

3 February 2015 | 7 pages

Biotechnology
North America | United States

Gilead Sciences Inc (GILD)

Results: Strong Q4 – New Dividend + Stock Buyback Are Big Positives But Pricing Is Softer Than Expected – Volume Going Up

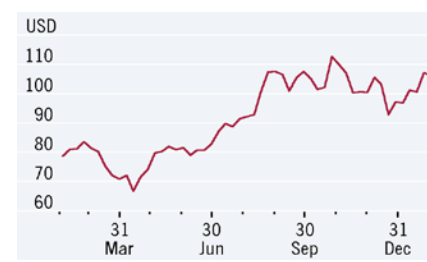
- Citi's Take** — Gilead posted a strong Q4 driven by 10% beat on revs and 11% on EPS. Both Harvoni and Sovaldi beat albeit ex-US hepC sales were weak as reimbursement was not fully secured until Q1. HepC sales should accelerate meaningfully ex-US in 2015. The surprise is that gross/net discounts are expected to be 46% vs our 25% driven by aggressive exclusivity based contracts. Gilead is winning the battle as only 20% of formularies are exclusive to ABBV. As volume will increase meaningfully and hence the 2015 guidance is only slightly lower than ests, we expect the stock to trade down c.5% but we remain Buyers.
- What the Pricing?** — Clearly this is a precedent setting situation as payers are demanding exclusivity contracts in both the public and private markets. The bad news is that this translates into very fast and deep discounting to gain access. But the good news is that Gilead is winning and this will carry over through YE '16 by which point Merck will launch their regimen and contracting is done for 2017. In the meantime, Gilead will capture share, docs will gain experience, and Gilead has the best hepC pipeline. We like the stock as it offers a low P/E multiple supported by stock buybacks, dividend, under-appreciated pipeline and M&A optionality.
- Capital Deployment** — Gilead announced a dividend unexpectedly for the first time of \$0.43/quarter or ~1.6% div yield (\$2.75B/yr) and a \$15B stock buyback on top of the remaining \$3B under the current plan. This will last for 5 years but typically the buybacks are accelerated. With \$14B-\$15B in free cash flow in 2015, this will allow for plenty of room for acquisitions to boost the pipeline and stimulate growth.
- Implications** — The worse news is now behind us on pricing and volume should now accelerate globally. The patient pull-through will be faster than was initially expected and will remain sustainable ex-US due to strict budgets. The dividend and stock buybacks are encouraging and leave room for further M&A as Gilead is gearing the company for acquisitions starting in 2015.

EPS	Q1	Q2	Q3	Q4	FY	FC Cons
2013A	0.48A	0.50A	0.52A	0.55A	2.05A	2.04A
2014E	1.48A	2.36A	1.84A	2.42E	8.11E	7.92E
Previous	1.48A	2.36A	1.84A	2.42E	8.11E	na
2015E	na	na	na	na	10.39E	9.79E
Previous	na	na	na	na	10.39E	na
2016E	na	na	na	na	12.27E	10.97E
Previous	na	na	na	na	12.27E	na

Source: Company Reports and dataCentral, Citi Research. FC Cons: First Call Consensus.

Buy	1
Price (03 Feb 15)	US\$104.58
Target price	US\$125.00
Expected share price return	19.5%
Expected dividend yield	0.0%
Expected total return	19.5%
Market Cap	US\$157,776M

Price Performance
(RIC: GILD.O, BB: GILD US)



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See Appendix A-1 for Analyst Certification, Important Disclosures and non-US research analyst disclosures.

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Gilead Sciences Inc

Valuation

We value Gilead on a comparative P/E vs. the large-cap biotech comp group. Our \$125 target price is based on 12x 2015E non-GAAP EPS estimate of \$10.39. This multiple is a substantial discount to both the S&P500 and large-cap biotech group and reflects the long-term uncertainty about the longevity of the hepC revenue stream.

Our DCF analysis suggests a value of \$81-\$119. In our DCF, we utilize a 10% discount rate to get to \$81, which is an overly conservative scenario. If we use an 8% discount rate that we typically apply to large-cap biotech stocks, we derive a \$104 DCF value. If we use the current cost of capital using a discount rate of 6.5% based on a risk-free rate of 2.59%, an equity risk premium of 5.45%, and a 52-week beta of 1.22, we derive a \$119 DCF value.

Risks

Risks we see to the stock achieving our target price include the following:

While Gilead has the premier HIV franchise today, future growth depends on the continued ability of Stribild, Complera, Truvada and Atripla to continue to capture share in the HIV market. TAF (2nd generation Viread) has completed ph 3 studies and has been filed for global regulatory approvals. Hence it is facing the typical regulatory risks albeit we believe that it will be approved.

Gilead is vulnerable to pricing pressure from US payors and European governments which could result in larger-than-expected rebates for its HIV/HCV products. Gilead must also successfully navigate its US HIV franchise through the opportunities and challenges that it faces stemming from the healthcare reform act.

Gilead is also facing some pricing/reimbursement challenges in the US relating to Sovaldi/Harvoni's price and sizable demand that will test the limits of funding for private payers, Medicaid, the VA system and the correction department. Hence, pricing will likely come under pressure especially given growing competition in hepC.

Finally, the hepC market will likely become very competitive given promising regimens from Merck, AbbVie, Bristol, JNJ, ACHN and others in development.

Appendix A-1

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Gilead Sciences Inc (GILD)

Ratings and Target Price History Fundamental Research

Analyst: Yaron Werber, MD



	Date	Rating	Target Price	Closing Price
1	8-Oct-11	Stock rating system changed		
2	2-Feb-12	1	*28.50	24.66
3	26-Apr-12	1	*32.00	26.36
4	26-Jul-12	1	*32.50	25.84
5	15-Oct-12	1	*44.50	33.66

* Indicates change

	Date	Rating	Target Price	Closing Price
6	28-Jan-13	1	*46.00	39.44
7	17-Mar-13	1	*60.00	45.17
8	2-May-13	1	*75.00	52.18
9	29-Oct-13	1	*85.00	69.50
10	19-Nov-13	1	*87.00	69.66

	Date	Rating	Target Price	Closing Price
11	6-Jan-14	1	*96.00	73.24
12	23-Jul-14	1	*111.00	90.34
13	19-Sep-14	1	*139.00	105.96
14	22-Dec-14	1	*125.00	92.90

Rating/target price changes above reflect Eastern Standard Time

Gilead Sciences Inc (GILD)

Ratings and Target Price History Best Ideas Research Relative Call (3 Month)

Analyst: Yaron Werber, MD



	Date	Rating	Target Price	Closing Price
1	10-Apr-12	*REM MP		

* Indicates change

	Date	Rating	Target Price	Closing Price
2	25-Oct-12	*ADD MP	-	33.69

	Date	Rating	Target Price	Closing Price
3	6-Feb-14	*REM MP		

Rating/target price changes above reflect Eastern Standard Time

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Data current as of 31 Dec 2014

Citi Research Global Fundamental Coverage

% of companies in each rating category that are investment banking clients

12 Month Rating			Relative Rating		
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49%	40%	12%	0%	100%	0%
65%	62%	54%	0%	63%	0%

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