



## COMPANY UPDATE / ESTIMATE CHANGE / PRICE TARGET CHANGE

### Key Metrics

|                             |                   |
|-----------------------------|-------------------|
| LLY - NYSE (as of 04/25/17) | \$81.20           |
| 2 Year Price Target         | \$93.00           |
| 52-Week Range               | \$86.72 - \$64.18 |
| Shares Outstanding (mm)     | 1,103             |
| Market Cap. (\$mm)          | \$89,592          |
| 1-Mo. Average Daily Volume  | 4,039,079         |
| Institutional Ownership     | 77.3%             |
| Debt / Total Capital        | 31.0%             |
| ROE (TTM)                   | 14.8%             |
| Book Value / Share          | \$13.20           |
| Price / Book Value          | 6.2x              |
| Indicated Dividend / Yield  | \$2.08 2.6%       |
| TTM Operating Margin        | 19.2%             |

### Non-GAAP EPS FY 12/31

|      | 2016A  | Prior<br>2017E | Curr.<br>2017E | Prior<br>2018E | Curr.<br>2018E |
|------|--------|----------------|----------------|----------------|----------------|
| 1Q   | \$0.83 |                | \$0.98A        | \$1.07         | \$1.03         |
| 2Q   | \$0.86 | \$1.07         | \$1.06         | \$1.09         | \$1.03         |
| 3Q   | \$0.88 | \$1.13         | \$1.13         | \$1.25         | \$1.26         |
| 4Q   | \$0.95 | \$0.96         | \$0.93         | \$1.14         | \$1.17         |
| Year | \$3.52 | \$4.13         | \$4.11         | \$4.55         | \$4.48         |
| P/E  | 23.1x  |                | 19.8x          |                | 18.1x          |

Figures may not add up due to rounding

### Revenue (\$billions)

|      | 2016A   | Prior<br>2017E | Curr.<br>2017E | Prior<br>2018E | Curr.<br>2018E |
|------|---------|----------------|----------------|----------------|----------------|
| 1Q   | \$4.87  |                | \$5.23A        | \$5.39         | \$5.19         |
| 2Q   | \$5.40  | \$5.71         | \$5.57         | \$5.66         | \$5.48         |
| 3Q   | \$5.19  | \$5.54         | \$5.48         | \$5.69         | \$5.62         |
| 4Q   | \$5.76  | \$5.65         | \$5.61         | \$5.87         | \$5.86         |
| Year | \$21.22 | \$22.21        | \$21.89        | \$22.61        | \$22.15        |

**Company Description** – Eli Lilly & Company is a multinational biopharmaceutical company focused on developing and marketing innovative medicines in the areas of endocrinology, oncology, neuroscience, pain, and autoimmune diseases. The company also sells several cardiovascular medicines.

### Pharmaceuticals

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## Eli Lilly & Company

LLY – NYSE – Long-term Buy – 1

### A Mixed First Quarter but Dynamics Remain Positive with or without Baricitinib

- **1Q17 Results:** LLY reported revenues of \$5.23 billion, growth of 7.5% year-over-year. This fell short of our estimate of \$5.31 billion but beat the Street consensus estimate of \$5.21 billion. Non-GAAP EPS were \$0.98 compared to our estimate of \$0.97 and the Street consensus of \$0.96. Management reiterated 2017 revenue and non-GAAP EPS guidance despite the setback from baricitinib but GAAP EPS guidance was lowered.
- **Positive Highlights:** Taltz, Trulicity, and Lartruvo delivered strong beats relative to our estimates. The gross margin expanded 180 basis points year-over-year to 74.6% versus our estimate of 73.3%.
- **Negative Highlights:** Jardiance revenues disappointed relative to our estimates, as did oncology drugs Alimta and Cyramza. The Animal Health segment disappointed due to weakness in Companion Animal sales. Cialis revenue fell well short of our estimates, but we note this product is nearing generic competition.
- **Outlook and Estimates:** Our outlook for Lilly remains positive. However, given the baricitinib news, we are revising downward our FY17 revenue estimate to \$21.89 billion versus our prior estimate of \$22.21 billion. We are also decreasing our non-GAAP EPS estimate to \$4.11 from \$4.13. For FY18, we decreased our revenue estimate to \$22.15 billion from \$22.61 billion and decreased our non-GAAP EPS estimate to \$4.48 from \$4.55.
- **Valuation and Rating:** LLY closed yesterday at 19.6X our next 12 months non-GAAP EPS estimate. Given an attractive growth profile and well diversified portfolio, we believe this is a P/E set for expansion. Using both a P/E and DCF valuation methodology (see page 5), we are raising our two year price target to \$93 from \$92 and maintaining our Long-term Buy rating. We note our increased price target is the result of moving our valuation model forward a quarter, offsetting the disappointment from baricitinib.

