

Zoetis

(ZTS-NYSE)

Stock Rating: Outperform
Industry Rating: Market Perform

Easing of US Drought and Lower Corn Prices Should Increase Confidence

Event

We are providing an update on Zoetis based on our analysis of US drought data and corn prices.

Impact

The unambiguous easing of US drought conditions and resulting sharp decline in corn prices (y/y) are incrementally positive for Zoetis's US livestock business, which accounts for roughly 18% of revenues. Lower corn prices should result in increased use of animal health products as livestock farmers take advantage to increase the amount of time on feedlots and probably grow herd sizes. Given that most of the negative impact of the 2012 drought started in 3Q12, we expect a favorable y/y comparison in 2H13.

Forecasts

Although, our forecasts remain on the lower range of the company's 2013 guidance, we now have increased confidence in the guidance. Our 10-year revenue forecast implies a CAGR of 4.4%, in line with 2Q13 operational growth. Our 2013-2016 EPS CAGR is 12.2%.

Valuation

\$36/share based on DCF assuming 2.5% terminal growth rate and 8.3% discount rate, supported by 22-23x our non-GAAP 2014-2016 EPS estimates.

Recommendation

Buy. We believe the key issue with ZTS shares is a shortage of investor comfort with bullish Street expectations given the lack of sales visibility. However, improving drought conditions in the US and lower feed prices lowers some of the near-term risk. As near-term investors exit post the Pfizer split-off in late June, and longer term investors enter after a worrisome 2Q13, we continue to believe that Zoetis is a unique healthcare growth story with therapeutic and geographically diversified revenues and strong fundamental growth drivers (i.e., growing global demand for animal protein and pet ownership, particularly in emerging markets).

This report was prepared by an analyst(s) employed by BMO Nesbitt Burns Inc. For disclosure statements, including the Analyst's Certification, please refer to pages 13 to 17.

September 6, 2013

Pharmaceuticals

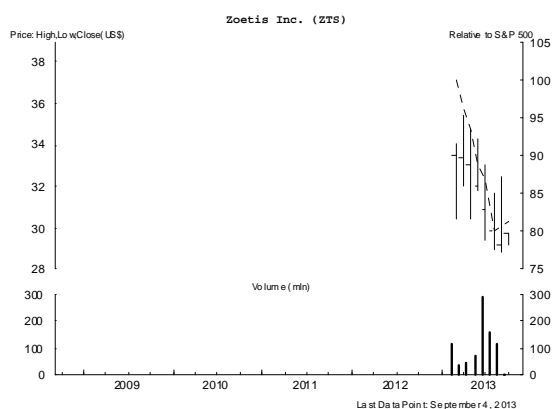
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Securities Info

Price (5-Sep)	\$30.33	Target Price	\$36
52-Wk High/Low	\$35/\$29	Dividend	\$0.26
Mkt Cap (mm)	\$15,165	Yield	0.9%
Shs O/S (mm, BASIC)	500.0	Float O/S (mm)	99.0
Options O/S (mm)	na	ADVol (30-day, 000s)	4,984

Price Performance



Valuation/Financial Data

(FY-Dec.)	2011 A	2012 A	2013 E	2014 E
EPS Pro Forma	\$1.01	\$1.08	\$1.37	\$1.54
P/E			22.1x	19.7x
First Call Cons.			\$1.40	\$1.61
EPS GAAP	\$0.49	\$0.87	\$1.05	\$1.39
FCF	\$0.72	\$0.66	\$1.46	\$1.42
P/FCF			20.8x	21.4x
EBITDA (\$mm)	\$943	\$1,142	\$1,216	\$1,402
EV/EBITDA			15.2x	13.2x
Rev. (\$mm)	\$4,233	\$4,336	\$4,459	\$4,661
EV/Rev			4.1x	4.0x
Quarterly EPS	1Q	2Q	3Q	4Q
2012 A	\$0.30	\$0.35	\$0.31	\$0.11
2013 E	\$0.36 A	\$0.36 A	\$0.33	\$0.33
Balance Sheet Data (30-Jun)				
Net Debt (\$mm)	\$3,333		Total Debt/EBITDA	3.0x
Total Debt (\$mm)	\$3,650		EBITDA/IntExp	11.3x
Net Debt/Cap.	na		Price/Book	21.4x

Notes: All values in US\$.

Source: BMO Capital Markets estimates, Bloomberg, Thomson Reuters, and IHS Global Insight.

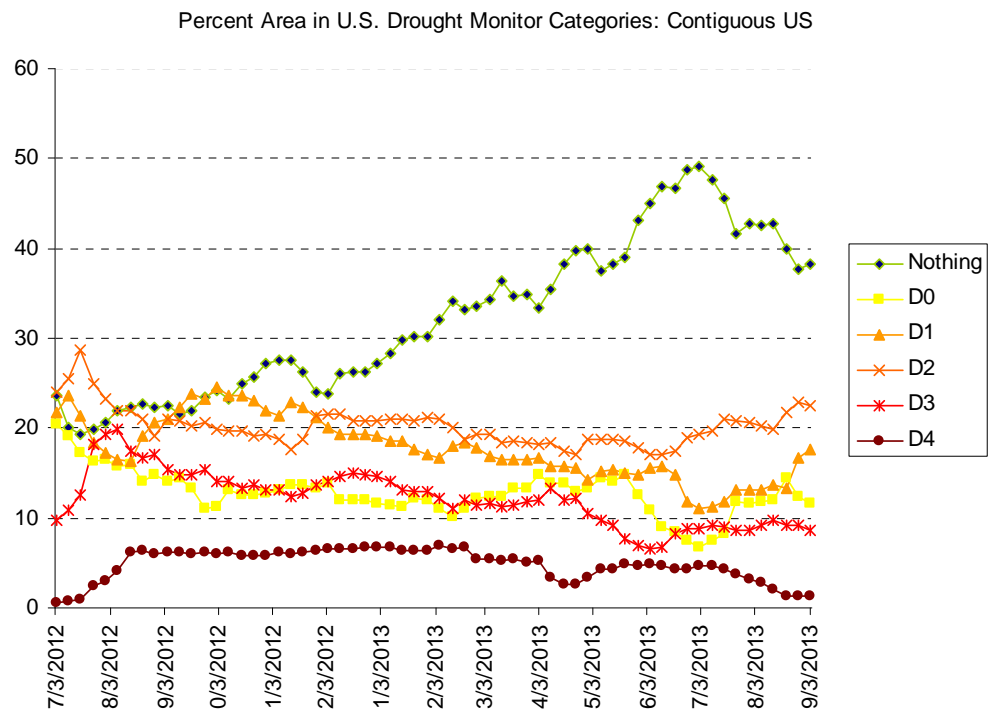
Impact of US Drought on Zoetis's Revenues

The 2012 drought in the US is considered the worst in many years. It not only reduced grazing pastures, but also destroyed or damaged significant portions of the major field crops in the Midwest, particularly field corn and soybeans. The decrease in harvested corn (a key ingredient in animal feed) resulted in higher corn prices, which impacted the profitability of livestock producers of cattle, pork, and poultry. Higher animal feed prices and reduced availability of grazing pastures contributed to reductions in herd or flock sizes that also resulted in reduced spending on animal health products.¹

