

Merck & Co.

Thoughts Post the 4Q call

Reiterate Rating: BUY | PO: 135.00 USD | Price: 126.38 USD

Solid 4Q; 2024 outlook looks beatable

MRK shares traded with strength (+4.6%; DRG index: +1%) following solid 4Q results driven by strong Keytruda sales, offset by a modest miss from Gardasil. Importantly, Merck's 2024 guidance was nominally above consensus but still looks beatable especially given bullish commentary on core products (Keytruda, Gardasil) and new launches (sotatercept and V116). For new launches, we thought that the tone ahead of the sotatercept launch (PDUFA date: March 26) and for V116 (PDUFA date: June 17) was quite positive with the latter expected to take a majority of the adult pneumococcal market based the strength of the data (admittedly preferential ACIP recommendation is unlikely). Moreover, Merck's pediatric RSV antibody could differentiate vs. competitors (Sanofi's Beyfortus and Pfizer's Abrysvo) on dosing / durability and gain a foothold in a multi-billion dollar market (potential launch in 2025). Overall, we remain bullish on MRK shares given its strong core business and a number of launches starting this year that could drive upside performance; we see ample of BD opportunities in coming years to further diversify away from Keytruda concentration. Reiterate Buy, \$135 PO.

Upside potential from new launches

Merck has made progress in diversification, as highlighted by: 1) sotatercept approval and launch in early 2024 (2030e rev: \$4.6B BofA vs. \$4.3B cons), 2) the Prometheus deal ([see our takeaways on the deal](#) report) which brings a potential disrupter (PRA023) in the inflammatory and immunology category, 3) V116 launch in the adult pneumococcal market, 4) HER3-DXd launch (PDUFA June 26) in EGFR lung cancer, and 5) RSV pediatric antibody data / launch in 2025. Separately, Merck's margin profile should continue to improve until the Keytruda LOE, driven by favorable product mix and reduced Keytruda/Gardasil royalties, which translates into better cash flow and likely higher BD activity.

Model updates

We've updated our Merck model to reflect today's 4Q results and updated outlook. We model \$64.2B and \$8.57 EPS for 2024e. See pg 3 for model changes >>

Estimates (Dec) (US\$)	2022A	2023A	2024E	2025E	2026E
EPS	7.48	1.51	8.57	10.05	10.90
GAAP EPS	5.71	0.63	8.14	9.66	10.54
EPS Change (YoY)	39.3%	-79.8%	467.5%	17.3%	8.5%
Consensus EPS (Bloomberg)			8.44	9.60	10.42
DPS	2.76	2.92	3.09	3.27	3.46
Valuation (Dec)					
P/E	16.9x	83.7x	14.7x	12.6x	11.6x
GAAP P/E	22.1x	200.6x	15.5x	13.1x	12.0x
Dividend Yield	2.2%	2.3%	2.4%	2.6%	2.7%
EV / EBITDA*	13.3x	30.8x	11.2x	9.8x	9.1x
Free Cash Flow Yield*	4.6%	1.0%	7.1%	8.3%	8.9%

* For full definitions of *IQmethod*SM measures, see page 5.

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Timestamp: 01 February 2024 05:57PM EST

01 February 2024

Equity

Key Changes

(US\$)	Previous	Current
2024E Rev (m)	64,962.9	64,166.8
2025E Rev (m)	69,908.3	69,440.0
2026E Rev (m)	73,705.5	73,868.3
2024E EPS	8.60	8.57
2025E EPS	9.70	10.05
2026E EPS	10.50	10.90
2024E EBITDA (m)	32,169.1	31,205.0
2025E EBITDA (m)	35,497.9	35,910.8
2026E EBITDA (m)	37,275.6	38,504.2

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Stock Data

Price	126.38 USD
Price Objective	135.00 USD
Date Established	26-Jan-2024
Investment Opinion	A-1-7
52-Week Range	99.14 USD - 126.43 USD
Mrkt Val (mn) / Shares Out (mn)	320,250 USD / 2,534.0
Free Float	99.6%
Average Daily Value (mn)	988.16 USD
BoFA Ticker / Exchange	MRK / NYS
Bloomberg / Reuters	MRK US / MRK.N
ROE (2024E)	53.4%
Net Dbt to Eqty (Dec-2023A)	94.7%
ESGMeter™	High

