

## COMPANY NOTE

Estimate Change

USA | Healthcare | Pharmaceutical Svcs.

May 5, 2015

# Jefferies

## Catalent, Inc. (CTLT) 3Q Better, 4Q Reduced; Key Insights from the Quarter

### Key Takeaway

**CTLT is likely to trade lower on the FY guidance cut. Favorable mix shifts and cost control drove F3Q above consensus, partially offset by a stiff FX revenue headwind. Excluding FX, FY15 EBITDA guidance was reduced by <1% on lower customer end-market demand. CTLT continued to pursue its acquisition strategy, buying Pharmapak during F3Q, while noting early pull-through benefit from its recent Micron acquisition, which should begin to show in '16.**

**M&A Remains Key Component of Revenue Growth Strategy.** CTLT's motivations for these acquisitions extend well beyond just the acquired revenue and capabilities. Micron, for example, is expected to be a driver of future growth for CTLT's Development segment. The acquisition gave CTLT access to a client base and >400 new compounds into which it has already begun cross-selling downstream solutions ("Follow The Molecule"). Employing this strategy can make even small acquisitions very impactful over time.

**Acquires Pharmapak Technologies,** a pharma packaging company in New South Wales, Australia. Financials/terms were not provided, but we believe the revenue contribution is relatively small (i.e., \$14-16M annually). Pharmapak will complement CTLT's existing oral dose facility and offer an integrated solution to clients in that region. This is CTLT's third, small acquisition in the last nine months. Leverage is below 4x now. Remaining under management's stated 5.5x EBITDA leverage ceiling, we estimate CTLT could buy up to \$100-150M in EBITDA (assuming it pays a 10-12x multiple).

**Long Cycle Development Revenue Growing 28% YTD Due to Seasonality.** This is 7-8% of total revenue, with 10-12% growth likely for FY15. While slower than the YTD number, the Micron opportunities could actually accelerate this development activity, enhancing both near-term Development revenue growth and long-cycle supply opportunities.

**Mostly FX-Driven Guidance Cut, Still Optically Large.** Management lowered the EPS midpoint by \$0.07, while exceeding the 3Q consensus by \$0.02. Thus, the 4Q implied reduction is fairly large. Because Oral Tech is growing faster (CDO), the long-term effect is muted by the positive shift in margin mix.

### Valuation/Risks

Our \$32 PT is based on the average of three different valuation analyses—EV/EBITDA comparables (\$28.50), P/E comparables (\$35), and discounted cash flow (\$32). Risks include success of client R&D projects, loss of large client contracts, and international (currency and geopolitical/regulatory) exposure.

USD	Prev.	2013A	Prev.	2014A	Prev.	2015E	Prev.	2016E
Rev. (MM)	--	1,800.3	--	1,827.4	1,849.0	1,823.5	1,986.3	1,970.4
EBITDA (MM)	--	412.9	--	432.3	448.2	436.6	488.7	475.9
EV/Rev		3.0x		3.0x		3.0x		2.8x
Cons. EPS	--	--	--	--	--	1.70	--	1.87
EV/EBITDA		13.2x		12.6x		12.5x		11.5x
<b>EPS</b>								
Sep	--	--	--	--	--	0.13A	--	--
Dec	--	--	--	--	--	0.44A	--	--
Mar	--	--	--	--	0.36	0.46A	--	--
Jun	--	--	--	--	0.73	0.59	--	--
FY Jun	--	1.09	1.74	1.88	1.72	1.67	--	1.96
FY P/E		26.8x		15.5x		17.5x		14.9x

**BUY**

Price target \$32.00

Price \$29.18

### Financial Summary

Book Value (MM):	\$492.4
Net Debt (MM):	\$1,765.7
Long-Term Debt (MM):	\$1,881.8
Cash & ST Invest. (MM):	\$116.1

### Market Data

52 Week Range:	\$31.66 - \$19.30
Total Entprs. Value (MM):	\$5,451.1
Market Cap. (MM):	\$3,685.4
Shares Out. (MM):	126.3
Float (MM):	79.2
Avg. Daily Vol.:	584,599

