

Zoetis Inc.(ZTS)

\$100.94 (As of 03/20/20)

Price Target (6-12 Months): **\$106.00**

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: C

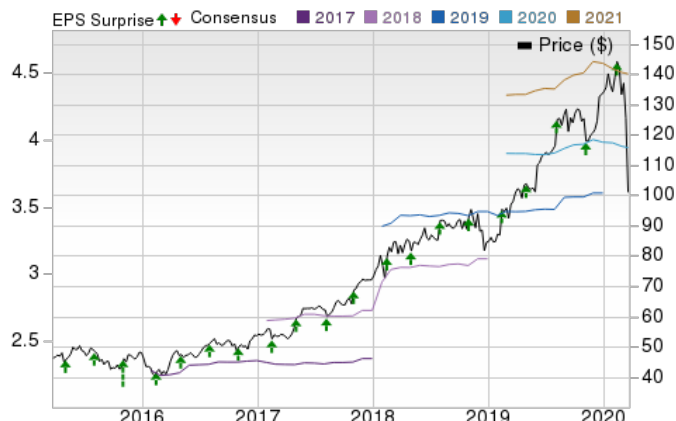
Growth: B

Momentum: B

Summary

Zoetis maintains momentum on the back of growth in new parasiticide products, vaccines and a solid dermatology portfolio. Key dermatology products, such as Apoquel and Cytopoint, continue to penetrate the market and generate additional revenues. Increased sales of parasiticides, including ProHeart 12 and Simparica, further boosted performance. The Abaxis acquisition has further strengthened its leading portfolio. Zoetis has been making other prudent acquisitions. Shares have outperformed the industry in the past year. However, the cattle market is witnessing challenges for beef and dairy customers. Moreover, the swine market is being affected by the African swine fever in China. Competition is stiff as well.

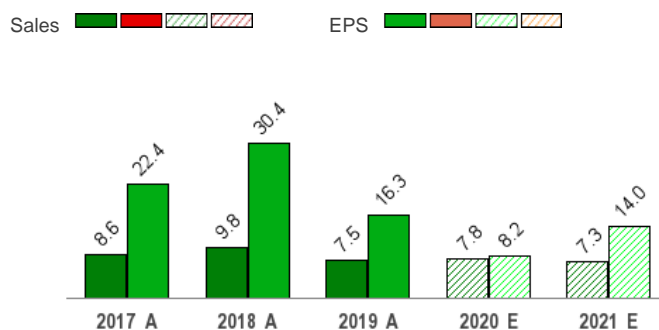
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$146.26 - \$93.25
20 Day Average Volume (sh)	3,456,951
Market Cap	\$47.9 B
YTD Price Change	-23.7%
Beta	0.74
Dividend / Div Yld	\$0.80 / 0.8%
Industry	Medical - Drugs
Zacks Industry Rank	Top 19% (48 out of 254)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	4.6%
Last Sales Surprise	2.1%
EPS F1 Est- 4 week change	0.0%
Expected Report Date	05/07/2020
Earnings ESP	0.7%
P/E TTM	27.7
P/E F1	25.6
PEG F1	2.2
P/S TTM	7.7

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	1,652 E	1,791 E	1,832 E	1,923 E	7,240 E
2020	1,528 E	1,675 E	1,727 E	1,807 E	6,748 E
2019	1,455 A	1,547 A	1,584 A	1,674 A	6,260 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$1.00 E	\$1.13 E	\$1.18 E	\$1.20 E	\$4.49 E
2020	\$0.88 E	\$0.99 E	\$1.05 E	\$1.04 E	\$3.94 E
2019	\$0.88 A	\$0.90 A	\$0.94 A	\$0.92 A	\$3.64 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 03/20/2020. The reports text is as of 03/23/2020.

