

**GlaxoSmithKline**  
**Accelerating our IPT strategy**  
**Wednesday, 19 December 2018**  
**Analyst Conference Call**

**Sarah Elton-Farr (Head of Investor Relations):** Good morning, everyone. Thank you for joining us to discuss our announcement today. You should have received our press release and can view the presentation, which is located on the investor section of the GSK website.

**Information regarding forward-looking statements and non IFRS measures**

Before we begin, please refer to slide two of our presentation for our cautionary statements.

**Agenda**

Our speakers today are Chief Executive Officer, Emma Walmsley; Brian McNamara, CEO of our Consumer business; and Simon Dingemans, Chief Financial Officer.

Following our presentation we will open the call to questions and answers. We request that you ask only a maximum of two questions so that everyone has a chance to participate, and with that, I will hand the call over to Emma.

**3 long-term priorities for sustainable growth**

**Emma Walmsley:** Thank you, Sarah, and thank you, everyone, for joining us on what is a landmark day for GSK.

When I became CEO last year I set out a new capital allocation framework and three long-term priorities for the business: innovation, performance, and trust.

These three priorities are designed to improve the competitive performance of our three global businesses and deliver long-term sustainable growth.

**Platform for improved operating performance and reshaped portfolio**

Since then we have taken a clear set of actions to improve our operating performance and to reshape the group's portfolio.

We have put in place new leadership, and have set about building a culture with a sharper focus on performance, setting new expectations for our people, while staying true to our values and purpose.

We have put a clear focus on launch execution, and have had considerable success, most notably with *Shingrix*, our new shingles vaccine.

Our clear priority is to improve Pharma performance, and under new leadership we have been restructuring to focus our Pharma business in both manufacturing and commercial operations.

Finally, last July Hal laid out our new R&D approach, with a focus on science related to the immune system, the use of genetics and advanced technologies all to strengthen our pipeline for our next wave of growth.

We have also made significant progress in reshaping our portfolio. Our first priority was R&D prioritisation, and here we have terminated or divested around 80 programmes to invest more behind the potential medicines we see bringing greater value to patients and stronger growth for GSK.

We have stepped up business development, be it in partnerships with 23andMe, or with the recently announced transaction with TESARO.

We have successfully bought out the Novartis stake in our Consumer Healthcare joint venture, and, finally, we have made non-core asset divestments, such as the recently announced divestment of *Horlicks* to Unilever.

Today's announcement means we can accelerate this work again, as it both supports further improvements to operating performance, and lays out a clear pathway to reshape the group over the medium term in a way that benefits shareholders, patients and consumers.

### **Creation of a new world-leading Consumer Healthcare Joint Venture**

The key details from today's proposed transaction are summarised here. This will be an all-equity transaction with GSK having a controlling equity interest of 68%, and Pfizer 32%.

The new joint venture would have combined sales of approximately £9.8 billion (\$12.7 billion), with cost synergy opportunity of £0.5 billion.

We expect the transaction to be accretive to total earnings in the second full year following completion, and to adjusted earnings and free cashflow in the first full year after completion.

This proposed transaction is transformational to the scale of GSK's Consumer Healthcare business, and within three years of the closing of the transaction GSK intends to separate the joint venture via a de-merger.

Over this period, GSK will substantially complete the integration and expect to make continued progress in strengthening its Pharma business in R&D pipeline.

This separation will enable the two resulting companies – one focused on Pharma/Vaccines, and the other Consumer Healthcare, to pursue their own long-term strategic and capital allocation priorities appropriate for delivering on their future growth potential.

The transaction and intended separation further strengthens our long-term outlook and cashflows, and as a consequence, we have announced we expect to pay a dividend of 80p in 2019 and going forward, with improvements in both businesses, we expect to be well-positioned to deliver returns to shareholders alongside continued investment in our strategic priorities.

### **Improved performance and increased value for shareholders**

The proposed transaction is a unique opportunity to create a new world leader in Consumer Healthcare with a partner we know and in a model we have successfully executed before. The new joint venture would be driven by category-leading power brands and science-based innovation and we shall have leadership positions in key categories and key geographies. There is significant opportunity for growth and to take cost synergies.

As I said, the new joint venture's transformation in scale within the Consumer Health sector and within GSK is also a key consideration in our announced intention to separate the business. The separation will allow the new company to pursue its own growth opportunities independently and it will provide both GSK shareholders and future investors with a new global equity investment in the attractive Consumer Health market.