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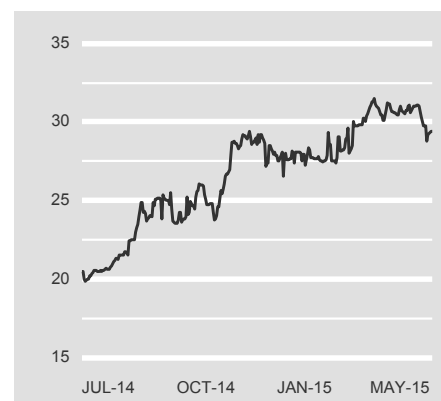
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### Price Performance



**Chart 1: Catalent, Inc. Summary of the Quarter**
**Catalent, Inc.**
**F3Q15 (March) Earnings Summary**

Source: Company filings and Jefferies LLC

Reports 5/5/2015 AMC

FY ending June 30 in thousands except EPS	Reported		Estimate	Actual	Consensus	Percentage Change		Difference		
	F3Q14	F2Q15	F3Q15	F3Q15		Seq	Y/Y	Seq	Y/Y	Est.
<b>Net revenue</b>	\$ 453.1	\$ 455.8	\$ 453.0	\$ 446.6	451.0	(2.0%)	(1.4%)	\$ (9.2)	\$ (6.5)	\$ (6.4)
Cost of products sold	301.4	299.7	297.8	294.4		(1.8%)	(2.3%)	(5.3)	(7.0)	(3.4)
Gross Profit	151.7	156.1	155.2	152.2		(2.5%)	0.3%	(3.9)	0.5	(3.0)
SG&A	87.6	88.1	96.8	80.9		(8.2%)	(7.6%)	(7.2)	(6.7)	(15.9)
EBIT ex-nonrecurring	64.1	68.0	58.4	71.3		4.9%	11.2%	3.3	7.2	12.9
Impairments (gains on asset sales)	0.4	3.5	-	0.3		(91.4%)	(25.0%)	(3.2)	(0.1)	0.3
Non-recurring items	3.5	2.1	-	5.2		147.6%	48.6%	3.1	1.7	5.2
EBIT	60.2	62.4	58.4	65.8		5.4%	9.3%	3.4	5.6	7.4
Interest expense (income)	40.4	23.9	23.5	23.0		(3.8%)	(43.1%)	(0.9)	(17.4)	(0.5)
Other expense (income)	5.2	(3.6)	-	0.8		(122.2%)	(84.6%)	4.4	(4.4)	0.8
Pre-tax income	14.6	42.1	34.8	42.0		(0.2%)	187.7%	(0.1)	27.4	7.2
Taxes	6.6	(4.1)	10.4	11.2		(373.2%)	69.7%	15.3	4.6	0.8
Net income	8.0	46.2	24.4	30.8		(33.3%)	285.0%	(15.4)	22.8	6.4
Comparable NI	20.7	33.9	28.3	36.4		7.4%	75.8%	2.5	15.7	8.1
Adjusted NI	38.9	55.9	46.6	57.6		3.0%	48.1%	1.7	18.7	11.0
GAAP EPS	0.11	0.37	0.19	0.24		(33.5%)	131.5%	(0.12)	0.14	0.05
Comparable EPS	0.27	0.27	0.22	0.29		7.1%	5.7%	0.02	0.02	0.07
Adjusted EPS	0.51	0.44	0.36	0.46	0.44	2.8%	(11.0%)	0.01	(0.06)	0.10
Diluted shares	75.9	126.0	129.0	126.3		0.2%	66.3%	0.3	50.4	(2.7)
EBITDA	90.5	101.7	97.4	100.1		(1.6%)	10.6%	(1.6)	9.6	2.7
Comparable EBITDA	97.7	105.3	94.2	106.8		1.4%	9.3%	1.5	9.1	12.6
Adjusted EBITDA	106.0	112.9	101.8	110.5	105.0	(2.1%)	4.2%	(2.4)	4.5	8.7
<b>COMMON SIZE</b>										
Cost of products sold	66.5%	65.8%	65.7%	65.9%				20 bps	(60 bps)	20 bps
Gross margin	33.5%	34.2%	34.3%	34.1%				(20 bps)	60 bps	(20 bps)
SG&A	19.3%	19.3%	21.4%	18.1%				(120 bps)	(120 bps)	(330 bps)
EBIT ex-nonrecurring	14.1%	14.9%	12.9%	16.0%				100 bps	180 bps	310 bps
One-time charges	0.9%	1.2%	0.0%	1.2%				0 bps	40 bps	120 bps
EBIT	13.3%	13.7%	12.9%	14.7%				100 bps	140 bps	190 bps
Interest expense (income)	8.9%	5.2%	5.2%	5.2%				(10 bps)	(380 bps)	0 bps
Other expense (income)	1.1%	(0.8%)	0.0%	0.2%				100 bps	(100 bps)	20 bps
Pre-tax income	3.2%	9.2%	7.7%	9.4%				20 bps	620 bps	170 bps
Income taxes	45.2%	(9.7%)	30.0%	26.7%				3,640 bps	(1,850 bps)	(330 bps)
Net income	1.8%	10.1%	5.4%	6.9%				(320 bps)	510 bps	150 bps
Comparable NI	4.6%	7.4%	6.3%	8.2%				70 bps	360 bps	190 bps
Adjusted NI	8.6%	12.3%	10.3%	12.9%				60 bps	430 bps	260 bps
EBITDA	20.0%	22.3%	21.5%	22.4%				10 bps	240 bps	90 bps
Comparable EBITDA	21.6%	23.1%	20.8%	23.9%				80 bps	240 bps	310 bps
Adjusted EBITDA	23.4%	24.8%	22.5%	24.7%				0 bps	130 bps	230 bps
<b>SEGMENTS</b>										
<b>Oral Technologies</b>										
Revenue	287.3	277.2	272.9	284.0		2.5%	(1.1%)	6.8	(3.3)	11.1
% of total	63.4%	60.8%	60.3%	63.6%				280 bps	20 bps	330 bps
EBITDA	76.2	74.7	72.9	81.7		9.4%	7.2%	7.0	5.5	8.8
Margin	26.5%	26.9%	26.7%	28.8%				180 bps	220 bps	210 bps
<b>Medication Delivery &amp; Solutions</b>										
Revenue	65.4	73.7	73.6	61.2		(17.0%)	(6.4%)	(12.5)	(4.2)	(12.4)
% of total	14.4%	16.2%	16.3%	13.7%				(250 bps)	(70 bps)	(260 bps)
EBITDA	15.7	18.1	14.7	10.9		(39.8%)	(30.6%)	(7.2)	(4.8)	(3.8)
Margin	24.0%	24.6%	20.0%	17.8%				(670 bps)	(620 bps)	(220 bps)
<b>Development &amp; Clinical Services</b>										
Revenue	103.7	107.8	109.3	103.7		(3.8%)	0.0%	(4.1)	-	(5.6)
% of total	22.9%	23.7%	24.1%	23.2%				(40 bps)	30 bps	(90 bps)
EBITDA	23.0	21.9	23.5	23.8		8.7%	3.5%	1.9	0.8	0.3
Margin	22.2%	20.3%	21.5%	23.0%				260 bps	80 bps	150 bps
<b>FY15 GUIDANCE</b>										
Revenue		Previous \$1,820-1,860M	JEF Previous \$1,849M	Updated \$1,800-1,830M	Prior Cons. \$1,845M					
EBITDA		\$434-444M	\$448M	\$428-436M	\$439M					
Net Income		\$204-214M	\$212M	\$197-205M						