**Note Important Disclosures on pages 9 and 10**  
**Note Analyst Certification on page 9**

**ADDITIONAL COMMENTARY**

| <b>Revenue Review</b> |                     |                     |                        |
|-----------------------|---------------------|---------------------|------------------------|
| <b>Drug/ Category</b> | <b>Our Estimate</b> | <b>1Q17 Results</b> | <b>1Q17 Y/Y Growth</b> |
| Neuroscience          | 565                 | 579                 | -10.0%                 |
| Humalog               | 628                 | 708                 | 16.8%                  |
| Humulin               | 365                 | 315                 | -11.8%                 |
| Forteo                | 332                 | 348                 | 9.1%                   |
| Tradjenta             | 117                 | 113                 | 19.7%                  |
| Jardiance             | 108                 | 74                  | 93.7%                  |
| Trulicity             | 355                 | 373                 | 159.7%                 |
| Basaglar              | 49                  | 46                  | 322.0%                 |
| Other Endocrinology   | 166                 | 147                 | -22.1%                 |
| Taltz                 | 82                  | 97                  | N/A                    |
| Olumiant              | 0                   | 2                   | N/A                    |
| Alimta                | 506                 | 490                 | -13.2%                 |
| Cyramza               | 190                 | 171                 | 30.7%                  |
| Lartruvo              | 15                  | 42                  | N/A                    |
| Other Oncology        | 182                 | 184                 | -7.8%                  |
| Cialis                | 601                 | 534                 | -7.5%                  |
| Other Cardiovascular  | 180                 | 164                 | -7.8%                  |
| Other Pharmaceutical  | 51                  | 74                  | 20.0%                  |
| Animal Health         | 813                 | 769                 | 2.0%                   |
| <b>Total Revenue</b>  | <b>5,306</b>        | <b>5,228</b>        | <b>7.5%</b>            |

Source: Company Reports, Hilliard Lyons Estimates

***Performance Review***

- Revenue growth of 7.5% fell short of our estimate but beat the Street consensus. Volume growth of 9% in the Pharmaceutical segment was driven mostly by new products, with 12% volume growth in the U.S.
- The **Neuroscience** portfolio continues to dwindle but beat our estimate. However, the outlook for the portfolio worsens this quarter with generic competition approaching for Strattera.
- Within **Endocrinology**, Humalog and Trulicity delivered solid outperformance. Humalog benefitted from a weak comparison in 1Q16 and increased demand. Trulicity growth continues to impress, as management noted the GLP-1 class is still growing rapidly in the U.S. and Trulicity continues to gain market share within the class. Trulicity is in line with class leader Victoza (Novo Nordisk) for new-to-brand (NBRx) prescriptions among endocrinologists. Humulin and Jardiance disappointed, as the latter decreased sequentially. Humulin faced tough comps and decreased demand. Jardiance remains the SGLT-2 class leader in NBRx among endocrinologists, and new therapy starts among both endocrinologists and primary care physicians jumped after the label expansion. However, this has yet to show through in a meaningful way, in our opinion.

