

Catalent, Inc.

Fiscal Second-Quarter Analysis; Solid Results Obscured by Foreign-Exchange Headwinds

- Conclusion.** On the evening of Wednesday, February 11, Catalent reported fiscal second-quarter earnings, which beat our estimate by \$0.13 and the consensus by \$0.10. Compared with our model, revenue (\$0.015 cents) and EBITDA margin (\$0.12) came in well ahead of our expectations, driven by very robust top- and bottom-line results in the medication delivery solutions segment. Despite better underlying results in the base business year-to-date, foreign-exchange headwinds more than offset these improvements. As a result, management reduced full-year guidance by \$70 million to \$80 million on the top line and roughly \$11 million on the bottom line. Given this headwind, we have reduced our estimates for fiscal 2015. We now expect fiscal 2015 EPS of \$1.70, which is down \$0.08 from our prior target and down 10% from fiscal 2014. Despite the significant foreign-exchange headwind, we are pleased with the stronger fundamentals and reiterate our Outperform rating.
- Financial Details.** Second-quarter revenue of \$456 million came in \$13.5 million ahead of our expectations, driven by stronger results in the medication delivery solutions business (about \$23 million ahead of our estimate), offset by slower oral technology growth (about \$9 million below our model) and essentially in line development and clinical services (\$400,000 below our model). For the full fiscal year (which ends June 30), management's outlook on a constant-currency basis is modestly better than original guidance. Clearly the non-oral portion of the long-cycle, dose-manufacturing business, medication delivery solutions, is experiencing the strongest performance—up 33% in the period. We also believe better new product awards and less generic and life-cycle erosion are beginning to help lift organic revenue growth, which was 300 basis points better than we expected overall in the quarter. In addition, we expect acquisitions to remain a focus for capital deployment, which should augment the base business and help offset the foreign-exchange headwind. The company completed two deals in the quarter, although neither were material to the top line.
- For the year, we now conservatively project \$1.84 billion in revenue (up 0.7% as reported or 5.5% on an organic constant-currency basis), which is down from \$1.89 billion previously (up 3.5% as reported and 5.7% on an organic constant-dollar basis). We project adjusted EBITDA of \$441 million, down \$17 million from our previous model. We note that foreign exchange had a slightly lower impact on the top line than we would have expected (\$10 million lower), but a slightly higher impact to EBITDA (\$13 million higher). Therefore, it will be important to watch for continued dollar strength, particularly relative to the euro, over the next few quarters. On the bottom line, we now expect EPS of \$1.70 for the fiscal year, down \$0.08 from our previous model.

Catalent is the world's leading provider of advanced delivery technologies to the pharmaceutical industry. The company was purchased by The Blackstone Group in 2007 from Cardinal Health and is based originally on R.P. Scherer's softgel manufacturing technology patented in 1934. The company operates in 27 facilities in five continents, and manufactures more than 70 billion doses of medication annually.

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February 11, 2015

Stock Rating: **Outperform**
Company Profile: **Established Growth**

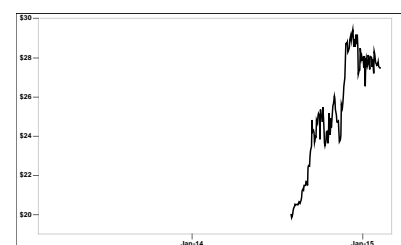
Symbol: CTLT (NYSE)
Price: \$29.32 (52-Wk.: \$19-\$30)
Market Value (mil.): \$3,630
Fiscal Year End: June
Long-Term EPS Growth Rate: 11%
Dividend/Yield: None

		2014A	2015E	2016E
Estimates				
EPS	Q1	\$-0.02	A\$0.13	NA
	Q2	\$0.37	A\$0.44	NA
	Q3	\$0.52	\$0.43	NA
	Q4	\$1.01	\$0.64	NA
	FY	\$1.89	\$1.70	\$1.82
	CY		\$1.68	\$1.90
Valuation				
FY P/E		15.5x	17.2x	16.1x
CY P/E			17.5x	15.4x

