Biota Holdings

GSK Reports Q3 Relenza

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$0.42

BUY

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Price Performance

Security/Capital Details

ASX Code	BTA
Market Cap	$73.9 M
Issued Shares	174.5 M
Avg Mth T'over	9.27 M
12 Mth High – Low	$1.63 - $0.40

Key Data/Ratios – FY 2009

Cash	$62.9 M
Burn	$28 M
EV	$11 M
Interest Cover	-1.9 x
ROE	19.3%
EPS Growth	415.6%
PEG Ratio	0.02 x
NTA / Share	$ 0.32
DCF	$ 1.27
12 Mth Price Target	$ 1.42

Recommendation

GSK reported their Q3 results last night which included Relenza sales of £12M ($27.1M). This corresponds to an indicative royalty to BTA of $1.9M. The GSK Q3 Relenza figure has been the weakest quarter, historically, so this small number does not come as a surprise. But it does put pressure on the Q4-2008 and Q1-2009 numbers, which have to be stronger now to bolster our faith in this product, and in gauging whether the renewed GSK/BTA commitment to Relenza is real. We make no change to our valuation. We reiterate our BUY recommendation and in doing so, provide further commentary on recent events and our outlook for BTA.

Key Points

- Overnight, GSK reported their Q3 results which included Relenza sales of £12M ($27.1M). This corresponds to an indicative royalty to BTA of approximately $1.9M subject to adjustments. The GSK Q3 Relenza figure has been the weakest quarter, historically, so this small number does not come as a surprise to us.
- This modest result does put pressure on the Q4-2008 and Q1-2009 numbers to come, which have to be stronger now to meet our FY09 forecast of $21.3M. A much stronger Q4-2008 and Q1-2009 result is also needed to bolster faith in the product. After the litigation settled both companies announced a renewed commitment to Relenza. The test of that is sales performance in the "good quarters" which are upon us now. Stockpile buying does exhibit an element of seasonality.
- BTA has completed its on-market share buyback scheme, filing its Appendix 3F on 7 October. During this process, BTA bought back 9.16M shares at a cost of $7.95M. This effort will have reduced their share capital base by ~5% once all those shares are cancelled.
- BTA remains one of the better resourced biotechnology companies and held $62M cash as at June 30. R&D costs are significant in FY09 on account of Phase II trials for BTA798 (HRV). BTA is forecasting a cash-neutral FY09 even after the buyback expense.
- The fundamentals of BTA's business remain the same and we retain high levels of conviction on several BTA programmes – Relenza, CS8958 (LANI; influenza) and BTA9881 (RSV) remain particular strengths.
- Our DCF for BTA is unchanged at $1.27 ps. **We reiterate our BUY case for the stock, which is now trading at cash backing plus 6 cps for Relenza royalties to 2013 and the mature product pipeline**.

BUY: Total return +10% or more over a 12 month period
HOLD: Total return expected to be between +10% to -10% over a 12-month period
SELL: Total return expected to be -10% or more over a 12 month period
TOTAL RETURN OR TSR = capital growth in share price + expected dividend yield in that period

Year to June	NPAT (Rep) $M	EPS (Norm) c	EPS Growth %	PER x	P/CF x	EV/EBITDA x	DPS c	Div Yld %	Franking %
2008a	-6.5	-2.6	-122.6	-30.0	29.3	-8.4	0.0	0.0	0
2009e	12.7	8.1	415.6	6.4	10.2	2.8	0.0	0.0	0
2010e	9.9	6.6	-19.1	7.9	-31.9	4.7	0.0	0.0	0
2011e	3.3	2.9	-56.3	18.1	4.9	25.0	0.0	0.0	0

BTA – an update

Keen observers at last Thursday's WHTM Life Science Conference would have observed a subtle but significant change in message from Peter Cook, the BTA CEO. For some time now, company presentations have spoken about rewarding shareholders though share price growth. Last Thursday's presentation spoke of asset growth, which meant the progress BTA is making made with the drug development programs it owns.

