

# Celgene Corporation CELG [Nasdaq] | ★★★

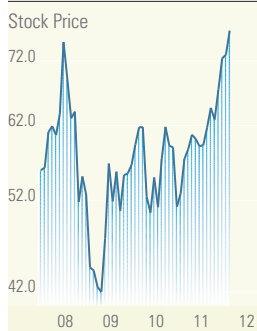
Last Price	Fair Value	Consider Buy	Consider Sell	Uncertainty	Economic Moat™	Stewardship	Morningstar Credit Rating	Industry
79.17 USD	76.00 USD	45.60 USD	117.80 USD	High	Narrow	C	A	Biotechnology

## Celgene's 2011 Performance as Expected, on Track to Meet our 2012 Forecast

by Karen Andersen, CFA  
Senior Stock Analyst  
Analysts covering this company do not own its stock.

Pricing data through April 17, 2012.  
Rating updated as of April 17, 2012.

Currency amounts expressed with "\$" are in U.S. dollars (USD) unless otherwise denoted.



### Analyst Note Jan. 26, 2012

Celgene reported full-year results that were in line with our estimates, and a 2012 forecast that largely matched our own. We're maintaining our fair value estimate. Revenue grew 34% in 2011 to reach \$4.8 billion, and once again this growth was largely attributable to blood cancer drug Revlimid (now the fifth-highest-selling cancer drug globally, sales grew 30% to \$3.2 billion in 2011). Non-GAAP EPS grew 36% to hit \$3.79, only slightly less than our \$3.83 estimate, largely due to expansion in operating income. However, Celgene did repurchase \$2.2 billion worth of shares in 2011, and we anticipate the firm could repurchase more shares in 2012, which boosts our non-GAAP EPS forecast for 2012 to \$4.89 (north of the firm's stated \$4.70-\$4.80 range). We think the firm is also on track to meet its goal of at least \$8 billion in revenue by 2015, assuming relatively steady midteens growth during the next four years.

Revlimid will remain the key driver for this growth--the recent approval in Japan, pending approval in China, and the expected expansion to the first-line setting in Europe in the first half of 2012 will all serve to continue Revlimid's growth trajectory. However, in 2012, we will also see critical data for two of Celgene's most important pipeline drugs, apremilast and pomalidomide, as well as approved chemotherapy drug Abraxane. Overall, we think Celgene's late-stage pipeline will struggle to help the firm maintain the rapid growth it has seen to date from Revlimid, and we think shares are fairly valued at recent prices.

Phase III apremilast data in psoriatic arthritis will be available midyear, and psoriasis data in the second half of the year. Because Phase II data looked weak relative to another emerging oral option in psoriasis (Pfizer's tofacitinib), we maintain a 50% probability that peak apremilast sales could surpass \$800 million. Celgene also expects to file for approval of pomalidomide as a

second-line multiple myeloma option in the U.S. and Europe in the first half. We're more enthusiastic about the potential of pomalidomide, and we now assume a 70% probability that the drug could hit \$1 billion in sales in 10 years. Abraxane could see label expansion into lung cancer this year, but we currently only peg a 50% probability of success. While we will also see data for Abraxane in 2012, we remain cautious on the drug's potential expansion into melanoma--taxanes are not a traditional therapy in this setting, and other new drugs are showing strong efficacy.

Celgene also announced that it plans to acquire private biotech Avila Therapeutics for \$350 million in cash and up to \$575 million in milestone payments tied to the success of lead candidate AVL-292 and other drug candidates based on the firm's protein silencing technology. We do not expect to include sales for AVL-292 in our model because it remains in Phase I development; however, we think this is a logical fit for Celgene, due to AVL-292's focus on hematological cancers.

### Thesis Oct. 27, 2011

Celgene is amid a global expansion led by its blood cancer drug Revlimid, and the acquisitions of Pharmion, Gloucester, and most recently Abraxis only add to the strength of its portfolio. We think Celgene still faces several competitive and regulatory risks, such as near-term competition for Vidaza and uncertainty surrounding Abraxane's growth potential. However, Revlimid's success and the potential of Celgene's growing cancer and immunoinflammatory drug pipeline give Celgene a narrow economic moat.