Trading Data (FactSet)	
Shares Outstanding (mil.)	106
Float (mil.)	124
Average Daily Volume	409,637

Financial Data (FactSet)	
Long-Term Debt/Total Capital (MRQ)	0.0
Book Value Per Share (MRQ)	4.1
Return on Equity (TTM)	0.0

Two-Year Price Performance Chart



Sources: FactSet, William Blair & Company estimate

- Valuation and stock thoughts.** Following the relatively minor changes to our model, Catalent now trades at 17.4 times our adjusted calendar 2015 EPS target (or 25.9 times our fully taxed calendar 2015 estimate of \$1.13). On an EV/EBITDA basis, the stock trades at 12.6 times our revised 2015 expectation. Comparatively, the CRO peer group trades at 20.8 times 2015 EPS (20.0 times, excluding Covance [CVD \$106.94; Market Perform]) and 12.5 times EV/EBITDA (also 12.5 times, excluding Covance). Despite the foreign-exchange headwind, we are encouraged with the company's underlying results and view the relative valuation as reasonable. Therefore, we maintain our Outperform rating on Catalent. Our updated model and exhibits detailing results relative to our expectations and updated guidance are included in the following pages.

Exhibit 1. Fiscal 2015 Guidance Relative to Previous Expectations

	Fiscal 2015 Guidance		Fiscal 2015 Estimates		
	Previous	Revised	WB - Prior to Call	WB - As Revised	Consensus - Prior to Call
Revenue (\$M)	\$1,890 to \$1,920	\$1,820 to \$1,860	\$1,891	\$1,840	\$1,899
Growth	3.4% to 5.0%	(0.4%) to 1.8%	3.5%	0.7%	3.9%
Adjusted EBITDA	\$450 to \$460	\$434 to \$444	\$457.6	\$441	\$456
Growth (decline)	4.0% to 6.3%	0.3% to 2.6%	5.8%	1.9%	5.4%
Adjusted Net Income	\$215 to \$225	\$204 to \$214	\$215.3	\$209.30	NA
Growth (decline)	51% to 58%	43% to 50%	51.19%	47.0%	NA

Source: William Blair estimates, FactSet, and Company reports

Exhibit 2. Fiscal Second-Quarter EPS Performance Relative to William Blair Expectations

Revenues	\$ 0.015
Gross Profit	\$ 0.036
SG&A	\$ 0.075
Depreciation	\$ 0.010
Net interest income (expense)	\$ (0.003)
Taxes	\$ (0.003)
Share Count	\$ (0.002)
Total	\$ 0.128