ESGMeter is not indicative of a company's future stock price performance and is not an investment recommendation or rating. ESGMeter is independent of BoFA Global Research's equity investment rating, volatility risk rating, income rating, and price objective for that company. For full details, refer to "BoFA ESGMeter Methodology".

iQprofileSM Merck & Co.

iQmethodSM – Bus Performance*

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Return on Capital Employed	22.6%	4.7%	24.7%	25.2%	24.4%
Return on Equity	45.1%	9.5%	53.4%	46.7%	38.8%
Operating Margin	38.0%	10.3%	40.3%	43.8%	44.5%
Free Cash Flow	14,707	3,319	22,860	26,487	28,385

iQmethodSM – Quality of Earnings*

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Cash Realization Ratio	1.0x	1.8x	1.2x	1.2x	1.2x
Asset Replacement Ratio	1.1x	0.7x	0.7x	0.8x	0.8x
Tax Rate	14.2%	35.7%	15.0%	15.5%	15.5%
Net Debt-to-Equity Ratio	39.1%	94.7%	40.7%	2.2%	-22.2%
Interest Cover	NA	NA	NA	NA	29.7x

Income Statement Data (Dec)

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Sales	59,283	60,115	64,167	69,440	73,868
% Change	21.7%	1.4%	6.7%	8.2%	6.4%
Gross Profit	44,136	46,219	51,654	56,233	59,981
% Change	19.1%	4.7%	11.8%	8.9%	6.7%
EBITDA	26,431	11,386	31,205	35,911	38,504
% Change	37.3%	-56.9%	174.1%	15.1%	7.2%
Net Interest & Other Income	(360)	0	0	0	176
Net Income (Adjusted)	19,005	3,841	21,793	25,509	27,597
% Change	39.5%	-79.8%	467.4%	17.1%	8.2%

Free Cash Flow Data (Dec)

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Net Income from Cont Operations (GAAP)	14,526	1,619	20,694	24,522	26,709
Depreciation & Amortization	3,909	5,175	5,354	5,510	5,633
Change in Working Capital	(3,162)	3	(495)	(916)	(780)
Deferred Taxation Charge	380	53	258	336	282
Other Adjustments, Net	3,442	215	1,047	1,362	1,144
Capital Expenditure	(4,388)	(3,746)	(3,998)	(4,327)	(4,603)
Free Cash Flow	14,707	3,319	22,860	26,487	28,385
% Change	69.6%	-77.4%	588.7%	15.9%	7.2%
Share / Issue Repurchase	384	0	(1,000)	(500)	(500)
Cost of Dividends Paid	(7,012)	(7,437)	(7,853)	(8,292)	(8,755)
Change in Debt	(2,251)	7,013	(500)	(2,495)	(1,362)

Balance Sheet Data (Dec)

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Cash & Equivalents	12,694	4,649	18,155	33,355	51,124
Trade Receivables	9,450	9,583	10,228	11,069	11,775
Other Current Assets	13,578	13,591	13,542	14,450	15,251
Property, Plant & Equipment	21,422	22,893	24,388	26,005	27,725
Other Non-Current Assets	52,016	54,334	51,484	48,684	45,934
Total Assets	109,160	105,050	117,797	133,564	151,809
Short-Term Debt	1,946	5,308	5,308	5,308	5,308
Other Current Liabilities	22,293	22,167	22,881	24,513	25,911
Long-Term Debt	28,745	32,396	31,896	29,401	28,039
Other Non-Current Liabilities	10,118	10,260	10,952	11,852	12,607
Total Liabilities	63,102	70,131	71,037	71,074	71,865
Total Equity	46,058	34,919	46,760	62,490	79,944
Total Equity & Liabilities	109,160	105,050	117,797	133,564	151,809

* For full definitions of iQmethodSM measures, see page 5.

Company Sector

Pharmaceuticals

Company Description

Merck & Co. is a global pharma company focused on discovering, developing and marketing drugs for respiratory, immunology, cardiovascular, diabetes, infectious diseases, oncology and other indications. The company is a global leader in vaccines and is further diversified with an animal health division.