Celgene funded its rich pipeline with sales of Thalomid, a drug that led to thousands of birth defects when it entered the market in the 1950s. Celgene recognized the drug's value to treat the blood cancer known as multiple myeloma, and with a system in place to restrict distribution, global Thalomid sales peaked at more than \$500 million in 2008. For growth, Celgene now looks to a less toxic and more potent derivative of Thalomid, known

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Close Competitors	Currency(Mil)	Market Cap	TTM Sales	Oper Income	Net Income
<b>Celgene Corporation</b>	USD	34,741	4,842	1,443	1,318
<b>Johnson &amp; Johnson</b>	USD	176,289	65,030	16,153	9,672
<b>Pfizer Inc</b>	USD	168,160	67,425	15,241	10,009
<b>Amgen Inc</b>	USD	53,303	15,582	4,312	3,683

Morningstar data as of April 17, 2012.

as Revlimid. Revlimid received Food and Drug Administration approval for low-risk myelodysplastic syndrome at the end of 2005 and relapsed multiple myeloma in mid-2006. Revlimid sales increased to almost \$2.5 billion in 2010, a sizable portion of Celgene's \$3.6 billion top line. Although Thalomid will remain an important part of multiple myeloma therapy--particularly in Europe, where its lower price tag could boost usage--it should take a back seat to Revlimid in the long term, and we think Revlimid sales will reach almost \$5 billion by 2014.

Growth prospects in multiple myeloma are strong. Revlimid and Thalomid constitute 70% of the first-line market in the United States, with competing drug Velcade taking the lion's share of the remainder. However, we think Revlimid use will expand in Europe following approval in the first-line setting (expected in the first half of 2012). Revlimid's recent launch in Japan and data showing the benefit of longer duration of use of the drug should also drive future growth. In the long term, approval of Revlimid in leukemia, lymphoma, or solid tumors such as prostate cancer could provide additional fuel, and Phase III trials are in progress. The outlook is weaker in MDS; Revlimid has quickly penetrated the U.S. low-risk MDS market, and while Pharmion's Vidaza (approved to treat high-risk patients) has boosted growth, the drug is vulnerable to generic competition.

Beyond Revlimid, Celgene has several mid- to late-stage drug candidates in development. Oral psoriasis and psoriatic arthritis drug apremilast looks particularly

promising, and Phase III trials should produce data in 2012. Pomalidomide is also entering Phase III trials in multiple myeloma and could serve patients who fail therapies such as Velcade and Revlimid. In addition, we think Abraxane sales could easily top \$1 billion if trials in lung and pancreatic cancer lead to approvals beyond the current breast cancer indication. Overall, we're enthusiastic about prospects for a second blockbuster emerging from Celgene's pipeline.

## Valuation, Growth and Profitability

To account for cash flows earned since our last update, stronger than expected Revlimid sales, and better operating leverage following the Abraxis acquisition than we had anticipated, we're raising our fair value estimate for Celgene to \$76 per share from \$67. Overall, we think Celgene will experience average annual top-line growth of 14% and bottom-line growth of 19% during the five years ending 2016. We think Revlimid will achieve roughly \$3.8 billion in sales in 2012, and we see Celgene's total revenue reaching \$5.6 billion. We think apremilast could reach the market in 2013 and pomalidomide in 2014, and we think both could reach close to \$1 billion in sales by the end of our 10-year explicit forecast period. While U.S. sales of Vidaza should decline as the drug has lost orphan drug exclusivity, we think Vidaza sales in Europe should remain protected until 2018. Although we've accounted for Thalomid's recent approval in Europe, we expect long-term sales to be limited by Revlimid's uptake. Given Revlimid's 95% gross margin and Gilead Sciences' GILD success with its small-molecule drugs, we see 40%-plus operating margins in Celgene's future. We assume an 11% cost of equity for Celgene.

## Risk

Most of the risk surrounding Celgene ties to its reliance on Thalomid and next-generation drug Revlimid in multiple

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myeloma and the potential for heavier branded competition and earlier generic competition than we currently anticipate. Although Celgene maintains a patented compliance and patient education program, generic firms could find a way to bypass Thalomid's formulation patents, and the lower cost of a generic Thalomid would mute sales of both Thalomid and Revlimid. Revlimid patents were also recently challenged by Indian generic firm Natco, which could lead to the introduction of generic Revlimid earlier than 2019. Celgene may struggle to obtain reimbursement for Revlimid as a first-line multiple myeloma therapy in many international markets, given the drug's high price tag relative to Thalomid. Takeda and Millennium's Velcade is also a popular, more affordable option in multiple myeloma, and this drug--as well as drugs poised to enter the market such as Onyx's carfilzomib--could limit Revlimid's growth potential. While some Abraxane patents extend until 2023, composition of matter and method of use patents on Abraxane begin to expire in 2013, opening the door for generic challenges.

