

# GlaxoSmithKline

United Kingdom/Pharmaceuticals

**21 April 2016**

UBS Research

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## 1Q16 preview: we estimate Core EPS of 19.4p; next-generation HIV drug news flow is the key focus

- We estimate sales of £5,973m and Basic Core EPS of 19.4p in 1Q16
- Products: we focus on HIV (Triumeq & Tivicay) and respiratory (Advair & Breo)
- Upcoming news flow: next-generation HIV drug news is likely most important
- Valuation: Neutral, PT 1,420p

### We estimate sales of £5,973m and Basic Core EPS of 19.4p in 1Q16

We estimate net sales of £5,973m in 1Q16: 4% above cons. of £5,728m (based on FOA consensus from March 2016). GSK flagged a number of items in 1Q16, including: Japanese biennial price cuts in April (in the 5-7% range) which will negatively impact 1Q16, the continuing 20% Advair US decline into 2016, and European Seretide generics. We have updated our model for these issues, together with updating for FX and the latest script data. We estimate Basic Core EPS of 19.4p: 7% above cons. of 18.1p. Key moving parts include slightly higher finance costs in 2016 with a rise in net debt resulting from spending on the restructuring programs, plus a rise in core effective tax rate to 20-21% in 2016 due to changes in geographical mix.

### Products: we focus on HIV (Triumeq & Tivicay) and respiratory (Advair & Breo)

In terms of key products, we estimate 1) Advair sales of £848m (2% below cons. of £868m), reflecting a continuing US decline, 2) Breo sales of £153m (3% above cons. of £148m), 3) Tivicay sales of £193m (7% above cons. of £181m), 4) Triumeq sales of £319m (8% above cons. of £296m).

### Upcoming news flow: next-generation HIV drug news is likely most important

In our view, next-generation HIV drug news flow likely has the greatest impact on the investment case – we should hopefully see some news this year on: 1) Ph III SWORD data on dolutegravir and rilpivirine; 2) the Salford lung study (a real-life COPD study), 3) ongoing commentary on Advair generics.

### Valuation: Neutral, PT 1,420p

Our PT is based on 16x 2017E Core EPS, a 5% premium to the sector.

12-month rating	<b>Neutral</b>
12-month price target	<b>1,420.00p</b>
Price	<b>1,495.50GBp</b>

### Trading data and key metrics

52-wk range	1,562p-1,238
Market cap.	£71.9bn/US\$104bn
Shares o/s	4,811m (ORD)
Free float	100%
Avg. daily volume ('000)	9,146
Avg. daily value (m)	£129.0
Common s/h equity (12/16E)	£2.75bn
P/BV (12/16E)	26.3x
Net debt / EBITDA (12/16E)	1.4x
RIC	GSK.L
BBG	GSK LN

Sources: UBS, Bloomberg

### EPS (UBS, diluted) (p)

	From	To	% ch	Cons.
12/16E	84.51	88.24	4	86.10
12/17E	87.23	88.64	2	90.09
12/18E	95.18	95.84	1	96.65

Definitions of terms and abbreviations are available in the appendix section of this report, and more extensively on internet at [www.ubs.com/glossary](http://www.ubs.com/glossary)

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# GlaxoSmithKline

## Company Profile: GlaxoSmithKline

GlaxoSmithKline (GSK) is a European large-cap pharmaceutical company. Following the asset swap with Novartis (closed in March 2015), it has emerged as a world leader in consumer/OTC healthcare products (Novartis is a minority shareholder with a 36.8% stake) and vaccines. GSK's pharma business consists of ViiV/HIV (with Pfizer and Shionogi as minority shareholders), respiratory and a few smaller therapeutic areas.

## Statement of Risk

(1) Company-specific risks include continuing execution issues, especially related to capturing merger synergies (Novartis asset swap), and the ongoing respiratory launches, as well as increased competitive pressures on the respiratory business. GSK has committed to pay an 80p dividend out to 2017, which could be difficult to fund, if GSK does not deliver on merger synergies and continues to deliver an underwhelming performance from the respiratory business. (2) Risks generally applicable to the pharmaceutical sector include: development risk – uncertainty regarding the timing, efficacy, and market potential of new products and technologies; commercial risk – threats from new/existing competition and pricing pressure; regulatory risk – timing/status of approvals and changes in labelling or new warnings on existing products and technologies; patent risk – products losing patent protection may face significant market share/price erosion and potential litigation; and currency risk – because of the mismatch between geographical location of cost base and sales. Valuation: Our PT is based on 16x 2017E Core EPS, a 5% premium to the sector.