Source: William Blair estimates and Company reports

Exhibit 3. Fiscal Second-Quarter Variance to William Blair Model

	2Q FY15 (Actual)	2Q FY14 (Actual)	Year/Year % Change	2Q FY15 (Estimate)	Year/Year % Change	Change
Net revenues	\$ 455.8	\$ 440.7	3.4%	\$ 442.3	0.4%	13.50
Cost of revenue	284.6	277.8	2.4%	281.3	1.3%	3.30
Gross profit	171.2	162.9	5.1%	161.0	-1.2%	10.20
SG&A	58.3	69.5	-16.1%	67.2	-3.3%	(8.90)
EBITDA	112.9	93.4	20.9%	93.8	0.4%	19.10
Depreciation	23.6	26.8	-11.9%	24.3	-9.3%	(0.70)
EBITA	89.3	66.6	34.1%	69.5	4.4%	19.80
Net interest income (expense)	(23.9)	(41.4)	-42.3%	(23.4)	-43.5%	(0.50)
Pretax income	65.4	25.2	159.5%	46.1	82.9%	19.30
Income tax expense	9.5	(2.7)	-451.9%	6.5	-338.9%	3.05
Adjusted Net income	55.9	27.9	100.4%	39.7	NM	16.25
Minority interest	(0.5)	(0.3)	66.7%	(0.4)	33.3%	
Amortization	(11.6)	(10.5)	10.5%	(10.6)	1.0%	
Nonrecurring items (net of tax)	2.4	(36.0)	-106.7%	0.2	-100.6%	
Net Income from continued operations (GAAP)	46.2	(18.9)	-344.4%	28.9	-252.6%	
Income from discontinued operations	0.2	0.6	-66.7%	0.5	-16.7%	
GAAP Net Income	46.0	(19.5)	-335.9%	28.4	NM	17.65
Diluted shares outstanding	126.0	74.8	68.4%	125.4	67.6%	0.60
Adjusted EPS	\$ 0.44	\$ 0.37	18.9%	\$ 0.32	NM	0.13
GAAP EPS	\$ 0.37	\$ (0.26)	-240.0%	\$ 0.23	-186.7%	0.14
Gross profit	37.6%	37.0%	0.6%	36.4%	-0.6%	
SG&A	12.8%	15.8%	-3.0%	15.2%	-0.6%	
EBITDA	24.8%	21.2%	3.6%	21.2%	0.0%	
Depreciation	5.2%	6.1%	-0.9%	5.5%	-0.6%	
EBITA	19.6%	15.1%	4.5%	15.7%	0.6%	
Pretax income	14.3%	5.7%	8.6%	10.4%	4.7%	
Tax rate	14.5%	-10.7%	25.2%	14.0%	24.7%	
Adjusted Net Income	12.3%	6.3%	5.9%	9.0%	2.6%	
GAAP Net Income	10.1%	-4.4%	14.5%	6.4%	10.8%	
Segment Breakdown	2Q FY15 (Actual)	2Q FY14 (Actual)	Year/Year % Change	2Q FY15 # # (Estimate) #	Year/Year % Change	
Oral Tech Revenue	277.2	285.9	-3.0%	285.9	0.0%	(8.70)
Oral Tech EBITDA	74.7	74.7	0.1%	73.8	-1.2%	0.94
% margin	27.0%	26.1%	0.8%	25.8%	-0.3%	1.1%
Medication Delivery Solutions Revenue	73.7	55.3	33.3%	50.3	-9.0%	23.40
Medication Delivery Solutions EBITDA	18.1	6.9	162.3%	8.1	17.4%	10.00
% margin	24.6%	12.5%	12.1%	16.1%	3.6%	8.5%
Development & Clinical Services Revenue	107.8	102.1	5.6%	108.2	6.0%	(0.40)
Development & Clinical Services EBITDA	21.9	18.5	18.4%	20.0	8.1%	1.90
% margin	20.3%	18.1%	2.2%	18.5%	0.4%	1.8%

Source: William Blair estimates and Company reports

Exhibit 4. Updated Catalent Financial Model, 2011 through 2017(E)

