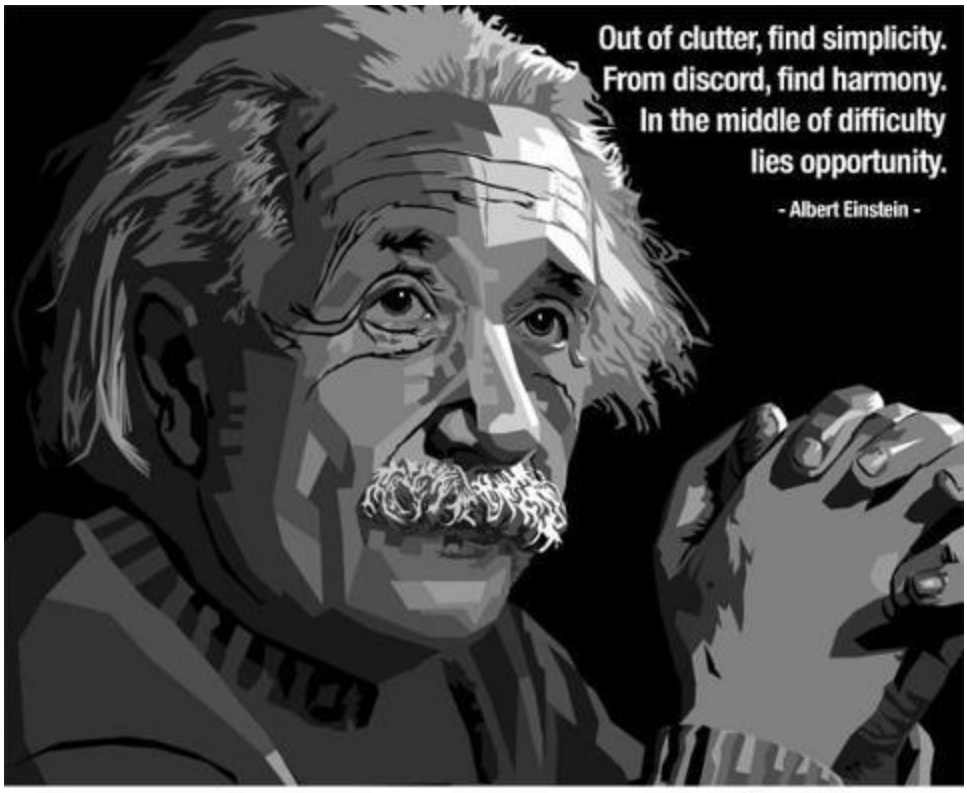
Hospira, Inc.
(NYSE: HSP)

May 2013



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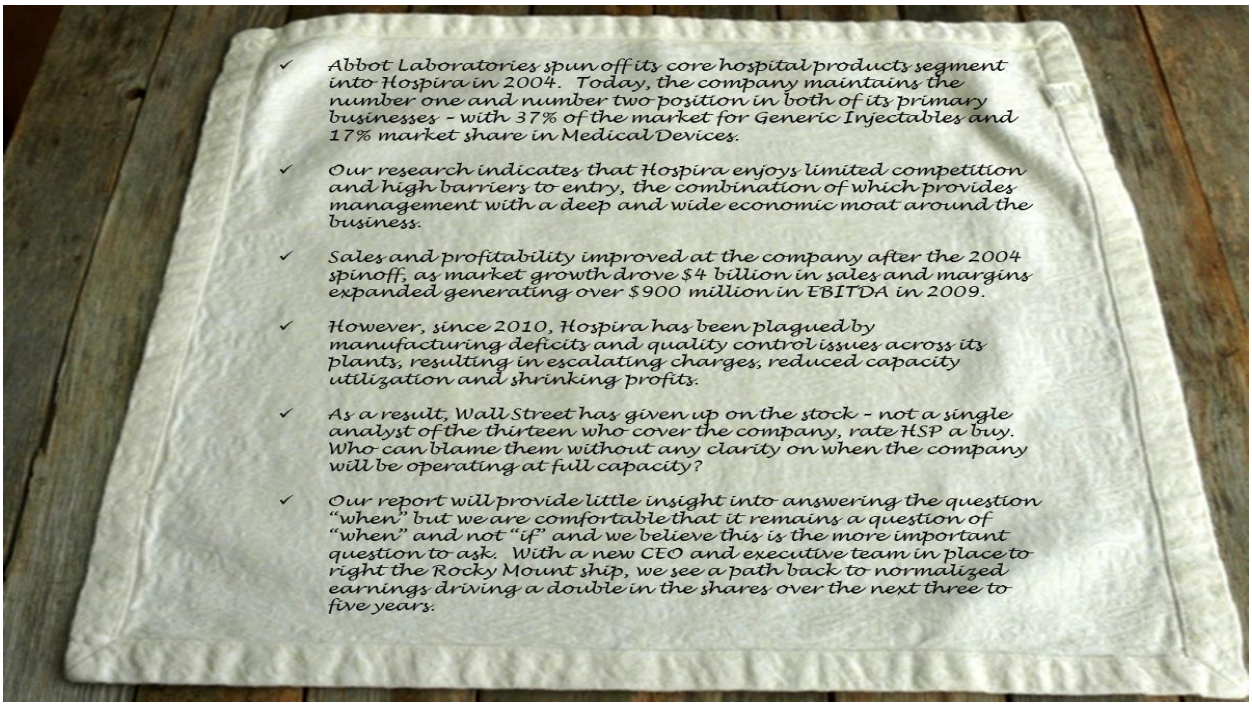
Executive Summary

Investment professionals have a knack for transforming simple into complex. It is in our DNA. If we don't spend countless hours building convoluted models, checking every channel and scrutinizing every data point, how else can we justify the exorbitant fees most managers feel entitled to? Worst still, we tend to take our model's output and blindly accept it without looking under the hood and asking the obvious question. Does this make sense? Investors would do well to remember that greater complexity often drives greater fees. As Ben Graham warned some time ago:

"Mathematics is ordinarily considered as producing precise and dependable results; but in the stock market the more elaborate and abstruse the mathematics the more uncertain and speculative are the conclusions we draw there from. Whenever calculus is brought in, or higher algebra, you could take it as a warning that the operator was trying to substitute theory for experience, and usually also to give to speculation the deceptive guise of investment."