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Highlights (£m)	12/13	12/14	12/15	12/16E	12/17E	12/18E	12/19E	12/20E
Revenues	26,505	23,006	23,923	25,479	26,053	27,177	28,620	29,790
EBIT (UBS)	8,015	6,594	5,729	6,835	7,067	7,606	8,320	8,905
Net earnings (UBS)	5,421	4,584	3,658	4,323	4,366	4,746	5,284	5,697
EPS (UBS, diluted) (p)	110.21	94.22	74.84	88.24	88.64	95.84	106.11	113.77
DPS (p)	78.00	80.00	80.00	100.00	80.00	80.00	80.00	80.00
Net (debt) / cash	(12,645)	(14,377)	(10,727)	(12,935)	(12,889)	(11,865)	(10,230)	(8,565)
Profitability/valuation	12/13	12/14	12/15	12/16E	12/17E	12/18E	12/19E	12/20E
EBIT margin %	30.2	28.7	23.9	26.8	27.1	28.0	29.1	29.9
ROIC (EBIT) %	36.7	31.3	27.0	32.0	33.3	36.9	42.1	46.6
EV/EBITDA (core) x	10.0	11.3	11.7	10.1	9.9	9.2	8.4	7.8
P/E (UBS, diluted) x	14.5	16.2	18.9	16.9	16.9	15.6	14.1	13.1
Equity FCF (UBS) yield %	6.2	3.7	0.0	4.2	6.1	7.6	8.6	8.7
Net dividend yield %	4.9	5.2	5.6	6.7	5.3	5.3	5.3	5.3

Source: Company accounts, Thomson Reuters, UBS estimates. Metrics marked as (UBS) have had analyst adjustments applied.

Valuations: based on an average share price that year, (E): based on a share price of 1,496p on 20 Apr 2016 20:32 BST

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UBS 12-Month Rating	Rating Category	Coverage <sup>1</sup>	IB Services <sup>2</sup>
Buy	Buy	47%	33%
Neutral	Hold/Neutral	42%	34%
Sell	Sell	11%	23%

1:Percentage of companies under coverage globally within the 12-month rating category.

2:Percentage of companies within the 12-month rating category for which investment banking (IB) services were provided within the past 12 months.

Source: UBS. Rating allocations are as of 31 March 2014.

UBS 12-Month Rating	Definition
Buy	FSR is > 6% above the MRA.
Neutral	FSR is between -6% and 6% of the MRA.
Sell	FSR is > 6% below the MRA.

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#### Global Equity 12-Month Rating Definitions

**Buy:** FSR is > 6% above the MRA. **Neutral:** FSR is between -6% and 6% of the MRA. **Sell:** FSR is > 6% below the MRA.

#### Key Definitions

**Forecast Stock Return (FSR)** is defined as expected percentage price appreciation plus gross dividend yield over the next 12 months.

**Market Return Assumption (MRA)** is defined as the one-year local market interest rate plus 5% (a proxy for, and not a forecast of, the equity risk premium).

**Under Review (UR)** Stocks may be flagged as UR by the analyst, indicating that the stock's price target and/or rating are subject to possible change in the near term, usually in response to an event that may affect the investment case or valuation.

#### Exceptions and Special Cases

**Core Banding Exceptions (CBE):** Exceptions to the standard +/-6% bands may be granted by the Investment Review Committee (IRC). Factors considered by the IRC include the stock's volatility and the credit spread of the respective company's debt. As a result, stocks deemed to be very high or low risk may be subject to higher or lower bands as they relate to the rating. When such exceptions apply, they will be identified the Companies Mentioned or Company Disclosure table in the relevant research piece.

