

BUY : Zoetis

Price : \$184

PT : \$224

Upside : 21%


Zoetis Inc. NYSE : ZTS

Healthcare Sector

Industry: Specialty Pharmaceutical

Analyst: Ethan Gee

Date: 04/22/22



Agenda

Executive Summary

Company & Industry Overview

Investment Thesis

Catalysts

Valuation Range

Risks & Mitigations

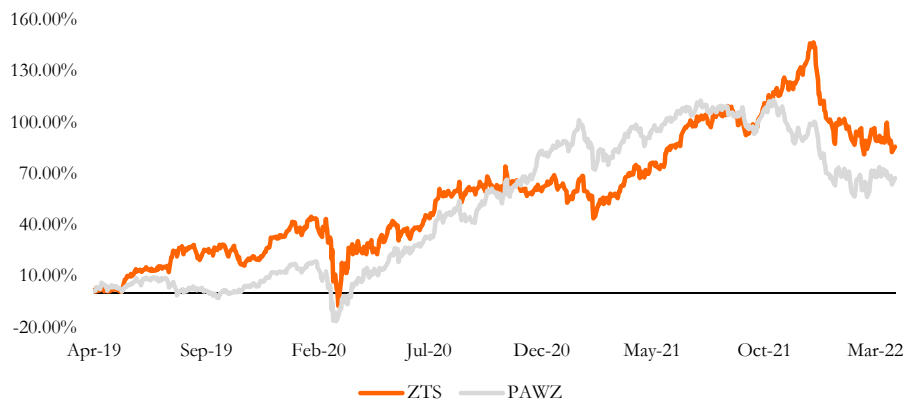
Executive Summary



Description

- Zoetis's **franchise dermatology** drug **Simparica** will continue to **gain market share** as their recently approved drug, **Simparica TRIO** edges out competition with **additional benefits**
- First of its kind **pain medication** for companion animals will **revolutionize** the **animal pain market**, opening the **opportunity** for **billions** in future sales
- A string of **veterinary diagnostics acquisitions** will begin Zoetis's **transition** into a **rapidly growing industry**

Stock Chart



Catalysts

Dermatology Domination

Pain Medication Pioneers

Expansion to New Industries

BUY: \$184

Target: \$224

Upside: 21%

Company Overview



Veterinary Services



Produce **vaccines** across a **mix** of 8 different **companion** and **livestock** animals



Leading producer of pharmaceutical and **anti-infective** medication for **cats/dogs**

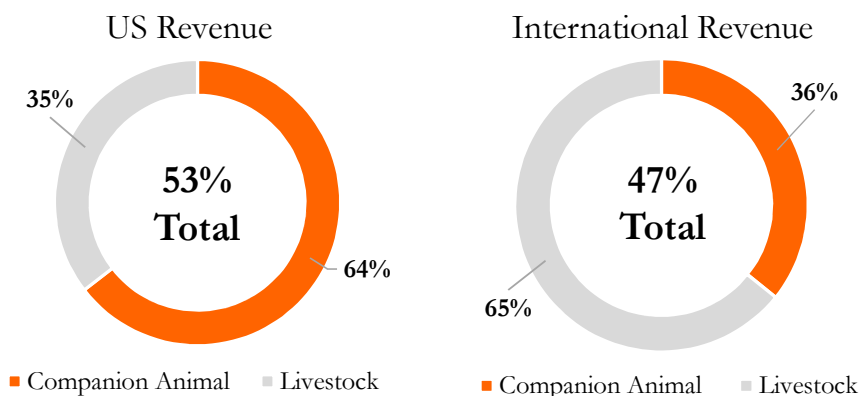


Breaking into the animal diagnostic industry through the **rollout** of **Vetscan**

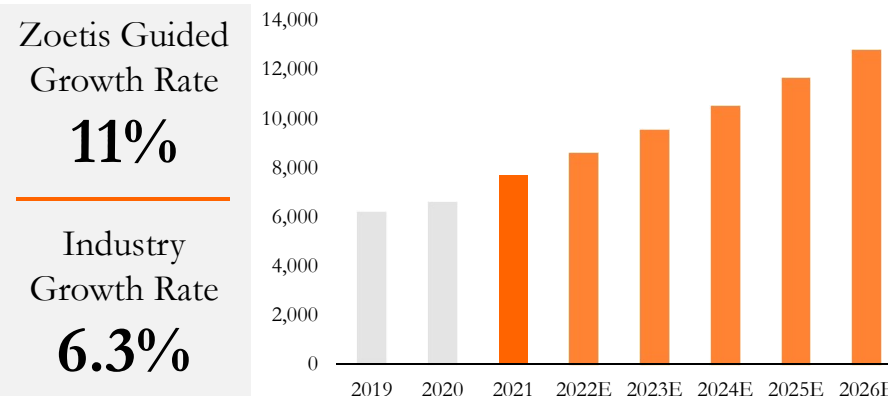
Key Statistics

Current Share Price	\$187
52 Week Range	\$161-249
Market Capitalization	\$88 B
Enterprise Value	\$93 B
TTM Revenue	\$2 B
EPS (TTM)	\$4.27

Revenue Segments



Revenue Projections



Industry Overview

Trends

- **Pet ownership** in the U.S. **rose over 70%** during the **pandemic**, **contributing** to an **increase** in overall **animal health spending**
- **Growing global population** and **continuous consumption** of **animal-based proteins** **drives** demand for **livestock products**
- Efforts to **maintain animal health** have **increased** as **animal welfare** efforts have **improved**

Competition



Owners & Their Pets

86%

say they would **pay whatever it takes** to cover their **pet's** **veterinary care**

