Allergan Inc. [AGN] – Further Downside Ahead

Target Price Analysis

Expected Return from $224 PPS (as of 8/18/17) = $117

-48% IRR for one-year hold period

Summary

- ***Allergan's non-GAAP financial metrics continue to mislead.***
- ***Herein we review Allergan's Q2 and 1H 2017 financial results.***
- ***GAAP results highlight clearly declining operational performance.***
- ***We reiterate our $117 target share price for Allergan.***

As a famous investor once proclaimed, price is what you pay and value is what you get. Anyone with an Internet connection can easily find the price today for Allergan (AGN) stock. What is much more difficult, however, determining the intrinsic value of the company's shares. This involves logical, unbiased and informed judgment and reasoning. Of course, as with any analysis, garbage input will yield garbage output. Therein lies the rub, as we assert herein that the assumptions used by the Allergan management team in their non-GAAP valuation models yield nonsensical output which is, with the assistance of conflicted analysts and unsophisticated financial journalists, unquestioningly accepted by investors.

Luckily, there is an alternative method of judging Allergan's recent financial performance, namely examining the company's GAAP financial statements and making reasonable (rather than pie-in-the-sky) adjustments thereto. These evidence a clear downtrend over the past eighteen months, with cash flow dropping off drastically and organic revenue growth grinding to a halt. Based on the results from the first six months of 2017, we see no reason to alter our previous target price for Allergan shares of $117, indicating nearly 50% expected downside ahead for Allergan shareholders. In other words, we continue to believe that investors are paying $1 for approximately $0.50 worth of value in buying Allergan at the current market price.

Table of Contents

I. Allergan Non-GAAP Metrics Flatter to Deceive

A. To GAAP or Not To GAAP?

> [In the late 1960s,] accounting shenanigans of all sorts – many of them ridiculously transparent – were excused or overlooked. Indeed, having an accounting wizard at the helm of an expanding conglomerate was viewed as a huge plus: Shareholders in those instances could be sure that *reported* earnings would never disappoint, no matter how bad the operating realities of the business might become… I [remember attending] a meeting at which an acquisitive CEO bragged of his "bold, imaginative accounting." Most of the analysts listening responded with approving nods, seeing themselves as having found a manager whose forecasts were certain to be met, whatever the business results might be.
>
> Eventually, however, the clock struck twelve, and everything turned to pumpkins and mice. Once again, it became evident that business models based on the serial issuances of overpriced shares – just like chain-letter models – most assuredly redistribute wealth, but in no way create it. Both phenomena, nevertheless, periodically blossom in our country – they are every promoter's dream – though often they appear in a carefully-crafted disguise. The ending is always the same: Money flows from the gullible to the fraudster. And with stocks, unlike chain letters, the sums hijacked can be staggering.
>
> *Warren Buffett, 2014 Berkshire Hathaway shareholder letter*

We have issued two prior articles on Allergan, in January and April of this year, each of which concerned the company's use (or misuse, as the case may be) of non-GAAP financial information and metrics. Both articles can be found at this link. Generally speaking, though, before one looks at Allergan in particular from an investment perspective, we believe such person should first consider GAAP versus non-GAAP at a conceptual level. This is because, with respect to Allergan, there is such a massive disparity between what an investor sees from a GAAP perspective versus a non-GAAP perspective—the former makes the company look terrible, while the latter (at least using management's numbers) makes the company look highly prosperous. We thus ask the following: "To GAAP…or not to GAAP?" That is indeed the question.

First, it should be noted that GAAP is an acronym for "generally accepted accounting principals". We would emphasis the first two words: generally accepted. These are not bizarre or arcane rules, they are commonly accepted established accounting practices which have been around for decades. Moreover, an organization called the FASB (Financial Accounting Standards Board) constantly refines the rules governing GAAP to insure that that they become more and more precise over time. The following is a description of the FASB's mission from its website:

> Established in 1973, the Financial Accounting Standards Board (FASB) is the independent, private-sector, not-for-profit organization based in Norwalk, Connecticut, that establishes financial accounting and reporting standards for public and private companies and not-for-profit organizations that follow Generally Accepted Accounting Principles (GAAP).

> *The FASB is recognized by the Securities and Exchange Commission as the designated accounting standard setter for public companies*. FASB standards are recognized as authoritative by many other organizations, including state Boards of Accountancy and the American Institute of CPAs (AICPA). The FASB develops and issues financial accounting standards through a transparent and inclusive process intended to promote financial reporting that provides useful information to investors and others who use financial reports.
>
> The Financial Accounting Foundation (FAF) supports and oversees the FASB. Established in 1972, the FAF is the independent, private-sector, not-for-profit organization based in Norwalk, Connecticut responsible for the oversight, administration, financing, and appointment of the FASB and the Governmental Accounting Standards Board (GASB).
>
> FASB MISSION
>
> *The collective mission of the FASB, the Governmental Accounting Standards Board (GASB) and the FAF is to establish and improve financial accounting and reporting standards to provide useful information to investors and other users of financial reports and educate stakeholders on how to most effectively understand and implement those standards*.
>
> The FASB, the GASB, the FAF Trustees, and the FAF management contribute to the collective mission according to each one's specific role:

- The FASB and the GASB are charged with setting the highest-quality standards through a process that is robust, comprehensive, and inclusive.
- The FAF management is responsible for providing strategic counsel and services that support the work of the standard-setting Boards.
- The FAF Trustees are responsible for providing oversight and promoting an independent and effective standard-setting process.

(Source: FASB Website)

To provide an example of how the FASB works and to correct accounting abuses, take the accounting rules governing share-based compensation. Back in the 1990s, there was an epidemic of misinformation emanating from C-suites across the country with respect to accounting for stock options. Basically, CEOs did not want options to be expensed in a company's income statement, because (duh) earnings—and, hence, stock prices—would consequently be lower than if option grants were not expensed when granted. Never mind that stock-based compensation is a real expense.

Warren Buffett decried this deception of investors in his [2002 Berkshire Hathaway chairman's letter](), writing as follows:

> The Chicago Tribune ran a four-part series on Arthur Andersen last September that did a great job of illuminating how accounting standards and audit quality have eroded in recent years. A few decades ago, an Arthur Andersen audit opinion was the gold standard of the profession. Within the firm, an elite Professional Standards Group (PSG) insisted on honest reporting, no matter what pressures were applied by the client. Sticking to these principles, the PSG took a stand in 1992 that the cost of stock options should be recorded as the expense it clearly was. *The PSG's position*

> *was reversed, however, by the "rainmaking" partners of Andersen who knew what their clients wanted – higher reported earnings no matter what the reality*. Many CEOs also fought expensing because they knew that the obscene megagrants of options they craved would be slashed if the true costs of these had to be recorded.
>
> Soon after the Andersen reversal, the independent accounting standards board (FASB) voted 7-0 for expensing options. Predictably, the major auditing firms and an army of CEOs stormed Washington to pressure the Senate – what better institution to decide accounting questions? – into castrating the FASB. The voices of the protesters were amplified by their large political contributions, usually made with corporate money belonging to the very owners about to be bamboozled. It was not a sight for a civics class.
>
> To its shame, the Senate voted 88-9 against expensing. Several prominent Senators even called for the demise of the FASB if it didn't abandon its position. (So much for independence.) Arthur Levitt, Jr., then Chairman of the SEC – and generally a vigilant champion of shareholders – has since described his reluctant bowing to Congressional and corporate pressures as the act of his chairmanship that he most regrets. (The details of this sordid affair are related in Levitt's excellent book, Take on the Street.)
>
> With the Senate in its pocket and the SEC outgunned, corporate America knew that it was now boss when it came to accounting. With that, a new era of anything-goes earnings reports – blessed and, in some cases, encouraged by big-name auditors – was launched. The licentious behavior that followed quickly became an air pump for The Great Bubble.
>
> After being threatened by the Senate, FASB backed off its original position and adopted an "honor system" approach, declaring expensing to be preferable but also allowing companies to ignore the cost if they wished. *The disheartening result: Of the 500 companies in the S&P, 498 adopted the method deemed less desirable, which of course let them report higher "earnings." Compensation-hungry CEOs loved this outcome: Let FASB have the honor; they had the system*. [Emphases added]