The change implies recognition by the company that the assets and the share price are no longer linked. That is obvious to all. The BTA share price has been horrible since May. BTA was punished by the market for the unexpected and disappointing resolution of the GSK litigation matter in July. Expectations around the GSK matter were not managed well; nor were the post-settlement communications. BTA have also suffered acutely through the recent worsening in market conditions, which have pushed the stock to a 3-year low.

With a projected end-FY09 cash balance of $62M the stock is now valued at cash backing plus 6 cps for the assets that Peter Cook talks about. They are good assets. Listing them once more:

- Relenza royalties to 2013;
- The CS8958 program in influenza, co-owned with Daiichi Sankyo and set to commence Phase III by the end of this year;
- the AstraZeneca RSV program;
- the Boehringer Ingelheim HCV program;
- the wholly owned Phase IIa HRV program.

BTA – underlining our investment case

We reiterate that our view on BTA is focussed on the BTA pipeline. The performance of this company in that endeavour – forget the share price for the time being – this year, has been excellent.

Our investment thesis is threefold:

- that this pipeline will provide the products that replace and surpass Relenza royalties;
- that the future earnings streams will be diversified and easier for the market to value than the very erratic and opaque Relenza product;
- that Relenza royalties, while volatile, subsidise operations and make capital raising and shareholder dilution less likely.

Catalysts – what will and won't turn BTA around?

Chair and Board appointments

The BTA Board did not come out of the GSK matter well, though it is probably simplistic to read too much into the resignations of Gibson and Grant. Nevertheless, their replacements are going to come under a lot of scrutiny in this market, which does entertain a less than charitable view of this Board. Only strong appointments here will be rewarded.

A Relenza turnaround

We suspect that some of the recent weakness in Relenza was due to the deteriorated relationship between GSK and BTA; particularly while the litigation matter was alive. It is too much to expect that relationship to have normalised materially; yet the dual commitment to Relenza is there, articulated in the post-settlement press release. Outside that relationship, the real world continues to express demand for more Relenza and Tamiflu – both the US and UK public health bureaucracies saying they should double their stockpiles. No new orders yet, but the UK has already put out a fresh batch of tenders to supply influenza drugs. We think it likely that GSK will find a role in supplying the UK tenders. GSK have also recently announced programs to supply Relenza to corporates – protecting workforces from seasonal influenza.

Partnering deals

The best prospects for new corporate activity are the CS8958 (LANI) and BTA798 (HRV) programs. The former has ex-Japanese rights to partner; the latter, worldwide rights. While these are significant events and we look forward to them, we do not expect they will have a large impact on the shareprice, because both products are still some years away from market. Licensing and milestone payments are expected to help BTA's working capital, they don't get distributed to shareholders. The RSV and HCV programs also hold prospects for success milestone payments, but we do not see the shareprice reacting to those events.

New programs

BTA has been very clear in its intentions to build the number of programs it runs – perhaps to a dozen or more. Already this year two new exploratory programs have been added in Hepatitis C and cytomegalovirus (CMV). We expect the in-licensing of early stage (preclinical, Phase I) programs will be ignored by the market. The company has a large enough balance sheet and mature enough business development capabilities to focus their intentions further upstream and acquire interests in more mature clinical assets.

Biota Holdings (BTA : $0.42)

INVESTMENT FUNDAMENTALS

Yr Ending June	2007A	2008A	2009E	2010E	2011E
EPS Reported (c)	11.2	-3.7	7.3	5.7	1.9
EPS Normalised (c)	**11.4**	**-2.7**	**8.4**	**6.8**	**3.0**
EPS Growth (%)	N/A	-123.7%	412.6%	-19.1%	-56.3%
PER Normalised (x)	**10.6**	**-28.6**	**6.2**	**7.7**	**17.5**
DPS (c)	0.0	0.0	0.0	0.0	0.0
Payout (%)	**0.0%**	**0.0%**	**0.0%**	**0.0%**	**0.0%**
Yield (%)	0.0%	0.0%	0.0%	0.0%	0.0%
Franking (%)	0%	0%	0%	0%	0%

