

Astrazeneca might have created value but now it needs to deliver



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Whatever your view on the actual value of AstraZeneca's pipeline, Pascal Soriot's power to talk it up cannot be doubted. From his robust defence of the drug maker two years ago in the face of Pfizer's bid approach that forced a substantial re-rating of the company to comments last week about its growing attractiveness, the chief executive has shown a canny ability to force investors to think again.

A look at how sell-side analysts view the company's pipeline suggests that many agree AstraZeneca has indeed created substantial value – \$24.4bn in NPV terms over the last three years, according to an analysis of *EvaluatePharma* data – a record that ranks them favourably among their big pharma peers (see table below). Whether that makes them vulnerable to another bid approach is another matter entirely.

The 8% jump in Astra's share price in the last few days – adding £4.8bn to its market cap – looks to have been down to investors' fears of missing out on a future big pharma mega merger, rather than any fundamental belief a bid is on the way.

As Goldman Sachs analysts put it: "A number of investors highlighted that being underweight AZN during the Pfizer bid process was detrimental to performance, and were anxious to avoid a similar situation again."

Speculation was sparked by a note from Citi analysts last week that suggested Astra's strength in biotechnology and its immuno-oncology pipeline might make it a target for Novartis. Mr Soriot fanned the flames – arguably unintentionally – on the company's second-quarter conference call, by acknowledging that the company's drug pipeline could become attractive to rivals as it has become more valuable.

Adding value - in the pipeline and on the stock market

	Current NPV of R&D pipeline (\$bn)	Change over three years (\$bn)	Current R&D NPV as % of mkt cap	% SP change over three years
Roche	43.4	33.4	20%	5%
Astrazeneca	27.3	24.4	32%	62%
Novartis	24.6	15.8	11%	20%
Eli Lilly	24.3	8.3	27%	69%
Pfizer	22.6	13.8	10%	33%
Sanofi	21.7	13.4	20%	-7%
Abbvie	19.2	16.2	17%	62%
Merck & Co	18.3	6.7	11%	26%
Johnson & Johnson	15.9	14.2	5%	46%
Glaxosmithkline	6.4	-5.6	5%	3%
Bristol-Myers Squibb	2.3	-12.7	2%	70%

As the table above shows, the company has indeed enjoyed a period of growing appreciation of its pipeline. Only Roche has added more value in the last three years.

Of course this analysis does not fully capture the evolving picture as a number of drugs will have moved from the R&D stage and onto the market in this time, where the value now sits. A prime example of this Bristol-Myers with Opdivo, which has had huge clinical and commercial success in the last two years. The product is now valued at an astonishing \$71.4bn and is hugely important to the company - in fact the entire NPV of the product is only \$15bn below that of the entire market cap of AstraZeneca.

However while having a highly valued R&D pipeline can be considered a boon, it can also be viewed as a risk. Many investors will be more focused on the substantial clinical and commercial challenges that await these late-stage products.

Astra has a number of hugely important data readouts approaching, mainly on its cancer portfolio. In particular four combination studies of its immuno-oncology agents will read out next year, with the Mystic study of durvalumab and tremelimumab in first line lung cancer perhaps the most hotly anticipated. Any move on AstraZeneca ahead of the result of this study would represent a massive bet on the company's immuno-oncology pipeline, a field in which it is undoubtedly playing catch up.

So while Mr Soriot is right to argue that the pipeline has increased in value, the company still has much to prove. This is underscored by the fact that the company's pipeline accounts for a third of its market cap, by far the highest in this peer group.

From having one of the weakest pipelines three years ago AstraZeneca now owns one of the most highly valued. It has also delivered substantial share price appreciation in that time, again among the highest among this peer group.

Mr Soriot must know that it is now all about delivery. For AstraZeneca to remain attractive to investors and potential bidder alike, these pipeline promises must come to fruition.

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