

GlaxoSmithKline

Price 1,401p

Strong confidence in reaching targets

Fair Value 1670p (+19%)

BUY

Bloomberg	GSK LN
Reuters	GSK.L
12-month High / Low (p)	1,642 / 1,238
Market Cap (GBPm)	68,230
Ev (BG Estimates) (GBPm)	93,401
Avg. 6m daily volume (000)	8 298
3y EPS CAGR	-0.8%

From a meeting with management last Friday we are back with strong confidence in reaching 2016 targets for double-digit core EPS growth. Momentum is improving. GSK is a BUY for the start of 2016.

ANALYSIS

- During a breakfast meeting with management, we addressed the following key topics:
- CHC** – a significant part of the meeting was dedicated to this business. GSK is pleased with how the business is developing and is absolutely convinced it will achieve profitability at least in line with peers. It confirmed the target for 20% operating margin by the end of the decade (11.3% in 2015). A lot has been done to improve manufacturing efficiency both at former GSK and Novartis sites. Two minor disruptions remain and very good OTIF scores are now achieved (about 96%) since quality remediation team from Pharmaceuticals has taken care of CHC. Average quality has also been improved by switching one state-of-the-art facility from Pharma in Canada to the JV. A lot has also been done to reduce the complexity of the business and for instance the number of formulations of each brand whenever it was possible (Sensodyne brought down from about 50 to a handle). As to the question of whether the JV can achieve Reckitt's margins of 23-25%, Andrew Witty answered that at some point, it will have to decide whether to prioritise profit over revenue growth. When GSK reached its peak of 22%, top-line was growing only 2-3%. This balance is key mid-term.
- ViiV** – GSK has seen no change in the dynamics of dolutegravir-based regimens since Gilead has launched Genvoya for HIV-1 infections and sequentially is expecting new data with dolutegravir vs active comparators and further triple combinations. Later on, ViiV hopes to deliver dual therapies (able to circumvent resistance), long-acting drugs (like cabotegravir) and then maturation inhibitors for new combinations. With recent acquisitions from BMS, GSK now believes it is back into this HIV business with solid assets and clear milestones over the next 3-4 years.
- Respiratory** – Talking about respiratory was an opportunity for management which stressed how pricing has changed in recent years in the US. It has clearly become a key argument. GSK illustrated this statement by saying that its last six products launched in the US had had no premium over existing products. Breo's net price is currently lower than Advair's. The dynamics are good and since DTC campaign was launched to support the asthma indication last November, it has improved a lot. The focus in 2016 is to build share before generics come in. Concerning Nucala, GSK confirmed it does not expect any price issue as it has been priced on par with Xolair's average pricing based on patient weight.
- Vaccines** – A word here to report that manufacturing issues in pediatric vaccines are not expected to resume fully before late 2016/early 2017 and have to do with an upgraded facility as well as with new facilities coming on stream. One objective with these new facilities is to reduce the number of reasons to stop production. Interestingly, GSK suggested it might benefit somewhat from Sanofi Pasteur's supply limitations in the US by prioritising some geographies over others.

	1 M	3 M	6 M	31/12/15
Absolute perf.	1.1%	1.1%	-1.3%	2.0%
Healthcare	-12.7%	-14.3%	-20.3%	-12.9%
DJ Stoxx 600	-9.2%	-14.0%	-19.3%	-10.9%

YEnd Dec. (GBPm)	2014	2015e	2016e	2017e
Sales	23,006	23,923	25,060	25,712
% change		4.0%	4.8%	2.6%
EBITDA	8,294	7,429	8,435	9,114
EBIT	6,594	5,729	6,735	7,414
% change		-13.1%	17.6%	10.1%
Net income	4,584	3,658	4,181	4,656
% change		-20.2%	14.3%	11.4%