(Source: Berkshire Hathaway 2002 Shareholder Letter)

To summarize, FASB attempted to correct an obvious accounting abuse that had become institutionalized in corporate America (and which produced misleading financial statements), only to be blocked by a more powerful institution (the U.S. Senate) due to lobbying by the very corporate executives that the FASB was formed to independently regulate—at least with respect to accounting issues. Fortunately, the FASB reinstituted its original position in 2004 when it issued a formal proposal calling for options to be expensed (see coverage of the issue here), and the cost of stock options now run through the income statement, as they should.

The point of recounting this background is that from it one draws the following inevitable conclusions with respect to accounting: (1) As Buffett states, corporate executives want higher reported earnings no matter what the economic reality; (2) in order to have accurate financial statements, an independent standards entity (the FASB) is needed to formulate accounting rules free from the meddling of those occupying C-suites; (3) in the United States, GAAP accounting (as defined by the FASB) is the version of accounting that will most likely produce financial statements that accord with economic reality (i.e., least mislead investors); and (4) any deviation from GAAP accounting proposed by a CEO or CFO with respect to a company's financials should be viewed with a high degree of skepticism and only accepted by an investor if management has produced a highly compelling (not merely semi-plausible) rationale for such deviation. Departures from GAAP should be the exception, not the rule.

B. Allergan's Continued (Mis)use of Non-GAAP Financial Metrics

We have noted in our prior two articles the vast disparity between Allergan's GAAP and non-GAAP financials. For example, in fiscal 2016 the company lost $941 million from continuing operations on a GAAP basis, yet claimed in its non-GAAP financials that it had made a $5.5 billion profit from continuing operations, a difference of $6.44 billion, or nearly $16 per share(!). That's correct, if one chooses (at the company's urging) to totally ignore **$6,440,000,000** in GAAP expenses, then Allergan's GAAP *loss* of $2.45/share for 2016 magically metamorphoses into a non-GAAP *gain* of $13.51/share for the year. Slap a multiple of 17X on the latter figure and one can easily justify today's stock price. Below please find the relevant 2016 non-GAAP reconciliation provided by the company from its Q4 2016 earnings release:

	Three Months Ended December 31, 2016	Three Months Ended December 31, 2015	Twelve Months Ended December 31, 2016	Twelve Months Ended December 31, 2015
GAAP to Non-GAAP Performance net income calculation				
GAAP (loss) from continuing operations attributable to shareholders	$ (41.9)	$ (790.2)	$ (941.1)	$ (2,945.8)
Adjusted for:				
Amortization	1,638.5	1,584.8	6,470.4	5,443.7
Acquisition and licensing charges [1]	800.4	517.2	1,593.6	3,673.1
Accretion and fair-value adjustments to contingent consideration	(143.5)	8.4	(64.2)	95.7
Impairment/asset sales and related costs	456.0	282.9	748.9	783.6
Non-recurring (gain) / losses	(9.5)	10.7	8.9	52.9
Legal settlements	17.3	10.6	117.3	31.1
Income taxes on items above and other income tax adjustments	(1,242.2)	(229.3)	(2,432.2)	(2,029.6)
Non-GAAP performance net income attributable to shareholders	$ 1,475.1	$ 1,395.1	$ 5,501.6	$ 5,104.7
Diluted earnings per share				
Diluted (loss) per share from continuing operations attributable to shareholders- GAAP	$ (0.12)	$ (2.00)	$ (2.45)	$ (8.01)
Non-GAAP performance net income per share attributable to shareholders	$ 3.90	$ 3.36	$ 13.51	$ 13.20
Basic weighted average ordinary shares outstanding	356.8	394.2	384.9	367.8
Effect of dilutive securities:				
Dilutive shares	21.8	21.5	22.3	18.8
Diluted weighted average ordinary shares outstanding [2]	378.6	415.7	407.2	386.6

(Source: Allergan Q4 2016 Earnings Release)

Moreover, we previously noted how we did not believe that Allergan's non-GAAP calculations were compliant with the SEC's May 2016 guidance on the subject, nor with the SEC's formal rules governing non-GAAP metrics in documents filed with the Commission. From the former we quoted the SEC's answer to Question 102.05, which includes the following statement:

> [N]on-GAAP liquidity measures that measure cash generated must not be presented on a per share basis in documents filed or furnished with the Commission,

> consistent with Accounting Series Release No. 142. Whether per share data is prohibited depends on whether the non-GAAP measure can be used as a liquidity measure, even if management presents it solely as a performance measure. When analyzing these questions, the staff will focus on the substance of the non-GAAP measure and not management's characterization of the measure.

(Source: SEC May 2016 Non-GAAP Guidance)

As we demonstrated in our prior article, we believed then (and continue to believe now) that Allergan's so-called "Performance Net Income Per Share" is really a disguised (and impermissible) per share measure of cash generated by operations. Indeed, the SEC told Allergan's CFO this specifically in a comment letter to the company in January 2017, stating that "we do not agree [with your characterization of "Performance Net Income Per Share" as solely a performance measure] and believe that the measure you present is clearly and closely related to cash flows" (see full letter here). Nevertheless, Allergan has continued use this flawed non-GAAP metric in its financial releases, thereby misleading investors into thinking it measures net income rather than cash flows or liquidity.

C. Reaction to Allergan's Q2 2017 Earnings

Turning now to Allergan's Q2 2017 results, the company reported a $902 million GAAP net operating loss on revenues of $4 billion, versus a $488 million GAAP net operating loss on revenues of $3.7 billion in the prior year quarter. By backing out over $2.1 billion in GAAP expenses in the quarter (an amount equal to over 50% of net revenues—no, the percentage is not a typo), the company also claimed to have generated Non-GAAP Performance Net Income Per Share of $4.02 in Q2 2017. News summaries regarding Allergan's Q2 2017 results predictably and myopically focused on the non-GAAP numbers as if they represented "real" earnings for the company, with headline references to "better-than-expected earnings", "beating estimates", "raising outlook", etc. and either total omitting the "non-GAAP" designation or referring to earnings that as being "adjusted" or "excluding special items":

> **Allergan Posts Better-Than-Expected Second Quarter Earnings**
>
> Allergan reports a narrower-than-expected per-share loss as products were hindered by patent exclusivity.
>
> Kinsey Grant • Aug 3, 2017 3:16 PM EDT
>
> Allergan plc (AGN) reported second quarter earnings per share of $4.02 on Thursday, Aug. 3.
>
> Analysts surveyed by FactSet expected Allergan to earn $3.92 per share in the second quarter.