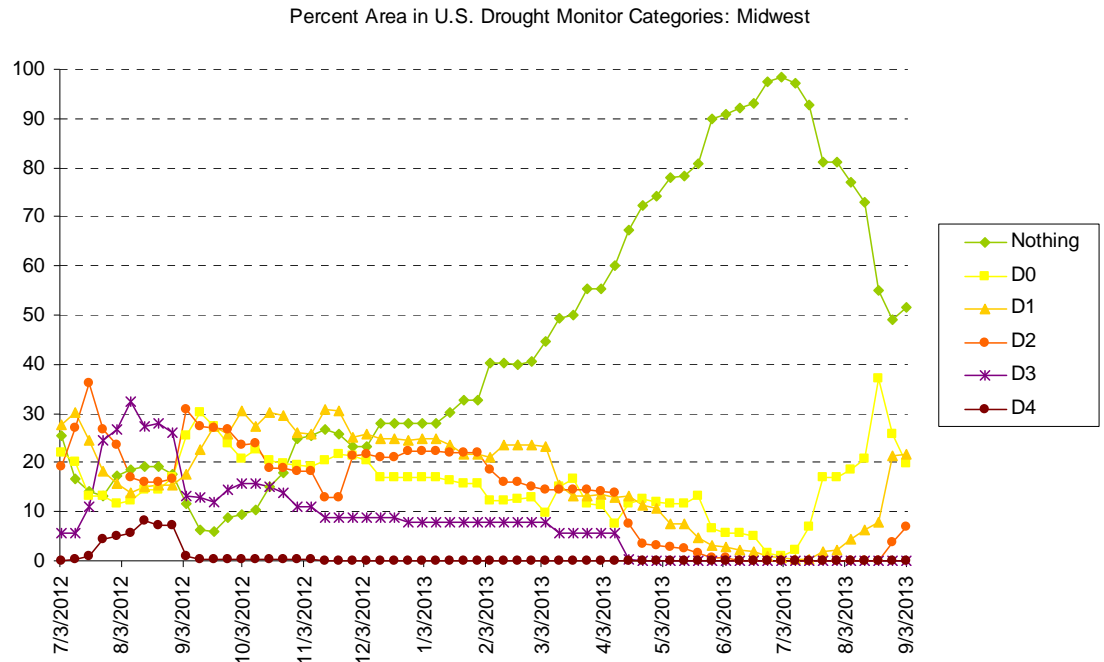
US livestock accounts for roughly 18% of Zoetis's revenues. Notably, the 2012 drought rapidly increased in severity in early July, during a critical time of crop development for corn, and persisted into August. Therefore, the negative impact for Zoetis started in 3Q12 as livestock revenues declined 4% y/y.

However, as illustrated in Exhibits 1 and 2, there are encouraging signs suggesting that the drought is easing and as a result animal feed prices have declined significantly. This should result in larger herd sizes and more animals moving from grazing pastures, where they feed primarily on grass, to smaller and more crowded feeding lots where they feed on corn and other grains that are often combined with pharmaceutical additives such as antibiotics. Therefore, lower corn prices should result in increased use of animal health products as farmers take advantage to increase the amount of time on feed.

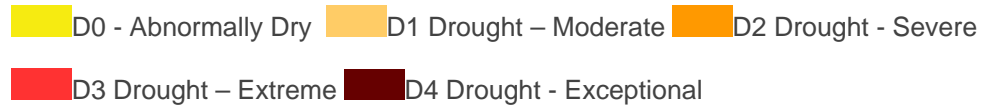
Exhibit 1: 2012 US Drought Appears to Be Easing



¹ Based on USDA reports and Zoetis management commentary.



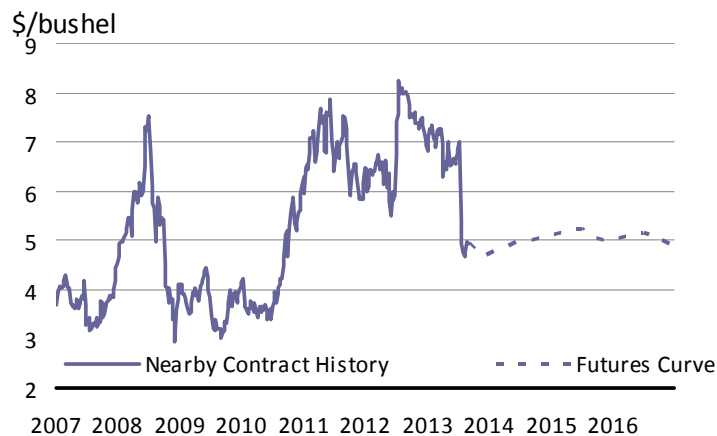
Drought Severity:



Source: United States Drought Monitor, BMO Capital Markets Pharmaceuticals Research

Exhibit 2. Corn Prices Are Now Below 2012 Levels, a Positive Driver for Livestock Industry and Zoetis

Corn Futures Prices



Source: CME Group

Exhibit 3. Following 2Q13 Earnings, Zoetis Confirmed its 2013 Guidance Partly Based on Confidence in Improving Livestock Business. We Remain on the Lower End of Guidance Range but Now Have More Confidence in Guidance.

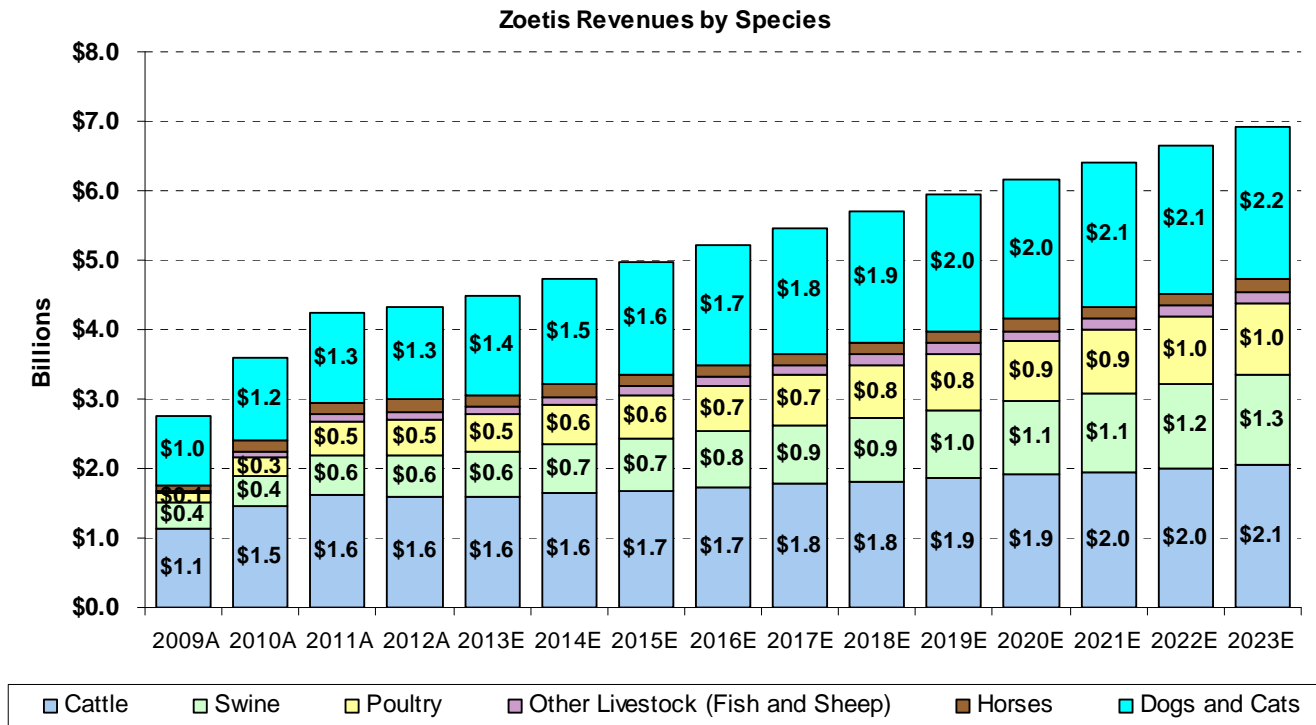
2013 Guidance & Date Provided	Apr. 30, 2013 (after 1Q 2013)	Aug. 06, 2013 (after 2Q 2013)	BMO	Street	Comments
Revenue	\$4,425 mn to \$4,525 mn	\$4,425 mn to \$4,525 mn	\$4,459 mn	\$4,501 mn	We're in the lower half.
Cost of Sales as % of Revenues	35.0% to 36.0%	35.0% to 36.0%	35.6%	35.5%	We're in-line; company is actively looking for manufacturing efficiencies.
SG&A Expenses	\$1,385 mn to \$1,435 mn	\$1,385 mn to \$1,435 mn	\$1,383 mn		Will increase throughout 2013, but at a slower rate than revenues. We're on the low end.
R&D Expenses	\$385 mn to \$415 mn	\$385 mn to \$415 mn	\$391 mn		We're in the lower half. Will increase slightly but at a slower rate than revenues.
Interest Expense	~\$115 mn	~\$115 mn	\$112 mn		We're in-line
Other (Income)/ Deductions	~(\$20 mn)	~(\$20 mn)	(\$13 mn)		
Effective Tax Rate	~29.5%	~29.5%	29.1%	29.6%	We're slightly below.
Adjusted Net Income	\$680 mn to \$710 mn	\$680 mn to \$710 mn	\$685 mn	\$697 mn	We're on the lower end.
Adjusted Diluted EPS	\$1.36 to \$1.42	\$1.36 to \$1.42	\$1.37	\$1.40	We're on the lower end of guidance, but believe it is achievable.