Source: Company data and Jefferies LLC

**Catalent, Inc.  
Earnings Model**

FY June	2013					2014					2015E					
Source: Jefferies LLC	Sep-12	Dec-12	Mar-13	Jun-13	2013	Sep-13	Dec-13	Mar-14	Jun-14	2014	Sep-14	Dec-14	Mar-15	Jun-15E	2015E	2016E
Net revenue	\$ 412.0	\$ 436.2	\$ 447.0	\$ 505.1	\$ 1,800.3	\$ 414.3	\$ 440.7	\$ 453.1	\$ 519.6	\$ 1,827.7	\$ 418.3	\$ 455.8	\$ 446.6	\$ 502.8	\$ 1,823.5	\$ 1,970.4
Cost of products sold	294.5	296.1	309.6	331.5	1,231.7	295.1	303.3	301.4	329.3	1,229.1	293.0	299.7	294.4	314.3	1,201.4	1,295.2
Gross profit	117.5	140.1	137.4	173.6	568.6	119.2	137.4	151.7	190.3	598.6	125.3	156.1	152.2	188.5	622.1	675.2
SG&A	81.8	86.2	83.7	88.9	340.6	81.1	87.5	87.6	78.6	334.8	81.4	88.1	80.9	97.7	348.1	355.6
EBIT ex-nonrecurring	35.7	53.9	53.7	84.7	228.0	38.1	49.9	64.1	111.7	263.8	43.9	68.0	71.3	90.7	273.9	319.5
Impairments (gains on asset sale)	(0.2)	2.6	2.2	0.6	5.2	-	-	0.4	2.8	3.2	-	3.5	0.3	-	3.8	-
Non-recurring items	3.5	5.6	3.6	5.7	18.4	3.0	5.4	3.5	7.8	19.7	1.4	2.1	5.2	-	8.7	-
EBIT	32.4	45.7	47.9	78.4	204.4	35.1	44.5	60.2	101.1	240.9	42.5	62.4	65.8	90.7	261.4	319.5
Interest expense (income)	53.9	53.2	53.6	42.5	203.2	40.9	41.5	40.4	40.3	163.1	35.5	23.9	23.0	22.9	105.3	89.7
Other expense (income)	-	12.0	8.3	4.8	25.1	(1.0)	(1.4)	5.2	7.6	10.4	41.3	(3.6)	0.8	-	38.5	-
Pretax income	(21.5)	(19.5)	(14.0)	31.1	(23.9)	(4.8)	4.4	14.6	53.2	67.4	(34.3)	42.1	42.0	67.9	117.7	229.9
Minority interest	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Taxes	(2.0)	8.0	(0.1)	18.2	24.1	(6.6)	23.3	6.6	26.2	49.5	(14.0)	(4.1)	11.2	20.4	13.5	69.0
Net income	(19.5)	(27.5)	(13.9)	12.9	(48.0)	1.8	(18.9)	8.0	27.0	17.9	(20.3)	46.2	30.8	47.5	104.2	160.9
Comparable NI	(20.2)	(0.2)	(8.9)	42.1	12.8	(13.5)	15.9	20.7	63.7	86.8	(9.6)	33.9	36.4	61.6	122.2	194.9
Adjusted NI	(5.9)	20.9	13.0	54.4	82.4	(1.4)	27.9	38.9	77.0	142.4	13.4	55.9	57.6	76.8	203.7	255.9
GAAP EPS	(0.26)	(0.36)	(0.18)	0.17	(0.63)	0.02	(0.25)	0.11	0.36	0.24	(0.19)	0.37	0.24	0.37	0.86	1.23
Comparable EPS	(0.27)	(0.00)	(0.12)	0.55	0.17	(0.18)	0.21	0.27	0.84	1.14	(0.09)	0.27	0.29	0.48	1.00	1.50
