

13 January 2010

Produced and issued by: RBS Morgans Limited

# Biota Holdings

## Looking through the noise

### Buy

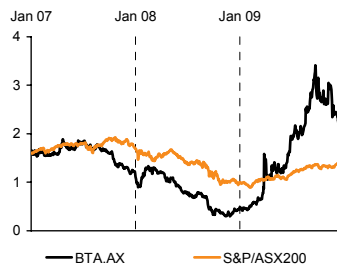
**Target price**  
A\$3.48

**Price**  
A\$2.07

**Short term (0-60 days)**  
n/a

#### Price performance

	(1M)	(3M)	(12M)
Price (A\$)	2.66	3.10	0.44
Absolute (%)	-22.2	-33.2	365.2
Rel market (%)	-26.4	-35.4	249.7
Rel sector (%)	-22.7	-34.1	351.9


**Market capitalisation**  
A\$353.97m (US\$328.93m)

**Average (12M) daily turnover**  
A\$2.13m (US\$1.79m)

 RIC: BTA.AX, BTA AU  
 Priced A\$2.07 at close 13 Jan 2010.  
 Source: Bloomberg

#### Analysts

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**BTA's share price continues its volatile ride. Press commentary surrounding lower infection rates and vaccines being returned to manufacturers are not helping sentiment. Putting swine flu aside, BTA is building a solid base for longer-term growth.**

#### Key forecasts

	FY08A	FY09A	FY10F	FY11F	FY12F
EBITDA (A\$m)	-9.78	44.30	98.30	128.0	52.40
Reported net profit (A\$m)	-6.49	38.20	76.10	87.70	40.20
Normalised net profit (A\$m) <sup>1</sup>	-6.49	38.20	76.10	87.70	40.20
Normalised EPS (c) <sup>1</sup>	-3.79	22.40	43.40	50.00	22.90
Normalised EPS growth (%)	n/a	n/a	94.20	15.20	-54.1
Dividend per share (c)	0.00	0.00	0.00	0.00	0.00
Dividend yield (%)	0.00	0.00	0.00	0.00	0.00
Normalised PE (x)	n/m	9.26	4.77	4.14	9.02
EV/EBITDA (x)	n/m	6.03	2.18	0.99	1.50
Price/net oper. CF (x)	73.50	10.50	4.91	4.07	7.15
ROIC (%)	-93.4	869.1	625.2	622.8	249.6

1. Pre non-recurring items and post preference dividends

year to Jun, fully diluted

Accounting standard: IFRS

Source: Company data, RBS Morgans forecasts

#### Press reports on lower hospitalisation rates may be short lived

Press reports suggesting that flu activity is decreasing in the northern hemisphere and some vaccines orders are being cut or returned to the manufacturer have significantly impacted the sentiment towards BTA. The latest Centre for Disease (CDC) briefing has cautioned against the general population and governments becoming complacent. Doctor visitation and hospitalisation rates are the key measures of disease spread. In the US, it appears that influenza peaked in November and returned to more normal levels in December. The CDC has commented that it is very difficult to predict the continuing spread and severity of the disease and note the possibility of another wave emerging later in the season. The flu season is expected to end in May. The provision of weekly updates enables us to monitor this closely.

#### Next milestone: GSK quarterly results

The next milestone to watch for will be GlaxoSmithKline's (GSK) quarterly results due 4 February 2010 (UK time). We expect continued strong growth in Relenza royalties. We forecast royalties of A\$133m for FY10, which will be driven by major government orders particularly from the UK and US. Although we don't forecast quarterly royalties in any detail, we estimate royalties between A\$30m to A\$35m could be achieved.