Source: Zoetis Reports, Thomson One, BMO Capital Markets Pharmaceuticals Research

Exhibit 4. Although, We Are More Cautious Than the Street on the Top-Line, the Difference Does Not Change Our Investment Thesis

Non-GAAP Measures	FY2013E		FY2014E		FY2015E		FY2016E	
	Street	BMO	Street	BMO	Street	BMO	Street	BMO
Revenue	\$4,501	\$4,459	\$4,755	\$4,661	\$5,017	\$4,932	\$5,302	\$5,165
Gross Margin	64.5%	64.4%	65.2%	64.7%	65.5%	65.0%	65.7%	65.3%
Operating Profit	\$1,096	\$1,097	\$1,216	\$1,211	NA	\$1,350	NA	\$1,482
Operating Margin	24%	25%	26%	26%	#VALUE!	27%	#VALUE!	29%
Pre-tax Profit	991	968	1,143	1,092	1,284	1,231	1,433	1,367
Effective Tax Rate	30%	29%	29%	29%	29%	29%	29%	29%
Net Income	\$697	\$685	\$808	\$771	\$910	\$870	\$1,019	\$967
Net Margin	15%	15%	17%	17%	18%	18%	19%	19%
EPS	\$1.40	\$1.37	\$1.61	\$1.54	\$1.81	\$1.74	\$2.02	\$1.94
Free Cash Flow per Share	\$1.46	\$1.34	\$1.55	\$1.46	\$1.59	\$1.63	\$1.90	\$1.93
Dividend per share	\$0.26	\$0.26	\$0.30	\$0.33	\$0.34	\$0.39	\$0.43	\$0.47
Dividend Payout Ratio	19%	19%	19%	21%	19%	22%	21%	24%

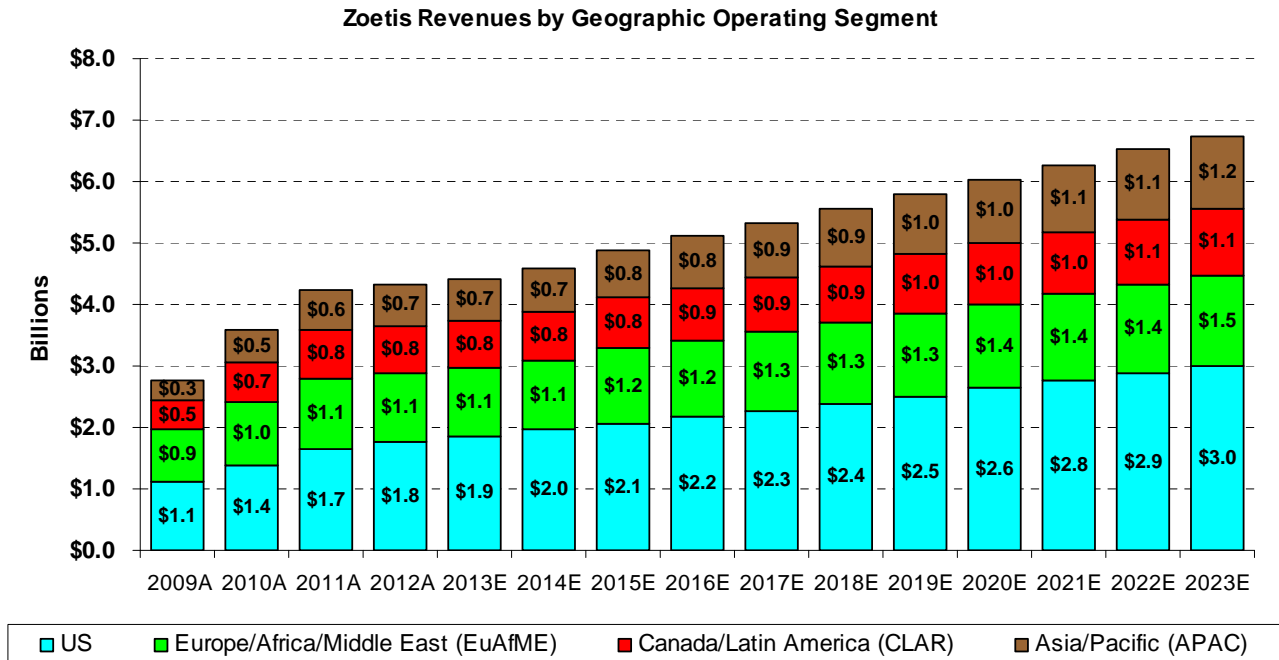
Source: Zoetis, Thomson One, BMO Capital Markets Pharmaceuticals Research

Exhibit 5. Our Zoetis Revenue Forecast by Species: 10-year CAGR of 4.4%; in Line With 2Q13 Operational Growth

Source: Zoetis, BMO Capital Markets.