Investment Rationale

Our Buy thesis is based on expectation of solid near-term revenue growth driven by strong commercial performance from core business (i.e., Keytruda and Gardasil), and favorable risk-reward profile with limited down-side risk. We think meaningful BD is still required to overcome Merck's tough growth trajectory post 2027, but the company has developed a strategy and has time to execute on BD deals.

Stock Data

Average Daily Volume 7,818,994

Quarterly Earnings Estimates

	2023	2024
Q1	1.40A	NA
Q2	-2.06A	NA
Q3	2.13A	NA
Q4	0.03A	NA

Model Changes

Exhibit 1: Model Changes

2024/25 model changes

\$ in millions	2024E		2025E	
	Prior	Current	Prior	Current
Keytruda - US	\$ 17,200	\$ 17,400	\$ 19,200	\$ 19,200
Keytruda - OUS	11,000	11,300	12,200	12,500
Keytruda Total	28,200	28,700	31,400	31,700
Lynparza	1,398	1,280	1,521	1,360
Lenvima	1,123	1,045	1,087	1,128
Gardasil	10,451	10,036	11,196	10,889
Sotatercept	293	300	810	900
Total Revenue	\$64,963	\$64,167	\$69,908	\$69,440
COGS	12,908	12,513	13,982	13,207
Gross Profit	52,055	51,654	55,927	56,233
SG&A	11,304	11,229	11,835	11,805
R&D	13,967	14,574	14,121	14,027
EBIT	26,784	25,851	29,970	30,401
Taxes	4,321	3,848	4,862	4,681
Adjusted Net Income	21,858	21,793	24,597	25,509
Non-GAAP EPS - Diluted	\$8.60	\$8.57	\$9.70	\$10.05

Source: BofA Global Research estimates

BofA GLOBAL RESEARCH

Abbreviations:

BD: business development

KOL: key opinion leader

ADC: antibody drug conjugate

PDUFA: The Prescription Drug User Fee Act

ACIP: Advisory Committee on Immunization Practices

EGFR: Epidermal growth factor receptor

RSV: Respiratory Syncytial Virus



Price objective basis & risk

Merck & Co. (MRK)

Our \$135 price objective (PO) is based on the intrinsic value of Merck standalone. We use a 50/50 blended average of our P/E multiple applied to 2025E EPS (we think the current 17x vs. 18x peer average makes sense to reflect continued strength of Merck's core growth franchises but broader Keytruda concentration risk concerns) and risk-adjusted DCF (7% WACC and -2% terminal growth rate).

Risks to our PO are 1) impressive competitor readouts results in key immuno-oncology (I/O) indications, 2) more rapid declines across the diabetes franchise than expected, 3) negative outcomes from the company's later-stage assets in ongoing development, and 4) pressures from headline risks facing the sector (including drug pricing reform).

Analyst Certification

I, Geoff Meacham, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.

