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PRESENTATION

David Risinger - *Morgan Stanley - Analyst*

Good morning, everyone. Our next company discussion is Pfizer. And please note that we need to refer you to disclosures at MorganStanley.com/researchdisclosures.

It's a pleasure for me to welcome Frank D'Amelio who is the CFO of Pfizer. He originally joined Pfizer in September of 2007 from Lucent where he was CFO and responsible for the turnaround of Lucent and the integration of the Alcatel-Lucent merger. Prior to the Alcatel merger, he was Chief Operating Officer of Lucent.

And at Pfizer, Frank has overseen Pfizer's delivery of Wyeth synergies, financial results and rising returns to shareholders. And, Frank, thanks so much for taking the time out of your busy schedule to join us today. Why don't I turn it over to you for a couple of opening remarks and then we will go right into the Q&A.

Frank D'Amelio - *Pfizer Inc. - EVP, Business Operations, & CFO*

Sure. Good morning, good day, everybody. I thought I would just make a couple of quick comments and then we'll get into the Q&A. First I just thought I would comment on our last quarter results which were good.

Hopefully you all noticed that in terms of the numbers that we printed. Some of the other things that we have been working on, we announced the sale of our nutrition business to Nestle for \$11.85 billion and we said we expect to complete that in the first half of 2013. We are continuing to work on the potential IPO of our animal health business. We filed our S-1 in August -- I believe it was August the 13th.

We continue to be disciplined with our capital allocation, hopefully you see that in terms of the actions we've been taking with dividends, with share buybacks and the like. And those are drumbeats that hopefully you will see us continue to execute on day to day. So with that, Dave, I will answer any questions you have.

QUESTIONS AND ANSWERS

David Risinger - *Morgan Stanley - Analyst*

Great. Well, maybe you could just talk about the longer-term vision for Pfizer as you see it and what your key objectives are?

Frank D'Amelio - *Pfizer Inc. - EVP, Business Operations, & CFO*

Sure. So to me it's really quite simple. When I think about the long-term vision, it's we want to be a company that delivers steady predictable earnings growth over time. And the way that we want to do that is we want to have earnings growth, earnings performance that's supported by our growth business, that's made up of our innovative patent protected products and powered by a productive, efficient R&D engine.



And then we also want a value business that is really a strong generator of operating cash flow but isn't nearly as dependent on R&D. And obviously we would want business models that optimize each of those businesses. So that is how I think about where are we going forward on a vision basis.

David Risinger - *Morgan Stanley - Analyst*

And with respect to the value business, some have speculated that you could exit that business. Maybe you could speak to how you've thought through that to date and what the opportunities and challenges might be for value realization out of that strong cash flow value business.

Frank D'Amelio - *Pfizer Inc. - EVP, Business Operations, & CFO*

Sure. So, first, I want to bump it up a level and then I will answer your question. I will be in investor meetings and sometimes I will get asked a question, and this isn't specific to established products, but Frank, why did you all sell the nutrition business? Isn't it a good business?

And the answer is, it's a really good business -- in fact, a very good business. But we believe -- I believe that we are unlocking trapped value by monetizing these assets. If you look at the value that a business like nutrition can get on its own like we did with the announced sale of nutrition to Nestle versus what kind of value it is generating inside of Pfizer, we think we can unlock trapped value.

So when all is said and done, the objective for this is how do we maximize after-tax return to our shareholders? That is what all of this is all about. So what we do is we regularly look at our portfolio and with the objective of what can we do to maximize value to our shareholders, what can we do to maximize after-tax return to our shareholders.

Now when we completed our strategic review a few years ago, we talked about what we would do and what we weren't going to do. One of the things we said at that time was we were going to keep the established products business. But please know we regularly review the portfolio and we will do what we believe is right on an after-tax return to our shareholders.

So the fact that at that time we said it was something we were going to not pursue is not in any way a precursor for what we may or may not do on a going forward basis. And let me make a couple other comments on this, Dave, see if I am answering your question.

One of the questions I will get asked about the established products business is, Frank, is it possible to separate the business? It's very intertwined with the business, is it possible to separate that business? My answer is it's possible but it is not easy. And there is really two areas I think in particular that represent challenges. I will give you kind of high level.