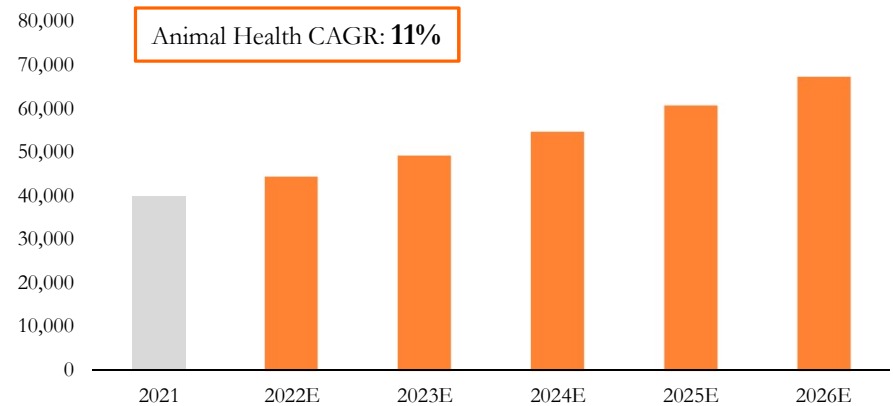
68%

of **owners** would rather **spend time with their pets** than with **other people**

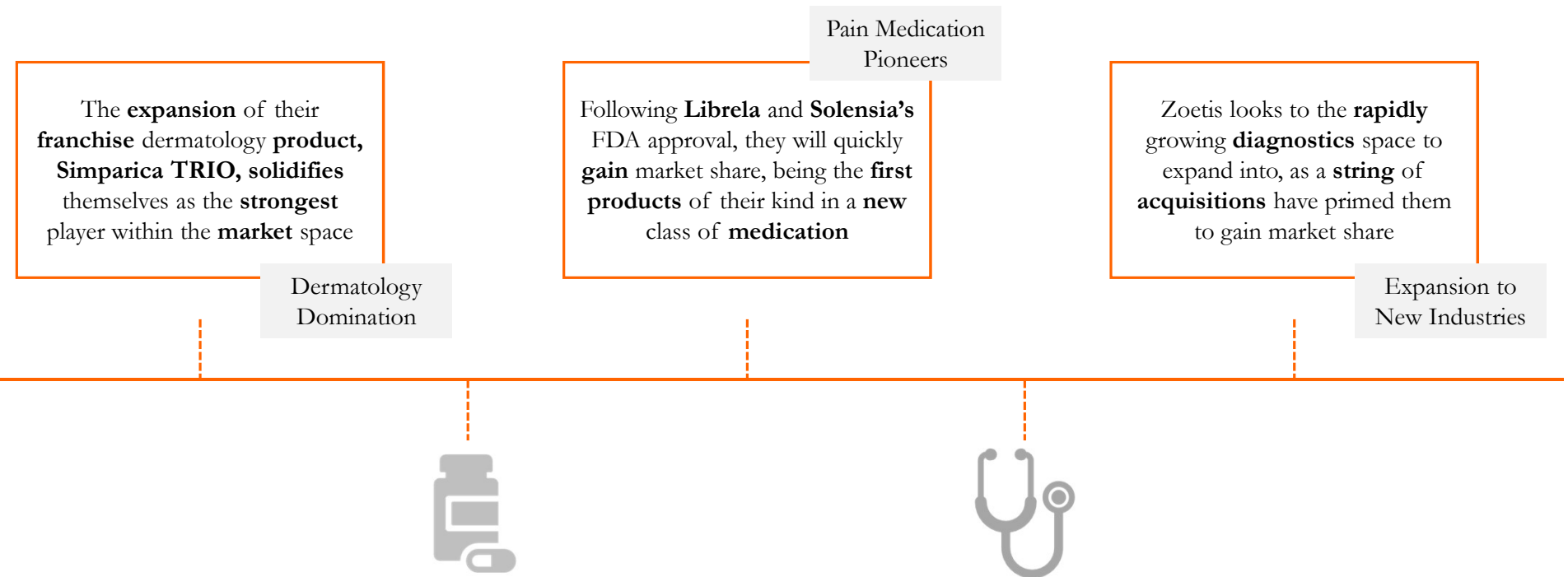
45%

of **owners** spend the **same or more** on their **pet's** **healthcare** than on **their own**

Market Growth



Investment Thesis



Dermatology Domination

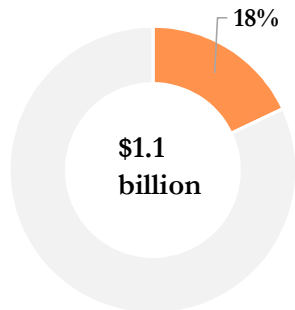
Dermatology Industry & Products

Dermatology focuses on **diseases** such as **fleas** and **ticks** to **allergic reactions** caused by **food**, contact, **inhalant allergies**

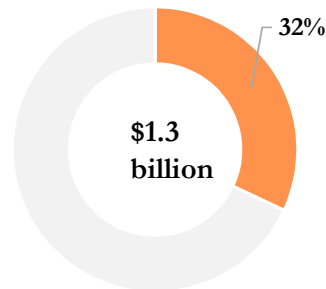
Zoetis offers a **range** of **products**, spanning from **prescriptions** that provide **long-lasting skin allergy relief** to **parasiticides** that prevent **heartworm disease** and **ticks**

Simparica TRIO

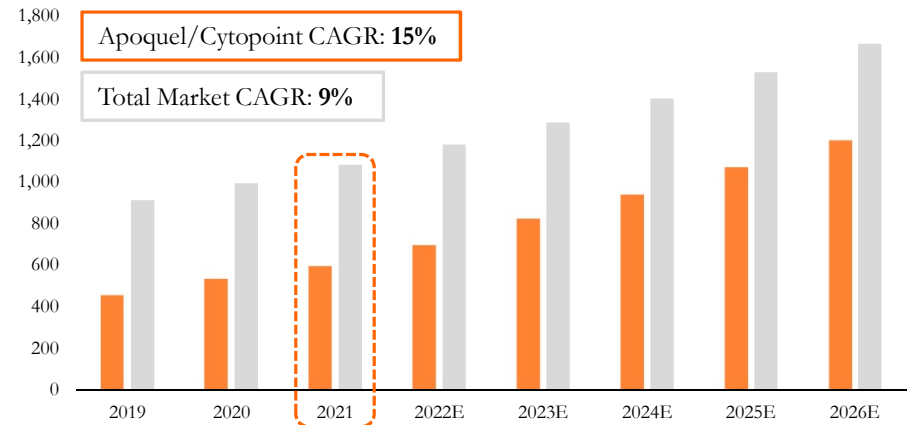
Simparica Addressable Market



Simparica TRIO Addressable Market



Canine Atopic Dermatitis Market



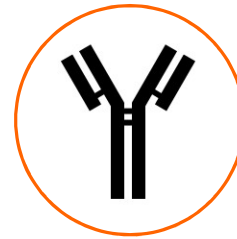
- **First and only combination** product demonstrated to **prevent infections** that may cause **Lyme disease**
- **Protects** dogs against **heartworm disease**, ticks & fleas, **roundworms & hookworms**
- Generated **revenue** of **\$475 million** in 2021, representing **upward growth** of more than **55% YoY**