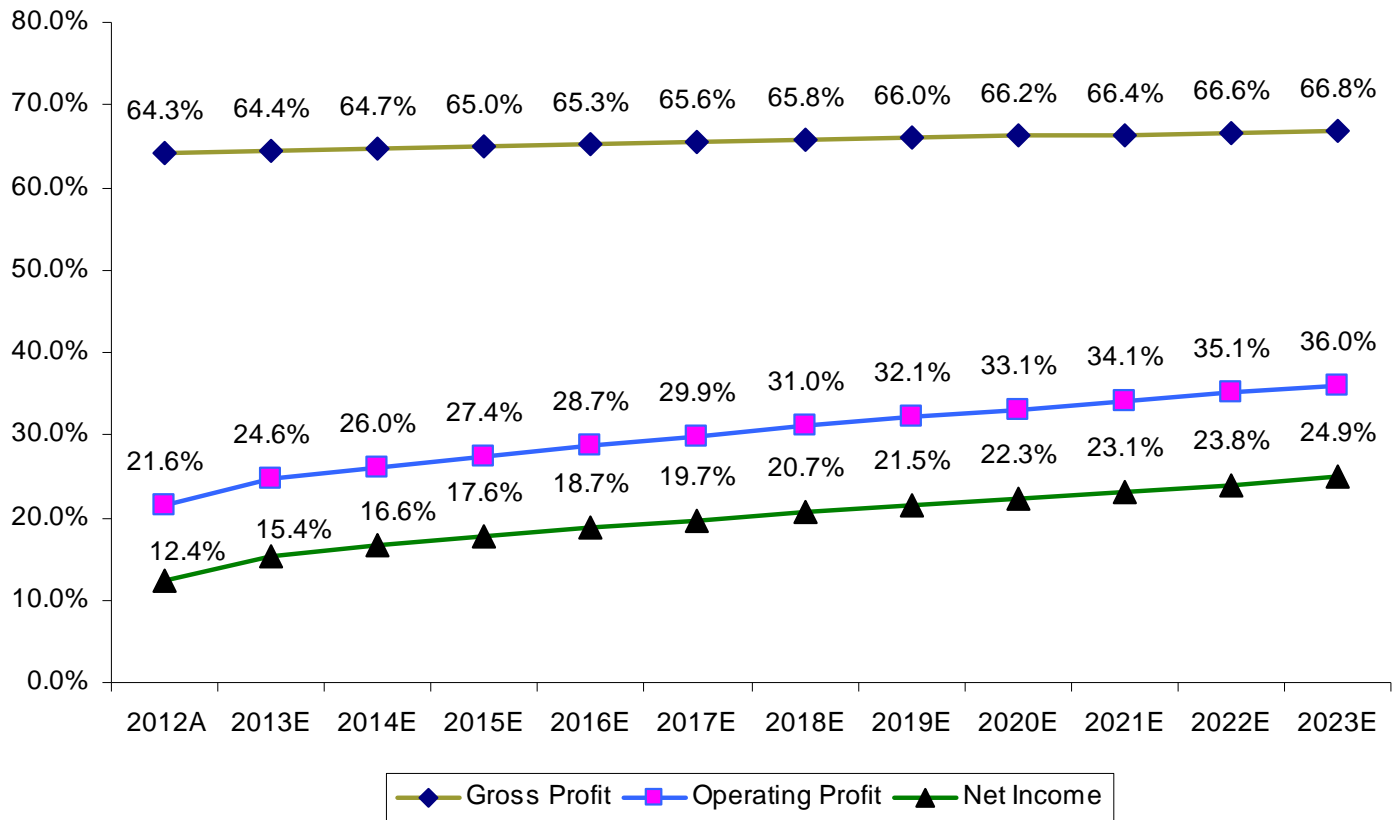
Exhibit 6. Our Zoetis Revenue Forecast by Geo-Segment: 10-year CAGR of 4.3%; in Line With 2Q13 Operational Growth

(NOTE: Our model uses the average of our revenue forecast by species and geographic segment)



Source: Zoetis, BMO Capital Markets.

Exhibit 7. We Expect Zoetis's Margins to Improve Over Time, Driven by Product Mix and Improved Operational Efficiency as SG&A and R&D Grow at a Slower Rate Than Revenues



Source: Zoetis, BMO Capital Markets.

Our Zoetis Valuation

We value ZTS shares using a DCF model and support it by using a P/E multiple. In our DCF, we assume a 2.5% terminal growth rate because of the sustainability of the business, and as such, our terminal value accounts for nearly 60% of the firm value. On a relative basis, applying a 22-23x P/E multiple, which is in the top range of that seen with other roughly similar companies, to our new 2014-2016E non-GAAP EPS estimates produces an average valuation of \$36, in line with our DCF valuation.

Exhibit 8. Our \$36/Share Valuation of ZTS Shares Is Based on DCF and P/E Multiple

FCFF Valuation, \$MM		2013E	2014E	2015E	2016E	2017E	2018E	2019E	2020E	2021E	2022E	2023E	>2023E
Cash flow from operations		548	860	940	1,083	1,164	1,286	1,395	1,501	1,609	1,718	1,894	1,941
Y/Y Growth			5%	9%	15%	7%	10%	8%	8%	7%	7%	10%	2.5%
CAPEX		(69)	(127)	(125)	(122)	(127)	(130)	(132)	(130)	(131)	(136)	(131)	(134)
Interest Expense (1-t)		41	83	83	80	80	70	70	70	70	70	41	41
Free Cash Flow to the Firm (FCFF)		521	815	898	1,042	1,116	1,226	1,332	1,440	1,547	1,651	1,803	1,848
Discount Period		0.3	1.3	2.3	3.3	4.3	5.3	6.3	7.3	8.3	9.3	10.3	11.3
Discount Rate 8.3%													
Discounted FCFF		510	738	750	804	796	807	809	808	802	790	796	
PV of FCFE (2013-2023) Terminal Value at 2023 PV of Terminal Value Cash & Equivalents Total Debt Funding obligation for pension & post retirement benefit plans Total Equity Value Minority Interest Total Zoetis Stockholders' Equity Value Diluted shares, MM Equity value per current PFE share	Total, \$MM	Terminal growth rate: 2.5% Accounts for nearly 60% of firm value given sustainability of business. Current outstanding debt As of 2Q13. Source: Zoetis Form 10-Q As of Q2'13											
	8,410												
	31,860												
	12,992												
	369												
	3,652												
	45												
	18,074												
	(23)												
	18,051												
500													
\$36													

PE Multiple Valuation Using Non-GAAP EPS

		2012A	2013E	2014E	2015E	2016E	2013-16 EPS CAGR
EPS		\$1.08	\$1.37	\$1.54	\$1.74	\$1.94	
PEx	20	\$22	\$27	\$31	\$32	\$33	12.2%
	21	\$23	\$29	\$32	\$34	\$35	
	22	\$24	\$30	\$34	\$35	\$36	
	23	\$25	\$31	\$35	\$37	\$38	
	24	\$26	\$33	\$37	\$39	\$40	