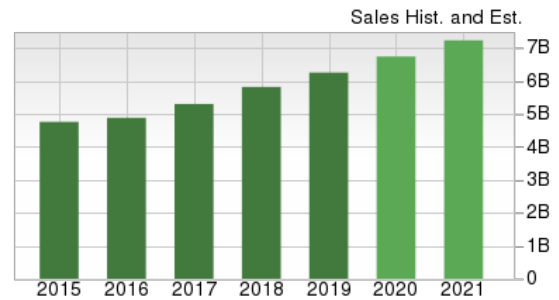
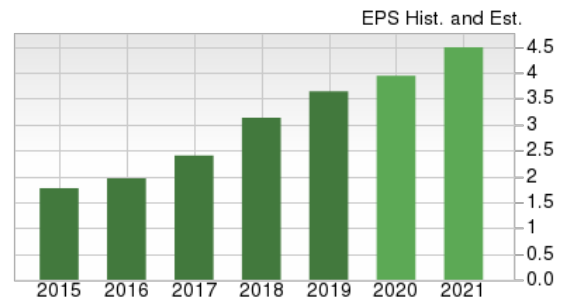
Overview

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 is a leader in the discovery, development, manufacture and commercialization of animal health medicines, vaccines and diagnostic products with a focus on both livestock and companion animals.

Zoetis has a diversified business, which caters to eight core species — cattle, swine, poultry, fish and sheep (collectively, livestock) and dogs, cats and horses (collectively, companion animals). The company focuses on seven major product categories: vaccines, anti-infectives, parasiticides, other pharmaceutical products, dermatology, medicated feed additives and animal health diagnostics.

Zoetis has been working on strengthening its product portfolio through acquisitions and deals. The company 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 practitioners in North America. In 2019, Zoetis acquired Phoenix Central Laboratory for Veterinarians, Inc. and ZNLabs, LLC, thereby entering into reference laboratory services. Zoetis also entered the field of animal nutritionals with the acquisition of Platinum Performance in 2019.

Zoetis has consolidated its four-region structure into a two-region structure comprising the United States and International. Revenues increased 7% year over year to \$6.26 billion in 2019. The United States contributed 51.2% of total revenues in 2019 and International revenues contributed the remaining.



Reasons To Buy:

- ▲ **Increasing Share Price:** Zoetis' stock has outperformed the industry in the past year.
- ▲ **Encouraging 2020 Outlook:** The company's guidance for 2020 was encouraging backed by the solid performance of its new products.

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

- ▲ **Strong Performance of New Products:** The company's companion animal business maintains momentum. Apoquel and other product launches continue to drive growth in the companion animal portfolio. Apoquel accounted for 9% of total revenues in 2019. New product launches have further boosted growth. 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 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. Zoamix, an alternative to antibiotics in medicated feed additives, has also delivered an impressive performance.

The recent approval of Simparica Trio in the EU should strengthen the company's market-leading parasiticide portfolio for companion animals. The FDA recently approved it too. 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 Foster's swine vaccine franchise in the second quarter, with approvals of different formulations in new geographies. Zoetis also received approval for Rimadyl (carprofen) for dogs in China, one of the fastest growing companion animal markets in the world. It is indicated for relief from pain and inflammation associated with osteoarthritis (chewables) and control of postoperative pain associated with soft tissue and orthopedic surgeries (injectable). Approval of innovative products should further boost sales.

- ▲ **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. Earlier, the company announced the acquisition of Ethos Diagnostic Science, a veterinary reference lab business dedicated to serving leading specialty animal hospitals, the greater veterinary community and researchers with accurate, reliable results.

- ▲ **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.

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.

▼ **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:** Market conditions for beef and dairy customers were challenging in 2019 and can affect growth in 2020.

Last Earnings Report

Zoetis' Earnings and Revenues Beat Estimates in Q4

Zoetis posted fourth-quarter 2019 adjusted earnings of 92 cents per share (excluding one-time items), which not only increased 16% year over year but also beat the Zacks Consensus Estimate of 88 cents.

Total revenues rose 7% year over year to \$1.67 billion, which beat the Zacks Consensus Estimate of \$1.64 billion.

Quarter Ending **12/2019**

Report Date	Feb 13, 2020
Sales Surprise	2.12%
EPS Surprise	4.55%
Quarterly EPS	0.92
Annual EPS (TTM)	3.64

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 6% year over year to \$861 million. Sales of companion animal products in this region grew 15%, primarily owing to higher sales of Apoquel and Cytopoint brands in the dermatology portfolio. ProHeart 12 and Simparica also led to the increase. However, sales of livestock products declined 3% in the quarter due to continued weakness across beef and dairy cattle sectors, which more than offset double-digit growth in poultry and swine.