Pain Medication Pioneers

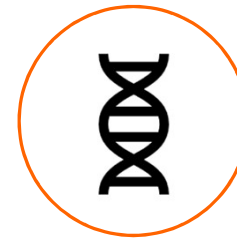
Overview

- Zoetis recently **launched** their **new osteoarthritis drug Librela** (dogs) **Solensia** (cats) in early 2021
- **First products** of their kind in a **new class of medication** for the management of **arthritis pain**
- Utilize **mAb's**, the **strongest and only** form of **therapy** available on the market for **OA** pain
- Target **NGF**, directly reducing **pain** and **inflammation**

Monoclonal Antibody Therapy



Mimics the body's **normal immune** response to **treat** diseases



Fuse myeloma cells with **antibody-producing** cells



Activates **cell lysis** or **blocks** transmission **signals**

Zoetis vs. Competition

- Previously, **NSAIDs** (nonsteroidal anti-inflammatory drugs) were the **only drugs** available to **manage OA pain**
- However, **not all pets** responded to therapy with **some not tolerating NSAIDs**, leading to **an under-treatment** of OA
- Through a 2018 partnership with Regeneron, **Zoetis developed** the **first antibody technology** capable of **targeting NGF's**, offering veterinarians a **new alternative** to **effectively deal** with OA pain in all animals

Pain Products

Solensia



First **injectable mAb** therapy for **monthly alleviation** of OA pain in **cats**



Received **FDA approval** in January **2022**

Librela



First **injectable mAb** therapy for **monthly alleviation** of OA pain in **dogs**



Voted best new companion animal product

Expansion to New Industries

Acquisitions



Through these acquisitions, Zoetis is **expanding into new industries**, adding point-of-care diagnostic instruments, reference laboratory services, and **new strategies** to strengthen their diagnostics offerings, thus **enhancing value for veterinarians**

Vetscan Imagyst



Zoetis does not have any pure-play competitors for this technology, allowing for seamless integration of this product into the market

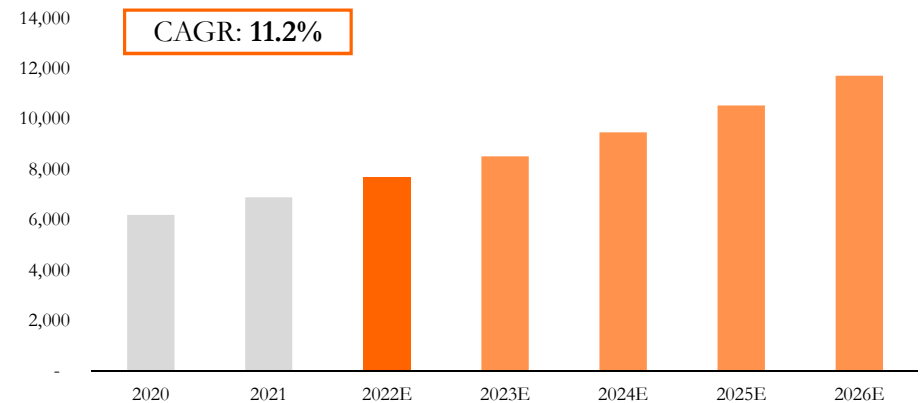


The addition of Digital Cytology Testing opens the door to same-day diagnosis and treatment, making Zoetis a strong competitor in the market

