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Zoetis Inc. (ZTS) CEO Juan Ramon Alaix on Q3 2019 Results - Earnings Call Transcript

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Q3: 11-07-19 Earnings Summary

Press Release SEC *10-Q*

EPS of $0.94 beats by $0.05 | Revenue of $1.58B (7.03% Y/Y) beats by $4.89M

Earning Call Audio

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Zoetis Inc. (NYSE:ZTS) Q3 2019 Earnings Conference Call November 7, 2019 8:30 AM ET

Company Participants

Steve Frank - VP of IR

Juan Ramon Alaix - CEO

Glenn David - CFO

Kristin Peck - Upcoming CEO

Conference Call Participants

Kevin Ellich - Craig-Hallum

Louise Chen - Cantor Fitzgerald

Erin Wright - Credit Suisse

Christopher Schott - JPMorgan

Michael Ryskin - Bank of America

Jon Kaufman - William Blair

Jon Block - Stifel

David Westenberg - Guggenheim Securities

David Risinger - Morgan Stanley

Prakhar Agarwal - UBS

Nathan Rich - Goldman Sachs

Kathy Miner - Cowen & Company

Gregg Gilbert - SunTrust

Operator

Welcome to the Third Quarter 2019 Financial Results Conference Call and Webcast for Zoetis. Hosting the call today is Steve Frank, Vice President of Investor Relations for Zoetis.

The presentation materials and additional financial tables are currently posted on the Investor Relations section of zoetis.com. The presentation slides can be managed by you the viewer and will not be forwarded automatically. In addition, a replay of this call will be available approximately two hours after the conclusion of this call via dial-in or on the Investor Relations section at zoetis.com.

At this time, all participants have been placed in a listen-only mode and the floor will be opened for your questions following the presentation. [Operator Instructions] In the interest of time, we ask that you limit yourself to one question and then queue up again with any follow-ups. Your line will be muted, when you complete your question. [Operator Instructions]

It is now my pleasure to turn the floor over to Steve Frank. Steve, you may begin.

Steve Frank

Good morning everyone and welcome to the Zoetis third quarter 2019 earnings call. I'm joined today by Juan Ramon Alaix, our Chief Executive Officer; Glenn David, our Chief Financial Officer and also by Kristin Peck, our CEO-elect.

Before we begin, I'll remind you that the slides presented on this call are available on the Investor Relations section of our website and that our remarks today will include forward-looking statements and that actual results could differ materially from those projections.

For a list and description of certain factors that could cause results to differ, I refer you to the forward-looking statements in today's press release and our SEC filings, including but not limited to our Annual Report on Form 10-K and our reports on Form 10-Q. Our remarks today will also include references to certain financial measures, which were not prepared in accordance with Generally Accepted Accounting Principles or U.S. GAAP. A reconciliation of these non-GAAP financial measures. For the most directly comparable U.S. GAAP measures is included in the financial tables that accompany our earnings press release and in the Company's 8-K filing dated today, November 7, 2019. We also cite operational results which exclude the impact of foreign exchange.

With that, I will turn the call over to Juan Ramon.

Juan Ramon Alaix

Thank you, Steve. Good morning everyone.

Today, you will hear commentary on the market dynamics and quarterly result from me and Glenn. I am also pleased to have a Kristin Peck our next CEO joining us to share some remarks with her appointment in the future of Zoetis.

As we near the end of the year, let me provide some context around recent market dynamics. The animal health industry in 2019 as we may facing a challenging year for swine and cut off while we have seen a very good performance in companion animal and poultry.

We have seen growing an appetite in the companion animal market for a spending on innovation and pet care and we once again expect to grow much faster than the market in companion animals for 2019.

We are excited by the new products and lifecycle innovations giving them more advance ways to assist pet owners, weakened skin conditions and parasites. The pathology treatment continues to be a critical need. And Zoetis has been rewarded for the innovation we have developed in this space, we have continued market penetration and our goal expansion of our key dermatology products Apoquel and CYTOPOINT, they are on track to achieve more than $700 million in sales for 2019.

In recent years Zoetis has also been a strengthening its position in parasiticides. This year we added two new products to our parasiticide portfolio, Revolution Plus to protect cats against ticks, fleas and internal parasites and ProHeart 12 once yearly injection to prevent heartworm disease in dogs.

Additionally, we are planning to launch Simparica Trio in the European countries and Canada in the first quarter. In the U.S. we expect the FDA to complete the review of Simparica Trio at the end of the first quarter. If approved, we will launch shortly after. Based on these assumptions, we project to generate incremental global sales of Simparica Trio in 2020 at around $150 million.

In other areas like pain, alternative to existing treatment for dogs and cats we've spent a significant opportunity. And in the case of GILTI tax, it is a largely unmet need today. We are excited by the potential for our researcher programs we have monoclonal antibodies in this area.

As I mentioned in the last quarter, we initiated the filing process in the EU and U.S. for a new fee line monoclonal antibody candidate to treat osteoarthritis, pain in cats and we have recently also initiated the filing process in the EU and U.S. for a canine monoclonal antibody candidate to treat osteoarthritis pain in dogs. If approved, we would anticipate this product coming to market in 2021.

Meanwhile, African swine fever trade uncertainties and weather conditions affecting mainly U.S. cattle, having a significant negative impact on the livestock market. As a result of this negative impact, we expect the overall animal shelter market to grow rationally between 3% to 4% in 2019 compared to 5.6% in 2018. And as note in our guidance, we expect to outpace the market with operational growth in revenue over 6% to 7% and this excluding the positive impact of Abaxis.

Turning now to our third quarter results. We continue our strong performance with 9% operational revenue growth in the third quarter driven by sales of our companion animal and poultry products. Our companion animal portfolio continues leading the way, we had 23% operational growth based on strong sales of our parasiticides, our key dermatology products and diagnostic portfolio.

Diagnostic revenue from the Abaxis acquisition accounted for 2% of the overall growth. In terms of the livestock, we saw an operational decline of 4%. Growth in poultry was 5% but it was offset by declines in cattle mainly due to lower feedlot placements in the U.S. and the impact of African Swine fever in China.

Our third quarter result demonstrate how our diverse portfolio and focus on meaningful innovations are driving our success. These trends remain the condition of our consistent and long-term performance. In the third quarter, we grew our adjusted net income by 10% operationally.