	2014	2015e	2016e	2017e
Operating margin	28.7	23.9	26.9	28.8
Net margin	19.9	15.3	16.7	18.1
ROE	81.4	78.0	86.9	94.4
ROCE	25.0	14.7	16.6	17.8
Gearing	264.9	118.9	131.8	107.7

(p)	2014	2015e	2016e	2017e
EPS	95.33	75.71	86.42	93.04
% change	-	-20.6%	14.1%	7.7%
P/E	14.7x	18.5x	16.2x	15.1x
FCF yield (%)	4.0%	2.8%	5.4%	6.5%
Dividends (p)	80.00	100.00	80.00	80.00
Div yield (%)	5.7%	7.1%	5.7%	5.7%
EV/Sales	3.5x	3.9x	3.8x	3.7x
EV/EBITDA	9.8x	12.6x	11.2x	10.3x
EV/EBIT	12.3x	16.3x	14.0x	12.7x



VALUATION

- As everything looks well on track and maybe sometimes ahead of schedule, the question was then asked as to why double-digit growth in core EPS in 2016 would be limited to 10%. The answer was suggestive of some room to exceed this level. The two arguments supportive of guidance are: (i) confirmation of a recovery in emerging markets and if countries like India are doing well, it is still tough in Latin America and in the Middle East for macroeconomic reasons; (ii) see Advair's dynamic in the US where GSK said it would be reasonable to expect another 20% drop in sales but the group would like to be sure no competitor takes a desperate attitude during the course of 2016.
- After this meeting, we have taken a more aggressive view on CHC margins, to the expense of Pharma but with no change in net numbers, thus leaving the FV unchanged.

NEXT CATALYSTS

- 18th February 2016: ex-dividend trading date (GBP23 normal + GBP20 special)



Analyst :

Eric Le Berrigaud
33(0) 1 56 68 75 33
eleberrigaud@bryangarnier.com

Sector Team :

Mickael Chane Du
Hugo Solvet

Bryan Garnier stock rating system

For the purposes of this Report, the Bryan Garnier stock rating system is defined as follows:

Stock rating

BUY	Positive opinion for a stock where we expect a favourable performance in absolute terms over a period of 6 months from the publication of a recommendation. This opinion is based not only on the FV (the potential upside based on valuation), but also takes into account a number of elements that could include a SWOT analysis, momentum, technical aspects or the sector backdrop. Every subsequent published update on the stock will feature an introduction outlining the key reasons behind the opinion.
NEUTRAL	Opinion recommending not to trade in a stock short-term, neither as a BUYER or a SELLER, due to a specific set of factors. This view is intended to be temporary. It may reflect different situations, but in particular those where a fair value shows no significant potential or where an upcoming binary event constitutes a high-risk that is difficult to quantify. Every subsequent published update on the stock will feature an introduction outlining the key reasons behind the opinion.
SELL	Negative opinion for a stock where we expect an unfavourable performance in absolute terms over a period of 6 months from the publication of a recommendation. This opinion is based not only on the FV (the potential downside based on valuation), but also takes into account a number of elements that could include a SWOT analysis, momentum, technical aspects or the sector backdrop. Every subsequent published update on the stock will feature an introduction outlining the key reasons behind the opinion.

