

COMPANY UPDATE

Galapagos NV (GLPG.AS)

Buy

Equity Research

Updating numbers for cystic fibrosis delay

What's changed

At its recent R&D day, Galapagos highlighted its intention to pursue at least three proprietary triple combinations for the treatment of Cystic Fibrosis (CF). We view the additional shots on goal as a positive. However, as a consequence of planned discussions with UK regulatory authorities around best trial design, its previous guidance of a mid-2017 triple combination trial initiation has now been revised to 4Q17. Because of this delay and the plan to initiate multiple triple combination studies, we revise our forecasts to model the launch of CF in late 2021 (previously 2020). AbbVie has the rights to Galapagos' cystic fibrosis compounds, and Galapagos receives royalties in the mid-teens to 20% and milestones.

Implications

As a result of this slight delay in timeline, the value of the CF indication in our DCF-based SOTP valuation decreases to €7/share (previously €9/share), resulting in a new 12-month price target of €94 (from €96).

Valuation

We maintain our Buy rating on Galapagos, but reduce our 12-month price target to €94. This is driven by a 12-month SOTP (DCF-based) value of €89/share (85% weighting) and an M&A valuation of €119/share (15% weighting, reflecting Galapagos' rank of 2 on our M&A framework). Our M&A valuation is calculated by: (1) applying a 7.5% WACC to our stand-alone DCF (assumed WACC of a larger potential acquirer), rather than the 10% WACC we assume for Galapagos; and (2) assuming 90% cost synergies (as we believe an acquirer would acquire Galapagos for its IP rather than the infrastructure).

Key risks

Key downside risks to our view include the outcomes of clinical trials, ability to recruit patients into later-stage CF trials and potential value-destructive M&A.

INVESTMENT LIST MEMBERSHIP

Pan-Europe Buy List

Coverage View: Neutral

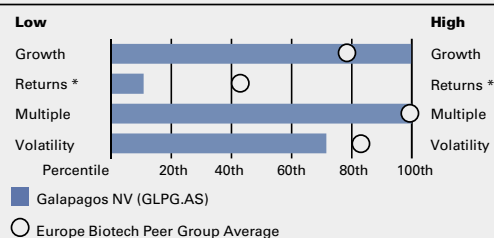
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Investment Profile

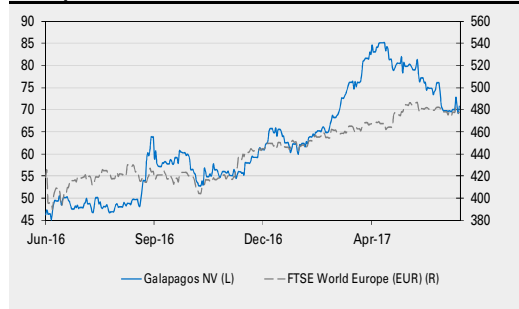


* Returns = Return on Capital For a complete description of the investment profile measures please refer to the disclosure section of this document.

Key data	Current
Price (€)	70.72
12 month price target (€)	94.00
Upside/downside (%)	33
Market cap (€ mn)	3,231.6
Enterprise value (€ mn)	2,270.4

	12/16	12/17E	12/18E	12/19E
Revenue (€ mn)	151.6	63.4	66.4	191.8
EBIT (€ mn)	(11.5)	(100.8)	(103.5)	18.1
EPS (€)	1.18	(1.45)	(1.46)	0.78
EV/EBITDA (X)	NM	NM	NM	114.4
P/E (X)	41.1	NM	NM	91.0
Dividend yield (%)	0.0	0.0	0.0	0.0
FCF yield (%)	10.6	(3.5)	(3.9)	(3.0)
CROCI (%)	99.1	672.4	675.8	(540.3)
CROCI/WACC (X)	--	--	--	--
EV/GCI (X)	--	--	--	61.2

Price performance chart



Share price performance (%)	3 month	6 month	12 month
Absolute	(7.3)	19.4	52.9
Rel. to FTSE World Europe (EUR)	(10.8)	10.7	34.1

Source: Company data, Goldman Sachs Research estimates, FactSet. Price as of 6/22/2017 close.

