

Pharming Group NV

Netherlands / Biotechnology

Primary exchange: Euronext Amsterdam /

Secondary exchange: Frankfurt

Bloomberg: PHARM NA

ISIN: NL0010391025

Acquisition of North
American marketing
rights

RATING**PRICE TARGET**

Return Potential

Risk Rating

BUY**€1.40**

527.8%

High

PHARMING TO TAKE OVER MARKETING OF RUCONEST IN THE U.S.A.

Pharming plans to acquire the North American commercialisation rights to its lead product, Ruconest, by the end of this year. Pharming has agreed to pay Valeant USD60m upfront and USD65m of self-funding milestone payments subject to procurement of adequate financing. Pharming proposes in a stepwise fashion to more than double the size of the team of sales representatives/medical liaison officers dedicated to Ruconest. We expect sharper focus as well as increased resources to enable Pharming to make the case for the advantages of its recombinant product, Ruconest over rival blood-based products more effectively than Valeant did. Pharming has so far received 30% of the revenue from US Ruconest sales. We expect the inclusion of 100% of Ruconest's US revenues on Pharming's P&L to push the company to profitability in 2017. According to management, this is three years earlier than previously budgeted. After taking into account likely future dilution and milestone payments to Valeant, we now see fair value for the Pharming share at €1.40 (previously: €1.00).

Valeant restructuring creates chance to acquire North American Ruconest rights Pharming plans to acquire North American commercialisation rights to Ruconest from Valeant. Santarus originally acquired the marketing rights to Ruconest in 2010 - four years ahead of the drug's FDA approval in July 2014. Santarus was then bought by Salix in 2013 which in turn was acquired by Valeant in spring 2015. Turmoil at Valeant, including a collapse in its share price, restatement of earnings, and management changes, prompted restructuring which has given Pharming the opportunity to acquire the North American Ruconest rights.

Payment to Valeant of USD60m upfront and USD65m in milestones Pharming has agreed an upfront payment to Valeant of USD60m and further self-funding milestone payments of up to USD65m. The USD60m payment will be funded through a combination of straight debt and new equity. (p.t.o.)

FINANCIAL HISTORY & PROJECTIONS

	2013	2014	2015	2016E	2017E	2018E
Revenue (€m)	6.84	21.19	10.83	12.86	45.60	65.30
Y-o-y growth	-35.5%	209.6%	-48.9%	18.8%	254.5%	43.2%
EBIT (€m)	-6.91	2.88	-12.83	-12.23	5.76	12.26
EBIT margin	-101.0%	13.6%	-118.5%	-95.1%	12.6%	18.8%
Net income (€m)	-15.06	-5.77	-9.96	-13.25	3.17	9.92
EPS (diluted) (€)	-0.07	-0.02	-0.02	-0.03	0.01	0.02
DPS (€)	0.00	0.00	0.00	0.00	0.00	0.00
FCF (€m)	-8.05	-3.23	-17.32	-79.42	-4.45	2.19
Net gearing	-302.8%	-109.9%	-67.0%	33.2%	39.0%	30.2%
Liquid assets (€m)	16.97	34.19	31.64	25.93	16.89	14.10

RISKS

The main risks to our price target include slower sales growth for Ruconest in the EU and the US than we currently model.

COMPANY PROFILE

Pharming develops and produces therapeutic proteins from the milk of genetically modified rabbits. Pharming and Chinese SIPI signed a collaboration agreement in 2013, which will accelerate the addition of new projects to the firm's R&D pipeline. Lead drug Ruconest received EMA approval in 2010 and FDA approval in July 2014.