Adjusted EPS	(0.08)	0.28	0.17	0.72	1.09	(0.02)	0.37	0.51	1.01	1.88	0.13	0.44	0.46	0.59	1.67	1.96
Diluted shares	75.9	75.9	75.9	75.9	75.9	75.9	75.9	75.9	75.9	75.9	105.5	126.0	126.3	129.3	121.8	130.3
EBITDA	69.7	72.1	78.8	111.2	331.8	72.8	83.4	90.5	127.7	374.4	36.6	101.7	100.1	124.8	363.2	455.7
Comparable EBITDA	76.3	94.5	88.4	129.7	388.9	79.1	91.9	97.7	152.8	421.5	82.4	105.3	106.8	126.0	420.5	460.5
Adjusted EBITDA	82.3	101.7	100.7	128.2	412.9	82.3	93.3	106.0	150.7	432.3	83.4	112.9	110.5	129.8	436.6	475.9
Common Size:																
Net revenue	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%
Cost of products sold	71.5%	67.9%	69.3%	65.6%	68.4%	71.2%	68.8%	66.5%	66.5%	67.2%	70.0%	65.8%	65.9%	62.5%	65.9%	65.7%
Gross margin	28.5%	32.1%	30.7%	34.4%	31.6%	28.8%	31.2%	33.5%	36.6%	32.8%	30.0%	34.2%	34.1%	37.5%	34.1%	34.3%
SG&A	19.9%	19.8%	18.7%	17.6%	18.9%	19.6%	19.9%	19.3%	19.3%	18.3%	19.5%	19.3%	18.1%	19.4%	19.1%	18.0%
EBIT ex-nonrecurring	8.7%	12.4%	12.0%	16.8%	12.7%	9.2%	11.3%	14.1%	21.5%	14.4%	10.5%	14.9%	16.0%	18.0%	15.0%	16.2%
Impairments (gains on asset sale)	(0.0%)	0.6%	0.5%	0.1%	0.3%	0.0%	0.0%	0.1%	0.5%	0.2%	0.0%	0.8%	0.1%	0.0%	0.2%	0.0%
Non-recurring items	0.8%	1.3%	0.8%	1.1%	1.0%	0.7%	1.2%	0.8%	1.5%	1.1%	0.3%	0.5%	1.2%	0.0%	0.5%	0.0%
EBIT	7.9%	10.5%	10.7%	15.5%	11.4%	8.5%	10.1%	13.3%	19.5%	13.2%	10.2%	13.7%	14.7%	18.0%	14.3%	16.2%
Interest expense (income)	13.1%	12.2%	12.0%	8.4%	11.3%	9.9%	9.4%	8.9%	7.8%	8.9%	8.5%	5.2%	5.2%	4.6%	5.8%	4.6%
Other expense (income)	0.8%	1.3%	0.8%	1.1%	1.0%	0.7%	1.2%	0.8%	1.5%	1.1%	0.3%	0.5%	1.2%	0.0%	0.5%	0.0%
Pretax income	(5.2%)	(4.5%)	(3.1%)	6.2%	(1.3%)	(1.2%)	1.0%	3.2%	10.2%	3.7%	(8.2%)	9.2%	9.4%	13.5%	6.5%	11.7%
Taxes	9.3%	(41.0%)	0.7%	58.5%	(100.8%)	137.5%	529.5%	45.2%	49.2%	73.4%	40.8%	(9.7%)	26.7%	30.0%	11.4%	30.0%
Net income	(4.7%)	(6.3%)	(3.1%)	2.6%	(2.7%)	0.4%	(4.3%)	1.8%	5.2%	1.0%	(4.9%)	10.1%	6.9%	9.4%	5.7%	8.2%
Adjusted net income	(1.4%)	4.8%	2.9%	10.8%	4.6%	(0.3%)	6.3%	8.6%	14.8%	7.8%	3.2%	12.3%	12.9%	15.3%	11.2%	13.0%