Botox-maker Allergan's quarterly profit beats estimates

August 03, 2017, 08:39:00 AM EDT By Reuters

(Adds details, forecast) Aug 3 (Reuters) - Botox-maker Allergan Plc <AGN.N> reported a better-than-expected quarterly profit, helped by strength in its medical aesthetics unit, prompting the drugmaker to raise its full-year revenue forecast. The company said it now expects full-year revenue in the range of $15.85 billion to $16.05 billion from its previous forecast of $15.80 billion to $16 billion. Net revenue for the quarter rose 9 percent to $4.01 billion, beating Wall Street estimates of $3.94 billion. Revenue in its medical aesthetics unit, which includes its Botox blockbuster wrinkle treatment, rose more than 53 percent to $643.9 million. Excluding special items, the company earned $4.02 per share, topping analysts' average estimate of $3.92, according to Thomson Reuters I/B/E/S. Net loss attributable to ordinary shareholders widened to $795.5 million, or $2.37 per share, in the second quarter ended June 30, from $571.3 million, or $1.44 per share, a year earlier.

Why Allergan Is Stagnant Despite Beating Views, Raising Outlook

ALLISON GATLIN

Botox-maker **Allergan** (AGN) topped Wall Street's second-quarter model Thursday, but stock reaction was muted on light sales of eye drug Restasis and stagnant revenue from fat-stripping drug Kybella.

Autoplay: On | Off

For the second quarter ended June 30, Allergan reported adjusted income of $4.02 per share on $4.01 billion in sales, up a respective 20% and 8.7% vs. the year-earlier period. The consensus expected adjusted earnings of $3.95 a share on $3.95 billion in sales.

Allergan also raised its 2017 guidance to $15.85 billion to $16.05 billion in revenue and adjusted income of $16.05-$16.45 per share. Previously, Allergan had guided to $15.8 billion to $16 billion in sales and adjusted earnings of $15.85-$16.35 a share.

"This raise was unexpected in our view," Mizuho analyst Irina Koffler said in a note to clients. Koffler kept her 267 price target and buy rating on Allergan stock. "The stock may be held back by some mixed performance in key products."

(Source: Google News Items Regarding AGN, 8/3/17)

Interestingly, Seeking Alpha's headline was one of the most accurate, noting that "non-GAAP" EPS was up and that guidance was revised, not "raised" (Allergan's GAAP guidance *actually got worse*, as they increased their expected 2017 GAAP loss from $(9.70) - $(10.20) per share to $(10.80) - $(11.20), due to higher spending for the rest of the year):

Allergan Q2 revenues up 8%; non-GAAP EPS up 20%; revises guidance

Aug. 3, 2017 8:25 AM ET | About: Allergan plc (AGN) | By: Mamta Mayani, SA News Edi...

- Allergan (AGN) Q2 results: Revenues: $4,007.4M (+8.8%); U.S. Specialized Therapeutics: $1,715M (+15.2%); U.S. General Medicine: $1,427.7M (-1.5%); International: $858.5M (+13.4%).
- Operating Loss: ($902.4M) (-85.1%); Net Loss: ($725.9M) (-44.7%); Loss Per Share: ($2.35) (-88.0%); Non-GAAP EPS: $4.02 (+20.0%); Quick Assets: $5,825.9M (-55.9%); CF Ops: $1,629.3M (+18.1%).
- **2017 Guidance**: Revenues: $15.850B - 16.050B from $15.8B - 16.0B; EPS: ($11.20 - 10.80) from ($10.20 - 9.70); Non-GAAP EPS: $16.05 - 16.45 from $15.85 - 16.35.

(Source: Seeking Alpha 8/3/17 AGN News Item)

Allergan's management appears to have been eager to boost the stock price by manufacturing a classic "beat and raise" narrative for the 2nd quarter via its non-GAAP legerdemain. Although the company in its earnings release under the heading "Forward-Looking Statement" includes the boilerplate language that "Non-GAAP adjusted financial measures have limitations as analytical tools and should not be considered in isolation, or as a substitute for our results as reported under GAAP", investors naturally skip right over the boilerplate (most likely just as management anticipates). Here is how the CEO stated the party line on the earnings conference call (see full transcript here; no mention of gigantic GAAP losses for him—see no evil, hear no evil, speak no evil):

> [A]t the midpoint of 2017, it is clear that we are delivering on our pivotal year with a focus on operational excellence and execution. With our strong first-half performance and solid outlook for the remainder of the year, we are raising our full-year guidance for both sales and non-GAAP performance net income per share.

When the expected beat-and-raise "pop" in the stock failed to materialize (Allergan shares ended the day down 3%, closing at $243), Allergan longs appeared flummoxed:

bardmaster
Comments (18) | + Follow | Send Message

why down? just not good enough of a beat and not enough raising to guidance? pe is not high and this is a solid company with a strong pipeline. I don't get it.

04 Aug 2017, 11:44 AM Report Abuse Like 0 Reply

(Source: Seeking Alpha 8/3/17 AGN News Item)

(Note here, again, the general confusion regarding "earnings", as this particular long refers to a P/E ratio based on the misleading non-GAAP "Performance Net Income" numbers.)

In light of the market's glum reaction to supposedly "strong" earnings, have investors at long last finally caught on to Allergan's non-GAAP "trickeration"? We again posit the question: Why should investors choose to blindly accept non-GAAP numbers cherry-picked by management, instead of GAAP figures endorsed by the FASB? Which numbers are more likely to realistically depict Allergan's true economic performance, those based on a painstakingly well thought-out accounting system devised by an impartial independent standards board, or those fabricated out of whole cloth by conflicted insiders in order to beat quarterly estimates and rack up higher annual bonuses? Non-GAAP figures are not reviewed or governed by any independent regulatory body, nor are they endorsed by the SEC—only GAAP is endorsed by the Commission. As Buffett states, most management teams want to show investors "higher reported earnings no matter what the reality". There would thus be no reason to proffer non-GAAP figures to investors at all unless they presented a consistently rosier (and likely misleading) picture of the health of the business overall vis-à-vis the GAAP figures. Thus, we would advise investors to take Allergan's "Performance Net Income Per Share" with a handful of salt.

II. Analysis of Allergan's Q2 and 1st Half 2017 Performance

A. Non-GAAP Performance Net Income

Allergan wants investors to consider its so-called "non-GAAP Performance Net Income" to be a measurement of the company's "core" earnings, instead of the relevant GAAP figures. Indeed, management repeatedly emphasizes the non-GAAP numbers to the investment community and tries to gloss over the GAAP numbers as irrelevant. For instance, despite racking up nine-figure GAAP losses from continuing operations in each of the past four quarters (in aggregate amounting to nearly $3 billion in losses, including over $1.8 billion in losses in 2017 thus far), in its prepared remarks on the past four earnings conference calls Allergan management has studiously avoided referencing the company's GAAP operating losses even a single time(!) (see Q2 2017 transcript here, Q1 2017 transcript here, Q4 2016 transcript here and Q3 2016 transcript here).