Discount Period 0 1 2
Discount rate 8.3%

Average \$36

Sources: Pfizer Reports, Zoetis, BMO Capital Markets Pharmaceuticals Research

Zoetis Non-GAAP Income Statement: Our Quarterly Estimates

	2012A				2013E				2014E			
Non-GAAP Income Statement, \$MM	Q1 2012	Q2 2012	Q3 2012	Q4 2012	Q1 2013	Q2 2013	Q3 2013	Q4 2013	Q1 2014	Q2 2014	Q3 2014	Q4 2014
Revenues	1,047	1,094	1,019	1,176	1,090	1,114	1,051	1,204	1,120	1,154	1,108	1,279
Cost of Sales	388	382	352	427	398	400	359	431	406	411	375	454
Gross Profit	659	712	667	749	692	714	692	773	714	743	733	825
Selling, Informational and Administrative Expenses	331	351	330	440	322	339	331	391	323	342	339	400
R&D Expenses	93	91	94	121	90	91	95	115	91	93	97	119
Operating Profit	235	270	243	188	280	284	267	266	300	308	297	306
Amortization of Intangible Assets	4	3	4	4	4	3	11	12	7	7	7	7
EBIT	231	267	239	184	276	281	256	255	293	302	290	299
Other (Income) / Deductions -- Net	2	2	(4)	10	24	29	23	23	23	23	23	23
Income From Cont. Operations Before Provision for Taxes	229	265	243	174	252	252	233	231	270	279	267	276
(Benefit) / Provision for Taxes on Income	76	90	89	117	73	74	68	67	78	81	77	80
Net income/(loss) before allocation to non-controlling interests	153	175	154	57	179	178	165	164	192	198	190	196
Less: Income / (Loss) Attributable to Non-Controlling Interests	1	(1)		0	0	0	1	1	1	1	1	1
Net Income/ (loss) Attributable to Zoetis	152	176	154	57	179	178	164	163	191	197	189	195
Earnings Per Share - Basic	\$0.30	\$0.35	\$0.31	\$0.11	\$0.36	\$0.36	\$0.33	\$0.33	\$0.38	\$0.39	\$0.38	\$0.39
Earnings Per Share - Diluted	\$0.30	\$0.35	\$0.31	\$0.11	\$0.36	\$0.36	\$0.33	\$0.33	\$0.38	\$0.39	\$0.38	\$0.39
Weighted-Average Shares - Basic	500	500	500	500	500	500	500	500	500	500	500	500
Weighted-Average Shares - Diluted	500	500	500	500	500	500	500	500	500	500	500	500
Dividend per Share	\$0.00	\$0.00	\$0.00	\$0.00	\$0.07	\$0.07	\$0.07	\$0.07	\$0.08	\$0.08	\$0.08	\$0.08

Zoetis Non-GAAP Income Statement: Our Annual Estimates

Non-GAAP Income Statement, \$MM	2012A	2013E	2014E	2015E	2016E	2017E	2018E	2019E	2020E	2021E	2022E	2023E
Revenues	\$4,336	\$4,459	\$4,661	\$4,932	\$5,165	\$5,397	\$5,628	\$5,867	\$6,106	\$6,343	\$6,588	\$6,834
Cost of Sales	1,549	1,588	1,646	1,727	1,793	1,857	1,925	1,995	2,064	2,132	2,201	2,269
Gross Profit	2,787	2,871	3,015	3,205	3,373	3,540	3,703	3,872	4,041	4,211	4,387	4,564
SG&A	1,452	1,383	1,404	1,444	1,469	1,495	1,516	1,538	1,559	1,578	1,598	1,616
R&D	399	391	400	412	422	431	440	450	459	468	477	486
Operating Profit	936	1,097	1,211	1,350	1,482	1,614	1,746	1,884	2,024	2,165	2,312	2,462
Amortization of Intangible Assets	15	29	26	26	26	26	26	26	26	26	26	26
Restructuring Charges & Certain Acquisition-Related Costs	0	0	0	0	0	0	0	0	0	0	0	0
Other (Income) / Deductions -- Net	10	99	93	93	88	88	75	74	74	74	74	34
Income From Cont. Operations Before Provision for Taxes	911	968	1,092	1,231	1,367	1,500	1,645	1,784	1,924	2,065	2,212	2,403
(Benefit) / Provision for Taxes on Income	372	282	317	357	397	435	477	517	558	599	642	697
Effective Tax Rate	40.8%	29.1%	29.0%	29.0%	29.0%	29.0%	29.0%	29.0%	29.0%	29.0%	29.0%	29.0%
Net income/(loss) before allocation to non-controlling interests	539	687	775	874	971	1,065	1,168	1,267	1,366	1,466	1,571	1,706
Gain / (Loss) Attributable to Non-Controlling Interests	0	2	4	4	4	4	4	4	4	4	4	4
Net Income (Loss) Attributable to Zoetis	\$539	\$685	\$771	\$870	\$967	\$1,061	\$1,164	\$1,263	\$1,362	\$1,462	\$1,567	\$1,702
Earnings Per Share - Basic	\$1.08	\$1.37	\$1.54	\$1.74	\$1.94	\$2.14	\$2.35	\$2.56	\$2.77	\$2.99	\$3.22	\$3.52
Earnings Per Share - Diluted	\$1.08	\$1.37	\$1.54	\$1.74	\$1.94	\$2.13	\$2.34	\$2.55	\$2.76	\$2.97	\$3.21	\$3.51
Weighted-Average Shares - Basic	500	500	500	499	498	497	495	494	491	488	486	483
Weighted-Average Shares - Diluted	500	500	500	500	500	499	498	496	494	492	489	486
Cash Dividend Paid per Share		\$0.26	\$0.33	\$0.39	\$0.47	\$0.54	\$0.62	\$0.68	\$0.68	\$0.71	\$0.75	\$0.75

	2012A	2013E	2014E	2015E	2016E	2017E	2018E	2019E	2020E	2021E	2022E	2023E
Growth Rates												
Revenue	2%	3%	5%	6%	5%	4%	4%	4%	4%	4%	4%	4%
Gross Profit	5%	3%	5%	6%	5%	5%	5%	5%	4%	4%	4%	4%
Operating Profit	17%	17%	10%	11%	10%	9%	8%	8%	7%	7%	7%	6%
Net Income	7%	27%	13%	13%	11%	10%	10%	8%	8%	7%	7%	9%
EPS	7%	27%	13%	13%	11%	10%	10%	9%	8%	8%	8%	9%
Dividend per share			25%	20%	20%	15%	15%	10%	0%	5%	5%	0%
Margins												
Gross Profit	64.3%	64.4%	64.7%	65.0%	65.3%	65.6%	65.8%	66.0%	66.2%	66.4%	66.6%	66.8%
Operating Profit	22%	25%	26%	27%	29%	30%	31%	32%	33%	34%	35%	36%
Net Income	12.4%	15.4%	16.6%	17.6%	18.7%	19.7%	20.7%	21.5%	22.3%	23.1%	23.8%	24.9%
Return Analysis												
Payout Ratio		19%	21%	22%	24%	25%	26%	27%	25%	24%	23%	21%

Sources: Pfizer Reports, Zoetis Form S-1, BMO Capital Markets Pharmaceuticals Research