One is I will call it operating platforms and then the second one is geography and let me just drill down a little bit on each of those. So if you look at operating platforms, functions or areas like manufacturing, systems, we don't have factories that are dedicated to established products, we have factories that support multiple business units. So there would be some challenges in I will call it the operating platforms.

And then in geographies, if you look at some of the emerging markets, for example, established products are very intertwined with our emerging markets business unit. So I call that challenges but is it possible? Yes. And is it doable? Yes. So if we chose to do that, we could do that.

David Risinger - *Morgan Stanley - Analyst*

And have you -- just to follow up on that, have you taken any steps with respect to operating platforms or geographical management in that direction?



Frank D'Amelio - Pfizer Inc. - EVP, Business Operations, & CFO

So, what we have really been focusing on in terms of those operating platforms to date, Dave, has been synergies. You follow? I mean we have really been driving synergies. So if you look, whether it be the Wyeth acquisition, the King acquisition, if you look at our cost structure -- last quarter if you looked year over year, in Q2 of 2011 our total costs and expenses were \$9.9 billion, Q2 of 2012 \$8.3 billion.

Now, that was a 16% reduction; now 4% of that, \$396 million, was foreign exchange. So that wasn't operational, put that aside. So \$9.9 billion to \$8.3 billion is \$1.3 billion, \$400 million of foreign exchange, almost \$1 billion was operational. So we have really been driving operational synergies which I think has been the right thing to do. So that is really what we have been focusing on.

David Risinger - Morgan Stanley - Analyst

Got it, and congrats on the cost cutting success.

Frank D'Amelio - Pfizer Inc. - EVP, Business Operations, & CFO

Thank you.

David Risinger - Morgan Stanley - Analyst

It has been very impressive. With respect to cash flow and the balance sheet, if you could just remind us where your cash and debt stood at the end of the June quarter? And then frame the operating cash flow and free cash flow of the Company before we think about potential use of divestiture proceeds?

Frank D'Amelio - Pfizer Inc. - EVP, Business Operations, & CFO

So, at the end of Q2 we had about \$35 billion to \$36 billion of cash and investments, about \$37 billion to \$38 billion of debt. So, give or take the cash and the debt we are roughly the same, pretty much net neutral, slightly -- \$1 billion or \$2 billion net debt but relatively neutral.

In terms of operating cash, what I have said, the guidance we've provided for the year is operating cash flow of about approximately \$19 billion. And then obviously there are uses of that cash in terms of investing in the business, mergers and acquisition, business development, buybacks, dividends and the like. But that is how I look at the cash flow that we generate.

David Risinger - Morgan Stanley - Analyst

Got it. You have said that the case to beat in terms of divestiture proceeds is share repurchase. But the Company, given the roughly \$19 billion in operating cash flow that should continue, maybe it's slightly less when you exit certain businesses. But we are looking at high teens operating cash flow going forward.

Seems like you have a significant amount of cash flow to purchase shares before potentially investing divestiture proceeds and share repurchase. So maybe you could talk about the two. So taking the operating cash flow and buying back stock and repurchasing shares with divestiture proceeds.

Frank D'Amelio - Pfizer Inc. - EVP, Business Operations, & CFO

Sure. So the way I think about this is, I call it, it's an "and" and not an "or". So what do I mean by that? If you look, put the divestitures aside -- to get your specific question -- we have been buying back a significant amount of our shares. If you look last year, we bought back \$9 billion of our shares last year at an average price of \$19.63 a share.



Through July 30 of this year, we have repurchased \$3 billion worth of our shares and I said on the call we are driving towards \$5 billion for the year. That is all separate and distinct from the divestitures, Dave, to your question. So to the extent that when we complete the sale of nutrition that \$11.85 billion, once again what do we want to do with that? We want to maximize return to shareholders on an after-tax basis.

The case to beat for the use of those proceeds are share buybacks. So that would be in addition to the \$9 billion in 2011 and the \$5 billion that I've said for 2012. So that is why I say it is an "and" and not an "or", it's not like one replaces the other.