Distribution of stock ratings

BUY ratings 72%

NEUTRAL ratings 0%

SELL ratings 28%

Research Disclosure Legend

1	Bryan Garnier shareholding in Issuer	Bryan Garnier & Co Limited or another company in its group (together, the "Bryan Garnier Group") has a shareholding that, individually or combined, exceeds 5% of the paid up and issued share capital of a company that is the subject of this Report (the "Issuer").	No
2	Issuer shareholding in Bryan Garnier	The Issuer has a shareholding that exceeds 5% of the paid up and issued share capital of one or more members of the Bryan Garnier Group.	No
3	Financial interest	A member of the Bryan Garnier Group holds one or more financial interests in relation to the Issuer which are significant in relation to this report	No
4	Market maker or liquidity provider	A member of the Bryan Garnier Group is a market maker or liquidity provider in the securities of the Issuer or in any related derivatives.	No
5	Lead/co-lead manager	In the past twelve months, a member of the Bryan Garnier Group has been lead manager or co-lead manager of one or more publicly disclosed offers of securities of the Issuer or in any related derivatives.	No
6	Investment banking agreement	A member of the Bryan Garnier Group is or has in the past twelve months been party to an agreement with the Issuer relating to the provision of investment banking services, or has in that period received payment or been promised payment in respect of such services.	No
7	Research agreement	A member of the Bryan Garnier Group is party to an agreement with the Issuer relating to the production of this Report.	No
8	Analyst receipt or purchase of shares in Issuer	The investment analyst or another person involved in the preparation of this Report has received or purchased shares of the Issuer prior to a public offering of those shares.	No
9	Remuneration of analyst	The remuneration of the investment analyst or other persons involved in the preparation of this Report is tied to investment banking transactions performed by the Bryan Garnier Group.	No
10	Corporate finance client	In the past twelve months a member of the Bryan Garnier Group has been remunerated for providing corporate finance services to the issuer or may expect to receive or intend to seek remuneration for corporate finance services from the Issuer in the next six months.	No
11	Analyst has short position	The investment analyst or another person involved in the preparation of this Report has a short position in the securities or derivatives of the Issuer.	No
12	Analyst has long position	The investment analyst or another person involved in the preparation of this Report has a long position in the securities or derivatives of the Issuer.	No
13	Bryan Garnier executive is an officer	A partner, director, officer, employee or agent of the Bryan Garnier Group, or a member of such person's household, is a partner, director, officer or an employee of, or adviser to, the Issuer or one of its parents or subsidiaries. The name of such person or persons is disclosed above.	No
14	Analyst disclosure	The analyst hereby certifies that neither the views expressed in the research, nor the timing of the publication of the research has been influenced by any knowledge of clients positions and that the views expressed in the report accurately reflect his/her personal views about the investment and issuer to which the report relates and that no part of his/her remuneration was, is or will be, directly or indirectly, related to the specific recommendations or views expressed in the report.	Yes
15	Other disclosures	Other specific disclosures: Report sent to Issuer to verify factual accuracy (with the recommendation/rating, price target/spread and summary of conclusions removed).	No

A copy of the Bryan Garnier & Co Limited conflicts policy in relation to the production of research is available at www.bryangarnier.com

London	Paris	New York	Geneva	New Delhi
Beaufort House	26 Avenue des Champs Elysées	750 Lexington Avenue	rue de Grenus 7	The Imperial Hotel
15 St. Botolph Street	75008 Paris	New York, NY 10022	CP 2113	Janpath
London EC3A 7BB	Tel: +33 (0) 1 56 68 75 00	Tel: +1 (0) 212 337 7000	Genève 1, CH 1211	New Delhi 110 001
Tel: +44 (0) 207 332 2500	Fax: +33 (0) 1 56 68 75 01	Fax: +1 (0) 212 337 7002	Tel +4122 731 3263	Tel +91 11 4132 6062
Fax: +44 (0) 207 332 2559	Regulated by the	FINRA and SIPC member	Fax+4122731 3243	+91 98 1111 5119
Authorised and regulated by the	Financial Conduct Authority (FCA) and		Regulated by the	Fax +91 11 2621 9062
Financial Conduct Authority	the Autorité de Contrôle prudentiel et de		FINMA	
(FCA)	resolution (ACPR)			

Important information

This document is classified under the FCA Handbook as being investment research (independent research). Bryan Garnier & Co Limited has in place the measures and arrangements required for investment research as set out in the FCA's Conduct of Business Sourcebook.

