

Zoetis Inc.(ZTS)

\$141.93 (As of 01/21/20)

Price Target (6-12 Months): **\$150.00**

Long Term: 6-12 Months

Zacks Recommendation:

Neutral

(Since: 08/01/19)

Prior Recommendation: Outperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

3-Hold

Zacks Style Scores:

VGM:B

Value: D

Growth: B

Momentum: A

Summary

Zoetis' performance in the past year has been stellar on the back of growth in new parasiticide products (Simparica and Stronghold Plus) and vaccines, a solid dermatology portfolio and the addition of Abaxis' diagnostics platform. Key dermatology products such as Apoquel and Cytopoint continue to penetrate the market and generate additional revenues. The Abaxis acquisition has further strengthened its leading portfolio. Zoetis has been making other prudent acquisitions as well. Moreover, Zoetis' five-year collaboration agreement with Regeneron will further diversify its portfolio. Shares have outperformed the industry in the year so far. However, the cattle market is witnessing challenging market conditions for beef and dairy customers. Moreover, the swine market is being affected by the African swine fever in China.

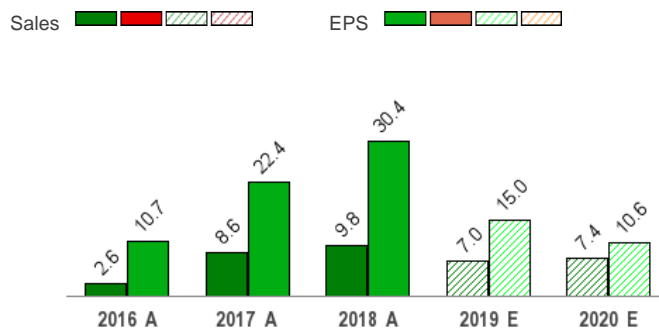
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$142.52 - \$82.80
20 Day Average Volume (sh)	1,490,249
Market Cap	\$67.6 B
YTD Price Change	7.2%
Beta	0.81
Dividend / Div Yld	\$0.80 / 0.6%
Industry	Medical - Drugs
Zacks Industry Rank	Top 43% (110 out of 255)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	5.6%
Last Sales Surprise	0.2%
EPS F1 Est- 4 week change	-0.1%
Expected Report Date	02/13/2020
Earnings ESP	0.9%
P/E TTM	40.4
P/E F1	35.7
PEG F1	3.1
P/S TTM	11.0

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2020	1,528 E	1,663 E	1,722 E	1,750 E	6,692 E
2019	1,455 A	1,547 A	1,584 A	1,639 E	6,230 E
2018	1,366 A	1,415 A	1,480 A	1,564 A	5,825 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2020	\$0.91 E	\$0.99 E	\$1.06 E	\$1.02 E	\$3.98 E
2019	\$0.88 A	\$0.90 A	\$0.94 A	\$0.88 E	\$3.60 E
2018	\$0.75 A	\$0.77 A	\$0.83 A	\$0.79 A	\$3.13 A

*Quarterly figures may not add up to annual.

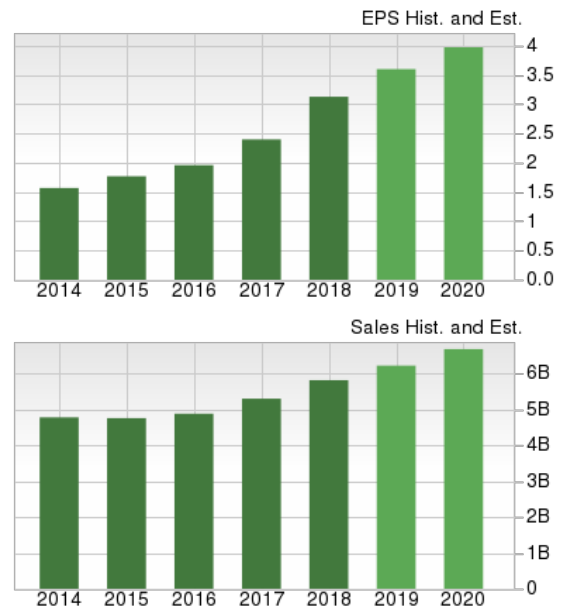
The data in the charts and tables, including the Zacks Consensus EPS and Sales estimates, is as of 01/21/2020. The reports text is as of 01/22/2020.

