

Elanco Animal Health

Solid initial FY24 guide with core business stabilizing; room for upside from launches

Reiterate Rating: BUY | PO: 18.00 USD | Price: 16.26 USD

4Q sales ahead; Adj EBITDA & Adj EPS below expectations

Elanco (ELAN US) reported mixed 4Q results. Sales of \$1,035mn were ahead of BofAe/Street; Adj EBITDA margin of 15.9% was below BofAe 17.0%, while Adj EPS of \$0.08 was 3c below Street. [Please see our 4Q First Look note for further details.](#)

Guide shows improving core; upside from 2H launches

ELAN initiated FY24 guidance which broadly met expectations while also containing several key moving pieces. Notably, ELAN's 1-3% constant currency sales growth outlook does not include the contribution from FY24 product launches, which are already partially baked into consensus. Although sales growth in the legacy portfolio will be driven by price as volumes (-3% to -4% ex-innovation) are expected to show another muted year, we highlight that volume declines have continued to improve since FY22 despite ongoing competitive headwinds. We see this as a sign of stabilization in the core business. Like sales, ELAN's Adj EBITDA outlook also excludes new products, with mgmt. remarking that they will make upward revisions to guidance as products are approved. Overall, we see this as a solid start to FY24, as new products are likely to drive upside to FY24 consensus ests that already embedded some contribution from these launches.

Pipeline on track; More restructuring to drive innovation

Mgmt reiterated prior 1H24 approval timelines for Credelio Quattro, Zenrelia, & Bovaer and indicated that their pre-approval dialogues with the FDA remain constructive. ELAN also announced a new round of restructuring focused on the Farm Animal segment which is expected to yield savings of \$20-\$25mn in FY24 and \$30-\$35mn in FY25 onward. These savings will be reinvested in supporting the rollout of upcoming launches as well as continued innovation in high growth/profitability areas, namely Pet Health and Livestock Sustainability. We view these investment shifts as a prudent way to support key areas of future growth without adding to the company's overall cost base.

Update estimates; Reiterate Buy & \$18 PO

All in all, ELAN ended FY23 on a steady note and the initial FY24 guide suggests that the core business is stabilizing while leaving upside for incremental contributions from new product launches. We make modest tweaks to our forecasts. Our PO remains \$18 (~14x BofAe FY24 Adj EBITDA), and we reiterate our Buy rating as we continue to see an attractive risk/reward setup presented by ELAN's coming product cycle.

Estimates (Dec) (US\$)	2022A	2023A	2024E	2025E	2026E
EPS	1.11	0.89	0.92	1.05	1.20
EPS Change (YoY)	3.7%	-19.8%	3.4%	14.1%	14.3%
Consensus EPS (Bloomberg)			0.89	1.00	1.09
DPS	0	0	0	0	0
Valuation (Dec)					
P/E	14.6x	18.3x	17.7x	15.5x	13.6x
EV / EBITDA*	14.9x	15.4x	15.2x	13.9x	12.6x
Free Cash Flow Yield*	3.9%	1.6%	3.4%	6.1%	7.1%

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

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Timestamp: 26 February 2024 07:55PM EST

26 February 2024

Equity

Key Changes

(US\$)	Previous	Current
2024E Rev (m)	4,520.1	4,514.7
2025E Rev (m)	4,720.2	4,719.8
2026E Rev (m)	NA	4,950.1
2026E EPS	NA	1.20

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Stock Data

Price	16.26 USD
Price Objective	18.00 USD
Date Established	27-Oct-2023
Investment Opinion	C-1-9
52-Week Range	7.88 USD - 16.88 USD
Mkt Val (mn) / Shares Out (mn)	8,013 USD / 492.8
Free Float	99.4%
Average Daily Value (mn)	75.48 USD
BofA Ticker / Exchange	ELAN / NYS
Bloomberg / Reuters	ELAN US / ELAN.N
ROE (2024E)	8.6%
Net Dbt to Eqty (Dec-2023A)	87.1%
ESGMeter TM	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 Elanco Animal Health

iQmethodSM – Bus Performance*

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Return on Capital Employed	5.1%	4.9%	5.5%	6.2%	6.8%
Return on Equity	7.3%	6.5%	8.6%	11.6%	12.6%
Operating Margin	20.7%	19.8%	19.4%	20.4%	21.5%
Free Cash Flow	315	131	270	491	567

iQmethodSM – Quality of Earnings*

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Cash Realization Ratio	0.8x	0.6x	1.0x	1.3x	1.3x
Asset Replacement Ratio	0.2x	0.2x	0.2x	0.2x	0.2x
Tax Rate	17.7%	22.8%	21.0%	21.0%	21.0%
Net Debt-to-Equity Ratio	75.3%	87.1%	120.3%	103.8%	89.9%
Interest Cover	NA	NA	NA	NA	NA

Income Statement Data (Dec)

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Sales	4,411	4,417	4,515	4,720	4,950
% Change	-7.4%	0.1%	2.2%	4.5%	4.9%
Gross Profit	2,498	2,488	2,542	2,696	2,872
% Change	-7.3%	-0.4%	2.2%	6.0%	6.5%
EBITDA	1,017	981	993	1,086	1,196
% Change	-4.0%	-3.5%	1.2%	9.4%	10.1%
Net Interest & Other Income	(252)	(307)	(295)	(295)	(295)
Net Income (Adjusted)	545	439	457	527	609
% Change	4.4%	-19.4%	4.2%	15.2%	15.6%

Free Cash Flow Data (Dec)

