

## Quintiles Transnational Steady in troubled waters

**Yesterday, Q reported 1Q14 earnings that bucked the trend among the CROs this quarter by reporting both strong operating results as well as strong new business.**

Adjusted cash EPS for the quarter was \$0.68 vs Barclays estimate (\$0.56) and consensus (\$0.55). FY14 EPS guidance was increased to a new range of \$2.45–2.58 from \$2.33–2.46/share. 1Q included \$0.04 of non-operating gains, but even adjusting for those this was a strong quarter. FY14 revenue guidance was raised to \$4.13–4.19B to reflect continued strength from the IHS segment. We raise FY14 to \$2.51 and FY15 to \$2.75. We see good likelihood of upside to our FY15 estimate, but choose to err on the cautious side given uncertainty in the macro environment for CROs.

**Good fundamentals all around.** 1Q revenues were ahead of our estimate by \$3 million. Most impressive to us was the very strong gross margins at 36% versus our modeled 34.7%. Operating margins in the Product Development segment were strong at 20.8%. The IHS segment showed progress from a top-line perspective but we're still waiting to see that flow through to improved margins which we expect in 2H14.

**Bookings were strong with the company's book-to-bill coming in at 1.27 with the backlog moving to above \$10 billion.** The book-to-bill is particularly impressive given the size of the company's revenue base. Bookings were very strong in the core Product Development segment (1.3) and solid in IHS at (1.15). Strength in the IHS segment was driven by the sales team business. The bookings strength, in contrast to peers, should rebut assertions that Q was a "share donor" to competitors.

**We continue to see Q as the CRO to own in the more volatile environment.** This was the third consecutive strong quarter for Quintiles since its IPO last May. We've consistently gotten earnings upside as well as upward revisions to results. We continue to believe the breadth of the company's portfolio and customer base should allow it to be least affected by potential consolidation among its clients. We uptick our price target to \$58, lifting our multiple to 21x FY15, vs our prior 20x FY15, given 1Q's strength.

### Q: Quarterly and Annual EPS (USD)

|        | 2013   |       | 2014  |       | 2015  |       | Change y/y |      |      |
|--------|--------|-------|-------|-------|-------|-------|------------|------|------|
| FY Dec | Actual | Old   | New   | Cons  | Old   | New   | Cons       | 2014 | 2015 |
| Q1     | 0.49A  | 0.56E | 0.68A | 0.55E | 0.66E | 0.66E | 0.63E      | 39%  | -3%  |
| Q2     | 0.50A  | 0.60E | 0.58E | 0.59E | 0.67E | 0.67E | 0.67E      | 16%  | 16%  |
| Q3     | 0.54A  | 0.62E | 0.62E | 0.62E | 0.69E | 0.69E | 0.69E      | 15%  | 11%  |
| Q4     | 0.58A  | 0.64E | 0.64E | 0.65E | 0.73E | 0.73E | 0.73E      | 10%  | 14%  |
| Year   | 2.10A  | 2.41E | 2.51E | 2.42E | 2.74E | 2.75E | 2.74E      | 20%  | 10%  |
| P/E    | 23.2   |       | 19.4  |       |       | 17.7  |            |      |      |

Source: Barclays Research.

Consensus numbers are from Thomson Reuters

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PLEASE SEE ANALYST CERTIFICATION(S) AND IMPORTANT DISCLOSURES BEGINNING ON PAGE 3.

Stock Rating **OVERWEIGHT**  
Unchanged

Industry View **POSITIVE**  
Unchanged

Price Target **USD 58.00**  
raised 5% from USD 55.00

Price (01-May-2014) USD 48.76  
Potential Upside/Downside +19%  
Tickers Q

Market Cap (USD mn) 6341  
Shares Outstanding (mn) 130.04  
Free Float (%) 84.42  
52 Wk Avg Daily Volume (mn) 0.6  
Dividend Yield (%) N/A  
Return on Equity TTM (%) N/A  
Current BVPS (USD) -5.15

Source: Thomson Reuters

Price Performance Exchange-NYSE  
52 Week range USD 55.00-40.10



[Link to Barclays Live for interactive charting](#)

### U.S. Specialty Pharmaceuticals

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## U.S. Specialty Pharmaceuticals