Revenues at the International segment increased 9% year over year on a reported basis (up 12% operationally) to \$791 million. Livestock sales grew 2% (up 5% operationally) in the quarter. Growth in the cattle portfolio was aided by higher sales in key markets, including Australia, Germany and Mexico. Alpha Flux, a recently launched parasiticide, was the main growth driver in fish, while promotional activities across Russia, India and Brazil drove growth in poultry. However, sales of swine products declined as a result of the ongoing impact of the African swine fever in China and other smaller markets in Southeast Asia.

Sales of companion animal products grew 23% on a reported basis, reflecting a rise in the dermatology portfolio and parasiticides, including Simparica and the Revolution/Stronghold franchise, as well as growth across key markets in Western Europe and China.

2019 Results

The company's adjusted earnings were \$3.64 per share, up 16% year over year.

The revenues came in at \$6.26 billion, reflecting an increase of 7% year over year.

2020 Guidance

The company expects adjusted earnings of \$3.90-\$4.00 per share. Revenues are expected to be \$6.650-\$6.800 billion.

Other Updates

During the fourth quarter, Zoetis received approval for Rimadyl (carprofen) for dogs in China, one of the fastest-growing companion animal markets in the world. Rimadyl, approved in both chewable and injectable formulations, is indicated for the relief of pain and inflammation associated with osteoarthritis (chewables), and for the control of postoperative pain associated with soft tissue and orthopedic surgeries (injectable).

Zoetis expanded its reference laboratory capabilities in the United States with the acquisitions of Phoenix Lab and ZNLabs in November 2019 and Ethos Diagnostic Science in February 2020.

Recent News

FDA Approval for Simparica Trio – Feb 27

Zoetis announced that the FDA has approved Simparica Trio (sarolaner, moxidectin, and pyrantel chewable tablets), the first once-monthly, chewable tablet in the United States that delivers all-in-one protection from heartworm disease, ticks and fleas, roundworms, and hookworms.

Acquires Ethos Diagnostic Science – Feb 7

Zoetis announced the acquisition of Ethos Diagnostic Science, a veterinary reference lab business dedicated to serving leading specialty animal hospitals, the greater veterinary community and researchers with accurate, reliable results.

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.

Valuation

Zoetis' shares are down 23.7% in the year-to-date period but up 3% over the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Medical sector are down 29.8% and 23.5% in the year-to-date period, respectively. Over the past year, the Zacks sub-industry is down 33.8% while the sector is down 23.2%. The S&P 500 index is down 28.2% in the year-to-date period and down 18.2% in the past year.

The stock is currently trading at 6.99X forward 12-month sales per share, which compares to 2.56X for the Zacks sub-industry, 2.14X for the Zacks sector and 2.5X for the S&P 500 index.

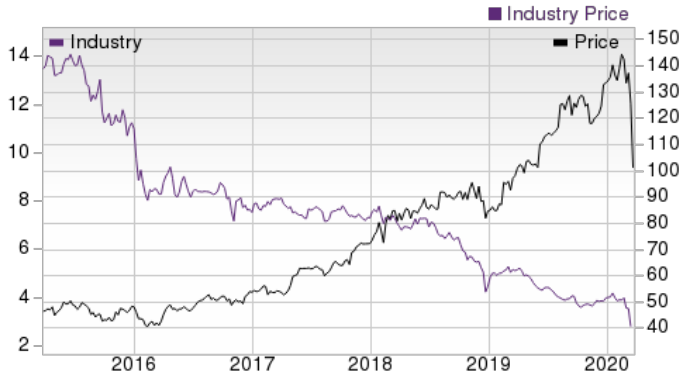
Over the past five years, the stock has traded as high as 10.25X and as low as 4.03X, with a 5-year median of 5.77X. Our Neutral recommendation indicates that the stock will perform in-line with the market. Our \$106 price target reflects 14.44X forward 12-month sales per share.

