

Emergent BioSolutions (EBS - \$30.76)

1Q17: Softer BioThrax Sales but FY17 Guidance Reiterated

EBS reported 1Q17 last night after the close with top and bottom line mostly in line with expectations. In fact, total revenues of ~\$117M slightly topped our estimated \$115M and adjusted bottom line of \$0.29 beat our estimated \$0.25. However, upon closer examination, we noticed BioThrax sales \$43.8M significantly missed our estimated \$55M, mostly due to the timing of BioThrax shipments. This was countered by Other Biodefense sales of ~\$38.2M vs. our estimated \$15M as a result of the timing of ~\$30M botulism antitoxin (BAT) sales to the Strategic National Stockpile (SNS). While Biothrax sales were softer than anticipated and EBS expects sales of only \$100M-\$115M in 2Q17, they have reiterated their FY17 forecast of \$500M-\$530M total revenue (BioThrax sales: \$265M-\$280M), GAAP net income of \$60M - \$70M, adjusted net income of \$70M to \$80M and EBITDA of \$135M - \$145M. We have adjusted our model accordingly and view their confidence in the FY guidance as a real positive at these levels. Additionally, on the FY16 EPS call, EBS reiterated their aspirational guidance of \$1B in top line revenues by 2020. Management believes an acquisition could be completed by year end, which should provide significant upside. With ~\$270M in cash at the end of 1Q17, we believe EBS has the ability to make a significant acquisition in the near term and are reiterating our Buy rating and \$50 price target.

- **Slow 1H17 Biothrax sales with FY17 guidance reiterated could signal opportunity.** While Biothrax sales are slow out of the blocks in 2017, we see the modest 2Q17 guidance (\$100M-\$115M) and reiteration of FY17 top-line (\$500-\$530M) with a potential acquisition (not included in guidance) as an interesting opportunity at these levels.
- **Aspirational \$1B top-line by 2020, deadline approaching quickly.** As 2020 is around the corner, EBS maintained that organic growth and M&A will help attain the \$1B goal. They are still targeting the CBRN, explosives, and emerging infectious disease accretive companies or products.
- **Reiterate Buy rating \$50 price target.** Our price target is based on a sum-of-the-parts analysis, with a base business DCF value of \$42/share, cash (net of debt) and tech value of \$8/share.

Adj-Earnings Estimates: (per share)

(Dec)	1Q	2Q	3Q	4Q	FY	P/E
FY18E	0.46	0.54	0.62	0.64	2.26	13.6x
FY17E	0.29A	0.25	0.45	0.67	1.65	18.6x
FY16A	0.16	(0.18)	0.64	0.74	1.39	22.1x
FY15A	(0.50)	0.36	0.83	0.78	1.60	19.2x

Source: Laidlaw & Company estimates

Healthcare / Biotechnology

Ticker:	EBS
Rating:	Buy
Price Target:	\$50

Trading Data:

Last Price (05/04/2017)	\$30.76
52-Week High (06/07/2016)	\$44.38
52-Week Low (11/03/2016)	\$24.47
Market Cap. (MM)	\$474.3
Shares Out. (MM)	40.96

Analyst

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Figure 1: Variance Analysis

Emergent BioSolutions					
Quarterly Variance Analysis					
<i>(\$000 except per share)</i>	1Q16A	1Q17A	1Q17E	Variance	% Y/Y
BioThrax sales	\$59,100	\$43,800	\$55,000	(\$11,200)	-25.9%
Contract manufacturing	7,587	17,628	20,000	(2,372)	132.3%
Other Biodefense	4,658	38,169	15,000	23,169	719.4%
Contracts and Grants	31,709	17,261	25,000	(7,739)	-45.6%
Total Revenue	\$111,002	\$116,858	\$115,000	\$1,858	5.3%
COGS	25,803	43,922	37,250	6,672	70.2%
Gross Profit	85,199	72,936	77,750	(4,814)	-14.4%
SG&A Expense	37,484	31,850	30,000	1,850	-15.0%
<i>R&D ex-ctrcs & grnts</i>	<i>2,445</i>	<i>3,215</i>	<i>3,000</i>	<i>215</i>	<i>31.5%</i>
R&D Expense	34,154	20,476	28,000	(7,524)	-40.0%
Operating Income	13,561	20,610	19,750	860	52.0%
Interest Expense	1,524	1,938	1,750	188	27.2%
Int. & Inv. Income	186	373	400	(27)	100.5%
Other Inc./ (Exp)	116	300	100	200	NA
Pretax Income	12,339	19,345	18,500	845	56.8%
Tax exp/(benefit)	4,818	5,160	5,920	(760)	NA
Adj-Net Income	7,521	14,185	12,580	1,605	88.6%
Shares out (000)	48,360	49,718	49,973	(254)	2.8%
Adj-Earnings Per Share	\$0.16	\$0.29	\$0.25	\$0.03	83.5%

