Stryker Corporation (SYK)

Updated February 1st, 2021 by Nathan Parsh

Key Metrics

Current Price:	$225	**5 Year CAGR Estimate:**	11.1%	**Market Cap:**	$83 billion
Fair Value Price:	$207	**5 Year Growth Estimate:**	12.0%	**Ex-Dividend Date:**	3/29/2021[1]
% Fair Value:	109%	**5 Year Valuation Multiple Estimate:**	-1.7%	**Dividend Payment Date:**	4/30/2021[2]
Dividend Yield:	1.1%	**5 Year Price Target**	$365	**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.

Stryker announced fourth quarter and full year earnings results on 1/27/2021. For the quarter, revenue grew 3.2% to $4.26 billion, beating estimates by $64 million. Adjusted earnings-per-share grew 12.9% to $2.81, $0.26 better than expected. For the year, revenue fell 3.6% to $14.4 billion. Adjusted earnings-per-share totaled $7.43 per share, a 10% decline from the prior year, but $0.24 better than our estimates.

Organic growth fell 1.1% for the quarter, though this was much improved from a decline of 3.3%, 8.6% and 24% in the first three quarters of the year. Pricing was a 0.8% headwind to results, but foreign currency exchange added 1.2% to sales. Orthopaedics had an organic sales decline of 5.8%. Stryker's Mako install base grew 33% and the company sold and installed more than 100 robots in the fourth quarter. The U.S. business grew more than 7% organically, but this was offset by weakness in international markets due to procedural slowdowns related to COVID-19 restrictions. MedSurg had 1.3% organic growth (9.7% growth in the U.S.). Instrument sales were higher as gains in power tool, waste management and smoke evacuation offsetting weakness in the endoscopy business. Neurotechnology & Spine was higher by 2.1%, due to strength in international markets in general and the Neurotech product line in particular. The adjusted operating margin grew 90 basis points to 29.2% for the quarter. Stryker expects organic revenue growth of 8% to 10% in 2021, more in-line with the company's long-term growth rate, and adjusted earnings-per-share to be in a range of $8.80 to $9.20. We have initiated our estimates for the current year accordingly.

Growth on a Per-Share Basis

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
EPS	$3.72	$3.39	$2.63	$2.36	$3.78	$4.35	$6.49	$7.28	$8.26	$7.43	***$9.00***	***$15.86***
DPS	$0.75	$0.90	$1.10	$1.26	$1.42	$1.57	$1.70	$1.93	$2.14	$2.36	***$2.52***	***$4.05***
Shares[3]	381	381	378	379	373	375	374	373	380	376	***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

[1] Estimated ex-dividend date
[2] Estimated dividend payment date
[3] Share count in millions

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dividend by 10.6% for the 1/31/2021 payment. We see the payout rising to $4.05 per share by 2026, up from the current $2.30.

Valuation Analysis

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	Now	2026
Avg. P/E	14.8	15.8	25.9	35.2	25.2	25.4	28.7	22.0	25.4	33.0	***25.0***	***23.0***
Avg. Yld.	1.4%	1.7%	1.6%	1.5%	1.5%	1.4%	1.2%	1.2%	1.0%	1.0%	***1.1%***	***1.1%***

Shares of Stryker have increased $22, or 10.8%, since our 11/2/2020 update. Based off of estimates for 2021, shares trade with an earnings multiple of 25. Given the organic growth that the company is producing under normal conditions and the benefit from acquisitions, we are reaffirming our 2026 target P/E of 23. If shares reverted to our new target price-to-earnings ratio by 2026, then valuation would be a 1.7% 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

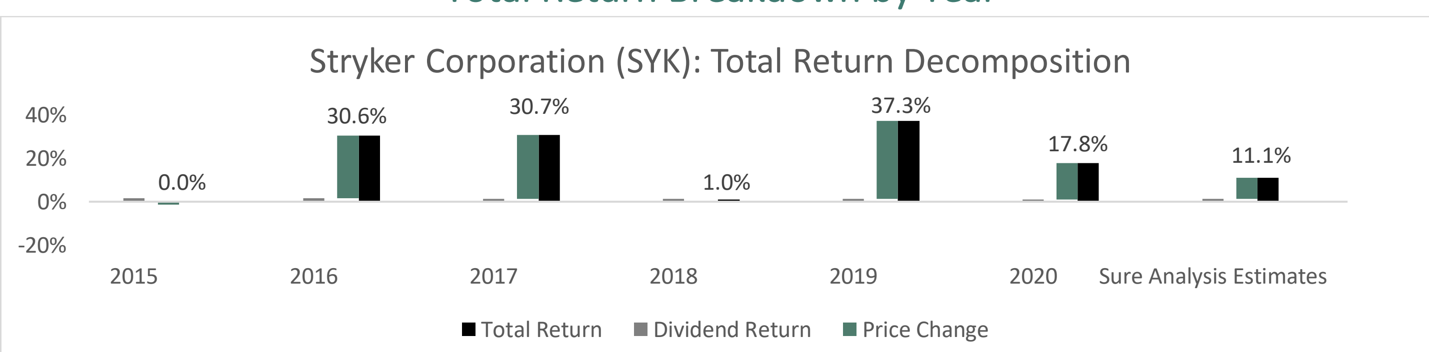
Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
Payout	20%	27%	42%	53%	38%	36%	35%	27%	25%	32%	***28%***	***26%***

