

Novartis

Price CHF74.60

More-resilient-than-expected Gleevec drives Q3 slightly above expectations

Fair Value CHF87 (+17%)

NEUTRAL

Bloomberg	NOVN VX
Reuters	NOVN.VX
12-month High / Low (CHF)	90.6 / 68.5
Market Cap (CHFm)	195,983
Ev (BG Estimates) (CHFm)	188,930
Avg. 6m daily volume (000)	4 321
3y EPS CAGR	5.3%

Third-quarter numbers at Novartis came out slightly above estimates, but almost entirely driven by a lower-than-expected decline in Gleevec's sales in the US, where only two generics have reached the market so far. The difference is about USD100m in sales and USD 0.03 on core EPS i.e. exactly the spread vs consensus expectations. Alcon is still weak. Limited positive share price reaction expected.

ANALYSIS

- This morning Novartis came out with third-quarter numbers slightly above estimates for the group and entirely driven by Innovative Medicines as the other two business units (Sandoz and Alcon) were in-line or slightly below. All in all, sales are more or less in line with consensus estimates, but Innovative Medicines beat expectations by close to USD100m, which corresponds to the better resilience of Gleevec in the US, where only two generics so far have reached the market, resulting in much lower-than-expected pressure on prices and loss of volumes. Gleevec in the US is down only 30% and achieved USD834m in total for the quarter where consensus was USD738m.
- Considering the profitability of the drug, this spread also makes a huge difference at the operating income level for the whole division which performed in line on sales during Q3, maintaining the operating margin almost flat at 32.7% (vs 33%). Other significant products within Innovative Medicines were roughly as expected, with ups and downs from one product to another (Afinitor did slightly better where Cosentyx did a touch less than anticipated).
- Margin-wise, the performance of the other two divisions diverged. Sandoz's advanced slightly to 21.1%, likely driven by the increased proportion of complex generics and biosimilars and despite some price pressures, but also in the absence of a major launch during the quarter. Alcon has not yet reached a plateau and is still on a downward trend, still suffering from competitive pressures in the lenses market and from a loss of market shares while also suffering from a slowdown in equipment sales. Core operating margin came out at 14.3% where we had expected 16.2%, which is another low point compared to previous quarters, as Alcon is still investing heavily.
- There is no update on R&D (meetings with regulatory authorities about BAF312 in SPMS are scheduled towards the turn of the year, new data comparing Ultribon to Anoro are also expected later this year to help decide what to do in Respiratory in the US).
- It looks like yesterday's press rumours about Roche and potential big acquisitions are pure speculation and are not the result of any interaction with the company.
- The outlook for the year is confirmed (flat to slightly declining core operating income, compared to -4% after 9 months). We note that without clear explanations, free cash-flow was down 7% in Q3 when net income was up 7%.

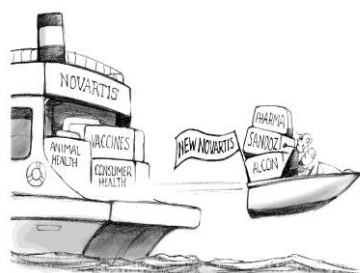
VALUATION

- We do not expect to make major changes to our numbers following this quarterly release.
- This quarterly set of results is not bad in absolute terms, but considering where the beat is coming from (i.e. from patent-expiring Gleevec), there is unfortunately little to extrapolate. It has to be considered also that neither Alcon nor Entresto are really showing meaningful turnarounds. So, all in all, we do expect a limited share price reaction to the Q3 numbers.

NEXT CATALYSTS

- Today 2pm : Conference Call on Q3 numbers
- 25 January 2017: Full-year results and R&D update (Basel)

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

Sector Team :
Mickael Chane Du
Hugo Solvet
Marion Levi

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Distribution of stock ratings

BUY ratings 72%

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London	Paris	New York	Munich	New Delhi
Beaufort House	26 Avenue des Champs Elysées	750 Lexington Avenue	Widenmayerstrasse 29	The Imperial Hotel Janpath
15 St. Botolph Street	75008 Paris	New York, NY 10022	80538 Munich	New Delhi 110 001
London EC3A 7BB	Tel: +33 (0) 1 56 68 75 00	Tel: +1 (0) 212 337 7000	Germany	Tel +91 11 4132 6062
Tel: +44 (0) 207 332 2500	Fax: +33 (0) 1 56 68 75 01	Fax: +1 (0) 212 337 7002	+49 89 2422 62 11	+91 98 1111 5119
Fax: +44 (0) 207 332 2559	Regulated by the	FINRA and SIPC member		Fax +91 11 2621 9062
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Financial Conduct Authority (FCA)	Autorité de Contrôle prudentiel et de			rue de Grenus 7
	resolution (ACPR)			CP 2113
				Genève 1, CH 1211
				Tel +4122 731 3263
				Fax+4122731 3243
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