

## Americas: Healthcare: Pharmaceuticals

Equity Research

### HepC price wars worsen, tail comes more quickly; ABBV PT to \$73

#### HepC pricing discounts greater than expected; but volumes higher

On GILD's 4Q earnings call, management called out a gross to net pricing discount of 46% in the US in 2015 for their hepC franchise vs. a gross to net discount of 22% at the end of 2014. This implies pricing of ~\$50K per cure for g1 patients vs. our expectations of ~\$70K. We had expected hepC pricing to decline, but the speed of the discounts is far greater than we had expected. On the positive side, GILD stated that they believe >250K patients could be treated per year in the US (prior expectations for 200K), but that means the peak likely comes more quickly (potentially 2016 versus 2017).

#### More to ABBV than hepC; updating our estimates and price target

We update our global 2016 ABBV hepC estimates to \$2.3 bn (from \$2.6 bn) including \$1.8 bn for the US market. We maintain our \$1.8 bn world wide forecast for 2015, which is below guidance. Our 2016 estimate assumes less than 20% market share of g1 patients in the US based on our assumption of \$50K pricing and 250K patients treated per year (around 75% of which are g1 patients). We also update our 12-month price target to \$73 (prior \$75). ABBV claims that they weren't surprised by GILD's comments and that their guidance for Viekira assumes "appropriate" gross to net discounts. However, with greater-than-expected price discounts we are now more conservative with our hepC estimates.

**HepC now out of ABBV's share price:** We calculate ABBV's \$2.3 bn in HepC sales in 2016 (peak) is worth about \$0.85 in EPS (assuming 75% operating margin). Using a GILD multiple (~10x 2015 EPS) that implies around \$8/share. ABBV shares have already declined \$8 since its peak in early Dec (mostly all based on hepC concerns in our view).

**Reiterate Buy:** HepC is a small piece to the ABBV story. Even at peak hepC represents only ~10% of ABBV sales. ABBV's multiple reflects basically no growth (12x 2016 vs 16x for pharma) despite 14% EPS CAGR from 2014-2018 and meaningful pipeline opportunities (eg. ABT-199, Elagolix, etc).

#### Risk to our MRK estimates; less room for newer competitors

We have MRK sales peaking at \$3-4 bn (unrisk adjusted) which looks to be at risk based on lower pricing for hepC drugs. We believe MRK's HepC plan hinges on a long tail and greater opportunity for late entrance.

#### RELATED RESEARCH

Americas: Healthcare: The ongoing evolution of the unique market that is hepC; October 7 2014

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**HepC class likely unique with limited risk for price war contagion:** As we called out in our global hepC note Oct 2014, we view the hepC market as an exception that is likely to be contained due to a fixed patient pool, acute curative treatments and substitutable drugs.

### Updating our ABBV estimates and 12-month price target

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#### Exhibit 1: Our current and prior estimates for ABBV

hepC estimates in \$ millions

ABBV estimates	2015	2016	2017	2018
Current hepC estimates	1,800	2,300	2,300	2,300
Prior hepC estimates	1,800	2,600	2,600	2,600
Current EPS estimates	4.21	4.89	5.42	5.63
Prior EPS estimates	4.21	5.01	5.55	5.70

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Source: Goldman Sachs Global Investment Research

We update our ABBV 12-month price target to \$73 (prior \$75) based on 17x our 2015E EPS (lower multiple on lower long-term hepC sales), weighted at 85%, and an unchanged M&A value of \$78, weighted at 15%.

Risk include Humira, product launches (hepC), pipeline and business development.