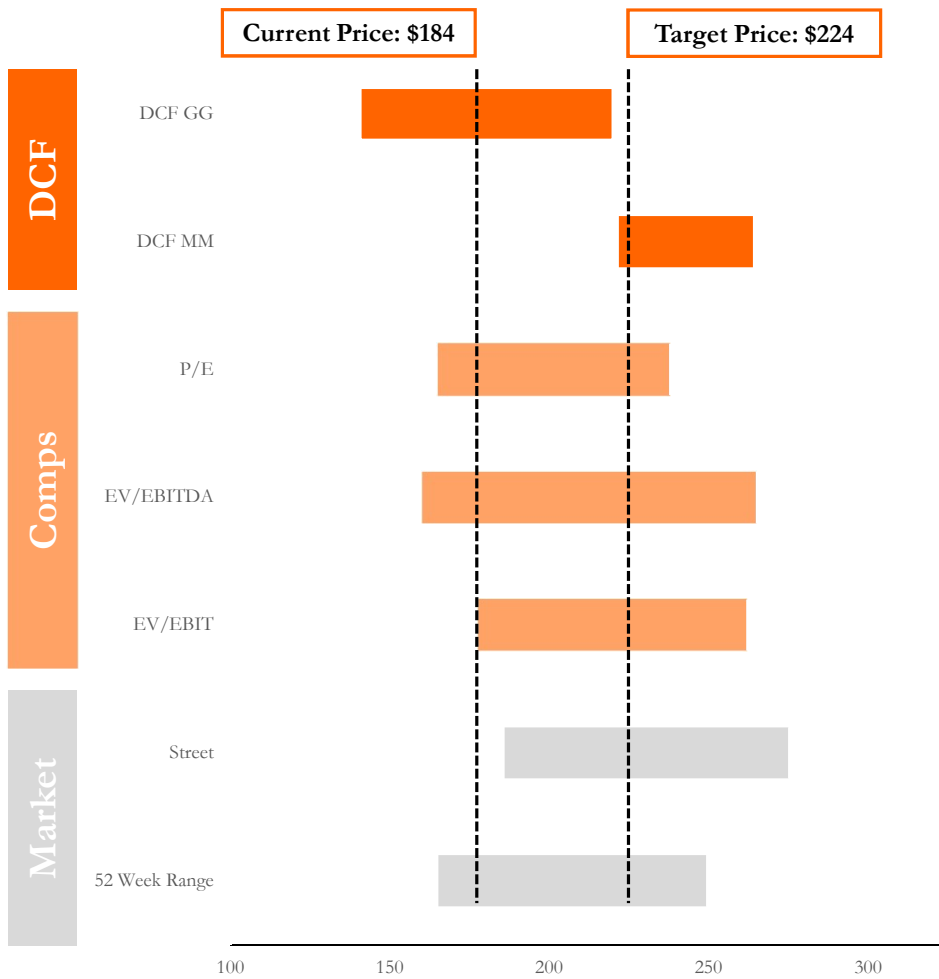
Geographic Expansion



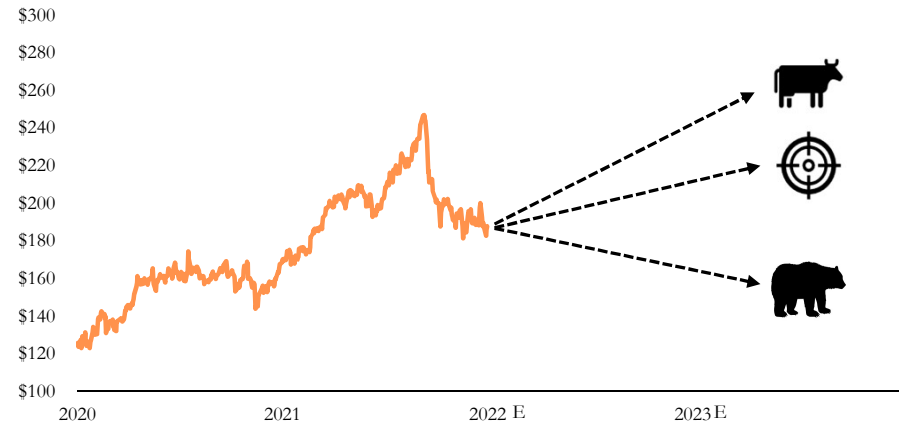
Animal Diagnostics Industry



Valuation



Bull vs. Bear



Analyst Rating

Cowen	BUY	\$252 PT
Morgan Stanley	BUY	\$264 PT
Stifel	BUY	\$275 PT
Barclays	BUY	\$245 PT
JP Morgan	BUY	\$250 PT

Risks and Mitigations

Zoetis's dermatology portfolio gets challenged by competitors within the industry

Zoetis portfolio already dominates the industry and has strong partnerships with veterinary clinics worldwide

Zoetis's OA medication for dogs (Librela) does not break into the US market nor receive FDA approval

Librela has shown repeated success during its debut in Europe, and with Solensia's recent approval, Librela soon follow

Zoetis fails to gain footing in the diagnostics industry as competition has made it hard to penetrate the market

Zoetis will be able to leverage their current partnerships to smoothly integrate new products into the pipeline

Conclusion

BUY : Zoetis

Price : \$184

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Upside : 21%

Thank You

Questions?

Appendix Overview

Appendix A: Income Statement

Appendix B: Balance Sheet

Appendix C: Cash Flow Statement

Appendix D: Revenue Build

Appendix E: NWC / D&A

Appendix F: WACC

Appendix G: Comparable Companies

Appendix H: DCF Analysis

Appendix I: Sensitivity Analysis

Appendix J: Revenue by Species

Appendix K: Revenue by Species

Appendix L: Operating Segment Results

Appendix M: Simparica TRIO vs. Competition

Appendix A: Income Statement



Zoetis Inc.								
Consolidated Statement of Operations								
<i>Figures in Millions</i>	2019	2020	2021	2022E	2023E	2024E	2025E	2026E
Revenue	6,260	6,675	7,776	8,588	9,552	10,562	11,630	12,742
<i>% growth</i>		7%	16%	10%	11%	11%	10%	10%
Costs and expenses:								
Cost of sales(a)	1,992	2,057	2,303	2,448	2,627	2,799	2,966	3,122
<i>% of revenue</i>	32%	31%	30%	29%	28%	27%	26%	25%
Selling, general and administrative expenses(a)	1,638	1,726	2,001	2,061	2,292	2,482	2,733	2,867
<i>% of revenue</i>	26%	26%	26%	24%	24%	24%	24%	23%
Research and development expenses(a)	457	463	508	544	582	622	666	712
<i>% of revenue</i>	7%	7%	7%	7%	7%	7%	7%	7%
Amortization of intangible assets(a)	155	160	161	180	201	222	244	268
<i>% of revenue</i>	2%	2%	2%	2%	2%	2%	2%	2%
Restructuring charges and certain acquisition-related costs	51	25	43	-	-	-	-	-
Income before Interest & Tax	1,967	2,244	2,760	3,355	3,850	4,437	5,021	5,773
Interest expense, net of capitalized interest	223	231	224	240	240	240	240	240
Other (income)/deductions-net	(57)	17	48	-	-	-	-	-
Income before provision for taxes on income	1,801	1,996	2,488	3,115	3,610	4,197	4,781	5,533
<i>% of revenue</i>	29%	30%	32%	36%	38%	40%	41%	43%
<i>% change</i>		4%	7%	13%	4%	5%	3%	6%
Provision for taxes on income	301	360	454	561	650	755	861	996
<i>Effective tax rate</i>	17%	18%	18%	18%	18%	18%	18%	18%
Net income before allocation to noncontrolling interest	1,500	1,636	2,034	2,555	2,961	3,442	3,920	4,537
Less: Net loss attributable to noncontrolling interests	-	(2)	(3)	-	-	-	-	-
Net income attributable to Zoetis	1,500	1,638	2,037	2,555	2,961	3,442	3,920	4,537
<i>% of revenue</i>	24%	25%	26%	30%	31%	33%	34%	36%