MARKET DATA

As of 29 Aug 2016

Closing Price	€ 0.22
Shares outstanding	412.56m
Market Capitalisation	€ 92.00m
52-week Range	€ 0.17 / 0.38
Avg. Volume (12 Months)	2,804,037

Multiples	2015	2016E	2017E
P/E	n.m.	n.m.	43.5
EV/Sales	8.0	6.7	1.9
EV/EBIT	n.m.	n.m.	15.0
Div. Yield	0.0%	0.0%	0.0%

STOCK OVERVIEW



COMPANY DATA

As of 30 Jun 2016

Liquid Assets	€ 21.41m
Current Assets	€ 46.33m
Intangible Assets	€ 0.70m
Total Assets	€ 53.67m
Current Liabilities	€ 18.46m
Shareholders' Equity	€ 18.16m

SHAREHOLDERS

Kingdon Capital Management LLC	3.1%
Free Float	96.9%



Pharming plans to raise €73-€90m as a combination of debt and equity On 23 August Pharming announced that it will hold an EGM on 5 October and further stated that it is looking to raise €73-€90m as a combination of straight debt and equity. The proceeds will be used to finance the acquisition of the North American commercialisation rights from Valeant, expand commercialisation efforts in the USA and EU in a stepwise fashion, and ensure the availability of sufficient working capital. The transaction is subject to completion of financing, but is expected to close in the fourth quarter of this year. The equity portion of the deal will first be offered to existing shareholders in the form of a rights issue. Pharming currently has authorised share capital of €650m (650m shares). 184m shares are held in treasury. At the current share price, the issue of 184m shares would raise only c. €40m. At the EGM, management will propose a raise in the share capital to 150m shares. On the assumption that this proposal is accepted, a total of 334m shares would become available for the transaction. However, management have indicated that they do not expect that all the 334m shares will be issued. Pharming already had interest-bearing debt on its balance sheet of €14.9m at the end of H1 2016 and so is constrained in the amount of new debt it can assume. We have assumed total new funding of €75m comprised of €45m equity and €30m debt.

Pharming plans to double size of US sales rep./medical liaison team Valeant has a dedicated US sales force of 11 people. In the event that the transaction goes through, management has undertaken to offer the current US sales team positions with Pharming. Management have stated that they plan to gradually enlarge the US sales team in the months following closure as well as hire several medical liaison personnel. According to Pharming, lack of “doctor to doctor” contact was one of the weaknesses of the Valeant marketing effort. Pharming also plans additional marketing activities including patient advocacy programs and unconditional support for the US Hereditary Angioedema Patients Association. Part of the funds raised would also be used to accelerate growth in the EU, Middle East and Africa markets which Pharming will be taking over from SOBI from October this year and to make Ruconest available in Canada and Mexico.

Proforma H1 2016 sales 155% above reported sales; gross margin 85.2% vs. 62.3% Pharming published H1 proforma figures in its press release which are summarised in figure 1 below. Under the commercialisation agreement with Valeant, 30% of US Ruconest revenues were transferred to Pharming. The 155% increase in proforma H1 2016 revenues vs. actual H1 2016 revenues illustrates the impact of own commercialisation vs commercialisation by Valeant and corroborates management’s statement that the deal will be immediately accretive. The gross profit margin rises from 62.3% to 85.2% because of the shift in the mix to US sales, which are more profitable than European sales.

Figure 1: H1 2016 proforma P&L (€m)

	Actual HY 2016	Proforma HY 2016	% Δ
Revenues	5.3	13.5	155%
of which:			
Product sales	4.2	12.4	195%
License fees	1.1	1.1	0%
Gross profit	3.3	11.5	248%
margin (%)	62.3%	85.2%	
Operating result	-6.2	-3.1	
margin (%)	-117.0%	-23.0%	

Source: Pharming

We assume the deal closes near end 2016 and so leave current year forecasts largely unchanged In our forecasts, we assume that Pharming succeeds in acquiring commercialisation rights to Ruconest from Valeant. For the sake of simplicity, we assume that the deal closes at the end of Q4 2016 and have therefore left our forecasts for the current year largely unchanged.



On a proforma basis, our current FY2016 US product sales forecast of €8.8m (the H1 figure was €3.5m) would be €29.5m. The basis of our new 2017 and 2018 revenue forecasts of €45.6m and €65.3m respectively are the assumptions of 41% growth in US sales next year followed by 43% growth in 2018. We further assume that Pharming will be able to sustain the gross profit margin of c. 85% shown in the H1 2016 proforma figures. We see R&D expenses rising from €15.5m this year to €22.5m in 2017 and €29.0m in 2018. The main item here is likely to be the next stage in the development of Ruconest in the indication prophylaxis. Pharming and Valeant shared the costs of the phase II trial of Ruconest for prophylaxis of hereditary angioedema (HAE), results of which were published in July.

