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## Biota

Buy BTA at around \$1.36

Solid fundamentals remain

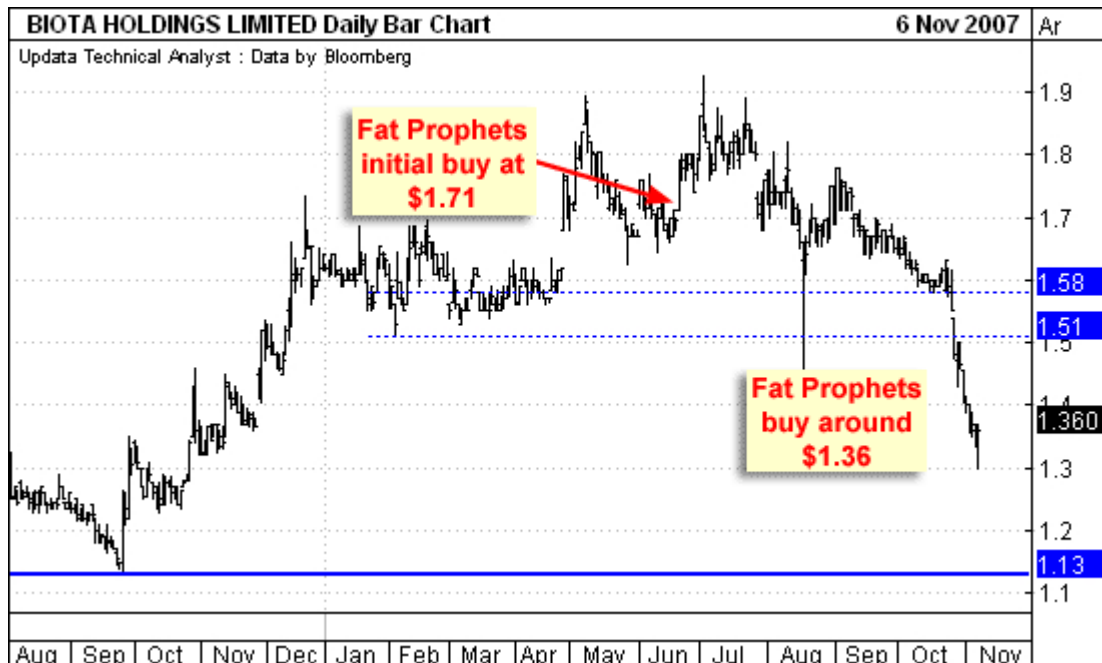
[Fat 351](#), 06 Nov, 2007  
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| SYMBOL DEFINITIONS   |   |
|--|---|
|  SPECIALTY DISH             |  HIGH RISK |
|  MARKET CAP <b>\$249m</b> |   |
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Melbourne based Biota (BTA) has suffered a deteriorating share price over the past few weeks and last week we had the opportunity to discuss this and other events with CEO and Managing Director Peter Cook, and Chief Financial Officer Damian Lismore.

*"While Biota does not receive specific sales information from Glaxo, it expects Relenza sales to grow as governments continue to stockpile influenza antivirals throughout the year."*

On the surface, the sliding share price appeared solely due to an announcement detailing Biota's latest indicative royalty receipt for flagship drug Zanamivir, marketed by licence holder GlaxoSmithKline as Relenza. The \$4.5 million quarterly payment from licence holder GlaxoSmithKline (GSK) reflected sales of GBP28 million, down 7 percent on the same quarter last year.



Despite the company stating the figures were "consistent with Biota's expectation that GSK will sell its installed capacity over the year" the annual decline spooked investors. As displayed on the daily chart, since breaching support between \$1.58 and \$1.51, there has been a steep decline into the \$1.34 region.

While this was initially concerning, management informed us they believed the pressure on the share price was largely related to a substantial private shareholder, Niako Investments, selling down their stake. They understand that the sell-down is for private liquidity reasons rather than with any fundamental concerns over the company.

Over the last two weeks, Niako has reduced its shareholding from 7.9 percent to 5.9 percent. While we acknowledge the risk that Niako could place additional pressure on the share price by further reducing its stake, we do not see this as a fundamental change in the business's prospects, and would instead view the weakness as a buying opportunity.

Speaking of fundamentals, let's provide a re-cap of Zanamivir, Biota's most important drug development. Marketed as Relenza, it is an inhalation administered drug used for the prevention and treatment of influenza. The drug was licensed to GlaxoSmithKline in 1990 for worldwide development and began commercialisation and marketing in 1999. Biota receives a 7 percent royalty on all of Relenza's sales.