- Taltz growth was impressive, and we now expect the drug to cross the \$500 million mark this year, its first full year on the market. In the U.S., the drug's NBRx among dermatologists is already higher than Enbrel (Amgen) and Cosentyx (Novartis), and total NBRx is already higher than Enbrel and approaching Cosentyx. The **Immunology** portfolio added Olumiant revenues this quarter.
- Within the **Oncology** portfolio, Alimta disappointed as generics continue to weigh on the drug in Europe, and immuno-oncology agents pressure the drug in non-small cell lung cancer (NSCLC) in the U.S. We remind investors of the company's success in U.S. courts regarding patent protection and the possibility of an accelerated approval of Alimta with Merck's Keytruda in 1L NSCLC. Thus, we are not significantly concerned about this quarter's miss. On the other hand, Cyramza also disappointed as sales were roughly flat sequentially. We expected competitive pressure in the U.S. and European markets to keep a lid on growth but anticipated continued growth in Japan due to strength in gastric cancer. However, sales in Japan were down ~9% sequentially, but management stated the Japanese disappointment was simply the result of timing, and they have seen recent uptake in lung and colorectal cancer in that market. Lartruvo was the lone outperformer in the Oncology portfolio, as heightened interest in the first new drug for soft tissue sarcoma in 40 years led to rapid uptake.
- **Cialis** revenue fell well short of our estimate as the market shrank in the U.S. due to generic sildenafil (Viagra). Despite the disappointment, our outlook has not changed as this drug will be subject to generic competition toward the end of 2017.
- **Animal Health** disappointed, as the Companion Animal segment's struggles were masked by the acquisition of Vetmedica. Including the Livestock segment, Elanco's 3% year-over-year organic decline became 2% growth due to \$40.8 million in revenue from Vetmedica.
- The GAAP gross margin increased 180 basis points from 1Q16 to 74.6%, which exceeded our estimate of 73.3%. The increase was driven primarily by manufacturing efficiencies. Management noted product mix was not a significant contributor to the gross margin gain.
- Core operating expenses came in slightly higher than anticipated due to MS&A expenses. MS&A expenses were \$1.54 billion versus our estimate of \$1.52 billion, and R&D expenses were \$1.24 billion versus our estimate of \$1.25 billion.
- The GAAP pretax profit of \$61.2 million fell well short of our estimate of \$210 million, primarily due to higher restructuring costs than we estimated (\$213.9 million in total). Overall, the low GAAP numbers for the quarter were also the result of an \$857.6 million R&D charge for the acquisition of CoLucid Pharmaceuticals. This charge did not generate a tax benefit, so the GAAP tax rate was actually 281.0%. After adjustments and a non-GAAP effective tax rate of 21.2% (versus our estimate of 20.7%), non-GAAP EPS were \$0.98 versus our estimate of \$0.97 and the Street consensus estimate of \$0.96.

#### *Earnings Conference Call and Other Notes*

- As expected, the Q&A portion of the call centered on baricitinib. Management largely remained quiet, which is understandable considering they haven't met with the FDA and were probably just as blindsided as the market by the complete response letter. Management restated their disagreement with the FDA multiple times. The most interesting tidbit from baricitinib discussion was CFO Derica Rice's comment that the company has generated additional data from extension studies that the FDA does not have in their hands. We encourage investors to take a conservative approach to their baricitinib outlook, but this does provide a glimmer of hope.
- There was also a lot of discussion about abemaciclib, for which management continued to show confidence. However, details on the call were sparse, as expected.
- In our opinion, the other substantive part of the conversation focused on this quarter's results for Jardiance and Cyramza. For the former, there seemed to be a disconnect between management and analysts in terms of performance and reasons for this quarter's number. We remain bullish on Jardiance but will be keeping a close eye on numbers for the next few quarters. For Cyramza, we believe management did a good job discussing the quarter and remain confident in the drug's success in Japan.

### *News Review*

Key news items since our last report on February 1, 2017:

- The most important piece of news, in our opinion, came from baricitinib. The European Commission approved the drug, branded as Olumiant, on February 13<sup>th</sup>. However, on April 14<sup>th</sup>, the FDA issued a complete response letter, rejecting the drug due to additional data requirements for dosing and safety.
- Another critical news item occurred when Lilly announced the Phase 3 MONARCH 2 study of abemaciclib, in combination with fulvestrant, met its primary endpoint of progression-free survival (PFS) in second-line (2L) metastatic breast cancer (MBC). The full data set will be revealed at the American Society for Clinical Oncology (ASCO) meeting at the beginning of June. Just a few days ago, Lilly also announced the positive readout of MONARCH 3, a Phase 3 study testing abemaciclib in combination with an aromatase inhibitor in 1L MBC. The combination outlasted aromatase inhibitor monotherapy in progression-free survival (PFS) and objective response rate (ORR). The company stated more detailed data will be presented in the second half of the year.
- Lilly and partner Boehringer Ingelheim initiated the EMPEROR HF clinical trial program, which will encompass two Phase 3 studies testing Jardiance in the treatment of chronic heart failure. The trials will include approximately 7,000 patients, with or without Type 2 Diabetes.
- Japan's Intellectual Property High Court ruled in favor of Lilly's Alimta vitamin regimen patents, giving the company protection until June 2021.
- The Trulicity label was updated to incorporate the use of basal insulin with the drug.
- Lilly completed its acquisition of CoLucid Pharmaceuticals for roughly \$960 million. As a reminder to investors, CoLucid's key asset, lasmiditan, is being evaluated for the acute treatment of migraine in a Phase 3 trial, SPARTAN. The trial is expected to be completed in the second half of 2017 and, if successful, could be approved in 2018. Lasmiditan could be a complementary offering in addition to Lilly's Phase 3 asset, galcanezumab, which is being evaluated for the prevention of migraine and cluster headaches. Lilly recognized an \$857.6 million acquired in-process R&D charge with no tax benefit.
- Fionnuala Walsh retired from her position as Senior Vice President of Global Quality. She was replaced by Johna Norton, who was promoted from Vice President of Global Quality for API Manufacturing, Product Research and Development. Additionally, Bart Peterson left his position as Senior Vice President of Corporate Affairs and Communications. Finally, Lilly appointed Dr. Carolyn Bertozzi to the Board of Directors.