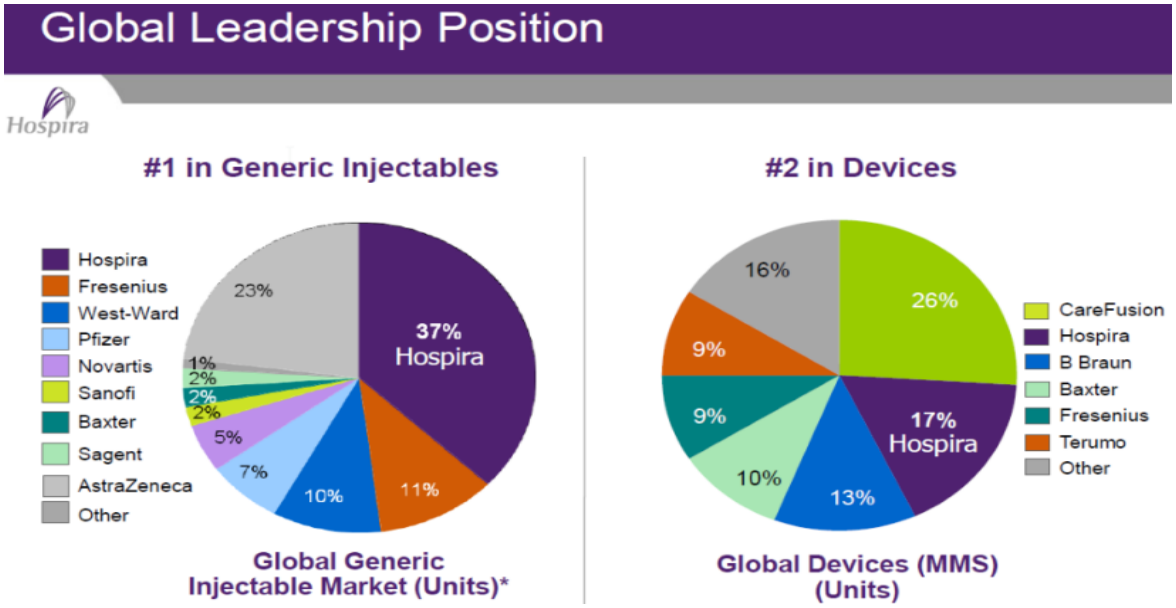
Simple thinking is frowned upon in the investment world. For our simple minds, this creates opportunity as Wall Street repeatedly overanalyzes and overestimates the impact of short term noise on long term value. Albert Einstein is credited with the statement, "Everything should be made as simple as possible, but not simpler." In this report, we will outline our investment thesis for shares of Hospira, Inc. as simple as possible. In fact, we think the thesis is so simple that it could be sketched on the back of a napkin. We understand that our napkin might not sit well with "sell side" research analysts whose investment banking clients pay big bucks for elaborate models, so we've included greater detail throughout the balance of our report, in addition to our napkin below:



Source: Broyhill Asset Management

Business Overview

Hospira (HSP) operated as the hospital products business of Abbot Laboratories until it was spun off into a stand-alone entity in 2004. Today, the company manufactures generic specialty injectable drugs, infusion pumps and other medical services, across thirteen manufacturing facilities globally generating $4.1 billion in annual sales. In 2012 the Americas accounted for 79% of net sales while EMEA and APAC generated 13% and 8% of revenues, respectively. By product, specialty injectable pharmaceuticals (SIP) represented 63% of total net sales in 2012. Medication management represented 25% of 2012 sales, including delivery pumps. Other Pharmaceuticals, which houses Hospira's contract manufacturing services and nutritional products, accounted for the remaining revenues.



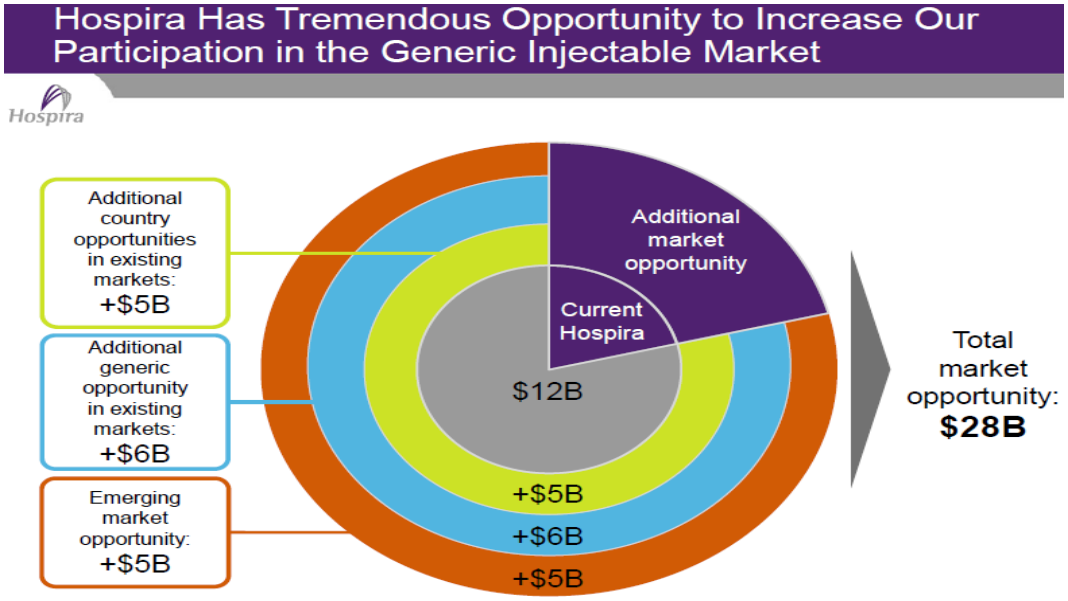
Source: Hospira, IMS, NSP and MIDAS Data

Hospira is the global leader of the Generic Injectables industry with 37% market share as of June 2012. The company has gained 14 points of share since 2008, driven primarily by new drug launches and through acquisitions. Our recent discussions with management indicated that the company has managed to broadly hold share, despite near term operational challenges (discussed below). Hospira's competitive advantage in this business is derived from the company's highly specialized manufacturing facilities which present a high hurdle for new entrants to gain ground on the incumbent. Additional barriers to entry, in the form of heightened regulatory focus and compliance, create a wide and deep moat around the company's operations.

In Devices, Hospira commands a 17% market share as the number two player in the industry, behind the market leader, CareFusion. These systems administer drugs via devices including smart infusion pumps. Over 575,000 installed devices help with drug therapy making the medication process more efficient. Service contracts on their installed devices usually last around three years providing Hospira with a recurring revenue base not only for services, but also for their injectable products.