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Galapagos NV: Summary Financials

Profit model (€ mn)	12/16	12/17E	12/18E	12/19E	Balance sheet (€ mn)	12/16	12/17E	12/18E	12/19E
Total revenue	151.6	63.4	66.4	191.8	Cash & equivalents	973.2	1,199.8	1,093.8	1,004.5
Operating costs	(23.5)	(24.2)	(25.0)	(25.7)	Accounts receivable	9.7	6.9	7.2	20.7
R&D	(139.6)	(140.0)	(145.0)	(148.0)	Inventory	0.3	0.0	0.0	0.0
Lease payments	0.0	0.0	0.0	0.0	Other current assets	24.0	24.0	24.0	24.0
Other operating profit/(expense)	0.0	0.0	0.0	0.0	Total current assets	1,007.2	1,230.6	1,125.0	1,049.2
EBITDA	(7.3)	(96.5)	(99.7)	22.1	Net PP&E	15.0	16.2	17.5	18.7
Depreciation & amortisation	(4.2)	(4.3)	(3.8)	(4.0)	Net intangibles	1.0	0.6	1.0	1.3
EBIT	(11.5)	(100.8)	(103.5)	18.1	Total investments	0.0	0.0	0.0	0.0
Net interest income/(expense)	8.3	16.3	17.1	15.6	Other long-term assets	60.1	56.1	56.1	56.1
Associates	0.0	0.0	0.0	0.0	Total assets	1,083.3	1,303.6	1,199.5	1,125.3
Profit/(loss) on disposals	0.0	0.0	0.0	0.0	Accounts payable	31.3	40.8	42.2	0.0
Others (recurring)	57.5	8.0	8.0	8.0	Short-term debt	0.0	0.0	0.0	0.0
Pretax profits	54.2	(76.5)	(78.4)	41.7	Other current liabilities	72.5	71.5	71.5	71.5
Income tax	(0.2)	5.2	5.3	(2.8)	Total current liabilities	103.8	112.3	113.7	71.5
Tax rate (%)	0.4	6.8	6.8	6.8	Long-term debt	0.0	0.0	0.0	0.0
Minorities	0.0	0.0	0.0	0.0	Other long-term liabilities	220.8	173.6	126.3	79.1
Preferred dividends	0.0	0.0	0.0	0.0	Total long-term liabilities	220.8	173.6	126.3	79.1
Net income (pre-exceptionals)	54.0	(71.3)	(73.1)	38.9	Total liabilities	324.6	285.9	240.0	150.6
Other non-recurring items post tax	0.0	0.0	0.0	0.0	Preferred shares	0.0	0.0	0.0	0.0
Net income	54.0	(71.3)	(73.1)	38.9	Total common equity	758.7	1,017.7	959.5	974.7
EPS (underlying) (€)	1.18	(1.45)	(1.46)	0.78	Minority interest	0.0	0.0	0.0	0.0
EPS (basic, reported) (€)	1.18	(1.45)	(1.46)	0.78	Total liabilities & equity	1,083.3	1,303.6	1,199.5	1,125.3
Weighted shares outstanding (mn)	45.7	49.1	50.0	50.0	Capitalised leases	0.1	0.1	0.1	0.1
Common dividends declared	0.0	0.0	0.0	0.0	Capital employed	758.7	1,017.7	959.5	974.7
DPS (€)	0.00	0.00	0.00	0.00	Adj for unfunded pensions & GW	0.0	0.0	0.0	0.0
Dividend payout ratio (%)	0.0	0.0	0.0	0.0	Adj capital employed	758.7	1,017.7	959.5	974.7