#### Investment view: A\$3.48 valuation and price target unchanged

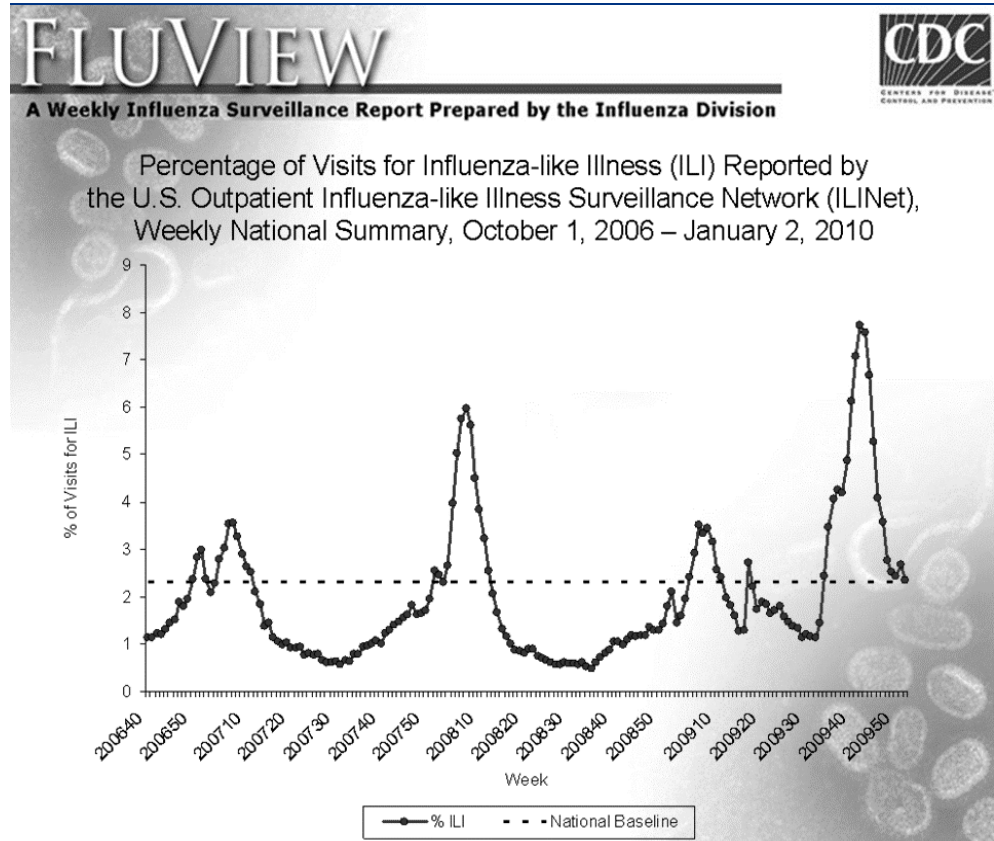
Our DCF valuation and price target remain unchanged at A\$3.48. The key assumptions in deriving the valuation include a risk-free rate of 5.25%, WACC of 13.6% and terminal growth rate of 3.5%. The main downside risk is a delay in GSK receiving regulatory approval for the alternative disk inhaler (known as Rotahaler) therefore limiting its ability to achieve theoretical full production of 190m courses.

**Important disclosures can be found in the Disclosures Appendix.**

### Centre for Disease cautions against becoming complacent

In a briefing on 7 January 2010, the CDC noted that the H1N1 virus was continuing to circulate in the US, although hospitalisation rates and doctor visitations had declined in December, possibly partially impacted by the holiday season. Chart 1 shows that the percentage of visits for influenza-like illness returned to normal levels in December after peaking in November. However, the CDC did caution against the general population and governments becoming complacent and continues to recommend vaccination as a key defence measure. It noted that it is too early to say whether or not another wave may not occur with the flu season not expected to finish until May 2010. According to the CDC, 15% of the US population has been infected with the H1N1 virus. Approximately 20% of the population has been vaccinated at this point.