### **ESTIMATES & GUIDANCE UPDATE**

We are revising downward our FY17 revenue estimate to \$21.89 billion versus our prior estimate of \$22.21 billion. We are also decreasing our non-GAAP EPS estimate to \$4.11 from \$4.13. For FY18, we decreased our revenue estimate to \$22.15 billion from \$22.61 billion and decreased our operating EPS to \$4.48 from \$4.55. Below are the material changes:

- We significantly lowered our Jardiance estimates due to our changed expectations on the speed of uptake. We initially believed the drug's established presence would allow it to rapidly capitalize on the expanded label, but this quarter's number and management commentary lead us to think it will take more time to educate the physician base and expand usage. However, our longer term bullishness is undeterred; we have simply changed our speed of uptake assumptions. Should Jardiance disappoint the next few quarters, we may have to revisit that outlook.
- Although we still expect Trulicity growth to slow down in FY18 as a result of heightened competition, we increased estimates as a result of continued impressive growth for the GLP-1 class and Trulicity's ability to take market share.
- We increased our Taltz estimates as a result of uptake that has surpassed even our bullish assumptions.

- As a result of the complete response letter from the FDA, we drastically reduced our estimates for baricitinib. This change had the biggest impact (\$264 million decrease) on our FY18 estimates.
- We lowered Cyramza estimates as a result of this quarter's disappointment, although we remain cautiously optimistic this number could see an upward revision in the future. On the other hand, it won't be easy to expand a 57% market share in Japanese gastric cancer, in our opinion.
- We increased our Lartruvo estimates to adjust for the rapid uptake. Longer term, we did not change estimates significantly given the small market size.
- After seeing completion dates moved back on clinicaltrials.gov, we moved back our tanezumab estimates by a couple of quarters.
- The final noteworthy revenue change came from the Companion Animal segment of Animal Health to incorporate struggles in that business.
- We tweaked our gross margin estimate for FY17 upward by approximately 20 basis points, although this was largely an adjustment for this quarter's surprise. Our FY18 gross margin estimate was actually decreased slightly due to management commentary about high margin products facing generic competition later this year. We decreased operating expenses by ~\$60 million for FY17 as a result of expectations for margin expansion to really accelerate toward the end of the year. The main drivers of this are further integration of Animal Health acquisitions and lower MS&A as older products lose marketing support.

### *Guidance*

Lilly left 2017 guidance largely unchanged. Revenue is still expected to be between \$21.8 billion and \$22.3 billion with non-GAAP EPS guidance remaining in a range from \$4.05-\$4.15. Due to the CoLucid acquisition and restructuring charges, GAAP EPS is expected to be between \$2.60 and \$2.70 versus the previous range of \$2.69-\$2.79. In between the top and bottom line, all guidance remains the same: the GAAP gross margin is expected to be 73.5%, MS&A is expected to be between \$6.4 and \$6.6 billion, and R&D is expected to be between \$4.9 and \$5.1 billion.

### **VALUATION & RATING**

LLY closed yesterday trading at 19.6X our next 12 months estimates. Based on our expectations for the company's growth profile and a risk profile that we view as low relative to the industry, we believe this is a P/E set for expansion. Our two year price target is derived through two methodologies: 50% discounted free cash flow and 50% forward P/E. Our forward P/E portion is derived through a proprietary method that assesses the biopharmaceutical industry on the basis of risk and growth. Risk is measured by product concentration while growth is determined through either our estimates or market assumptions about long-term growth. For LLY, this results in a 22.5X multiple applied to FY18/FY19 GAAP EPS estimates for a \$93 price target. We note our use of GAAP estimates given weaker earnings quality, although we do project earnings quality to increase over the next few years. Our discounted free cash flow assumptions include a WACC of 7.8%, which we note is lower than the 7.9% WACC previously used due to our expectations for a shift toward more debt from the Vetmedica acquisition. However, we note this could subject to change as the company has not released its balance sheet or cash flow statement for the quarter yet. Our terminal growth rate estimate is 2.0%, and we added back net cash. The DCF model results in a \$92 price target. Thus, we assign shares a price target of \$93, up from \$92 previously. We note the increased price target comes despite the baricitinib setback primarily due to our model looking forward another quarter, now incorporating 1Q19. We maintain our Long-term Buy rating.