## Bulls Say

- Revlimid continues to generate impressive data in approved and potential new indications, and growth should be bolstered by expanded duration of use and geographic reach.
- Celgene has made two sizable purchases that contribute to its positive moat trend. The acquisition of Pharmion further solidified Celgene's strategic focus on blood-related cancer therapies, and the more recent Abraxis acquisition moves the firm into the broader oncology market.
- While its size limits the number of potential suitors, Celgene's strong growth and profitability could make it an attractive takeout target for large pharmaceutical or biotech firms looking to expand their oncology product portfolios.

- Celgene has a strong pipeline of immunology-focused drug candidates, led by late-stage oral drug candidate apremilast for psoriasis and arthritis.

## Bears Say

- Revlimid's safety profile is still being elucidated, and the drug requires a restricted distribution program similar to Thalomid's STEPS program.
- Competition in the multiple myeloma market is getting stronger; Velcade has produced outstanding trial results and is vying with Revlimid in the first-line setting, and Onyx's carfilzomib could serve as an approved second-line option as early as 2012.
- Revlimid sales cannibalize sales of Thalomid, stunting initial sales growth in the multiple myeloma market.
- Launched at \$54,000 a year to treat MDS and \$74,000 per year to treat multiple myeloma in the U.S., the cost of Revlimid fuels legislator and health insurer debates regarding cancer drug pricing.
- Indian generic firm Natco's challenge to Celgene's Revlimid patents could mean generic competition before 2019 (the expiration of the drug's basic composition patent).

## Financial Overview

Financial Health: Celgene had \$2.6 billion in cash at the end of the third quarter of 2011, against \$1.25 billion in senior notes. With free cash flow of more than \$1 billion annually, Celgene has plenty of cash for share repurchases and additional in-licensing and acquisition activity.

## Company Overview

Profile: Celgene is a biopharmaceutical firm that discovers, develops, and markets therapeutics for the treatment of cancer and immunological diseases. Celgene

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Management: Longtime president and COO Sol Barer replaced John Jackson as CEO and chairman in 2006. Barer's \$3.7 million in 2009 cash compensation strikes us as reasonable, given the significant growth that the firm has seen in recent years. However, Barer pocketed almost \$100 million in 2008-09 by exercising deep-in-the-money options and selling his shares, and we were concerned to see his ownership dip below 1%. Barer stepped down as CEO in 2010 but retains his position as board chairman. Robert Hugin, previously Celgene's CFO (and subsequently COO), took over the CEO position. We're disappointed by the composition of the board; eight of Celgene's 10 directors are considered independent, but two of them have been on the board for more than 10 years, which casts doubt on their true level of independence. On the basis of these factors, we think Celgene warrants a Stewardship Grade of C. That said, we applaud the recent addition of Pharmacia and Schering-Plough veteran Carrie Cox to the board and the recent separation of the chairman and CEO roles.

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Oct. 27, 2011

### Raising our Celgene Fair Value Following 3Q on Revlimid Sales Visibility and Operating Leverage

We're raising our fair value estimate for Celgene following a positive regulatory outlook for Revlimid in Europe and other international markets going into 2012, as well as

strong operating leverage despite multiple large-scale clinical trials and the integration of Abraxis. Revlimid sales grew 28% in the quarter to reach \$820 million and the drug

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## Analyst Notes (continued)

continues to see growth on three fronts: geographic expansion, market share gains, and longer duration of therapy. Outside the United States, the launch in Japan helped Revlimid grow despite falling prices and austerity measures in Europe. Now that the safety review of Revlimid in Europe is complete, we expect Revlimid could receive approval in Europe in first-line multiple myeloma in early 2012, which will provide an important growth driver as off-label use in this indication is much less prevalent in Europe than in the U.S. International sales will also start to benefit from potential Revlimid launches in markets such as Russia and China in late 2012. As Phase III trials continue for Revlimid in several other indications including leukemia, lymphoma, and prostate cancer, we think the drug is poised to achieve peak global sales of \$7 billion in 2019.