### **Supports our priority of strengthening Pharma**

I have stated very clearly that strengthening GSK's Pharma business and pipeline is our clear priority and in evaluating this transaction, it was essential that it would support and strengthen this effort which it does. The Consumer JV's cashflow and visibility of the intended separation will help support GSK's future capital planning and the capacity for investment we want to make in our Pharma pipeline over the next few years with the R&D approach that Hal laid out at Q2. This means maximising opportunities such as BCMA and, of course, investing in new ones like the assets we acquired through our recent proposed acquisition of TESARO, as well as continuing to invest in the competitive delivery of our HIV,

Respiratory and Vaccines execution and new launches. The intended separation means we shall have more flexibility to accelerate our long-term ambitions for the Pharma/Vaccines business and to do so while also delivering returns to shareholders.

### **Clear pathway for creation of two new UK-based global companies**

The proposed transaction lays out a clear pathway for the Group over the next few years. It is a pathway that is consistent with our stated strategy and, with effective execution, I am confident that we can strengthen our Pharma pipeline and business and deliver a very successful integration for the Consumer business. In doing so, we shall prepare these businesses for separation, ultimately to create two exceptional and exciting UK-based global companies with the appropriate capital structures. A new global Pharma and Vaccines company with an R&D approach focused on the science of the immune system, the use of genetics and advanced technologies, and a new world-leading Consumer Healthcare company, powered by category-leading brands and science-based innovation. At the same time, we shall concentrate on delivering further improvements to our current operating performance and delivering returns for our shareholders.

Let me now hand you over to Brian who was my partner when we successfully created the joint venture with Novartis, and I am truly delighted that he will be leading this next major opportunity for GSK's Consumer Healthcare business.

**Brian McNamara (CEO, GSK Consumer Healthcare):** Thanks, Emma. It is great to be talking to you all today about the opportunity to create an even stronger, world-leading Consumer Healthcare business.

### **Positive Consumer Healthcare industry trends**

As a reminder, Consumer Healthcare is a great business to be in. It is very clear that the trends are in our favour, with people taking more control of their own health, with an aging population and a growing emerging middle-class. There is still a lot of opportunity to drive growth by innovating and delivering on unmet consumer needs.

### **Creation of a global leader in Consumer Healthcare**

The combination of GSK Consumer Healthcare and Pfizer Consumer Healthcare brings together two highly complementary portfolios into a world-leading company with significant scale. Annual sales will be about £9.8 billion. The combined business will be the No.1 global player in OTC with leadership positions in pain relief, respiratory, and vitamins, minerals and supplements (VMS), and still with a No.1 position in therapeutic oral health.

We shall have a strong geographic footprint, being No.1 in the US and No.2 in China, the two largest OTC markets worldwide, and with a strong overall presence in Emerging Markets. We have a proven integration capability and we have the opportunity to create significant scale and significant value delivering £0.5 billion in synergies by 2022.

### **Pfizer has a strong portfolio of category leading brands**

Looking at the Pfizer portfolio, they have strong brands and leadership positions like Advil which is the number one pain reliever globally including the number one position in the US, which is the largest pain relief market in the world.

They have a strong portfolio of vitamins, minerals and supplements with brands like Centrum, Caltrate and Emergen-C. Importantly they have a concentrated portfolio with top ten brands accounting for 80% of the business. This focussed portfolio fits well with our power brand strategy.

### **Category leading positions of combined portfolio**

Importantly, the portfolios are complementary with leadership positions in key categories, and adding a global leadership position in VMS which is the largest OTC category with some very fast-growing sub-segments. And of course we continue to have our strong position in therapeutic oral health behind brands like *Sensodyne* and *Paradontax*.

### **Creates OTC leadership positions in key geographies**

Additionally, it gives us a very strong leadership position in key geographies. As I said earlier, we will be in No. 1 position in the US and No. 2 position in China, the two largest OTC markets in the world, and the No. 2 position in key emerging markets across Latin America and Central and Eastern Europe and number one position in Middle East and Africa.

### **Proven integration capability through GSK-Novartis joint venture**

So we have a great portfolio and a strong geographic footprint. The key is to integrate with excellence while continuing to deliver on our performance objectives.

One thing that builds our confidence is our successful integration of the Novartis transaction. We over-delivered on cost synergies and delivered significant operating margin improvement while continuing to deliver strong top line growth.