#### Company Disclosures

GlaxoSmithKline	GSK LN	Neutral	1,501p	19 Apr 2016
AstraZeneca	AZN LN	Buy	4,160p	19 Apr 2016
Sanofi	SAN FP	Neutral	€77.71	19 Apr 2016
Novartis	NOVN VX	Neutral	CHF74.15	19 Apr 2016
Roche	ROG VX	Buy	CHF254.40	19 Apr 2016
Novo Nordisk	NOVOB DC	Sell	DKr377.80	19 Apr 2016
Bayer	BAYN GR	Neutral	€109.37	19 Apr 2016
Company Name	Reuters	12-mo rating	Price	Price date

Source: UBS. All prices as of local market close.

Ratings in this table are the most current published ratings prior to this report. They may be more recent than the stock pricing date

#### Disclosures (21 April 2016)

AstraZeneca 1, 2, 3, 4, GlaxoSmithKline 1, 2, Novartis 1, 2, 5, 6, 7, 8, 9, 10, 11, Novo Nordisk 1, 12; Roche 2, 6, 7, 8, 9, 10, Sanofi 1, 2, 1. UBS Securities LLC makes a market in the securities and/or ADRs of this company.

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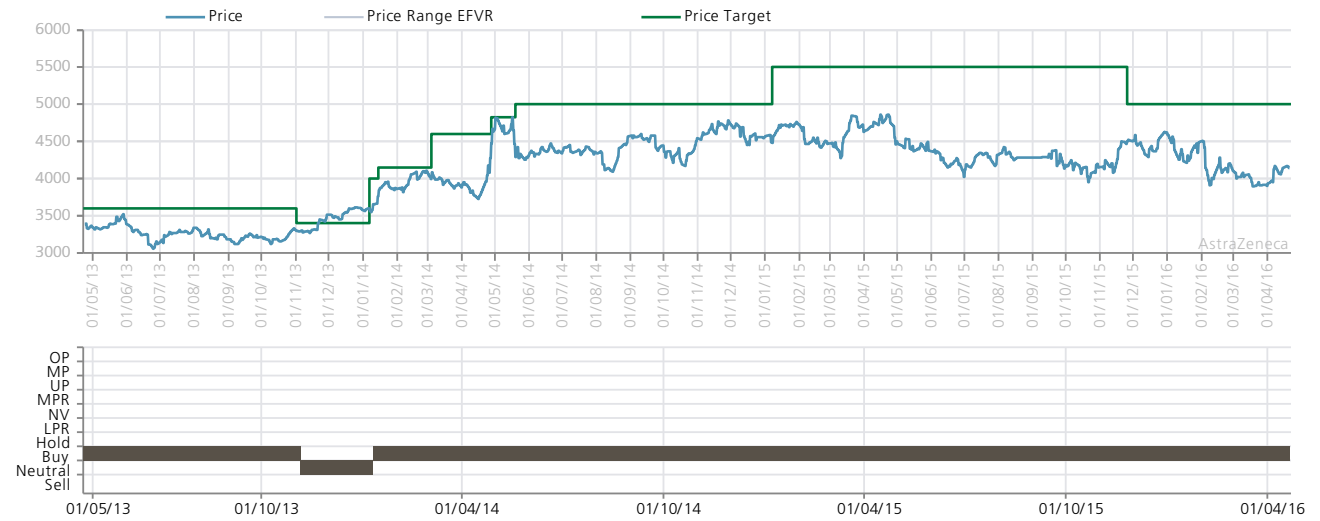
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# GlaxoSmithKline