Industry View: POSITIVE

## Quintiles Transnational Holdings Inc. (Q)

Stock Rating: OVERWEIGHT

| Income statement (\$mn) | 2013A | 2014E | 2015E | 2016E | CAGR  |
|-------------------------|-------|-------|-------|-------|-------|
| Revenue                 | 3,808 | 4,133 | 4,453 | 4,806 | 8.1%  |
| EBITDA (adj)            | 608   | 671   | 726   | 799   | 9.5%  |
| EBIT (adj)              | 476   | 564   | 615   | 678   | 12.5% |
| Pre-tax income (adj)    | N/A   | N/A   | N/A   | N/A   | N/A   |
| Net income (adj)        | 269   | 337   | 371   | 426   | 16.6% |
| EPS (adj) (\$)          | 2.10  | 2.51  | 2.75  | 3.13  | 14.2% |
| Diluted shares (mn)     | 127.9 | 134.0 | 135.0 | 136.0 | 2.1%  |
| DPS (\$)                | 0.00  | 0.00  | 0.00  | 0.00  | N/A   |

| Margin and return data   | Average |       |      |      |      |
|--------------------------|---------|-------|------|------|------|
| EBITDA (adj) margin (%)  | 16.0    | 16.2  | 16.3 | 16.6 | 16.3 |
| EBIT (adj) margin (%)    | N/A     | N/A   | N/A  | N/A  | N/A  |
| Pre-tax (adj) margin (%) | N/A     | N/A   | N/A  | N/A  | N/A  |
| Net (adj) margin (%)     | 7.1     | 8.2   | 8.3  | 8.9  | 8.1  |
| ROIC (%)                 | 57.3    | 53.1  | 57.7 | 64.6 | 58.1 |
| ROA (%)                  | 11.2    | 10.7  | 11.0 | 11.6 | 11.1 |
| ROE (%)                  | -39.0   | 227.8 | 75.1 | 48.7 | 78.1 |

| Balance sheet and cash flow (\$mn) | CAGR  |       |       |       |        |
|------------------------------------|-------|-------|-------|-------|--------|
| Tangible fixed assets              | 205   | 229   | 253   | 276   | 10.5%  |
| Intangible fixed assets            | 714   | 686   | 664   | 651   | -3.0%  |
| Cash and equivalents               | 1,296 | 1,580 | 1,629 | 1,722 | 9.9%   |
| Total assets                       | 3,487 | 3,858 | 4,001 | 4,206 | 6.5%   |
| Short and long-term debt           | 2,061 | 2,028 | 1,703 | 1,378 | -12.5% |
| Other long-term liabilities        | 172   | 194   | 213   | 233   | 10.5%  |
| Total liabilities                  | 3,508 | 3,540 | 3,329 | 3,127 | -3.8%  |
| Net debt/(funds)                   | 762   | 445   | 71    | -347  | N/A    |
| Shareholders' equity               | -22   | 317   | 672   | 1,079 | N/A    |
| Change in working capital          | 850   | 312   | 35    | 78    | -54.8% |
| Cash flow from operations          | 332   | 438   | 480   | 531   | 17.0%  |
| Capital expenditure                | -101  | -101  | -105  | -114  | N/A    |
| Free cash flow                     | 231   | 337   | 374   | 417   | 21.8%  |

| Valuation and leverage metrics | Average |      |      |      |       |
|--------------------------------|---------|------|------|------|-------|
| P/E (adj) (x)                  | 23.2    | 19.4 | 17.7 | 15.6 | 19.0  |
| EV/sales (x)                   | 1.8     | 1.6  | 1.4  | 1.2  | 1.5   |
| EV/EBITDA (adj) (x)            | 11.4    | 9.9  | 8.6  | 7.3  | 9.3   |
| FCF yield (%)                  | 3.7     | 5.2  | 5.7  | 6.3  | 5.2   |
| P/BV (x)                       | -289.9  | 20.6 | 9.8  | 6.1  | -63.4 |
| Dividend yield (%)             | 0.0     | 0.0  | 0.0  | 0.0  | 0.0   |
| Total debt/capital (%)         | 101.7   | 83.3 | 70.9 | 61.5 | 79.3  |

| Selected operating metrics | Average |      |      |      |      |
|----------------------------|---------|------|------|------|------|
| SG&A/sales (%)             | 22.6    | 21.3 | 21.1 | 21.1 | 21.5 |
| R&D/sales (%)              | N/A     | N/A  | N/A  | N/A  | N/A  |
| R&D growth (%)             | N/A     | N/A  | N/A  | N/A  | N/A  |
| SG&A growth (%)            | 5.2     | 2.5  | 6.5  | 7.8  | 5.5  |

Price (01-May-2014) USD 48.76  
Price Target USD 58.00

**Why Overweight?** We see Quintiles as the "best of class" CRO that is positioned to extend its market leadership as the CRO industry enters a new era of growth. We believe Quintiles' advantages in scientific expertise and global scale will allow the company to grow faster than the underlying CRO industry's 8% growth with operational leverage pushing EPS growth into mid-teens.