**SUITABILITY**

Eli Lilly & Co. is a large and well-established biopharmaceutical company with a diversified portfolio and robust pipeline. Additionally, at this time, we believe Lilly is better positioned than peers to deal with any potential pricing regulation. However, we strongly note this favorable relative position does not equate to immunity from pricing regulation or market pressures. Based on these considerations, we assign LLY shares a suitability rating of 1.

**RISKS & CONSIDERATIONS**

- **Competition and innovation** – The biopharmaceutical business requires complex operations with many unique and uncertain aspects. A competitor or new company could produce new therapies that could displace LLY drugs.
- **Regulatory** – The biopharmaceutical industry is subject to an intense regulatory environment throughout a product life cycle. Regulatory actions against the company or an individual product may harm financial results.
- **Legal** – Product lawsuits are extremely common in the biopharmaceutical sector. An unfavorable court decision could hamper the ability to market a product or subject the company to earlier generic competition.

Prices of other stocks mentioned:

|                              |
|------------------------------|
| Novo Nordisk (NVO - \$37.08) |
| Merck & Co. (MRK - \$62.30)  |
| Amgen (AMGN - \$164.70)      |
| Novartis AG (NVS - \$76.24)  |

| Revenue Build         |                      |                      |                     |                     |                     |                     |                      |                      |                      |                      |                      |
|-----------------------|----------------------|----------------------|---------------------|---------------------|---------------------|---------------------|----------------------|----------------------|----------------------|----------------------|----------------------|
| <i>In millions</i>    | <u>2015 A</u>        | <u>2016 A</u>        | <u>1Q17 A</u>       | <u>2Q17 E</u>       | <u>3Q17 E</u>       | <u>4Q17 E</u>       | <u>2017 E</u>        | <u>2018 E</u>        | <u>2019 E</u>        | <u>2020 E</u>        | <u>2021 E</u>        |
| Strattera             | 784                  | 855                  | 196                 | 157                 | 107                 | 113                 | 573                  | 372                  | 327                  | 292                  | 260                  |
| Other Neuroscience    | 2,151                | 1,866                | 383                 | 354                 | 325                 | 325                 | 1,387                | 1,172                | 1,018                | 890                  | 773                  |
| Humalog               | 2,842                | 2,769                | 708                 | 688                 | 649                 | 724                 | 2,769                | 2,675                | 2,601                | 2,544                | 2,489                |
| Humulin               | 1,307                | 1,366                | 315                 | 326                 | 329                 | 358                 | 1,327                | 1,339                | 1,351                | 1,355                | 1,359                |
| Forteo                | 1,348                | 1,500                | 348                 | 384                 | 405                 | 427                 | 1,564                | 1,606                | 1,503                | 1,293                | 1,241                |
| Tradjenta             | 357                  | 437                  | 113                 | 144                 | 132                 | 131                 | 520                  | 551                  | 586                  | 624                  | 658                  |
| Jardiance             | 60                   | 202                  | 74                  | 98                  | 138                 | 178                 | 488                  | 1,027                | 1,313                | 1,477                | 1,566                |
| Trulicity             | 249                  | 926                  | 373                 | 399                 | 425                 | 441                 | 1,638                | 1,908                | 2,308                | 2,621                | 2,956                |
| Basaglar              | 11                   | 86                   | 46                  | 76                  | 104                 | 128                 | 354                  | 653                  | 813                  | 943                  | 1,033                |
| Other Endocrinology   | 862                  | 798                  | 147                 | 158                 | 158                 | 156                 | 618                  | 574                  | 559                  | 542                  | 525                  |
| Taltz                 | 0                    | 113                  | 97                  | 123                 | 143                 | 163                 | 524                  | 843                  | 1,275                | 1,475                | 1,600                |
| Olumiant              | 0                    | 0                    | 2                   | 10                  | 16                  | 24                  | 52                   | 226                  | 415                  | 610                  | 825                  |
| Alimta                | 2,493                | 2,283                | 490                 | 508                 | 526                 | 509                 | 2,032                | 1,932                | 1,850                | 1,800                | 1,300                |
| Cyramza               | 384                  | 614                  | 171                 | 167                 | 167                 | 167                 | 672                  | 738                  | 784                  | 836                  | 858                  |
| Lartruvo              | 0                    | 12                   | 42                  | 44                  | 48                  | 52                  | 186                  | 258                  | 318                  | 425                  | 500                  |
| Abemaciclib           | 0                    | 0                    | 0                   | 0                   | 0                   | 5                   | 5                    | 132                  | 300                  | 500                  | 625                  |
| Other Oncology        | 633                  | 813                  | 184                 | 195                 | 198                 | 171                 | 748                  | 743                  | 742                  | 710                  | 680                  |
| Cialis                | 2,311                | 2,472                | 534                 | 603                 | 576                 | 471                 | 2,184                | 1,034                | 631                  | 439                  | 395                  |
| Other Cardiovascular  | 757                  | 754                  | 164                 | 199                 | 148                 | 115                 | 625                  | 380                  | 345                  | 312                  | 280                  |
| Other Pharmaceutical* | 228                  | 200                  | 74                  | 49                  | 45                  | 40                  | 208                  | 406                  | 870                  | 1,413                | 1,856                |
| Animal Health         | 3,181                | 3,158                | 769                 | 894                 | 845                 | 911                 | 3,418                | 3,579                | 3,840                | 4,071                | 4,262                |
| <b>Total</b>          | <b><u>19,959</u></b> | <b><u>21,222</u></b> | <b><u>5,228</u></b> | <b><u>5,573</u></b> | <b><u>5,483</u></b> | <b><u>5,608</u></b> | <b><u>21,892</u></b> | <b><u>22,149</u></b> | <b><u>23,750</u></b> | <b><u>25,171</u></b> | <b><u>26,042</u></b> |
| <b>% of Total</b>     |                      |                      |                     |                     |                     |                     |                      |                      |                      |                      |                      |
| Neuroscience          | 14.7%                | 12.8%                | 11.1%               | 9.2%                | 7.9%                | 7.8%                | 9.0%                 | 7.0%                 | 5.7%                 | 4.7%                 | 4.0%                 |
| Endocrinology         | 35.3%                | 38.1%                | 40.6%               | 40.8%               | 42.7%               | 45.3%               | 42.4%                | 46.7%                | 46.5%                | 45.3%                | 45.4%                |
| Immunology            | 0.0%                 | 0.5%                 | 1.9%                | 2.4%                | 2.9%                | 3.3%                | 2.6%                 | 4.8%                 | 7.1%                 | 8.3%                 | 9.3%                 |
| Oncology              | 17.6%                | 17.4%                | 17.0%               | 16.4%               | 17.1%               | 16.1%               | 16.6%                | 17.2%                | 16.8%                | 17.0%                | 15.2%                |
| Cardiovascular        | 15.4%                | 15.2%                | 13.3%               | 14.4%               | 13.2%               | 10.5%               | 12.8%                | 6.4%                 | 4.1%                 | 3.0%                 | 2.6%                 |
| Other Pharmaceutical* | 1.1%                 | 0.9%                 | 1.4%                | 0.9%                | 0.8%                | 0.7%                | 0.9%                 | 1.8%                 | 3.7%                 | 5.6%                 | 7.1%                 |
| Animal Health         | 15.9%                | 14.9%                | 14.7%               | 16.0%               | 15.4%               | 16.2%               | 15.6%                | 16.2%                | 16.2%                | 16.2%                | 16.4%                |

