

Animal Health

A frosty start to 2024 for vet clinic trends

Industry Overview

Worsening data builds on 2+ years of negative trends

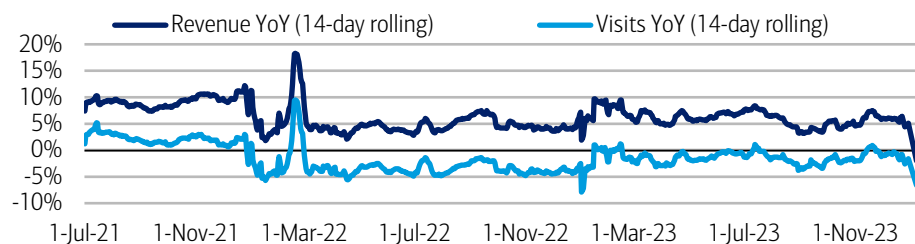
Year-on-year vet clinic visit and revenue data has had an unexpectedly soft start to 2024, particularly considering the declines observed through much of 2022 and 2023. As shown in Exhibit 1, per 3rd party Vetsource, visits in January are tracking down ~7% y/y and revenues have declined ~1.5% (after upwards adjustments to the data). Some of this can be explained by nuances in dataset construction (i.e. Vetsource compares the first Monday in January 2024 [01/01/24, or New Year's day] to the first Monday in 2023 [01/02/23], instead of comparing by date) or industry conditions like the structural shortage of vet labor and consumer challenges. That said, these weak readings on increasingly easy stacked comps give us added cause for concern on the end-market. Arguably more troubling than the visit numbers is the fact that revenue growth, which has held in relatively well, posted a year-on-year decline in early January 2024 for the first time in the life of the data, suggesting vet pressures may be growing more acute.

Could weather be to blame?

Although poor vet clinic trends are a headwind to the entire Animal Health space, they are particularly impactful to in-clinic diagnostic providers such as IDXX. Notably, our channel checks from the recent VMX industry conference ([linked here](#)) were relatively positive, with no indication from vets of incremental market weakness. For now, our leading hypothesis is that recent bouts of winter storms across the U.S. are to blame. The available vet data is noisy and limited in timespan, but in the past severe weather has occasionally led to temporary slowdowns in vet volumes. IDXX has also previously called out weather as a transient drag in prior year's earnings reports and filings. VMX itself might also be playing a role (ie, it's such a well-attended event that vet clinics were closed as everyone was in Orlando for the conference). Still, the duration of the downturn is concerning, and is starting to erode some of our confidence in the space for FY24. We maintain our ratings on ELAN, IDXX, and ZTS as we continue to appreciate the secular growth drivers, although we acknowledge persistent near-term challenges.

Exhibit 1: U.S vet clinic revenue and clinic growth

Clinic visits (-7%) and revenues (-1.5%) have both been surprisingly poor to start January



Source: Vetsource, BofA Global Research

BofA GLOBAL RESEARCH

25 January 2024

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ELAN: Elanco Animal Health

IDXX: IDEXX Laboratories

ZTS: Zoetis

VMX: Veterinary Meeting and Expo

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Timestamp: 25 January 2024 05:00AM EST

Exhibit 2: Stocks mentioned

Prices and ratings for stocks mentioned in this report

BofA Ticker	Bloomberg ticker	Company name	Price	Rating
ELAN	ELAN US	Elanco Animal Health	US\$ 14.56	B-1-9
IDXX	IDXX US	IDEXX	US\$ 520.21	B-2-9
ZTS	ZTS US	Zoetis Inc.	US\$ 186.07	B-1-7

Source: BofA Global Research

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Price objective basis & risk

Elanco Animal Health (ELAN)

Our \$18 PO is based on 14x our FY24 EV/EBITDA estimate.

Our target multiple is a roughly 5x discount to the company's closest animal health peer, given the slower sales growth and lower margin profile, but reflects some expectation of further improvements by Elanco.

