

Merck & Co., Inc.

US CORE HOLDING*

Recommended since 18.12.15

01.03.2024



Country US	Market capitalization (bn) USD 324,7
Sector Health Care	Free float 99,8%
Factset MRK-US	Closing price USD 127,15
ISIN US58933Y1055	ESG Risk score* 22,1 Medium risk

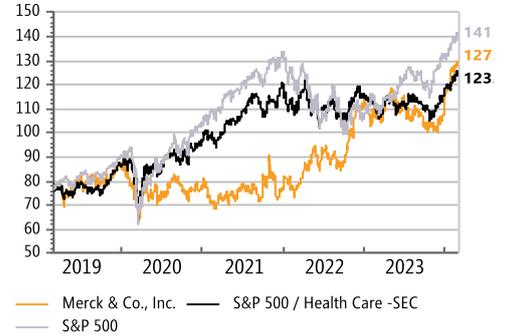
Perf. since reco. (%)
Merck & Co., Inc. 158,2
Sector 106,8



*From 2015, B&Cie separates its investment recommendations into Core Holdings (higher organic growth potential, high free cash flow, ROCE in excess of the cost of capital and balance sheet efficiency throughout the cycle) and Satellite Recommendations, which do not meet the above criteria but are likely to outperform in the short-to-medium term.

Profile

Originally the US subsidiary of Merck AG, Merck & Co was established and run by George Merck in 1891. The company became fully independent in 1917. Following the sale of the Consumer Care business in 2014, the company is focused on two areas: (1) pharmaceuticals (90% of sales), dedicated to cardiovascular diseases, diabetes, hepatitis C, HIV, oncology and vaccines, and (2) animal health (10%).



Source: Factset

Market - competition - positions - barriers to entry

Merck & Co is a pharma sector pure player and one of the top five global groups in the sector. Barriers to entry are innovation, with a large R&D budget (17% of sales), the clinical development process, the complexity of molecules, and the regulatory environment.

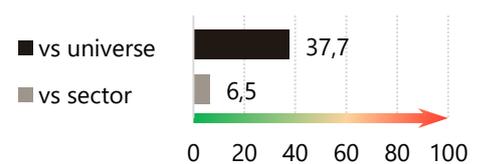
Investment case

- ⦿ The Group will benefit from solid growth in the medium term, driven by Keytruda indication extensions (immunotherapy against various forms of cancer - 42% of sales in 2023), but also by favorable trends in animal health and vaccines. These last two segments represent 30% of sales, with growth rates averaging between 5% and 10% per year. For its part, Keytruda offers potential sales of over USD 30 billion by 2027 (vs. USD 25 billion in 2023), and a significant improvement in margins.
- ⦿ The strategy of targeted acquisitions and partnerships, successfully implemented since 2019 for a total of USD 50mia, has strengthened and diversified the pipeline. The Group is now in a position to limit the impact of Keytruda's patent expiry in 2028. Among the most promising assets, we highlight sotatercept (pulmonary arterial hypertension - scheduled for launch in 2024), V116 (pneumococcal vaccine - scheduled for launch in 2024), six antibody-drug conjugates (oncology - in clinical phases III/II/I), tulisokibart (chronic inflammatory bowel disease - in phase III). The opportunities over the next ten years will be significant, whether in oncology (with over USD 20bn potential sales identified), cardiometabolic (USD 15bn) or immunology (multibillion dollars).
- ⦿ The year 2024 will be marked by two major launches, sotatercept (USD 5bn in sales by 2028-30e) and V116 (USD 3bn by 2030e), for which we are awaiting the FDA's decision at the end of March and June respectively.
- ⦿ This will enable the Group to generate sales and EPS growth of 6% and 12% on average per annum respectively over the next three years.

ESG - risks and key points

- ⦿ Merck & Co's ESG risk is medium, mainly linked to its presence in the US market (46% of sales), where litigation is more commonplace. The group has in the past been involved in a number of controversies. However, the shift in its business away from its legacy franchises (cardiovascular; primary care) towards oncology tends to mitigate this risk.
- ⦿ A strong performance on overall management of ESG issues.

ESG risk vs. universe & sector (percentile)*



Source: Sustainalytics

Valuation** in USD

Current price	Value Bordier Scenario
127	162

Our scenario assumes a US risk-free interest rate of 3.50%; sales growth averaging 3% a year out to 2027 and a subsequent decline in sales averaging 5% a year towards the end of the period; an EBITDA margin improvement to 45% in 2026 and then a gradual return towards 39% to reflect expiry of the Keytruda patent.