And we continue to benefited from increase in revenue, improved gross margins and moderate growth in operating expenses. We remain confident in our latest innovation, future pipeline and core business before future growth and deliver our 2019 guidance which Glenn will discuss later.

As we look ahead, we are making good progress with innovations and investment that will generate our future growth. As I said, we are preparing for the launch of Simparica Trio in European markets and Canada at the beginning of next year with the product currently in production.

All regulatory reviews remain underway in Australia, Brazil, and Japan with a further submission expected in China and Mexico. In the U.S., we have been expanding our field force to better support our growing companion animal portfolio including the diagnostic products and in preparation for the launch of Simparica Trio next year once approved.

We also continue to enhance our vaccine portfolios for livestock. In October Zoetis received USDA approval for Poulvac, Procerta, HVT-ND, the companies first vector vaccine for poultry. It will help to protect against both Mareks disease and Newcastle disease, highly contagious and infection for poultry. The product complements our market leading innovative vaccine delivery system for poultry producers and it is the first in what is expected to become an important new global vaccine franchise for Zoetis over the next several years, especially in international markets.

We are also taking important first steps to address African Swine Fever having reached a non-exclusive license agreement with the U.S. Department of Agriculture in late September. This agreement gives us access to three patents and materials related to African swine fever vaccines strengths that will be incorporated into our research.

While it could take several years to complete the development our licensing of our vaccine, our work with the USDA another partner provides a comprehensive approach to addressing these three infectious diseases.

In addition to new products approval and lifecycle innovations, Zoetis continues to support future growth through business development activities. Last week we announced the acquisition of Phoenix Lab, Seattle based reference laboratory that is highly valued by veterinarians for quality assurance and customer care.

The Zoetis has first entry to the veterinary reference laboratory space and it is expected to further strengthen our overall diagnostic portfolio, building of our 2018 purchase of Abaxis, a leading provider of a point-of-care diagnostic instruments. We view reference labs as another important part of our comprehensive diagnostic offering and we plan to build our presence in reference lab over time to organic expansions and other small acquisitions in this space.

Now I would like to say a few words regarding our leadership transition. As we announced in October, I am retiring at the end of the year. This has been an amazing opportunity to be in a company like Zoetis over the last seven years.

And I feel very positive about the Zoetis future based on our proven strategy, hard and track record of execution, the diverse and innovative portfolio that underlies our success with customers and the growth investment we are making for the long-term.

I am confident our talented colleagues and management team led by our next CEO Kristin Peck will continue to capitalize growth opportunities ahead of Zoetis and create significant value for our company, customers and our shareholders.

Kristin has been with the company since the beginning of Zoetis and currently serve as Zoetis Executive Vice President and Group President of U.S. Operations Business Development and Strategy. I worked with Kristin for many years, I note that she is the right leader for Zoetis next phase of our growth and industry leadership.

She's a strong advocate for our customer needs, a champion offers Zoetis culture and values professional and collaborative leader for our people and industry. The track record of a strong performance through her tenure at Zoetis as well as her operational experience, innovative strategies and deep customer knowledge positions her well to drive Zoetis continued growth. She will build on our long-term study which she felt to develop alongside with the rest of the Zoetis management team and bringing her own vision leading the next stage of Zoetis journey.

I will remain an advisor to Zoetis during the course of 2020 and Kristin and I are already working closely to ensure a smoother transition and maintain the momentum of our business growth.

Before Glenn to discuss our third quarter results, I have asked Kristin to say a few words. Kristin?

Kristin Peck

Thank you, Juan Ramon.

I'm honored to be named the next CEO of Zoetis and I look forward to leading our Company into its next phase of industry leadership and value creation. I want to thank Juan Ramon for establishing Zoetis as the world's leading animal health company. I have deep respect for Juan Ramon and its track record of creating value for our customers and for delivering strong returns for our shareholders. His innovative mindset has kept Zoetis at the forefront of the industry and Juan Ramon confidence in our Company's solid foundation and prospects for continued growth.

So when it has a diverse and innovative portfolio, deep expertise in animal health and a winning culture shared by our talented colleagues around the world. We know how to partner with our customers to address their evolving needs across the continuum of care from prediction and prevention to detection and the treatment of disease. We have a promising pipeline of new products and lifecycle innovations and we are focused on making investments in digital technology, data and analytics that will fuel our future growth.

As CEO, I will continue to drive forward with our successful long-term strategy. I will look for opportunities to accelerate our progress in the most meaningful areas for our veterinary and producer customers and I'm committed to building on the strategies, diverse portfolio and financial discipline that have been critical to our success. To that end, I've been working with Juan Ramon, Glenn and the rest of the Zoetis team as well as the Board over the last few weeks to ensure a seamless transition.

As we look ahead, I continue to view animal health as a very valuable sector for investors. With steady growth prospects as the fundamental macroeconomic drivers of global population growth of innovation and a growing middle class in emerging markets, we'll drive growth in both companion animal and livestock. The long-term history of animal health and Zoetis is the testament to the resiliency of our business.

The drivers in pet care and animal agriculture are fundamental to the world economy. And Core to people's connections with animals for both companionship and nutrition. I'm excited by the new opportunities for raising the standard of care with innovative new medicines, biologics and integrations across the continuum of care.

As I prepare for my new role, a key priority for me has been directly connecting with our stakeholders around the world to better understand their perspective and how we can build on our Company's success. I look forward to engaging with many of you as part of this process and sharing more on our outlook for the market and plans for 2020 early next year.

And now Glenn will cover the financials.

Glenn David

Thank you, Kristin and good morning.

Before discussing our Q3 financial results, I first like to congratulate Juan Ramon on his upcoming retirement and welcome Kristi as the next CEO of Zoetis. In his role as CEO Juan Ramon has led our business to a remarkable transformation from a business unit advisor to an independent and publicly traded industry leader in animal health.

Indeed Revenue and adjusted net income growth, well above the market during that period while managing acquisitions and a significant restructuring and from a personal perspective, he supported me to my own transition to CFO during that time as well.