Dividend cover (X)	NM	NM	NM	NM	Gross cash invested	(17.8)	(24.3)	(20.0)	41.3
Growth & margins (%)	12/16	12/17E	12/18E	12/19E	Ratios	12/16	12/17E	12/18E	12/19E
Revenue growth	150.3	(58.2)	4.7	188.7	CROCI (%)	99.1	672.4	675.8	(540.3)
EBITDA growth	91.5	(1,220.1)	(3.4)	122.2	CROCI/WACC (X)	--	--	--	--
EBIT growth	87.2	(777.3)	(2.7)	117.5	ROIC (%)	29.0	158.8	150.1	(47.6)
Net income growth	145.6	(232.0)	(2.4)	153.2	ROIC/WACC (X)	--	--	--	--
EPS growth	135.6	(223.0)	(0.5)	153.2	ROA (%)	6.0	(7.2)	(7.1)	2.1
DPS growth	NM	NM	NM	NM	WACC (%)	--	--	--	--
EBITDA margin	(4.8)	(152.1)	(150.1)	11.5	Inventory days	0.8	0.9	--	--
EBIT margin	(7.6)	(158.9)	(155.9)	9.4	Asset turnover (X)	10.5	4.1	3.9	10.6
Cash flow statement (€ mn)	12/16	12/17E	12/18E	12/19E	Net debt/equity (%)	(128.3)	(117.9)	(114.0)	(103.1)
Net income	54.0	(71.3)	(73.1)	38.9	EBITDA interest cover (X)	0.9	5.9	5.8	(1.4)
D&A add-back (incl. ESO)	4.2	4.3	3.8	4.0	Valuation	12/16	12/17E	12/18E	12/19E
Minority interest add-back	0.0	0.0	0.0	0.0	EV/sales (X)	8.2	35.8	36.8	13.2
Net (inc)/dec working capital	235.0	11.6	1.1	(55.7)	EV/EBITDAR (X)	NM	NM	NM	114.5
Other operating cash flow	(53.7)	(59.6)	(64.4)	(86.1)	EV/EBITDA (X)	NM	NM	NM	114.4
Cash flow from operations	239.4	(114.9)	(132.5)	(98.9)	EV/EBIT (X)	NM	NM	NM	140.1
Capital expenditures	(4.8)	(5.2)	(5.4)	(5.6)	P/E (X)	41.1	NM	NM	91.0
Acquisitions	(2.8)	0.0	0.0	0.0	Dividend yield (%)	0.0	0.0	0.0	0.0
Divestitures	0.0	0.0	0.0	0.0	FCF yield (%)	10.6	(3.5)	(3.9)	(3.0)
Others	0.2	0.0	0.0	0.0	EV/GCI (X)	--	--	--	61.2
Cash flow from investing	(7.3)	(5.2)	(5.4)	(5.6)	EV/adj. capital employed (X)	NM	NM	NM	NM
Dividends paid (common & pref)	0.0	0.0	0.0	0.0	Price/book (X)	3.7	3.5	3.7	3.6
Inc/(dec) in debt	0.0	0.0	0.0	0.0	Note: Ratios are adjusted for leases where appropriate. Only separately disclosed where significant and ongoing.				
Other financing cash flows	396.0	346.6	32.0	15.2	Note: Last actual year may include reported and estimated data.				
Cash flow from financing	396.0	346.6	32.0	15.2	Source: Company data, Goldman Sachs Research estimates.				
Total cash flow	632.9	226.5	(105.9)	(89.3)					
Capex/D&A (%)	114.5	119.7	142.1	137.9					
Reinvestment rate (%)	107.7	(4.1)	(4.1)	(12.9)					
Cash flow cover of dividends (X)	NM	NM	NM	NM					
Free cash flow cover of dividends (X)	--	--	--	--					