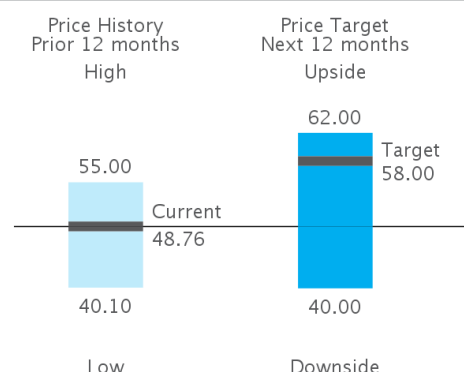
**Upside case** USD 62.00

Our upside case of \$62 is predicated on Quintiles succeeding in winning significant strategic deals with major customers, which would drive acceleration in revenue and earnings growth. This would drive further multiple expansion.

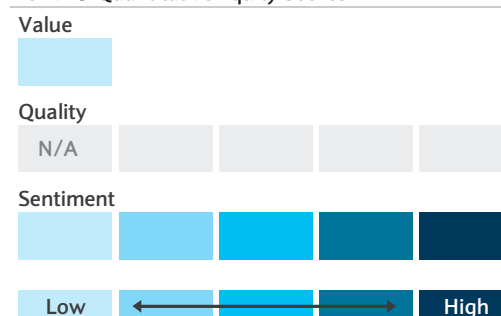
**Downside case** USD 40.00

We see risk from continued pressure on R&D spending from major drug companies, especially in the context of consolidation. This would result in contract delays and cancellations, reducing visibility on earnings growth, and result in EPS valuation compression.

## Upside/Downside scenarios



## POINT® Quantitative Equity Scores



Source: POINT®. The scores are valid as of the date of this report and are independent of the fundamental analysts' views. To view the latest scores, please go to the equity company page on Barclays Live.

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### Primary Stocks (Ticker, Date, Price)

Quintiles Transnational (Q, 01-May-2014, USD 48.76), Overweight/Positive, A/C/D/J/K/L/M/O

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|                                  |                                       |                                  |
|----------------------------------|---------------------------------------|----------------------------------|
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| Charles River Laboratories (CRL) | Covance Inc. (CVD)                    | Forest Laboratories Inc. (FRX)   |
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| Mylan Inc. (MYL)                 | Pacira Pharmaceuticals Inc. (PCRX)    | PAREXEL International (PRXL)     |
| Quintiles Transnational (Q)      | Teva Pharmaceutical Industries (TEVA) | Zoetis Inc. (ZTS)                |

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## Quintiles Transnational (Q)

USD 48.76 (01-May-2014)

Stock Rating

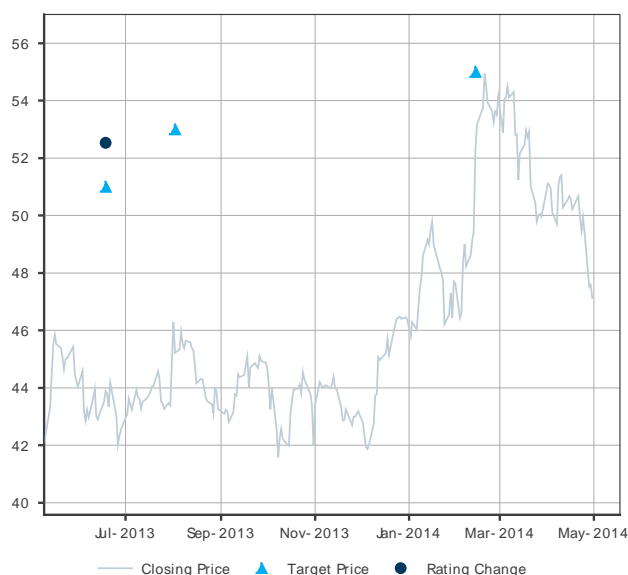
OVERWEIGHT

Industry View

POSITIVE

## Rating and Price Target Chart - USD (as of 01-May-2014)

Currency=USD



| Date        | Closing Price | Rating     | Adjusted Price Target |
|-------------|---------------|------------|-----------------------|
| 13-Feb-2014 | 52.20         |            | 55.00                 |
| 02-Aug-2013 | 45.22         |            | 53.00                 |
| 18-Jun-2013 | 43.89         | Overweight | 51.00                 |

Source: Thomson Reuters, Barclays Research

Historical stock prices and price targets may have been adjusted for stock splits and dividends.

Source: IDC, Barclays Research

[Link to Barclays Live for interactive charting](#)

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**Valuation Methodology:** We derive our \$58 price target using a 21x PE multiple on our FY15 EPS estimate of \$2.75. We think this is appropriate since Quintiles currently trades at roughly 21x FY14 EPS estimates.

**Risks which May Impede the Achievement of the Barclays Research Price Target:** Our valuation and earnings estimates are predicated on certain assumptions. If the competitive dynamics of the pharmaceutical market changes; if interest rates rise or if the manufacturers change outsourcing practices, this would have a negative impact on earnings at our covered companies. In that event, we would revisit our investment thesis.

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