In order to bend over backwards to be fair to management, however, we review in this section their non-GAAP numbers for Q2 and the first half of 2017, as well as our own updated non-GAAP adjusted earnings calculations for the period. Below are the company's calculations from their most recent earnings press release:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2017	2016	2017	2016
GAAP to Non-GAAP Performance net income calculation				
GAAP (loss) from continuing operations attributable to shareholders	$ (717.5)	$ (424.4)	$ (3,279.6)	$ (517.3)
Adjusted for:				
Amortization	1,757.9	1,633.1	3,493.9	3,222.8
Acquisition and licensing charges (1)	273.2	232.2	2,631.6	471.7
Accretion and fair-value adjustments to contingent consideration	(15.5)	29.6	15.2	63.4
Impairment/asset sales and related costs	717.3	251.3	1,064.7	255.6
Non-recurring (gain) / losses	174.1	(8.6)	174.1	0.2
Legal settlements	42.5	49.7	41.4	59.2
Income taxes on items above and other income tax adjustments	(796.9)	(364.9)	(1,510.4)	(907.8)
Non-GAAP performance net income attributable to shareholders	$ 1,435.1	$ 1,398.0	$ 2,630.9	$ 2,647.8
Diluted earnings per share				
Diluted (loss) per share from continuing operations attributable to shareholders-GAAP	$ (2.14)	$ (1.07)	$ (9.78)	$ (1.31)
Non-GAAP performance net income per share attributable to shareholders	$ 4.02	$ 3.35	$ 7.37	$ 6.34
Basic weighted average ordinary shares outstanding	335.2	395.6	335.2	395.2
Effect of dilutive securities:				
Dilutive shares	21.5	21.8	21.8	22.3
Diluted weighted average ordinary shares outstanding	356.7	417.4	357.0	417.5

(1) Includes stock-based compensation due to the Zeltiq, Allergan and Forest acquisitions as well as the valuation accounting impact in interest expense, net.

(Source: Allergan Q2 2017 Earnings Release)

Although "Performance Net Income Per Share" increased by 20% for the three months ended June 30, 2017 (from $3.35 to $4.02), this was almost entirely due to share repurchases rather than underlying operational performance. Aggregate non-GAAP Performance Net Income increased just $37 million year-over-year in the second quarter, or 2.65%, and actually decreased by $17 million year-over-year in the first half of 2017, down 6/10th of one percent. This type of performance should not cause shareholders to be doing handsprings, but not jumping off of the nearest bridge either.

If one accepts management's claim that Allergan's GAAP numbers are excessively punitive, a prudent investor should still desire some sort of sanity check with respect to the non-GAAP amounts above. In our article from April 2017, we offered what we believed was "A Realistic Method of Calculating Allergan's True Economic Earnings", which involved adding back to GAAP net income the following: (1) 1/3rd of the company's amortization of intangible assets[1]; (2) all of the company's accretion and fair-value adjustments to contingent consideration; (3) all of the company's self-described non-recurring gains and losses; and (4) all of the company's expenses for legal settlements. But, wait, there's more—to be excessively conservative and fair to management, we are even willing to add back all acquisition and licensing charges, no questions asked. Below are our non-GAAP net income numbers for Allergan for the past 3 and 6 months, in each case compared to the respective 2016 figures (note that we have applied the same tax rates that Allergan uses in its non-GAAP reconciliation):

GAAP to Non-GAAP Performance Net Income calculation	3 mos 6/30/17	3 mos 6/30/16	YOY CHANGE	6 mos 6/30/17	6 mos 6/30/16	YOY CHANGE
GAAP (loss) from continuing operations attributable to shareholders	-717.5	-424.4	69.1%	-3,279.60	-517.3	534.0%
Adjusted for:						
Amortization	1,172.52	1,089.28	7.6%	2,330.43	2,149.61	8.4%
Acquisition and licensing charges (1)	273.2	232.2	17.7%	2,631.60	471.7	457.9%
Accretion and fair-value adjustments to contingent consideration	-15.5	29.6	-152.4%	15.2	63.4	-76.0%
Non-recurring (gain) / losses	174.1	-8.6	NM	174.1	0.2	NM
Legal settlements	42.5	49.7	-14.5%	41.4	59.2	-30.1%
Total Amount Of Addbacks To Arrive At Adjusted PFI	1,646.82	1,392.18	18.3%	5,192.73	2,744.11	89.2%
Income taxes on items above and other income tax adjustments	-444.64	-232.49	91.2%	-1,059.32	-611.94	73.1%
TAX RATE USED TO COMPUTE ROW ABOVE	27.0%	16.7%		20.4%	22.3%	
Non-GAAP Performance Net Income attributable to shareholders	484.68	735.28	-34.1%	853.81	1,614.87	-47.1%
Diluted (loss) per share from continuing operations attributable to shareholders- GAAP	-2.14	-1.07	100.0%	-9.78	-1.31	646.6%

[1] Although Allergan asks investors to ignore 100% of GAAP amortization of intangibles when calculating its non-GAAP figures, the company implicitly admits in its SEC filings that amortization of intangibles represents a "real" cost to the company. On page 19 of its Q2 2017 10-Q filing, for example, the company states that the amount assigned to these intangibles represents "an estimate of the fair value of [the] asset based on market participant expectations of the cash flows [the] asset would generate over its remaining useful life". In addition, the assumptions used to arrive at the estimated fair value include "the estimated net cash flows for each year for each asset or product (including net revenues, cost of sales, R&D costs, selling and marketing costs, other allocated costs, and working capital/contributory asset charges), the appropriate discount rate to select in order to measure the risk inherent in each future cash flow stream, the assessment of each asset's life cycle, the potential regulatory and commercial success risks, competitive trends impacting the asset and each cash flow stream." In other words, the company's drug assets depreciate over just as surely as an oil well depletes; therefore, Allergan must spend money (i.e., incur expenses) roughly in line with this depreciation in order to offset the inevitable decline in cash flows represented by the amortization charges. Nevertheless, in an effort to give the company the benefit of the doubt, we have added back 1/3rd of the amortization charges in our non-GAAP EPS calculations.

Non-GAAP Performance Net Income Per Share attributable to shareholders	1.36	1.76	-22.9%	2.39	3.87	-38.2%
Basic weighted average ordinary shares outstanding	335.2	395.6	-15.3%	335.2	395.2	-15.2%
Effect of dilutive securities:						
Dilutive shares	21.5	21.8	-1.4%	21.8	22.3	-2.2%
Diluted weighted average ordinary shares outstanding	356.7	417.4	-14.5%	357	417.5	-14.5%

(Source: Allergan SEC filings; Seven Corners calculations)

Using our (in our view, much more reasonable) methodology, we find that aggregate non-GAAP net income declined 34% in the second quarter and 47% in the first half of 2017, respectively, versus the 2016 numbers. Even after factoring in the massive $15 billion share repurchase that Allergan has executed over the past year, non-GAAP net income per share has still declined 23% in the second quarter and 38% in the first half of 2017, respectively, versus 2016. We believe that these figures evidence that Allergan's underlying business is currently experiencing significant operational stress which is hidden in Allergan's non-GAAP Performance Net Income numbers. Finally, we note that at the current share price, Allergan trades at a massive 47X annualized first half 2017 net income per share of $4.78 ($2.39 X 2), a multiple usually reserved for companies experiencing significant earnings growth, not contraction or stasis.