\* Includes our estimate of risk-adjusted revenues from the pipeline

Source: Company Reports and Hilliard Lyons Estimates

| Eli Lilly & Co.                 |                      |                      |                     |                     |                     |                      |                      |                      |                      |                      | LLY: Long-term Buy   |  |  |  |  |
|---------------------------------|----------------------|----------------------|---------------------|---------------------|---------------------|----------------------|----------------------|----------------------|----------------------|----------------------|----------------------|--|--|--|--|
| In billions (except share data) |                      |                      |                     |                     |                     |                      |                      |                      |                      |                      |                      |  |  |  |  |
| Fiscal Period End               | 2015 A<br>12/31/2015 | 2016 A<br>12/31/2016 | 1Q17 A<br>3/31/2017 | 2Q17 E<br>6/30/2017 | 3Q17 E<br>9/30/2017 | 4Q17 E<br>12/31/2017 | 2017 E<br>12/31/2017 | 2018 E<br>12/31/2018 | 2019 E<br>12/31/2019 | 2020 E<br>12/31/2020 | 2021 E<br>12/31/2021 |  |  |  |  |
| Income Statement                |                      |                      |                     |                     |                     |                      |                      |                      |                      |                      |                      |  |  |  |  |
| Net Revenue                     | 19.96                | 21.22                | 5.23                | 5.57                | 5.48                | 5.61                 | 21.89                | 22.15                | 23.75                | 25.17                | 26.04                |  |  |  |  |
| Gross Margin %                  | 74.8%                | 73.4%                | 74.6%               | 74.5%               | 72.5%               | 73.6%                | 73.8%                | 73.9%                | 75.5%                | 76.3%                | 76.8%                |  |  |  |  |
| Core Operating Expenses         | 11.3                 | 11.7                 | 2.8                 | 3.0                 | 2.7                 | 3.0                  | 11.5                 | 11.0                 | 11.6                 | 12.1                 | 12.6                 |  |  |  |  |
| GAAP Core Operating Income      | 3.6                  | 3.9                  | 1.1                 | 1.2                 | 1.3                 | 1.1                  | 4.7                  | 5.3                  | 6.3                  | 7.1                  | 7.4                  |  |  |  |  |
| GAAP Operating Margin %         | 18.0%                | 18.2%                | 21.4%               | 21.2%               | 23.5%               | 19.8%                | 21.4%                | 24.1%                | 26.6%                | 28.0%                | 28.5%                |  |  |  |  |
| Non-Core Expenses               | 0.8                  | 0.5                  | 1.1                 | 0.1                 | 0.1                 | 0.1                  | 1.2                  | 0.2                  | 0.2                  | 0.2                  | 0.2                  |  |  |  |  |
| Non-GAAP Adjustments            | 1.8                  | 1.3                  | 1.3                 | 0.2                 | 0.2                 | 0.2                  | 2.0                  | 0.8                  | 0.5                  | 0.3                  | 0.2                  |  |  |  |  |
| Non-GAAP Pre-Tax Profit         | 4.6                  | 4.7                  | 1.3                 | 1.4                 | 1.5                 | 1.3                  | 5.4                  | 6.0                  | 6.6                  | 7.2                  | 7.4                  |  |  |  |  |
| Margin %                        | 23.2%                | 22.0%                | 25.2%               | 24.7%               | 26.7%               | 23.0%                | 24.9%                | 27.1%                | 27.8%                | 28.5%                | 28.5%                |  |  |  |  |
| Non-GAAP Effective Tax Rate     | 12.7%                | 20.1%                | 21.2%               | 18.8%               | 18.7%               | 24.6%                | 20.7%                | 22.1%                | 22.2%                | 22.2%                | 22.2%                |  |  |  |  |
| Non-GAAP Net Income             | 3.7                  | 3.7                  | 1.0                 | 1.1                 | 1.2                 | 1.0                  | 4.3                  | 4.7                  | 5.1                  | 5.6                  | 5.8                  |  |  |  |  |
| Diluted Shares Outstanding      | 1.1                  | 1.1                  | 1.1                 | 1.1                 | 1.1                 | 1.0                  | 1.1                  | 1.0                  | 1.0                  | 1.0                  | 1.0                  |  |  |  |  |