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Net Income from Cont Operations (GAAP)	545	439	457	527	609
Depreciation & Amortization	682	694	803	828	852
Change in Working Capital	(462)	(300)	0	0	0
Deferred Taxation Charge	(57)	(80)	(50)	(50)	(50)
Other Adjustments, Net	(256)	(482)	(761)	(623)	(645)
Capital Expenditure	(137)	(140)	(180)	(190)	(200)
Free Cash Flow	315	131	270	491	567
% Change	-11.8%	-58.4%	106.1%	82.0%	15.3%
Share / Issue Repurchase	NA	NA	NA	NA	NA
Cost of Dividends Paid	0	0	0	0	0
Change in Debt	(502)	(77)	(300)	(300)	(300)

Balance Sheet Data (Dec)

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Cash & Equivalents	345	352	197	264	405
Trade Receivables	1,002	1,010	1,051	1,094	1,150
Other Current Assets	1,932	2,045	1,516	1,577	1,658
Property, Plant & Equipment	999	1,026	1,087	1,153	1,222
Other Non-Current Assets	11,213	9,929	9,929	9,929	9,929
Total Assets	15,491	14,362	13,781	14,016	14,365
Short-Term Debt	388	38	38	38	38
Other Current Liabilities	1,314	1,203	1,713	1,742	1,814
Long-Term Debt	5,448	5,736	5,436	5,136	4,836
Other Non-Current Liabilities	1,052	1,162	2,208	2,370	2,708
Total Liabilities	8,202	8,139	9,395	9,287	9,395
Total Equity	7,289	6,223	4,386	4,730	4,969
Total Equity & Liabilities	15,491	14,362	13,781	14,016	14,365

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

Company Sector

Pharmaceuticals

Company Description

Elanco is one of the largest global manufacturers of animal health medicines and vaccines for both the production and companion animal markets. Its portfolio is well-diversified with a presence in every major species, product class, and geography.

Investment Rationale

We believe Elanco should benefit from rising demand for companion and production animal health products, particularly in emerging markets, new products launches in key growth categories, and substantial margin expansion driven by manufacturing site optimization and productivity initiatives. Additionally, the pending Bayer Animal Health acquisition is a source of substantial upside to margin expansion and scale, albeit with some ongoing uncertainty.

Stock Data

Average Daily Volume 4,642,209

Quarterly Earnings Estimates

	2023	2024
Q1	0.45A	0.27E
Q2	0.18A	0.25E
Q3	0.18A	0.20E
Q4	0.08A	0.20E



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.

Analyst Certification

I, Michael Ryskin, 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.

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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
	Bruker 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
	Marava	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
	Revity Inc	RVTY	RVTY US	Derik de Bruin
	Schrodinger, Inc.	SDGR	SDGR US	Michael Ryskin
	Waters Corp.	WAT	WAT US	Derik de Bruin

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

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
UNDERPERFORM	Align Technology	ALGN	ALGN US	Michael Ryskin
	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

iQmethodSM Measures Definitions**Business Performance**

Return On Capital Employed

Return On Equity

Operating Margin

Earnings Growth

Free Cash Flow

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

Denominator

Total Assets – Current Liabilities + ST Debt + Accumulated Goodwill

Amortization

Shareholders' Equity

Sales

N/A

N/A

Quality of Earnings

Cash Realization Ratio

Asset Replacement Ratio

Tax Rate

Net Debt-To-Equity Ratio

Interest Cover

Numerator

Cash Flow From Operations

Capex

Tax Charge

Net Debt = Total Debt – Cash & Equivalents

EBIT

Denominator

Net Income

Depreciation

Pre-Tax Income

Total Equity

Interest Expense

Valuation Toolkit

Price / Earnings Ratio

Price / Book Value

Dividend Yield

Free Cash Flow Yield

Enterprise Value / Sales

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

Diluted Earnings Per Share (Basis As Specified)

Shareholders' Equity / Current Basic Shares

Current Share Price

Market Cap = Current Share Price × Current Basic Shares

Sales

EV / EBITDA

Basic EBIT + Depreciation + Amortization

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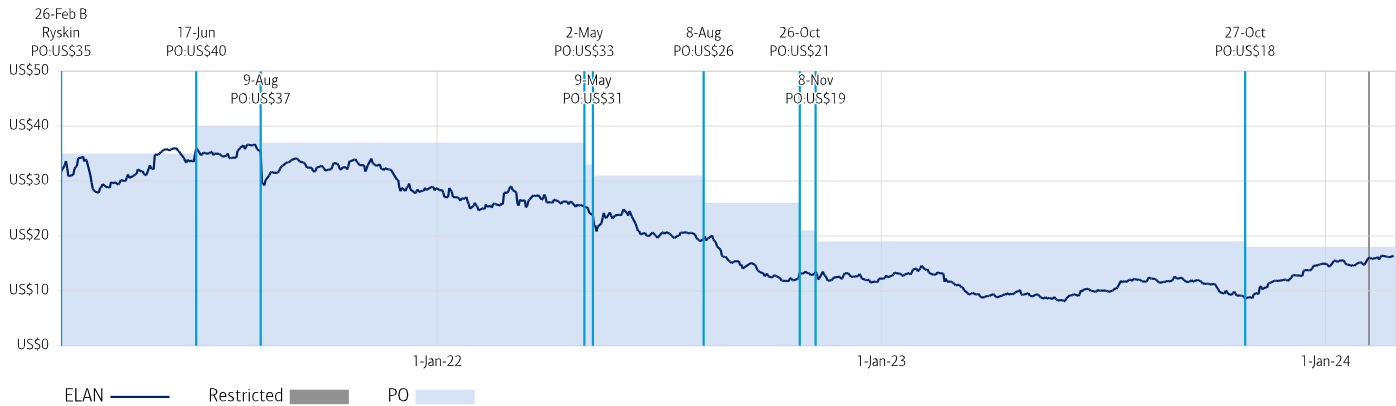
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Elanco Animal Health (ELAN) Price Chart



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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