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 fourth quarter and full year results, Stryker Corporation is now projected to return 11.1% annually over the next five years, up from our prior estimate of 8.7%. Our projected return stems from a 12% earnings growth rate and starting yield of 1% partially offset by a slight headwind from valuation reversion. Stryker navigated a difficult year as well as can be expected. COVID-19 restrictions greatly reduced elective procedures, but the growth rates following the easing of restrictions demonstrates the company's strength. The newly minted Dividend Aristocrat remains one of our favorite names in the medical device segment. We have increased our five-year price target $74 to $365 due to Stryker's guidance for the current year and now rate shares of the company as a buy due to expected returns.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Revenue	8,307	8,657	9,021	9,675	9,946	11,325	12,444	13,601	14,884	14,351
Gross Profit	5,496	5,876	6,019	6,356	6,602	7,504	8,180	8,938	9,696	9,057
Gross Margin	66.2%	67.9%	66.7%	65.7%	66.4%	66.3%	65.7%	65.7%	65.1%	63.1%
SG&A Exp.	3,150	3,367	3,467	3,547	3,610	4,137	4,552	5,099	5,356	5,361
D&A Exp.	282	277	307	378	397	546	642	723	778	812
Operating Profit	1,762	1,915	1,878	2,007	2,157	2,333	2,470	2,560	2,905	2,240
Operating Margin	21.2%	22.1%	20.8%	20.7%	21.7%	20.6%	19.8%	18.8%	19.5%	15.6%
Net Profit	1,345	1,298	1,006	515	1,439	1,647	1,020	3,553	2,083	1,599
Net Margin	16.2%	15.0%	11.2%	5.3%	14.5%	14.5%	8.2%	26.1%	14.0%	11.1%
Free Cash Flow	1,208	1,447	1,691	1,549	711	1,425	961	2,038	1,542	2,790
Income Tax	341	407	206	645	296	274	1,043	-1,197	479	355

Balance Sheet Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Total Assets	12,146	13,206	15,743	17,279	16,223	20,435	22,197	27,229	30,167	34,330
Cash & Equivalents	905	1,395	1,339	1,795	3,379	3,316	2,542	3,616	4,337	2,943
Accounts Receivable	1,417	1,430	1,518	1,572	1,662	1,967	2,198	2,332	2,893	2,701
Inventories	1,283	1,265	1,422	1,588	1,639	2,030	2,465	2,955	3,282	3,494
Goodwill & Int. Ass.	3,514	3,566	5,833	6,204	5,930	9,864	10,645	12,726	13,296	18,332
Total Liabilities										
Accounts Payable	345	288	314	329	410	437	487	646	675	
Long-Term Debt	1,768	1,762	2,764	3,973	3,998	6,914	7,222	9,859	11,090	13,230
Shareholder's Equity	7,683	8,597	9,047	8,595	8,511	9,550	9,966	11,730	12,807	13,084
D/E Ratio	0.23	0.21	0.31	0.46	0.47	0.72	0.72	0.84	0.87	1.01

Profitability & Per Share Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Return on Assets	11.7%	10.2%	7.0%	3.1%	8.6%	9.0%	4.8%	14.4%	7.3%	5.0%
Return on Equity	18.1%	15.9%	11.4%	5.8%	16.8%	18.2%	10.5%	32.8%	17.0%	12.4%
ROIC	15.2%	13.1%	9.1%	4.2%	11.5%	11.4%	6.1%	18.3%	9.2%	6.4%
Shares Out.	381	381	378	379	373	375	374	373	380	376
Revenue/Share	21.33	22.60	23.61	25.27	26.11	29.92	32.74	35.76	39.18	37.74
FCF/Share	3.10	3.78	4.43	4.05	1.87	3.76	2.53	5.36	4.06	7.34

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

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