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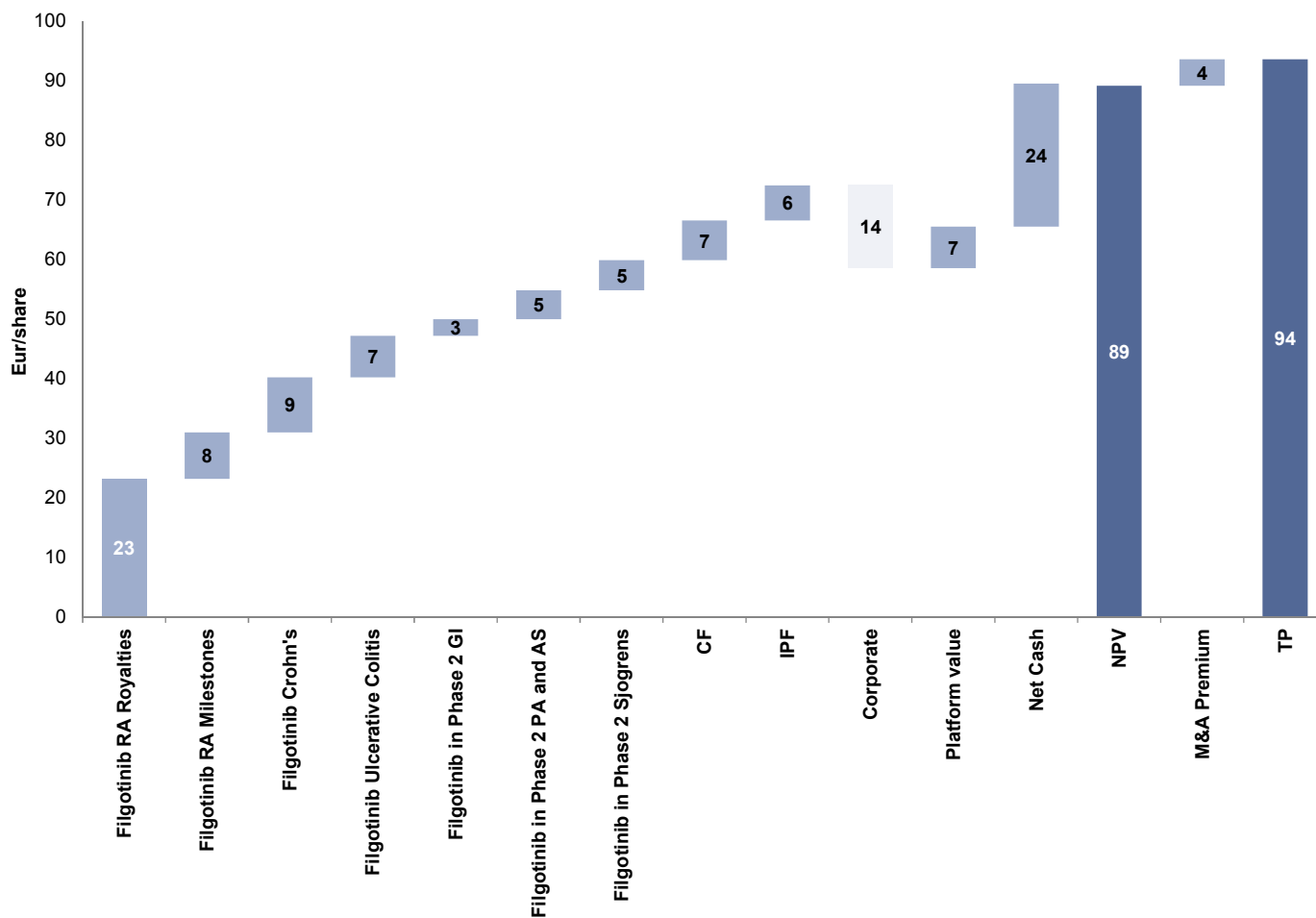
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Overview of SOTP valuation and upcoming catalysts