I'm very thankful to have worked with him over the past decade and appreciate that we will continue to benefit from his insight and knowledge as he remains an advisor & Director on the Board. I'm also very excited to work with Christian as he transitions to her new role, building upon Zoetis a strong foundation and delivering the next phase of growth. Christian and I have worked together at Zoetis for many years and we share our commitment to customers, colleague and value creation which is driven our company's success.

Now let's review the financial results. We delivered another healthy quarter with operational revenue growth of 9% and adjusted net income growth of 10%, these quarterly results which built upon our strong performance for the first half of the year give me confidence in delivering on our full-year improved earnings outlook.

For the full-year we are narrowing operational revenue growth at the high end of the range increasing operational growth for adjusted net income and increasing and narrowing adjusted diluted EPS. Reported revenue growth for the third quarter was 7% including a negative 2% impact from foreign exchange. Foreign exchange was primarily driven by the strengthening of the dollar against the Euro, Argentinian peso and the Australian dollar.

Operational revenue growth of 9% for the quarter is driven by 1% price and 8% volume. The volume contribution of 8% includes 3% from key dermatology products, 2% from new products, 2% from legacy Abaxis products and 1% from other in-line products. Breaking down our operational revenue growth by species, companion animal grew 23% partially offset by livestock declines of 4%.

Companion animal revenue growth was driven by our parasiticides portfolio including new products Revolution Plus and ProHeart 12 key dermatology products. the impact of the Abaxis acquisition and growth in emerging markets such as China. Excluding the impact of the Abaxis acquisition, companion animal products grew 20% operationally.

Equine also had strong growth in the quarter benefiting from the acquisition of Platinum Performance, a nutrition focused animal health company. Livestock products declined in the quarter were primarily driven by market weakness in U.S. beef and dairy sectors. The ongoing impact of African Swine Fever and the revenue recovery of the Brazil truck driver strike that increased revenue in Q3 2018. These headwinds were partially offset by growth in poultry.

Our key dermatology portfolio demonstrated continued strength this quarter with sales of $217 million representing 27% operational growth. This is our first quarter with revenue, greater than $200 million. Positive performance in this portfolio was driven by the ongoing expansion of the addressable market, increasing market share and continued uptake of both Apoquel and CYTOPOINT until recently launched markets.

As Juan Ramon mentioned we are clearly on pace to exceed a combined $700 million in revenue this year. New products, especially Revolution Plus and Stronghold Plus as it's known internationally, ProHeart 12 swine combination vaccines 2% to overall growth in the quarter. This growth is net of cannibalization of the original formulations and highlights the success of our investments and lifecycle innovation.

Sales from legacy Abaxis products for $68 million in the quarter represent 10% operational growth over the prior year pro-forma revenue. Other in-line products contributed 1% growth in the quarter including Simparica with $55 million in revenue and 28% operational growth. This growth was partially offset by declines in U.S. cattle and the ongoing impact of African Swine Fever.

Now let's discuss the revenue growth by segment for the quarter. U.S. revenue grew 11% with companion animal growing 26% and livestock declining 9%. Excluding the impact of the Abaxis acquisition, U.S. revenue grew 10%.

Strong companion animal products performance in the quarter were driven by growth of our parasiticide portfolio, key dermatology products and the impact of the Abaxis acquisition. Excluding the impact of legacy Abaxis products, companion animal growth was 25%.

Our parasiticide portfolio including in-line products such as Simparica and ProHeart 6 and new products such as Revolution Plus and ProHeart 12 which launched in the quarter contributed the strong companion animal growth. U.S. dermatology sales were $154 million for the quarter, growing 28%. Growth this quarter was driven by market expansion, increasing market share, returns on direct to consumer investments and price.

Positive companion animal performance was partially offset by U.S. livestock declines in the quarter driven by cattle and to a lesser extent swine. Sales of our cattle products were negatively impacted by unfavorable market conditions in the beef and dairy sectors, while feedlot placements in the quarter impacted sales of our products as well as pricing pressure driven by competition.

While we continue to see good adoption and growth of the Fostera Gold swine vaccine declines in other product sales while it's the lowest swine revenue this quarter primarily due to the timing of promotional activities. These challenges in cattle and swine were partially offset by continued growth in poultry, primarily due to sales of our portfolio of alternatives to antibiotics in medicated feed additives.

In addition, we were able to capitalize on competitive challenges, including lack of efficacy and supply constraints. To summarize, the U.S. business had a very positive quarter with diversity and innovation driving results despite challenging market conditions in the cattle sector.

Our International segment also contributed to growth this quarter with operational revenue growth of 5%. Companion animal operational revenue growth was 16% while livestock declined 1% operationally.

Excluding the impact of the Abaxis acquisition, international revenue grew 4% operationally, companion animal product growth was driven by key dermatology products, the addition of legacy Abaxis products and growth in emerging markets such as China excluding the impact of the Abaxis acquisition companion animal operational growth was 13%.

International livestock declined modestly primarily due to the impact of African Swine Fever as well as an unfavorable comparison to the prior year which included the revenue recovery from the Brazil truck driver strike. Growth in cattle and poultry, partially offset the declines in swine driven by favorable market conditions in key markets including Mexico, the U.K. and Canada while poultry benefited from increased sales in China, Australia and Brazil.

Now, I would like to review in more detail a few markets in the quarter. Beginning with China, revenue declined 9% operationally driven by the ongoing impact of African Swine Fever which was partially offset by continued double-digit growth in companion animal.

Our livestock portfolio declined 40% operational in China driven by swine declines that were partially offset by growth in poultry and cattle. As we indicated in last quarter, we expect the full-year impact of African Swine Fever to our revenue to be approximately $50 million. While the outbreak has continued to spread to other markets in Southeast Asia, our full-year estimate remains consistent.

In the medium to long term, we continue to anticipate that other regions will increase exports of pork and other proteins however, we have not seen increases in productions to any significant extent. Our companion animal products continue to grow significantly in

China increasing 43% operationally. Sales from parasiticides, vaccines and Apoquel were the primary drivers of growth aided by field force expansion and effectiveness.

Moving on to Brazil, sales grew 1% operationally driven by companion animal growth of 17%, partially offset by our livestock decline of 5%. Companion animal revenue growth in Brazil was driven by our key dermatology portfolio including CYTOPOINT which launched in the second quarter as well as growth in Simparica.