Given Revlimid's faster than anticipated growth and the

lack of generic competition to Vidaza in the U.S. to date, management has increased its guidance once again. We now think non-generally accepted accounting principles EPS is on track to hit \$3.83 per share in 2011, slightly above management's new guidance of \$3.78 to \$3.80. Operating expenses are significantly higher than last year's comparables, mostly due to the Abraxis acquisition and a ramp up in the number of late-stage clinical trials that Celgene is conducting. However, they remain below our expectations, as the Abraxane salesforce appears to be integrating nicely. We see several potential catalysts outside of Revlimid that contribute to Celgene's positive moat trend, including advancement of pomalidomide in relapsed multiple myeloma, as well as Phase III drug candidate apremilast in psoriasis and rheumatoid arthritis (which should yield data beginning mid-2012).

## Disclaimers & Disclosures

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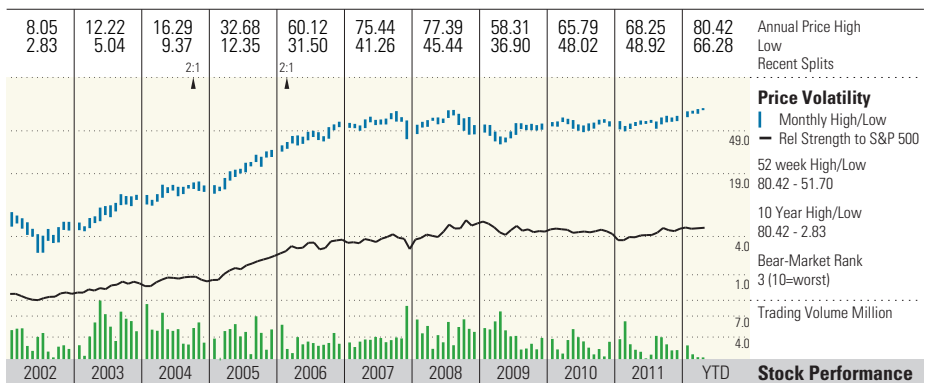
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**Sales USD Mil** 4,842 **Mkt Cap USD Mil** 34,741 **Industry** Biotechnology **Sector** Healthcare

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per share prices in USD



Growth Rates Compound Annual					
Grade: A	1 Yr	3 Yr	5 Yr	10 Yr	
Revenue %	33.5	29.0	40.0	45.5	
Operating Income %	45.8	—	52.5	—	
Earnings/Share %	51.6	—	73.8	—	
Dividends %	—	—	—	—	
Book Value/Share %	-0.9	18.3	17.6	28.5	
Stock Total Return %	38.9	27.4	6.7	28.8	
+/- Industry	24.7	11.3	3.0	24.4	
+/- Market	33.5	10.5	7.8	26.7	

Profitability Analysis				
Grade: B	Current	5 Yr Avg	Ind	Mkt
Return on Equity %	22.9	4.1	-20.5	22.6
Return on Assets %	13.1	1.9	-12.2	9.4
Fixed Asset Turns	9.5	9.3	3.6	7.5
Inventory Turns	1.9	2.5	1.5	16.6
Revenue/Employee USD K1085.7	969.6*	—	1040.0	
Gross Margin %	91.2	90.8	84.5	39.9
Operating Margin %	29.8	10.7	24.0	16.7
Net Margin %	27.2	5.7	-36.7	11.2
Free Cash Flow/Rev %	34.6	25.8	-17.1	0.1
R&D/Rev %	33.0	0.3	—	9.4

Financial Position		
Grade: A	12-10 USD Mil	12-11 USD Mil
Cash	1351	1859
Inventories	260	190
Receivables	706	946
Current Assets	4343	4353
Fixed Assets	510	506
Intangibles	5145	4732
Total Assets	10177	10006
Payables	106	152
Short-Term Debt	—	527
Current Liabilities	1070	1540
Long-Term Debt	1248	1276
Total Liabilities	4193	4493
Total Equity	5984	5513