## Company Description

Catalent, Inc. is the leading global provider of advanced delivery technologies and development solutions for drugs, biologics and consumer health products. With over 80 years serving the industry, Catalent has proven expertise in bringing more customer products to market faster, enhancing product performance and ensuring reliable clinical and commercial product supply. Catalent employs approximately 8,000 people, including over 1,000 scientists, at nearly 30 facilities across 5 continents.

## Analyst Certification:

I, David Windley, CFA, CPA, certify that all of the views expressed in this research report accurately reflect my personal views about the subject security(ies) and subject company(ies). I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or views expressed in this research report.

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## Company Specific Disclosures

Jefferies Group LLC, its affiliates or subsidiaries expect to receive or intend to seek compensation for investment banking services from Catalent, Inc. within the next three months.

Within the past 12 months, Jefferies Group LLC, its affiliates or subsidiaries has received compensation from investment banking services from Catalent, Inc..

Within the past twelve months, Catalent, Inc. has been a client of Jefferies LLC and investment banking services are being or have been provided.

Jefferies Group LLC, its affiliates or subsidiaries has acted as a manager or co-manager in the underwriting or placement of securities for Catalent, Inc. or one of its affiliates within the past twelve months.

## Meanings of Jefferies Ratings

Buy - Describes stocks that we expect to provide a total return (price appreciation plus yield) of 15% or more within a 12-month period.

Hold - Describes stocks that we expect to provide a total return (price appreciation plus yield) of plus 15% or minus 10% within a 12-month period.

Underperform - Describes stocks that we expect to provide a total negative return (price appreciation plus yield) of 10% or more within a 12-month period.