Source: Company reports; Laidlaw & Company estimates

Figure 2: Valuation

Sum-of-the-parts valuation		
Segment	Valuation (000's)	Per share value
DCF of base business	\$2,115,840	\$42
Net Cash, end '16E	\$248,230	\$5
Technology value	\$150,000	\$3
SUM	\$2,514,071	\$50
Fully diluted shares out '17E (000)		50,318

Source: Company reports; Laidlaw & Company estimates

Figure 3: Quarterly Income Statement

Emergent BioSolutions										
Quarterly income statement										
(\$000 except per share)	2016A				2016A Year	2017E				2017E Year
	1QA	2QA	3QA	4QA		1QA	2QE	3QE	4QE	
BioThrax - US sales	\$59,100	\$40,000	\$94,100	\$43,800	\$237,000	\$43,800	\$55,000	\$75,000	\$92,500	\$266,300
NuThrax - US sales										
OUS Biodefense sales						0	0	2,500	5,000	7,500
Other Biodefense	4,658	8,300	2,598	43,693	59,249	38,169	17,500	17,500	16,000	89,169
Total Biodefense	63,758	48,300	96,698	87,493	296,249	81,969	72,500	95,000	113,500	362,969
Total Biosciences	7,948	10,200	3,109		21,257					
Contract manufacturing	7,587	10,200	14,712	16,683	49,182	17,628	17,500	17,500	17,500	70,128
Contracts & grants	31,709	32,787	31,504	47,487	143,487	17,261	15,000	15,000	17,500	64,761
Total revenues	\$111,002	\$101,487	\$146,023	\$151,663	\$510,175	\$116,858	\$105,000	\$127,500	\$148,500	\$497,858
Expenses										
COGS	25,803	35,612	38,460	36,159	136,034	43,922	37,250	42,100	46,300	169,572
Gross margin	85,199	65,875	107,563	115,504	374,141	72,936	67,750	85,400	102,200	328,286
% product sales	67%	48%	66%	65%	63%	56%	59%	63%	65%	61%
R&D	34,154	33,947	27,188	27,117	122,406	20,476	20,000	20,000	20,000	80,476
SG&A	37,484	40,148	27,388	30,858	135,878	31,850	27,500	30,000	30,000	119,350
Operating income	13,561	(8,220)	52,987	57,529	115,857	20,610	20,250	35,400	52,200	128,460
Interest expense	1,524	1,509	2,049	2,535	7,617	1,938	2,250	2,500	2,500	9,188
Interest income, net	186	220	358	289	1,053	373	200	200	250	1,023
Other income/(expense)	116	17	(134)	439	438	300	100	100	100	600
Pretax income (loss)	12,339	(9,492)	51,162	55,722	109,731	19,345	18,300	33,200	50,050	120,895
Tax exp/(benefit)	4,818	(2,345)	19,565	19,136	41,174	5,160	5,856	10,624	16,016	37,656
Loss to non-ctrl interest										
Adjusted Net Income	7,521	(7,147)	31,597	36,586	68,557	14,185	12,444	22,576	34,034	83,239
Non-cash charges	(3,530)	(3,800)	(8,100)	(4,300)	(19,730)	(3,800)				
GAAP net income	3,991	(10,947)	23,497	32,286	48,827	10,385				
EPS ex non-cash items	\$0.16	(\$0.18)	\$0.64	\$0.74	\$1.39	\$0.29	\$0.25	\$0.45	\$0.67	\$1.65
EPS as reported	\$0.08	(\$0.27)	\$0.48	\$0.65	\$0.99	\$0.21				
Fully diluted shares (000)	48,360	40,203	49,440	49,573	49,335	49,718	50,118	50,518	50,918	50,318