Emerging Growth Opportunities

Hospira has multiple levers to drive growth in the years ahead. Management has outlined a plan to increase the company's share of the generic injectable market through both increased sales in markets they currently operate in, as well as new growth in emerging economies, where they have begun laying the groundwork. Currently 79% of sales are in the Americas, with only 13% of revenues generated in EMEA and 8% in APAC, providing Hospira with an opportunity to leverage their expertise and expand their footprint. Management is taking drugs approved on the U.S. market and registering them in other markets requiring little investment from an R&D standpoint. We think this represents $1.8 billion in potential revenue (assuming 37% market share of a $5 billion opportunity set) and see even greater potential in new launches across emerging markets where significant investments are being made. While we are not counting on these sales to drive our intrinsic value estimates, Hospira is well positioned to capitalize on an additional $4 billion in potential in the years ahead.



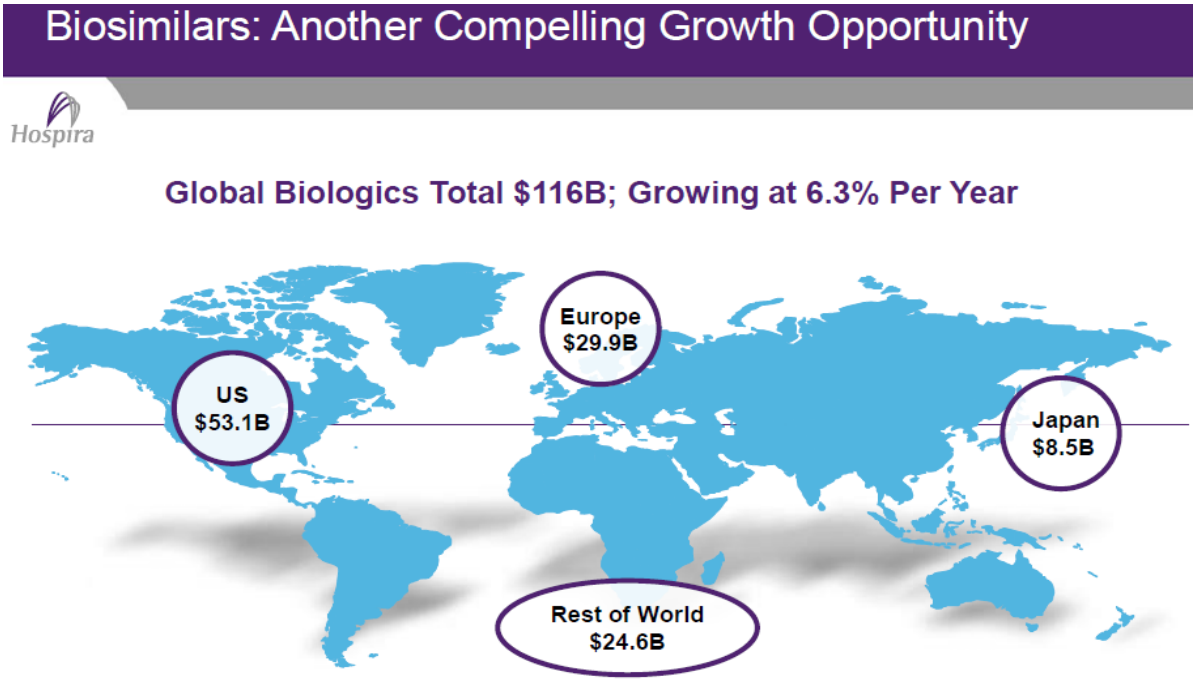
Source: IMS, Hospira, Datamonitor

Strategic investments recently made by management should enhance Hospira's reach and opportunity set in emerging and existing markets. Specifically, to expand their global manufacturing and distribution footprint, management acquired the generic injectable pharmaceutical business of Orchid Pharmaceuticals, based in India, in 2010, while the acquisition of their API manufacturing facility is currently pending. In the meantime, Hospira has broken ground on a new $450 million 1.2 million square feet manufacturing facility in Vizag, India which should be completed in 2014. Commercial production from Vizag is expected to commence in the second half of 2014 and ramp over the following 12 to 24 months. Importantly, the company's new India operations should enhance manufacturing and R&D capabilities and act as a tailwind to margins. Granted, this will take time to flow through to the bottom line, but patient investors should be pleasantly surprised by the positive impact that Wall Street simply can't wait for.

Biosimilars

Follow-on Biologics, or Biosimilars, are biopharmaceutical products that exhibit high molecular complexity and are generally quite sensitive to changes in manufacturing processes. As a result of this complexity and the difficulty in manufacturing these products, very few companies have been authorized to produce biosimilars, effectively creating large barriers to entry around incumbent firms.

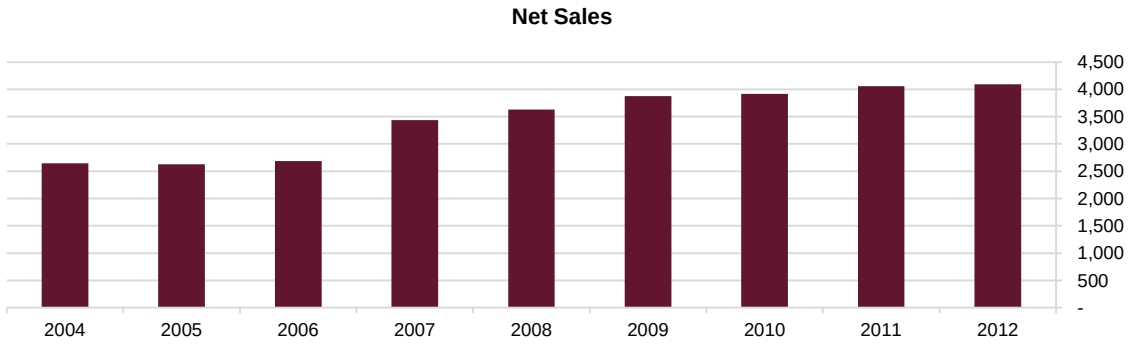
This market represents a compelling growth opportunity for Hospira as the industry is estimated to have a branded total market value of $116 billion, growing at 6.3% annually. Currently, Hospira distributes biosimilars in Europe and Australia and is gaining acceptance across the globe. Management is leading the formation of the biosimilar market in the US and has one of the largest biosimilar pipelines in the industry with several drugs in phase 1 and phase 2 clinical trials with expected approval by 2015. While it's difficult to quantify the actual market value of the opportunity - pricing will be lower due to the nature of generics and competition - curtailing the branded market value by 60% and applying a very conservative 5% market share represents a $4 billion opportunity for the company.



Source: Hospira, Datamonitor, IMS Data

Operating Results & Setbacks

Sales have increased from $2.6 billion post-spin in 2005 to $4.1 billion in 2012, but have stagnated since 2010 when FDA warning letters starting coming in for manufacturing defects and quality control issues that did not meet government standards. One of the company's largest facilities in Rocky Mount, NC, representing one quarter of total revenues, has been running at 60% capacity since 2011. Despite these issues, Hospira has been able to maintain sales at current levels driven by growth in its other markets.