	2011	2012	2013	2014	Q1'15	Q2'15	Q3'15E	Q4'15E	2015E	2016E	2017E
Net revenue	\$1,531.8	\$1,694.8	\$1,800.3	\$1,827.7	\$418.3	\$455.8	\$450.7	\$515.5	\$1,840.2	\$1,907.5	\$1,998.2
Cost of revenue	\$954.0	\$1,056.1	\$1,143.8	\$1,145.7	\$272.9	\$284.6	\$280.8	\$318.6	\$1,156.8	\$1,184.6	\$1,239.8
Gross profit	\$577.8	\$638.8	\$656.5	\$682.0	\$145.4	\$171.2	\$169.9	\$196.9	\$683.5	\$723.0	\$758.5
Selling, general and administrative expense	\$224.0	\$250.4	\$243.8	\$249.3	\$62.0	\$58.3	\$63.1	\$59.3	\$242.7	\$254.7	\$263.0
EBITDA	\$353.8	\$388.3	\$412.7	\$432.6	\$83.4	\$112.9	\$106.8	\$137.6	\$440.7	\$468.2	\$495.5
Depreciation	\$86.7	\$95.7	\$108.8	\$100.4	\$23.7	\$23.6	\$20.7	\$20.4	\$88.4	\$109.0	\$112.1
EBITA	\$267.1	\$292.6	\$303.9	\$332.2	\$59.7	\$89.3	\$86.1	\$117.3	\$352.4	\$359.3	\$383.3
Interest and other income (expense), net	(\$165.5)	(\$183.2)	(\$203.3)	(\$163.4)	(\$35.5)	(\$23.9)	(\$22.2)	(\$20.3)	(\$101.9)	(\$75.0)	(\$75.5)
Pretax income	\$101.6	\$109.4	\$100.6	\$168.9	\$24.2	\$65.4	\$63.9	\$97.0	\$250.5	\$284.3	\$307.9
Income tax expense	\$27.7	\$28.2	\$18.3	\$26.5	\$10.8	\$9.5	\$8.3	\$12.6	\$41.2	\$48.3	\$72.6
Adjusted Net Income	\$73.9	\$81.2	\$82.3	\$142.4	\$13.4	\$55.9	\$55.6	\$84.4	\$209.3	\$235.9	\$235.3
Minority Interest	\$3.9	\$1.2	(\$0.1)	(\$1.0)	(\$0.4)	(\$0.5)	(\$0.5)	(\$0.6)	(\$2.0)	(\$2.6)	(\$3.3)
Nonrecurring items	(82.0)	(58.1)	(81.1)	(57.9)	(\$46.8)	(\$11.2)	(\$3.5)	(\$3.2)	(64.7)	(5.6)	(8.4)
Tax adjustment	3.9	11.7	(8.7)	(23.0)	\$24.8	\$13.6	\$2.3	\$6.6	47.3	22.3	44.6
Nonrecurring items (net of tax)	(78.1)	(46.4)	(89.8)	(81.0)	(\$22.0)	\$2.4	(\$1.2)	\$3.4	(17.4)	16.7	36.2
Net income from continuing operations (GAAP)	(29.1)	2.1	(50.9)	18.0	(\$20.3)	\$46.2	\$43.1	\$76.9	145.9	206.8	222.1
Income from Discontinued Operations	21.0	41.3	(1.2)	2.7	(\$0.4)	\$0.2	\$0.5	\$0.5	0.8	2.0	0.0
Net income	(\$50.1)	(\$39.2)	(\$49.7)	\$15.3	(\$19.9)	\$46.0	\$42.6	\$76.4	\$145.1	\$204.8	\$222.1
EPS (excl. nonrecurring items, incl. options beg Q105)	\$0.99	\$1.09	\$1.10	\$1.89	\$0.13	\$0.44	\$0.43	\$0.64	\$1.70	\$1.82	\$1.85
EPS (as reported)	(\$0.67)	(\$0.52)	(\$0.66)	\$0.20	(\$0.19)	\$0.37	\$0.33	\$0.58	\$1.18	\$1.58	\$1.75
Calendar EPS	\$1.20	\$0.80	\$1.25	\$2.10					\$1.68	\$1.90	\$1.83
Weighted average shares outstanding (diluted)	74.8	74.8	74.8	75.2	105.5	126.0	128.5	131.0	122.8	129.4	127.1
MARGIN ANALYSIS:											
Gross profit	37.7%	37.7%	36.5%	37.31%	34.8%	37.6%	37.7%	38.2%	37.1%	37.9%	38.0%
SG&A	14.6%	14.8%	13.5%	13.6%	14.8%	12.8%	14.0%	11.5%	13.2%	13.4%	13.2%
EBITDA	23.1%	22.9%	22.9%	23.7%	19.9%	24.8%	23.7%	26.7%	24.0%	24.5%	24.8%
Depreciation	5.7%	5.6%	6.0%	5.5%	5.7%	5.2%	4.6%	4.0%	4.8%	5.7%	5.6%
Amortization	1.9%	2.0%	2.4%	2.3%	2.7%	2.5%	2.4%	2.0%	2.4%	2.3%	2.3%
Depreciation & amortization	7.5%	7.7%	8.5%	7.8%	8.4%	7.7%	7.0%	6.0%	7.2%	8.0%	7.9%
Operating income	17.4%	17.3%	16.9%	18.2%	14.3%	19.6%	19.1%	22.8%	19.1%	18.8%	19.2%
Tax rate (adjusted)	27.2%	25.8%	18.2%	15.7%	44.6%	14.5%	13.0%	13.0%	16.5%	17.0%	23.6%
Net income	4.8%	4.8%	4.6%	7.8%	3.2%	12.3%	12.3%	16.4%	11.4%	12.4%	11.8%
GROWTH RATES:											
Revenue	3.5%	10.6%	6.2%	1.5%	1.0%	3.43%	-0.5%	-0.8%	0.7%	3.7%	4.8%
Revenue (excl. foreign exchange effect)			0.0%	2.2%	1.2%	8.3%	7.3%	7.2%	6.1%	5.8%	
Revenue (organic)			6%	2%	1.2%	6.3%	6.3%	6.3%	5.5%	5.6%	5%
Gross profit	12%	11%	3%	4%	6%	5%	-1%	-6%	0%	6%	5%
SG&A	10%	12%	-3%	2%	13%	-16%	-4%	0%	-3%	5%	3%
EBITDA	12.6%	9.7%	6.3%	4.8%	1.5%	20.9%	0.7%	-8.9%	1.9%	6.2%	5.8%
EBITA	18%	10%	4%	9%	7%	34%	5%	-8%	6%	2%	7%
Net income (excl. non-recurring items)	56.2%	9.9%	1.3%	73.0%	-1024.8%	100.1%	42.9%	9.5%	47.0%	12.7%	-0.3%
Net income (WB Calculation)	55.6%	7.7%	-8.0%	67.8%	60.9%	159.5%	54.4%	11.2%	48.3%	13.5%	8.3%
EPS (excl. non-recurring items, incl. options)	56.2%	9.9%	1.3%	72.2%	-755.5%	18.8%	-16.8%	-36.2%	-10.0%	6.9%	1.6%
Diluted shares outstanding	0%	0%	0%	0%	41%	68%	72%	72%	63.33%	5.43%	-1.81%