Appendix B: Balance Sheet



Zoetis Inc.			
Consolidated Balance Sheet			
<i>Figures in Millions</i>	2019	2020	2021
Assets			
Cash and cash equivalents(a)	1934 \$	3,604 \$	3,485
Accounts receivable, less allowance for doubtful accounts	1086	1,013	1,133
Inventories	1410	1,628	1,923
Other current assets	318	366	389
Total current assets	4748	6,611	6,930
Property, plant and equipment	1940	2,202	2,422
Operating lease right of use assets	189	192	181
Goodwill	2592	2,694	2,682
Identifiable intangible assets, less accumulated amortization	1890	1,710	1,474
Noncurrent deferred tax assets	88	94	100
Other noncurrent assets	98	106	111
Total assets	\$ 11,545	\$ 13,609	\$ 13,900
Liabilities and Equity			
Short-term borrowings	-	4	-
Current portion of long-term debt	500	600	-
Accounts payable	301	457	436
Dividends payable	95	119	154
Accrued expenses	543	556	710
Accrued compensation and related items	276	295	392
Income taxes payable	36	46	38
Other current liabilities	55	93	67
Total current liabilities	1,806	2,170	1,797
Long-term debt, net of discount and issuance costs	5947	6,595	6,592
Noncurrent deferred tax liabilities	434	378	320
Operating lease liabilities	164	163	151
Other taxes payable	257	260	257
Other noncurrent liabilities	229	270	239
Total liabilities	\$ 8,837	\$ 9,836	\$ 9,356

Appendix C: Cash Flow Statement



Zoetis Inc.				
Consolidated Statement of Cash Flows				
<i>Figures in Millions</i>	2019	2020	2021	
Operating Activities				
Net income before allocation to noncontrolling interests	\$ 1,500	\$ 1,636	\$ 2,034	
Adjustments to reconcile net income before noncontrolling interests to net cash provided by operating activities:				
Depreciation and amortization expense	412	441	448	
Share-based compensation expense	67	59	58	
Asset write-offs and asset impairments	7	43	47	
Net loss/(gain) on sales of assets	(20)	(19)	2	
Provision for losses on inventory	68	105	46	
Deferred taxes	(79)	(62)	(80)	
Loss on treasury locks	-	(6)	-	
Employee benefit plan contribution from Pfizer Inc	3	3	3	
Other non-cash adjustments	(12)	11	(2)	
Other changes in assets and liabilities, net of acquisitions and divestitures:				
Accounts receivable	(69)	74	(155)	
Inventories	(104)	(346)	(366)	
Other assets	(51)	(68)	(7)	
Accounts payable	(10)	147	(17)	
Other liabilities	91	91	227	
Other tax accounts, net	(8)	17	(25)	
Net cash provided by operating activities	1,795	2,126	2,213	
Investing Activities				
Capital expenditures	(460)	(453)	(477)	
Acquisitions, net of cash acquired	(195)	(113)	(14)	
Purchase of investments	-	-	(12)	
Proceeds from maturities and redemptions of investments	101	-	-	
Settlements on swaps designated as net investment hedges	37	(27)	44	
Net proceeds from sale of assets	21	21	2	
Other investing activities	(8)	-	(1)	
Net cash used in investing activities	(504)	(572)	(458)	
Financing Activities				
(Decrease)/increase in short-term borrowings, net	(9)	4	(4)	
Principal payments on long-term debt	-	(500)	(600)	
Proceeds from issuance of long-term debt-senior notes, net of discount	-	1,240	-	
Payment of consideration related to previous acquisitions	(9)	(2)	(6)	
Share-based compensation-related proceeds, net of taxes paid on withholding shares	7	20	(35)	
Purchases of treasury stock	(626)	(250)	(743)	
Cash dividends paid	(314)	(380)	(474)	
Payment of debt issuance costs	-	(12)	-	
Acquisition of a noncontrolling interest, net of cash acquired	-	3	-	
Net cash (used in)/provided by financing activities	(951)	123	(1,862)	

Appendix D: Revenue Build



Zoetis Inc.								
Revenue Build								
<i>Figures in Millions</i>	2019	2020	2021	2022E	2023E	2024E	2025E	2026E
Revenue by Species								
Companion Animal	3145	3652	4689	5439	6310	7193	8128	9103
<i>% Change</i>		16%	28%	16%	16%	14%	13%	12%
<i>% Total</i>	51%	55%	61%	63%	66%	68%	70%	71%
Livestock	3030	2940	3005	3065	3157	3283	3415	3551
<i>% Change</i>		-3%	2%	2%	3%	4%	4%	4%
<i>% Total</i>	49%	45%	39%	36%	33%	31%	29%	28%
Contract manufacturing & human health	85	83	82	84	85	86	87	88
<i>% Change</i>		-2%	-1%	2%	2%	1%	1%	1%
<i>% Total</i>	1%	1%	1%	1%	1%	1%	1%	1%
Revenue by Operating Segment								
U.S.	3203	3557	4042	4638	5254	5809	6396	7008
<i>% Change</i>		11%	14%	15%	13%	11%	10%	10%
<i>% Total</i>	52%	54%	53%	54%	55%	55%	55%	55%
International Revenue	2972	3035	3652	3950	4298	4753	5233	5734
<i>% Change</i>		2%	20%	8%	9%	11%	10%	10%
<i>% Total</i>	48%	46%	47%	46%	45%	45%	45%	45%
Total Revenue	6175	6592	7694	8588	9552	10562	11630	12742
<i>Growth Rate</i>		7%	17%	12%	11%	11%	10%	10%

Appendix E: NWC / D&A



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Revenue by Species								
Companion Animal	3145	3652	4689	5439	6310	7193	8128	9103
<i>% Change</i>		16%	28%	16%	16%	14%	13%	12%
<i>% Total</i>	51%	55%	61%	63%	66%	68%	70%	71%
Livestock	3030	2940	3005	3065	3157	3283	3415	3551
<i>% Change</i>		-3%	2%	2%	3%	4%	4%	4%
<i>% Total</i>	49%	45%	39%	36%	33%	31%	29%	28%
Contract manufacturing & human health	85	83	82	84	85	86	87	88
<i>% Change</i>		-2%	-1%	2%	2%	1%	1%	1%
<i>% Total</i>	1%	1%	1%	1%	1%	1%	1%	1%
Revenue by Operating Segment								
U.S.	3203	3557	4042	4638	5254	5809	6396	7008
<i>% Change</i>		11%	14%	15%	13%	11%	10%	10%
<i>% Total</i>	52%	54%	53%	54%	55%	55%	55%	55%
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Total Revenue	6175	6592	7694	8588	9552	10562	11630	12742
<i>Growth Rate</i>		7%	17%	12%	11%	11%	10%	10%

