

## Galapagos (Buy from Hold) - Valuation update following corona pandemic (EUR 174.45 / TP EUR 215 from EUR 185)

### Facts – Stock hit hard by Covid-19

The coronavirus pandemic outbreak led to a massive sell off in financial markets. The healthcare industry was not spared from the hit, leading to substantial stock price declines, from small caps all the way to big pharma companies.

Prior to this correction, we communicated on Galapagos' share price having surged massively over the preceding 4 months. This occurred in absence of news that would have substantially affected valuation, in our view. The latter resulted in a peak share price of approximately EUR 250 in February.

As massive as the surge was, so was the hit the stock took following the pandemic outbreak, being pushed down to levels as low as EUR 134, implying a value loss of more than EUR 7bn.

We took the liberty to assess the company's challenges, risks and strengths in view of the current uncertain, volatile period and performed a valuation update.

### Our view - Galapagos' risks are industry-specific, its strengths are company-specific

As for all biotech comps, Galapagos' risk profile is mainly driven by the intrinsic risk of technical failure of its clinical assets, which we factor in our valuation by the attribution of success rates. Following the outbreak, the healthcare industry faces additional challenges, particularly clinical trial delays. Galapagos recently communicated on pausing enrollment of several filgotinib trials, including the Phase III trials in Crohn's disease (CD), psoriatic arthritis (PsA) and ankylosing spondylitis (AS). The extent of these delays is hard to predict at this point.

A unique strength of Galapagos is its blockbuster clinical asset filgotinib, which is currently in the registration phase for rheumatoid arthritis (RA) and set to start generating operational revenues in the near future. In addition, the Phase III readout in ulcerative colitis (UC) remains on schedule for 2Q20, which could imply a first label extension in 2021. In our view, filgotinib holds best-in-class potential for RA, UC, CD, PsA and AS. In this regard, we lowered our WACC for these programs from 12% to 10%, which is in line with industry peers.

Last but not least, a key - if not the most crucial - strength of the company is its extremely solid cash position (EUR 5.8bn YE19). Not only does this allow intensifying (pre)clinical R&D efforts, it also eliminates the risk of potential financial distress in the near future, which could arise for other biotechs given that fundraising might prove to be very challenging during this period.

## Investment conclusion - An overstated correction providing a viable entry point

In our view, the aforementioned strengths of the company outweigh its risks. Although the stock price surged towards illogical levels in February - leading to our downgrade in January - we believe the correction the company received has been overstated and now offers a viable entry point. Based on our updated input assumptions, we arrive at a TP of EUR 215 and therefore upgrade to a Buy rating. We await further clinical updates on the Phase III trial in UC in 2Q20, Phase II trials in idiopathic pulmonary fibrosis (IPF), systemic sclerosis (SSc) and osteoarthritis (OA) in 2H20 and the regulatory filing for filgotinib in RA in 2H20.

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