



## **GVI Global Industrial Share Fund**

### **Stock Update 19 December 2006 – Pfizer withdrawals phase III drug**

As a result of recent events, one of our core holdings Pfizer fell over 10%. We thus thought it appropriate to communicate with advisors what we consider to be the catalysts for the fall, our current thinking and our assessment of the business going forward.

#### **Brief Background**

Pfizer is the largest pharmaceutical company in the world with a strong, diversified drug portfolio and development pipeline. It is also the second largest company in the global Healthcare sector. With no debt on its balance sheet, Pfizer is in a very strong financial position and is one of only 7 companies worldwide with a AAA rating from both S&P and Moody's.

Pfizer is well known for its expertise in cholesterol-fighting drugs. Pfizer's main cholesterol drug has been Lipitor, which has been extremely successful for the company. It represented 23% of sales for 2005. Lipitor will come off patent in 2010 and one of the challenges Pfizer faces is to replace this revenue stream.

#### **Recent events affecting Pfizer**

Pfizer's share price has declined by 10% since December 1st following the withdrawal of Torcetrapib from Phase III trials. The company also announced development of this drug will be discontinued. Torcetrapib was important for Pfizer because it had been seen as the replacement revenue stream for Lipitor when it comes off patent in 2010.

Pfizer was hoping that it would create the ultimate medication combination in the fight against cholesterol by launching Torcetrapib. Torcetrapib was designed to raise the level of good cholesterol in patients. Used in conjunction with cholesterol-lowering Lipitor, it was hoped that the launch of Torcetrapib would preserve sales of Lipitor. Unfortunately, Pfizer had to cancel the Phase III trial as the results produced unacceptable levels of negative results.

The reaction to the termination of Torcetrapib was exacerbated as it followed only a week after promising announcements made about the drug at Pfizer's Investor R&D Day. In addition, the market's main take-away from the R&D Investor Day was an undue emphasis on Torcetrapib as the only major blockbuster drug that was close to being filed with the FDA.

#### **GVI's assessment**

We originally invested in Pfizer due to its diversified drug portfolio, solid cashflow generation and compelling valuation. While the news on Torcetrapib is clearly a negative, we still believe that Pfizer's current valuation is still compelling relative to both its global pharmaceutical peers and its historical long term valuation.

Pfizer's management remains highly focused on improving shareholder returns and has so far acted in a proactive way to ensure this continues. Pfizer believes that it will be able to continue to grow its sales after 2010 when Lipitor's patent runs out.

Notwithstanding recent pipeline disappointments, the company outlined plans after their R&D Day that are designed to increase EPS in the interim. It is expected that management will:

- Accelerate its restructuring measures - the company announced in late November 2006 that it will be cutting 20%, or more than 2000 people, out of its sales force.
- Repurchase up to \$17 billion worth of shares up until 2007. This is achievable due to Pfizer's current net holding of \$13 billion in liquid assets.
- Increase the company's dividend payments by up to 20% in 2007
- Potentially buyback up to 25% of its shares, which at these valuation levels would be earnings enhancing.

Our expectations for higher dividends and buybacks are founded on the fact that we expect Pfizer to generate over \$14 billion in operating cash flow before dividends every year in the medium term. In addition, in 2007 Pfizer will receive \$13.5 billion from the sale of its consumer products division.

Pfizer is currently trading on a PE of 11.6x and a historical yield of 3.8%, and we expect this dividend yield to grow to over 4% in 2007. Pfizer's current weighting in our portfolio is 1.4% and we have been adding to our position during this period of recent share price weakness.

We believe that Pfizer is a quality company trading at very attractive prices and represents one of our core holdings. We expect it to deliver favourable returns to investors over the long term.

Kind regards,

GVI Investment Team

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