Appendix F: WACC

Zoetis, Inc	
Weighted Average Cost of Capital	
Market Value of Debt	6,743
Weight of Debt	7%
Pre-Tax Cost of Debt	4.42%
After-Tax Cost of Debt	3.54%
Market Value of Equity	88,111
Weight of Equity	93%
Market Return	9.0%
Risk-Free-Rate	2.83%
Equity Risk Premium	6.00%
Beta	0.85
Cost of Equity	7.92%
Weighted Average Cost of Capital	7.61%

Interest Expense Ratio	
EBIT	2,760
Interest Expense	224
Coverage Ratio	12.32
Spread	1.59%
Risk-Free-Rate	2.83%
Cost of Debt	4.42%

DSO	477
Share Price	184.72

Appendix G: Comparable Companies



Comparable Companies Analysis (\$USD in Millions)

Company	Ticker	Industry	Share Price	Shares Outstanding	Market Capitalization	Debt	Cash	Enterprise Value	EPS	LTM EBIT	LTM EBITDA	LTM R&D
Zoetis Inc.	ZTS	Specialty Pharmaceutical	184.72	477	88,111	6,743	3,485	91,369	\$ 4.27	2,982	3,430	508
Elanco Animal Health	ELAN	Specialty Pharmaceutical	26.25	487	12,784	6,480	638	18,626	\$ 1.06	711	1,427	369
IDEXX Laboratories	IDXX	Specialty Pharmaceutical	496.78	86	42,723	930	145	43,509	\$ 8.70	954	1,064	161
Dechra Pharama	DPH	Specialty Pharmaceutical	38.00	109	4,142	317	124	4,335	\$ 0.69	103	118	52

Average

Min

Q1

Median

Q3

Max

Comps Output	EV	Debt	Cash	Equity	Shares	Per Share	22' EBIT 22' EBITDA 22' R&D			P/E EV/EBIT EV/EBITDA EV/R&D EV/22' EBIT EV/22' EBITDA EV/22' R&D								
EBIT	2,982																	
Min	26x	78,118	6743	3485	74,860	477 \$ 156.94	3,312	3,643	560	43x	31x	27x	180x	28x	25x	163x		
Q1	30x	88,057	6743	3485	84,799	477 \$ 177.77	1,015	1,161	405	25x	26x	13x	50x	18x	16x	46x		
Median	36x	108,437	6743	3485	105,179	477 \$ 220.50	1,046	1,178	184	57x	46x	41x	270x	42x	37x	236x		
Q3	43x	128,142	6743	3485	124,884	477 \$ 261.81	176	190	62	55x	42x	37x	83x	25x	23x	70x		
Max	46x	136,056	6743	3485	132,798	477 \$ 278.40												
EBITDA	3,430									45x	36x	29x	146x	28x	25x	129x		
Min	13x	44,770	6743	3485	41,512	477 \$ 87.03				25x	26x	13x	50x	18x	16x	46x		
Q1	23x	79,719	6743	3485	76,461	477 \$ 160.30				39x	30x	23x	75x	23x	21x	64x		
Median	32x	108,689	6743	3485	105,431	477 \$ 221.03				49x	36x	32x	132x	26x	24x	117x		
Q3	38x	129,584	6743	3485	126,326	477 \$ 264.84				56x	43x	38x	202x	31x	28x	181x		
Max	41x	140,311	6743	3485	137,053	477 \$ 287.32				57x	46x	41x	270x	42x	37x	236x		
P/E	\$ 4.27																	
Min	25x					\$ 105.88												
Q1	39x					\$ 165.01												
Median	49x					\$ 210.12												
Q3	56x					\$ 237.64												
Max	57x					\$ 243.98												

Appendix H: DCF Analysis



Zoetis Inc.								
Discounted Cash Flow Analysis								
<i>Figures in Millions</i>	2019	2020	2021	2022E	2023E	2024E	2025E	2026E
Revenue	6,260	6,675	7,776	8,588	9,552	10,562	11,630	12,742
<i>% growth</i>		7%	16%	10%	11%	11%	10%	10%
EBIT	1,967	2,244	2,760	3,355	3,850	4,437	5,021	5,773
<i>EBIT Margin</i>	31%	34%	35%	39%	40%	42%	43%	45%
Taxes	301	360	454	671	770	887	1,004	1,155
<i>Rate %</i>	17%	18%	18%	20%	20%	20%	20%	20%
NOPAT	1,639	1,840	2,258	2,684	3,080	3,550	4,017	4,619
Plus: D&A	412	441	448	474	444	496	558	494
Less: CapEx	460	453	477	515	478	528	581	510
Less: Δ NWC	-	24	305	247	229	249	237	280
Free Cash Flow	1,591	1,804	1,924	2,396	2,818	3,269	3,757	4,324
<i>Discount Factor</i>				0.5	1.5	2.5	3.5	4.5
<i>% change</i>				25%	18%	16%	15%	15%
Present Value of Cash Flows				2,310	2,524	2,721	2,906	3,109

Terminal Value Calculations

Perpetuity Method

Terminal Cash Flow	4,324
WACC	7.61%
Terminal Growth Rate	2.75%
Terminal Value	91,467
PV of Terminal Value	65,763

Enterprise Value

Less: Debt	6,743
Add: Cash	3,485

Equity Value

DSO

Price Per Share

Terminal Multiple Method

Terminal EBITDA	6,268
WACC	7.61%
EV/EBITDA	24
Terminal Value	150,427
PV of Terminal Value	108,154

