

1st July 2016

Healthcare

Shire PLC

Price 4,641p

SHP607 is not dead!

Fair Value 6500p (+40%)

BUY

Bloomberg	SHP LN
Reuters	SHP.L
12-month High / Low (p)	5,730 / 3,480
Market Cap (GBPm)	41,703
Ev (BG Estimates) (GBPm)	56,863
Avg. 6m daily volume (000)	2,718
3y EPS CAGR	14.0%

Shire announced yesterday that SHP607 failed to meet the primary endpoint of its Phase II study. But as some key secondary endpoints were met, the development of the compound might continue with quite a different therapeutic goal (preventing the occurrence of severe bronchopulmonary dysplasia and intraventricular haemorrhage). Pending the outcome of the discussion with the regulators regarding this potential repositioning, we are sticking to our USD700m peak sales along with a 20% PoS we have assigned to this drug candidate. Buy reiterated with a FV of GBP6,500.

	1 M	3 M	6 M	31/12/15
Absolute perf.	8.9%	17.2%	-1.2%	-1.2%
Healthcare	0.9%	8.7%	-5.2%	-5.2%
DJ Stoxx 600	-5.1%	-2.3%	-9.8%	-9.8%

YEnd Dec. (USDm)	2015	2016e	2017e	2018e
Sales	6,100	10,774	15,121	16,400
% change		76.6%	40.3%	8.5%
EBITDA	2,924	4,564	6,647	7,532
EBIT	2,785	4,220	6,073	6,876
% change		51.5%	43.9%	13.2%
Net income	2,310	3,184	4,463	5,228
% change		37.8%	40.2%	17.1%

	2015	2016e	2017e	2018e
Operating margin	45.7	39.2	40.2	41.9
Net margin	37.9	29.6	29.5	31.9
ROE	23.5	9.9	12.0	12.2
ROCE	16.3	5.7	8.0	9.3
Gearing	13.8	63.0	42.6	24.2

(USD)	2015	2016e	2017e	2018e
EPS	3.89	4.11	4.92	5.77
% change	-	5.5%	19.8%	17.1%
P/E	15.9x	15.1x	12.6x	10.8x
FCF yield (%)	6.0%	0.1%	8.3%	10.2%
Dividends (USD)	0.23	0.20	0.23	0.32
Div yield (%)	0.4%	0.3%	0.4%	0.5%
EV/Sales	9.4x	7.1x	4.7x	4.0x
EV/EBITDA	19.5x	16.7x	10.8x	8.8x
EV/EBIT	20.5x	18.0x	11.8x	9.6x

ANALYSIS

- **The Phase II trial evaluating SHP607 in patients with retinopathy of prematurity** (a rare eye disease characterised by an incomplete vascular development of the retina) **did not meet its primary endpoint** of reducing the severity of the disease.
- **That said, some key secondary endpoints were met.** And more precisely, the top-line data showed 1/ a reduction of 53% in the incidence of severe bronchopulmonary dysplasia when compared with the control arm, and 2/ a 44% decrease in the frequency of severe intraventricular haemorrhage... This is far from insignificant as research suggests that c. 60% of premature infants do experience these kind of complications.
- We understand **the company is willing to discuss with regulatory authorities regarding a potential Phase III clinical programme with a focus on these novel endpoints.**
- Against this backdrop, three scenarios have to be considered: 1/ the rejection of the “repositioning” and a development deadlock... If so, we would remove the compound from our valuation and trim our FV by GBP50; 2/ Shire could adopt a more cautious stance and rather launch another Phase II to assess this new working hypothesis. In such a scenario, our FV would be slightly reduced due to the delay in approval; 3/ but assuming the Phase III trials could be initiated, we might increase our PoS to 50% along with our FV (+GBP100).
- For now, **we stick to our USD700m peak sales along with a PoS of 20%** we have assigned to this drug candidate.

VALUATION

- **BUY rating reiterated with a FV of GBP6,500 (+40%).**
- At current levels, **SHP trades on a 55% discount to CSL on 2017e PE**, whereas Shire displays 1/ a more attractive growth profile (EPS CAGR 2015-2020: +14% vs +10% respectively), along with 2/ a quite similar product mix and profile risk. But more broadly speaking, the discount vs the European sector as a whole stands at 30%...

NEXT CATALYSTS

- 22nd July 2016: Potential approval of lifitegrast as a treatment for dry eye disease (potential impact on our FV: -GBP150 if negative, +GBP150 if positive).
- 2nd August 2016: Q2 2016 results + Update on the expected cost synergies with Baxalta... And we believe the previous guidance could be raised to USD750m (impact on our mid-term EPS in such a scenario: +4%. FV: +GBP200).

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