The table below shows summary valuation data for ZTS

Valuation Multiples - ZTS					
		Stock	Sub-Industry	Sector	S&P 500
P/S F12M	Current	6.99	2.56	2.14	2.5
	5-Year High	10.25	3.76	3.84	3.43
	5-Year Low	4.03	2.33	2.14	2.5
	5-Year Median	5.77	2.81	2.96	3
P/B TTM	Current	17.75	1.12	2.9	3.11
	5-Year High	25.5	13.2	5.05	4.56
	5-Year Low	14.64	0.98	2.9	2.85
	5-Year Median	19.42	2.53	4.31	3.63

As of 03/20/2020

Industry Analysis Zacks Industry Rank: Top 19% (48 out of 254)



Top Peers

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

Industry Comparison Industry: Medical - Drugs				Industry Peers		
	ZTS Neutral	X Industry	S&P 500	BAYRY Neutral	ELAN Neutral	MRK Neutral
VGM Score	B	-	-	B	D	B
Market Cap	47.94 B	70.65 M	15.82 B	49.07 B	6.97 B	180.99 B
# of Analysts	11	2	13	2	5	7
Dividend Yield	0.79%	0.00%	2.79%	4.15%	0.00%	3.42%
Value Score	C	-	-	A	C	C
Cash/Price	0.03	0.35	0.06	0.12	0.04	0.05
EV/EBITDA	21.39	-1.23	9.77	6.39	19.00	12.79
PEG Ratio	2.12	0.51	1.42	0.93	1.16	1.82
Price/Book (P/B)	17.75	2.27	2.07	0.96	1.18	6.99
Price/Cash Flow (P/CF)	22.19	10.60	8.39	3.48	9.21	10.67
P/E (F1)	24.37	12.16	12.42	6.78	15.71	12.47
Price/Sales (P/S)	7.66	4.50	1.68	0.97	2.27	3.86
Earnings Yield	3.90%	-22.68%	7.97%	14.75%	6.34%	8.02%
Debt/Equity	2.26	0.02	0.70	0.82	0.42	0.87
Cash Flow (\$/share)	4.55	-0.56	7.01	3.78	1.90	6.69
Growth Score	B	-	-	D	D	B
Hist. EPS Growth (3-5 yrs)	20.29%	3.93%	10.85%	NA	NA	8.10%
Proj. EPS Growth (F1/F0)	8.27%	17.71%	4.90%	9.60%	5.09%	10.24%
Curr. Cash Flow Growth	18.22%	4.82%	6.03%	60.37%	-2.65%	5.54%
Hist. Cash Flow Growth (3-5 yrs)	16.87%	5.48%	8.55%	6.70%	NA	0.15%
Current Ratio	2.63	3.30	1.23	1.29	2.90	1.24
Debt/Capital	69.29%	7.14%	42.57%	45.00%	29.58%	46.65%
Net Margin	23.96%	-112.83%	11.57%	9.07%	2.21%	21.01%
Return on Equity	69.41%	-65.75%	16.74%	13.92%	7.33%	49.41%
Sales/Assets	0.56	0.31	0.54	0.35	0.35	0.56
Proj. Sales Growth (F1/F0)	7.79%	0.95%	3.13%	-3.06%	0.34%	6.36%
Momentum Score	B	-	-	B	D	B
Daily Price Chg	-1.36%	0.00%	-4.39%	-2.63%	0.17%	0.89%
1 Week Price Chg	-8.44%	-18.43%	-11.01%	-20.89%	-11.66%	-6.63%
4 Week Price Chg	-29.68%	-32.84%	-36.57%	-34.97%	-42.11%	-13.49%
12 Week Price Chg	-24.12%	-31.57%	-34.28%	-36.39%	-39.99%	-21.87%
52 Week Price Chg	1.30%	-49.24%	-27.95%	-24.00%	-46.12%	-13.97%
20 Day Average Volume	3,456,951	250,769	3,981,936	904,423	7,094,851	17,246,028
(F1) EPS Est 1 week change	0.00%	0.00%	-0.01%	0.00%	0.00%	0.00%
(F1) EPS Est 4 week change	0.00%	0.00%	-0.85%	-3.72%	-1.06%	0.00%
(F1) EPS Est 12 week change	-0.78%	0.00%	-1.70%	-3.72%	-7.60%	4.22%
(Q1) EPS Est Mthly Chg	0.20%	0.00%	-0.88%	NA	4.17%	0.00%

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	C
Growth Score	B
Momentum Score	B
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.

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