

## Equities

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# U.S. Pharmaceuticals

## Alert: Our Thoughts on Pharma Sales Exposure in Japan

**Conclusion:** We estimate that BMY is the least exposed to any slowdown in the Japanese pharmaceutical market, with Japan projected to account for ~3% of total 2011E pharma sales vs. ~9%, 10% & 10% for PFE, LLY & MRK, respectively (see **Figure 1** for 2010/'11E Japan Pharma Sales & EPS Exposure). Our Japanese pharmaceutical analyst estimates that the 3 prefectures most affected by the tsunami account for only ~5% of pharma sales in Japan. We would not expect a significant sales impact in 1Q11 for our coverage however; a modest slowdown in prescriptions could potentially impact sales in 2Q11. We estimate that each 5% decline in 2011E sales in Japan would decrease EPS by ~0.2% for BMY, & ~0.4% for LLY, MRK & PFE, respectively (see **Figure 2** for our U.S. Major Pharma: Sensitivity Analysis on Prescription Slowdown in Japan). According to IMS, Japan is the 2<sup>nd</sup>-largest drug market in the world, with sales approaching \$100B+ in 2014. Our top pick remains BMY.

### US Major Pharma Infrastructures Largely Located in Central/Southern Japan.

Each U.S. large-cap has manufacturing facilities & corporate offices in Japan. However, there does not appear to be any major disruption, given that the facilities are located in central and southern Japan (see **Figure 3**). However, we could see a modest impact on prescription volume from the overall disruption to the Japanese economy. We note that 2011 sales in Japan for the group have a robust mid-to-upper single digit FX tailwind from continued strengthening of the yen.

### Significant Number of New Product Submissions, Approvals & Launches

**Could be Modestly Impacted.** In 2011, each company in our coverage has regulatory submissions, anticipated approvals and new product launches planned for its Japanese operating affiliates. **BMY** is waiting on approval for Sprycel in 1<sup>st</sup>-line chronic myelogenous leukemia (CML) and could potentially file Onglyza (type-2 diabetes) in 2011. **LLY** & its partner Boehringer Ingelheim (BI) have filed linagliptin (type-2 diabetes) in 4Q10, with regulatory action anticipated in 2012; LLY also recently launched Byetta & Forteo. **MRK** has recently launched Januvia and is awaiting approval for daptomycin, Gardasil & Rotateg. Finally, **PFE** is awaiting approval for Prevnar-13 in children and Lyrica was recently approved in the treatment of neuropathic pain. The U.S. major pharma group has committed significant SG&A to grow their sales in Japan through multiple planned new product launches. We assume only modest regulatory delays. In addition, we would also anticipate a limited impact to ongoing clinical trials in Japan to support regulatory submissions.

### ■ Industry Overview

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**Figure 1. U.S. Major Pharma: 2010E/'11E Japan Pharma Sales & EPS Exposure**

	BMJ*	LLY	MRK	PFE*
2010 Japan Pharma Sales	\$585	\$1,565	\$3,645	\$4,389
2010 Total Pharma Sales	\$19,484	\$21,051	\$39,811	\$58,523
<b>% of Total Pharma</b>	<b>3%</b>	<b>7.4%</b>	<b>9.2%</b>	<b>7.5%</b>
<b>2011E Japan Pharma Sales</b>	<b>\$625</b>	<b>\$2,035</b>	<b>\$4,192</b>	<b>\$5,048</b>
<b>YoY Growth</b>	<b>7%</b>	<b>30%</b>	<b>15%</b>	<b>15%</b>
2011E Total Pharma Sales	\$20,228	\$20,732	\$40,956	\$56,747
<b>% of Total Pharma</b>	<b>3.1%</b>	<b>9.8%</b>	<b>10.2%</b>	<b>8.9%</b>
<i>Estimated Japan Operating Margin</i>	35.0%	30.0%	33.0%	42.0%
<i>2011E Company Op Margin</i>	32.5%	27.3%	30.7%	39.0%
Estimated Japan After-Tax Contribution	\$142	\$397	\$899	\$1,378
Estimated Japan EPS Contribution	\$0.08	\$0.36	\$0.29	\$0.17
2011E Company EPS	\$2.16	\$4.29	\$3.70	\$2.26
<b>% of EPS</b>	<b>3.8%</b>	<b>8.3%</b>	<b>7.9%</b>	<b>7.7%</b>

\*Assumed sales based on 10-Ks

Note: We assume a 35% tax rate on JP pre-tax income

Source: Citi Investment Research and Analysis; Company Reports

**Figure 2. U.S. Major Pharma: Sensitivity Analysis on Prescription Slowdown in Japan**

	BMJ	LLY	MRK	PFE
5% Sales Reduction (full year)	(\$31)	(\$102)	(\$210)	(\$252)
2011E EPS Impact	(\$0.00)	(\$0.02)	(\$0.01)	(\$0.01)
<b>% of EPS</b>	<b>0.2%</b>	<b>0.4%</b>	<b>0.4%</b>	<b>0.4%</b>
10% Sales Reduction (full year)	(\$63)	(\$203)	(\$419)	(\$505)
2011E EPS Impact	(\$0.01)	(\$0.04)	(\$0.03)	(\$0.02)
<b>% of EPS</b>	<b>0.4%</b>	<b>0.8%</b>	<b>0.8%</b>	<b>0.8%</b>
25% Sales Reduction (full year)	(\$156)	(\$509)	(\$1,048)	(\$1,262)
2011E EPS Impact	(\$0.02)	(\$0.09)	(\$0.07)	(\$0.04)
<b>% of EPS</b>	<b>1.0%</b>	<b>2.1%</b>	<b>2.0%</b>	<b>1.9%</b>

Note: We assume a 35% tax rate on JP pre-tax income

Source: Citi Investment Research and Analysis

**Figure 3. Locations of US Major Pharma Facilities in Japan**

	Japan Infrastructure
<b>BMJ</b>	Tokyo (office) Aichi (mfg)
<b>LLY</b>	Kobe (office, mfg)
<b>MRK</b>	Tokyo (office), Osaka (office) Shiga (mfg), Minuma (mfg)
<b>PFE</b>	Nagoya (mfg)

Source: Company Reports

## Bristol-Myers Squibb

(BMY.N; US\$26.20; 1M)

### Valuation

Our \$30 target price is based on a forward P/E multiple supported by our discounted cash flow (DCF) analysis. Our \$30 price target assumes BMY trades at 14.9x our 2012E EPS of \$2.02, which assumes BMY trades at a premium to its peers reflecting a favorable growth outlook supported by its late stage pipeline. Applying our DCF analysis, we also arrive at a \$30 target price, assuming a terminal growth rate of -1%.

### Risks

We rate Bristol-Myers Squibb shares Medium Risk because the potential for pipeline setbacks has decreased with each success. However, the company will incur patent expirations in 2012-14 on key growth drivers (Plavix, Avapro/Avalide & Sustiva). We believe the current valuation does not fully factor in success with recently launched products like Onglyza (oral DPP-IV inhibitor for treating type-2 diabetes), the several late-stage products (belatacept [renal transplantation], apixaban (DVT's/ACS/atrial fibrillation), ipilimumab [metastatic melanoma] & dapagliflozin [type-2 diabetes]); we believe any setback can be absorbed. In addition, uncertainty remains on BMY's ability to offset the Plavix earnings stream from US competition from LLY's Effient and the entry of generic Plavix in Europe. These risks are balanced by BMY's track record of strong pipeline execution, better growth prospects (relative to peer group) over the next several years, coupled with an attractive dividend yield and a strong balance sheet (net cash position).

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