Evaluate Vantage

November 17, 2016

Investor sentiment vs sellside consensus: a chicken and egg situation

Amy Brown

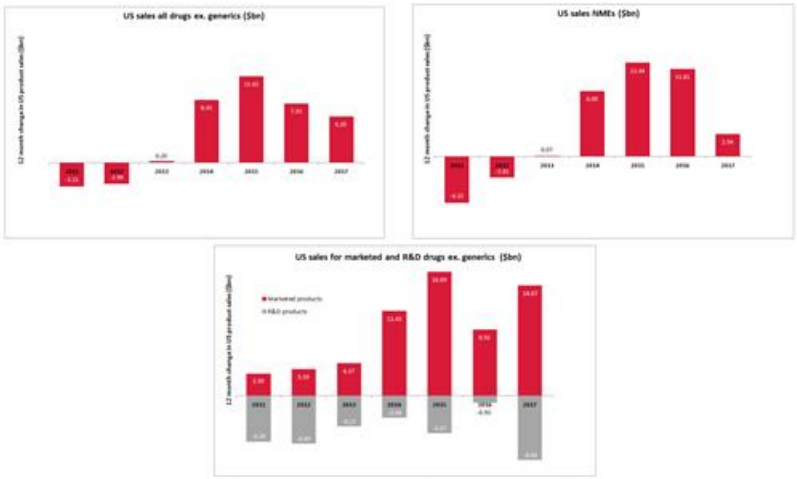
In a fluid and ever-shifting industry like pharmaceuticals, even near-term predictions can change, sometimes dramatically. For example, over the course of this year the consensus forecast for total US drug sales in 2017 has grown by $6.2bn.

On the surface this figure looks encouraging, until compared with the substantially bigger upgrades the previous four years received, in their preceding 12 month run-ups. If this measure can be considered a barometer for the sector, then maybe confidence in the coming year is not running as high as in the recent past.

This would seem to be a reasonable conclusion when looking at US drug indices, such as the Nasdaq Biotechnology Index and S&P Pharmaceuticals. As the graphs below show, the acceleration in stock prices that really kicked off in 2013 is reflected in a period of ever-improving previous-year consensus drug forecasts. Pre-biotech boom, the sellside was adopting a more cautious stance on the approaching 12-month periods.

Whether consensus follows sentiment or the other way around is an open question, and to a certain extent they probably exist as a feedback loop.

The shifting outlook for US drug sales: change in consensus over the previous year



This analysis was constructed from EvaluatePharma's consensus of sell-side analysts' drug forecasts. The change in consensus over a 12 months period running October to October for the following calendar year was calculated, and the net change, positive or negative, is reflected here. It excludes generics.

Given that this consensus view is compiled by sellside analysts, one read of the past few years' trend is that it reflects a need to assign ever-higher asset valuations to justify surging market valuations. However what looks like growing optimism about the future will also have been spurred by the rapid and spectacular uptake curves seen with the hepatitis C agents, and to a certain extent earlier-than-expected success of the anti-PD-1 immuno-oncology drugs.

So why the comparative retrenchment this year? Given that this is the view of next year, R&D failures are unlikely to have hit the numbers too much, as these would show further out. An overall moderation of expectations to reflect lower market values will have had an impact, as will downgrades to big established classes like insulins and respiratory drugs, where payer pressure has been effective at curtailing revenue growth.

Of course this analysis still reflects growing optimism over the year for the coming 12 months, in the US. It is just more moderate than previously.

Another cut

It is important to remember that this analysis does not include generics. The second graph only includes the most novel agents – so excludes products approved as an NDA or being developed with drug formulation technology – and this shows a similar pattern in consensus shifts.

A closer look at which individual products have seen big swings shows that Gilead's new HIV drug Genvoya and hepatitis C doublet Epclusa have been substantially upgraded. Meanwhile, its hep C incumbents Harvoni and Sovaldi have been taken down.

Other notable downgrades include Novartis's heart drug Entresto, which has experienced a much slower launch than hoped, and Biogen's Tecfidera, which has seen increasing competition. Those whose fortunes have improved for the coming year include the anti-PD-1 antibodies Opdivo and Keytruda, and Bristol-Myers Squibb's oral drug thinner Eliquis, a product that finally seems to making headway in the market.

The final cut of these data shows the forecast split shifts between marketed drugs and R&D projects. A pattern of R&D downgrades being outweighed by marketed upgrades is clear – the failure of large proportions of the drug pipeline each year is a given.

2016's more substantial R&D downgrades than previously are likely to reflect the big retrenchment in stock market values, which necessarily require the sellside to take a red pen to their models.

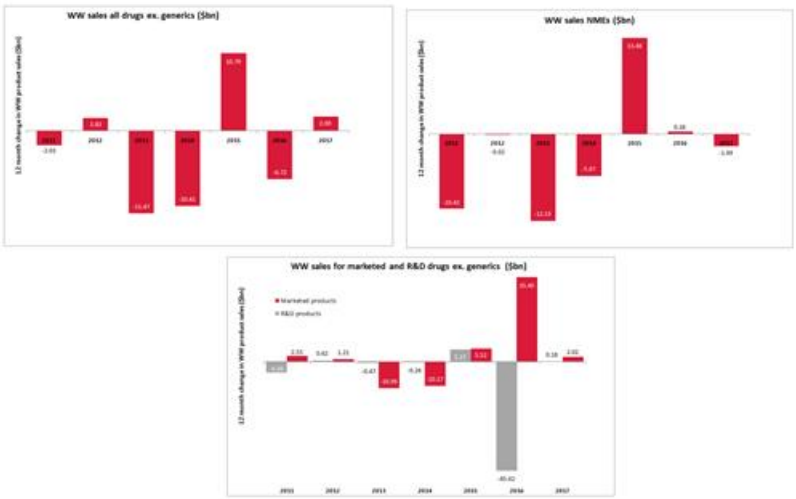
Closer scrutiny of the data reveals a couple of standout R&D downgrades. Puma's breast cancer pill neratinib is struggling to remain relevant in its class, while Pfizer's PCSK-9 contender bococizumab was abandoned in phase III and Biomarin called time on the duchenne muscular dystrophy project Kyndrisa after an FDA rejection.

However it is clear that, going into 2017, equity analysts are adopting an optimistic stance for the US drugs market.

The analyses below, looking at how consensus for global drug sales has shifted, reveals much less of a pattern. Covering more disparate regions this is to be expected, although perhaps a signal of confidence can be gleaned from the fact that 2017 is only the second year to be upgraded over the previous 12 months, since 2011. The outlook for novel drugs is less rosy on a global basis, perhaps reflecting a much stricter reimbursement climate outside the US.

A major caveat is that this analysis was conducted before the surprise outcome of the US election. With investors and companies already factoring in a much more friendly business environment in the world's biggest drugs market, this fluid situation could easily shift once again.

The shifting outlook for WW drug sales: change in consensus over the previous year



This analysis was constructed from EvaluatePharma's consensus of sell-side analysts' drug forecasts. The change in consensus over a 12 months period running October to October for the following calendar year was calculated, and the net change, positive or negative, is reflected here. It excludes generics.

To contact the writer of this story email Amy Brown in London at AmyB@epvantage.com or follow @ByAmyBrown on Twitter