DUE DILIGENCE

Analysts see bargain in Pfizer shares
With Pharmacia acquisition done, competition looms

By Ted Griffith, CBS.MarketWatch.com
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NEW YORK (CBS.MW) -- With Pfizer having completed its $60 billion buyout of Pharmacia, could it be time for investors to do some buying of their own?

A sizable number of newsletter editors, analysts and fund managers are recommending Pfizer's shares in the wake of the Pharmacia acquisition, which closed Wednesday.

Pfizer (PFE: news, chart, profile), which already was the world's largest pharmaceutical company with products such as cholesterol medication Lipitor and anti-impotence drug Viagra, expanded its lead over No. 2 drugmaker GlaxoSmithKline through the Pharmacia deal. Pfizer gained full ownership of Celebrex, the blockbuster arthritis medication that the two companies had marketed jointly, and also won rights to Inspra, a promising blood pressure medication.

"Pfizer is our favorite drug stock and among our favorite large-cap U.S. stocks," said Richard Moroney, editor of the Dow Theory Forecasts newsletter.

Popular choice

Moroney isn't alone. Nearly 10 percent of newsletters tracked by the Hulbert Financial Digest hold the stock in their portfolios, making it one of the most popular picks. Pfizer shares are also a favorite of analysts and fund managers, partly because the New York-based company has little exposure to the generic competition that has ravaged profits of other major drug companies. Pfizer fans say the company is likely to post reliable, double-digit earnings growth for years thanks to merger-related cost cutting.

But Pfizer has been turning in strong earnings growth for years, and it hasn't helped the shares. Pfizer's stock is down 18 percent over the past year and off 16 percent over three years.

Steven Check, editor of the Blue Chip Investor, said Pfizer shares tumbled in recent years because they became overvalued during the exuberant days of the late 1990s as their price-to-earnings ratio ballooned to 60. Today, Check said, overvaluation isn't a problem with shares trading at 20 times last year's earnings of $1.59 per share.

At current prices, Check said, investors can buy shares of a company with above-average earnings growth at a price-to-earnings multiple that's about average for the pharmaceutical industry.

"It looks attractive relative to the market and relative to the pharmaceutical group," Check said.

Breaking away

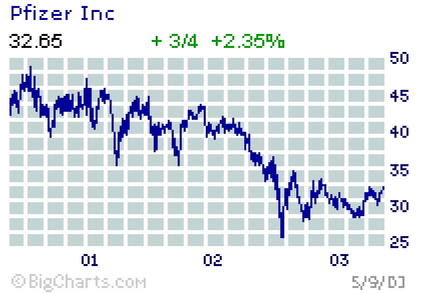
Jeffrey Kraws, co-founder of Crystal Research Associates, an independent pharmaceutical research firm, said Pfizer's shares have been weak largely because of investor concerns about the overall pharmaceutical industry, which has been hurt by generic competition and a dearth of new blockbuster prescription drugs. Kraws predicts Pfizer "will be able to separate itself from the pack" with annual earnings growth that he believes could approach 20 percent in coming years.

"The bottom line is, this is the best-run company in the industry," Kraws said.

Pfizer officials, of course, are optimistic.

"The new, combined company enhances our growth potential," CFO David Shedlarz said in an interview with **CBS.MarketWatch.com.** "This dramatically enhances the ability of the company to meet unmet medical needs."

Shedlarz was eager to point out the growth potential of the company's prescription drugs, but a big part of the earnings-building strategy is predicated on deep cost cuts, including job reductions. Shedlarz wouldn't say exactly how many jobs are slated for elimination, but he said the company expects merger-related cost savings to reach $2.5 billion in 2005.



Analyst Robert Hazlett at SunTrust Robinson Humphrey said he expects job cuts to be "across the board, immediate and substantial."

Shedlarz also wouldn't discuss Pfizer's post-merger earnings and revenue expectations for 2003, saying the company will likely provide an updated financial forecast in June.

Projections that accompanied Pfizer's acquisition announcement back in July called for the combined company to have $52.8 billion in revenue and profit of $14.4 billion, or $1.84 per share, in 2003. But that forecast will have to be revised because it took Pfizer longer than initially expected to close the deal. Pfizer had once hoped to complete the acquisition by the end of 2002, but final federal approval didn't come until this week.

Rivals arrive

No. 1 is an enviable position, but it means that everybody is gunning for you. In the near future, Pfizer will face stepped up competition for two key drugs.

Viagra will likely face competition in the U.S. later this year from a drug developed by Bayer (BAY: news, chart, profile) and its partner GlaxoSmithKline (GSK: news, chart, profile) and another from Eli Lilly (LLY: news, chart, profile) and its biotech partner Icos (ICOS: news, chart, profile).

AstraZeneca (AZN: news, chart, profile) hopes to win U.S. clearance for a new cholesterol-lowering medication that could be a formidable competitor to Pfizer's Lipitor. The world's top-selling prescription drug, Lipitor generated nearly $8 billion in sales last year.

Shedlarz downplays the potential threat to Viagra and Lipitor, saying the drugs will continue to enjoy popularity because of their established records of safety and effectiveness.

"We've never been afraid of competition, given the strength of our products," the chief financial officer said.

Generic competition, which so far hasn't plagued Pfizer as it has other drugmakers, also looms on the horizon. Analyst Richard Evans at Sanford Bernstein has projected that anti-epilepsy drug Neurontin could lose patent protection later this year, followed in 2006 by blockbuster antidepressant Zoloft and high blood pressure medication Norvasc.

Lots of muscle

Pfizer's admirers say the post-merger company has the marketing and research resources to outmuscle generic and branded competitors.

"The industry is already very competitive, and Pfizer has performed well," said Crystal Research's Kraws, who said he doesn't own Pfizer shares. "If you're going to make a case for any pharmaceutical company, one of the most compelling cases can be made for Pfizer."

Not everybody is convinced that Pfizer's prospects are bright. Sam Isaly, manager of the Eaton Vance Worldwide Health Sciences Fund, said he has questions about the long-term outlook for Pfizer because its enormous size will make it difficult to post substantial sales and earnings growth.

"It takes a lot to keep those locomotive engines going," the fund manager said.

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