B. Operating Cash Flow Analysis

Perhaps Allergan's cash flow figures tell a different story, though. Allergan states that it expects the company to produce non-GAAP adjusted cash flow of $1.5 to $2 billion per quarter, or $6 to $8 billion annually. On the surface, the company's enterprise value of approximately $100 billion seems reasonable in relation to this level of annual cash flow. But is the $6 to $8 billion number accurate? If Allergan's non-GAAP numbers were realistic measurements of economic performance of the company's assets, then logically one would expect Allergan's GAAP cash flows to converge over time towards the non-GAAP figures, as the accounting "noise" of the Actavis-Allergan combination burns off over time. Analyst Jami Rubin of Goldman Sachs asked about this point on the Q3 2016 earnings call:

> **Jami Rubin - Goldman Sachs & Co.**: [A] question on GAAP versus non-GAAP cash flow from operations, there's still a very wide gap between the two, with the fourth quarter reporting negative cash flow from operations versus $1.5 billion in adjusted cash flow from operations, and I see your guidance this year is for negative cash flow on a GAAP basis. Obviously, the company is very busy with deals et cetera, et cetera. *When are we going to start to see GAAP and non-GAAP from a cash flow perspective start to narrow?* Thanks very much.
>
> **Maria Teresa Hilado - Allergan Plc**: On cash flow, Jami, this quarter there are a couple of things that drove that. One was the taxes paid on the gain on sale of Teva, which was roughly $700 million. That obviously won't be recurring. *There may be further adjustments as we true up taxes, but I think that's probably the last large payment*. And then secondly, there were restructuring charges, including additional compensation for Foresight, Vitae, and Tobira. And so obviously to the extent that we don't do any other acquisitions that impact cash flow related to this, then that

will also go away. *So I think you would get GAAP to non-GAAP closer, but there are always additional adjustments to that number*. [emphases added]

(Source: Allergan Q3 2016 Earnings Call)

Despite Allergan's CFO's assertions, however, the company's GAAP and non-GAAP numbers do *not* appear to be getting closer once working capital and extraordinary tax payments are adjusted out. Below we present Allergan's statement of operating cash flows for (1) the six months ended 6/30/16, (2) the six months ended 12/31/16, (3) the twelve months ended 12/31/16, (4) the six months ended 6/30/17, and (5) the twelve months ended 6/30/17, respectively:

Consolidated Statements of Cash Flows $ in Millions	***6 MOS 6/30/16***	***6 MOS 12/31/16***	***12 MOS 12/31/16***	***6 MOS 6/30/17***	***TTM 6/30/17***
Cash Flows From Operating Activities:					
Net income / (loss)	-243.5	15,223.0	14,979.5	-3,288.1	*11,934.9*
Reconciliation to net cash provided by operating activities:					
Depreciation	76.9	78.9	155.8	81.2	*160.1*
Amortization	3,227.6	3,247.6	6,475.2	3,493.9	*6,741.5*
Provision for inventory reserve	116.9	64.5	181.4	48.7	*113.2*
Share-based compensation	188.8	145.7	334.5	148.5	*294.2*
Deferred income tax benefit	-327.1	-1,116.8	-1,443.9	-1,478.8	*-2,595.6*
Pre-tax gain on sale of businesses to Teva	0.0	-24,511.1	-24,511.1	0.0	*-24,511.1*
Non-cash tax effect of gain on sale of businesses to Teva	0.0	5,285.2	5,285.2	1,978.0	*7,263.2*
In-process research and development impairments	274.9	469.0	743.9	1,043.3	*1,512.3*
Goodwill impairment	0.0	0.0	0.0	0.0	*0.0*
Loss / (gain) on asset sales and impairments, net	-19.3	24.3	5.0	21.4	*45.7*
Amortization of inventory step-up	42.4	0.0	42.4	87.8	*87.8*
Amortization of deferred financing costs	21.0	30.0	51.0	13.2	*43.2*
Accretion and contingent consideration	60.8	-127.6	-66.8	15.2	*-112.4*
Excess tax benefit from stock-based compensation	0.0	-20.4	-20.4	0.0	*-20.4*
Non-cash impact of debt extinguishment	0.0	0.0		-8.2	*-8.2*
Impact of assets held for sale	0.0	0.0		0.0	*0.0*
Other, net	-26.4	-33.5	-59.9	-22.6	*-56.1*
Changes in assets and liabilities (net of effects of acquisitions):					
Decrease / (increase) in accounts receivable, net	-501.2	310.2	-191.0	-139.0	*171.2*
Decrease / (increase) in inventories	-183.2	-85.2	-268.4	-95.1	*-180.3*
Decrease / (increase) in prepaid expenses and other current assets	245.4	-215.5	29.9	10.5	*-205.0*
Increase / (decrease) in accounts payable and accrued expenses	424.0	-110.5	313.5	-207.5	*-318.0*
Increase / (decrease) in income and other taxes payable	-477.6	151.0	-326.6	673.7	*824.7*
Increase / (decrease) in other assets and liabilities	-267.5	-16.4	-283.9	-23.5	*-39.9*
Net cash provided by operating activities	2,632.9	-1,207.6	1,425.3	2,352.6	*1,145.0*
Net cash provided by Ops (ex-WC Changes):	***3,393.0***	***-1,241.2***	***2,151.8***	***2,133.5***	***892.3***
Net cash provided by Ops (ex-WC Changes + TEVA Tax):	***3,393.0***	***1,330.5***	***4,723.5***	***2,133.5***	***3,464.0***

(Source: Allergan SEC filings; Seven Corners calculations)

On the surface, Allergan's operating cash flows seem to be improving dramatically, with $2.35 billion for the first 6 months of 2017 (the 5th column) versus of $1.43 billion for all of 2016 (the 4th column), a $928 million (or 65%) increase. In the penultimate row of the table, though, we show Allergan's operating cash flows excluding changes in working capital, which generally are not indicative of the underlying state of the business. These numbers present a much more negative picture of Allergan's business, showing that cash from underlying operations (ex-working capital) fell 37% in the first half of 2017 versus the prior year (from $3.39 billion to $2.13 billion). Furthermore, if one adds back to 2016 cash flows (ex-working capital changes) the extraordinary $2.57 billion tax payment that Allergan made in the 2nd half of 2016 with respect to the Teva generic divestiture (the last row of the table, highlighted in yellow), we find that Allergan's $3.46 billion in cash flow for the trailing twelve months ended June 30, 2017 is 27% below the $4.72 billion figure for all of 2016.

In addition, 1st half 2017 underlying cash flows of $2.13 billion have only come it at $1.07 billion per quarter, far below the $1.5 to $2 billion cash flow run rate per quarter that management claims is its "normalized" cash flow figure (and, let us not forget, this number is before any capital expenditures, so a free cash flow figure for Allergan would be *far* below any claimed "normalized" cash from operations number). On a trailing twelve-month basis, Allergan has only produced $866 million of adjusted cash flow per quarter ($3.464 divided by 4), again vastly below the claimed normalized $1.5 to $2 billion quarterly run rate. Something is clearly not adding up. If Allergan's business is so vibrant, as Allergan's management claims, why have underlying adjusted cash flows on a trailing 6- and 12-month basis come in so far below the non-GAAP figures repeated cited by management?

