but growth quickly returned in the ensuing years. While the COVID-19 impact will have a short-term impact on results due to the postponement of elective surgeries, demand for Stryker's products should rebound during the recovery from the pandemic. We have increased our earnings growth rate to 12% from 10% to account for this. This is still a slight discount to the company's long-term growth rate. Stryker has increased its dividend at an average rate of almost 15% per year over the past 10 years, though that growth has slowed recently. The company increased its dividend by 10.6% for the 1/31/2020 payment. We see the payout rising to $4.05 per share by 2025, up from the current $2.30.

---

[1] Share count in millions

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

Stryker Corporation (SYK)

Updated July 31st, 2020 by Nathan Parsh

Valuation Analysis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2018	Now	2025
Avg. P/E	15.7	14.8	15.8	25.9	35.2	25.2	25.4	28.7	22.0	25.4	***29.9***	***23.0***
Avg. Yld.	1.2%	1.4%	1.7%	1.6%	1.5%	1.5%	1.4%	1.2%	1.2%	1.0%	***1.2%***	***1.6%***

Shares of Stryker have increased $9, or 5%, since our 5/2/2020 update. Based off of updated estimates for 2020, shares trade with an earnings multiple of 29.9. Given the organic growth that the company is producing and the benefit from acquisitions, we are reaffirming our 2025 target P/E of 23. If shares reverted to our new target price-to-earnings ratio by 2025, then valuation would be a 5.1% headwind to annual returns over this time period. If Stryker were able to return to its average growth rate (14%), then shares would likely command a greater multiple.

Safety, Quality, Competitive Advantage, & Recession Resiliency

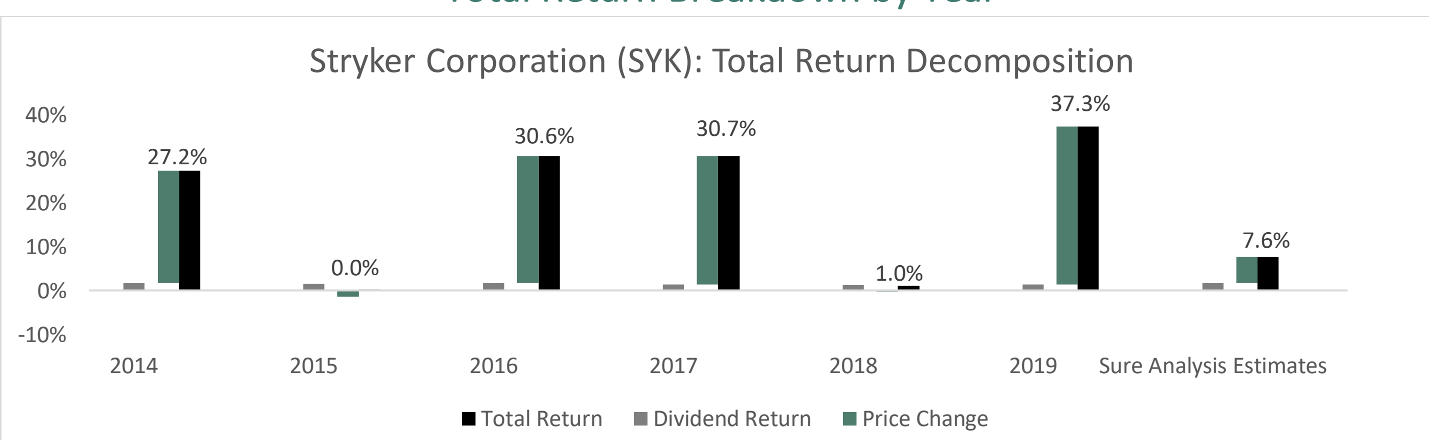
Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
Payout	19%	20%	27%	42%	53%	38%	36%	35%	27%	25%	***36%***	***36%***

Stryker's strength during the most recent recession should give shareholders the confidence that the company can thrive in a difficult economic climate. As the leader in the medical device sector, Stryker's products are in demand around the world. For example, the company continues to see growth in its Mako robot installations, as well as a higher number of procedures performed. These figures are likely to grow as more surgeons become comfortable with using a robot during surgery. Another competitive advantage Stryker has over its peers is its organic growth. Over the past 4 years, Stryker has averaged 6.4% organic growth while the medical device sector has averaged 4.2%. Investors are willing to pay up for that type of growth, which is why the company's price-to-earnings ratio has been higher than normal in recent years.