Source: Company reports, FactSet, and William Blair & Company, L.L.C. estimates

William Blair & Company, L.L.C.

IMPORTANT DISCLOSURES

William Blair was a manager or co-manager of a public offering of equity securities for Catalent, Inc. within the prior 12 months.

William Blair is a market maker in the security of Catalent, Inc.

William Blair intends to seek investment banking compensation in the next three months from Catalent, Inc.

Within the past 12 months William Blair has provided or is providing investment banking services to or has an investment services relationship with Catalent, Inc.

Additional information is available upon request.

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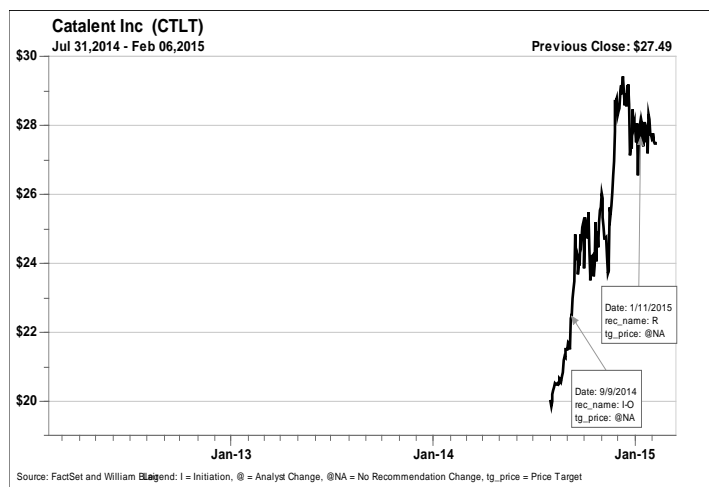
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DOW JONES: 17,862.14

S&P 500: 2,068.53

NASDAQ: 4,801.18



Current Rating Distribution (as of 01/31/15)

Coverage Universe	Percent	Inv. Banking Relationships*	Percent
Outperform (Buy)	64	Outperform (Buy)	16
Market Perform (Hold)	32	Market Perform (Hold)	2
Underperform (Sell)	2	Underperform (Sell)	0

*Percentage of companies in each rating category that are investment banking clients, defined as companies for which William Blair has received compensation for investment banking services within the past 12 months.

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