C. Sources and Uses

Another way to examine Allergan's recent performance is by looking at aggregate cash inflows and cash outflows. Below is a chart showing the sources and uses of cash for the company for the twelve months ended June 30, 2017:

TTM SOURCES (AS OF 6/30/17)	AMOUNT	% OF TOTAL
Cash from operations	1,145.0	3.3%
Teva Sale	33,804.2	96.1%
Proceeds from sales of property, plant and equipment	23.1	0.1%
Proceeds from stock plans	189.5	0.5%
Excess tax benefit from stock-based compensation	20.4	0.1%
Effect of currency exchange rate changes on cash and cash equivalents	1.0	0.0%
TOTAL SOURCES	*35,183.2*	
TTM USES (AS OF 6/30/17)	AMOUNT	
Increase in Investments	1,587.8	4.6%
Additions to property, plant and equipment	285.8	0.8%
Additions to product rights and other intangibles	588.3	1.7%
Acquisitions of businesses, net of cash acquired	6,489.3	18.7%
Debt issuance and other financing costs	17.5	0.1%
Net Debt Reductions	9,419.3	27.1%
Payments of contingent consideration	602.4	1.7%
Repurchase of ordinary shares	15,044.3	43.2%
Dividends	751.1	2.2%
TOTAL USES	*34,785.8*	
REMAINDER (UNUSED FUNDS)	397.4	

(Source: Allergan SEC filings; Seven Corners calculations)

The most striking thing in the above table is that out of the over $35 billion in cash generated in the trailing twelve months, only $400 million remained as of June 30, 2017 (or ~$2 billion if one includes the increase in investments). By far the greatest portion of the proceeds (over 43%) was used to repurchase Allergan's stock. In addition just over a quarter of the proceeds went to pay down debt, and just under 1/5th of the proceeds was used for business acquisitions. Given that Allergan's enterprise value currently stands at approximately $100 billion, we can calculate that over one-third of the entire Allergan enterprise value has been recycled in just the past twelve months, highlighting the importance for shareholders of the capital allocation skills of the CEO.

We believe a prudent investor should stop and consider exactly why the CEO has made the allocation decisions highlighted above in the chart. Have these decisions, on a per-share basis, increased or decreased the value of the overall enterprise? Was it a wise decision to recycle such a large portion of the enterprise value in stock repurchases? What incentives did the CEO have to make these decisions the way he did? Would an entirely different capital allocation program (for example, prioritizing dividends instead of repurchases) have left shareholders better off?

If we just consider share repurchases, one should note that Allergan's CEO is highly incentivized to reduce the gross share count, regardless of whether it actually is an intelligent decision from the shareholders' viewpoint. Reducing the share count automatically causes non-GAAP Performance Net Income Per Share to increase, even if in aggregate Performance Net Income stagnates (as has been the case for the first half of 2017, with Performance Net Income Per Share up 20%, but aggregate Performance Net Income up only 2.65%). This benefits the CEO for a number reasons: *first*, because it will cause the stock price to be artificially propped up (most investors value a company using an earnings multiple, and other things being equal the higher the per share net income, the higher the resulting stock price), which will get those pesky shareholders off the CEO's back (CEOs who can get the stock up rarely get challenged by the actual owners of the company); *second*, a higher stock price means that the CEO's existing stock options and restricted shares are worth more then they would be absent a repurchase program; and *third*, because the CEO's annual compensation is keyed off of the non-GAAP Performance Net Income Per Share results, so the higher this metric can be boosted via buybacks, the higher the bonus the CEO banks.

Of course, the CEO will always publicly claim that the company is buying back stock because "our shares are undervalued" or "we view the repurchase of our stock as the best investment our company can make right now", etc. Don't be fooled, though—the real reasons are those listed in the paragraph immediately above. Moreover, by engaging in an accelerated repurchase program, the CEO can ratchet the non-GAAP numbers up even faster, since the share count is immediately reduced by the amount of the accelerated repurchase even though he shares are not actually repurchased on the open market immediately. Please see here for a detailed explanation of the mechanics of an ASR.

D. Organic Stagnation.

Allergan trumpets its 9% revenue increase in Q2 2017 as evidence that its "growth Pharma" business model is working. On the Q2 2017 earnings call, Allergan executives used the word "growth" no less than 29 times in their prepared remarks, referencing "revenue growth", "durable growth", "long-term growth drivers", "growth areas", "future growth", "growth trajectory" and "growth catalysts". Clearly they are trying to drive home a message—the gospel of growth. But is it actually true?

Below is a table showing organic revenues during Q2 2017 (to construct the table we used the information included in the company's Q2 2017 earnings release and removed revenues related to CoolSculpting, Alloderm, Vraylar and Namzaric, which Allergan deems "new products" in its earnings release, but left in Viberzi in an effort to be conservative[2]):

	Three Months Ended June 30, 2017					Three Months Ended June 30, 2017						
Product	US Specialized Therapeutics	US General Medicine	Int'l	Corp	TOTAL	US Specialized Therapeutics	US General Medicine	Int'l	Corp	TOTAL	$ CHANGE	% CHANGE
Botox®	574.0	0.0	242.1	0.0	816.1	502.2	0.0	217.5	0.0	719.7	96.4	13.4%
Restasis®	336.4	0.0	17.3	0.0	353.7	371.3	0.0	19.3	0.0	390.6	-36.9	-9.4%
Juvederm Collection **	126.2	0.0	137.3	0.0	263.5	117.6	0.0	107.3	0.0	224.9	38.6	17.2%
Lumigan®/Ganfort®	79.0	0.0	94.4	0.0	173.4	80.6	0.0	94.5	0.0	175.1	-1.7	-1.0%
Linzess®/Constella®	0.0	167.8	5.5	0.0	173.3	0.0	150.5	4.6	0.0	155.1	18.2	11.7%
Bystolic® /Byvalson®	0.0	150.7	0.5	0.0	151.2	0.0	150.3	0.4	0.0	150.7	0.5	0.3%
Alphagan®/Combigan®	96.4	0.0	42.7	0.0	139.1	96.0	0.0	44.2	0.0	140.2	-1.1	-0.8%
Eye Drops	50.7	0.0	70.7	0.0	121.4	49.1	0.0	72.0	0.0	121.1	0.3	0.2%
Namenda XR®	0.0	118.7	0.0	0.0	118.7	0.0	166.5	0.0	0.0	166.5	-47.8	-28.7%
Lo Loestrin®	0.0	113.0	0.0	0.0	113.0	0.0	101.0	0.0	0.0	101.0	12.0	11.9%
Breast Implants	61.3	0.0	41.1	0.0	102.4	51.7	0.0	40.2	0.0	91.9	10.5	11.4%
Estrace® Cream	0.0	90.1	0.0	0.0	90.1	0.0	97.2	0.0	0.0	97.2	-7.1	-7.3%
Viibryd®/Fetzima®	0.0	85.2	0.7	0.0	85.9	0.0	81.7	0.1	0.0	81.8	4.1	5.0%
Ozurdex ®	24.9	0.0	51.2	0.0	76.1	21.5	0.0	45.7	0.0	67.2	8.9	13.2%
Carafate ® /Sulcrate ®	0.0	59.2	0.7	0.0	59.9	0.0	50.3	0.6	0.0	50.9	9.0	17.7%
Asacol®/Delzicol®	0.0	45.6	12.8	0.0	58.4	0.0	119.8	11.0	0.0	130.8	-72.4	-55.4%
Zenpep®	0.0	50.5	0.0	0.0	50.5	0.0	43.0	0.0	0.0	43.0	7.5	17.4%
Saphris®	0.0	43.0	0.0	0.0	43.0	0.0	41.3	0.0	0.0	41.3	1.7	4.1%
Canasa®/Salofalk®	0.0	38.4	4.3	0.0	42.7	0.0	46.7	4.6	0.0	51.3	-8.6	-16.8%
Armour Thyroid	0.0	42.0	0.0	0.0	42.0	0.0	40.6	0.0	0.0	40.6	1.4	3.4%
Viberzi®	0.0	41.3	0.1	0.0	41.4	0.0	20.4	0.0	0.0	20.4	21.0	102.9%
Aczone®	41.0	0.0	0.1	0.0	41.1	54.1	0.0	0.1	0.0	54.2	-13.1	-24.2%
Teflaro®	0.0	33.0	0.0	0.0	33.0	0.0	35.2	0.0	0.0	35.2	-2.2	-6.3%
Rapaflo®	25.7	0.0	1.7	0.0	27.4	29.4	0.0	1.5	0.0	30.9	-3.5	-11.3%
Savella®	0.0	26.0	0.0	0.0	26.0	0.0	22.3	0.0	0.0	22.3	3.7	16.6%
SkinMedica®	25.4	0.0	0.0	0.0	25.4	29.1	0.0	0.0	0.0	29.1	-3.7	-12.7%
Dalvance®	0.0	15.2	1.2	0.0	16.4	0.0	10.2	0.0	0.0	10.2	6.2	60.8%
Latisse®	13.3	0.0	2.4	0.0	15.7	17.7	0.0	2.2	0.0	19.9	-4.2	-21.1%
Kybella® /Belkyra®	12.7	0.0	2.0	0.0	14.7	12.7	0.0	0.6	0.0	13.3	1.4	10.5%
Avycaz®	0.0	14.5	0.0	0.0	14.5	0.0	13.7	0.0	0.0	13.7	0.8	5.8%
Lexapro®	0.0	13.1	0.0	0.0	13.1	0.0	16.5	0.0	0.0	16.5	-3.4	-20.6%
Tazorac®	12.8	0.0	0.2	0.0	13.0	23.4	0.0	0.2	0.0	23.6	-10.6	-44.9%
Minastrin® 24	0.0	11.4	0.0	0.0	11.4	0.0	83.0	0.6	0.0	83.6	-72.2	-86.4%
Liletta®	0.0	6.6	0.0	0.0	6.6	0.0	5.7	0.0	0.0	5.7	0.9	15.8%
Other	71.7	161.7	104.5	6.2	344.1	32.5	125.2	89.8	14.2	261.7	82.4	31.5%
Total Net Revenues	1,551.5	1,327.0	833.5	6.2	3,718.2	1,488.9	1,421.1	757.0	14.2	3,681.2	37.0	1.0%

