

## AstraZeneca

Price 4,405p

The call is intact but the margin of error has narrowed in our view

Fair Value 5100p vs. 5220p (+16%)

BUY

Bloomberg	AZN LN
Reuters	AZN.L
12-month High / Low (p)	5,220 / 3,774
Market Cap (GBPm)	55,719
Ev (BG Estimates) (GBPm)	67,994
Avg. 6m daily volume (000)	2 786
3y EPS CAGR	-8.3%

AstraZeneca very much remains a medium-term call based on the ability of the pipeline to transform the company and its business mix, mainly to the benefit of oncology. However, for investors to be comfortable that this scenario could happen, two upcoming catalysts in H1 2017 (filing of acalabrutinib based on a single phase II and PFS outcome in MYSTIC phase III trial) are key, but uncertain.

## ANALYSIS

- First of all, we would like to take another look at third-quarter results and more specifically the underlying message behind the unchanged core EPS guidance, despite an unexpected tax settlement benefit of USD453m booked in Q3. CFO Marc Dunoyer explained that this positive one-off was offset by several negative ones, which in the end resulted in an unchanged guidance. Among the negatives were emerging market one-offs in LatAm and Saudi Arabia, the Flumist setback in the US and the true-up of rebate reversals for Symbicort. But, Flumist was in Q2 (and guidance was confirmed at the time) while other elements are “business as usual” and must be included in guidance. Pricing pressure and increased rebates should not result in guidance changes for any pharma company. This leads us to more relevant explanations in our view. Without this one-time tax effect, core EPS would have been tough to reach or no better than its bottom-end. But we think also that it has given AstraZeneca an opportunity to increase R&D spending (now R&D expenses are expected to be above last year’s level vs previous guidance of flat costs) and also to be less aggressive in terms of other operating income (now flat vs 2015 compared to a previous increase). There is no pressure left on AstraZeneca to divest or out-license any additional non-core assets by year-end and anything new can therefore benefit 2017 from now on.

- Considering extra costs incurred in 2016 as a consequence of the tax benefit, our overall comment about Q3 is that it simply shows that AstraZeneca has limited margin to keep earnings relatively flat in 2016-2017. We do not expect Respiratory to be in a better shape in 2017 considering first Gx Advair entry in the US. The same goes for Diabetes, where pressure on prices is at a peak. Oncology is clearly endorsing a major part of the investment case on its own.

- And our feeling at the end of yesterday’s conference call was that the scenario that actually has a reasonable chance of prevailing is not positive for the stock’s performance in coming weeks and months. This is the scenario that would see two of the most important oncology assets in AstraZeneca’s pipeline not fully delivering the expected data in H1 2017. On the one hand, acalabrutinib, whose data read-out has shifted from end-2016 to early-2017, which is not very material. However, we found AstraZeneca much more cautious than it has been so far in its wording about the likelihood of a filing on the basis of this data. It has now reported on slides that a short-term filing is a “fast-to-market opportunity ahead of randomised, controlled trials” which, in other words means that it is uncertain whether a filing will be possible. On the other hand, of course, still durvalumab and another check that in H1 2017 only PFS will be available which is a much weaker and uncertain endpoint than OS for immune-oncology drugs, as already demonstrated and evidenced in many other trials. And so, what if acalabrutinib does not deliver outstanding enough data to be filed on a single non-randomised phase II trial and if MYSTIC does not deliver positive PFS data in H1 2017? Well, let’s say that without changing that much the picture for 2020 or 2023, it would delay major triggers until 2018, which could result in an underperforming stock.

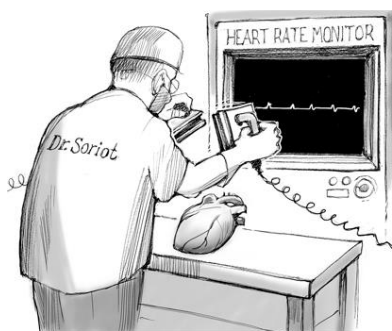
- We are eagerly awaiting our Conference next week to discuss some of the points with the company that will be represented by its EVP Global Product & Portfolio Strategy, Mark Mallon.

## VALUATION

- We have pushed first revenues for aca and durva by 12 months to H2 2018 and slightly adjusted Symbicort sales as well. This results into a minor FV adjustment to GBP5,100.

## NEXT CATALYSTS

- 14 November 2016: 4<sup>th</sup> BG Healthcare Conference - [Click here to download document](#)



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