Below, we show our updated sum-of-the-parts valuation. Our valuation is explained by filgotinib in its Phase 3 trials (rheumatoid arthritis, Crohn’s and Ulcerative Colitis) and the company’s cash. Upside optionality comes from cystic fibrosis, idiopathic pulmonary fibrosis (IPF) and the earlier Phase 2 trials for filgotinib – which Galapagos and partner Gilead continue to add to.

Exhibit 1: Valuation is driven by filgotinib and cash, with cystic fibrosis and early-stage pipeline offering upside
 Overview of SOTP valuation and derivation of 12-month price target



Source: Goldman Sachs Global Investment Research.

Exhibit 2: The key events for 2017 include data in IPF and the results of the ALBATROSS study in cystic fibrosis

Timeline of upcoming readouts

Timing	Drug	Indication	Study	Partner	Phase	Event
Dec 17	GLPG2222 + Kalydeco	Cystic Fibrosis	ALBATROSS	ABBV	2	Data read-out
3Q17	GLPG1690	IPF	FLORA	JNJ	2	Topline results phase 2a
28/10/17-01/11/2017: UEGW (GI) Conference						
2-4/11/17: NACFC (Cystic Fibrosis) Conference						
3-8/11/17: ACR (Rheumatology) Conference						
2H17	MOR106	Atopic Dermatitis		Morphosys	1b	Data read-out
4Q17	GLPG2737+ Orkambi	Cystic Fibrosis		ABBV	1b	Phase 1 study initiation
4Q17	'2451+'2222+'2737	Cystic Fibrosis		ABBV	1b	Phase 1 study initiation; read out mid 2018
Mar 18	GLPG2222	Cystic Fibrosis	FLAMINGO	ABBV	2	Data read-out
Early 2018	'3067+'2222+'2737	Cystic Fibrosis		ABBV	1b	Phase 1 study initiation; read out 2H18
1Q18	GLPG1972	Osteoarthritis		Servier	1	Data read-out
May 18	Filgotinib	Ankylosing Spondylitis	TORTUGA	Gilead	2	Data read-out
Jun 18	Filgotinib	Rheumatoid Arthritis	FINCH 2	Gilead	3	Data read-out
Jun 18	Filgotinib	Psoriatic Arthritis	EQUATOR	Gilead	2	Data read-out
Mid 2018	'3067+'2222+'3221'	Cystic Fibrosis		ABBV	1b	Phase 1 study initiation; read out 2019
Aug 18	Filgotinib	Sjogren's Syndrome		Gilead	2	Data read-out
Sep 18	Filgotinib	Cutaneous Lupus		Gilead	2	Data read-out
Apr 19	Filgotinib	Rheumatoid Arthritis	FINCH 1	Gilead	3	Data read-out
Apr 19	Filgotinib	Crohn's disease-SBCD		Gilead	2	Data read-out
May 19	Filgotinib	Crohn's disease-FCD		Gilead	2	Data read-out
Nov 19	Filgotinib	Crohn's disease	DIVERSITY 1	Gilead	3	Data read-out
Nov 19	Filgotinib	Ulcerative colitis	SELECTION 1	Gilead	2/3	Data read-out
Feb 20	Filgotinib	Rheumatoid Arthritis	FINCH 3	Gilead	3	Data read-out

Source: Company data, Goldman Sachs Global Investment Research.

Disclosure Appendix

Reg AC

We, Tim Woodward, CFA, Keyur Parekh, Rebekah Yu, Ph.D. and Mick Readey, hereby certify that all of the views expressed in this report accurately reflect our personal views about the subject company or companies and its or their securities. We also certify that no part of our compensation was, is or will be, directly or indirectly, related to the specific recommendations or views expressed in this report.

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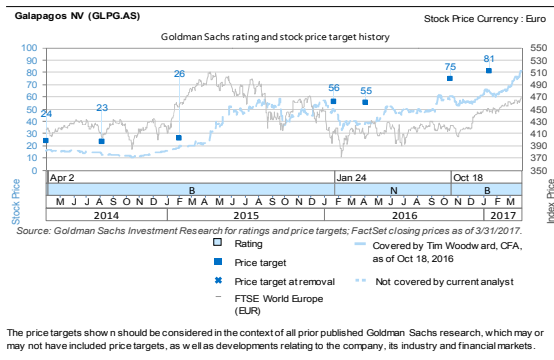
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Price target and rating history chart(s)



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