Overview

Florham Park, NJ-based Zoetis Inc. came into existence following Pfizer's decision to spin-off its animal health business. The entity started trading on NYSE from Feb 1, 2013, under the name Zoetis. The company focuses on the discovery, development, manufacturing and commercialization of animal health medicines and diagnostic products, with a focus on both livestock and companion animals.

Zoetis has been working on strengthening its product portfolio through acquisitions and deals. In August 2016, the company acquired a veterinary diagnostic focused company, Scandinavian Micro Biodevices, for \$80 million. The acquisition added a suite of specialty test instruments and cartridges to Zoetis' diagnostics portfolio and pipeline. Zoetis strengthened its portfolio of diagnostic products with the Abaxis acquisition in 2018, a leading provider of veterinary point-of-care diagnostic instruments. The acquisition added the VetScan portfolio of benchtop and handheld diagnostic instruments and consumables, which serves a large customer base of veterinary practices in North America.

Zoetis has consolidated its four-region structure into a two-region structure comprising the United States and International. Revenues increased 10% year over year to \$5.83 billion in 2018. United States contributed 49% of total revenue in 2018 and International revenues contributed 50% to the total.



Reasons To Buy:

▲ **Increasing Share Price:** Zoetis' stock has outperformed the industry in the past year.

▲ **Encouraging 2019 Outlook:** The company raised its annual guidance while reporting the third-quarter results backed by the solid performance of its new products.

▲ **Strong Performance of Companion Animal Portfolio:** The company's companion animal business maintains momentum. Apoquel and other product launches continue to drive growth in the companion animal portfolio. New product launches have further boosted growth. The company received approval for Clavamox Chewable in the United States in May 2017, Cytopoint in the European Union in April 2017 and in Canada in March 2017. The European Commission also granted approval for a new addition to the Suvaxyn/Fostera family of vaccines for swine. Key dermatology products Apoquel and Cytopoint, new products such as Simparica and Stronghold Plus, and increased medicalization rates in key international markets such as China and Brazil should propel further growth. The dermatology portfolio and Simparica continued to grow in 2018 and gained additional market share, both in the United States and international markets. The company has launched Revolution Plus, the topical parasiticide for cats and plans to launch a new injectable formulation to protect dogs against heartworms for up to 12 months, pending FDA approval. The FDA earlier approved ProHeart 12 (moxidectin), the industry's only once-yearly injection to prevent heartworm disease in dogs aged 12 months or older.

Zoetis' diversified product portfolio, global footprint and productive R&D should help drive both top- and bottom-line growth.

The recent approval of Simparica Trio in the EU should strengthen the company's market-leading parasiticide portfolio for companion animals. Moreover, the FDA should also complete its review of the same by the end of the first quarter. Per the company, the global canine parasiticides market is worth more than \$4 billion and the largest therapeutic category in medicines for dogs. Potential filings for new products and continued market expansions of major products like Cytopoint, Simparica, and Apoquel should boost growth further. The company also continues to bolster its vaccine portfolio for livestock. In October, Zoetis received the United States Department of Agriculture's (USDA) approval for Poulvac Procerta HVT-ND, its first vector vaccine that will help protect against Marek's disease and Newcastle disease, which are highly contagious viral infections affecting poultry. The company expanded its Fostera swine vaccine franchise in the second quarter, with approvals of different formulations in new geographies.

▲ **Expansion through Acquisitions:** We are positive on Zoetis' acquisitions made so far. The company acquired Abbott Laboratories' Animal Health assets for \$254 million in February 2015. The acquisition expanded the company's companion animal product portfolio to include veterinarian solutions for anesthesia, pain management and diabetes monitoring. Further, the November 2015 acquisition of Pharmaq, a privately held Norwegian company, has expanded Zoetis' aquaculture portfolio.

In August 2016, the company acquired Scandinavian Micro Biodevices — developer and manufacturer of microfluidic "lab on a chip" diagnostic analyzers and tests for veterinary point-of-care services — in a transaction valued at \$80 million. The acquisition added a suite of specialty test instruments and cartridges to Zoetis' complementary point-of-care diagnostics portfolio.

