

Biota Holdings Ltd (BTA.ASX)

Profit downgrade presents buying opportunity

Tuesday 31 July 2007
Healthcare

Biota Holdings has advised that indicative Relenza royalties were \$39.8m, above 2006 royalties of \$5.2m. This was a strong performance, but it was weaker than both we and the company had anticipated. This was due to lower than expected Q4 royalties of \$11.1m, which had been expected to be similar to the \$16.0m received in Q3. We remain convinced that Relenza royalties will continue their upward trajectory over FY2008.

665% increase in royalties. It must be remembered that 2007 royalties grew an astounding 665% over the pcp. Overall, Relenza royalties are still continuing their strong upward trend, albeit at a slightly lower rate in the near term.

Guidance marginally reduced. Following the lower than expected Q4 royalties, management has reduced guidance by \$1m to a PBT of greater than \$17m.

We have downgraded our 2007e NPAT by 20% to \$20.6m. In order to reflect the slightly reduced Relenza royalty growth rate we have also marginally reduced our 2008 earnings to \$25.9m, but we note that we are still expecting an impressive 35% sales growth in 2008. We have made no changes to our longer term royalty forecasts, as we are confident in the underlying growth story.

No change to valuation or price target. We have made no changes to our valuation or price target, as the deferral of tax credits from 2007 and 2008 into 2009 has offset the lost near term earnings.

Upgrade to damages estimate expected imminently. Biota Holdings is expected to soon release an updated estimate for its damages claim against GSK. We believe this new estimate could be as high as \$500m at the upper end. In our forecast we are only estimating damages of \$100m.

We retain our Buy recommendation for Biota Holdings and our price target of \$2.83/share. We continue to believe the company is a strong growth story and the best quality biotechnology company in Australia.

Rating: Buy
(previous): Buy

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Share price: \$1.76

Price target: \$2.83
NPV per share: \$2.83
Risk: High

Shares on issue (m): 181.7
Shares on issue (diluted) (m): 182.7
Free float: 100%
Average daily volume: 286,539

Market cap (\$m): \$321.5
Enterprise value FY06e (\$m): \$275.4
Net Debt FY06e (\$m): -46.2
Gearing (ND/ND+E) FY06e: NA
S'holders equity FY06e (\$m): 46.9
NTA per share FY06e: \$0.26

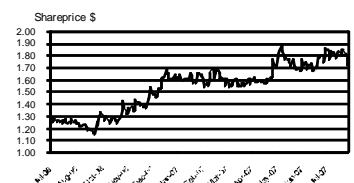
Forecast: 2007

Free cash flow (\$m): 9.2
Return on average equity: 30.7%
Net interest cover: NA

Forecast: 2008

Free cash flow (\$m): 24.4
Return on average equity: 28.2%
Net interest cover: NA

Shareprice (\$):



Year to Jun (\$m)	2005a	2006a	2007e	2008e	*2009e
Sales revenue	3.7	12.7	53.9	72.8	196.7
% change		246%	324%	35%	170%
EBITDA	-15.5	-12.6	15.6	17.5	175.9
EBITDA margin	-422%	-99%	29%	24%	89%
NPAT rep. (incl. sig items)	-15.1	-11.3	19.9	24.5	136.6
NPAT normalised	-15.1	-11.3	20.6	25.9	67.9
EPS diluted norm. (c)	-0.11	-0.06	0.11	0.14	0.37
% change	0%	-43%	NA	26%	162%
Dividend (c)	0	0	0	0	0
PER (x)	-16.0	-27.9	15.6	12.4	4.7
EV/EBITDA (x)	-14.0	-21.4	16.7	13.5	0.6
Yield (%)	0.00%	0.00%	0.00%	0.00%	0.00%

*2009 estimate includes settlement from GSK in reported numbers.

Source: Company, Foster Stockbroking

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FULL YEAR RELENZA ROYALTY \$39.8M

Biota Holdings has advised that indicative Relenza royalties were \$39.8m, well above 2006 royalties of \$5.2m. This was a strong performance, but it was weaker than both we and the company had anticipated. This was due to lower than expected Q4 royalties of \$11.1m, which had been expected to be similar to the \$16.0m received in Q3.

We are not overly concerned by this lower than expected figure, as we believe that Q3 was an abnormally high figure rather than Q4 being abnormally low. During the production capacity ramp up we expect to see some lumpy quarters, as large Government orders are filled, and this is what we believe occurred in Q3.

It must be remembered that royalties over 2007 grew an impressive 665% over the pcip. Overall, Relenza royalties are still continuing their strong upward trend, albeit at a slightly lower rate in the near term.

SLIGHT DOWNGRADE TO PBT GUIDANCE

Biota had previously forecast a PBT of at least \$18m. Following the lower than expected Q4 royalties, management has reduced guidance to a PBT of greater than \$17m. As a result we have downgraded our 2007e NPAT to \$20.6m. In order to reflect the slightly reduced Relenza royalty growth rate we have also marginally reduced our 2008 earnings to \$25.9m, but we are still expecting 35% sales growth in 2008. We have made no changes to our longer term royalty forecasts, as we are confident in the underlying growth story.

Our changes are as follows.