Importantly, while we were integrating we didn't just deliver the synergies. We also created a scalable model and brought in talent from both companies to improve our capabilities and accelerate our performance-driven culture.

## **Leverage strengths of both companies to deliver sustained profitable growth**

It will be equally important to do the same during this integration and I believe both companies bring strong talent and capabilities to the table. Let me take you through a few examples.

On innovation, at GSK we have a capability in external innovation that can be leveraged, leading to approximately 30% of our pipeline being sourced from external partnerships. Both companies have a strong record of scientific excellence and delivery. The two largest OTC switches in the last few years were Pfizer's *Nexium* and GSK's *Flonase*.

On performance there are a number of areas we can leverage. One is around digital capabilities. For example, GSK has a direct tech stack deal with Google which allows us to drive efficiencies and effectiveness in our digital marketing. Pfizer has a very strong ecommerce business in China, one of the fastest-growing ecommerce markets in the world.

In addition to digital capabilities, both companies have strong sales forces in retail partnerships and of course Pfizer has an expertise in VMS both on innovation and marketing that has not been a focus for GSK.

On trust, both companies have a strong focus on quality and compliance and both have a track record of delivering supply chain efficiencies and a focus on customer service.

## **Deliver an industry leading margin**

This transaction offers a significant value creation opportunity. Post the Novartis buy-out we guided that we were targeting an operating margin for GSK's Consumer business of approaching mid-20s percentage by 2022 at 2017 constant exchange rates and we have a clear plan to deliver on that commitment.

In addition, we are now targeting to deliver £0.5 billion of cost synergies behind this transaction. We expect to reinvest up to 25% of this amount into our business to support innovation, brand development and drive our top line taking us to a percentage operating margin for the new JV of mid to high 20s by 2022.

It's worth noting we did not include any revenue synergies in our plans. Given our track record, I am confident we can deliver on this.

Now I will hand it over to Simon and he will talk you through the details.

**Simon Dingemans (Chief Financial Officer):** Thank you, Brian. I'll run through the headline details of the transaction before going into more detail on some of the key areas.

### **Proposed transaction: financial details**

Today we've entered into an agreement under which Pfizer will contribute their Consumer Healthcare business to GSK's existing Consumer Healthcare operations in return for an equity share in the combined entity. This will create a new global joint venture which GSK will control with a 68% equity interest. Pfizer will have a 32% stake.

GSK is contributing all of its Consumer Healthcare businesses, including its retained OTC brands in India. Horlicks and the other businesses recently agreed to be sold to Unilever are outside the scope of the joint venture, as is our stake in our quoted Nigerian consumer company.

The terms of the equity split reflect the relative profit contributions made by each party to the new entity, plus a premium to Pfizer, recognising our control of the new joint venture. The level of premium is in line with other all-equity transactions. Both businesses will be contributed to the joint venture cash-free and debt-free, bar a small cash balance for working capital. The new joint venture will stay debt-free until the point of separation.

The proposed transaction is subject to approval by shareholders, as Pfizer is treated as a related party under the UK listing rules. We will post a circular to shareholders seeking their approval during Q1 2019. The board of GSK intends to recommend that shareholders vote in favour of the proposed transaction. The transaction is also conditional upon the receipt of certain Antitrust Authority approvals and subject to these, the transaction is expected to complete in the second half of 2019.

Until separation, the joint venture will be consolidated in GSK's financial statements, and free cashflow from the new entity will be distributed to both shareholders on a regular basis, so that we each have ready access to our respective share of the JV's cashflows.

As Brian mentioned, the proposed transaction is expected to realise substantial cost synergies, around £0.5 billion annually by 2022, and we expect a percentage adjusted operating margin for the new joint venture in the mid to high 20s at 2017 constant exchange rates by 2022. I will talk more about the phasing of the synergies in a minute.

We expect the proposed transaction to be accretive to total earnings in the second full year following completion, reflecting the upfront timing of the costs of integration and restructuring, but importantly, to be accretive to adjusted earnings and free cashflow in the first full year after completion.

On the dividend, we remain committed to our current dividend policy and continue to expect to pay 80p per share in dividends for 2018. We have also announced we expect to pay 80p in 2019. The transaction is expected to be cashflow accretive and build on the strengthening of cashflows that we have been delivering over the last couple of years.

Going forward, the proposed transaction enhances prospects for the Consumer Healthcare business and supports the development of GSK's Pharmaceutical and Vaccines business. With expected improvements in both businesses, GSK expects to be well-positioned to deliver returns to shareholders alongside continued investment in our strategic priorities.