The company acquired Abaxis, Inc. for \$2 billion. The deal boosted Zoetis' presence in veterinary diagnostics space of the animal health market. This sector has witnessed an annual compound growth rate of about 10% over the past three years. With the acquisition, Zoetis has accessed Abaxis' VetScan portfolio of bench top and handheld diagnostic instruments and consumables. The company can now provide a broader range of veterinary diagnostics products, leveraging its global scale and direct customer relationships. It expects the veterinary diagnostics category to continue to grow faster than the animal health industry, with mid to high-single-digit growth. Moreover, Zoetis five-year collaboration agreement with Regeneron to research the use of latter's monoclonal antibody therapeutics in animals and discover new veterinary treatments will further diversify the broad portfolio. It recently acquired Platinum Performance, a privately held, nutrition-focused animal health company, which will further strengthen Zoetis' portfolio in the equine and pet-care markets. Zoetis recently announced the acquisition of ZNLabs, a full-service veterinary clinical reference laboratory company with a network of labs across the United States. The acquisition will strengthen the company's portfolio, expand its diagnostics footprint and enhance its value proposition to veterinary customers. The company can now provide a broader range of veterinary diagnostics products, leveraging its global scale and direct customer relationships. It expects the veterinary diagnostics category to continue to grow faster than the animal health industry.

In 2019, Zoetis acquired Phoenix Central Laboratory for Veterinarians, Inc. (Phoenix Lab), a full-service veterinary reference laboratory company, to enter the reference laboratory services market. Per the company, reference laboratories and point-of-care diagnostic testing are highly synergistic, offering veterinarians a single source for a full spectrum of tests, as well as access to the expertise of board-certified specialists and pathologists to support test results. It also acquired Platinum Performance, a privately-held, nutrition-focused animal health company. These acquisitions will further strengthen its market-leading portfolio.

▲ **Returning Value to Shareholders:** Zoetis is working on returning value to shareholders in the form of share buybacks and dividends. In December 2018, the company announced a multi-year share repurchase program worth \$2 billion. The company also hiked its quarterly dividend by 30% in 2019 and recently announced a 22% increase in the dividend for the first quarter of 2020.

Reasons To Sell:

- ▼ **Impact of Disease Outbreaks on Livestock Business:** Disease outbreak among animals is a material cause of concern for Zoetis' livestock products. Such outbreaks may hurt regional or global sales of particular animal-derived food products or result in reduced exports of the same, due to either heightened export restrictions or import prohibitions, in turn, dampening demand for livestock products. In addition, outbreak of a highly contagious disease near the company's main production sites could require immediate production halt at these sites or force the company to incur substantial additional expenses for procuring raw materials or products elsewhere. Thus, such incidents could hurt the top line considerably. The outbreak of the African swine fever is expected to adversely impact the overall industry growth in 2019 as it will pose challenges in the supply of pork.
 - ▼ **Pipeline Setbacks:** We note that clinical development involves a high degree of risk. Gaining approval for pipeline candidates has become more difficult given the tough regulatory environment. Development and regulatory setbacks for late-stage pipeline candidates would be a major disappointment for the company. Zoetis suffered a setback in the third quarter of 2013 when it decided to withdraw its new drug applications with the FDA for arsenical feed medicines, 3-Nitro and Carb-O-Sep. Similar setbacks can pull down the stock significantly.
 - ▼ **Stiff Competition:** Zoetis faces stiff competition from other animal health medicines and vaccine companies like Merck Animal Health and Elanco Animal Health, which recently inked a definitive agreement to acquire Bayer's Animal Health business for \$7.6 billion. Other competitors include IDEXX Laboratories and Boehringer Ingelheim Animal Health (the animal health division of Boehringer Ingelheim).
 - ▼ **Slowdown in Growth:** Anti-infective and medicated feed additives recorded modest growth in 2018 due to regulatory changes around the use of antibiotics in animal products. Moreover, growth in the cattle market has been limited in 2019 based on the challenging market conditions for beef and dairy customers.
-

Development and regulatory setbacks for late-stage pipeline candidates would be a major disappointment for the company. Stiff competition in the animal health space remains a threat as well.

Last Earnings Report

Zoetis Beats on Earnings in Q3, Reports In-Line Sales

Zoetis posted third-quarter 2019 adjusted earnings of 94 cents per share (excluding one-time items), which not only increased 13% year over year but also beat the Zacks Consensus Estimate of 89 cents.

Total revenues rose 9% year over year to \$1.58 billion, which were in line with the Zacks Consensus Estimate.

Quarter Ending **09/2019**

Report Date	Nov 07, 2019
Sales Surprise	0.17%
EPS Surprise	5.62%
Quarterly EPS	0.94
Annual EPS (TTM)	3.51

Quarterly Highlights

The company reports business results under two geographical operating segments — the United States and International. It has a diverse portfolio of products for livestock and companion animals.