David Risinger - Morgan Stanley - Analyst

Got it. And maybe you could talk about dividends, your current annual dividend and the opportunity to raise that in the future. It seems like your peers are raising their targets in terms of dividend payout ratios. At the same time, though, you are obviously exiting some businesses that generate substantial cash flow, which may constrain the ability to raise the total dollar dividend payments for the Company.

Frank D'Amelio - Pfizer Inc. - EVP, Business Operations, & CFO

Okay. So I want to give a little bit of history on this and then I will get to the question. So you have got to remember when you look at our dividend, in 2009 when we announced the Wyeth acquisition we did a couple of things to our capital structure. One of the things we did is we had cut the dividend in half. And we also raised our tax rate, but we cut the dividend in half, right.

So we cut the dividend at that time -- I think it was January of 2009 from \$1.28 to \$0.64 a share. And then if you look from that \$0.64 a share to this year, in the last three years we have increased the dividend from \$0.64 to \$0.72, \$0.72 to \$0.80, \$0.80 to \$0.88, so that's 12.5%, 11% and 10% dividend increases, respectively, over the last three years. So that is kind of a history in terms of where we were, where we are today and a little bit of why, which was capital planning relative to the Wyeth acquisition.

Now what you asked me though is what about going forward. So now let me get to the going forward question, which is, going forward we get the importance of the dividend. We get the importance of the dividend to our owners and we expect to increase the dividend on a going forward basis.

In terms of the amount of the increase, that will be determined by multiple factors, the amount of operating cash flow that we generate, the overall performance of the business and then we will look at other metrics like yield and the like.

And just one other thing you mentioned about the industry peers, and I won't comment on any specific peers, but one of the things you have to remember is the payout ratio can go up even though the dividend hasn't increased because earnings can be going down.

So that is why I always say you can't look at a single metric. When you look at these things you've got to get underneath the underlying drivers of what is causing the numbers to move. In many instances, we have some peers whose earnings are declining because of LOEs and the like. So if you don't do anything to dividend, the payout ratio goes up.

So we will look at what our peers do, but we will do what we think is right and we will look at the metrics that I have discussed. But the one thing I will say is we expect to increase the dividend going forward.

David Risinger - Morgan Stanley - Analyst

Got it. Let me pause there and see if there are any questions from the audience. Okay, maybe we can just ask a few more financial questions and then go into some product questions. So you've achieved a tremendous amount of cost cutting over the last several years. How should we think about future cost cutting potential from where you are going to end up at the end of this year, what remains to be cut and in what areas?



Frank D'Amelio - Pfizer Inc. - EVP, Business Operations, & CFO

Sure. So once again I want to give a little history. I always like to set context when I answer these kinds of questions. And then I will talk about where do we go from here, which is the -- well, the meat of the question.

So once again back to the Wyeth acquisition because I think it will paint an interesting picture and I will start with workforce. Because one of the things I always look at relative to cost structure is workforce, which, by the way, is extremely difficult in terms of reducing because you are impacting individuals, right. On the other hand, it is a massive part of any company's cost structure.

So if you look, when we announced the Wyeth acquisition again, the combined company back in January of 2009 had 130,000 people, Pfizer had roughly 80,000 people, Wyeth had roughly 50,000. When we announced that acquisition, we said at the time we targeted a 15% reduction in the workforce in approximately three years, so 15% on 130,000 is 19,500 and approximately three years would have been the end of 2012. I mean that is what we said.

At the end of last quarter, so Q2 of 2012, so two and a half years later our workforce was 101,000 so 29,000 workforce reduction or 22% in two and a half years. And by the way, that is a net number because we have been adding resources in certain parts of the organization, even with those adds, the net reduction was 29,000. So I always like to say that just to give people a feel for the work we have been doing and our ability to execute in this area.

Now let me answer your question because that doesn't answer your question. But I always like to use that because I think it's a good leading indicator of what we have been able to do and hopefully what we can continue to do.

So if you say to me, all right, Frank, you have done that, what about going forward, what are the opportunities? I still think we have significant opportunities. Let me give you a couple of examples and then I will end with a baseball analogy, Yankees are playing the Red Sox tonight so we will do a baseball analogy.