(Source: Allergan SEC filings; Seven Corners calculations)

Organic revenue growth was just 1% in Q2 of 2017, even including all revenues in the "Other" category and all Botox revenues as organic (Allergan provides no disclosure to enable us to determine organic versus non-organic growth with respect to these two categories).

[2] In its earnings release, Allergan states that "Total net revenues were $4.0 billion, a 9 percent increase from the prior year quarter, driven by BOTOX®, JUVEDERM Collection®, the addition of ALLODERM® and CoolSculpting® and new products, including VRAYLARTM, NAMZARIC® and VIBERZI®".

Below is a table showing organic revenues during the first six months of 2017 (constructed in a similar manner to the table immediately above):

	Six Months Ended June 30, 2017					Six Months Ended June 30, 2017						
Product	US Specialized Therapeutics	US General Medicine	Int'l	Corp	TOTAL	US Specialized Therapeutics	US General Medicine	Int'l	Corp	TOTAL	$ CHANGE	% CHANGE
Botox®	1,083.4	0.0	446.6	0.0	1,530.0	957.7	0.0	399.5	0.0	1,357.2	172.8	12.7%
Restasis®	645.2	0.0	31.2	0.0	676.4	670.0	0.0	34.3	0.0	704.3	-27.9	-4.0%
Juvederm Collection **	246.0	0.0	259.5	0.0	505.5	220.3	0.0	207.4	0.0	427.7	77.8	18.2%
Lumigan®/Ganfort®	153.3	0.0	180.3	0.0	333.6	162.1	0.0	182.6	0.0	344.7	-11.1	-3.2%
Linzess®/Constella®	0.0	315.4	10.4	0.0	325.8	0.0	287.6	8.4	0.0	296.0	29.8	10.1%
Bystolic® /Byvalson®	0.0	290.5	1.0	0.0	291.5	0.0	313.9	0.8	0.0	314.7	-23.2	-7.4%
Alphagan®/Combigan®	182.8	0.0	85.0	0.0	267.8	180.9	0.0	86.0	0.0	266.9	0.9	0.3%
Namenda XR®	0.0	240.7	0.0	0.0	240.7	0.0	339.6	0.0	0.0	339.6	-98.9	-29.1%
Eye Drops	98.5	0.0	136.0	0.0	234.5	89.9	0.0	139.2	0.0	229.1	5.4	2.4%
Lo Loestrin®	0.0	212.8	0.0	0.0	212.8	0.0	190.3	0.0	0.0	190.3	22.5	11.8%
Breast Implants	115.6	0.0	78.7	0.0	194.3	98.1	0.0	76.9	0.0	175.0	19.3	11.0%
Estrace® Cream	0.0	163.5	0.0	0.0	163.5	0.0	177.8	0.0	0.0	177.8	-14.3	-8.0%
Viibryd®/Fetzima®	0.0	157.7	1.1	0.0	158.8	0.0	165.0	0.1	0.0	165.1	-6.3	-3.8%
Ozurdex ®	47.4	0.0	102.3	0.0	149.7	40.9	0.0	86.8	0.0	127.7	22.0	17.2%
Asacol®/Delzicol®	0.0	103.2	24.9	0.0	128.1	0.0	225.7	26.3	0.0	252.0	-123.9	-49.2%
Carafate ® /Sulcrate ®	0.0	117.9	1.4	0.0	119.3	0.0	111.3	1.1	0.0	112.4	6.9	6.1%
Zenpep®	0.0	97.0	0.0	0.0	97.0	0.0	92.6	0.0	0.0	92.6	4.4	4.8%
Aczone®	81.6	0.0	0.1	0.0	81.7	87.1	0.0	0.1	0.0	87.2	-5.5	-6.3%
Canasa®/Salofalk®	0.0	76.7	8.7	0.0	85.4	0.0	87.8	8.6	0.0	96.4	-11.0	-11.4%
Saphris®	0.0	80.3	0.0	0.0	80.3	0.0	82.8	0.0	0.0	82.8	-2.5	-3.0%
Armour Thyroid	0.0	79.3	0.0	0.0	79.3	0.0	82.7	0.0	0.0	82.7	-3.4	-4.1%
Viberzi®	0.0	72.8	0.1	0.0	72.9	0.0	24.4	0.0	0.0	24.4	48.5	198.8%
Teflaro®	0.0	63.6	0.0	0.0	63.6	0.0	68.6	0.0	0.0	68.6	-5.0	-7.3%
Rapaflo®	51.6	0.0	3.7	0.0	55.3	62.4	0.0	2.7	0.0	65.1	-9.8	-15.1%
SkinMedica®	53.4	0.0	0.0	0.0	53.4	55.7	0.0	0.0	0.0	55.7	-2.3	-4.1%
Minastrin® 24	0.0	52.5	0.0	0.0	52.5	0.0	162.6	1.4	0.0	164.0	-111.5	-68.0%
Savella®	0.0	50.3	0.0	0.0	50.3	0.0	46.0	0.0	0.0	46.0	4.3	9.3%
Tazorac®	36.2	0.0	0.4	0.0	36.6	40.5	0.0	0.4	0.0	40.9	-4.3	-10.5%
Kybella® /Belkyra®	27.8	0.0	3.5	0.0	31.3	24.0	0.0	1.1	0.0	25.1	6.2	24.7%
Latisse®	26.9	0.0	4.3	0.0	31.2	37.5	0.0	4.3	0.0	41.8	-10.6	-25.4%
Lexapro®	0.0	26.5	0.0	0.0	26.5	0.0	35.2	0.0	0.0	35.2	-8.7	-24.7%
Dalvance®	0.0	24.8	1.2	0.0	26.0	0.0	16.4	0.0	0.0	16.4	9.6	58.5%
Avycaz®	0.0	25.8	0.0	0.0	25.8	0.0	22.1	0.0	0.0	22.1	3.7	16.7%
Liletta®	0.0	13.8	0.0	0.0	13.8	0.0	10.6	0.0	0.0	10.6	3.2	30.2%
Enablex®	0.0	1.9	0.0	0.0	1.9	0.0	12.8	0.0	0.0	12.8	-10.9	-85.2%
Namenda® IR	0.0	0.1	0.0	0.0	0.1	0.0	9.9	0.0	0.0	9.9	-9.8	-99.0%
Other	129.7	329.5	189.2	14.0	662.4	60.5	295.3	162.3	19.7	537.8	124.6	23.2%
Total Net Revenues	3,197.0	2,773.5	1,595.8	14.0	7,159.6	2,787.6	2,902.8	1,430.3	-36.6	7,098.6	61.0	0.9%