Livestock declines in Brazil this quarter were driven by an unfavorable comparison to the prior year when sales were recovered due to the resolution of a national truck drivers' strike that occurred in Q2 of the prior year.

In Mexico, sales grew 22% operationally driven by livestock growth of 15% and companion animal growth of 46%. Livestock benefited from sales of our premium products for cattle while strong companion animal performance was driven by growth in legacy Abaxis products, parasiticides and vaccines.

Other emerging and developed markets also contributed to international growth this quarter, particularly in companion animal driven by parasiticides and key dermatology products. Overall, our International segment continued to perform well, demonstrating the importance of our global diversity and helping to offset the impact of African Swine Fever.

Now moving on to the rest of the P&L. Adjusted gross margin of 70.1% increased approximately 140 basis points in the quarter on a reported basis compared to the prior year. The increase is driven by foreign exchange, product mix and price partially offset by tariffs on certain products and the inclusion of the lower margin legacy Abaxis portfolio.

Total adjusted operating expenses including the impact of the Abaxis acquisition through 6% operationally. The increase is primarily related to compensation-related expenses and investments to support future growth of the business.

The adjusted effective tax rate for the quarter was 20.5%. The increase from the comparable 2018 period is primarily related to the impact of the global intangible low tax income or GILTI tax which is effective for Zoetis in 2019.

Adjusted net income for the fourth quarter grew 10% operationally and adjusted diluted EPS grew 11% operationally, again, outpacing revenue growth. The combination of revenue growth, improving gross margins and disciplined operating expense growth enabled us to deliver strong bottom line results while still investing strategically for long-term sustainable growth.

Now moving on to guidance for the full-year. As a result of our strong performance in the first nine months of the year, we are narrowing operational revenue growth at the high end of the range, raising operational growth for adjusted net income and raising and narrowing the range for adjusted diluted EPS. Please note that guidance reflects foreign exchange rates as of late October.

I'll now walk you through each of the individual line items, beginning with revenue. We are now expecting to deliver revenue between $6.2 billion and $6.25 billion as compared to our previous range of $6.175 billion to $6.275 billion. The dollar decrease in revenue guidance at the high-end of the range is related to unfavorable foreign exchange. Operational revenue growth is now expected to be between 9% and 10% as compared to our previous estimate of 8.5% to 10% reflecting the continued momentum of our companion animal portfolio.

Our organic operational revenue growth which excludes the impact of Abaxis is now expected to be between 6% and 7%. We are now projecting adjusted cost of sales as a percentage of revenue to be approximately 30% compared to our previous range of 30% to 31%. Adjusted SG&A for the year is expected to be between $1.525 billion and $1.55 billion compared to our previous range of $1.505 billion to $1.545 billion.

The increase in narrowing at the high-end of the range reflects our focus on critical investments to support revenue growth including promotional activity on key companion animal products. Adjusted R&D expense for 2019 is now expected to be between $445 million and $455 million for the year compared to our previous estimate of $450 million to $465 million. The decrease was related to the timing of project spend.

Our full-year adjusted interest and other income deductions is expected to be approximately $190 million and our full-year adjusted tax rate is expected to be approximately 20% which are both consistent with previous estimates.

Adjusted net income is now expected to be in the range of $1.72 billion to $1.745 billion representing an increase of $10 million at the high end of the range. The updated adjusted net income range represents operational growth of 11% to 14% compared to previous range of 9% to 12%. The improved outlook for adjusted net income is primarily driven by gross margin favorability.

We are also increasing our adjusted diluted EPS to a range of $3.57 to $3.62 compared to our previous guidance of $3.53 to $3.60. Our range for reported diluted EPS is increasing and narrowing now expected to be between $2.99 to $3.08 based upon operational increases. Our previously estimated range was $2.93 to $3.04.

We expect approximately $450 million to $475 million in capital expenditures this year with increased investment in information technology and manufacturing to support our Abaxis acquisition, improve cost efficiencies and increased capacity. We anticipate continuing an elevated level for the next few years as we invest in manufacturing and infrastructure to support future growth and product launches.

We also repurchased approximately $450 million of Zoetis shares in the first nine months of the year. We have $1.9 billion remaining under the multi-year share repurchase plan that was approved last year and we remain committed to our capital allocation priorities of internal investment, M&A and returning excess cash to shareholders.

Our guidance for reported and adjusted earnings per share reflects the shares repurchased through the end of Q3. While we not provide guidance for 2020 until February, we view next year as a continuation of strategic investment to support recent and future product launches, our recent acquisitions including Phoenix Lab and Platinum Performance and other strategic priorities.

Now to summarize before we move to Q&A. We have consistently delivered strong top and bottom line growth in the first nine months of the year despite market challenges in cattle and swine. We are narrowing our outlook the operational revenue growth at the high end of the range and we are increasing and narrowing our outlook for adjusted net income and adjusted diluted EPS reflecting the strong performance year-to-date.

And our investments in R&D, diagnostics integration, manufacturing capabilities and field force expansion will provide a solid platform for continued growth in 2020 and beyond.

Now, I'll hand things over to the operator to open the line for your questions, operator?

Question-and-Answer Session

Operator

[Operator Instructions] We'll take our first question from Kevin Ellich with Craig-Hallum. Please go ahead.

Kevin Ellich

Good morning. Juan Ramon, it's been great working with you and I hope you enjoy your retirement and get the play a lot of golf.

Juan Ramon Alaix

Thank you.

Kevin Ellich

Congratulations. We all know you're going to do a terrific job succeeding Juan Ramon. The questions I have first, I think you guys talked about some Simparica Trio saying that your assumption is if it's approved in the U.S. by the end of Q1, revenue would be about $150 million in 2020 did I get that right?

Glenn David

Yes. The incremental sales that we expect for Trio over our existing portfolio is $150 million.

Kevin Ellich

And what is the underlying assumptions there Glenn in terms of pricing, how much will come from the U.S. versus international and how much cannibalization?

Glenn David

So in terms of the breakout between U.S. international like we've set all along, we expect the majority of the sales for this product to be in the U.S. I really want to go into details on price from a competitive perspective at this point but like we said we do expect it to be priced significant premium to Simparica and the cannibalization impact obviously there'll be some cannibalization to Simparica but we also expect to take significant share from competition.