Revenues from the United States segment increased 11% year over year to \$844 million. Sales of companion animal products in this region were up 26%, primarily owing to higher sales of the dermatology portfolio across the ProHeart, Revolution and Simparica franchises. New product introductions, notably Revolution Plus for cats and ProHeart 12 for dogs, were key drivers. Increased sales from key dermatology portfolio and revenues from the acquisition of Abaxis also contributed to growth. However, sales of livestock products declined 9% in the quarter, due to continued weakness across both the beef and dairy cattle sectors, as well as the timing of promotional activities in swine.

Revenues at the International segment inched up 2% year over year on a reported basis (up 5% operationally) to \$721 million. Livestock sales declined 4% (down 1% operationally) in the quarter. However, growth in the poultry portfolio was aided by higher sales in key markets, including China, Australia and Brazil. Cattle product sales grew owing to favorable market conditions in Mexico, the U.K. and Canada. However, sales in this category were negatively impacted by an unfavorable comparison to the prior-year quarter, which benefited from the end of the national trucking strike in Brazil.

Moreover, sales of companion animal products grew 12% on a reported basis, reflecting a rise in the dermatology portfolio and parasiticides, including Simparica and Stronghold Plus. The acquisition of Abaxis also fueled growth.

2019 Guidance

The company raised its guidance for the full year. It expects adjusted earnings of \$3.57-\$3.62 per share, compared with the previous expectation of \$3.53-\$3.60. Revenues are expected to be \$6.200-\$6.250 billion compared with the prior projection of \$6.175-\$6.275 billion.

The guidance reflects the current strength and performance of its business. Plus, it takes into account the foreign exchange rates in late October.

Other Updates

During the third quarter, Zoetis received approval in the European Union and Canada for its three-way combination parasiticide for dogs, Simparica Trio (sarolaner/moxidectin/pyrantel) chewable tablets, and expects to launch it in these markets in the first quarter of 2020. Regulatory reviews are also underway in the United States, Australia, Brazil and Japan, with submissions expected globally.

In October, Zoetis received the United States Department of Agriculture's (USDA) approval for Poulvac Procerta HVT-ND, the company's first vector vaccine to protect against Marek's disease and Newcastle disease, highly contagious viral infections affecting poultry.

The company completed the acquisition of Phoenix Lab to enter the veterinary reference laboratory space. The acquisition will further build on Zoetis' buyout of Abaxis. Phoenix Lab provides Zoetis a reference laboratory, highly valued by veterinarians for quality assurance and customer care.

Recent News

Declares First Quarter Dividend, Approves 22% Increase – Dec 11

Zoetis declared a first-quarter 2020 dividend of \$0.20 per share, an increase of 22% from the quarterly dividend rate in 2019. The dividend will be paid on Mar 3, 2020, to holders of record as of Jan 17, 2020.

Acquires ZNLabs – Nov 22

Zoetis announced the acquisition of ZNLabs, a full-service veterinary clinical reference laboratory company with a network of labs across the United States.

This laboratory company is founded by veterinarians who are seeking to revolutionize reference laboratory services for companion animals. The company has differentiated itself by offering a simple test menu and fast results with friendly service and no contracts.

The acquisition will strengthen Zoetis' portfolio, expand its diagnostics footprint and enhance its value proposition to veterinary customers.

Completes Acquisition of Phoenix Lab – Oct 31

Zoetis acquired Phoenix Central Laboratory for Veterinarians, Inc. (Phoenix Lab), a full-service veterinary reference laboratory company, after fulfilling all closing requirements.

Valuation

Zoetis' shares are up 68.7% over the trailing 12-month period. Over the past year, the Zacks sub-industry is up 0.9% while the sector is up 5.5%. The S&P 500 index is up 25.4% in the past year.

The stock is currently trading at 10.06X forward 12-month sales per share, which compares to 2.66X for the Zacks sub-industry, 2.87X for the Zacks sector and 3.56X for the S&P 500 index.

Over the past five years, the stock has traded as high as 10.25X and as low as 4.03X, with a 5-year median of 5.7X. Our Neutral recommendation indicates that the stock will perform in-line with the market. Our \$150 price target reflects 10.63X forward 12-month sales per share.