Chart 1 : Weekly Influenza Surveillance Report



Source: CDC

### GSK quarterly results the next driver

The next milestone to watch for will be GSK's quarterly results due early February 2010. We expect continued strong growth in Relenza royalties. We forecast royalties of A\$133m for FY10, which will be driven by major government orders particularly from the UK and US. Although we don't forecast quarterly royalties in any detail, we estimate 4Q royalties between A\$30m to A\$35m could be achieved. The 3Q royalty was A\$24.1m and BTA had A\$77.4m in cash as at 30 September 2009.

Underpinning our forecasts is GSK's intention to increase production from 60m to 190m courses. To achieve this increase, GSK is seeking regulatory approval for an alternative device known as a Rotahaler. In previous notes, we have highlighted the growing body of evidence which suggests resistance is emerging to the competing product Tamiflu to certain H1N1 strains. As a result, there is the potential for governments to look to rebalance stockpiles with a more equal weighting towards Relenza. Typically global stockpiles are 20% Relenza and 80% Tamiflu.

## BTA overview

BTA is a leading anti-infective drug development company with expertise in respiratory diseases, particularly influenza. Biota developed the flu drug known as Relenza™ which is marketed by GSK. Relenza is used to treat seasonal influenza and is currently being stockpiled by various governments for defence against possible pandemic outbreaks of avian (bird) and swine (pig) influenza. BTA receives a 7% royalty on the sale of each course of Relenza.