Valuation Analysis				
	Current	5 Yr Avg	Ind	Mkt
Price/Earnings	27.8	—	—	15.4
Forward P/E	13.8	—	—	13.5
Price/Cash Flow	20.2	49.3	—	7.3
Price/Free Cash Flow	21.8	—	—	17.6
Dividend Yield %	—	—	0.3	2.0
Price/Book	6.3	5.9	2.2	2.0
Price/Sales	7.6	9.8	5.3	1.2
PEG Ratio	0.6	—	—	1.9

2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	YTD	Stock Performance
-32.7	109.0	18.2	144.3	77.6	-19.7	19.6	0.7	6.2	14.3	17.1	Total Return %
-9.3	82.6	9.2	141.3	64.0	-23.2	58.1	-22.7	-6.6	14.3	6.5	+/- Market
6.2	71.8	5.6	132.9	76.2	-15.3	26.8	-5.8	2.3	4.5	4.7	+/- Industry
—	—	—	—	—	—	—	—	—	—	0.0	Dividend Yield %
1690	3646	4366	10991	20276	17831	25329	25573	27819	30010	34741	Market Cap USD Mil

2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	TTM	Financials
136	271	378	537	899	1406	2255	2690	3626	4842	4842	Revenue USD Mil
87.2	81.9	84.2	85.0	86.0	90.7	88.5	92.0	91.5	91.2	91.2	Gross Margin %
-124	-3	43	84	175	425	-1464	842	990	1443	1443	Oper Income USD Mil
-91.4	-1.0	11.3	15.6	19.4	30.2	-64.9	31.3	27.3	29.8	29.8	Operating Margin %
-100	14	53	64	69	226	-1534	777	881	1318	1318	Net Income USD Mil
-0.32	0.04	0.16	0.18	0.18	0.54	-3.46	1.66	1.88	2.85	2.85	Earnings Per Share USD
—	—	—	—	—	—	—	—	—	—	—	Dividends USD
309	342	346	354	407	432	443	467	470	463	463	Shares Mil
0.88	0.95	1.45	1.87	5.61	7.37	7.62	9.57	12.72	12.42	12.56	Book Value Per Share USD
-38	19	156	42	84	478	182	910	1182	1809	1809	Oper Cash Flow USD Mil
-11	-11	-36	-36	-59	-64	-77	-93	-99	-132	-132	Cap Spending USD Mil
-49	8	120	6	25	413	105	816	1083	1677	1677	Free Cash Flow USD Mil

2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	TTM	Profitability
-29.4	2.4	5.6	5.4	3.5	7.1	-38.1	15.8	11.3	13.1	13.1	Return on Assets %
-34.1	4.6	13.4	11.4	5.3	9.4	-48.4	19.7	17.0	22.9	22.9	Return on Equity %
-73.7	5.0	14.0	11.9	7.7	16.1	-68.0	28.9	24.3	27.2	27.2	Net Margin %
0.40	0.49	0.40	0.46	0.45	0.44	0.56	0.55	0.47	0.48	0.48	Asset Turnover
1.2	2.5	2.3	2.0	1.4	1.3	1.3	1.2	1.7	1.8	1.8	Financial Leverage

2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	12-11	Financial Health
252	658	708	837	2071	2651	2314	3350	3273	2813	2813	Working Capital USD Mil
—	400	400	400	422	23	—	—	1248	1276	1276	Long-Term Debt USD Mil
277	310	477	636	1976	2844	3491	4395	5984	5513	5513	Total Equity USD Mil
0.00	1.29	0.84	0.63	0.21	0.01	—	—	0.21	0.23	0.23	Debt/Equity

2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	TTM	Valuation
—	—	85.5	—	—	85.5	—	33.6	31.4	23.7	27.8	Price/Earnings
—	—	—	—	—	—	—	—	—	1.3	1.8	P/E vs. Market
12.2	14.1	12.1	21.0	23.1	14.2	10.9	9.7	7.7	6.5	7.6	Price/Sales
6.1	11.8	9.1	17.3	10.3	6.3	7.3	5.8	4.7	5.4	6.3	Price/Book
—	—	29.4	—	—	41.8	135.1	28.6	23.5	17.5	20.2	Price/Cash Flow