I think, one, manufacturing. We think there are approximately 10 facilities that we will exit over the next couple years, that is a significant item. We continue to have opportunities with our real estate. We have a huge real estate portfolio; we've done a really good job of reducing our gross square footage, there is still a significant opportunity to do more.

I think all of our corporate centers, our enabling functions, there have -- there has been significant progress made. There are still opportunities to do more on a going forward basis. I think our marketing efforts globally, our promotional spend, there is continued -- I think there are opportunities there to be more efficient, to be more productive, to continue to drive savings to the bottom line.

So those are just some examples, Dave, of some of the things that we can continue to do on a going forward basis. So if you were looking at this as a baseball game, a major league game has nine innings, we are clearly not in the early innings, but we are not in the late innings.

I think we are still in the middle innings and I still think we have opportunities to continue to drive more cost savings and productivity improvements in the Company. And the nice thing about this is we have to execute and do it and then hopefully you will see that when we produce our results. But that is what we are all about doing.

David Risinger - Morgan Stanley - Analyst

That's great. So it sounds like net cost reductions still to come even though you have experienced tremendous net cost reductions to date.

Frank D'Amelio - Pfizer Inc. - EVP, Business Operations, & CFO

Yes, there is still more we can do. No doubt.

David Risinger - Morgan Stanley - Analyst

Maybe changing to the pipeline, obviously given your role and your position within the Company, even though it is not your responsibility, you are privy to the profile of the products and what is most exciting. So I would love to hear your perspective on the late stage pipeline. I'm assuming you mentioned Eliquis, but other key products to watch in coming years.

Frank D'Amelio - Pfizer Inc. - EVP, Business Operations, & CFO

Sure. So I won't mention Eliquis and tofa specifically, although I will come back to tofa for some additional indications that we are looking at. But in terms of the late stage pipeline there are several I will mention.

So in oncology there is dacomitinib, which is for lung cancer, it is in Phase III; there is inotuzumab, which is for non-Hodgkin's lymphoma, which is Phase III; there is CDK4/6, which is for breast cancer, we expect that to move to Phase III next year; there is the meningitis B vaccine that we actually expect to move into Phase III this year.

There is PCSK9 which is an anti-body for cholesterol, we had a positive proof of concept for that in Phase IIa that is now moving into Phase IIb. The Phase IIa positive proof of concept was an intravenous formulation; the Phase IIb will be a subcutaneous formulation. So that is another key compound.

And then on tofacitinib, in addition to rheumatoid arthritis, which I assume everyone knows about, we are also looking at additional indications in ulcerative colitis and psoriasis. So those would be the ones that I would mention in addition to tofacitinib and to Eliquis.

David Risinger - Morgan Stanley - Analyst

Great, so thank you very much. And maybe you could talk about the financial management of R&D given your role. And it is obviously extremely hard to assess return on capital in R&D since you start to develop compounds many, many years before you get a final read out. But how have you been overseeing the financial management of R&D and any changes you have made in recent years?

Frank D'Amelio - Pfizer Inc. - EVP, Business Operations, & CFO

So once again on this question I want to provide some context and this will be the third time I do this and I apologize, but the context I think helps paint the picture. So I want to go back to the Wyeth acquisition again because it gives you all a feel for the rhythm of the numbers, right.

So once again, you back to January of 2009, the combined spend of the two companies on a pro forma basis in 2008 was \$11 billion. I want to make sure I say that again, \$11 billion. \$7.5 billion was Pfizer give or take, \$3.5 billion was Wyeth. If you look at our latest guidance on R&D for this year, which takes into account the Nexium over-the-counter agreement, our R&D guidance range for the year is \$6.75 billion to \$7.25 billion.

So take the midpoint, which is \$7 billion, so we have taken that combined R&D spend from what was \$11 billion to approximately \$7 billion in less than three years. So the question becomes, how did we do that and I'll start getting to your question now, Dave.

What we really did is we looked at that spend and said, okay, we really asked ourselves three specific questions in terms of how to drive the portfolio on a going forward basis. The first question was, where are there large areas of unmet medical need? Question one. Question two was, where could those large areas of unmet medical need translate into real value for patients and for our shareholders?