VALUATION DATA

Yr Ending June	2007A	2008A	2009E	2010E	2011E
EV / EBITA (x)	8.6	-7.7	2.7	4.9	-58.8
EV / EBITDA (x)	8.0	-8.4	2.5	4.3	20.5
CFPS (c)	11.6	2.8	5.3	-1.7	11.1
Price / CF	**10.3**	**27.9**	**9.9**	**-30.8**	**4.7**
Book Value / Share ($)	0.4	0.4	0.4	0.4	0.4
Price / Book (x)	**3.0**	**2.1**	**1.3**	**1.2**	**1.2**

PROFIT & LOSS ($m)

Yr Ending June	2007A	2008A	2009E	2010E	2011E
Sales Revenue	55.8	20.5	21.3	27.6	28.2
EBITDA	19.2	-9.8	11.3	7.6	0.7
Depreciation	1.2	0.9	1.0	1.0	1.0
EBITA	**18.0**	**-10.7**	**10.3**	**6.6**	**-0.3**
Amortisation	0.3	1.8	2.0	2.0	1.9
EBIT	**17.7**	**-12.5**	**8.3**	**4.6**	**-2.2**
Net Interest Expense	-2.5	-3.2	-4.4	-5.3	-5.4
Pre-tax Profit	**20.2**	**-9.3**	**12.7**	**9.9**	**3.3**
Tax	0.0	-2.8	0.0	0.0	0.0
Tax rate (%)	0.0%	30.3%	0.0%	0.0%	0.0%
Minorities / pref divs	0.0	0.0	0.0	0.0	0.0
Equity accounted NPAT	0.0	0.0	0.0	0.0	0.0
Net Profit	**20.2**	**-6.5**	**12.7**	**9.9**	**3.3**
Abn's / Extraord's	0.0	0.0	0.0	0.0	0.0
Reported Net Profit	20.2	-6.5	12.7	9.9	3.3
Revenue Growth (%)	N/A	-63.2%	3.7%	29.7%	2.2%
EBIT Growth (%)	N/A	-170.8%	166.1%	-44.3%	-146.8%
NPAT Growth (%)	N/A	-132.2%	295.4%	-22.2%	-66.7%

PROFITABILITY RATIOS

Yr Ending June	2007A	2008A	2009E	2010E	2011E
EBIT / Sales (%)	**31.7%**	**-60.9%**	**38.8%**	**16.7%**	**-7.6%**
ROA (%)	N/A	-42.0%	27.9%	15.3%	-7.8%
ROE (%)	**N/A**	**-9.6%**	**19.3%**	**13.8%**	**4.4%**
ROFE (%)	N/A	-170.8%	248.9%	60.4%	-3.1%

INTERIMS ($m)

Half Yr	Dec 07	Jun 08	Dec 08	Jun 09	Dec 09
Yr Ending June	**1H A**	**2H A**	**1H E**	**2H E**	**1H E**
Sales Revenue	16.5	4.1	8.5	12.8	11.1
EBIT	5.7	-18.2	3.1	5.2	2.4
Net Profit	**5.5**	**-12.0**	**6.1**	**6.6**	**5.6**
EBIT / Sales (%)	34.6%	-448.7%	36.3%	40.5%	22.1%

BALANCE SHEET ($m)