Quarterly Results						
Revenue USD Mil	Mar 11	Jun 11	Sep 11	Dec 11		
Most Recent Period	1125.3	1183.2	1249.7	1283.9		
Prior Year Period	791.3	852.7	910.1	1071.7		
Rev Growth %	Mar 11	Jun 11	Sep 11	Dec 11		
Most Recent Period	42.2	38.8	37.3	19.8		
Prior Year Period	30.8	35.6	30.9	40.8		
Earnings Per Share USD	Mar 11	Jun 11	Sep 11	Dec 11		
Most Recent Period	0.54	0.59	0.81	0.91		
Prior Year Period	0.50	0.33	0.60	0.44		

Industry Peers by Market Cap				
	Mkt Cap USD Mil	Rev USD Mil	P/E	ROE%
Celgene Corporation	34741	4842	27.8	22.9
Johnson & Johnson	176289	65030	18.4	17.0
Pfizer Inc	168160	67425	20.1	11.8

Major Fund Holders		% of shares
		—
		—
		—

\*3Yr Avg data is displayed in place of 5Yr Avg TTM data based on rolling quarterly data if available; otherwise most recent annual data shown.  
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## Morningstar's Approach to Rating Stocks

### Our Key Investing Concepts

- ▶ Economic Moat™ Rating
- ▶ Discounted Cash Flow
- ▶ Discount Rate
- ▶ Fair Value
- ▶ Uncertainty
- ▶ Margin of Safety
- ▶ Consider Buying/Consider Selling
- ▶ Stewardship Grades

At Morningstar, we evaluate stocks as pieces of a business, not as pieces of paper. We think that purchasing shares of superior businesses at discounts to their intrinsic value and allowing them to compound their value over long periods of time is the surest way to create wealth in the stock market.

We rate stocks 1 through 5 stars, with 5 the best and 1 the worst. Our star rating is based on our analyst's estimate of how much a company's business is worth per share. Our analysts arrive at this "fair value estimate" by forecasting how much excess cash--or "free cash flow"--the firm will generate in the future, and then adjusting the total for timing and risk. Cash generated next year is worth more than cash generated several years down the road, and cash from a stable and consistently profitable business is worth more than cash from a cyclical or unsteady business.

Stocks trading at meaningful discounts to our fair value estimates will receive high star ratings. For high-quality businesses, we require a smaller discount than for mediocre ones, for a simple reason: We have more confidence in our cash-flow forecasts for strong companies, and thus in our value estimates. If a stock's market price is significantly above our fair value estimate, it will receive a low star rating, no matter how wonderful we think the business is. Even the best company is a bad deal if an investor overpays for its shares.

Our fair value estimates don't change very often, but market prices do. So, a stock may gain or lose stars based

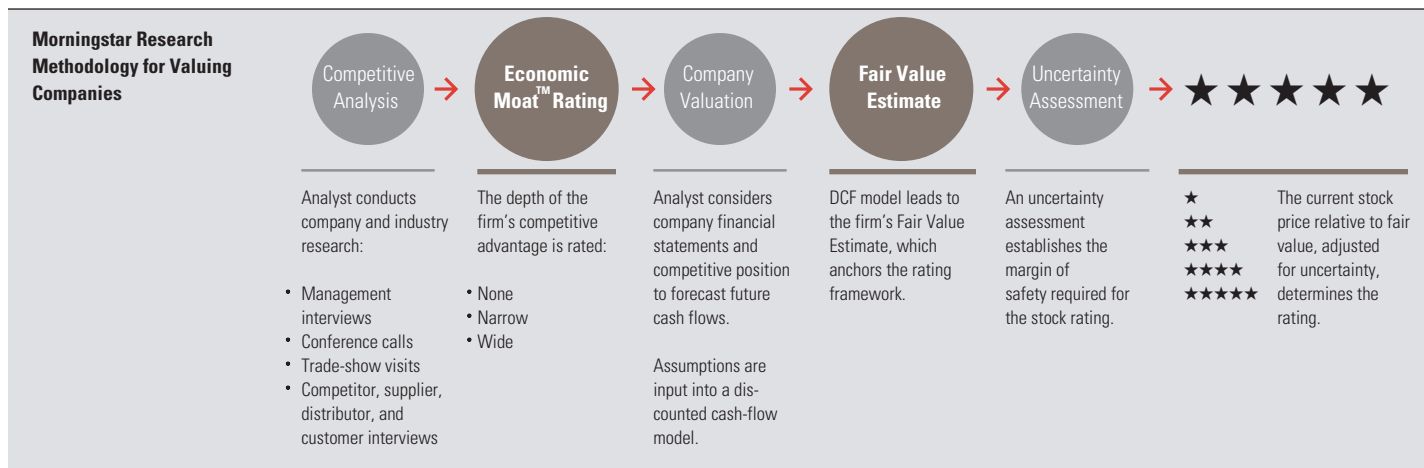
just on movement in the share price. If we think a stock's fair value is \$50, and the shares decline to \$40 without much change in the value of the business, the star rating will go up. Our estimate of what the business is worth hasn't changed, but the shares are more attractive as an investment at \$40 than they were at \$50.