***) The theoretical value reflects the company's business model, our baseline growth and profit scenario and market data, exogenous to the company (risk-free rate and equity risk premium). It does not in itself constitute a target price.

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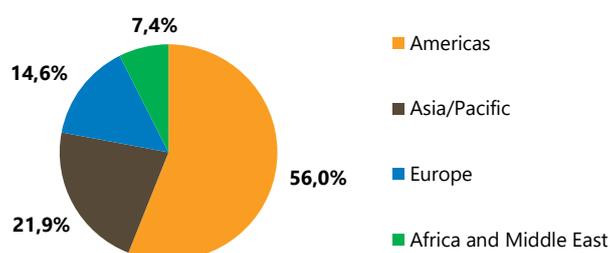
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"Bordier Core Holding" indicators

In millions of USD	2022	2023	2024e	2025e	2026e
Sales revenue	59 283	60 115	63 722	67 545	71 260
Sales growth %	21,7%	1,4%	6,0%	6,0%	5,5%
<i>o/w organic</i>	25,0%	4,4%	8,0%	6,0%	5,5%
EBIT adjusted	22 522	6 211	25 807	27 694	29 573
% of sales	38,0%	10,3%	40,5%	41,0%	41,5%
Net income	19 005	3 837	21 788	23 519	25 244
Adjusted EPS	7,48	1,51	8,57	9,25	9,93
Adjusted EPS growth	24,2%	-79,8%	467,8%	7,9%	7,3%
Capex/Sales	7,4%	6,4%	4,5%	4,5%	4,5%
Free cash-flow	14 707	9 143	20 607	22 266	24 017
FCF/Sales	24,8%	15,2%	32,3%	33,0%	33,7%
Dividend per share	2,80	2,92	3,70	4,00	4,31
Dividend yield	2,5%	2,7%	2,9%	3,1%	3,4%
ROCE - WACC	24,2%	-4,4%	27,5%	31,0%	28,2%
ROE (%)	41,3%	10,2%	44,5%	39,2%	35,2%
Net debt/Ebitda	76,0%	393,5%	52,7%	6,4%	-37,2%

Source: Factset, Bordier estimates

Sales breakdown - 12/2023



Ratios

	Merck & Co., Inc.	S&P 500 Sector	Market
PE (x)***		Health Care	SP 500
2023	72,2	15,7	18,5
2024e	14,8	22,6	23,3
2025e	13,7	19,6	21,0
P/B (x)***			
2023	7,3	4,6	4,0
2024e	6,6	5,0	4,7
2025e	5,4	4,6	4,3
Beta (2Y, daily) vs market: 0,36			

***) The valuation ratios set out are provided for information only. They do not constitute the criteria based upon which Core Holdings are selected, and may present significant premi-ums representing the quality of the company's business model.

Governance and ownership structure

Since 2021 - CEO Robert M. Davis

Key shareholders (if any):

100% free float

Agenda

25 Apr. 2024 : Q1 results / 30 July 2024 : Q2 Results
31 Oct. 2024 : Q3 results

Any special characteristics of ownership (multiple voting rights, controlling holding company, shareholders' agreements, etc.):

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Glossary

ESG Risk Score

At B&Cie, we take particular care to ensure that the companies in which we recommend investing are sustainable. Accordingly, our selection process takes account of risks relating to environmental, social and governance (ESG) issues. This approach is underpinned by research from Sustainalytics, the global leader in ESG and corporate governance analysis, whose methodology aims to identify major controversies and risks and assess a company's ESG risks relative to both its sector and the investment universe as a whole. The corresponding score is expressed as a percentile: the lower the overall risk score, the lower the risk within the investment universe.

b-Digital, b-Transition & b-Well

Over and above the conventional geographical and sectoral approaches to asset management, at B&Cie we believe the world of tomorrow is being shaped by structural trends. We have identified three main megatrends: ongoing digital globalisation of the economy; economic transition, particularly in the energy sector; and the quest for wellness. We believe selecting and investing in companies that play an active role in these transformations should lead to more resilient portfolios that generate higher long-term returns. Our investment recommendations in the digital globalisation space are labelled "b-Digital", those in the economic transition space "b-Transition" and those in the wellness space "b-Well". A given recommendation may fall under more than one theme, in which case it will carry the relevant matching labels.

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