### **Significant cost synergy potential for the JV, with cash restructuring costs offset by divestments**

Turning to the synergies, the proposed transaction is expected to realise substantial cost synergies, with the joint venture expected to generate total annual cost savings of approximately £0.5 billion by 2022. The expected costs to deliver these synergies are cash costs of £0.9 billion, and £0.3 billion of non-cash costs. We will be driving synergies from across the combined footprint, using our experience from the Novartis transaction to plan our execution and mitigate delivery risk. We have a particular focus on streamlining the supply chain, but also overlapping commercial infrastructure. In addition, we see considerable opportunity in procurement, logistics, media spend and marketing costs, aided by our increasing digital focus over the last couple of years.

We plan to re-invest up to 25% of the cost savings back into the business to support innovation, brand development and other growth opportunities, subject to delivering appropriate returns.

As we expect this transaction to close in the second half of 2019, we currently don't expect much contribution from synergies in 2019, but we expect to be able to realise around 40% of the total in 2020, rising to around 80% in 2021, as we get to the later stages of the synergy programme, including rationalisation of manufacturing sites, and we expect to achieve the full amount in 2022.

Consistent with the delivery on Novartis, costs of the transaction will be more upfront, with around £0.2 billion of cash costs in 2019 and half a billion in 2020. The cash outflow of the integration costs will be offset by the proceeds of disposals we are planning to further focus the combined portfolio, and we are aiming to raise about £1 billion pounds of net proceeds over 2019 and 2020.

## **Key financials**

On the financials, we set out for you the relative contributions of GSK and Pfizer to the joint venture in terms of sales and operating profit. Pfizer contributions have not been formally restated into IFRS, but we are not expecting significant differences so we think this gives you a reasonable comparison between the two businesses. The results for Pfizer in 2017 were impacted by Hurricane Maria, and we estimate that the operating profit drag was around \$50 million. Without this, Pfizer's adjusted operating margin would have been closer to 19%.

The relative margin particularly reflects the higher US contribution in the Pfizer business and the scale of their US consumer operations will increase the weighting to the US for the new joint venture. The JV overall will have a more balanced geographic distribution of revenues as shown on the right. With the synergies we expect to achieve and after any reinvestments, we expect combined business to take its adjusted operating margin into the mid to high 20s in percentage terms by 2022.

## **Path to separation**

This transaction presents a clear and visible pathway forward to the creation of two new leading global companies, once the integration is complete, and we have made further progress with our R&D pipeline. Each will have its own independent balance sheet and capital structure, better able to support the different investment requirements of those businesses alongside continued distribution to shareholders. This will allow greater financial flexibility when it comes to capital planning for the future, as each business invests for growth and delivery of long-term shareholder returns.

We will position the new Consumer Healthcare business at separation with an investment grade balance sheet appropriate to its scale, geographic diversity and durable cashflows. We have agreed with Pfizer that the business will target leverage of three and a half to four times net debt to adjusted EBITDA at the point of separation, so we expect the business to deliver strongly, reflecting its momentum and free cashflow generation.

We have also agreed that the new company will target a dividend pay-out ratio in the range of 30-50% of adjusted earnings, placing it in line with its core consumer peers.

The separation of GSK Consumer Healthcare will also allow us to de-lever the continuing Pharma and Vaccines business, creating significantly greater flexibility for future investments, and with that I will hand you back to Emma.

## **A clear pathway for improved performance across both businesses**

**Emma Walmsley:** Thank you, Simon. So, in conclusion, this is a unique opportunity to accelerate the priorities I laid out last year. The transaction supports our capital planning and investment in our pipeline, and creates substantial further value for shareholders, patients and consumers. We now have a clear pathway forward to the creation of two UK-based global companies with appropriate capital structures. We will have a new focused global Pharma and Vaccines company with an R&D approach based on science related to the immune system, the use of genetics and advanced technologies, and we will create a new world leading Consumer Healthcare company with a very powerful portfolio of brands and science-based innovation.

With that, I am going to now ask the operator to open up the line for your Q&A.