(Source: Allergan SEC filings; Seven Corners calculations)

Organic revenue growth was just 0.9% in the first half of 2017, even including all revenues in the "Other" category and all Botox revenues as organic (again, Allergan provides no disclosure to enable us to determine organic versus non-organic growth with respect to these two categories).

The "growth" part of Allergan's "growth Pharma" business model seems to be missing recently—at least with respect to organic growth.

III. Conclusion

Although headlines may suggest that Allergan is experiencing healthy growth in both revenues and income, a closer look at the actual numbers reveals an entirely different story. Even if one uses Allergan's management's cherry picked non-GAAP calculations, one finds that "Performance Net Income" actually declined slightly in the first half of 2017 versus 2016 and was up just under 3% in Q2 year-over-year. Moreover, if we use much more realistic assumptions in calculating non-GAAP net income, we find that this metric has declined precipitously in both the second quarter and first half of 2017 (down 34% and 47%, respectively), in each case compared with 2016. In addition, cash flow from operations (adjusted to back out working capital changes and the extraordinary 2016 Teva divestiture tax payment) shows a similar decline, down 37% in the first half of 2017 versus the prior year and down 27% on a trailing twelve-month basis versus calendar 2016. Finally, organic growth seems to have come almost entirely to a half in the first half of 2017, with the vast majority of Allergan's supposed "growth" coming from acquisitions, not its existing product portfolio.

The inescapable conclusion from our analysis is that Allergan's underlying business has either stagnated (in terms of revenues) or declined significantly (in terms of income and cash flows) in 2017 versus 2016, despite management's assertions to the contrary in their earnings press releases and conference calls. The GAAP financials, along with our reasonable adjustments thereto to adjust out non-operational noise, tell this story quite clearly. Paradoxically, though, Allergan trades at an obscenely high multiple of our conservatively calculated non-GAAP net income per share—approximately 47X the 1st half 2017 adjusted EPS run rate, most likely because the investment community continues to unquestioningly accept management's misleading non-GAAP metrics. No intelligent investor, however, need mindlessly accept these numbers.

The Intelligent Investor opens with the following quote from Horace: "Many shall be restored that now are fallen and many shall fall that now are in honor". While Allergan may now be in honor among investors, in actuality we believe it many have already fallen. Investors just don't seem to realize it yet. We therefore reiterate our previously issued $117 target price for Allergan shares, with expected downside of approximately 50% from the current market price.

IV. Disclaimer

As of the publication date of this report, Seven Corners Capital Management and its affiliates (collectively, "Seven Corners") have short positions in Allergan Plc ("Allergan"). In addition, others that contributed research to this report and others that we have shared our research with (collectively with Seven Corners, the "Authors") likewise may have short positions in, and/or own options on, Allergan. The Authors stand to realize gains in the event that the price of the stock decreases. Following publication of the report, the Authors may transact in the securities of the company covered herein. All content in this report represent the opinions of Seven Corners. The Authors have obtained all information herein from sources they believe to be accurate and reliable. However, such information is presented "as is," without warranty of any kind—whether express or implied. The Authors make no representation, express or implied, as to the accuracy, timeliness, or completeness of any such information or with regard to the results obtained from its use. All expressions of opinion are subject to change without notice, and the Authors do not undertake to update or supplement this report or any information contained herein.

This document is for informational purposes only and it is not intended as an official confirmation of any transaction. All market prices, data and other information are not warranted as to completeness or accuracy and are subject to change without notice. The information included in this document is based upon selected public market data and reflects prevailing conditions and the Authors' views as of this date, all of which are accordingly subject to change. The Authors' opinions and estimates constitute a best efforts judgment and should be regarded as indicative, preliminary and for illustrative purposes only.

Any investment involves substantial risks, including, but not limited to, pricing volatility, inadequate liquidity, and the potential complete loss of principal. This report's estimated fundamental value only represents a best efforts estimate of the potential fundamental valuation of a specific security, and is not expressed as, or implied as, assessments of the quality of a security, a summary of past performance, or an actionable investment strategy for an investor.

This document does not in any way constitute an offer or solicitation of an offer to buy or sell any investment, security, or commodity discussed herein or of any of the affiliates of the Authors. Also, this document does not in any way constitute an offer or solicitation of an offer to buy or sell any security in any jurisdiction in which such an offer would be unlawful under the securities laws of such jurisdiction. To the best of the Authors' abilities and beliefs, all information contained herein is accurate and reliable. The Authors reserve the rights for their affiliates, officers, and employees to hold cash or derivative positions in any company discussed in this document at any time. As of the original publication date of this document, investors should assume that the Authors are short shares of Allergan and may have positions in financial derivatives that reference this security and stand to potentially realize gains in the event that the market valuation of the company's common equity is lower than prior to the original publication date. These affiliates, officers, and individuals shall have no obligation to inform any investor or viewer of this report about their historical, current, and future trading activities. In addition, the Authors may benefit from any change in the valuation of any other companies, securities, or commodities discussed in this document. Analysts who prepared this report are compensated based upon (among other factors) the overall profitability of the Authors' operations and their affiliates. The compensation structure for the Authors' analysts is generally a derivative of their effectiveness in generating and communicating new investment ideas and the performance of recommended strategies for the Authors. This could represent a potential conflict of interest in the statements and opinions in the Authors' documents.

The information contained in this document may include, or incorporate by reference, forward-looking statements, which would include any statements that are not statements of historical fact. Any or all of the Authors' forward-looking assumptions, expectations, projections, intentions or beliefs about future events may turn out to be wrong. These forward-looking statements can be affected by inaccurate assumptions or by known or unknown risks, uncertainties and other factors, most of which are beyond the Authors' control. Investors should conduct independent due diligence, with assistance from professional financial, legal and tax experts, on all securities, companies, and commodities discussed in this document and develop a stand-alone judgment of the relevant markets prior to making any investment decision.