Downside risks to our price objective are continued pressure from negative news flow on Seresto safety, market challenges from ongoing Coronavirus outbreak, deal integration challenges, competitive and generic launches for key products, slower-than-expected ramp for new product launches, increased regulation on antibiotic use in livestock, macroeconomic conditions, and currency risks.

IDEXX Laboratories (IDXX)

IDXX shares are trading at a significant premium to the broader animal health peer group and many other high growth healthcare companies. However, given the many positive secular and product tailwinds the company currently enjoys, we believe a premium valuation is justified. Our \$600 PO is based on roughly 55x our 2024E EPS estimate, which is in-line with (but at the higher end of) the company's historic valuation range, which we feel is justified given current macro and company-specific concerns.

Downside risks to our PO are continued market challenges from ongoing Coronavirus outbreak, lower spending on vet services in the event of an economic slowdown, slower-than-expected uptake of new products or OUS expansion, competition, lower-than-expected margin expansion, weather disruptions, and currency fluctuations.

Upside risks are a faster recovery in core vet volume trends in the US and abroad.

Zoetis Inc. (ZTS)

Our \$205 PO is based on 34x our FY24 EPS estimates. This is roughly in-line with the historic ZTS multiple, which we believe is justified given upside from new product launches and incremental capital deployment, further margin expansion opportunity, and the defensive nature of the business, as well as reflects the near-term headwinds due to the Coronavirus outbreak.

Upside risks are continued ramp of new products, larger-than-expected contribution from future and ongoing launches, and accelerating growth from Abaxis acquisition.

Downside risks to our price objective are continued challenges from ongoing Coronavirus outbreak, competition in select markets or new product launches by competitors, weaker demand for animal health products, regulatory issues such as failure to get approval of key products in the pipeline, macroeconomic conditions, currency risks, and headwinds related to regulations of antibiotic use in animal feed additives.