Figure 2 : BTA – financial summary

Year to 30 Jun (A\$m)	AIFRS 2008A	AIFRS 2009A	AIFRS 2010F	AIFRS 2011F	AIFRS 2012F	Closing price (A\$)	2.07	Price target (A\$)	3.48		
<b>Income statement</b>						<b>Valuation metrics</b>					
Divisional sales	41.7	80.4	148.8	165.9	70.3	Preferred methodology	DCF	Val'n (A\$)	\$ 3.48		
Total revenue	41.7	80.4	148.8	165.9	70.3	<b>DCF valuation inputs</b>					
<b>EBITDA</b>	<b>-9.8</b>	<b>44.3</b>	<b>98.3</b>	<b>128.0</b>	<b>52.4</b>	Rf	5.25%	10-year rate	5.25%		
Associate income	0.0	0.0	0.0	0.0	0.0	Rm-Rf	6.00%	Margin	2.0%		
Depreciation	-2.7	-5.4	-6.0	-5.4	-1.7	Beta	1.40	Kd	7.25%		
EBITA	-12.5	38.9	92.2	122.6	50.7	CAPM (Rf+Beta(Rm-Rf))	13.6%	Ke	13.7%		
Amortisation/impairment	0.0	0.0	0.0	0.0	0.0	Equity (E/EV)	100.0%	NPV cash flow (A\$m)	471.1		
EBIT	-12.5	38.9	92.2	122.6	50.7	Debt (D/EV)	0.0%	Minority interest (A\$m)	0.0		
EBIT (incl associate profit)	-12.5	38.9	92.2	122.6	50.7	Interest rate	7.25%	Net debt (A\$m)	-139.4		
Net interest expense	3.2	2.9	2.6	4.2	6.8	Tax rate (t)	30.0%	Investments (A\$m)	0.0		
Pre-tax profit	-9.3	41.9	94.8	126.8	57.5	Franking credit	100.0%	Equity market value (A\$m)	610.4		
Income tax expense	2.8	-3.6	-18.7	-39.1	-17.2	<b>WACC</b>	13.7%	Diluted no. of shares (m)	175.3		
After-tax profit	-6.5	38.2	76.1	87.7	40.2			<b>DCF valuation (A\$)</b>	<b>3.48</b>		
Minority interests						<b>Multiples</b>		<b>2009A</b>	<b>2010F</b>	<b>2011F</b>	<b>2012F</b>
<b>NPAT</b>	<b>-6.5</b>	<b>38.2</b>	<b>76.1</b>	<b>87.7</b>	<b>40.2</b>	Enterprise value (A\$m)	265.6	212.9	125.6	76.6	
Significant items	0.0	0.0	0.0	0.0	0.0	EV/Sales (x)	3.3	1.4	0.8	1.1	
NPAT post abnormal	-6.5	38.2	76.1	87.7	40.2	EV/EBITDA (x)	6.0	2.2	1.0	1.5	
						EV/EBIT (x)	6.8	2.3	1.0	1.5	
						PE (pre-goodwill) (x)	9.2	4.7	4.1	9.0	
<b>Cash flow statement</b>	<b>2008A</b>	<b>2009A</b>	<b>2010F</b>	<b>2011F</b>	<b>2012F</b>	<b>At target price</b>	<b>2009A</b>	<b>2010F</b>	<b>2011F</b>	<b>2012F</b>	
EBITDA	-9.8	44.3	98.3	128.0	52.4	EV/EBITDA (x)	11.5	4.6	2.9	6.1	
Change in working capital	8.6	-9.9	-8.3	-4.0	8.8	PE (pre-goodwill) (x)	15.6	8.0	7.0	15.2	
Net interest (pd)/rec	3.2	2.9	2.6	4.2	6.8	<b>Comparable company data (x)</b>		<b>2010F</b>	<b>2011F</b>	<b>2012F</b>	
Taxes paid	2.8	-3.6	-18.7	-39.1	-17.2	Avexa	EV/EBITDA	-5.5	-16.8	0.5	
Other oper cash items	0.0	0.0	0.0	0.0	0.0	Year to 30 Jun	EV/EBIT	-5.4	-15.6	0.5	
Cash flow from ops (1)	4.8	33.7	73.8	89.0	50.7		PE	-11.8	-31.1	2.3	
Capex (2)	-3.8	-0.8	-1.2	-1.8	-1.7	Pharmaxis	EV/EBITDA	-12.8	-14.5	92.0	
Disposals/(acquisitions)	0.0	0.0	0.0	0.0	0.0	Year to 30 Jun	EV/EBIT	-11.9	-13.5	183.2	
Other investing cash flow	0.0	0.0	0.0	0.0	0.0		PE	-14.6	-14.8	157.2	
Cash flow from invest (3)	-3.8	-0.8	-1.2	-1.8	-1.7	<b>Per share data</b>		<b>2009A</b>	<b>2010F</b>	<b>2011F</b>	<b>2012F</b>