Enterprise Value

Less: Debt	6,743
Add: Cash	3,485

Equity Value

477 DSO

159.49 Price Per Share

121,724

6,743

3,485

118,466

477

248.36

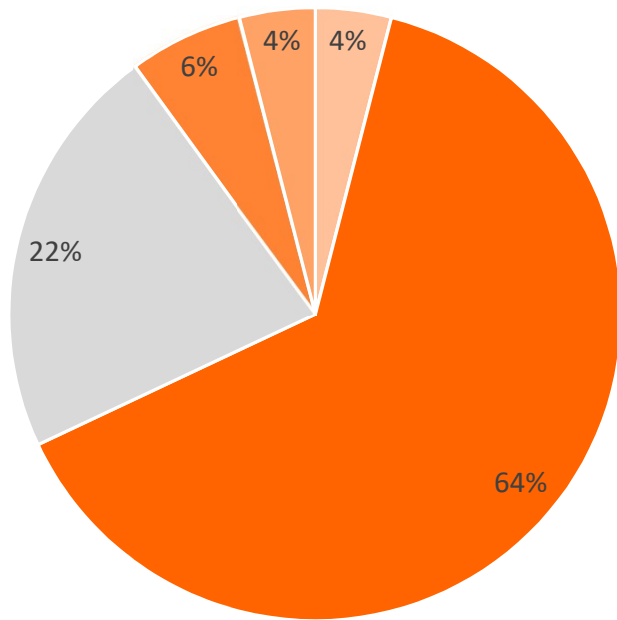
Appendix I: Sensitivity Analysis

		Terminal Growth Rate				
		2.00%	2.50%	3.00%	3.50%	4.00%
WACC	6.50%	177.17	197.37	223.34	257.96	306.44
	7.00%	158.43	174.32	194.19	219.74	253.80
	7.50%	143.10	155.90	171.53	191.08	216.22
	8.00%	130.34	140.83	153.42	168.80	188.04
	8.50%	119.54	128.28	138.60	150.99	166.13

		EV/EBITDA				
		22	23	24	25	26
WACC	6.50%	239.36	249.26	259.16	269.06	278.95
	7.00%	234.82	244.51	254.20	263.89	273.59
	7.50%	230.40	239.89	249.37	258.86	268.35
	8.00%	226.08	235.37	244.67	253.96	263.26
	8.50%	221.87	230.98	240.08	249.18	258.29

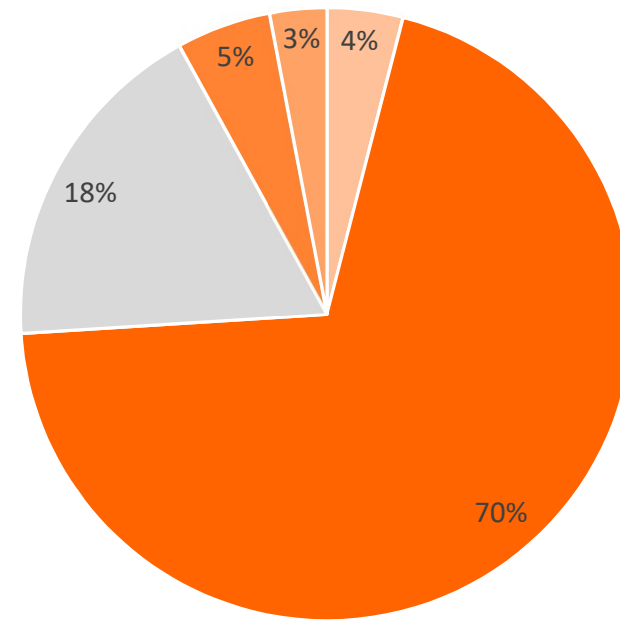
Appendix J – Revenue by Species

2020 United States Segment Revenue - By Species



■ Horse ■ Dogs/Cats ■ Cattle ■ Poultry ■ Swine

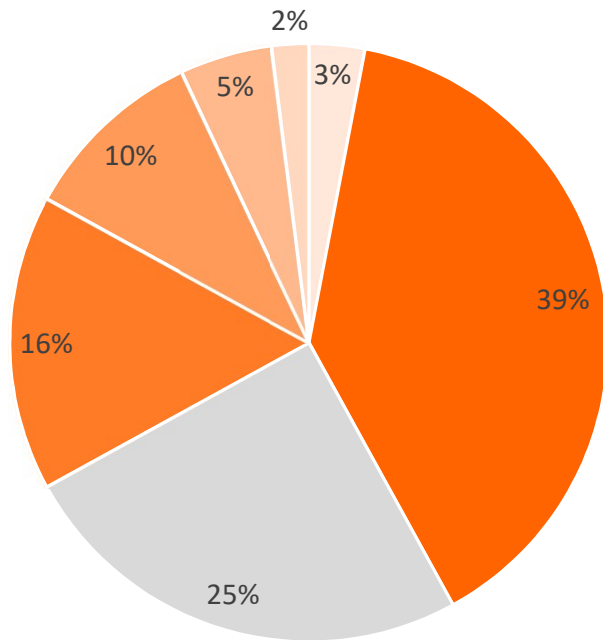
2021 United States Segment Revenue - By Species



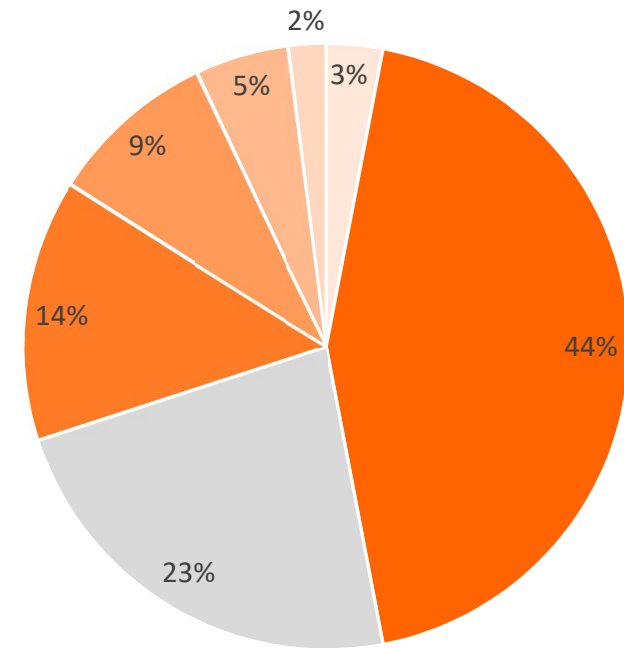
■ Horse ■ Dogs/Cats ■ Cattle ■ Poultry ■ Swine