The expected total return (price appreciation plus yield) for Buy rated stocks with an average stock price consistently below \$10 is 20% or more within a 12-month period as these companies are typically more volatile than the overall stock market. For Hold rated stocks with an average stock price consistently below \$10, the expected total return (price appreciation plus yield) is plus or minus 20% within a 12-month period. For Underperform rated stocks with an average stock price consistently below \$10, the expected total return (price appreciation plus yield) is minus 20% within a 12-month period.

NR - The investment rating and price target have been temporarily suspended. Such suspensions are in compliance with applicable regulations and/or Jefferies policies.

CS - Coverage Suspended. Jefferies has suspended coverage of this company.

NC - Not covered. Jefferies does not cover this company.

Restricted - Describes issuers where, in conjunction with Jefferies engagement in certain transactions, company policy or applicable securities regulations prohibit certain types of communications, including investment recommendations.

Monitor - Describes stocks whose company fundamentals and financials are being monitored, and for which no financial projections or opinions on the investment merits of the company are provided.

## Valuation Methodology

Jefferies' methodology for assigning ratings may include the following: market capitalization, maturity, growth/value, volatility and expected total return over the next 12 months. The price targets are based on several methodologies, which may include, but are not restricted to, analyses of market risk, growth rate, revenue stream, discounted cash flow (DCF), EBITDA, EPS, cash flow (CF), free cash flow (FCF), EV/EBITDA, P/E, PE/growth, P/CF, P/FCF, premium (discount)/average group EV/EBITDA, premium (discount)/average group P/E, sum of the parts, net asset value, dividend returns, and return on equity (ROE) over the next 12 months.

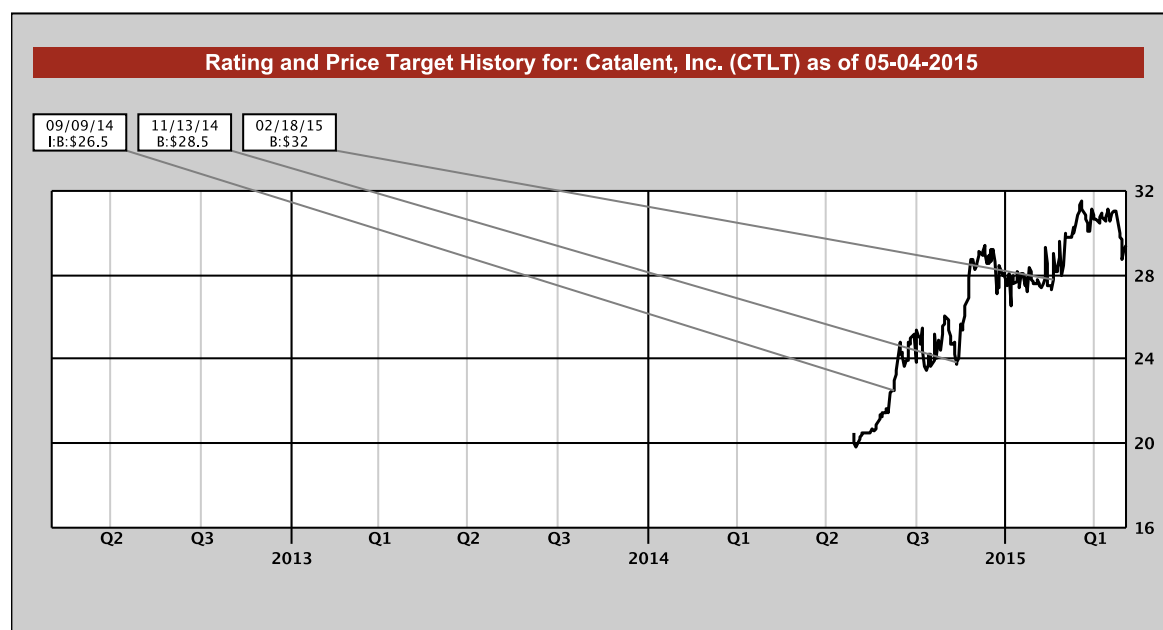
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## Distribution of Ratings

Rating	Count	Percent	IB Serv./Past 12 Mos.	
			Count	Percent
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HOLD	841	40.55%	160	19.02%
UNDERPERFORM	170	8.20%	11	6.47%

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