And then question three was, and could we be -- given one and two, could we play? Could we be successful in that space? Because you could have one and two, but if you don't have a hand to play what do you do? Or if you have a weak hand to play the question is, can we supplement the hand and make it strong so that we can play in that space? Right?



So those were the three questions we really zoomed in on to really try to get at how do we really start to improve the return on our R&D investment on the return on capital. That led us to several conclusions, the biggest was what were kind of the strategic key therapeutic areas that we needed to play in? And then quite frankly, which ones did we need to not play in?

So what did we decide to play in? Pain, oncology, neuroscience, immunology and inflammation, CVMED, vaccines, rare diseases. But we also exited certain therapeutic areas like allergy and respiratory, urology, to name a few. By doing that, we are really able to quite frankly not only significantly reduce the spend, but in my mind actually make that spend more productive than what the previous spend level was.

So I think the productivity we will get out of the current spend level will exceed -- I think significantly exceed the productivity we would have gotten out of the bigger prior spend level because of how we focused with those parameters that we kind of did, and it was all bottoms up, right. Then we've done a few other things but this is what you are looking for in terms of spend.

David Risinger - Morgan Stanley - Analyst

Yes, thank you.

Frank D'Amelio - Pfizer Inc. - EVP, Business Operations, & CFO

Then we've also done some other things. So several years ago, you go back five, six, seven years ago, all of the R&D spend was in a functional organization called WRD, worldwide research and development -- not that that was good or bad, it was just what it was. If you look today we have really partitioned the spend.

So our research and development spend through proof of concept is in the research organization. But then once it hits proof of concept, it has to be bought up by a business unit. And by the way, you understand that beyond proof of concept you get into Phase III trials, that is where the big crank is on spending.

So the business unit that has to buy that up has to fund the development spend. It is in their budget, it is in their P&L. It creates a nice constructive tension in the process as the compound moves through the various stages to hopefully ultimate submission and approval. So we have done things like that.

And quite frankly I could spend an hour on all the things we have done on R&D. We have changed compensation. If you look at our R&D colleagues, a significant portion now of their annual equity grants are based on R&D specific metrics. R&D specific metrics, so proof of concepts delivered, products submitted for approval, Phase III starts, products actually approved.

So we have done things like that to once again hopefully drive the right focus and behavior relative to the R&D productivity of the Company. So those are some of the things that we have done to really get after this.

David Risinger - Morgan Stanley - Analyst

That's very helpful, thank you. And then maybe you could speak to the potential for M&A going forward. Once again, you have tremendous cash flow and you have additional cash coming in. How do you see the landscape for transactions?

Frank D'Amelio - Pfizer Inc. - EVP, Business Operations, & CFO

So I will make a couple of comments on this, just a couple of high-level comments and then I will drill down. So first, the way I always think about mergers and acquisitions business development is they're never a strategy in and of themselves, they are an enabler of our strategies, right, kind of point one.

And then point two is, you have heard Ian and me talk about -- although we never say never, the focus right now is really on bolt-on acquisitions. You have heard us talk about bolt-on acquisitions, it continues to remain on bolt-on acquisitions.

So now let me and so the question, which is, where are the focus areas for our M&A? I would say there is two primary focus areas, one is in support of those key strategic therapeutic areas that I just ran through, once again -- pain, oncology, neuroscience, immunology, inflammation, CVMED, vaccines, rare diseases, so that would be one area of focus. And the other one would be key geographies. And for us that is the emerging markets.

So if you look, we have been taking kind of I'll call it a local solution to local market approach. So what does that translate to? Teuto in Brazil, the Hisun joint venture in China, the recent announcement with Mylan in Japan. So a local solution to local market approach because emerging markets aren't some compilation of markets, they are individual markets that we approach on a local basis.

You have also seen us announce a couple of deals in the consumer products space, Alacer earlier in the year, that is the Emergen-C product, and then most recently the over-the-counter global agreement with Nexium. So I think those will be the areas you will see us continue to focus on, key therapeutic areas, key geographies.

And the one thing that we will do is hopefully what you have seen us doing, which is we will continue to be opportunistic, we will continue to be disciplined and prudent in our allocation to capital on business development.