Source: Broyhill Asset Management, Company Filings

The Rocky Mount facility has struggled with violations of Current Good Manufacturing Practices (CGMP) and quality control issues. On March 5, 2013, the FDA sited an additional twenty observations and three repeat issues related to the facility, reducing optimism that the plant would be able to move forward on increasing capacity. It's important to note that these issues have led to drug shortages resulting in small batch releases. JPMorgan estimates that 47% of the FDA's Drug Shortage List was either fully or partly manufactured by Hospira. We believe that the FDA sees it in the best interest of the entire medical community to get Rocky Mount back up to speed as soon as possible, particularly given President Obama's Oct 2011 Executive Order to reduce shortages.

Drug Shortages Caused by HSP Manufacturing Delays

Product	Availability and Estimated Shortage Duration	Date Updated
Ammonium Chloride Injection	Company estimates a release date by 1Q 2013; Estimated recovery: 2Q 2013	Reverified 10/12/2012
Atropine Sulfate Injection	Next delivery and estimated recovery 1Q 2013	Reverified 10/12/2012
Bupivacaine Hydrochloride Injection	Next delivery November Estimated recovery: December	Revised 10/31/2012
Chromic Chloride Injection	Next delivery and estimated recovery December	Reverified 10/12/2012
Diazepam Injection	Next delivery October; Estimated recovery: December	Revised 10/12/2012
Epinephrine Injection (Initial Posting Date) – 4/27/2012	Next delivery November; Estimated recovery 4Q 2012	Revised 11/5/2012
Etomidate Injection (Initial Posting Date) - 2/9/2012	Next delivery December; Estimated recovery: December	Revised 10/31/2012
Fentanyl Citrate Injection	Next delivery November Estimated recovery 2Q 2013	Revised 10/31/2012
Furosemide Injection (Initial posting-6/20/12)	Next delivery October; Estimated recovery 3Q 2013	Revised 10/31/2012
Heparin Sodium Premixes (Initial Posting - 7/5/2012)	Next delivery and estimated recovery 2Q 2013	Reverified 10/31/2012
Intravenous Fat Emulsion	Hospira continues to investigate manufacturing process improvements.	Reverified 10/12/2012
Magnesium Sulfate Injection	Next delivery and estimated recovery 1Q 2013	Reverified 10/12/2012
Mannitol Injection (Osmitrol, Resectisol) (Initial Posting Date) - 12/21/2011	Next delivery October Estimated recovery: 1Q 2013	Revised 9/28/2012
Nalbuphine HCl (Nubain) Injection (Initial Posting - 5/15/2012)	Next delivery January Estimated recovery 2Q 2013	Revised 10/31/2012
Naloxone (Narcan) Injection (Initial Posting Date) - 2/22/2012	Next delivery November; Estimated recovery December	Revised 10/31/2012
Pancuronium Bromide Injection	Next delivery 1Q 2013; Estimated Recovery: 2Q 2013	Revised 10/31/2012
Procainamide HCL Injection	Next delivery December Estimated 1Q 2013	Revised 10/12/2012
Propofol Injection (Initial Posting Date) - 4/5/2012	Next delivery December	Revised 10/23/2012
Sodium Bicarbonate Injection (Initial Posting-3/20/12)	Next delivery November/Estimated recovery 1Q 2013	Revised 10/22/2012
Sodium Chloride 23.4%	Expected recovery 1Q 2013	Revised 10/12/2012
Sufentanil Citrate Injection	Next delivery 3Q 2013	Revised 10/31/2012
Tobramycin Solution for Injection	Next delivery 1Q 2013; Estimated recovery: 1Q 2013	
Tromethamine Injection (Initial Posting Date) - 5/2/2012	Next delivery September 2013; Estimated recovery 4Q 2013	Reverified 10/31/2012
Zinc Injection (Initial Posting Date)- 2/15/2012	Next delivery November; Estimated recovery 1Q 2013	Revised 10/31/2012

Source: FDA, JP Morgan

Given the street's obsession with Hospira's ongoing remediation efforts, we will resist the urge to outline the company's regulatory challenges which reach far beyond Rocky Mount. However, we will note that every analyst report we've read on the company details these issues in excruciating detail so curious minds can feel free to indulge themselves with the full history via Bloomberg or via the FDA here and here. We've provided a brief overview from Barclays below for those investors better suited to cliff notes.

HSP Remediation Comments

Facility	Update 11/7/12	Update 2/13/13
Rocky Mount	Progress update 1) plant: significant investments in capital improvements and facility modifictions ex: started buidling 'state-of-the-art' quality control lab and first automated visual inspection machine; 2)reduced the number of 3rd party consultants and replaced with HSP operators and quality personnel; 3)implementing IT solutions to enhance quality systems in oreder to improve robustness of maunfacturing; 4)"production and release levels are moving in right direction". Next milestone will be FDA inspection	Continue to make progress. Next major milestone is the FDA's re-inspection of the facility, which began 2/12/13. HSP believes, due to the size and complexity of the plant, that the inspection could be extensive and lengthy (estimated ~1 month) - plans to disclose results of re-inspection once complete
Clayton	During 3Q12 manufactured a limited amount of propofol; plan on manufacturing and building inventory levels through the remainder of the year in order have an adequate supply of product prior to reentry into the market (expected in late '12 early '13)	Re-started manufacturing propofol batches and building inventory in 4Q1212 for an early 2013 re-launch. Recently released a limited number of batches to the market. Consistent with re-launch plans, HSP is starting with the 20mL and will follow with the 50mL and 100mL offerings in 2Q13. Pricing propofol above current market levels, commensurate with the significant resources required to bring the product back to the market.
Boulder	No Update	No Update
Austin	Inspected during 3Q12 and received 483 with 19 observations. HSP provided FDA with full response and set of commitments to address 483 observations and is moving forward with remediation efforts	No Update
Lake Forest	HSP had submitted its action plan to FDA to address the 10 previously announced 483 observations received in early 3Q12 relating to device design and control systems and "remain on target" to complete the commitments identified in the commitment plan. In the week of 10/29/12 HSP received an 'untitled letter' from the FDA stating it was not satifsfied with the corrective action for 2 of the observations - HSP is working on response	Received a 483 with 10 observations in late January (many repeat observations from July 2012 inspection); "disappointing"; outcome confirms "there is a lot of work to be done there"
Costa Rica	Warning letter received in August following April investigation. HSP has provided FDA with response.	No Update
McPherson	FDA performed full CGMP inspection that was recently completed and received two 483 observations. Result of the inspection "helped to confirm belief that remeidation is largely on track"	No Update
Zydus Hopsira Oncology Private Ltd. - Joint ventur in India (ZHOPL)	FDA performed an inspection that resulted in zero observations.	No Update
Irungattukottai (IKKT)	FDA inspection of plant resulted in five 483 observations. Stopped production in September 2012 in order to address observations and recently resumed production (expect to be fully operational in next few weeks)	No Update

Source: Company reports and Barclays Research

On the surface, the reports look very bad - you can glean this from the media reports which emphasize that twenty observations were found and that three of them were repeats, which are not good things. However, one of our industry contracts notes that it is not uncommon for the FDA to repeat observations that had accepted remediation plans but were not yet fully implemented. "They usually only do this when they're in a testy mood, though" an idea reinforced by an inspection which lasted 2.5 weeks, "an extremely long time to have them breathing down your neck."