| GAAP Diluted EPS                | \$2.26               | \$2.58               | -\$0.10             | \$0.88              | \$0.97              | \$0.76               | \$2.51               | \$3.86               | \$4.58               | \$5.16               | \$5.45               |  |  |  |  |
| Non-GAAP Diluted EPS            | \$3.43               | \$3.52               | \$0.98              | \$1.06              | \$1.13              | \$0.93               | \$4.11               | \$4.48               | \$4.94               | \$5.39               | \$5.59               |  |  |  |  |
| *Balance Sheet                  |                      |                      |                     |                     |                     |                      |                      |                      |                      |                      |                      |  |  |  |  |
| Cash and Equivalents            | 3.7                  | 4.6                  | 2.9                 | 1.8                 | 2.0                 | 2.1                  | 2.1                  | 3.5                  | 6.0                  | 8.9                  | 11.8                 |  |  |  |  |
| Other Current Assets            | 8.9                  | 10.5                 | 9.3                 | 9.5                 | 9.6                 | 9.6                  | 9.6                  | 9.7                  | 9.6                  | 9.7                  | 10.0                 |  |  |  |  |
| Total Current Assets            | 12.6                 | 15.1                 | 12.1                | 11.3                | 11.6                | 11.8                 | 11.8                 | 13.3                 | 15.5                 | 18.6                 | 21.8                 |  |  |  |  |
| Net PP&E                        | 8.1                  | 8.3                  | 8.2                 | 8.1                 | 8.1                 | 8.0                  | 8.0                  | 7.6                  | 7.4                  | 7.2                  | 7.1                  |  |  |  |  |
| Other Assets                    | 14.9                 | 15.5                 | 17.3                | 17.3                | 17.3                | 17.3                 | 17.3                 | 17.3                 | 17.3                 | 17.3                 | 17.3                 |  |  |  |  |
| Total Assets                    | 35.6                 | 38.8                 | 37.6                | 36.7                | 36.9                | 37.1                 | 37.1                 | 38.2                 | 40.2                 | 43.1                 | 46.1                 |  |  |  |  |
| Current Liabilities             | 8.2                  | 11.0                 | 8.6                 | 7.5                 | 8.3                 | 8.4                  | 8.4                  | 8.4                  | 8.5                  | 8.8                  | 9.0                  |  |  |  |  |
| Non-Current Liabilities         | 12.7                 | 13.7                 | 14.6                | 14.6                | 13.8                | 13.8                 | 13.8                 | 13.5                 | 13.3                 | 13.3                 | 13.3                 |  |  |  |  |
| Total Liabilities               | 21.0                 | 24.7                 | 23.2                | 22.2                | 22.1                | 22.2                 | 22.2                 | 21.9                 | 21.8                 | 22.1                 | 22.3                 |  |  |  |  |
| Total Shareholders' Equity      | 14.6                 | 14.1                 | 14.4                | 14.6                | 14.8                | 14.9                 | 14.9                 | 16.3                 | 18.4                 | 21.0                 | 23.8                 |  |  |  |  |
| *Cash Flow Statement            |                      |                      |                     |                     |                     |                      |                      |                      |                      |                      |                      |  |  |  |  |
| Cash Flow from Operations       | 3.0                  | 4.9                  | 0.6                 | 1.3                 | 1.4                 | 1.3                  | 2.8                  | 5.8                  | 6.8                  | 7.1                  | 7.2                  |  |  |  |  |
| Cash Flow from Investing        | 0.0                  | (3.1)                | (1.6)               | (0.3)               | (0.3)               | (0.3)                | (2.6)                | (1.3)                | (1.4)                | (1.5)                | (1.5)                |  |  |  |  |
| Cash Flow from Financing        | (3.1)                | (0.6)                | (0.7)               | (2.1)               | (0.8)               | (0.8)                | (4.4)                | (3.0)                | (2.9)                | (2.7)                | (2.8)                |  |  |  |  |
| Free Cash Flow to Equity        | -3.8                 | 4.0                  | -1.3                | -0.3                | 1.1                 | 1.0                  | 0.4                  | 4.0                  | 5.2                  | 5.7                  | 5.8                  |  |  |  |  |