David Risinger - Morgan Stanley - Analyst

Great. There is a question here.

Unidentified Audience Member

You had mentioned on the balance sheet you are now kind of net neutral on debt and cash.

Frank D'Amelio - Pfizer Inc. - EVP, Business Operations, & CFO

Yes, net debt by a couple of billion.

Unidentified Audience Member

Net debt by a couple billion. And I guess I wondered if you could give us some insight into your thinking about it? You have this fascinating phenomenon with Pfizer where your dividend yield is actually exceeding your cost of long-term debt even on a pre-tax basis.

If you look even yesterday, some of your peers issued some very low rate kind of 10 and 30 year paper. And I wondered how does that factor into your thinking about the balance sheet, if it does? It seems to us that it might present some interesting opportunities.

And secondly, if you are sort of net neutral on a net debt basis should we expect anything that it is an impending maturity at the very least would be refinanced given these low rates? And secondly, is there any propensity to consider taking up the leverage for potentially accretive uses like buying back shares given the metric that I just threw out?

Frank D'Amelio - Pfizer Inc. - EVP, Business Operations, & CFO

Yes. So, let me see if I answer the question. I had trouble hearing the first part of the question, so let me answer everything and if I missed it --.



Unidentified Audience Member

(Inaudible - microphone inaccessible)?

Frank D'Amelio - Pfizer Inc. - EVP, Business Operations, & CFO

Yes, would you please? The second part I got; I didn't hear the first part.

Unidentified Audience Member

Right, I guess the first part was I was observing how your long-term cost of borrowing kind of are way below even on a pre-tax basis your dividend yield on your stock. If you look over your 30 year or 10 year debt trade and where some of your peers are showing.

So I said how does that factor into your thinking about the balance sheet longer-term? And at the very least if you're net debt neutral, would we expect that any near-term maturities would at least be extended and refinanced given those rates? And when might that speak to other opportunities in the evolution of your balance sheet going forward?

Frank D'Amelio - Pfizer Inc. - EVP, Business Operations, & CFO

Okay, I got it. So, we don't have any maturities in 2012, just to be crystal clear. Now we had a maturity that we prepaid actually for 2012 in 2011, I think we did that -- that was done in the fourth quarter. We do have some maturities coming up in 2013, there is actually two maturities coming up give or take for about \$4 billion, give or take, it is roughly \$4 billion.

I don't want to -- I am not going to say today what I am going to do in 2013, but we will consider all options including, by the way, rolling that debt over, which is what you asked me. But I'm not going to declare today what we will or won't do. But clearly rolling the debt over is something that we are evaluating for the reasons that you talked about, kind of point one.

Point two in terms of the thought process on leveraging up to buy back shares, I think that was the way you phrased the question. My thought process on that is, we are buying back a significant amount of shares without leveraging up the balance sheet.

Quite frankly \$1 billion in 2010, \$9 billion in 2011, we said \$5 billion this year -- none of that factors in the \$11.85 billion from Nestle, nor the potential proceeds from an animal health separation regardless of what kind of form that takes. I have got to be careful what I say on animal health; we are in a quiet period for that.

So my reaction is I can accomplish a major buyback program and not lever up the balance sheet, which gives me flexibility with that balance sheet to potentially use it for whatever else I need to use it for. So I can have my cake and eat it too I think relative to buybacks and leveraging up the balance sheet.

Then in terms of the cost of our long-term debt, I think this was the first question and the rates I am paying on that, which I always look at at an after-tax basis and compare that to the dividend which is really kind of an after-tax number -- you've almost got to gross it up, right, because it is not tax-deductible.

We do those analytics all the time in terms of deciding where is best to deploy capital. And you also understand we have lots of options on our debt including swaps from fixed rate, the floating rate to take advantage of the current low interest environment and we do lots of that where it tactically makes sense to do so.



David Risinger - Morgan Stanley - Analyst

Great. Well, we are out of time, I apologize. Layton, you can come on up and ask here. Thanks, everybody, for joining. Frank, thanks much for your time.

Frank D'Amelio - Pfizer Inc. - EVP, Business Operations, & CFO

Thank you very much.

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