Incr/(decr) in equity	-3.0	-5.1	-20.0	0.0	0.0	No. shares	171.0	175.3	175.3	175.3	
Incr/(decr) in debt	0.0	0.0	0.0	0.0	0.0	EPS (cps)	22.4	43.4	50.0	22.9	
Ordinary dividend paid	0.0	0.0	0.0	0.0	0.0	EPS (normalised) (c)	22.4	43.4	50.0	22.9	
Preferred dividends (4)	0.0	0.0	0.0	0.0	0.0	Dividend per share (c)	0.0	0.0	0.0	0.0	
Other financing cash flow	0.0	0.0	0.0	0.0	0.0	Dividend payout ratio (%)	0.0	0.0	0.0	0.0	
Cash flow from fin (5)	-3.0	-5.1	-20.0	0.0	0.0	Dividend yield (%)	0.0	0.0	0.0	0.0	
Forex and disc ops (6)	0.0	0.0	0.0	0.0	0.0	<b>Growth ratios</b>		<b>2009A</b>	<b>2010F</b>	<b>2011F</b>	<b>2012F</b>
Incr/(decr) cash (1+3+5+6)	-2.0	27.8	52.7	87.3	49.0	Sales growth	92.6%	85.1%	11.5%	-57.6%	
<b>Equity FCF (1+2+4)</b>	<b>1.0</b>	<b>32.9</b>	<b>72.7</b>	<b>87.3</b>	<b>49.0</b>	Operating cost growth	-30.0%	40.2%	-25.1%	-52.8%	
						EBITDA growth				-59.1%	
						EBITA growth				-58.7%	
<b>Balance sheet</b>	<b>2008A</b>	<b>2009A</b>	<b>2010F</b>	<b>2011F</b>	<b>2012F</b>	<b>Operating performance</b>		<b>2009A</b>	<b>2010F</b>	<b>2011F</b>	<b>2012F</b>
Cash & deposits	60.2	86.7	139.4	226.6	275.6	Asset turnover (%)	20.0	26.4	19.5	6.4	
Trade debtors	4.3	8.1	18.3	20.5	8.7	EBITDA margin (%)	55.2	66.0	77.2	74.6	
Inventory	0.0	0.0	0.0	0.0	0.0	EBIT margin (%)	48.4	62.0	73.9	72.1	
Investments	0.0	0.0	0.0	0.0	0.0	Net profit margin (%)	47.6	51.2	52.9	57.2	
Goodwill						Return on net assets (%)	40.1	60.2	50.9	18.0	
Other intangible assets	12.1	8.4	4.2	0.5	0.5	Net debt (A\$m)	-86.7	-139.4	-226.6	-275.6	
Fixed assets	7.5	6.9	6.3	6.4	6.4	Net debt/equity (%)	-89.4	-91.0	-94.1	-98.1	
Other assets	5.2	1.5	1.5	1.5	1.5	Net interest/EBIT cover (x)	-13.3	-35.5	-29.3	-7.5	
<b>Total assets</b>	<b>89.3</b>	<b>111.6</b>	<b>169.7</b>	<b>255.5</b>	<b>292.7</b>	ROIC (%)	869.1	625.2	622.8	249.6	
Short-term borrowings	0.0	0.0	0.0	0.0	0.0	<b>Internal liquidity</b>		<b>2009A</b>	<b>2010F</b>	<b>2011F</b>	<b>2012F</b>
Trade payables	12.0	5.6	7.6	5.7	2.7	Current ratio (x)	6.5	9.5	16.8	24.4	
Long-term borrowings	0.0	0.0	0.0	0.0	0.0	Receivables turnover (x)	13.0	11.3	8.6	4.8	
Provisions	0.0	0.0	0.0	0.0	0.0	Payables turnover (x)	4.1	7.6	5.7	4.3	
Other liabilities	13.9	9.0	9.0	9.0	9.0						
<b>Total liabilities</b>	<b>26.0</b>	<b>14.6</b>	<b>16.6</b>	<b>14.7</b>	<b>11.7</b>						
Share capital	159.1	154.6	210.7	298.4	338.6						
Other reserves	1.4	1.5	1.5	1.5	1.5						
Retained earnings	-97.3	-59.1	-59.1	-59.1	-59.1						
Other equity	0.0	0.0	0.0	0.0	0.0						
Total equity	63.3	97.0	153.2	240.8	281.1						
Minority interest											
Total shareholders' equity	63.3	97.0	153.2	240.8	281.1						
<b>Total liabilities &amp; SE</b>	<b>89.3</b>	<b>111.6</b>	<b>169.7</b>	<b>255.5</b>	<b>292.7</b>						