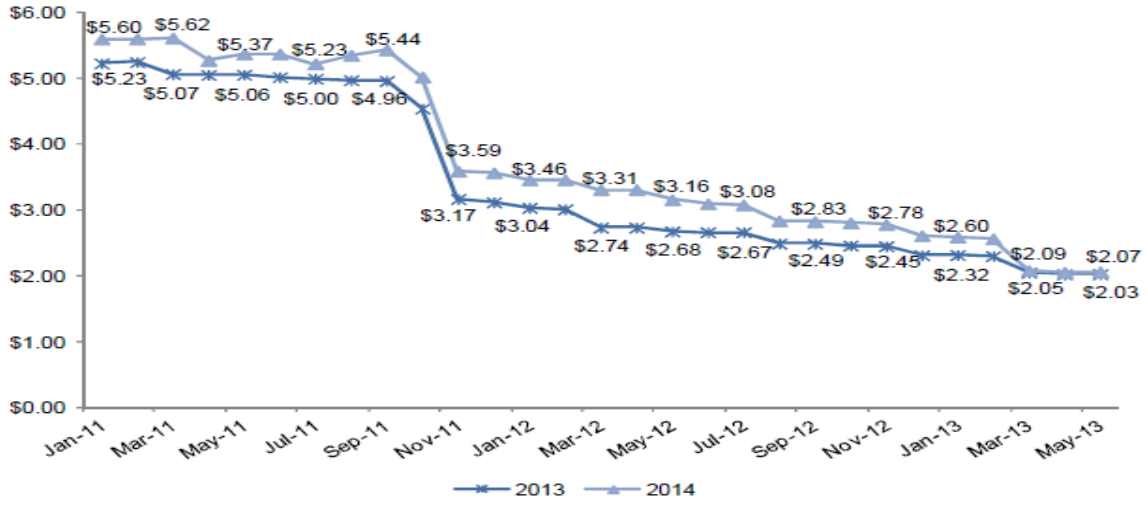
"The good news according to our contact is that, "most of the items were matter of procedure/training issues and many could be fixed with documentation. Four related to actual facility problems, which could cost, but two of these still looked like they could be handled by documenting that the equipment deficits were not causing QC issues and one cited bad caulking, which could be fixed with a trip to Home Depot. More telling is that the recurrent theme with all the observations was proving sterile process and lack of bacterial contamination. The bottom line is that this is probably a direct result of the meningitis contamination issues at the New England Compounding Center last October. Injectables are a hot-button issue at the FDA right now and HSP was a convenient whipping boy." So what does this mean? "I think it could actually be good news. It means that the problems are very fixable, given the right people on the job. I think if they have a good plan for this facility, then the other ones should be fine as well."

It's In The Price

These are real issues which have cost the company real money to address – the company has spent over $375 million to date on remediation. It is not at all our intention to gloss over these risks. Investors should be aware of the potential for additional costs and further delays. Rather, we merely suggest that the street's fanatical obsession with each and every FDA-related piece of news serves to distract consensus from the company's normalized earnings power, which should ultimately determine the company's intrinsic worth.

Not long ago, consensus estimates indicated that Hospira was capable of generating over $5 per share in earnings in 2013. Today, those same analysts are estimating earnings power around $2 per share, a 60% decline. Unlike most stocks in today's lofty market, expectations for Hospira have been greatly reduced. The bar has been drastically lowered, and while near term pressures may continue to weigh on earnings short term, the stock's reaction to additional disappointments has begun to dissipate. **In other words, disappointment is in the price and any indication that charges are nearing their ultimate conclusion, should result in a sharp rerating in Hospira shares.**