Analyst Certification

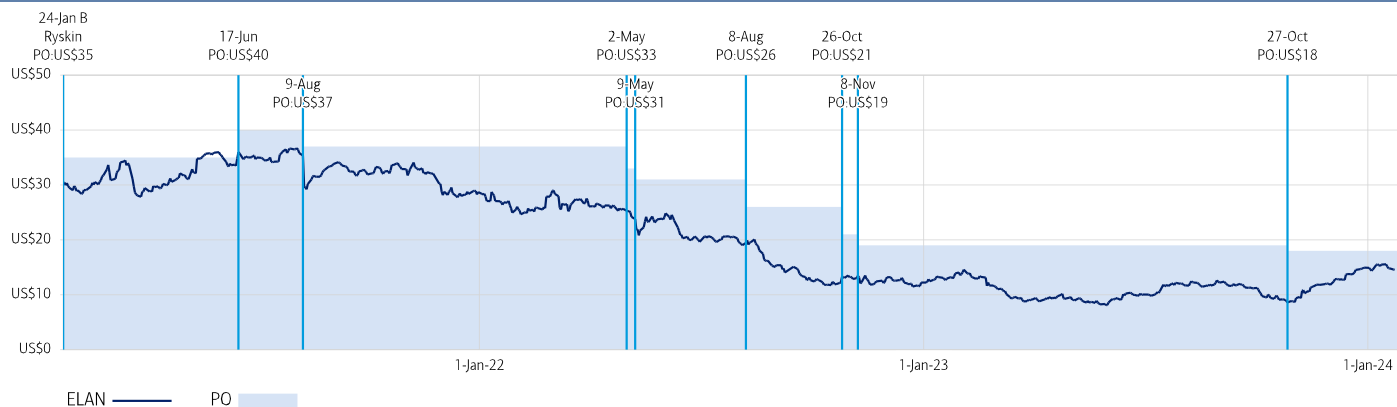
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US - Life Science, Diagnostic Tools and Animal Health Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
BUY				
	Avantor, Inc.	AVTR	AVTR US	Michael Ryskin
	Brucker Corporation	BRKR	BRKR US	Derik de Bruin
	Certara	CERT	CERT US	Michael Ryskin
	Charles River Laboratories	CRL	CRL US	Derik de Bruin
	Elanco Animal Health	ELAN	ELAN US	Michael Ryskin
	Exact Sciences	EXAS	EXAS US	Derik de Bruin
	Guardant Health	GH	GH US	Derik de Bruin
	ICON plc	ICLR	ICLR US	Derik de Bruin
	IQVIA Holdings Inc	IQV	IQV US	Derik de Bruin
	LabCorp	LH	LH US	Derik de Bruin
	Maravai	MRVI	MRVI US	Michael Ryskin
	Qiagen	QGEN	QGEN US	Derik de Bruin
	Qiagen N.V.	XQGNF	QIA GY	Derik de Bruin
	Quest Diagnostics	DGX	DGX US	Derik de Bruin
	Stevanato Group S.p.A.	STVN	STVN US	Derik de Bruin
	Thermo Fisher Scientific	TMO	TMO US	Derik de Bruin
	West Pharmaceutical Services	WST	WST US	Derik de Bruin
	Zoetis Inc.	ZTS	ZTS US	Michael Ryskin
NEUTRAL				
	10x Genomics, Inc.	TXG	TXG US	Michael Ryskin
	Agilent Technologies	A	A US	Derik de Bruin
	Danaher Corporation	DHR	DHR US	Michael Ryskin
	Evotec SE	EVO	EVO US	Michael Ryskin
	Hologic, Inc.	HOLX	HOLX US	Derik de Bruin
	IDEXX Laboratories	IDXX	IDXX US	Michael Ryskin
	Mettler-Toledo	MTD	MTD US	Derik de Bruin
	NeoGenomics Inc.	NEO	NEO US	Derik de Bruin
	Revvity Inc	RVTY	RVTY US	Derik de Bruin
	Schrodinger, Inc.	SDGR	SDGR US	Michael Ryskin
	Waters Corp.	WAT	WAT US	Derik de Bruin
UNDERPERFORM				
	Align Technology	ALGN	ALGN US	Michael Ryskin
	Catalent, Inc.	CTLT	CTLT US	Derik de Bruin
	Fortrea	FTRE	FTRE US	Derik de Bruin
	Ginkgo Bioworks Holdings, Inc	DNA	DNA US	Derik de Bruin
	Illumina, Inc.	ILMN	ILMN US	Michael Ryskin
	Myriad Genetics	MYGN	MYGN US	Derik de Bruin
	Phibro Animal Health	PAHC	PAHC US	Michael Ryskin