## **Question & Answer Session**

**Matthew Weston (Credit Suisse):** Many thanks. Two questions, if I can, please. The first around Emma's comments about the ability to invest in pharma innovation as a consequence of doing the transaction. Clearly, the increased profitability in the near-term allows modest reinvestment in R&D, but obviously a larger spin-out opportunity gives you a much greater opportunity for inorganic growth in the future, and I would just like to understand the potential timing of that. Obviously there is an IPO route that could lead to a lot of funds, or there is the leverage opportunity as indicated at the time of spin-out. Is there any opportunity to bring forward that leverage of the consumer JV earlier to give you a significant slug of funds for inorganic growth or, Emma, do you not think large scale M&A is part of the pharma strategy in the near and mid-term?

Secondly, just one strategic comment; in the last, I guess, 18 months with the success of *Shingrix*, both Emma and Luke have highlighted the success that there has been by leveraging the consumer OTC footprint in pharmacists driving the success of the *Shingrix* launch, and how you saw that potentially having a role in other countries as *Shingrix* capacity became available. How do you see that now playing out as two separate companies? Thank you.

**Emma Walmsley:** Thank you, Matt. Obviously very comprehensive questions there; I will try and hit on most of your points.

First of all, why are we setting the timing to within three years? We believe it is important that we take a bit of time to do this right for a couple of reasons. First of all, we have done a global scale integration of a Consumer Healthcare company before, we know exactly what it takes and it is extremely important that integration is done very well while, at the same time, delivering operating performance. Both Brian and I don't want everybody distracted around the notion of a separation during the first part of value creation.

The second reason why we like it taking a few years is the contribution of this larger, stronger Consumer Healthcare business in terms of cashflow to the investment in our Pharma pipeline on which you know we are very focused. Exactly as you say, what is so exciting about this deal today is not just the significant value creation but also the support that it gives to our Pharma business through the visibility of the eventual separation. That means it supports our capital planning and, at the point of separation, we are able to and have agreed with Pfizer to set up the new larger Consumer Healthcare company, a highly profitable one, with leverage of 3.5 to 4.0 net debt to EBITDA. The consequence of that is a very deleveraged Pharma company with capacity to invest in both future growth opportunities and shareholder returns.

It is also important to note when you go through the terms of this deal, obviously we paid Pfizer a premium for control of the operating management but also control of the separation which you will see in the details of the press release, so that is a decision for us. However, our thinking is that the right time for a demerger is around the timeframe that we have laid out.

Now to your question of potential dis-synergies, you are right that we have always tried to take a very pragmatic view around the Group structure. We have said there are benefits but there are also conditions around the Group structure, particularly related to access to capital and that we would review it regularly. This deal today vastly outweighs the benefits of those synergies and is a tremendous opportunity to create value both for shareholders and to support the Pharma priority.

The dis-synergies that I believe are worth consideration, even if they are significantly outweighed, are there is a bit of scale around things like procurement, and there is a bit of life-cycle management around switches. Brian referred to Pfizer and what we have done recently, but the new scale of this new Consumer business is going to be so significant and with the track record of switches that it has done, it will compete easily in in-licensing any potential switch opportunities whether it be from either parent or anyone else.

The example you give, which is the last point on synergy capabilities, is of things like, frankly, the growing power of the patient in this industry. You refer to the launch of our

*Shingrix* vaccine, which has been substantially in the retail environment which we know well, but that is also true when you think about building digital capabilities in Pharma which are being used commercially more and more as well.

There are two points on that. One is that our Pharma business under new leadership is also building up those capabilities already reasonably aggressively. Also, remember the new GSK will be both a Pharma and a Vaccines business and that we shall still be together for a few years yet. Therefore, these sort of dis-synergies are massively outweighed by this value creation opportunity from today. I hope that covers most of your points and perhaps we can go to the next question now.

**Emmanuel Papadakis (Barclays):** The first one is just a follow-up for Emma to try to re-ask the question about organic versus inorganic future growth opportunity for Pharma. The question is: to what extent should we think that this strategic shift signals confidence about the Pharma and Vaccines portfolio that you now have, including TESARO, versus an intention to do further potential inorganic business development?

The second question may be one for Brian. It would be very helpful if you could give us an update on where we are with the Consumer market dynamics we have seen in the last couple of years, i.e. things around digital channel penetration, private label pricing pressures. The sales trajectory for GSK seems to have improved over the last few quarters but it would be great to hear your perspective on 2019 and indeed somewhat beyond that? Many thanks.