Source: Bloomberg LP; Company reports; Laidlaw & Company estimates

Figure 4: Annual Income Statement

Emergent BioSolutions							
Annual income statement							
(\$000 except per share)	2015A	2016A	2017E	2018E	2019E	2020E	Comments
BioThrax - US sales	\$293,900	\$237,000	\$266,300	\$309,000	\$310,000	\$25,500	'17E guide: \$265M-\$280M
NuThrax - US sales					25,000	318,500	Launch 2019
OUS Biodefense sales			7,500	24,000	25,000	26,000	OUS sales ~10% of US sales
Other Biodefense	<u>34,994</u>	<u>59,249</u>	<u>89,169</u>	<u>70,000</u>	<u>75,000</u>	<u>85,000</u>	RSDL, BAT, other Biodefense here
Total Biodefense	328,894	296,249	362,969	403,000	435,000	455,000	
Total biosciences	28,068	21,257					Spun out mid-2016
Contract manufacturing	42,968	49,182	70,128	85,000	100,000	111,000	Acquired with Cangene 3Q13
Contracts & grants	122,905	143,487	64,761	92,000	90,000	85,000	Offset in R&D
Total revenues	\$522,789	\$510,175	\$497,858	\$580,000	\$625,000	\$651,000	'17E guide: \$500M-\$530M 2020 guide: \$1B in revenue
Expenses							
COGS	112,895	136,034	169,572	193,020	215,015	221,990	
Gross margin	409,894	374,141	328,286	386,980	409,985	429,010	
% product sales	72%	63%	61%	60%	60%	61%	Cangene impacts margins
R&D	153,997	122,406	80,476	90,000	100,000	110,000	ex-Biosciences R&D in 2017
SG&A	141,758	135,878	119,350	124,000	130,000	132,000	
Operating income	114,139	115,857	128,460	172,980	179,985	187,010	'17E EBITDA: \$135M-\$145M
Interest expense	6,523	7,617	9,188	7,475	7,900	8,400	
Interest income, net	572	1,053	1,023	1,500	2,750	3,350	
Other inc/(exp)	(319)	438	600	400	400	400	
Pretax income	107,869	109,731	120,895	167,405	175,235	182,360	
Tax expense	32,299	41,174	37,656	50,222	52,571	54,708	
Loss to non-cont. int	0	0	0	0	0	0	
Adj-Net income	75,570	68,557	83,239	117,184	122,665	127,652	'17E adj-NI: \$70M-\$80M
Non-cash charges	(12,700)	(19,730)					
GAAP net income	62,870	48,827					'17E GAAP NI: \$60M-\$70M
EPS ex non-cash items	\$1.60	\$1.39	\$1.65	\$2.26	\$2.30	\$2.30	+10% CAGR 2016-2020E
EPS as reported	\$1.33	\$0.99					
Fully diluted shares (000)	47,256	49,335	50,318	51,918	53,368	55,493	

Source: Bloomberg LP; Company reports; Laidlaw & Company estimates

Major Risks

Exogenous events could impact our outlook. We believe pharmaceutical companies have the least control over competitive, political, and regulatory risks. Although we have incorporated competitive assumptions into our forecasts, there may be other risks beyond the scope of our analysis. Changes in the drug reimbursement system, as well as any political or regulatory amendments, may significantly influence the earnings power of these companies.

Actual clinical results and the FDA's conclusions may deviate from expectations. Many of our assumptions are based on a review of incomplete clinical trial data available in the public domain. Often, our conclusions are drawn from early stage data, which may not be reflected by pivotal studies. Furthermore, the FDA's conclusions may not coincide with our own, materially changing our revenue and earnings assumptions.

Compliance issues, product recalls, and other mandates by regulatory authorities could materially change our expectations. Regulatory compliance issues, ranging from accounting irregularities to defective manufacturing practices, could materially change our assumptions and earnings outlook. Unanticipated product recalls and labeling changes could also have adverse consequences on our earnings assumptions.

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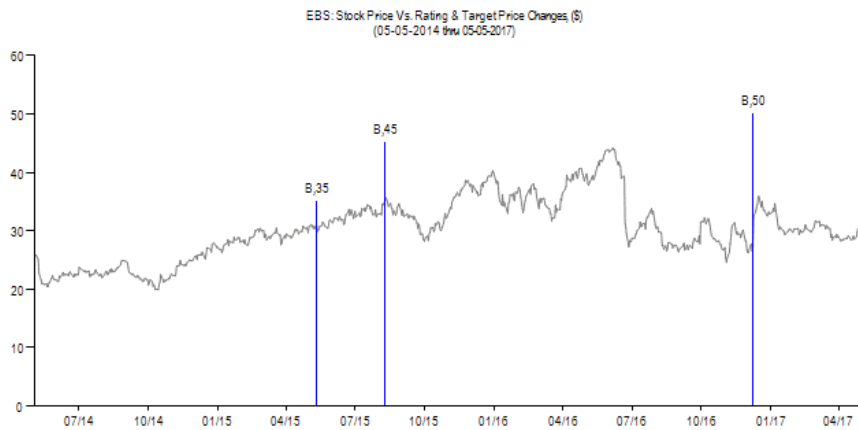
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3 Year Rating Change History

Date	Rating	Closing Price (\$)
05/11/2...	Buy (B)	31.11

3 Year Price Change History

Date	Target Price (\$)	Closing Price, (\$)
05/11/2...	35.00	31.11
08/10/2...	45.00	35.29
12/09/2...	50.00	32.37

Source: Laidlaw & Company

Created by: Blue-Compass.net

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			Investment Banking	Brokerage
Strong Buy (SB)	Expected to significantly outperform the sector over 12 months.	2.27%	2.27%	0.00%
Buy (B)	Expected to outperform the sector average over 12 months.	61.36%	29.55%	2.27%
Hold (H)	Expected returns to be in line with the sector average over 12 months.	0.00%	0.00%	0.00%
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