US - Biopharmaceuticals Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
BUY				
	89bio, Inc	ETNB	ETNB US	Geoff Meacham
	Acumen Pharma	ABOS	ABOS US	Geoff Meacham
	Agios Pharmaceuticals	AGIO	AGIO US	Greg Harrison, CFA
	Amylyx Pharmaceuticals	AMLX	AMLX US	Geoff Meacham
	BioMarin	BMRN	BMRN US	Geoff Meacham
	BioXcel Therapeutics	BTAI	BTAI US	Greg Harrison, CFA
	BridgeBio Pharma	BBIO	BBIO US	Greg Harrison, CFA
	Caribou	CRBU	CRBU US	Geoff Meacham
	CRISPR Therapeutics	CRSP	CRSP US	Geoff Meacham
	Eli Lilly and Company	LLY	LLY US	Geoff Meacham
	Gilead Sciences Inc.	GILD	GILD US	Geoff Meacham
	HUTCHMED	HCM	HCM US	Alec W. Stranahan
	Immatics	IMTX	IMTX US	Alec W. Stranahan
	Insmid Incorporated	INSM	INSM US	Jason Zemansky
	Intellia Therapeutics	NTLA	NTLA US	Greg Harrison, CFA
	Janux Therapeutics	JANX	JANX US	Geoff Meacham
	Keros	KROS	KROS US	Greg Harrison, CFA
	Kiniksa Pharmaceuticals, Ltd.	KNSA	KNSA US	Geoff Meacham
	Krystal Biotech	KRYS	KRYS US	Alec W. Stranahan
	Kura Oncology	KURA	KURA US	Jason Zemansky
	Liquidia Corporation	LQDA	LQDA US	Greg Harrison, CFA
	Lyell Immunopharma	LYEL	LYEL US	Geoff Meacham
	MeiraGTx	MGTX	MGTX US	Alec W. Stranahan
	Merck & Co.	MRK	MRK US	Geoff Meacham
	Mineralys Therapeutics	MLYS	MLYS US	Greg Harrison, CFA
	Neumora Therapeutics	NMRA	NMRA US	Geoff Meacham
	Rani Therapeutics	RANI	RANI US	Geoff Meacham
	Regenxbio, Inc.	RGNX	RGNX US	Alec W. Stranahan
	Revolution Medicines	RVMD	RVMD US	Alec W. Stranahan
	Rocket Pharmaceuticals, Inc.	RCKT	RCKT US	Greg Harrison, CFA
	Royalty Pharma	RPRX	RPRX US	Geoff Meacham
	Sana Biotechnology	SANA	SANA US	Geoff Meacham
	SpringWorks	SWTX	SWTX US	Alec W. Stranahan
	Syndax Pharmaceuticals	SNDX	SNDX US	Jason Zemansky
	Traverse Therapeutics Inc	TVTX	TVTX US	Greg Harrison, CFA
	Turnstone Biologics	TSBX	TSBX US	Geoff Meacham
	Vertex Pharmaceuticals Inc.	VRTX	VRTX US	Geoff Meacham

US - Biopharmaceuticals Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
	Werewolf Therapeutics	HOWL	HOWL US	Jason Zemansky
	Xencor	XNCR	XNCR US	Alec W. Stranahan
NEUTRAL	AbbVie	ABBV	ABBV US	Geoff Meacham
	Alector, Inc	ALEC	ALEC US	Greg Harrison, CFA
	Amgen Inc.	AMGN	AMGN US	Geoff Meacham
	Arcus Biosciences	RCUS	RCUS US	Jason Zemansky
	Beam Therapeutics	BEAM	BEAM US	Greg Harrison, CFA
	Biogen Inc.	BIIB	BIIB US	Geoff Meacham
	Bristol-Myers Squibb	BMJ	BMJ US	Geoff Meacham
	Cytokines, Incorporated	CYTK	CYTK US	Jason Zemansky
	Editas Medicine	EDIT	EDIT US	Greg Harrison, CFA
	Erasca	ERAS	ERAS US	Alec W. Stranahan
	Esperion	ESPR	ESPR US	Jason Zemansky
	Exscientia	EXAI	EXAI US	Alec W. Stranahan
	IGM Biosciences	IGMS	IGMS US	Greg Harrison, CFA
	Johnson & Johnson	JNJ	JNJ US	Geoff Meacham
	Kymera Therapeutics	KYMR	KYMR US	Geoff Meacham
	Moderna	MRNA	MRNA US	Geoff Meacham
	Pfizer	PFE	PFE US	Geoff Meacham
	Recursion Pharmaceuticals, Inc.	RXR	RXR US	Alec W. Stranahan
	Tyra Biosciences	TYRA	TYRA US	Greg Harrison, CFA
	Vir	VIR	VIR US	Geoff Meacham
	Y-mAbs Therapeutics, Inc	YMAB	YMAB US	Alec W. Stranahan
UNDERPERFORM	AlloVir, Inc.	ALVR	ALVR US	Jason Zemansky
	CureVac	CVAC	CVAC US	Geoff Meacham
	Day One Biopharmaceuticals	DAWN	DAWN US	Alec W. Stranahan
	LianBio	LIAN	LIAN US	Geoff Meacham
	Novavax	NVAX	NVAX US	Alec W. Stranahan
	Regeneron Pharmaceuticals Inc.	REGN	REGN US	Geoff Meacham
	Reneo Pharmaceuticals	RPHM	RPHM US	Jason Zemansky
	TG Therapeutics	TGTX	TGTX US	Alec W. Stranahan
	United Therapeutics Corporation	UTHR	UTHR US	Greg Harrison, CFA