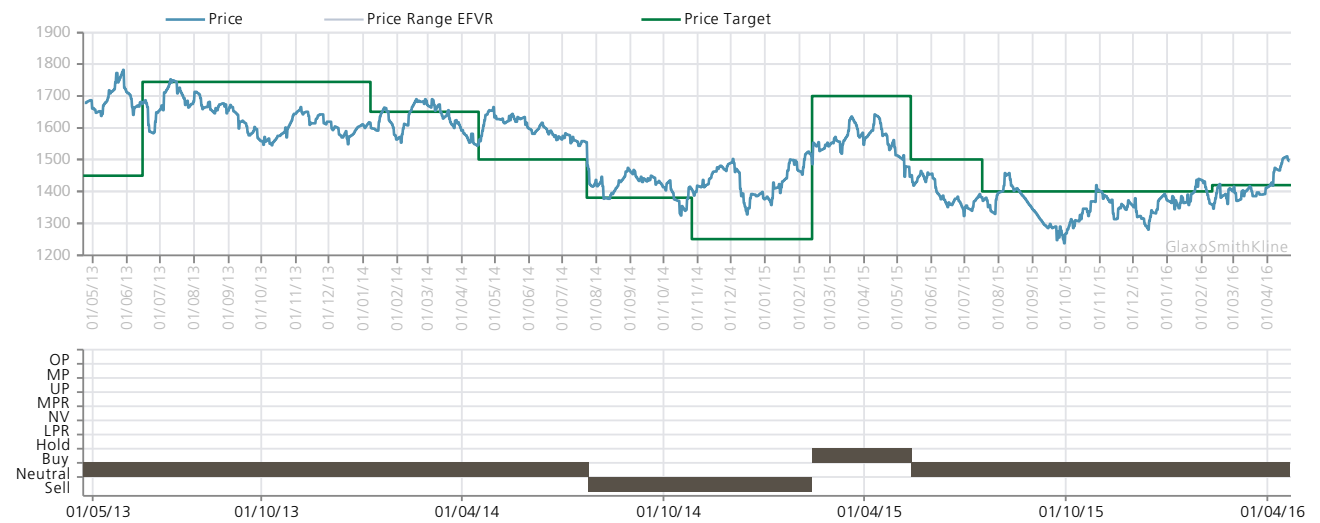
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11. UBS AG is acting as agent in regard to Novartis AG's announced share buyback programme.
12. A U.S.-based global equity strategist, a member of his team, or one of their household members has a long common stock position in Novo Nordisk A/S.

## Global rating history -- AstraZeneca, AZN LN



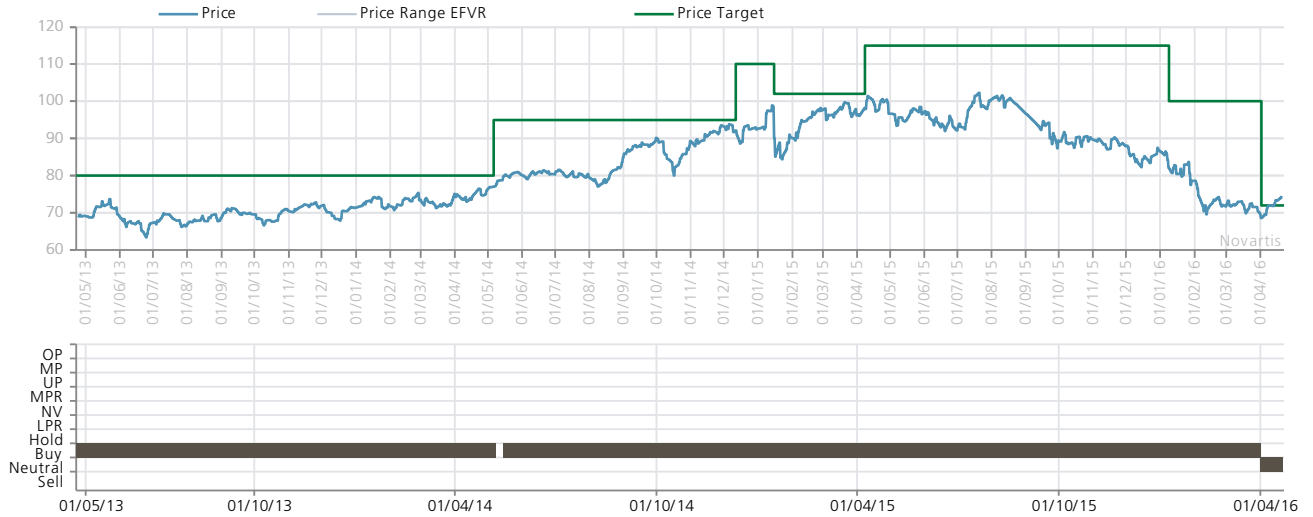
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## Global rating history -- GlaxoSmithKline, GSK LN