Final Thoughts & Recommendation

Following second quarter results, Stryker Corporation is now projected to return 7.6% annually over the next five years, down from our prior estimate of 8.6%. As with the prior quarter, Stryker was impacted by the COVID-19 pandemic. Elective surgeries were postponed as the health care system dealt with the spread of the virus. Several markets have seen an improvement in procedures as the quarter progressed. Stryker believes that the company will average 85% capacity across its entire business in the third quarter. This is a stark improvement from the second quarter and shows the demand for the company's products remains high. We have raised our 2025 price target $1 to $258 due to slightly higher EPS estimates and maintain our hold rating on the stock due to projected returns.

Total Return Breakdown by Year



[Click here to rate and review this research report. Your feedback is important to us.]

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

Stryker Corporation (SYK)

Updated July 31st, 2020 by Nathan Parsh

Income Statement Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Revenue	7320	8307	8657	9021	9675	9946	11325	12444	13601	14884
Gross Profit	5034	5496	5876	6019	6356	6602	7504	8180	8938	9696
Gross Margin	68.8%	66.2%	67.9%	66.7%	65.7%	66.4%	66.3%	65.7%	65.7%	65.1%
SG&A Exp.	2707	3150	3367	3467	3547	3610	4137	4552	5099	5356
D&A Exp.	223	282	277	307	378	397	546	642	723	778
Operating Profit	1875	1762	1915	1878	2007	2157	2333	2470	2560	2905
Operating Margin	25.6%	21.2%	22.1%	20.8%	20.7%	21.7%	20.6%	19.8%	18.8%	19.5%
Net Profit	1273	1345	1298	1006	515	1439	1647	1020	3553	2083
Net Margin	17.4%	16.2%	15.0%	11.2%	5.3%	14.5%	14.5%	8.2%	26.1%	14.0%
Free Cash Flow	1365	1208	1447	1691	1549	711	1425	961	2038	1542
Income Tax	456	341	407	206	645	296	274	1043	-1197	479

Balance Sheet Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Total Assets	10895	12146	13206	15743	17279	16223	20435	22197	27229	30167
Cash & Equivalents	1758	905	1395	1339	1795	3379	3316	2542	3616	4337
Accounts Receivable	1252	1417	1430	1518	1572	1662	1967	2198	2332	2893
Inventories	1057	1283	1265	1422	1588	1639	2030	2465	2955	3282
Goodwill & Int. Ass.	1775	3514	3566	5833	6204	5930	9864	10645	12726	13296
Total Liabilities	3721	4463	4609	6696	8684	7712	10885	12217	15499	17360
Accounts Payable	292	345	288	314	329	410	437	487	646	675
Long-Term Debt	1021	1768	1762	2764	3973	3998	6914	7222	9859	11090
Shareholder's Equity	7174	7683	8597	9047	8595	8511	9550	9966	11730	12807
D/E Ratio	0.14	0.23	0.21	0.31	0.46	0.47	0.72	0.72	0.84	0.87

Profitability & Per Share Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Return on Assets	12.8%	11.7%	10.2%	7.0%	3.1%	8.6%	9.0%	4.8%	14.4%	7.3%
Return on Equity	18.5%	18.1%	15.9%	11.4%	5.8%	16.8%	18.2%	10.5%	32.8%	17.0%
ROIC	17.2%	15.2%	13.1%	9.1%	4.2%	11.5%	11.4%	6.1%	18.3%	9.2%
Shares Out.	390	381	381	378	379	373	375	374	373	380
Revenue/Share	18.32	21.33	22.60	23.61	25.27	26.11	29.92	32.74	35.76	39.18
FCF/Share	3.42	3.10	3.78	4.43	4.05	1.87	3.76	2.53	5.36	4.06

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