**Exhibit 2: ABBV summary revenue and income statement**

\$ mns, except per share value

5 Year Sales and Earnings	2012	2013	2014	2015E	2016E	2017E	2018E	2019E	2020E
Humira	9,266	10,659	12,543	13,778	15,034	15,851	15,681	15,020	14,425
<b>Lipid Franchise</b>	<b>2,113</b>	<b>1,039</b>	<b>297</b>	<b>128</b>	<b>104</b>	<b>87</b>	<b>73</b>	<b>61</b>	<b>51</b>
Tricor & Trilipix franchise - US	1,099	303	115	41	35	32	29	26	23
Niaspan	911	650	112	44	35	28	23	18	14
Simcor (Niaspan+simvastatin)	103	86	70	42	34	27	22	17	14
<b>Virology Franchise</b>	<b>1,402</b>	<b>1,432</b>	<b>1,390</b>	<b>2,642</b>	<b>2,969</b>	<b>2,799</b>	<b>2,710</b>	<b>2,249</b>	<b>2,197</b>
Norvir (ritonavir PI for HIV)	389	470	472	157	90	73	60	50	42
Kaletra (lopinavir/ritonavir PI for HIV)	1,013	962	870	685	579	425	350	299	255
Viekira Pak			48	1,800	2,300	2,300	2,300	1,900	1,900
<b>Metabolics/Hormones</b>	<b>2,055</b>	<b>2,069</b>	<b>2,159</b>	<b>1,820</b>	<b>1,842</b>	<b>1,882</b>	<b>1,926</b>	<b>1,985</b>	<b>2,019</b>
Synthroid (thyroid disease)	551	622	709	744	782	821	862	905	950
Androgel (testosterone replacement)	1,151	1,035	934	492	419	356	302	257	180
Creon (pancreatic enzyme therapy)	353	412	516	583	641	706	762	823	889
<b>Endocrinology</b>	<b>800</b>	<b>785</b>	<b>778</b>	<b>748</b>	<b>713</b>	<b>679</b>	<b>646</b>	<b>615</b>	<b>586</b>
Lupron (palliative treatment of prostate cancers)	800	785	778	748	713	679	646	615	586
<b>Other pharmaceuticals</b>	<b>2,744</b>	<b>2,806</b>	<b>2,712</b>	<b>2,636</b>	<b>2,719</b>	<b>2,789</b>	<b>2,853</b>	<b>2,848</b>	<b>2,878</b>
Sevoflurane /Sevorane (Anesthesia)	602	568	550	488	478	468	459	450	441
Zemplar (renal care)	383	389	228	176	155	149	137	69	34
Synagis	842	827	835	810	850	893	938	984	1,034
Doudopa	153	178	220	331	404	447	487	513	537
Other pharma	764	844	879	832	832	832	832	832	832
<b>New Products</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>401</b>	<b>864</b>	<b>1,514</b>	<b>2,378</b>	<b>3,278</b>
daclizumab	-	-	-	-	152	248	300	352	408
ABT-888/Veliparib	-	-	-	-	-	-	225	575	800
ABT-199	-	-	-	-	150	330	480	600	720
elotuzumab	-	-	-	-	99	186	234	276	375
Elagolix	-	-	-	-	-	100	275	425	750
atrasentan (formerly Xinlay)	-	-	-	-	-	-	-	150	225
<b>Total Sales</b>	<b>18,380</b>	<b>18,790</b>	<b>19,879</b>	<b>21,752</b>	<b>23,781</b>	<b>24,950</b>	<b>25,403</b>	<b>25,156</b>	<b>25,434</b>
COGS	4,448	4,051	3,947	3,907	4,233	4,416	4,369	4,277	4,324
<b>Gross Profit</b>	<b>13,932</b>	<b>14,739</b>	<b>15,932</b>	<b>17,844</b>	<b>19,548</b>	<b>20,534</b>	<b>21,034</b>	<b>20,879</b>	<b>21,110</b>
SG&A	4,659	5,084	5,487	5,565	5,945	6,038	6,097	6,037	6,104
R&D	2,511	2,831	3,252	3,371	3,520	3,618	3,760	3,773	3,815
<b>Operating Expenses</b>	<b>7,170</b>	<b>7,915</b>	<b>8,739</b>	<b>8,936</b>	<b>9,465</b>	<b>9,656</b>	<b>9,856</b>	<b>9,811</b>	<b>9,919</b>
<b>Operating Income</b>	<b>6,762</b>	<b>6,824</b>	<b>7,193</b>	<b>8,908</b>	<b>10,083</b>	<b>10,878</b>	<b>11,177</b>	<b>11,069</b>	<b>11,191</b>
Net foreign exchange (gain) loss	17	44	12	20	20	20	20	20	20
Total other non-operating (income)/expense	37	265	257	279	257	157	90	38	(8)
<b>Earnings before taxes</b>	<b>6,708</b>	<b>6,515</b>	<b>6,924</b>	<b>8,610</b>	<b>9,806</b>	<b>10,701</b>	<b>11,067</b>	<b>11,011</b>	<b>11,179</b>
Tax expense (non-GAAP)	793	1,449	1,549	1,911	2,177	2,376	2,457	2,444	2,482
<b>Net Income</b>	<b>5,916</b>	<b>5,066</b>	<b>5,375</b>	<b>6,698</b>	<b>7,629</b>	<b>8,326</b>	<b>8,610</b>	<b>8,566</b>	<b>8,697</b>
earnings 2-class adjustment		(26)	(37)	-	-	-	-	-	-
<b>Diluted EPS (continuing)</b>	<b>\$3.75</b>	<b>\$3.14</b>	<b>\$3.32</b>	<b>\$4.21</b>	<b>\$4.89</b>	<b>\$5.42</b>	<b>\$5.63</b>	<b>\$5.60</b>	<b>\$5.68</b>
Diluted shares	1,577	1,607	1,610	1,591	1,559	1,536	1,530	1,530	1,530
Annual EPS Growth	23%	-14%	6%	25%	14%	9%	3%	-1%	2%

Source: Company Data, Goldman Sachs Global Investment Research

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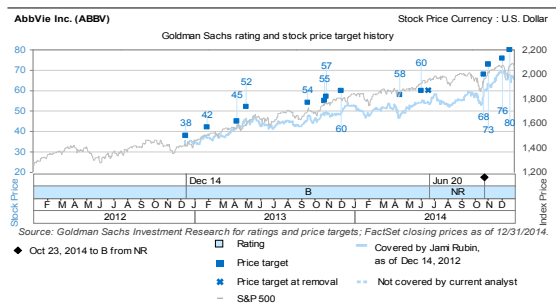
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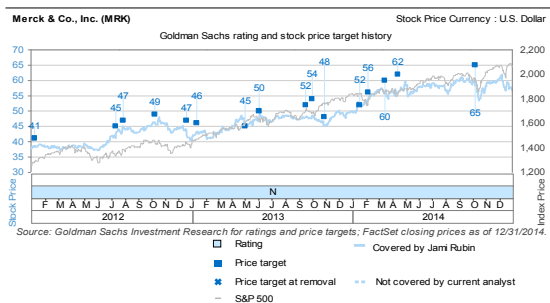
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