Operator

We'll take our next question from Louise Chen with Cantor Fitzgerald.

Louise Chen

So Juan Ramon, we will miss you and Kristin and congratulations on the new role. My first question is for you, Kristin, as the new CEO of Zoetis what will you do differently from Juan Ramon? And then also just on 2020, I know you're not giving guidance till February but how should we think about the pushes and pulls as we look into next year? Thank you.

Kristin Peck

Sure. Thanks so much Louise. I'm going to be focused on really continuing the strong path of value creation. If you look at the strategy that we've had over which I feel actually is delivered significant results both for our customers and for our shareholders. It is been a dynamic strategy that has always been predicated on continuous innovation and disruption which I think is really would have helped us stand out.

It's also been characterized by a great diversity of our portfolio and my goal is to maintain that strong momentum to stay ahead of competitors. I think if I look into 2020 and 2021 and beyond, I'm really going to be focused on innovation, making sure we continue to bring to market products that really solve both our customers and animals' challenges.

I will continue to relentless focus on our customer making sure that we're finding ways to make their job easier to do and to make them more productive. And I'll be looking for better leverage our digital and data both to make us more efficiently internally as well as to drive better productivity and greater growth in some of our data and digital revenue products both in diagnostics and precision livestock farming. So that will be my focus as we look into 2020 and some of the sources of where I think you'll see our continued growth.

Glenn David

And in terms of the pushes and pulls for 2020, starting with the revenue line, where we continue to see good momentum in our companion animal business and particularly with the expected launch of Simparica Trio subject to approval, we expect to see very strong performance there as well as the continued growth in some of the new products that we launched this year such as ProHeart 12 and Revolution Plus.

Also, when you take into account the impact of African Swine Fever that we had this year, we would expect that to stabilize this year and not to be a negative detractor to growth in 2020 so that should benefit us as well. When we look at the expenses, obviously there'll be some investments to support our new product launches.

We want to make sure that we get those products off to a strong start and also some investments to support the recent acquisitions that we have in place. So overall, we would expect revenue to grow faster than the market again in 2020 and we would expect that we able to grow our income faster than revenue.

Operator

We'll take our next question from Erin Wright with Credit Suisse. Please go ahead.

Erin Wright

Great, thanks and Kristin congrats, Juan Ramon as well. It's obviously been very, very nice working with you. I had a quick question on Simparica Trio - $150 million in 2020, it's a little bit higher I guess than what we were contemplating on a net basis, I just want to confirm some of the assumptions that you're making, does it assume that you launch ahead of ZeoMAX and does it assume that you'll be the only player in the U.S. and does it also assume of puppy indication or other label caveats from a safety perspective. A separate question here, but can you also speak to the diagnostic strategy in the reference laboratory market. I guess how quickly can you scale up the U.S. lab footprint and what are some of your plans internationally from a reference lab perspective as well? Thanks.

Juan Ramon Alaix

So, Kristin will answer all this question, so please Kristin.

Kristin Peck

Sure, so starting with Trio. We do not expect to be launching ahead of ZeoMAX and Western vet but we do expect to be launching ahead, a very important Q2, Q3 parasiticides season. So I think we will not be there but I do think if you look at the $150 million to your point, we still expect to deliver a very strong year there.

We do expect to get puppy claim that is part of the assumptions that is in there that's obviously subject to back to approval but that is our going in assumption as we look at that. So as I move towards the reference lab, we continue to believe that diagnostics is an important part of our go-forward portfolio.

It is critical to that and as a part of their business that will stay there, we think it enhances as Zoetis is currently value proposition and is a great complement to our existing portfolio, it's a large and very fast growing market. As the market has been growing at 10% plus, we strongly believe that we can accommodate a third player.

We've also known the customers that we're looking for a third-party alternative and if you look and different MSAs shares of third-parties have actually been significant as our acquisition of Phoenix demonstrates, they had over 50% share in the MSA they operated in. Our plan in this space is to invest both organically and inorganically over the next few years and we remain committed to the space.

Operator

We'll take our next question from Christopher Schott with JPMorgan. Please go ahead.

Christopher Schott

Great, thanks very much for the question. I guess my first one was on Apoquel and CYTOPOINT ex-U.S., can you just provide any additional color in terms of where penetration rate stand in some of the bigger markets in terms of Europe, Brazil, et cetera and where do you think those penetration rates can go over the next several years? And my second question is, sorry I keep going back to $150 number but I'm still not quite clear, can you help me understand again how much of that 150 is incremental revenue on top of what you're parasiticide business is already doing as compared to erosion from I guess legacy Simparica and some of your heart products et cetera. I'm trying to understand the magnitude of overall growth I should be thinking about for parasiticides next year. Thank you.

Juan Ramon Alaix

Glenn will provide some data related to the penetration range and also details of the 150, how much is [indiscernible] revenues.

Glenn David

So when you look at Apoquel and CYTOPOINT particularly in the U.S., we see that we are plus 60% share in that market. The data internationally is not as clear in terms of, we don't get the same level of data but we know we're not at that penetration rate. Also we've launched Cytopoint later international than we do in the U.S. so we do think we have continued uptake there.

So we do see significant opportunities in international if you continue to gain share as we move up to similar levels that we have in the U.S. We also see continued opportunities in the U.S. as we continue to expand that market and raise disease awareness of dermatology and atopic dermatitis. So we see continued opportunity in the U.S. as well.

In terms of $150 million revenue for Simparica Trio, I want to be clear that is incremental sales overall what we see for Simparica alone and that does include the cannibalization effect. So we would expect greater sales of Trio then $150 million as a stand-alone product.

Operator

We'll go next to Michael Ryskin with Bank of America. Please go ahead.

Michael Ryskin

And I want to mirror the earlier comments, congrats Juan Ramon. It's been great working with you and Kristin look forward to working with you going forward. Two quick questions from me, one on some of the moving pieces in the quarter and sort of looking forward, I would say one of the bigger surprises this year has been in the entire market not just very specifically but some of the challenges in U.S. livestock, particularly given the negative tone of ASF internationally, there is an expectation that you will see some stabilization in U.S. livestock in the market in cattle and swine.