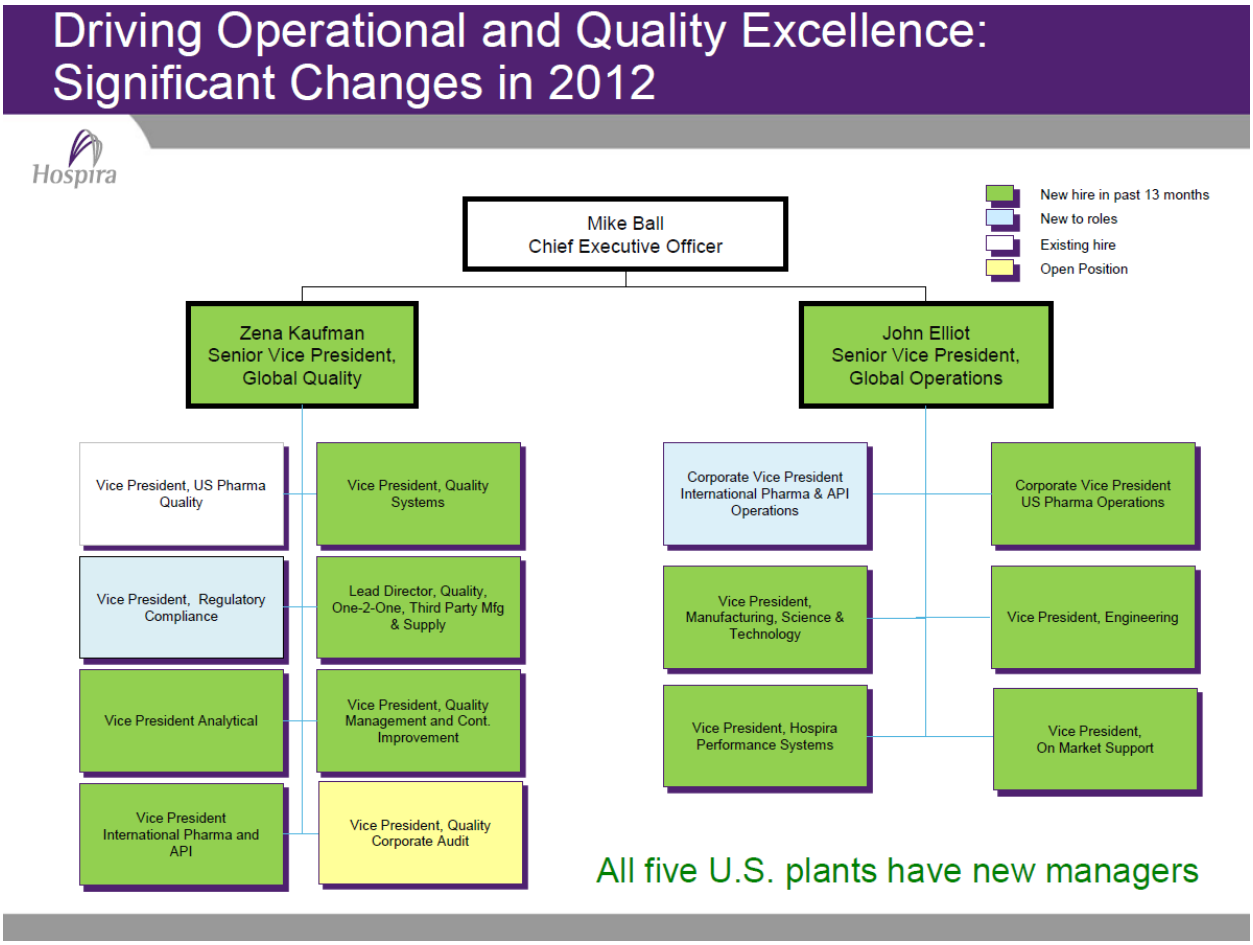
Consensus Earnings Estimates



Source: FactSet, Goldman Sachs

New Leadership

Importantly, new management is doing the right things to aggressively attack the problems at Hospira facilities. Michael Ball was appointed CEO in March 2011 to take on the challenges imposed by the FDA, get the company back on track and rebuild credibility with investors. Before joining Hospira, Ball was President of Allergan, a leading pharmaceuticals, biologics and medical device company. Since joining Hospira, he has been very active and engaged with FDA officials, leading the way for a high-quality, transparent and efficient operational structure. Under his leadership, he has fired executives and plant managers who downplayed production trouble, replacing them with industry leaders who understand the challenges the company is facing while also pursuing new opportunities. Richard Davies, Neil Ryding and Zena Kaufman are a few examples. Mr. Davies was brought on from Amgen in February 2012 to spearhead global strategies and commercial development. Mr. Ryding joined Hospira from CareFusion and serves as Senior Vice President of Devices. Ms. Kaufman plays a pivotal role leading quality control for Hospira. Since her appointment in 2012, she has led the company's efforts in revamping processes, systems and controls to meet regulatory standards.



Source: Company Filings

Bottom Line: Hospira has undergone a dramatic change in leadership. A change that is often required by companies in transition, but these things do not happen overnight. They take time. It often takes years to play out and longer for conventional wisdom to realize that the underlying business has begun to turn. Mr. Market, however, looks forward and will begin to price in normalized earnings power well ahead of consensus expectations.

Change is scary and uncertainty is even worse. While we spend much of our time, looking to invest in "change" which is often misunderstood, the street is more concerned with meeting quarterly numbers. As CEO, Michael Ball, stated on the company's Q2-12 earnings call, "I am committed to resolving our quality issue, and getting as much done in 2012 as possible. I believe the FDA understands, and I know that our employees do as well, my commitment in this respect. But it is not a quick fix. It's complex, it takes time and money, and there may be additional gators yet to be uncovered along the way." Unfortunately, Wall Street is short on time and doesn't like to spend money, so naturally, as EBITDA has dropped from a peak of over $900 million to under $370 million, analysts have bailed on the stock. With plenty of time on our hands and plenty of dry powder in portfolios, we are happy to wait for the gators to pass and earnings power to accrue over time.

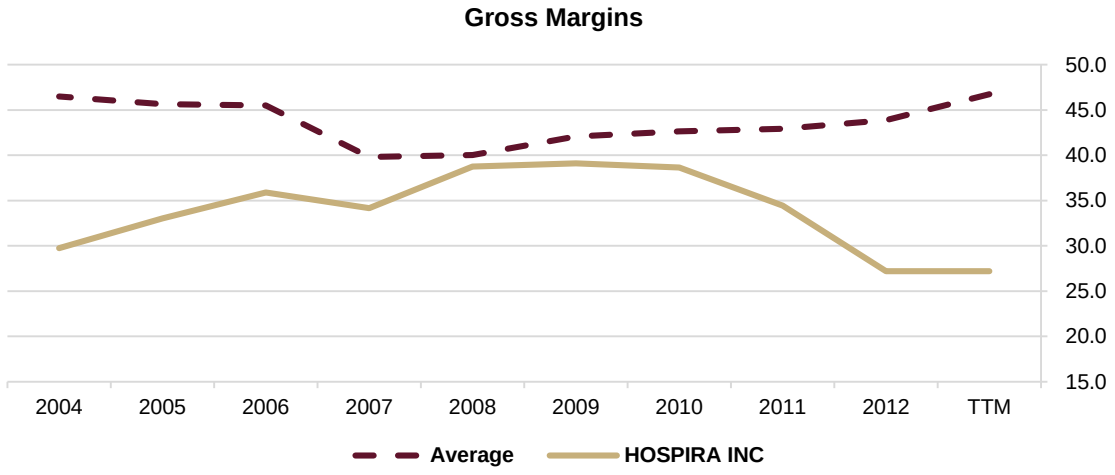
Variant Perception

Consensus is predictably obsessed with the potential for greater margin compression and a protracted return to normalized earnings. Per one sell-side analyst, "It is difficult for HSP to predict a timeline at this stage; we believe that the import ban will last a least a few quarters based on experience with prior warning letters, recalls and other dealings with the FDA of this nature. Net-net, we remain on the sidelines on HSP due to lack of visibility on the ramp of production."

As a general rule of thumb, investors could do much worse than simply buying stock in companies which pose challenges for Wall Street to "predict a clear timeline" for at "least a few quarters." Our own experience with Avon Products this year is an example which comes quickly to mind (and another high quality company undergoing a major transition under new leadership). More broadly, I don't think we have ever purchased a company with a clear timeline for the next few quarters. Instead, we prefer to value businesses on normalized cash flow looking out three to five years. Ironically, the market's increasing focus on the next few quarters, often provides investors with an opportunity to buy good businesses at great prices. It is this fixation on the immediate present that has distracted investors from the true long term earnings power of Hospira.