Biota Profit & Loss \$m						
	FY07e	FY07e	%	FY08e	FY08e	%
Y/e Jun	new	old	change	new	old	change
Sales revenue	53.9	58.9	-8%	72.8	74.4	-2%
EBITDA	15.6	18.6	-16%	17.5	19.2	-9%
EBITDA margin	29%	32%	-8%	24%	26%	-7%
Depreciation	1.0	1.0	0%	1.0	1.0	0%
EBITA	14.6	17.6	-17%	16.5	18.1	-9%
EBITA margin	27%	30%	-9%	23%	24%	-7%
Amortisation	0.7	0.7	0%	1.3	1.3	0%
EBIT	13.9	16.9	-18%	15.1	16.8	-10%
EBIT margin	26%	29%	-10%	21%	23%	-8%
Net interest expense	-3.0	-3.0	0%	-4.4	-4.4	0%
PBT	16.9	19.9	-15%	19.5	21.2	-8%
Tax	-3.0	-5.0	-40%	-5.0	-7.0	-29%
NPAT	19.9	24.9	-20%	24.5	28.2	-13%
NPAT normalised	20.6	25.6	-20%	25.9	29.5	-12%

Source: Company; Foster Stockbroking estimates.

These downgrades have not affected our valuation and price target, as the deferral of tax credits from 2007 and 2008 into 2009 has offset the lost near term earnings.

RECOMMENDATION

We retain our **Buy** recommendation for Biota Holdings and our price target of \$2.83/share. We continue to believe the company is a strong growth story and the best quality biotechnology company in Australia.

FINANCIALS

Biota Profit & Loss \$m

Y/e Jun	2006a	2007e	2008e	2009e	1H 07a	2H 07e
Sales revenue	12.7	53.9	72.8	196.7	19.1	34.8
EBITDA	-12.6	15.6	17.5	175.9	2.9	12.7
EBITDA margin	-99%	29%	24%	89%	15%	36%
Depreciation	1.0	1.0	1.0	1.1	0.0	1.0
EBITA	-13.6	14.6	16.5	174.8	2.9	11.7
EBITA margin	-107%	27%	23%	89%	15%	33%
Amortisation	0.0	0.7	1.3	1.3	0.0	0.7
EBIT	-13.6	13.9	15.1	173.5	2.9	11.0
EBIT margin	-107%	26%	21%	88%	15%	32%
Net interest expense	-2.3	-3.0	-4.4	-7.3	-1.2	-1.9
PBT	-11.3	16.9	19.5	180.7	4.1	12.8
Tax	0.0	-3.0	-5.0	44.2	0.0	-3.0
NPAT	-11.3	19.9	24.5	136.6	4.1	15.8
NPAT normalised	-11.3	20.6	25.9	67.9	4.1	16.5

Source: Company; Foster Stockbroking estimates.

Biota Cashflow \$m

Y/e Jun	2006a	2007e	2008e	2009e
Receipts	7.0	40.4	70.7	190.4
Payments	-23.5	-30.0	-54.1	-17.3
Interest	2.1	-3.0	4.4	7.3
Tax	0.0	3.0	5.0	-44.2
Other	6.7	0.0	0.0	0.0
Operating cash flow	-7.7	10.4	26.0	136.1
Loans to related parties	0.0	0.0	0.0	0.0
Sale of PPE	0.1	0.0	0.0	0.0
Acquisitions	0.0	-4.0	0.0	-4.0
Capex	-2.0	-1.2	-1.6	-1.7
Investing Cashflow	-1.9	-5.2	-1.6	-5.7
Debt repayments	-0.8	0.0	0.0	0.0
Debt borrowed	0.0	0.0	0.0	0.0
Equity proceeds	31.8	46.0	0.0	0.0
Dividends	0.0	0.0	0.0	0.0
Other	0.0	0.0	0.0	0.0
Finance Cashflow	31.0	46.0	0.0	0.0

Source: Company; Foster Stockbroking estimates.

Biota Balance Sheet \$m

Y/e Jun	2006a	2007e	2008e	2009e
Cash and cash equivalents	46.2	61.5	85.8	216.2
Receivables	5.9	17.3	19.4	25.8
Inventories	0.0	0.0	0.0	0.0
PPE	5.5	5.1	5.7	6.3
Intangibles	0.0	10.0	9.3	8.0
Total Assets	57.6	93.8	119.5	256.3
Payables	4.0	9.5	10.7	14.2
Deferred revenue	6.0	0.0	0.0	0.0
Tax liabilities	0.0	0.0	0.0	11.0
Debt	0.0	0.0	0.0	0.0
Provisions	0.6	4.8	0.9	0.3
Other	0.0	12.3	16.3	2.5
Total Liabilities	10.7	26.7	27.8	28.0
Net assets	46.9	67.1	91.7	228.2
Contributed Equity	158.0	158.3	158.3	158.3
Reserves	-0.1	-0.2	-0.2	-0.2
Retained profits	-111.0	-91.0	-66.5	70.1
Total Equity	46.9	67.1	91.7	228.2

Source: Company; Foster stockbroking estimates.

Biota Financial Ratios

Y/e Jun	2006a	2007e	2008e	2009e
DPS c	0.0	0.0	0.0	0.0
Yield %	0.0	0.0	0.0	0.0
Ave wtd shares dil m	179.3	182.7	182.7	182.7
EPS rep c	-0.06	0.11	0.13	0.75
EPS normalised c	-0.06	0.11	0.14	0.37
PER x	-27.9	15.6	12.4	4.7
EPS growth %	-43%	NA	26%	162%
Interest cover x	6.0	-4.6	-3.4	-23.9
Ave RoE (%)	-24%	31%	28%	30%
Ave RoA (%)	-119%	43%	45%	433%
EV/EBITDA x	-21.4	16.7	13.5	0.6

Source: Company; Foster Stockbroking estimates.

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