**Emma Walmsley:** Thanks, Emmanuel, and we shall come to Brian in a minute. First of all, apologies, Matthew's question was multi-faceted so I missed the inorganic part of it. When I laid out the capital priorities for the company last year, I was very clear - and indeed Hal repeated it this July - that we did expect to develop our pipeline both organically and inorganically. The No. 1 focus on that right now is for the major announcement we made around the acquisition of TESARO and we are extremely focussed, hopefully getting to close reasonably soon, on getting the value from that both for GSK and for oncology patients.

We do expect to continue doing further in-licensing partnerships and indeed out-licensing of some of the portfolio as we continue to strengthen our prospects, and this transaction doesn't change our intent around BD at all. The main focus right now is on the execution of what we have, but more to follow, and in fact this transaction supports it both in

terms of, as I said, the visibility around our capital planning, and eventually in a few years' time, the separation that creates this reset balance sheet and more capacity for the future.

Brian, would you like to come back on the market, please?

**Brian McNamara:** Yes, great, thanks for the question. On market dynamics, a few things. Obviously we see the shift globally and the impact on ecommerce and that varies by market, depending on category regulatory environment. In our portfolio today it's still about 2% of the market but growing, and we have invested heavily in the capability and a focus on having a balanced approach to omni-channel players like the Walmarts and Boots and Walgreens along with the pure plays like Amazon. We have done very well in that space, and *Sensodyne* in the US is a great example where we've been quite successful.

Pfizer, on the other hand, also has had some real strong success in ecommerce, especially in China so we see it as a challenge but a big opportunity to do it right and do it well. I do think over time it will become a bigger part of the business that we play in and we are focussed on being prepared to win when that happens.

On the move of Consumer and the role of digital and consumer marketing, this is something we are very focussed on, and I've talked in the past about the tech stack deal we've done with Google which gives us really incredible capabilities. Pfizer again has good capabilities in this space and we are looking to leverage them both.

On private label, honestly the private label in the categories we compete, it doesn't really exist in oral health at all. We don't really have private label competition in toothpaste. We do in OTC and it tends to be somewhere between 25% and 30% of the category once private label launches. That's been very, very stable for a long time, so the dynamic in OTC is typically you have a branded business and a private label business which also protects from other small entrants into the categories because of the regulatory environment.

So we have been saying we expect the categories to grow in the 2% to 3% range based on our footprint and that's consistent with what we are seeing and consistent with what we expect going forward.

**Emma Walmsley:** Thanks, Brian. Next question, please.

**James Gordon (JP Morgan):** Hello, thanks for taking the questions. The first question would just be the Pfizer shareholders get 32% of the equity in the JV but if you look at 2017 adjusted EBIT it looks like they are contributing about 27%, so is the disparity

just the control premium or does it also reflect better growth prospects for the Pfizer business versus the GSK business? That's the first question.

The second question was just about the payout in terms of dividend. You have given a target payout ratio for the Consumer business post-spin but what does that imply for the stub if it's a lower payout ratio than where we are for the overall group? Could the Consumer spin be an opportunity to revisit the payout approach or how you think about dividends for the GSK stub? That would be the second question.

And then if I could just squeeze in a confirmation. One benefit of the spinoff could be that you could put some more debt in the spinoff and it allows the GSK stub to deliver, but is the Pfizer business coming with any debt initially and when we think about how much debt GSK can put into the new entity, is the right way to think about it that you could put 68% of the debt in and Pfizer could put 32% of the debt in? Is that the right way to think about it, please?

**Emma Walmsley:** Okay, thanks James. I will answer your dividend question and then I am going to come to Simon on explaining the control premium and your question around the allocation of debt.

To be clear, there is no change in our dividend policy. Obviously because 2019 is a year of significant transactional impact we believe it's important to be clear with shareholders about our intent to distribute 80p to them, but the most important thing to understand about this transaction is that it strengthens both businesses and cashflows so that we are better positioned to invest in shareholder returns and growth.

We have been specific about the Consumer debt structure and distribution policy, because that's part of the public terms with our partners, but again let's remember Rx is going to be less levered, significantly less levered, and therefore better able to invest. When within three years, we come to the point of split, it will be better able to invest in growth and pay its dividends.

Simon, do you want to pick up the other two?

**Simon Dingemans:** Yes, sure. James, on the relative split, you are right in terms of the contributions today. If we look forward at the prospects as Brian has described, we operate in very similar categories, so the difference in terms of the eventual terms is all about the premium for having complete control of this venture operationally, but, importantly, also in terms of how we structure it, how we manage the exit, to give us the maximum flexibility in terms of resetting the business into these two new companies, so that's really the difference.