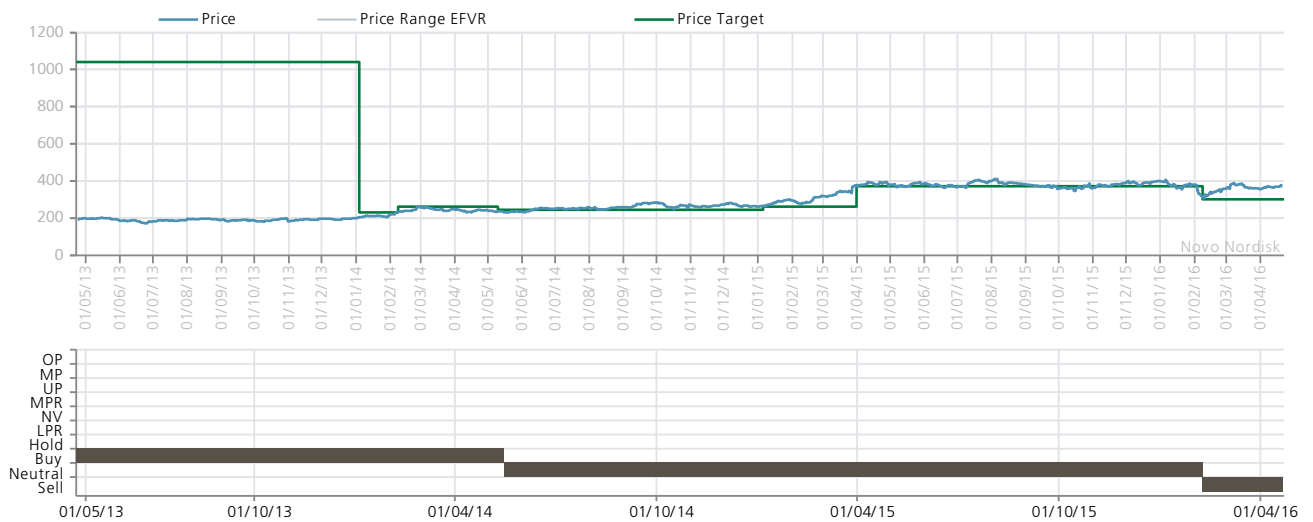
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## Global rating history -- Novartis, NOVN VX



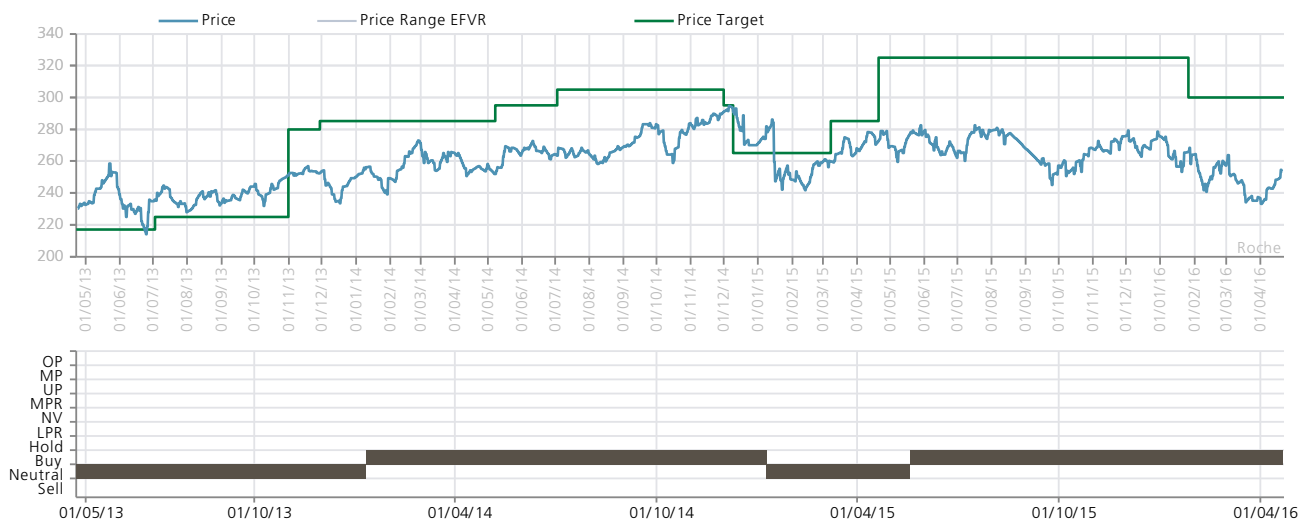
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## Global rating history -- Novo Nordisk, NOVOB DC