And it's been a little bit slow probably slower expected this year, if you look back in the line months earlier. How do you see some of these dynamics playing out? We talked about ASF internationally but if you think about the cattle herd in the U.S., some of the feedlot pressures that we've seen this year in terms of placements, if you could talk automatically sort of over that six months to 12-months.

And then a quick follow-up on the seasonality question, you talked about the Simparica Trio approval likely end of 1Q early 2Q launch, could you talk about the timing that you think about the vet purchasing a lot of the ordering by that's happens relatively early in the year. So how much wiggle room do you have built-in and how quickly can you ramp up manufacturing to make sure that you don't miss a fleas season if there is a month or two movement either way there.

Juan Ramon Alaix

Let me answer the question on Simparica Trio and then Kristin will cover the trends and also the challenge that we have seen in the U.S. livestock and we also talked about the African Swine Fever. We expected approval in late first quarter from FDA and then shortly after we launched the product in the market. We are thinking already they are prepared to step to ensure ample supply of the product as soon as we obtain approval in the U.S.

So we don't think that the supply will be efficient in terms of capturing the opportunities of the high season that it's mainly in the Q2 following the Q3. We are confident that we told earlier we are making now it is probably is approved by the FDA, we will be able to generate a significant opportunity for Simparica as we are in 2020.

So moving into the U.S. livestock, Kristin?

Kristin Peck

Sure. As you saw our numbers both dairy and beef in the U.S. continue to be weak. As we said in previous conversations in previous quarters, we expect this to continue for the rest of the year. From a dairy perspective and we've seen depressed milk prices versus historical trends which has limited producer profitability income and in the last few months there has been a small improvement in pricing but it's not yet sustained enough we believe for producers to believe recovery M&A and to start investing significantly.

On the beef side, we're at the end of what's been a very long expansion period. So we are expecting a little bit of contraction or flattening out over the medium term. As you look at beef, there has also been a lack of innovation that has driven significant pricing and competitive pressures.

We had a wet spring which had good past through this year which is kept cattle out longer and as you've seen there's been a significant increase in some of those prices and live cattle prices, which has encouraged them to wait of their animals were heavier and older to put them in the feedlot.

So as we look at U.S. cattle, I think we'll continue to see challenges of there as we look into next year. And as we look at ASF as we've spoken about previously, we believe with China specifically, we see about a $50 million impact across the Zoetis primarily based out of China. As we look into next year, we are hoping for that to stabilize and we are hoping to see some recovery moderate but obviously that remains to be seen based on how that goes. But we do see offsets were the Chinese swine.

We are expecting imports from EU, Brazil and the U.S. both in swine as well as across other proteins to help compensate that we've seen significant price increases in pork globally. We see Brazil and EU probably best positioned to take some of this, but I think overall, it seems certainly enough in the U.S., the U.S. will also go after trying to get a greater share of. So we remain quite committed but I think what we believe that the impact of ASF should flatten out as we look into next year. So hopefully that explains.

Operator

We will go next to John Kreger with William Blair. Please go ahead.

Jon Kaufman

This is Jon Kaufman on for Kreger. Juan Ramon, we wish you well and Kristin congrats on the new role. One of your competitors has talked a lot recently about the importance of alternative channels. Can you guys talk a little bit about that? How important are the online and the mass market retail channels for you today? How has your strategy evolved here over the past year or so and as you think about the future outlook for the company, how much of the growth, do you think will come from these alternative channels? Thank you.

Juan Ramon Alaix

We have seen Jon the changes on the how vet owners are getting that product from different channels, we have seen that mainly the U.S., but also in some other markets there are changes but really having an impact into the veterinary space but Kristin will provide much more color on how things are changing in the U.S. as these affecting the market, affecting manufacturers, affecting alternative channels, so Kristin do you want to provide some comments please?

Kristin Peck

Sure. I would certainly. If you look at our portfolio is the contrast of other is the majority of what we sell requires a prescription. So our goal is to work with vet to make our product available to pet owners in a way that works best for them.

And what we've seen is in the areas such as parasiticides and chronic medications, many pet owners have looked more to buy their products from e-commerce and retail and as such we've evolved our own strategy to work more directly with e-commerce and retail. We implemented as we discussed on previous calls the minimum advertised price or Matt pricing which is an agreement with all e-commerce and retailers to ensure that they cannot advertise our products beyond a certain price.

This has allowed us to legitimately sell our product, eliminate some of the great market and provide veterinarians and pet owners the convenience to fill their prescriptions where and how they want. This I think is an evolving thing so just to give you context still 50% of what we sell we'll have to remain no matter what in the clinic.

It's definitely expanding quickly but still on a relative basis is still a small part of our business today, but something we're monitoring closely and we're making sure that we continue to develop and enhance our capabilities to best serve this new channel as we move forward.

Operator

We'll go next to Jon Block with Stifel. Please go ahead.

Jon Block

And maybe just a handful of small questions most of is clarification. So first clarification for companion animal, did you guys see both canine and theme line labs both targeting U.S. approval in 2021 one, a clarification for ASF I was a little mixed up there is the thought that the drag for 2020 will be less than the $50 million incremental hit in '19 but you still think there could be additional incremental headwinds for 2020?

And then lastly, Glenn, not going into 2020 guidance on you but just only we think about that COGS in sort of hitting that 70% bogey for 2019 which is certainly impressive. I would think you still going to have a favorable mix shift in 2020 is companion grows faster than livestock based on all the commentary but do somebody investments in manufacturing offset that. Thanks guys.

Juan Ramon Alaix

Thank you, John. Let me confirm that we have to file both antibodies for cats and dogs in EU and the U.S. and we expect to launch in 2021 of these two products in the U.S. Moving into the African Swine Fever, the assumption that we are making on the comments that we provided today is we are assuming that there will not be a further spreading of African Swine Fever outside of China.

We have seen that cases in the Southeast Asia, Korea, the Philippines to a lesser extent also in Eastern European markets. But we expect that customers now are improving that vital security and they are protecting better against the African Swine Fever.

We are not expecting that China to continue growing in terms of cases may be an opportunity to slight increase in production in China and definitely we see the opportunity in other markets to compensate the gap that have in terms of supply of meat into the Chinese population with more production from Brazil, European markets, Spain, Germany and some other markets, Canada and the U.S. and this is something that in our opinion will help also to generate that growth in livestock in 2020.