On your debt question, because we're going to consolidate the whole business until the point of separation, there's not a lot of advantage in pushing debt down into the business until the point at which it's going to leave, and we've established this range with Pfizer, setting a level that allows us to de-lever the continuing GSK group significantly, but also gives the Consumer company a balance sheet that starts with a reasonable amount of leverage on it but paying down quickly, given the strong cashflows that will then allow it to go and do things going forward, so I think that's really most appropriate when the business separates.

**Emma Walmsley:** Thanks, Simon. Next question please?

**Keyur Parekh (Goldman Sachs):** Emma, you have spoken about this separation being within three years. Can you give us a sense of some of the drivers that might make it Year 2 as opposed to Year 3, and what might you need to see from a pharma perspective for you to feel more confident around that?

Then secondly, post-TESARO and 23andMe, how much incremental pipeline backfill do you think GSK needs for the Pharma business, and from that perspective, how much incremental time do you need to sort out the Pharma business for the long term?

**Emma Walmsley:** I'm not sure I have an enormous amount more to say on the timing than I already have. As Simon mentioned, we have the control of the timing, for up to five years if you read the detail of the press release, but our intent is to demerge within three. We've done integrations before, we know it does take a bit of time to do it well, and we do not want the Consumer business to be distracted by the separation while they are doing a global scale, reasonably complex integration, and delivering a step change in terms of the margin.

We also like that time because, as you know, over the next two or three years we have a significant amount of both investment and readouts in our Pharma pipeline, be that in our own oncology pipeline or assets like aGM-CSF, or indeed the new TESARO acquisition, which we are hoping to close on in the relatively near term.

If you think about the new Pharma and Vaccines business that we are talking about, this is a company that will be, and is today, the world leader in vaccines, with a very strong growth rate and prospects off the back of the most successful launch in biopharma for a decade with *Shingrix*, which has plenty of prospects ahead of it. No. 1 in respiratory, a leader in HIV with, frankly, some very exciting new medicines coming through both in dual therapies and in long-acting, and quite an exciting new portfolio with a lot of readouts to come through

in immunology-based assets, oncology-based assets, and also now with the overlay of TESARO.

Our intention is, with Hal and Luke and also Deborah and David, over the quarters ahead, and with Hal's updates, to bring visibility to you all about the progress we are making there. That will be with predominantly what we have but we do expect to further supplement it with other early-stage inorganic activity, and more news on that to come.

Thanks very much. Next question, please.

**Richard Parkes (Deutsche Bank):** Thanks very much for taking my questions, just a couple. Firstly, just on the strategy for the planned independent Pharma/Vaccines business. Obviously that would leave that business more exposed to the ultimate dolutegravir patent expiry, so should we think about the planned Consumer spin as simply improving your capability to do bolt-on M&A as a result of the expected deleveraging, or does it signal an openness to a sale or merger with a larger group given the sharpened focus of the independent business. That is the first question.

The second question, I was just going to push you a little bit more on the planned dividend pay-out policy for the remaining Pharma/Vaccines business post-the expected spin. So if we look at consensus numbers, which I think some people are assuming an 80 pence dividend is maintained, it is implying about a 60% pay-out ratio for the group currently. Given the 30-50% pay-out ratio for the expected independent Consumer business, it would imply that you would have to be willing to pay out a greater proportion of profits from the remaining Pharma business without a reduction to total shareholder pay-out. Can you talk about what level of earnings pay-out for the independent Pharma/Vaccines business you would be comfortable with, that would allow you to still reinvest in building out the pharma pipeline? Thank you.

**Emma Walmsley:** Thanks very much. In terms of what this and the output of this deal signals today is that we are very excited about the significant value creation opportunity of the deal, and also the fact that it supports our Pharma priority with the ability to invest near-term behind the development of our pipeline, to support the capital planning for the further development of that, and at the moment of separation to have a de-levered balance sheet that allows us the capacity, as you say, to invest in further growth both organically and inorganically. We are going to have a lot more news over the period between now and that separation within three years to give more content to that.

In terms of dividend, I really don't have much to add from what I have already said in terms of there being no change to the policy, but that this deal actually strengthens both businesses and cashflows, so we are better positioned to distribute and invest in growth.

Simon, I don't know if there is anything further you want to add in terms of the specifics?