The Spin On Margins

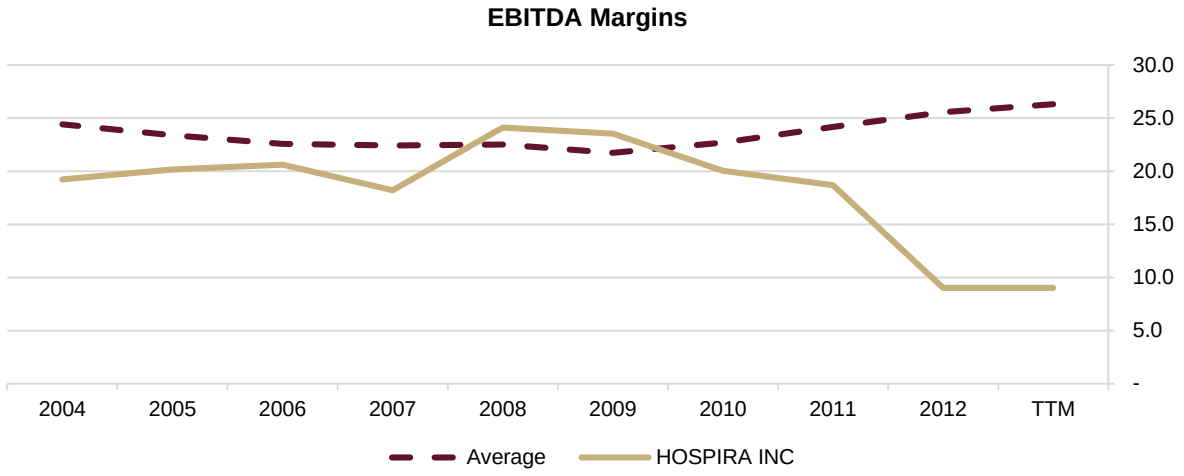
Leading up to the rocky road in Rocky Mount, Hospira was performing on all cylinders as the market began to appreciate the true value of Abbot's former hospital products business as a stand-alone entity. With the business and management free from the distractions of a large corporate parent, the combination of accountability, responsibility and direct incentives took their natural course resulting in consistent operating improvements. From 2004 through 2009, management offloaded low-margin contracts while increasing sales of higher-margin products, introduced new products through R&D and acquisitions, and closed or sold plants to better align the company's cost structure and focus. During this time, gross margins expanded from 29% to 39%, fully closing the gap with peers.



Source: Broyhill Asset Management, Company Filings

However, since the onset of FDA inquires in 2010, gross margins have been impacted by charges of $462 million, representing 4% of aggregate revenues. Charges were incurred from ongoing remediation efforts, outside consultants, third-party oversight and inventory write-downs. Additional charges of $112 million have been incurred in relation to the company's launch of Project Fuel in 2009. A number of improvements have been undertaken at Hospira facilities since the financial crisis, as management aims to optimize the product portfolio, shed non-core assets and streamline the organizational structure. While management has indicated that these operating improvements have resulted in a higher cost structure, price increases on various products should help offset some of the increased overhead.

Bottom Line: Hospira has significant opportunity for margin improvement relative to industry peers. CEO, Michael Ball, spoke to this potential at the company's recent analyst day. "So, from my standpoint there are a number of things that we are doing, that are moving, or will cause gross margin to move forward. I have said before that if you look at our gross margin being in the mid-30%s and our peer competitors being in the mid-40%s, one would think that there should be something that we can do to move our gross margins up the line. I'm not necessarily saying to that level, but what I am saying is there's probably more pressure, positive pressure to move gross margins up than for them to stay the same or go down."



Source: Broyhill Asset Management, Company Filings

In addition to these cost of sales charges, the company has taken $664 million in restructuring charges, with $400 million in 2011 stemming from a goodwill impairment charge on their EMEA reporting units. As a result EBITDA margins have followed a similar path – expanding post-spin and eventually surpassing industry peers, before falling back to new lows following the company's regulatory travails in 2010. We expect margins to revert back to normal levels as the company works through their FDA issues and gradually rolls out new products from lower-cost facilities.

Balance Sheet & Financial Health

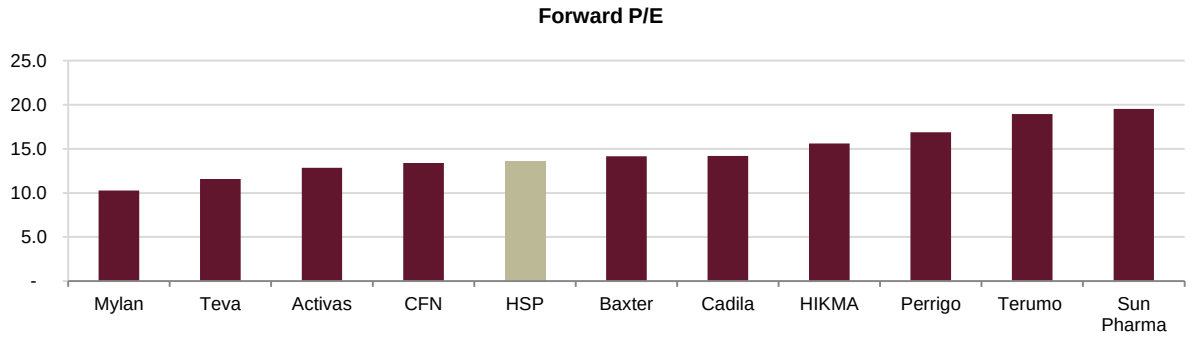
We view Hospira's overall balance sheet as healthy. The company has been building cash since 2010 even as they have been spending on their remediation efforts. This has helped reduce their net debt balance slightly, with total debt at $1.7 billion today and the earliest maturity of $400 million due in 2014. Hospira has access to a $1 billion unsecured revolver with no borrowings against it, providing management with ample liquidity if necessary. While this week's guidance points to negative free cash flow generation in 2013, we expect the company to maintain a strong financial position, despite the temporary increase on the revolver's maximum leverage ratio.

(dollars in millions)	2012	2011
Long-term debt:		
5.90% Notes due June 2014	$ 400.0	$ 400.0
6.40% Notes due May 2015	250.0	250.0
6.05% Notes due March 2017	550.0	550.0
5.60% Notes due September 2040	500.0	500.0
Other, due 2015	4.3	3.0
Deferred gains on terminated interest rate swap instruments	5.5	12.3
Unamortized debt discount	(3.0)	(3.4)
Total long-term debt	1,706.8	1,711.9
Short-term borrowings:		
Deferred gains on terminated interest rate swap instruments	6.8	6.8
Other	22.1	29.8
Total short-term borrowings	28.9	36.6
Total debt	$ 1,735.7	$ 1,748.5

Hospira repurchased 9.4 million shares for $400 million from 2006 to 2010. In April 2011, the board authorized another $1.0 billion repurchase program and later executed on $200 million, buying in 3.7 million shares. No repurchases were made in 2012 as the company dedicated capital resources to quality issues. We note that the remaining balance would retire close to 15% of current shares outstanding.

