



CAIRN
INVESTMENT
GROUP

COMPANY SPOTLIGHT:

Novo Nordisk

COMPANY DESCRIPTION

Headquartered in Denmark, Novo Nordisk is a global pharmaceutical company, leading in the production of insulin and providing services for those with diabetes, rare bleeding disorders, and obesity.

Lars Fruergaard Jørgensen became Novo Nordisk's CEO in 2017 after working in various positions in the company since 1991.

COMPANY HIGHLIGHTS AND FINANCIALS

KEY POINTS

- :: A leader in diabetes and obesity care.
- :: Strong market position, claiming 28% of the branded diabetes treatment market.
- :: Excellent financial health with no debt and over \$2 billion in cash.
- :: Compelling upside as valuations remain attractive due to continued growth in diabetes care outside the U.S.
- :: R&D is over 13% of sales.
- :: Consistently ranks in Fortune magazine Top 100 Best Companies to Work For.

Novo Nordisk is the result of a 1989 merge between two Danish insulin production companies, founded in the early 1920s. Novo Nordisk is a global leader in insulin production, with the goal of preventing, treating, and eventually curing diabetes. The company also provides services for hemophilia and other rare bleeding disorders. Novo Nordisk is distinct in its approach to diabetes and illness management in that the company creates initiatives which support underlying habits and causes of illness, rather than just symptom management. One such initiative, Cities Changing Diabetes, is a collaboration between the company and seven large cities. The goal is to understand the driving factors behind the rise of urban diabetes, share the results, and identify and implement solutions.

Strong internal drug development enables the company to generate large amounts of cash (over \$5 billion in free cash flow) that is used to reinvest back into the business, pay dividends, and repurchase shares at attractive prices. More recently, the company has boosted their research and development efforts to diversify their business outside of diabetes care.

VALUATION AND RISKS

As of the date of this report, Novo Nordisk is trading at a discount compared to historical valuations (20% below sales and 50% below cash flow multiples) and below fair value based on scenario analysis of free cash flow growth. Novo Nordisk has a dividend yield over 3% and generates over \$5 billion in free cash flow allowing flexibility to continue raising their dividend over time. On a free cash flow basis, we expect them to grow

cash flow at 5% annually over the next decade, below its current growth rate of 20% over the previous 10 years, due to higher pricing pressure on pharmaceuticals, increased competition and high revenue concentration. Modeling our conservative estimation places a price of \$45 on shares which is almost a 28% premium based on current price. If our conservative assumption turn out to be overly optimistic, we still feel there is a margin of safety built into the current price based on the company's high returns on capital (75%) and strong cash flow generation.

Though considered the leader in the diabetes care market, Novo Nordisk operates in a highly competitive environment. Eli Lilly and Sanofi are their primary competitors. We would like to see management's continued discipline in regards to capital allocation and research and development funding. Novo Nordisk's diabetes and obesity care division accounts for roughly 80% of their revenue. Continued focus on competitive pressures within the U.S. and growth initiatives outside the U.S. will be monitored closely.

Weighing the risks and rewards, we feel the substantial discount at which Novo Nordisk currently trades offers a good long-term opportunity.

—Patrick Mason, Investment Analyst, Cairn Investment Group



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