

Lilly (Eli) & Co.

United States of America/Pharmaceuticals,
Biotechnology & Life Sciences

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UBS Research

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Solid 1Q17; Clarity on Baricitinib Is Key

- What we learned on the conference call
- Additional takeaways
- Thoughts on the stock: Investors expected more
- Valuation: Maintaining our Neutral rating and price target of \$85

(1) A key focus was on the next steps for baricitinib, given the recent CRL. There was little new info, and it still looks like whether another clinical trial will be conducted depends on the outcome of mgt's meeting with the FDA. Mgt believes it has sufficient data to try to address the FDA's concerns, and the FDA hasn't seen some data from the extension study. EU sales of ~\$2M represented initial stocking in Germany. (2) Despite the baricitinib set-back, mgt remains confident in its mid-term guidance of at least a 5% revs CAGR as the guidance doesn't rest on any one specific asset. (3) On abemaciclib, Lilly moved the filing of MONARCH-2 from 3Q to 2Q17. Mgt maintains that the totality of the clinical data, along with the profile to cross the blood brain barrier, continuous dosing, and a manageable/transient GI profile could help to differentiate abemaciclib from Pfizer's Ibrance and Novartis's Kisqali.

Additional takeaways

(4) For Jardiance, there was no change in rebates/discounts estimates in 1Q17, and the Q/Q growth was muted by the \$15M rebates/co-pay benefits in 4Q16. With the inclusion of the CV outcomes data in the label, Lilly has started to realize better pricing, with changes in co-pay cards, a higher price in Germany, and a minor price benefit in Japan. (5) On Cyramza, the lower Y/Y GtN was largely driven by a 1x GtN benefit in 1Q16. US sales remained challenged by IOs, but Japan remained strong driven by gastric cancer and recent uptake of lung and colorectal cancer. (6) Without the ~\$41M sales from BI Vetmedica, Animal Health declined -3% (vs 2% growth with Vetmedica). Mgt still expects 2017 growth to be back-half loaded.

Thoughts on the stock: Investors expected more

A key part of the positive thesis on Lilly this year is the new diabetes franchise/Taltz driving both top-line and earnings upside. And in 1Q Taltz and Trulicity ramped nicely, but investors were clearly disappointed with Jardiance (& probably need to lower sales forecasts) and the lack of new news on baricitinib plans. Hence, the -3% stock move.

Valuation: Maintaining our Neutral rating and price target of \$85

The 1 cent EPS beat (vs UBSe) in 1Q17 increases our 2017 EPS to \$4.16. Our 2018 EPS of \$4.45 remains unchanged and applying our prior ~19x multiple yields our same PT.

12-month rating	Neutral
12-month price target	\$85.00
Price	\$81.27

Contributing authors: Uy Ear

Trading data and key metrics

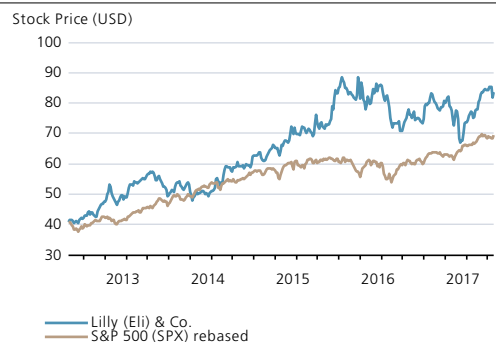
52-wk range	US\$86.25-65.97
Market cap.	US\$85.8bn
Shares o/s	1,056m (COM)
Free float	100%
Avg. daily volume ('000)	1,070
Avg. daily value (m)	US\$87.5
Common s/h equity (12/17E)	US\$14.3bn
P/BV (12/17E)	6.0x
Net debt / EBITDA (12/17E)	1.3x
RIC	LLY.N
BBG	LLY US

Sources: UBS, Bloomberg

EPS (UBS, diluted) (US\$)

	12/17E			Cons.
	From	To	% ch	
Q1	0.97	0.98	1	0.96
Q2E	1.03	1.03	NM	1.04
Q3E	1.05	1.05	NM	1.05
Q4E	1.10	1.10	NM	1.06
12/17E	4.15	4.16	0	4.11
12/18E	4.45	4.45	NM	4.38
12/19E	4.95	4.95	NM	4.96

Performance



Sources: Bloomberg, UBS

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

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Lilly (Eli) & Co.

Company Profile: Lilly (Eli) & Co.

Eli Lilly & Co., with its subsidiaries, develops, makes and markets pharmaceutical and animal health products, sold in approximately 155 countries around the world. Key franchises include central nervous system and endocrine disorders, oncology and women's health.