So moving into the third question, in terms of gross profit Glenn, you want to cover that?

Glenn David

Yes, so John your thoughts on gross margin. When you look into 2020 there should definitely be a favorable mix impact as we would still expect companion animal to grow faster than livestock in 2020. Just one thing to note on that Trio being the first year of product launch will not be as favorable to gross margin as the rest of the companion animal portfolio we typically be. Over time we do expect that product to have very favorable margin.

But with the first year of launch there is always learnings and efficiencies that will be delivered over time. The other thing to take into account is that FX had a very positive impact in 2019 our overall gross margin. We would not expect it to be positive in 2019 probably be somewhat of a detractor in 2012.

Operator

We'll go next to David Westenberg with Guggenheim Securities. Please go ahead.

David Westenberg

I echo the congratulations. So just in terms of market sizing up, can you help us size the market for the cat opportunity given that there is no existing market? just any sort of framework so that we can think about in terms of there would be population age, et cetera.

And then secondly, a competitor called out the ASA-African Swine Fever vaccine market is a multi-billion dollar market. Can you maybe give us a framework on the size of that as well? Do you agree with that assessment? What are the puts and takes there? Thank you.

Juan Ramon Alaix

Okay, so let's me provide some comments on the market size for cat and local antibodies. So first, there is no any specific product today in the market developed specifically for cat. We know that the number of cats, it's lower than the number of dogs and even more the number of medicalized cats it's even lower than the number of medicalized dogs in the U.S. and also worldwide. If I compare the market of dogs in terms of managing their pain it's about $400 million to $500 million worldwide.

So with the comments I made in terms of medicalization rates and the number of cats, you should expect that the market potential for cat in pain is lower than these $400 million to $500 million. But the advantage is that we will be entering into a space that there is no any clear product addressing that pain in dogs and that we think that we can generate a significant growth opportunity in these areas.

Then how big is the African Swine Fever market? Well, I don't know if the question is related of how much has been the impact on the African Swine Fever and the vaccine. Well, I think it's something that it is reaching because definitely we see a significant opportunity in China, developing this vaccine but also not only in China that we have already the disease but also, they need to protect African Swine Fever in other markets.

We are convinced that this can be one of the top vaccine products worldwide, more than FMB or even more than PCV2. So the opportunity for developing a vaccine in this area is significant.

Operator

We'll go next to David Risinger with Morgan Stanley. Please go ahead.

David Risinger

And me please add my congrats to you both Juan Ramon and Kristin. So my two questions are first, with respect to U.S. tick, could you help us understand what percentage of the U.S. dog market needs tick coverage. Obviously, there are no ticks in the south, I just don't know what percentage of dogs reside in tick infested areas in the country? And then second, could you comment on livestock pipeline launch opportunities in the next year or so? Thank you.

Juan Ramon Alaix

Thank you, David, Kristin?

Kristin Peck

Sure. If you look at, U.S. tick average, very significant tick coverage across the United States. There are different ticks. In the South, you might see more of a Gulf Coast tick which is actually a very difficult tick to treat [indiscernible] tick in the North. So we do believe that most pets in the United States needs a comprehensive tick protection. There may be some geography where there's not a lot but I think there may varies a tick but insect protection is critical we move across the U.S.

As we think about our livestock population opportunity, as you saw in the press release, we are quite focused on driving innovation across livestock. We announced a partnership with Colorado State. So look at antibiotic alternative to the livestock space. We're also really focused on immuno therapies in livestock as alternatives to antibiotics and are excited about some projects there as well.

We're also looking at precision livestock farming can make producers more productive and to better predict animal looking sick. We are also excited in the area of genetics where we can breed healthier animals that are also more productive. And as we've talked about in previous calls looking through diagnostics to bring more shoot side farm side diagnostics across that.

Operator

We'll go next to Mavin Jacobs with UBS. Please go ahead.

Prakhar Agarwal

This is Prakhar on for Mavin. I had two questions. First on Simparica Trio, one thing we are hoping to get more clarity on is around duration of therapy, so tick free products are more seasonal which is not typically the case with hard one product. So how are you thinking about the duration of therapy for Simparica Trio? Do you expect this to be predominantly used in the tick season or good duration of therapy, be more? And secondly on Abaxis you've talked about expansion into OES markets are the key opportunity so could you provide an update on the expansion plan and have you identified target markets or regions that might be ideal and longer term could Abaxis reach similar size in international markets and the U.S. market. Thank you.

Juan Ramon Alaix

Thank you very much for the two questions. So let me answer the duration of therapy. One thing is that what should be the duration of therapy that we believe that it should be in many of the markets are 12 months. And what is the actual duration of therapy that is probably three or less month. So a significant opportunity in terms of compliance and we may see some high season for ticks and fleas depending on the warmer weather but they need to protect animals goes going across the year and definitely in the case of a high warm, it's a 12-month the need of protecting against these type of disease.

And I like Kristin to talk about our budgeted rate expansion plans both U.S. and international.

Kristin Peck

Sure. When we announced back since there, we talked a lot about the fact that we think we can continue to operate the business in the U.S. much better and drive more efficiencies and drive growth but acknowledged that the competition in the U.S. is a little steeper. As we look into international, we strongly believe in international, there are significant growth opportunities. It's more of a blue ocean with a much more fragmented base. The use of diagnostics also varies dramatically by market.

We're very focused on and building our own direct demand generation field force which is really being lacking across most companies, the operator international we looked at 2019, as we've talked about for Abaxis as a platform year to really establish ourselves there and we plan to move to direct distribution from some of our existing distributors across most markets as we look into 2020.

So we do think there is a significant opportunity in Abaxis to reach us by a similar if not higher share than we have in the U.S. just given it is a less mature market with much more fragmentation but it will require a market by market approach.

Operator

We'll go next to Nathan Rich with Goldman Sachs. Please go ahead.

Nathan Rich

Thanks for the questions and let me also offer my congratulations. On the triple combo, have you guys gotten feedback from the FDA just on where they are in their review process and kind of what is driving your expectations for maybe a little bit later of an approval than you originally expected. And then can you also talk about the timing for a submission. And when you would expect approval for the triple combo in China and some of the other geographies that you mentioned like Mexico?