The table below shows summary valuation data for ZTS

Valuation Multiples - ZTS					
		Stock	Sub-Industry	Sector	S&P 500
P/S F12M	Current	10.06	2.66	2.87	3.56
	5-Year High	10.25	3.67	3.82	3.56
	5-Year Low	4.03	2.28	2.43	2.54
	5-Year Median	5.7	2.83	2.94	3
P/B TTM	Current	25.24	1.57	4.6	4.54
	5-Year High	25.5	12.96	5.03	4.55
	5-Year Low	14.64	0.96	3.43	2.85
	5-Year Median	19.13	2.5	4.29	3.61

As of 01/21/2020

Industry Analysis Zacks Industry Rank: Top 43% (110 out of 255)



Top Peers

Eisai Co. (ESALY)	Outperform
Pacira Pharmaceuticals, Inc. (PCRX)	Outperform
Pfizer Inc. (PFE)	Outperform
Bayer Aktiengesellschaft (BAYRY)	Neutral
Grifols, S.A. (GRFS)	Neutral
IDEXX Laboratories, Inc. (IDXX)	Neutral
Merck & Co., Inc. (MRK)	Neutral
Elanco Animal Health Incorporated (ELAN)	Underperform

Industry Comparison Industry: Medical - Drugs				Industry Peers		
	ZTS Neutral	X Industry	S&P 500	BAYRY Neutral	ELAN Underperform	MRK Neutral
VGM Score	B	-	-	A	F	A
Market Cap	67.60 B	124.00 M	24.43 B	78.28 B	11.42 B	229.06 B
# of Analysts	11	2	13	2	7	6
Dividend Yield	0.56%	0.00%	1.75%	2.60%	0.00%	2.71%
Value Score	D	-	-	A	F	B
Cash/Price	0.03	0.26	0.04	0.08	0.03	0.03
EV/EBITDA	32.84	-2.26	14.00	8.59	30.56	18.44
PEG Ratio	3.10	1.15	2.06	0.97	2.83	1.79
Price/Book (P/B)	25.31	3.41	3.39	1.53	2.04	8.56
Price/Cash Flow (P/CF)	37.20	10.82	13.69	5.55	15.38	14.49
P/E (F1)	35.66	14.74	19.00	10.41	26.56	16.24
Price/Sales (P/S)	10.99	5.87	2.68	1.53	3.70	4.98
Earnings Yield	2.80%	-14.40%	5.26%	9.62%	3.76%	6.16%
Debt/Equity	2.47	0.03	0.72	0.82	0.43	0.84
Cash Flow (\$/share)	3.82	-0.61	6.94	3.78	1.99	6.21
Growth Score	B	-	-	D	D	A
Hist. EPS Growth (3-5 yrs)	19.65%	8.54%	10.60%	NA	NA	7.23%
Proj. EPS Growth (F1/F0)	10.40%	18.93%	7.57%	14.81%	9.21%	7.41%
Curr. Cash Flow Growth	28.45%	13.56%	14.00%	60.37%	9,351.95%	3.40%
Hist. Cash Flow Growth (3-5 yrs)	14.83%	8.38%	9.00%	6.70%	NA	-1.53%
Current Ratio	4.39	3.65	1.23	1.29	3.12	1.26
Debt/Capital	71.19%	7.98%	42.99%	45.00%	29.85%	45.72%
Net Margin	23.76%	-110.57%	11.15%	-2.89%	3.04%	20.26%
Return on Equity	70.78%	-67.23%	17.16%	13.42%	7.79%	48.16%
Sales/Assets	0.56	0.29	0.55	0.35	0.35	0.55
Proj. Sales Growth (F1/F0)	7.41%	9.10%	4.05%	2.64%	0.56%	5.95%
Momentum Score	A	-	-	A	F	A
Daily Price Chg	1.26%	0.00%	-0.27%	0.24%	2.07%	-1.10%
1 Week Price Chg	3.39%	1.03%	2.29%	-0.26%	4.42%	1.61%
4 Week Price Chg	6.78%	4.33%	2.13%	2.34%	4.04%	-1.61%
12 Week Price Chg	12.50%	7.70%	6.99%	15.18%	12.66%	5.72%
52 Week Price Chg	68.78%	-15.79%	21.25%	11.86%	-1.16%	18.65%
20 Day Average Volume	1,490,249	172,731	1,415,064	300,840	5,146,248	6,443,652
(F1) EPS Est 1 week change	0.00%	0.00%	0.00%	0.00%	0.00%	0.10%
(F1) EPS Est 4 week change	-0.12%	0.00%	0.00%	0.00%	-6.75%	0.88%
(F1) EPS Est 12 week change	0.26%	1.35%	-0.34%	-3.59%	-9.73%	3.44%
(Q1) EPS Est Mthly Chg	0.56%	0.00%	0.00%	NA	-3.85%	NA

Zacks Stock Rating System

We offer two rating systems that take into account investors' holding horizons: Zacks Rank and Zacks Recommendation. Each provides valuable insights into the future profitability of the stock and can be used separately or in combination with each other depending on your investment style.