Zoetis Income Statement: GAAP or Fully Reported Estimates

GAAP Income Statement, \$MM	2012A	2013E	2014E	2015E	2016E	2017E	2018E	2019E	2020E	2021E	2022E	2023E
Revenues	\$4,336	\$4,459	\$4,661	\$4,932	\$5,165	\$5,397	\$5,628	\$5,867	\$6,106	\$6,343	\$6,588	\$6,834
Cost of Sales	1,563	1,610	1,650	1,731	1,797	1,861	1,929	1,999	2,068	2,136	2,205	2,273
Gross Profit	2,773	2,849	3,011	3,201	3,369	3,536	3,699	3,868	4,037	4,207	4,383	4,560
SG&A	1,470	1,513	1,420	1,456	1,481	1,507	1,528	1,550	1,571	1,590	1,610	1,628
R&D Expenses	409	405	416	424	434	443	452	462	471	480	489	498
Amortization of Intangible Assets	64	63	66	66	66	66	66	66	66	66	66	66
Restructuring Charges & Certain Acquisition-Related Costs	135	29	32	24	24	24	24	24	24	24	24	24
Other (Income) / Deductions -- Net	(15)	95	93	93	88	88	75	74	74	74	74	34
Income Before Provision for Taxes	710	743	984	1,139	1,275	1,408	1,553	1,692	1,832	1,973	2,120	2,311
(Benefit) / Provision for Taxes on Income	274	217	285	330	370	408	450	491	531	572	615	670
Net income/(loss) before allocation to non-controlling interests	436	527	699	809	905	1,000	1,103	1,202	1,300	1,401	1,505	1,641
Gain / (Loss) Attributable to Non-Controlling Interests	0	2	4	4	4	4	4	4	4	4	4	4
Net Income (Loss) Attributable to Zoetis	\$436	\$525	\$695	\$805	\$901	\$996	\$1,099	\$1,198	\$1,296	\$1,397	\$1,501	\$1,637
Earnings Per Share - Basic	\$0.87	\$1.05	\$1.39	\$1.61	\$1.81	\$2.00	\$2.22	\$2.43	\$2.64	\$2.86	\$3.09	\$3.39
Earnings Per Share - Diluted	\$0.87	\$1.05	\$1.39	\$1.61	\$1.80	\$2.00	\$2.21	\$2.41	\$2.62	\$2.84	\$3.07	\$3.37
Weighted-Average Shares - Basic	500	500	500	499	498	497	495	494	491	488	486	483
Weighted-Average Shares - Diluted	500	500	500	500	500	499	498	496	494	492	489	486
Cash Dividend per Share	\$0.00	\$0.26	\$0.33	\$0.39	\$0.47	\$0.54	\$0.62	\$0.68	\$0.68	\$0.71	\$0.75	\$0.75

Note: Includes revenues and expenses from acquisitions from the acquisition date

Sources: Pfizer Reports, Zoetis Form S-1, BMO Capital Markets Pharmaceuticals Research

Zoetis Balance Sheet

Zoetis Balance Sheet, \$MM	2012A	2013E	2014E	2015E	2016E	2017E	2018E	2019E	2020E	2021E	2022E	2023E
Assets												
Cash and cash equivalents	317	783	1,330	1,920	2,182	2,812	2,728	3,385	4,057	4,762	5,443	4,861
Accounts receivable, less allowance for doubtful accounts	900	785	807	877	917	958	998	1,040	1,082	1,124	1,167	1,210
Inventories	1,345	1,179	1,237	1,263	1,283	1,339	1,388	1,426	1,474	1,522	1,571	1,586
Current deferred tax assets	101	92	92	92	92	92	92	92	92	92	92	92
Receivable from Pfizer Inc		212	212	212	212	212	212	212	212	212	212	212
Other current assets	201	207	210	210	210	210	210	210	210	210	210	210
Total current assets	2,864	3,258	3,887	4,574	4,897	5,623	5,628	6,365	7,128	7,922	8,696	8,172
Property, plant and equipment, less accumulated depreciation	1,241	1,259	1,258	1,247	1,234	1,220	1,203	1,180	1,149	1,112	1,074	1,024
Identifiable intangible assets, less accumulated amortization	868	801	735	669	603	537	471	405	339	273	207	141
Goodwill	985	982	982	982	982	982	982	982	982	982	982	982
Non-current deferred tax assets	216	54	54	54	54	54	54	54	54	54	54	54
Other noncurrent assets	88	68	66	65	65	65	65	65	65	65	65	65
Total Assets	6,262	6,423	6,982	7,591	7,835	8,482	8,403	9,052	9,718	10,409	11,078	10,438
Liabilities and Equity												
Current portion of allocated long-term debt	73	0	0	0	0	0	0	0	0	0	0	0
Current portion of long-term debt	0	12	0	400	0	750	0	0	0	0	1,350	0
Accounts payable	319	235	238	206	187	183	184	178	184	190	196	202
Income taxes payable	30	53	58	58	58	58	58	58	58	58	58	58
Accrued compensation and related items	194	158	158	161	164	166	169	171	173	175	177	179
Payable to Pfizer Inc.	0	297	297	297	297	297	297	297	297	297	297	297
Other current liabilities	507	469	463	462	462	462	462	462	462	462	462	462
Total current liabilities	1,123	1,224	1,214	1,585	1,168	1,917	1,169	1,166	1,175	1,183	2,541	1,199
Allocated long-term debt	509	0	0	0	0	0	0	0	0	0	0	0
Long-term debt	0	3,640	3,640	3,240	3,240	2,490	2,490	2,490	2,490	2,490	1,140	1,140
Noncurrent deferred tax liabilities	323	321	319	319	319	319	319	319	319	319	319	319
Other taxes payable	159	77	67	66	66	66	66	66	66	66	66	66
Other noncurrent liabilities	107	118	119	119	119	119	119	119	119	119	119	119
Total Liabilities	2,221	5,381	5,359	5,329	4,912	4,910	4,163	4,160	4,168	4,176	4,185	2,843
Commitments and Contingencies												
Total Equity	4,041	1,042	1,623	2,262	2,923	3,572	4,240	4,892	5,549	6,232	6,893	7,595
Total liabilities and equity	6,262	6,423	6,982	7,591	7,835	8,482	8,403	9,052	9,718	10,409	11,078	10,438

Sources: Pfizer Reports, Zoetis Form S-1, BMO Capital Markets Pharmaceuticals Research