The outlook for future royalty payments is a point of focus for investors. In a Open Briefing provided to the market in August, Mr Cook said he expects 'modest growth' in Relenza royalties in the current financial year. While Biota does not receive specific sales information from Glaxo, it expects Relenza sales to grow as governments continue to stockpile influenza antivirals throughout the year.

Stockpiling of influenza treatment began on the back of World Health Organisation (WHO) recommendations. The WHO indicated several years ago that influenza treatment increases were necessary to protect against a possible pandemic. The SARS outbreak in 2003 and subsequent 'bird-flu' scares have lifted government awareness of the potential threat.

The WHO says that even though production capacity should almost double by 2010 at the current rate of capacity expansion, it will still be insufficient to protect the global population in the event of a serious outbreak.

Thus, we believe there is scope for influenza treatment capacity to rise in the coming years. Indeed, the value of the global stockpiling market continues to grow, reaching an estimated US\$6.5 billion, up from the previous estimate of US\$5.6 billion only a few months ago.

This solid market growth bodes well for Relenza. And in terms of market share, the drug is a long way behind competitor Tamiflu, an orally administered drug developed by Roche. While Tamiflu may have secured a higher market share due to ease of administration (as opposed to Relenza's disk-inhaler delivery), Tamiflu side effects have started to surface.

As Tamiflu's administered treatment of the virus is achieved when it is absorbed through the bloodstream, the wider exposure to unaffected parts of the body means side effects become more likely.

In addition, there is increasing evidence that Relenza's effectiveness is superior to that of Tamiflu. Biota's management explained that this may be because Relenza's treatment is delivered directly to the infected lung area, whereas Tamiflu's oral administration fails to target the area precisely.

Biota also has other products in the pipeline. It has recently commenced Phase I clinical trials for its respiratory syncytial virus (RSV) drug, partnering with MedImmune. For a more detailed discussion on this, refer to FAT338.

In addition to the RSV development, Biota is also developing a Hepatitis C virus program in conjunction with Boehringer Ingelheim (BI). BI will be paying Biota milestone and research support, together with future royalties if the product progresses to commercialisation.

The third major drug program in the pipeline is human rhinovirus, which is a major cause of hospitalisation for patients with underlying respiratory conditions. Phase I trials have been completed and the company is looking to complete Phase IIa before partnering with a larger pharmaceutical.

And related to Relenza is Biota's development of LANI, a second generation influenza product which is also administered by inhalation, developed in partnership with Daiichi-Sankyo. Phase II testing is due to commence very shortly.

Three out of the four development programs are conducted in partnership with others. This effectively reduces the company's development risk and offers some stability in earnings by virtue of "collaboration income" earned during the process.

Almost a quarter of Biota's revenues last year came from collaboration income. By partnering with pharmaceutical companies early in the process, Biota also secures distribution channels and marketing support should the drugs successfully complete clinical trials. We therefore view the collaboration strategy as a low risk and efficient use of shareholder funds.

So despite the recent share price weakness, we view the underlying fundamentals of the business as positive. Perhaps investors are also concerned with the ongoing legal feud between Biota and Glaxo.



Biota has a litigation claim against Glaxo which now stands at between \$564 - \$704 million, the reasons for which we outlined in our initial report (FAT332). Biota remains confident they have a very strong case against Glaxo, however the big Pharma is employing delaying tactics in responding to Biota's claims.

Because of this, the trial date initially set for April has been pushed back to 1 July 2008. However, we believe there is a strong chance mediation may result in a settlement before this date.

In the meantime, legal costs are mounting for Biota. In this financial year, the company expects litigation costs of around \$15 million, following 2007 financial costs of \$10.4 million. While this is an obvious drag on short term earnings, Biota remains committed to the fight and has ample funds to do so, finishing the year with a cash balance of \$62.2 million

From a charting perspective, although the near term outlook for Biota has deteriorated significantly over the past month and we cannot rule out a further decline in prices in the near term, the daily technical indicators signal that the stock is 'oversold' at current levels.

While the technical indicators have been damaged due to the sell-down of a substantial shareholder, we do not believe the company's fundamentals have changed to warrant the sell-off. As such, we view the current

weakness as a buying opportunity. We are increasing our exposure to Biota and **recommend the stock as a buy to all Members around \$1.36.**

Note that Biota is a high risk recommendation. Due to the lack of analyst coverage, no consensus earnings estimates are included.

Interests associated with Fat Prophets declare a holding in BTA

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