Zacks Recommendation

The Zacks Recommendation aims to predict performance over the next 6 to 12 months. The foundation for the quantitatively determined Zacks Recommendation is trends in the company's estimate revisions and earnings outlook. The Zacks Recommendation is broken down into 3 Levels; Outperform, Neutral and Underperform. Unlike many Wall Street firms, we have an excellent balance between the number of Outperform and Neutral recommendations. Our team of 70 analysts are fully versed in the benefits of earnings estimate revisions and how that is harnessed through the Zacks quantitative rating system. But we have given our analysts the ability to override the Zacks Recommendation for the 1200 stocks that they follow. The reason for the analyst over-rides is that there are often factors such as valuation, industry conditions and management effectiveness that a trained investment professional can spot better than a quantitative model.

Zacks Rank

The Zacks Rank is our short-term rating system that is most effective over the one- to three-month holding horizon. The underlying driver for the quantitatively-determined Zacks Rank is the same as the Zacks Recommendation, and reflects trends in earnings estimate revisions.

Zacks Style Scores

The Zacks Style Score is as a complementary indicator to the Zacks rating system, giving investors a way to focus on the highest rated stocks that best fit their own stock picking preferences.

Academic research has proven that stocks with the best Value, Growth and Momentum characteristics outperform the market. The Zacks Style Scores rate stocks on each of these individual styles and assigns a rating of A, B, C, D and F. We also produce the VGM Score (V for Value, G for Growth and M for Momentum), which combines the weighted average of the individual Style Scores into one score. This is perfectly suited for those who want their stocks to have the best scores across the board.

Value Score	D
Growth Score	B
Momentum Score	A
VGM Score	B

As an investor, you want to buy stocks with the highest probability of success. That means buying stocks with a Zacks Recommendation of Outperform, which also has a Style Score of an A or a B.

Disclosures

This report contains independent commentary to be used for informational purposes only. The analysts contributing to this report do not hold any shares of this stock. The analysts contributing to this report do not serve on the board of the company that issued this stock. The EPS and revenue forecasts are the Zacks Consensus estimates, unless indicated otherwise on the reports first page. Additionally, the analysts contributing to this report certify that the views expressed herein accurately reflect the analysts personal views as to the subject securities and issuers. ZIR certifies that no part of the analysts compensation was, is, or will be, directly or indirectly, related to the specific recommendation or views expressed by the analyst in the report.

Additional information on the securities mentioned in this report is available upon request. This report is based on data obtained from sources we believe to be reliable, but is not guaranteed as to accuracy and does not purport to be complete. Any opinions expressed herein are subject to change.

ZIR is not an investment advisor and the report should not be construed as advice designed to meet the particular investment needs of any investor. Prior to making any investment decision, you are advised to consult with your broker, investment advisor, or other appropriate tax or financial professional to determine the suitability of any investment. This report and others like it are published regularly and not in response to episodic market activity or events affecting the securities industry.

This report is not to be construed as an offer or the solicitation of an offer to buy or sell the securities herein mentioned. ZIR or its officers, employees or customers may have a position long or short in the securities mentioned and buy or sell the securities from time to time. ZIR is not a broker-dealer. ZIR may enter into arms-length agreements with broker-dealers to provide this research to their clients. Zacks and its staff are not involved in investment banking activities for the stock issuer covered in this report.

ZIR uses the following rating system for the securities it covers. **Outperform-** ZIR expects that the subject company will outperform the broader U.S. equities markets over the next six to twelve months. **Neutral-** ZIR expects that the company will perform in line with the broader U.S. equities markets over the next six to twelve months. **Underperform-** ZIR expects the company will underperform the broader U.S. equities markets over the next six to twelve months.

No part of this report can be reprinted, republished or transmitted electronically without the prior written authorization of ZIR.