\*1Q17 Balance Sheet and Cash Flow numbers are still estimates, as the company has not released a 10-Q yet  
Source: Company Reports and Hilliard Lyons estimates

Additional information is available upon request.



**Analyst Certification**

I, Kurt A. Kemper, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject company(ies) and its (their) securities. I also certify that I have not been, am not, and will not be receiving direct or indirect compensation in exchange for expressing the specific recommendation(s) in this report.

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**Buy** - We believe the stock has significant total return potential in the coming 12 months.

**Long-term Buy** - We believe the stock is an above average holding in its sector, and expect solid returns to be realized over a longer time frame than our Buy rated issues, typically 2-3 years.

**Neutral** - We believe the stock is an average holding in its sector, is currently fully valued, and may be used as a source of funds if better opportunities arise.

**Underperform** - We believe the stock is vulnerable to a price set back in the next 12 months.

**Definitions of Suitabilities:**

1. A large cap, core holding with a solid history.
2. A historically secure company which could be cyclical, has a shorter history than a "1" or is subject to event driven setbacks.
3. An above average risk/reward ratio could be due to small size, lack of product diversity, sporadic earnings or high leverage.
4. Speculative, due to small size, inconsistent profitability, erratic revenue, volatility, low trading volume or a narrow customer or product base



| Hilliard Lyons<br>Recommended Issues |                        |                        | Investment Banking<br>Provided in Past 12 Mo. |            |
|--------------------------------------|------------------------|------------------------|---|------------|
| Rating                               | # of<br>Stocks Covered | % of<br>Stocks Covered | Banking                                       | No Banking |
| Buy                                  | 36                     | 30%                    | 14%   | 86%        |
| Hold/Neutral                         | 71                     | 58%                    | 6%  | 94%        |
| Sell                                 | 15                     | 12%                    | 7%  | 93%        |

As of 5 April 2017

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