Yr Ending June	2007A	2008A	2009E	2010E	2011E
Cash	62.2	60.2	62.9	58.1	75.5
Receivables	9.4	4.3	5.0	5.2	4.4
Inventories	0.0	0.0	0.0	0.0	0.0
Other	0.0	0.0	0.0	0.0	0.0
Current Assets	**71.5**	**64.4**	**67.9**	**63.3**	**79.9**
Net PPE	4.9	7.5	8.0	8.9	9.9
Investments	0.0	0.0	0.0	0.0	0.0
Intangibles	13.7	12.1	10.1	8.1	6.2
Other	2.4	5.2	7.0	8.0	4.9
Non-current Assets	**21.0**	**24.8**	**25.2**	**25.0**	**21.0**
Total Assets	**92.5**	**89.3**	**93.1**	**88.3**	**100.9**
Current Payables	6.0	12.0	12.0	7.0	7.5
Current Debt	0.0	0.0	0.0	0.0	0.0
Non-Current Debt	0.0	0.0	0.0	0.0	0.0
Provisions	7.4	1.3	2.8	2.4	0.7
Other	7.5	12.7	10.2	4.0	17.4
Total Liabilities	**20.9**	**26.0**	**25.0**	**13.4**	**25.6**
Equity	161.7	159.1	154.2	154.2	154.2
Reserves	0.6	1.4	1.4	1.4	1.4
Retained Profits	-90.8	-97.3	-87.6	-80.7	-80.3
Minorities	0.0	0.0	0.0	0.0	0.0
Total Equity	**71.5**	**63.3**	**68.0**	**74.9**	**75.3**
Total Funds Employed	**9.4**	**3.1**	**5.1**	**16.8**	**-0.2**

LIQUIDITY & LEVERAGE RATIOS

Yr Ending June	2007A	2008A	2009E	2010E	2011E
Net Debt (Cash) ($m)	-62.2	-60.2	-62.9	-58.1	-75.5
Net Debt / Equity (%)	**-86.9%**	**-95.0%**	**-92.5%**	**-77.6%**	**-100.3%**
Interest Cover (x)	-7.0	3.9	-1.9	-0.9	0.4
Debt / CashFlow (x)	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**

CASHFLOW ($m)

Yr Ending June	2007A	2008A	2009E	2010E	2011E
EBIT	17.7	-12.5	8.3	4.6	-2.2
Dep'n and Amort'n	1.6	2.7	3.0	3.0	2.9
Net Int Rec'd (Paid)	2.5	3.2	4.4	5.3	5.4
Tax Paid	0.0	0.0	0.0	0.0	0.0
Dec / (Inc) W'kg Cap	-4.7	9.7	-0.8	-5.2	1.3
Other	4.0	2.6	-2.7	-7.6	14.8
Operating Cash Flow	**21.0**	**4.8**	**9.2**	**-3.0**	**19.4**
Capital Expenditure	-0.9	-3.8	-1.5	-1.9	-2.0
Asset Sales	0.0	0.0	0.0	0.0	0.0
Investments	-5.5	0.0	0.0	0.0	0.0
Other Inv. Flows	0.0	0.0	0.0	0.0	0.0
Investing Cash Flow	**-6.4**	**-3.8**	**-1.5**	**-1.9**	**-2.0**
Equity Raised	1.4	0.0	0.0	0.0	0.0
Inc / (Dec) in Loans	0.0	0.0	0.0	0.0	0.0
Dividends Paid	0.0	0.0	0.0	0.0	0.0
Other Fin. Flows	0.0	-3.0	-5.0	0.0	0.0
Financing Cash Flow	**1.4**	**-3.0**	**-5.0**	**0.0**	**0.0**
Net Cash Flow	**16.0**	**-2.0**	**2.8**	**-4.8**	**17.4**

Disclosure of Interest. The Directors of Wilson HTM Ltd advise that at the date of this report they and their associates have relevant interests in 58,080 securities in Biota Holdings. They also advise that Wilson HTM Ltd and Wilson HTM Corporate Finance Ltd A.B.N. 65 057 547 323 and their associates have received and may receive commissions or fees from Biota Holdings in relation to advice or dealings in securities. Some or all of Wilson HTM Ltd authorised representatives may be remunerated wholly or partly by way of commission.

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