UBS

Sanofi

France/Pharmaceuticals
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UBS Research
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12-month rating	**Neutral**
12-month price target	**€78.00**
Price	**€74.39**

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Thoughts on a strategic transaction with Actelion

- Press reports that Sanofi is in deal discussions with Actelion after JNJ pulls out
- What if the "strategic transaction" was CHF240 cash + CHF45 CVR per share?
- The financial metrics may be clear, but the "strategic" part isn't
- Valuation:

The WSJ (13 Dec.) reported Sanofi as interested in a deal that "could value Actelion at as much as $30bn" (~CHF285 per share). Actelion (14 Dec.) confirmed JNJ's withdrawal and said there were discussions on a "strategic transaction" with another party.

What if the "strategic transaction" was CHF240 cash + CHF45 CVR per share?
Sanofi could quickly de-lever from EV/EBITDA of 3.1x in year 1 to 1.7x in year 3, on our estimates. Such a deal would be EPS accretive; +c.5% in year 1, +c.9% in year 4. Were Sanofi worried about Praluent and/or Dupixent, the deal might help hit post-2018 EPS growth targets. However, much the same could be achieved, without paying an acquisition premium, if Sanofi simply bought its own stock. What is there here above financial metrics?

The financial metrics may be clear, but the "strategic" part isn't
JNJ withdrew from deal discussions with Actelion (JNJ announcement, 14 Dec.), unable to reach an agreement that would "create value for [its] shareholders". It is not clear to us why a deal might be worth more to Sanofi. Sanofi would probably not achieve much higher synergies given limited portfolio overlap. Sanofi's ability to cut Actelion R&D would be constrained versus JNJ by the CVR. Furthermore, Sanofi's big challenge is exposure to drug classes where payer power is growing and Actelion's pipeline does not solve the problem, in our view. Sanofi and Actelion overlap in multiple sclerosis (MS) and – arguably - in sleep. But US payers appear to have the MS category in their sights, with profits threatened by the entry of Ocrevus (Roche), the genericization of Gilenya (Novartis), and crowding in the S1P-1 class (Actelion, Celgene, Biogen). Expensive new sleep drugs (e.g., Actelion's almorexant) will likely struggle against cheap generics, as does Merck's Belsomra. Were it done, the deal could raise questions about Sanofi's strategy, in our view.

Valuation:
We focus on DCF in setting price targets (Sanofi WACC 4.9%, terminal growth 2%), but sense-check vs. PE multiples for "core" and IFRS earnings. Our price target for Sanofi is €78 which is 20.1x 2017e IFRS EPS and 13.7x 2017e "business" EPS. Sanofi looks cheap on an adjusted earnings basis. However, it has relatively low growth ('17e-'25e EBIT CAGR near 2%), the lowest ROIC of the group (<5% including capitalized R&D), and looks close to fair value on DCF and IFRS earnings multiples.

Trading data and key metrics

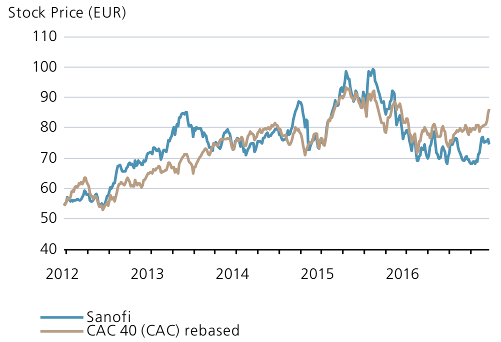
52-wk range	€80.10-67.27
Market cap.	€98.7bn/US$103bn
Shares o/s	1,327m (ORD)
Free float	89%
Avg. daily volume ('000)	3,039
Avg. daily value (m)	€221.0
Common s/h equity (12/16E)	€58.7bn
P/BV (12/16E)	1.6x
Net debt / EBITDA (12/16E)	0.5x
RIC	SASY.PA
BBG	SAN FP

Sources: UBS, Bloomberg

EPS (UBS, diluted) (€)

	UBS	Cons.
12/16E	5.89	5.60
12/17E	5.70	5.50
12/18E	5.89	5.87

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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Sanofi

Company Profile: Sanofi
Sanofi has capabilities in branded and generics, vaccines and consumer health, and has agreed to swap its Animal Health business for Boehringer Ingelheim's consumer business (expected closure end 2016). Pharma (including consumer) contributed 80% of 2015 group sales, and vaccines 13%. Key franchises in pharma are diabetes (Lantus, Toujeo), cardiovascular and Genzyme (focused on rare diseases, multiple sclerosis and oncology). Sanofi's collaboration with Regeneron has yielded key marketed drugs (Praluent) and late-stage assets including dupilumab (atopic dermatitis) and sarilumab (rheumatoid arthritis).

Statement of Risk
Risks for the pharmaceutical industry include low R&D productivity, generic competition, and legislative pressure on pricing and litigation risk. Company-specific risks include lack of visibility on US pricing dynamics for basal insulin, uptake of dupilumab in atopic dermatitis and potential pipeline setbacks.Valuation: We consider several methods when we set our price targets (Sanofi WACC 4.9%, terminal growth 2%). We are most heavily influenced by DCF analysis. Our explicit forecasts run to 2025. From 2025, we assume 2% annual growth in (operating income x (1 – tax rate)) and a straight-line ROIC fade. ROIC fades to WACC over a 20 year period. This approach means that our DCF valuations are particularly sensitive to 2 parameters; WACC and our estimate of ROIC around 2025. Given these sensitivities, we sense-check our DCF valuation against PE multiples calculated on the basis of both adjusted ("core" or "non-GAAP" numbers) and IFRS or GAAP numbers, calibrated against the rest of the sector and considering the EPS growth profile.

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Highlights (€m)	12/13	12/14	12/15	12/16E	12/17E	12/18E	12/19E	12/20E
Revenues	31,291	31,999	34,861	34,843	37,258	38,744	41,054	42,913
EBIT (UBS)	8,893	8,937	9,270	9,692	10,396	10,710	11,320	11,162
Net earnings (UBS)	6,686	6,847	7,371	7,585	7,345	7,584	8,015	7,886
EPS (UBS, diluted) (€)	4.99	5.14	5.58	5.89	5.70	5.89	6.22	6.12
DPS (€)	2.80	2.85	2.93	2.94	3.67	3.46	3.57	3.91
Net (debt) / cash	(6,333)	(7,473)	(7,406)	(6,945)	(6,926)	(7,364)	(7,731)	(8,295)

Profitability/valuation	12/13	12/14	12/15	12/16E	12/17E	12/18E	12/19E	12/20E
EBIT margin %	28.4	27.9	26.6	27.8	27.9	27.6	27.6	26.0
ROIC (EBIT) %	13.9	14.4	15.6	16.9	18.0	18.3	18.9	18.3
EV/EBITDA (core) x	8.8	8.9	9.7	8.2	7.4	7.3	7.0	7.1
P/E (UBS, diluted) x	15.4	15.1	15.8	12.6	13.0	12.6	12.0	12.2
Equity FCF (UBS) yield %	5.5	6.1	5.3	5.2	4.5	4.2	4.7	4.4
Net dividend yield %	3.6	3.7	3.3	4.0	4.9	4.7	4.8	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 €74.39 on 16 Dec 2016 21:37 GMT

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UBS 12-Month Rating	Rating Category	Coverage [1]	IB Services [2]
Buy	**Buy**	45%	28%
Neutral	**Hold/Neutral**	39%	25%
Sell	**Sell**	15%	17%

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 2013.

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

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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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