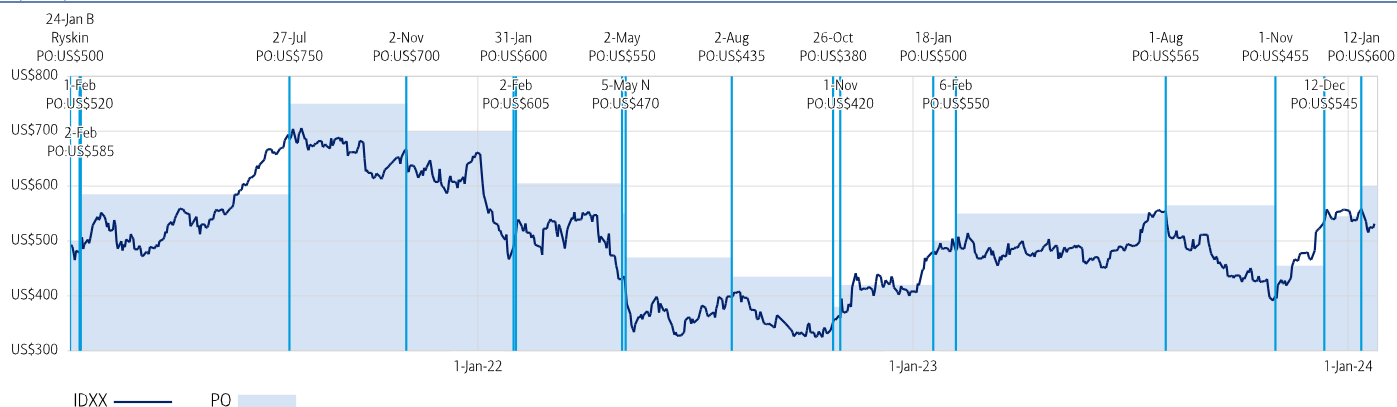
Disclosures

Important Disclosures

Elanco Animal Health (ELAN) Price Chart

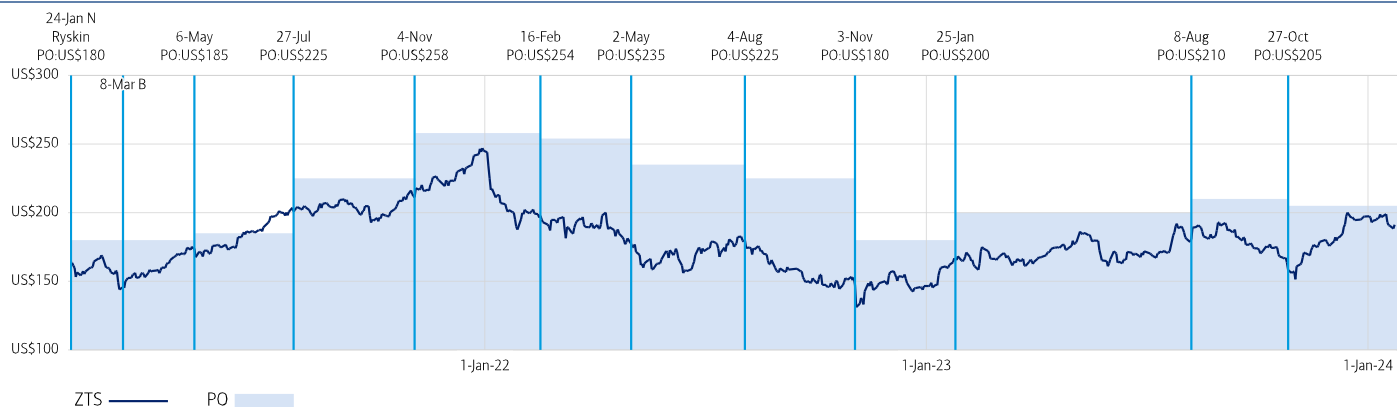
B: Buy, N: Neutral, U: Underperform, PO: Price Objective, NA: No longer valid, NR: No Rating

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IDEXX (IDXX) Price Chart

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Zoetis Inc. (ZTS) Price Chart

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Equity Investment Rating Distribution: Health Care Group (as of 31 Dec 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships ^{R1}	Count	Percent
Buy	234	60.94%	Buy	115	49.15%
Hold	80	20.83%	Hold	36	45.00%
Sell	70	18.23%	Sell	29	41.43%

Equity Investment Rating Distribution: Global Group (as of 31 Dec 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships ^{R1}	Count	Percent
Buy	1895	53.62%	Buy	1083	57.15%
Hold	832	23.54%	Hold	454	54.57%
Sell	807	22.84%	Sell	383	47.46%

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Investment rating	Total return expectation (within 12-month period of date of initial rating)	Ratings dispersion guidelines for coverage cluster ^{R2}
Buy	≥ 10%	≤ 70%
Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

^{R2} Ratings dispersions may vary from time to time where BofA Global Research believes it better reflects the investment prospects of stocks in a Coverage Cluster.

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