Statement of Risk

Our price target is based on a P/E multiple. Lilly faces several risks impacting the overall pharmaceutical industry including (1) pricing pressure and branded drug restrictions resulting from healthcare reform or managed care initiatives; (2) generic competition as well as competition from other international branded players; (3) clinical and regulatory risk with regard to new product development; (4) inability to develop or acquire suitable pipeline assets; and (5) political instability risk associated with multi-national operations.

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Highlights (US\$m)	12/14	12/15	12/16	12/17E	12/18E	12/19E	12/20E	12/21E
Revenues	19,615	19,958	21,219	22,184	21,929	22,412	23,292	24,457
EBIT (UBS)	3,978	4,359	4,552	5,547	5,900	6,339	6,671	7,119
Net earnings (UBS)	3,336	3,644	3,733	4,392	4,697	5,069	5,311	5,637
EPS (UBS, diluted) (US\$)	3.11	3.42	3.52	4.16	4.45	4.95	5.35	5.84
DPS (US\$)	1.96	2.00	2.04	2.12	2.16	2.21	2.25	2.25
Net (debt) / cash	(7,596.50)	(6,299.50)	(9,117.60)	(8,305.95)	(8,014.63)	(9,094.69)	(10,479.03)	(11,697.74)
Profitability/valuation	12/14	12/15	12/16	12/17E	12/18E	12/19E	12/20E	12/21E
EBIT margin %	20.3	21.8	21.5	25.0	26.9	28.3	28.6	29.1
ROIC (EBIT) %	28.4	28.7	25.5	30.4	31.5	32.1	33.0	34.1
EV/EBITDA (core) x	14.1	16.8	15.1	13.6	12.8	12.0	11.4	10.7
P/E (UBS, diluted) x	19.8	23.0	21.7	19.5	18.3	16.4	15.2	13.9
Equity FCF (UBS) yield %	5.2	2.0	4.8	3.6	5.5	5.7	5.8	6.0
Net dividend yield %	3.2	2.5	2.7	2.6	2.7	2.7	2.8	2.8

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 US\$81.27 on 25 Apr 2017 15:43 EDT

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Lilly (Eli) & Co.

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UBS 12-Month Rating	Rating Category	Coverage ¹	IB Services ²
Buy	Buy	45%	29%
Neutral	Hold/Neutral	39%	27%
Sell	Sell	15%	16%

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 December 2016.

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.

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Company Disclosures

Company Name	Reuters	12-mo rating	Price	Price date
Lilly	LLY US	Neutral	US\$83.42	24 Apr 2017

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

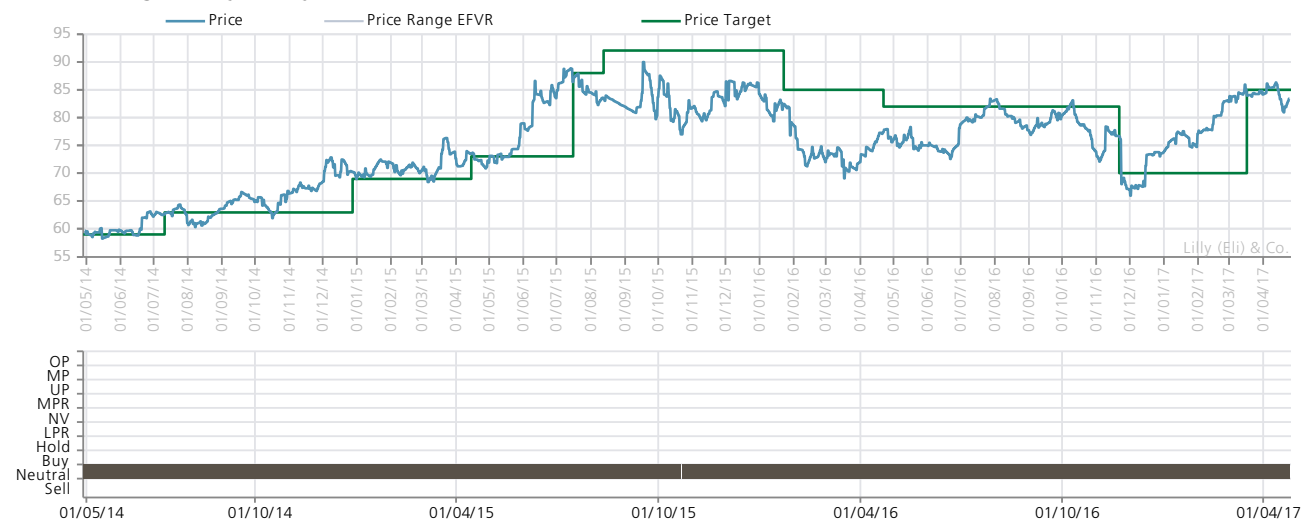
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Lilly (Eli) & Co.

Global rating history -- Lilly (Eli) & Co., LLY US



Source: UBS CIO as of 25 April 2017

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

Lilly (Eli) & Co.

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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