Zoetis Statement of Cash Flows

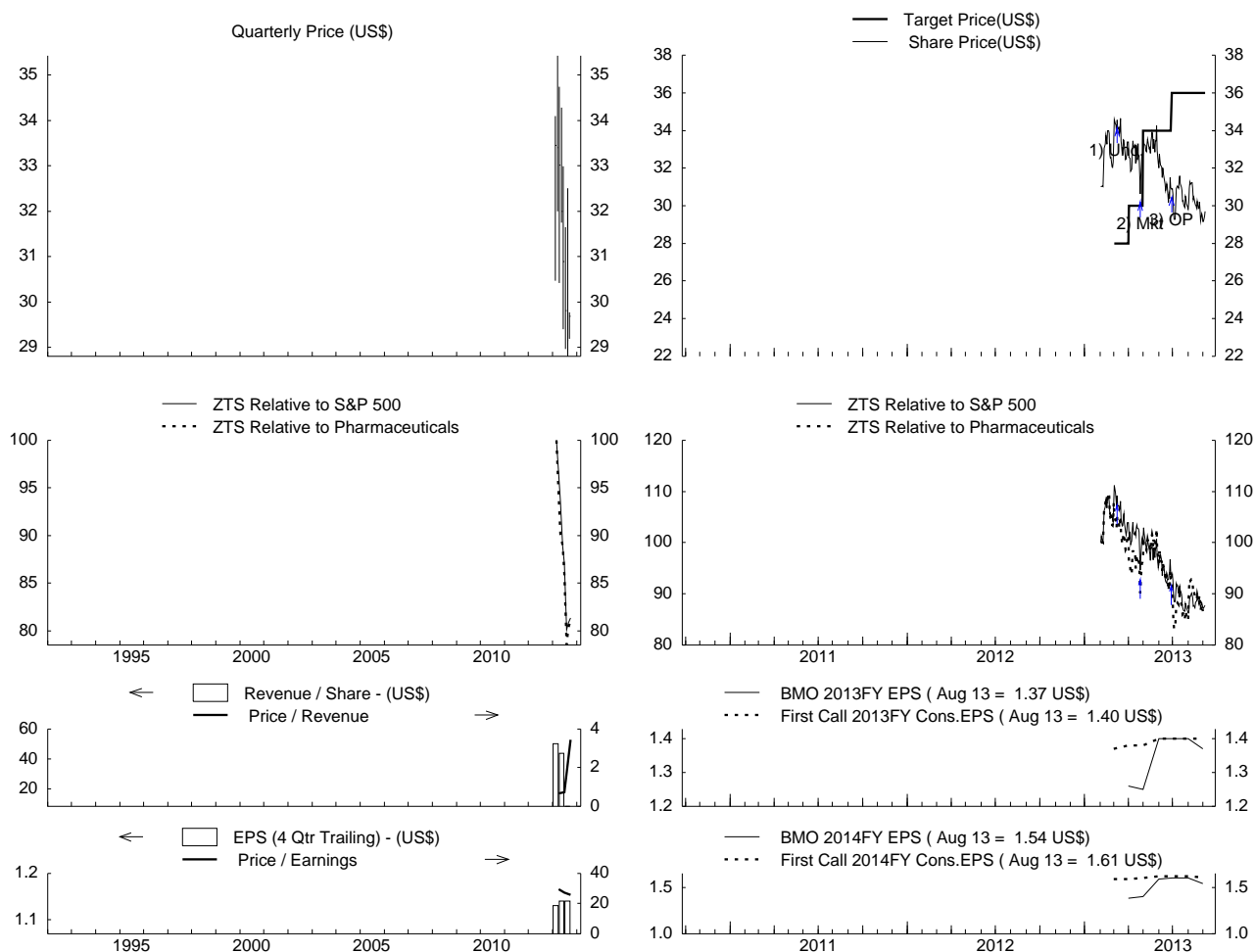
Zoetis Statement of Cash Flows, \$MM	2012A	2013E	2014E	2015E	2016E	2017E	2018E	2019E	2020E	2021E	2022E	2023E
Operating activities												
GAAP Net income/(loss) before allocation to non-controlling interests	436	527	699	809	905	1,000	1,103	1,202	1,300	1,401	1,505	1,641
Adjustments:												
Depreciation and amortization expense	200	197	195	202	200	207	214	220	227	234	241	248
Share-based compensation expense	28	56	56	56	56	56	56	56	56	56	56	56
Asset write-offs and impairments	10	3	0	0	0	0	0	0	0	0	0	0
Net gains on sales of assets	0	0	0	0	0	0	0	0	0	0	0	0
Deferred taxes	(74)	(6)	(2)	(0)	(0)	(0)	(0)	0	0	0	0	0
Other non-cash adjustments	3	(1)	0	0	0	0	0	0	0	0	0	0
Other changes in assets and liabilities, net of acquisitions and divestitures:	(149)	41	(88)	(126)	(78)	(98)	(86)	(83)	(83)	(81)	(84)	(50)
Net cash provided by operating activities	454	817	860	940	1,083	1,164	1,286	1,395	1,501	1,609	1,718	1,894
Investing Activities												
Purchases of property, plant and equipment	(126)	(149)	(127)	(125)	(122)	(127)	(130)	(132)	(130)	(131)	(136)	(131)
Net proceeds from sales of assets	3	6	0	0	0	0	0	0	0	0	0	0
Acquisitions, net of cash acquired	0	0	0	0	0	0	0	0	0	0	0	0
Other investing activities	(12)	0	0	0	0	0	0	0	0	0	0	0
Net cash used in investing activities	(135)	(143)	(127)	(125)	(122)	(127)	(130)	(132)	(130)	(131)	(136)	(131)
Financing activities												
Debt - Net issuance / payment	0	2,636	(12)	0	(400)	0	(750)	0	0	0	0	(1,350)
Cash dividends paid	(63)	(98)	(162)	(195)	(233)	(267)	(307)	(336)	(335)	(349)	(365)	(363)
Purchase of subsidiary shares from noncontrolling interests	0	0	0	0	0	0	0	0	0	0	0	0
Share repurchases	0	0	(11)	(31)	(67)	(140)	(183)	(270)	(364)	(425)	(535)	(632)
Net financing activities with Pfizer	(15)	(2,743)	0	0	0	0	0	0	0	0	0	0
Net cash provided by/(used in) financing activities	(78)	(205)	(186)	(225)	(700)	(407)	(1,240)	(606)	(698)	(774)	(900)	(2,344)
Effect of exchange-rate changes on cash and cash equivalents	(3)	(3)	0	0	0	0	0	0	0	0	0	0
Net increase/(decrease) in cash and cash equivalents	238	466	547	590	262	630	(84)	657	672	704	681	(582)
Cash and cash equivalents, as of beginning of year	79	317	783	1,330	1,920	2,182	2,812	2,728	3,385	4,057	4,762	5,443
Cash and cash equivalents, as of end of year	317	783	1,330	1,920	2,182	2,812	2,728	3,385	4,057	4,762	5,443	4,861

Sources: Pfizer Reports, Zoetis Form S-1, BMO Capital Markets Pharmaceuticals Research

Other companies mentioned (priced as of the close on September 5, 2013):

Pfizer (PFE, \$28.27, Outperform)

Zoetis Inc. (ZTS)



FYE (Dec.)	EPS US\$	P/E Hi - Lo	DPS US\$	Yield% Hi - Lo	Payout %	BV US\$	P/B Hi - Lo	ROE %	ZTS - Rating as of 1-Feb-13 = NR		
Range*:		na na		NC			>15 >15		Date	Rating Change	Share Price
Current*	1.14	25.6	0.26	0.9	23	1.4	20.5	>50	1 7-Mar-13	NR to Und.	\$34.56
									2 24-Apr-13	Und.to Mkt	\$30.62
									3 27-Jun-13	Mkt to OP	\$30.87