IQmethodSM Measures Definitions**Business Performance**

Return On Capital Employed

Return On Equity

Operating Margin

Earnings Growth

Free Cash Flow

Quality of Earnings

Cash Realization Ratio

Asset Replacement Ratio

Tax Rate

Net Debt-To-Equity Ratio

Interest Cover

Valuation Toolkit

Price / Earnings Ratio

Price / Book Value

Dividend Yield

Free Cash Flow Yield

Enterprise Value / Sales

EV / EBITDA

Numerator

NOPAT = (EBIT + Interest Income) × (1 – Tax Rate) + Goodwill Amortization

Net Income

Operating Profit

Expected 5 Year CAGR From Latest Actual

Cash Flow From Operations – Total Capex

Numerator

Cash Flow From Operations

Capex

Tax Charge

Net Debt = Total Debt – Cash & Equivalents

EBIT

Numerator

Current Share Price

Current Share Price

Annualised Declared Cash Dividend

Cash Flow From Operations – Total Capex

EV = Current Share Price × Current Shares + Minority Equity + Net Debt +

Other LT Liabilities

Enterprise Value

Denominator

Total Assets – Current Liabilities + ST Debt + Accumulated Goodwill Amortization

Shareholders' Equity

Sales

N/A

N/A

Denominator

Net Income

Depreciation

Pre-Tax Income

Total Equity

Interest Expense

Denominator

Diluted Earnings Per Share (Basis As Specified)

Shareholders' Equity / Current Basic Shares

Current Share Price

Market Cap = Current Share Price × Current Basic Shares

Sales

Basic EBIT + Depreciation + Amortization

Valuation Toolkit

Numerator

Denominator

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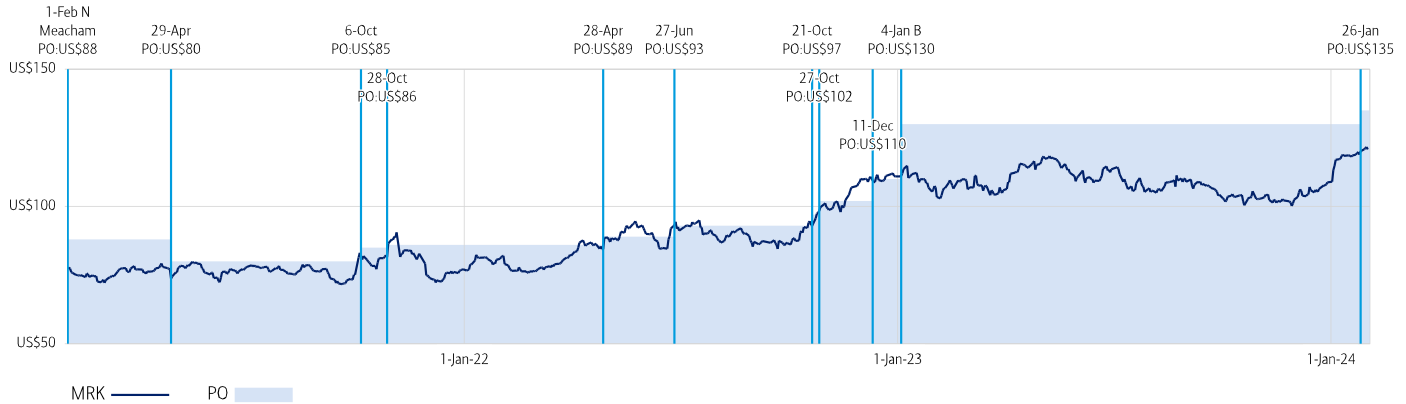
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Important Disclosures

Merck & Co. (MRK) Price Chart



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

The Investment Opinion System is contained at the end of the report under the heading "Fundamental Equity Opinion Key". Dark grey shading indicates the security is restricted with the opinion suspended. Medium grey shading indicates the security is under review with the opinion withdrawn. Light grey shading indicates the security is not covered. Chart is current as of a date no more than one trading day prior to the date of the report.

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%

^{R1} Issuers that were investment banking clients of BofA Securities or one of its affiliates within the past 12 months. For purposes of this Investment Rating Distribution, the coverage universe includes only stocks. A stock rated Neutral is included as a Hold, and a stock rated Underperform is included as a Sell.

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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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