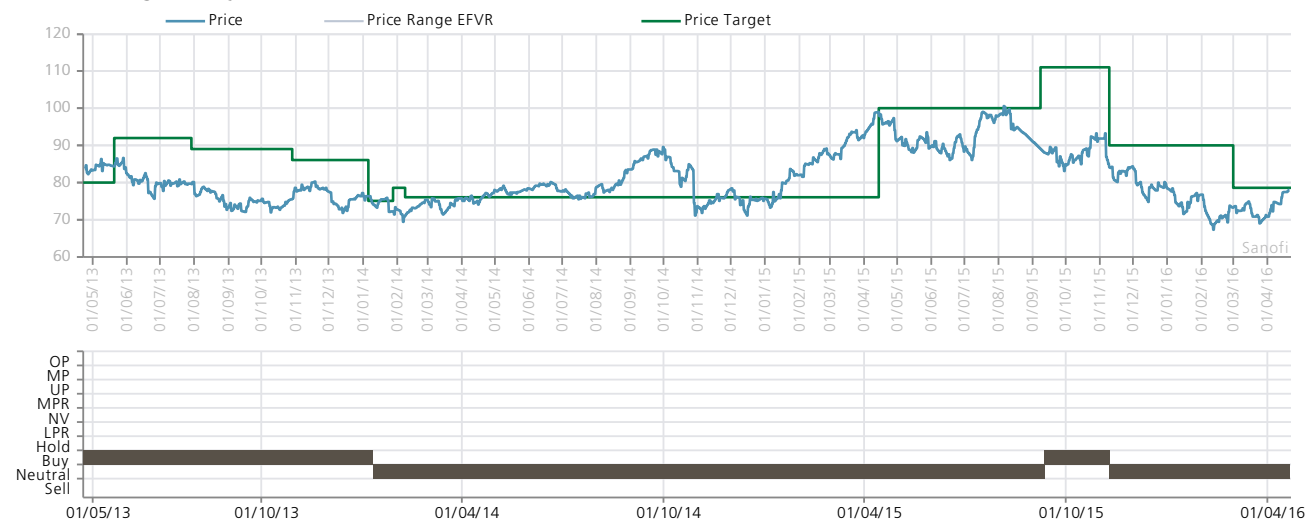
Source: UBS CIO as of 21 April 2016

## Global rating history -- Roche, ROG VX



Source: UBS CIO as of 21 April 2016

## Global rating history -- Sanofi, SAN FP



Source: UBS CIO as of 21 April 2016

### Terms and Abbreviations

Term / Abbreviation	Description / Definition	Term / Abbreviation	Description / Definition
1H, 2H, etc. or 1H11, 2H11, etc.	First half, second half, etc. or first half 2011, second half 2011, etc.	1Q, 2Q, etc. or 1Q11, 2Q11, etc.	First quarter, second quarter, etc. or first quarter 2011, second quarter 2011, etc.
2011E, 2012E, etc.	2011 estimate, 2012 estimate, etc.	A	actual i.e. 2010A
ADR	American depositary receipt	ARPU	Average Revenue Per User
AUM	Assets under management = total value of own and third-party assets managed	Avg.	average
bn	Billion	bp or bps	Basis point or basis points (100 bps = 1 percentage point)
BVPS	Book value per share = shareholders' equity divided by the number of shares	CAGR	Compound annual growth rate
Cant Inc/Capita	Cantonal income per capita (Switzerland only)	Capex	Capital expenditures
CF	Cash flow	CFO	1) Cash flow from operations, 2) Chief financial officer
COGS	Cost of goods sold	COM	Common shares
Cons.	Consensus	Core Tier 1 Ratio	Tier 1 capital minus tier 1 hybrid securities
Cost/Inc Ratio (%)	Costs as a percentage of income	CPI	Consumer price index
CR	Combined ratio = ratio of claims and expenses as a percentage of premiums (for insurance companies)	CY	Calendar year
DCF	Discounted cash flow	DDM	Dividend discount model
Dividend Yield (%)	Dividend per share divided by price per share	DPS	Dividend per share
E	expected i.e. 2011E	EBIT	Earnings before interest and taxes
EBIT Margin (%)	EBIT divided by revenues	EBITDA	Earnings before interest, taxes, depreciation and amortization
EBITDA Margin (%)	EBITDA divided by revenues	EBITDA/Net Interest	EBITDA divided by net interest expense
EBITDAR	Earnings before interest, taxes, depreciation, amortization and rental expense	EFVR	Estimated fair value range
EmV	Embedded value = net asset value + present value of forecasted future profits (for life insurers)	EPS	Earnings per share
Equity Ratio (%)	Shareholders' equity divided by total assets	EV	Enterprise value = market value of equity, preferred equity, outstanding net debt and minorities
FCF	Free cash flow = cash a company generates above outlays required to maintain/expand its asset base	FCF Yield (%)	Free cash flow divided by market capitalization
FFO	Funds from operations	FY	Fiscal year / financial year
GDP	Gross domestic product	Gross Margin (%)	Gross profit divided by revenues
H	half year	h/h	Half-year over half-year; half on half
hist av.	Historical average	Interbank Ratio	Interbank deposits due from banks divided by interbank deposits due to banks
Interest Coverage	Ratio that expresses the number of times interest expenses are covered by earnings	Interest exp	Interest expense
ISIN	International securities identification number	K	One thousand
LLP/Net Int Inc (%)	Loan loss provisions divided by net interest income	LLR/Gross Loans (%)	Loan loss reserves divided by gross loans