Juan Ramon Alaix

Let me make some comments about the process of approval in the U.S. There is something which is part of the normal process of questions and answers. We get there some additional requests for information from FDA, not related to safety or efficacy and we already answered these questions and now we are waiting for the feedback and we expect the final decision on Simparica Trio by late first quarter next year. But there is something that is part of a regulatory discussion with many of the regulatory authorities across the globe. We said before that we were expecting approval and launch in the first quarter.

We have already obtained approval in Europe and Canada and we have the first quarter in these markets. And we'll be ready for launching shortly after approval in the U.S. And as I said, we are already taking the steps to have ample supply to meet the market needs in the 2020 always base with the assumption that we provided that today of these 150 additional revenues in Simparica sale.

And then you also ask about approval time in China. These unfortunately something that at this point, it's difficult to answer. We are preparing the filing in China and then after the filing probably we will get a little bit more clarity on the timing and we expect that to launching in this market.

So first we intend to launch Simparica as a single item in China and then also CYTOPOINT that is another important product that we plan also to launch in China and then later we'll be launching Simparica Trio. So even if it will take maybe some years, we have products that are coming into the market in China that will generate very positive growth momentum in this market. Next question please.

Operator

Our next question is from Kathy Miner with Cowen & Company. Please go ahead.

Kathy Miner

First again Juan Ramon and Kristin congratulations to you both. Just a couple of questions, first on the canine pain map that you filed. Can you tell us if that is the compound that you acquired from Nexvet a couple of years ago? Second, I noticed that fish sales were down 9% this quarter and that's somewhat unusual that's been a growing market. Is that something temporary or is there a change in the outlook? And last question when we look at African Swine Fever, I think it took everyone by surprise, are there any other diseases that you're monitoring that could impact your business over the next three to five years? Thank you.

Juan Ramon Alaix

Thank you for the question. So let me start with answering the question about the monoclonal antibody for dogs. So we have multiple programs in our R&D activity. The product that we are now planning to launch it's an internal product for dogs. The one that we are planning to launch for cat is coming from Nexvet. You also asked about the decline in the quarter related to fish.

We have been growing very fast in previous years in fish. This year we had some challenge related to the PD vaccine in Norway. We expect that it is a temporary adjustment and we expect fish to continue growing faster than the overall animal health market. The long-term opportunities in fish is related to adding new vaccines to protect all species different than salmon. Today, we have most of our revenues concentrated in salmon in Norway and Chile.

But we expect to continue developing new vaccines to protect animals different than the salmon and to review the use of antibiotic which is today the only treatment or the only protection against infections for species like the gases or tilapia or other fish. Definitely, we continue investing in fish and we are confident that fish will be a growing opportunity in the future. Next question please.

Operator

We'll go next to Gregg Gilbert with SunTrust. Please go ahead.

Gregg Gilbert

A couple longer term ones for Kristin and clearly Zoetis is the leader overall industry but is there an area or areas we'd like to see is they want us be more of a leader than it is today. And secondly on the companion side do you think pet owners they are anywhere close the maxing out and what they can afford or where they chose to afford in carrying for their pets, I realize flees, ticks heart worm is not in this category. But thinking the three to five years plus on the line we spent biotech products, et cetera. Maybe this comment on that longer term. Thank you.

Juan Ramon Alaix

So let me answer the first question and then Kristin will cover the second. So when we see that we can improve our market share and becoming the leader and becoming leader and, in this call, we announced that we obtain approval of new vaccine for both which is related to vector technology it's an area that we believe that will be a growing opportunity.

So I think we are starting that with one vaccine but the objective is to develop a complete set of vector vaccine to cover multiple diseases in totally and this will help us and also to maximize the opportunities with our leadership in lower vaccination which is the machine that is used in country to protect chicken before hatchery.

So we are injecting X and we see an area in where we are less share that the overall share that this area has. The second area in where we think that we have been improving significantly is the launch of Simparica followed by the launch of Revolution Plus, ProHeart 12 it's parasiticides and we expect also with the launch of Simparica Trio to become much stronger leader in parasiticides than today. Kristin?

Kristin Peck

Sure, on you second question. We've seen as increases over the last few years and the spend per pet, I think a lot of that has to do with the demographic shifts in developed markets where people are having fewer children, spending more time with their pets, Millennials in particular are much more engaged with their pets. And we've spoken about the increase in pet spending start when they move from the backyard to your house and then ultimately to your bed. So we don't see any end in this market. It's been a very resilient business even in times of economic challenges people have continue to spend on their pets.

So we don't see right now any indicators that that spending per pet will be going down. So I think it remains a strong market as we look to the future and if you look at the urbanization and the emerging middle class and emerging market, we see significant growth there as you add more markets that keep more pets and medicalized like that.

Operator

And we'll go next to Kevin Ellich with Craig-Hallum. Please go ahead.

Kevin Ellich

So one quick one, thinking about African Swine Fever in a different way, down the road when it's time to re-populate the herd, just wondering how much benefit that could bring to Zoetis especially given your presence in genomics and genetics?

Kristin Peck

Sure. If you look at repopulation I mean essentially in China and some of these other geographies will repopulate. We believe when they do more move more to industrialized production and more away from the small backyard farms. We think that does play to the strength of innovative companies like Zoetis so we do see the future of African Swine Fever as it goes down meeting, more technologically based production which we think it will be an increase for us and certainly if we're able to create a vaccine for African Swine Fever that will be even more in picture.

Operator

And there appears to be no further questions, I'll return the floor to Juan Ramon for closing remarks.

Juan Ramon Alaix

Thank you very much and since this will be my last earnings call, I want to thank you all of you for the support you have given to me and Zoetis over the last seven years. It has been an amazing journey and I'm very proud of the value that we have been created. I know that you will enjoy the same ongoing commitment to our valuable provision from Kristin, Glenn and the rest of our leadership team and the data as I think into the next phase of growth.

In closing, I remain confident in a brighter future of Zoetis. This company and its people have the capabilities, experience and customer focus to continue delivering a world-class for our customers and our shareholders. Thank you very much.

Operator

And this will conclude today's program. Thank for your participation. You may now disconnect.