**Simon Dingemans:** Richard, remember the policy that we are maintaining for the Pharma business is one based around free cashflow, not earnings, and we are targeting a range of one and a quarter to one and a half times cover. Over the last couple of years, we have been building the free cashflow across the business steadily, and we have seen some very good forward momentum on that front. As Emma said, this transaction is about strengthening both halves of the company and the cashflow generation that they produce to allow us to both invest and pay dividends, so I think that is probably the sum total of our comments at this point, but that is absolutely the intention.

**Emma Walmsley:** Thank you, next question, please.

**Luisa Hector (Exane):** Good morning. Congratulations on the deal. The Pfizer business has essentially been for sale for some time, so I just wondered whether you can give us a little bit more colour on the history; how long have you been talking with the company? You clearly have your existing relationship. Did you need the Unilever deal, TESARO, in place first before you could move forward, and were there any really key negotiating points on each side that have allowed you to come to the deal as it stands today?

Any comments at this stage on the demerger in terms of spin-out versus IPO and the pros and cons of those routes? Thank you.

**Emma Walmsley:** Thanks very much. Very briefly, we have declared today that our intent is to demerge for a variety of reasons but, not least, because it is simpler. Although we do have the right to IPO, the intent is to demerge with a UK listing.

You wouldn't expect me to go into any very specific detail about how this came about, but it is a matter of public record that we were looking at the Pfizer auction earlier in the year. We have always loved this business. As Brian outlined in his presentation, it is an extremely complementary portfolio. We know it's a business with a very strong reputation for innovation and talent, and actually we are extremely excited, and one of the great things about the joint venture with Novartis is the opportunity, as Brian said, to combine some fantastic teams of people, capability, and have that acceleration of culture. But, at the time,

it was clear that although the combination would be fantastic, and the synergies very significant, it was going to cut across the capital allocation priorities that I had laid out and my first priority for capital was the strengthening of the Pharma business, for example to allow for investments like the exciting one in TESARO that we announced just recently. Therefore, reluctantly and rightly, we walked away from it.

However, we then focused on the necessary, and our stated capital allocation priority, buying-out of the Novartis put. This was really important because, unlike in the deal we have announced today, it was an overhang for us and it was important to buy this out and then get control of the destiny of our Consumer business, so we were able to execute that in the spring.

Then very recently, the opportunity of an all-equity transaction came up, which is obviously a fundamental difference for us both. Pfizer is a fantastic partner with which we have worked very well in our ViiV joint venture, recognising the tremendous value creation for us both and for shareholders and, in our case, the opportunity it has strategically to help support our Pharma priority in the near and medium term. We were able to negotiate terms quickly and, importantly, quietly which is how we have come to where we are. I hope that gives you a bit more context.

Next question please?

**Peter Welford (Jefferies):** I have a couple of quick ones. First, when you talked about the roughly £1 billion of net proceeds from disposals, I am curious to know whether any of those disposals are required from a clearance point of view of this transaction, or are all of those believed to be elective to, as you say, refocus the portfolio for future growth?

Secondly, regarding the margin target for 2022 and beyond, does that include any potential incremental cost that may be required to operate the Consumer Healthcare business as a stand-alone company, or would any incremental G&A costs etc., for that business be in addition to the guidance you have given?

Finally, quick clarity on a prior question: is there any debt from Pfizer that is coming over at the time of this deal being consummated, or is this essentially a debt-free merger of the two? Thank you.

**Emma Walmsley:** Thank you and I shall hand all three of those questions to Simon.

**Simon Dingemans:** Thanks, Peter. To your last question, the business is coming cash free and debt free, and both partners have agreed to contribute a small amount to make sure that the business has the right working capital balances.

On the disposals, this is about focusing a now larger portfolio. We see them as very complementary and we don't see a lot of overlap between them, although we shall have to go through the regulatory processes. We are targeting the £1 billion on the basis of sharpening up the focus of the portfolio.

As we get towards the point of separation, we shall have to put some additional cost into the company to support it as a separate quoted entity. We are not expecting those to be material and they are factored into the margin trajectory that we have given you but, clearly, when we get to the point of separation, we shall be able to update you more precisely.

**Emma Walmsley:** Thanks, Simon. I understand that there are no further questions. I would like to reiterate my thanks to you all for joining another last minute call from GSK. I hope that you all have an incredibly well-deserved and peaceful rest over the holiday, and for the majority of you I hope and look forward to seeing you at JP Morgan in early January. Thank you very much.

[Concluded]