

Equity Research

May 16, 2016

Price: \$41.91 (05/13/2016)

Price Target: \$49.00

MARKET PERFORM (2)

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Key Data

Symbol	NYSE: GSK
52-Week Range:	\$44.98 - 36.70
Market Cap (MM):	\$102,083.4
Net Debt (MM):	\$10,727.0
Cash/Share:	NA
Dil. Shares Out (MM):	2,435.8
Enterprise Value (MM):	\$87,297.0
ROIC:	NA
ROE (LTM):	NA
BV/Share:	NA
Dividend:	\$2.22
Yield:	5.30%

FY (Dec)	2015A	2016E	2017E
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Earnings Per Share

Q1	p17.30	p19.80A	p21.30
<i>Prior Q1</i>	-	-	<i>p18.30</i>
Q2	p17.30	p20.00	p20.70
<i>Prior Q2</i>	-	-	<i>p18.40</i>
Q3	p23.00	p28.50	p28.70
<i>Prior Q3</i>	-	<i>p25.90</i>	<i>p26.90</i>
Q4	p18.10	p20.70	p21.30
<i>Prior Q4</i>	-	<i>p18.70</i>	<i>p20.40</i>
Year	p75.70	p89.00	p92.00
<i>Prior Year</i>	-	<i>p84.40</i>	<i>p84.00</i>
Core EPS			

Revenue (MM)

Year	£23,923.0	£25,710.0	£26,470.0
<i>Prior Year</i>	-	<i>£25,150.0</i>	<i>£25,810.0</i>
EV/S	2.2x	2.0x	2.0x

Company Update

Consumer Outlook Healthy; Estimates Raised Post Q1 Model Update

The Cowen Insight

Meeting with head of GSK Consumer highlighted significant potential. Separately, we are raising turnover and EPS estimates post Q1 model update.

Consumer Outlook Remains Encouraging

The new GSK/NVS Consumer segment includes seven "power brands" (Voltaren, Panadol, Sensodyne, Theraflu, Otrivin, Paradontax, and Poligrip) and 12 core brands which are expected to drive 90%+ of growth (brand loyalty, geographic expansion, and line extensions key). These power brands offer above-average gross margins, and are key to meeting the 20% operating margin target in 2020. Consumer margins in the Developed and Emerging world are not that much different from one another. Switch (Rx-to-OTC) product Flonase is off to a very successful start; it was launched in February 2015 and is already a top-3 nasal allergy OTC product in the U.S. Private label brands (20% share as of Q1:16) and generic Rx Nasonex may add some competitive pressure. Glaxo has had 9 switch products over the past 25 years and expects to add at least one every 5 years; "switchability" and turnover potential are criteria GSK considers when evaluating candidates. Management is targeting mid-single turnover growth (at/just ahead of 4% industry growth). Each of the four Consumer segments (OTC, Oral Care, Nutrition, Skin Care) deliver similar growth and there is not a major difference in profitability. GSK Consumer operates in 160 countries. Over time, Emerging Markets are expected to become a larger portion of total Consumer, and the U.S. is critical to success. China offers the world's largest e-commerce opportunity. Expectations for China overall have been rebased. GSK operates separate Rx and Consumer sales forces in the majority of markets. We estimate Consumer sales of £6.64B (+10%) in 2016, £7.355B in 2018, and £8.795B in 2022.

JV With NVS Trending Well; Margin Target Achievable

The JV (established March 2015, GSK share 63.5%) appears to have met/exceeded internal expectations. Integration efforts have progressed quickly. Former Novartis executives now represent roughly one-third of the new Consumer division management team. The biggest area of focus across the JV is innovation. As an example, Glaxo has recently hired a new head of R&D. GSK Consumer operating margin expansion is expected to be driven roughly 50% from synergies and the remaining 50% from a combination of mix, P&L leverage, improved procurement efficiencies, more effective A&P spend (A&P remains critical to Consumer success), and COGS benefits (targeted annual 10% SKU reduction, less use of contract manufacturing). Future Consumer M&A is a board decision, which involves both GSK and NVS representatives.

GlaxoSmithKline Annual Product Sales Buildup (£MM) (continued)

	2015	2016E	2017E	2018P	2019P	2020P	2021P	2022P	2016-20 CGR	2016-22 CGR	Comment
3377794					25	50	75	100	NM	NM	NY-ESO-1 T cell receptor; cancer; Phase
Tarextumab					25	50	75	100	NM	NM	Anti-notch 2/3 mAB; pancreatic and ova
Other Oncology/emesis	16										
Oncology	216				50	100	150	200	NM	NM	Sold to Novartis for \$16B, \$1.5B of which 3/2/15
% Change	-82%										
Flolan - U.S. (lc, ex fx)											
Flolan - U.S.	17	20	25	30	35	40	45	50	19%	16%	
Flolan - EU (lc, ex fx)											
Flolan - EU	8	10	15	20	25	30	35	40	32%	26%	
Flolan - EM											
Flolan - ROW	33	35	40	45	50	55	60	65	12%	11%	
Flolan	58	65	80	95	110	125	140	155	18%	16%	Pulmonary arterial hypertension
Volibris - U.S. (lc, ex fx)											
Volibris - U.S.											
Volibris - EU (lc, ex fx)											
Volibris - EU	91	110	130	150	170	190	210	230	15%	13%	
Volibris - EM											
Volibris - ROW	61	75	100	120	140	160	180	200	21%	18%	
Volibris	152	185	230	270	310	350	390	430	17%	15%	Pulmonary arterial hypertension
2696273				25	50	75	100	125	NM	NM	Ex-vivo stem cell gene therapy; ADA-SCI
2998728				25	50	75	100	125	NM	NM	Transthyretin-mediated amyloidosis; Pha
2696274					25	50	75	100	NM	NM	Ex-vivo stem cell gene therapy; metachro
2696275					25	50	75	100	NM	NM	Ex-vivo stem cell gene therapy; Wiscott-A
2398852 + 23156898					25	50	75	100	NM	NM	SAP mAB + SAP depleter; amyloidosis; P
Other	161	175	190	200	210	220	230	240	6%	5%	
Rare Diseases	371	425	500	615	805	995	1,185	1,375	24%	22%	
% Change	-11%	15%	18%	23%	31%	24%	19%	16%			
Avodart - U.S. (lc, ex fx)											
Avodart - U.S.	166	5	0	0	0	0	0	0	NM	NM	Patent expired 2015; generic launched 10
Avodart - EU (lc, ex fx)											
Avodart - EU	254	285	190	100	50	25	10	5	-46%	-49%	Patent expires 2017
Avodart - EM											
Avodart - Japan											
Avodart - ROW	237	215	195	175	155	135	115	95	-11%	-13%	
Avodart	657	505	385	275	205	160	125	100	-25%	-24%	BPH; good growth despite finasteride ge

Source: Company data, Cowen and Company estimates