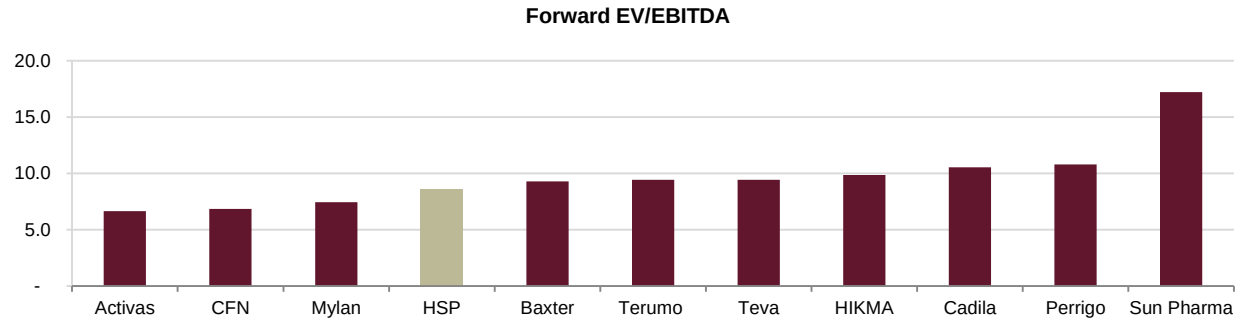
Valuation Analysis

Hospira is currently trading at 9.4x forward EBITDA and 15.4x forward earnings both of which are above the stock's brief historical averages of 8.5x and 13.6x respectively, as the company has been under-earning due to recent challenges. On a relative basis, HSP shares trade at the lower end of their peers on both a forward P/E and EV/EBITDA basis. **Most of the street points to the stock's "unattractive" valuation as justification for their sell ratings. We disagree. Hospira appears to be valued in line with peers on current earnings despite the fact that current earnings are severely depressed.**



Source: Broyhill Asset Management, Company Filings

We believe a market share leader in an industry characterized by sustainable competitive advantages and high barriers to entry, with operating leverage to improving fundamentals, should command a premium multiple to peers and to what Mr. Market is affording Hospira today. We discuss our estimate of intrinsic value below.



Source: Broyhill Asset Management, Company Filings

What's It Worth?

In order to better understand Hospira's normalized earnings power we assume that Rocky Mount will again reach full capacity at *some* point in time. We make no attempt to estimate precisely which quarter this will occur but we can estimate our expected return over a range of scenarios. It is our understanding that Rocky Mount is currently running at 60% capacity. The facility currently represents 25% of total company sales so by grossing up production at this facility and growing the remaining business at a conservative rate of 3.5% annually, we estimate normalized sales would range from $5.2 billion to $5.4 billion.

We expect that the resulting increase in operating leverage, combined with newer and more efficient facilities should drive operating margins back towards levels in line with the industry average, and consistent with levels Hospira has comfortably operated at in the past. Putting a 10x multiple on normalized EBITDA - transactions in the industry have ranged from 11x to 14x EBITDA - drives an enterprise value of $11.8 billion to $12.3 billion. Backing out debt and adding back cash gets us to a firm value of $10.9 billion to $11.4 billion or $66 to $69 per diluted share, more than double the current share price. If we assume this transition occurs over three to five years, our investment today offers us the potential for annual returns of 27% to 17% over three and five years, respectively. We see downside risk to $26 assuming no sales growth, operating margins below depressed 2011 levels and multiple compression to 7x EBITDA, a multiple consistent with the stock's sell off from initial FDA warnings in September 2011.

On balance, the risk-reward here appears extremely favorable, particularly given the market's extremely depressed expectations. Any good news should predictably drive sell-side upgrades, reinforcing a move higher in the stock. At current levels, we see a high probability of 100% upside and a relatively low probability of a 20% loss. We don't see these odds very often in an "efficient market" and strongly suggest that investors move to capitalize on them when Mr. Market occasionally offers them up.

"Out of clutter, find simplicity. From discord, find harmony. In the middle of difficulty lies opportunity."

– Albert Einstein

Upside Catalysts

Mergers & Acquisitions: Conventional wisdom in the investment banking world would suggest that once a high quality operating segment is spun-off from a larger conglomerate, it is only logical that it be reacquired years down the road. Academic research suggests that conventional wisdom may be on to something as spin-offs are five times more likely to find themselves the target of an acquisition. Coincidentally, Hospira recently implemented a "Change in Control" document for CEO Michael Ball and other named executives which is set to expire in 2015. We would note that most of Mr. Ball's options are struck around $35 per share, so he has plenty of incentive to consider a "change in control." At the same time, many large global pharmaceutical companies, struggling for growth, are building out generic portfolios to drive future profits as blockbuster drugs come off patent.

We believe Hospira would be a particularly good fit for many of these businesses looking to acquire a large share of an attractive market at a bite size which could be easily swallowed. If Hospira can't fix their problems themselves, it's likely that other, bigger fish have noticed that the problems are fixable. In recent years, the average price paid for similar companies has ranged from 11x to 14x EBITDA. Using the midpoint of this valuation and applying it to our estimate of normalized EBITDA, would value the deal at $13.8 billion, or $83 per diluted share – more than 150% above current levels.

Biosimilars Are Coming: Hospira is ahead of the game in the US and is currently selling biosimilars in Europe and Australia. The total global market branded value is estimated at $116 billion and growing at 6.3% annually. While we did not incorporate this opportunity into our numbers, there is potential for biosimilar approval by the US FDA in 2015.

Emerging Generics: Hospira has the potential to capture over $6 billion in new growth opportunities in generic injectables through existing markets, new product introductions and expansion into new markets. The company's new state-of-the-art manufacturing facility in India should support international growth efforts through additional output and distribution capabilities.

Downside Risks

Regulatory Risk: The biggest risk to our thesis is regulatory risk and the potential that Hospira's problems are even larger than what has been disclosed to investors. The ultimate blow would be a consent decree brought on by the FDA which could jeopardize the company's ability to continue as a going concern. Given the drug shortages discussed and Hospira's progress to date, we think this is a very low probability scenario, but investors should be aware of it nonetheless.

Market Share: FDA scrutiny and ongoing facility upgrades have resulted in capacity reductions, limiting output. While this should be a temporary issue, a prolonged capacity reduction would force clients to find other alternatives.

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