Appendix K – Revenue by Species

2020 International Segment Revenue - By Species



2021 International Segment Revenue - By Species



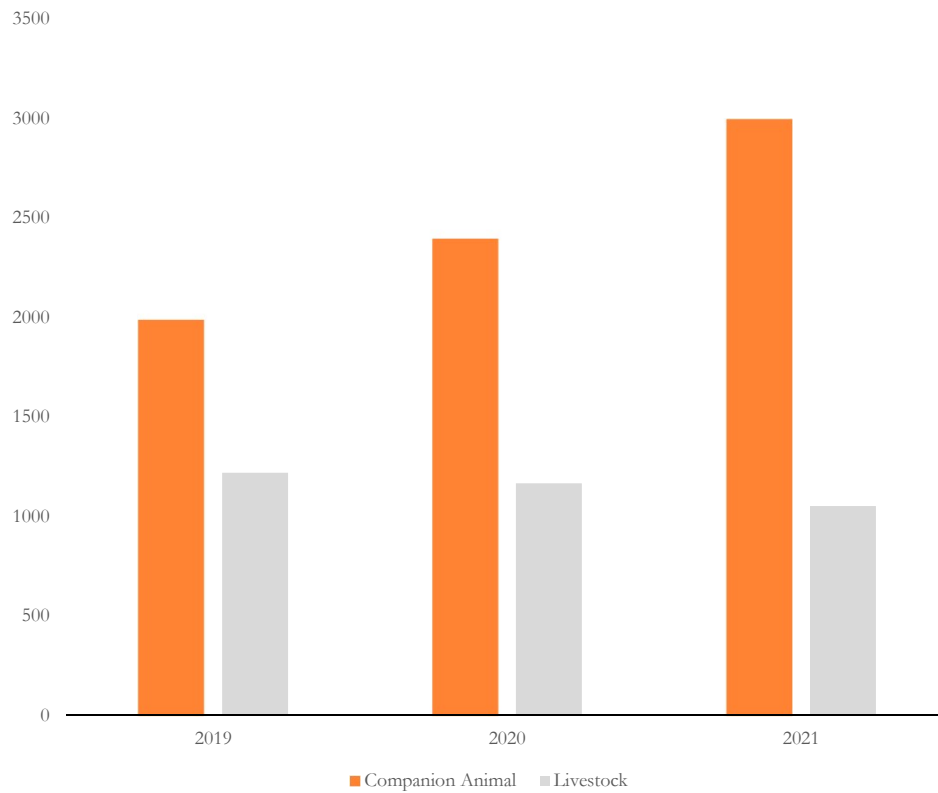
■ Horses ■ Dogs/Cats ■ Cattle ■ Swine ■ Poultry ■ Fish ■ Sheep

■ Horses ■ Dogs/Cats ■ Cattle ■ Swine ■ Poultry ■ Fish ■ Sheep

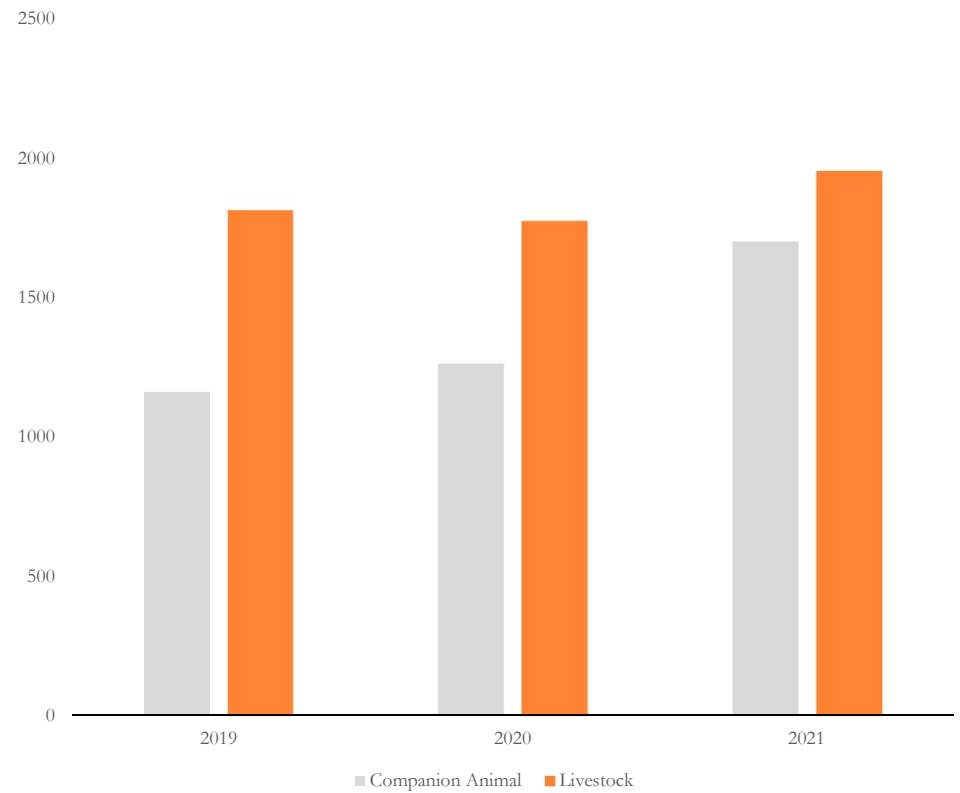
Appendix L – Operating Segment Results



US Revenue Growth



International Revenue Growth



Appendix M: Simparica TRIO vs. Competition

	 <small>gabapentin, moxidectin, and praziquantel chewable tablets</small>	Heartgard® Plus ¹	NexGard® ²	Bravecto® ³	Credelio® ⁴	Interceptor® Plus ⁵
Prevents Lyme Infections*	✓		✓			
Prevents Heartworm Disease	✓	✓				✓
Kills 5 Types of Ticks	✓		4 types	4 types	4 types	
Kills Fleas	✓		✓	✓	✓	
Kills Fleas Before They Can Lay Eggs	✓		✓	✓	✓	
Treats Roundworms	✓	✓				✓
Treats Hookworms	✓	✓				✓
Approved for Dogs 8 Weeks+	✓	✓	✓		✓	✓
Approved for Dogs 2.8lbs+	✓	✓	4lbs+	4.4 lbs +	4.4 lbs +	✓