Source: Company data, RBS Morgans forecasts

## Recommendation structure

Absolute performance, short term (trading) recommendation: A Trading Buy recommendation implies upside of 5% or more and a Trading Sell indicates downside of 5% or more. The trading recommendation time horizon is 0-60 days. For Australian coverage, a Trading Buy recommendation implies upside of 5% or more from the suggested entry price range, and a Trading Sell recommendation implies downside of 5% or more from the suggested entry price range. The trading recommendation time horizon is 0-60 days.

Absolute performance, long term (fundamental) recommendation: The recommendation is based on implied upside/downside for the stock from the target price. A Buy/Sell implies upside/downside of 10% or more and a Hold less than 10%. For UK Mid/Small Cap Analysis a Buy/Sell implies upside/downside of 10% or more, an Add/Reduce 5-10% and a Hold less than 5%. For UK-based Investment Funds research the recommendation structure is not based on upside/downside to the target price. Rather it is the subjective view of the analyst based on an assessment of the resources and track record of the fund management company. For listed property trusts (LPT) or real estate investment trusts (REIT) the recommendation is based upon the target price plus the dividend yield, ie total return.

Performance parameters and horizon: Given the volatility of share prices and our pre-disposition not to change recommendations frequently, these performance parameters should be interpreted flexibly. Performance in this context only reflects capital appreciation and the horizon is 12 months.

Sector relative to market: The sector view relative to the market is the responsibility of the strategy team. Overweight/Underweight implies upside/downside of 10% or more and Neutral implies less than 10% upside/downside.

Target price: The target price is the level the stock should currently trade at if the market were to accept the analyst's view of the stock and if the necessary catalysts were in place to effect this change in perception within the performance horizon. In this way, therefore, the target price abstracts from the need to take a view on the market or sector. If it is felt that the catalysts are not fully in place to effect a re-rating of the stock to its warranted value, the target price will differ from 'fair' value.

## Distribution of recommendations

The tables below show the distribution of recommendations (both long term and trading). The first column displays the distribution of recommendations globally and the second column shows the distribution for the region. Numbers in brackets show the percentage for each category where there is an investment banking relationship.

### Long term recommendations (as at 13 Jan 2010)

	Global total (IB%)	Asia Pacific total (IB%)
Buy	635 (9)	415 (0)
Add	0 (0)	0 (0)
Hold	391 (6)	216 (0)
Reduce	0 (0)	0 (0)
Sell	102 (0)	63 (0)
Total (IB%)	1128 (7)	694 (0)

Source: ABN AMRO

### Trading recommendations (as at 13 Jan 2010)

	Global total (IB%)	Asia Pacific total (IB%)
Trading Buy	3 (0)	3 (0)
Trading Sell	0 (0)	0 (0)
Total (IB%)	3 (0)	3 (0)

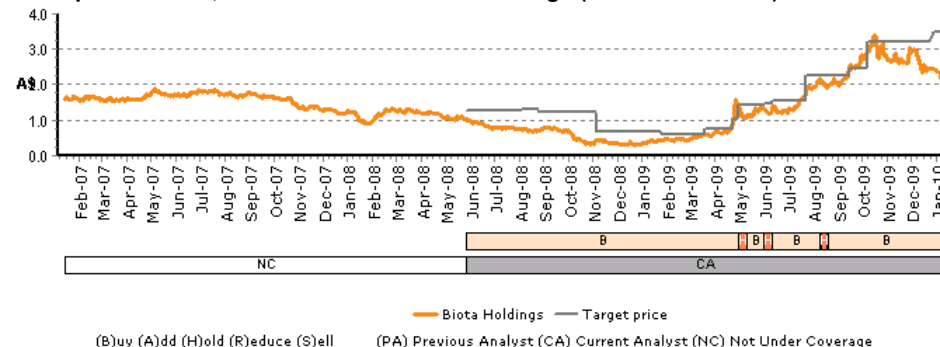
Source: ABN AMRO

## Valuation and risks to target price

**Biota Holdings (RIC: BTA.AX, Rec: Buy, CP: A\$2.07, TP: A\$3.48):** In valuing BTA we use a DCF methodology, from which we derive our target price. Key risks to our target price relate to a delay in partnering key projects or a failure to achieve key end points.

## Biota Holdings coverage data

### Stock performance, recommendations and coverage (as at 12 Jan 2010)



Scott Power started covering this stock on 27 May 08

Source: ABN AMRO

### Trading recommendation history (as at 13 Jan 2010)

Date	Rec	Analyst
19 Jun 2009	n/a	CA
30 Apr 2009	Trading Buy	CA

Source: ABN AMRO

## Regulatory disclosures

Subject companies: **BTA.AX**

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