This report is prepared by Bryan Garnier & Co Limited, registered in England Number 03034095 and its MIFID branch registered in France Number 452 605 512. Bryan Garnier & Co Limited is authorised and regulated by the Financial Conduct Authority (Firm Reference Number 178733) and is a member of the London Stock Exchange. Registered address: Beaufort House 15 St. Botolph Street, London EC3A 7BB, United Kingdom

This Report is provided for information purposes only and does not constitute an offer, or a solicitation of an offer, to buy or sell relevant securities, including securities mentioned in this Report and options, warrants or rights to or interests in any such securities. This Report is for general circulation to clients of the Firm and as such is not, and should not be construed as, investment advice or a personal recommendation. No account is taken of the investment objectives, financial situation or particular needs of any person.

The information and opinions contained in this Report have been compiled from and are based upon generally available information which the Firm believes to be reliable but the accuracy of which cannot be guaranteed. All components and estimates given are statements of the Firm, or an associated company's, opinion only and no express representation or warranty is given or should be implied from such statements. All opinions expressed in this Report are subject to change without notice. To the fullest extent permitted by law neither the Firm nor any associated company accept any liability whatsoever for any direct or consequential loss arising from the use of this Report. Information may be available to the Firm and/or associated companies which are not reflected in this Report. The Firm or an associated company may have a consulting relationship with a company which is the subject of this Report.

This Report may not be reproduced, distributed or published by you for any purpose except with the Firm's prior written permission. The Firm reserves all rights in relation to this Report.

Past performance information contained in this Report is not an indication of future performance. The information in this report has not been audited or verified by an independent party and should not be seen as an indication of returns which might be received by investors. Similarly, where projections, forecasts, targeted or illustrative returns or related statements or expressions of opinion are given ("Forward Looking Information") they should not be regarded as a guarantee, prediction or definitive statement of fact or probability. Actual events and circumstances are difficult or impossible to predict and will differ from assumptions. A number of factors, in addition to the risk factors stated in this Report, could cause actual results to differ materially from those in any Forward Looking Information.

Disclosures specific to clients in the United Kingdom

This Report has not been approved by Bryan Garnier & Co Limited for the purposes of section 21 of the Financial Services and Markets Act 2000 because it is being distributed in the United Kingdom only to persons who have been classified by Bryan Garnier & Co Limited as professional clients or eligible counterparties. Any recipient who is not such a person should return the Report to Bryan Garnier & Co Limited immediately and should not rely on it for any purposes whatsoever.

Notice to US investors

This research report (the "Report") was prepared by Bryan Garnier & Co Limited for information purposes only. The Report is intended for distribution in the United States to "Major US Institutional Investors" as defined in SEC Rule 15a-6 and may not be furnished to any other person in the United States. Each Major US Institutional Investor which receives a copy of this Report by its acceptance hereof represents and agrees that it shall not distribute or provide this Report to any other person. Any US person that desires to effect transactions in any security discussed in this Report should call or write to our US affiliated broker, Bryan Garnier Securities, LLC, 750 Lexington Avenue, New York NY 10022. Telephone: 1-212-337-7000.

This Report is based on information obtained from sources that Bryan Garnier & Co Limited believes to be reliable and, to the best of its knowledge, contains no misleading, untrue or false statements but which it has not independently verified. Neither Bryan Garnier & Co Limited and/or Bryan Garnier Securities LLC make no guarantee, representation or warranty as to its accuracy or completeness. Expressions of opinion herein are subject to change without notice. This Report is not an offer to buy or sell any security.

Bryan Garnier Securities, LLC and/or its affiliate, Bryan Garnier & Co Limited may own more than 1% of the securities of the company(ies) which is (are) the subject matter of this Report, may act as a market maker in the securities of the company(ies) discussed herein, may manage or co-manage a public offering of securities for the subject company(ies), may sell such securities to or buy them from customers on a principal basis and may also perform or seek to perform investment banking services for the company(ies).

Bryan Garnier Securities, LLC and/or Bryan Garnier & Co Limited are unaware of any actual, material conflict of interest of the research analyst who prepared this Report and are also not aware that the research analyst knew or had reason to know of any actual, material conflict of interest at the time this Report is distributed or made available..