Because we focus on the long-term value of businesses, rather than short-term movements in stock prices, at times we may appear out of step with the overall stock market. When stocks are high, relatively few will receive our highest rating of 5 stars. But when the market tumbles, many more will likely garner 5 stars. Although you might expect to see more 5-star stocks as the market rises, we find assets more attractive when they're cheap.

We calculate our star ratings nightly after the markets close, and issue them the following business day, which is why the rating date on our reports will always be the previous business day. We update the text of our reports as new information becomes available, usually about once or twice per quarter. That is why you'll see two dates on every Morningstar stock report. Of course, we monitor market events and all of our stocks every business day, so our ratings always reflect our analyst's current opinion.

### Economic Moat™ Rating

The Economic Moat™ Rating is our assessment of a firm's ability to earn returns consistently above its cost of capital in the future, usually by virtue of some competitive advantage. Competition tends to drive down such





## Morningstar's Approach to Rating Stocks (continued)

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economic profits, but companies that can earn them for an extended time by creating a competitive advantage possess an Economic Moat. We see these companies as superior investments.

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### Discounted Cash Flow

This is a method for valuing companies that involves projecting the amount of cash a business will generate in the future, subtracting the amount of cash that the company will need to reinvest in its business, and using the result to calculate the worth of the firm. We use this technique to value nearly all of the companies we cover.

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### Discount Rate

We use this number to adjust the value of our forecasted cash flows for the risk that they may not materialize. For a profitable company in a steady line of business, we'll use a lower discount rate, also known as "cost of capital," than for a firm in a cyclical business with fierce competition, since there's less risk clouding the firm's future.

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### Fair Value

This is the output of our discounted cash-flow valuation models, and is our per-share estimate of a company's intrinsic worth. We adjust our fair values for off-balance sheet liabilities or assets that a firm might have--for example, we deduct from a company's fair value if it has issued a lot of stock options or has an under-funded pension plan. Our fair value estimate differs from a "target price" in two ways. First, it's an estimate of what the business is worth, whereas a price target typically reflects what other investors may pay for the stock. Second, it's a long-term estimate, whereas price targets generally focus on the next two to 12 months.

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### Uncertainty

To generate the Morningstar Uncertainty Rating, analysts consider factors such as sales predictability, operating leverage, and financial leverage. Analysts then classify their ability to bound the fair value estimate for the stock into one of several uncertainty levels: Low, Medium, High,

Very High, or Extreme. The greater the level of uncertainty, the greater the discount to fair value required before a stock can earn 5 stars, and the greater the premium to fair value before a stock earns a 1-star rating.

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### Margin of Safety

This is the discount to fair value we would require before recommending a stock. We think it's always prudent to buy stocks for less than they're worth. The margin of safety is like an insurance policy that protects investors from bad news or overly optimistic fair value estimates. We require larger margins of safety for less predictable stocks, and smaller margins of safety for more predictable stocks.

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### Consider Buying/Consider Selling

The consider buying price is the price at which a stock would be rated 5 stars, and thus the point at which we would consider the stock an extremely attractive purchase. Conversely, consider selling is the price at which a stock would have a 1 star rating, at which point we'd consider the stock overvalued, with low expected returns relative to its risk.

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### Stewardship Grades

We evaluate the commitment to shareholders demonstrated by each firm's board and management team by assessing transparency, shareholder friendliness, incentives, and ownership. We aim to identify firms that provide investors with insufficient or potentially misleading financial information, seek to limit the power of minority shareholders, allow management to abuse its position, or which have management incentives that are not aligned with the interests of long-term shareholders. The grades are assigned on an absolute scale--not relative to peers--and can be interpreted as follows: A means "Excellent," B means "Good," C means "Fair," D means "Poor," and F means "Very Poor."

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