# GlaxoSmithKline

Term / Abbreviation	Description / Definition	Term / Abbreviation	Description / Definition
LPR	Least Preferred: The stock is expected to both underperform the relevant benchmark and depreciate in absolute terms.	Market cap	Number of all shares of a company (at the end of the quarter) times closing price
m/m	Month-over-month; month on month	mn or m	Million
M and A	Merger and Acquisition	MP	Marketperform: The stocks expected performance is in line with the sector benchmark
MPR	Most Preferred: The stock is expected to both outperform the relevant benchmark and appreciate in absolute terms.	n.a.	Not available or not applicable
NAV	Net asset value	Net Debt	Short- and long-term interest-bearing debt minus cash and cash equivalents
Net DPS	Net dividends per share	NIM or Net Int Margin (%)	Net interest income divided by average interest-bearing assets
Net Margin (%)	Net income dividend by revenues	NV	Neutral View: The stock is expected to neither outperform nor underperform the relevant benchmark nor significantly appreciate or depreciate in absolute terms.
n.m. or NM	Not meaningful	NPL	Non-performing loans
OP	Outperform: The stocks is expected to outperform the sector benchmark	Op Margin (%)	Operating income divided by revenues
p.a.	Per annum (per year)	P/BV	Price to book value
P/E or PE	Price to earnings / Price Earnings Ratio	P/E Relative	P/E relative to the market
P/EmV	Price to embedded value	PEG Ratio	P/E ratio divided by earnings growth
PPI	Producer price index	Prim Bal/Cur Rev (%)	Primary balance divided by current revenue (total revenue minus capital revenue)
Profit Margin (%)	Net income divided by revenues	q/q or QQQ	Quarter-over-quarter; quarter on quarter
R and D	Research and development	ROA (%)	Return on assets
ROAE (%)	Return on average equity	ROCE (%)	Return on capital employed = EBIT divided by difference between total assets & current liabilities
ROE (%)	Return on equity	ROIC (%) or ROI	Return on invested capital
Shares o/s	Shares outstanding	Solvency Ratio (%)	Ratio of shareholders' equity to net premiums written (for insurance companies)
sotp or SOTP	Sum of the parts	Tax Burden Index	Swiss tax index; 100 = average tax burden of all cantons
tgt	Target	Tier 1 Ratio (%)	Tier 1 capital divided by risk-weighted assets; describes a bank's capital adequacy
tn	Trillion	UP	Underperform: The stock is expected to underperform the sector benchmark
Valor	Swiss company identifier	WACC	Weighted average cost of capital
CIO	UBS WM Chief Investment Office	x	multiple / multiplier
y/y or YOY	Year-over-year; year on year	yr	Year
YTD	Year-to-date		

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