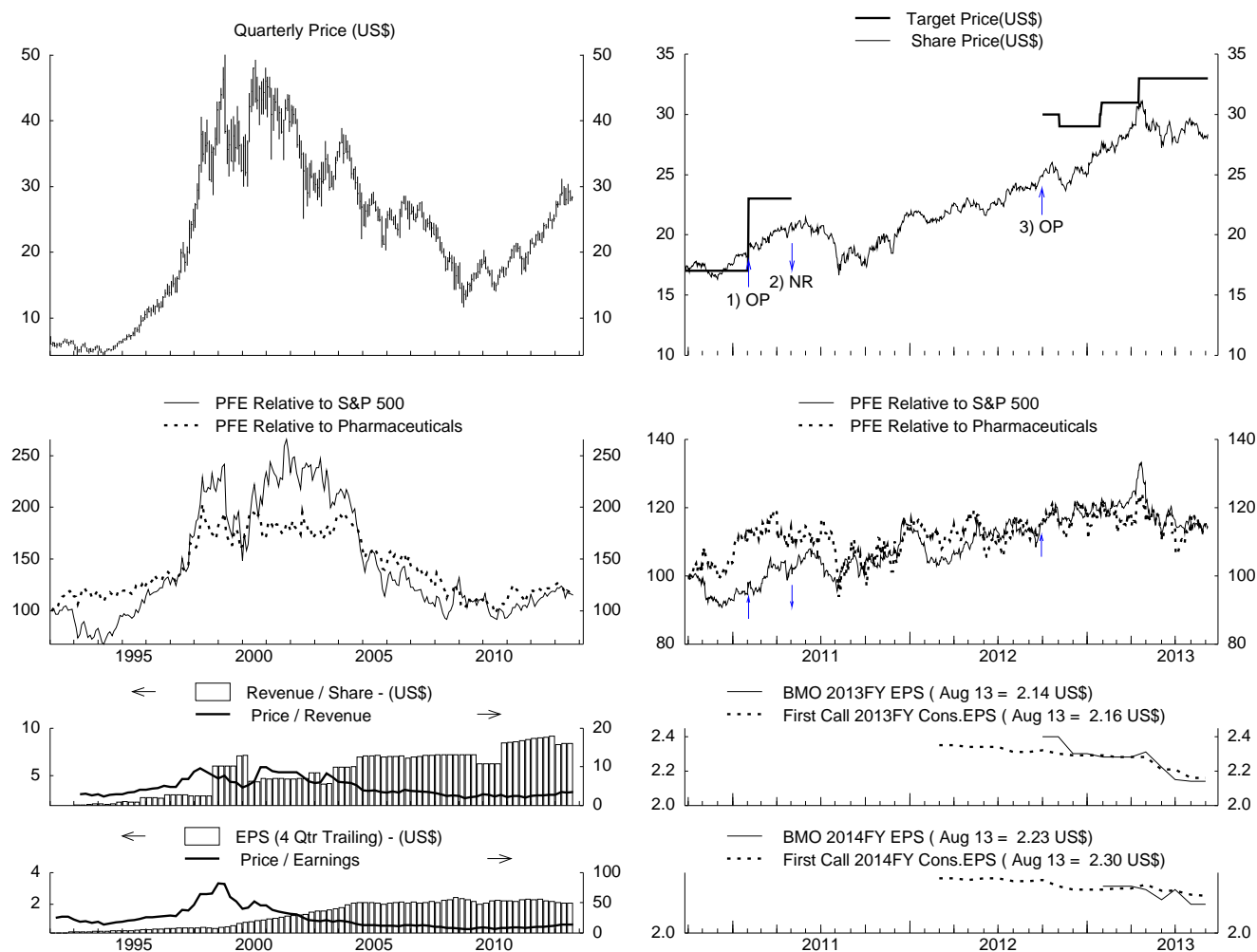
* Current EPS is the 4 Quarter Trailing to Q2/2013.

* Valuation metrics are based on high and low for the fiscal year.

* Range indicates the valuation range for the period presented above.

Last Price (September 4, 2013): \$29.69
Sources: IHS Global Insight, Thomson Reuters, BMO Capital Markets.

Pfizer Inc. (PFE)



FYE (Dec.)	EPS US\$	P/E Hi - Lo	DPS US\$	Yield% Hi - Lo	Payout %	BV US\$	P/B Hi - Lo	ROE %
1992	0.27	26.9 20.1	0.12	2.3 1.7	46	1.2	6.0 4.5	
1993	0.31	21.5 14.1	0.14	3.2 2.1	45	1.0	6.6 4.4	28
1994	0.35	18.9 12.6	0.16	3.5 2.4	45	1.1	5.8 3.9	33
1995	0.41	27.2 14.9	0.09	1.4 0.8	21	1.4	7.7 4.3	32
1996	0.50	30.4 19.4	0.20	2.1 1.3	40	1.8	8.5 5.4	31
1997	0.53	50.3 25.0	0.23	1.7 0.9	43	2.0	13.1 6.5	28
1998	0.51	84.3 45.5	0.29	1.3 0.7	58	2.3	>15 10.2	24
1999	0.82	61.0 38.5	0.36	1.1 0.7	44	2.3	>15 13.7	36
2000	1.02	48.3 29.4	0.44	1.5 0.9	43	2.6	>15 11.8	42
2001	1.27	37.8 26.8	0.52	1.5 1.1	41	2.9	>15 11.7	47
2002	1.53	28.7 16.4	0.60	2.4 1.4	39	3.2	13.6 7.8	50
2003	1.75	21.1 15.4	0.68	2.5 1.8	39	8.5	4.3 3.2	30
2004	2.12	18.3 10.4	0.76	3.5 2.0	36	9.1	4.3 2.4	24
2005	2.02	14.5 10.0	0.96	4.7 3.3	48	8.9	3.3 2.3	22
2006	2.08	13.8 9.7	1.16	5.7 4.1	56	10.0	2.9 2.0	22
2007	2.20	12.7 10.1	1.28	5.8 4.6	58	9.6	2.9 2.3	22
2008	2.43	10.1 5.9	1.28	9.0 5.2	53	8.5	2.9 1.7	27
2009	2.02	9.4 5.8	0.72	6.2 3.8	36	11.2	1.7 1.0	21
2010	2.22	9.2 6.3	0.80	5.7 3.9	36	11.0	1.9 1.3	20
2011	2.31	9.5 7.1	0.88	5.4 4.0	38	10.8	2.0 1.5	21
2012	2.19	11.9 9.0	0.96	4.9 3.7	44	11.1	2.4 1.8	20
Range*		84.3 5.8		9.0 0.7			>15 1.0	
Current*	2.07	13.6	0.96	3.4	46	11.6	2.4	18
Growth(%):								
5 Year:	-1.7		-5.6			3.8		
10 Year:	2.7		4.8			13.6		
20 Year:	10.3		10.1			12.5		

PFE - Rating as of 24-Sep-10 = Mkt

Date	Rating Change	Share Price
1 2-Feb-11	Mkt to OP	\$18.96
2 3-May-11	OP to NR	\$20.44
3 27-Sep-12	NR to OP	\$24.96

* Current EPS is the 4 Quarter Trailing to Q2/2013.

* Valuation metrics are based on high and low for the fiscal year.

* Range indicates the valuation range for the period presented above.

Last Price (September 4, 2013): \$28.37

Sources: IHS Global Insight, Thomson Reuters, BMO Capital Markets.

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Company Specific Disclosure for ZTS

Methodology and Risks to Our Price Target/Valuation

Methodology: DCF and P/E Multiple

Risks: Demand for animal health products could fluctuate and there are relatively low barriers to entry for competitors.

Company Specific Disclosures for PFE

9 - BMO Capital Markets makes a market in this security.

Methodology and Risks to Our Price Target/Valuation

Methodology: DCF: Free Cash Flow To Equity.

Risks: Uncertainty of Phase 3 Pipeline.

Distribution of Ratings (June 30, 2013)

Rating Category	BMO Rating	BMOCM US Universe*	BMOCM US IB Clients**	BMOCM US IB Clients***	BMOCM Universe****	BMOCM IB Clients*****	Starmine Universe
Buy	Outperform	37.9%	17.6%	52.7%	39.6%	51.0%	53.2%
Hold	Market Perform	56.8%	10.2%	45.9%	53.9%	45.5%	41.1%
Sell	Underperform	5.3%	3.2%	1.4%	6.5%	3.5%	5.6%

* Reflects rating distribution of all companies covered by BMO Capital Markets Corp. equity research analysts.

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Und = Underperform - Forecast to underperform the analyst's coverage universe on a total return basis;

(S) = Speculative investment;

NR = No rating at this time; and

R = Restricted – Dissemination of research is currently restricted.

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