We maintain our Buy recommendation with a price target of €1.40 (previously: €1.00)

If self-commercialisation of Ruconest goes ahead, Pharming will bear the cost of the next stage of the development of Ruconest for HAE prophylaxis alone. We see general and administrative costs rising from €4.3m this year to €7.0m and €8.5m in 2017 and 2018 respectively as administrative requirements in the US rise. We also see marketing costs rising sharply to €5.8m by 2018 as Pharming takes on the cost of the existing Valeant Ruconest sales personnel and further expands the team itself. We further assume that milestones of USD20m and USD45m become payable in 2020 and 2021 respectively. Management have indicated that self-commercialisation of Ruconest will mean Pharming will reach profitability in 2017 - three years earlier than previously budgeted. We now see fair value for the share at €1.40 (previously: €1.00). We maintain our Buy recommendation.

Figure 2: Pipeline valuation

Compound	Project ¹⁾	Present Value	Patient Pop	Treatment Cost	Market Size	Market Share	Peak Sales	PACME Margin ²⁾	Discount Factor	Patent Life ³⁾	Time to Market
Ruconest (EU)	HAE-AA	€114.9M	4K	€90,909	€318M	20%	€79M	61%	0%	15	-
Ruconest (US)	HAE-AA	€1,215.2M	5K	€136,364	€727M	25%	€378M	86%	10%	12	-
Ruconest (EU)	HAE-PR	€48.8M	1K	€272,727	€250M	20%	€62M	61%	5%	6	3 Years
Ruconest (US)	HAE-PR	€479.9M	2K	€409,091	€636M	25%	€401M	86%	15%	7	3 Years
PACME PV		€1,858.8M			€1,932M		€920M				
Costs PV⁴⁾		€982.9M									
NPV		€875.9M									
Milestones PV		-€26.9M									
Net Cash (pro-forma)		€62.6M									
Fair Value		€911.6M									
Share Count (fully diluted)		642,013K									
Fair value per share		€1.42									

1) A project typically refers to a specific indication or, where necessary or relevant, a combination between indication and geographic market

2) PACME (Profit After Costs and Marketing Expenses) reflects the company's profit share on future revenues.

This share may be derived in the form of royalties (outsourced marketing/manufacturing) or operating EBITDA margin (in-house model), or some mix of both (depending on the specific parameters of partnership agreements)

3) Remaining patent life after the point of approval

4) Includes company-level R&D, G&A, Financing Costs and CapEx; COGS and S&M are factored into the PACME margin for each project

*) Combined PV of R&D projects DGF and AMI due to lower priority of the two projects

Source: First Berlin Equity Research

Figure 3: Changes to our pipeline valuation model

	Old	New	Delta
PACME PV	€598.8M	€1,858.8M	210.4%
Costs PV	€193.4M	€982.9M	408.2%
NPV	€405.4M	€875.9M	116.1%
Milestones PV	€1.1M	-€26.9M	0.0%
Net Cash	€19.3M	€62.6M	224.2%
Fair Value	€425.8M	€911.6M	114.1%
Share Count	447,771K	642,012K	43.4%
Fair value per share	€0.95	€1.42	49.3%

Source: First Berlin Equity Research



INCOME STATEMENT

All figures in EUR '000	2013A	2014A	2015A	2016E	2017E	2018E
Revenues	6,844	21,186	10,828	12,864	45,600	65,300
Costs of sales	-1,112	-3,427	-4,800	-4,334	-6,840	-9,795
Gross profit	5,732	17,759	6,028	8,530	38,760	55,505
Other income	106	105	147	275	0	0
Research and development	-10,232	-11,663	-14,180	-15,529	-22,500	-29,000
General and administrative	-2,518	-3,324	-3,744	-4,299	-7,000	-8,500
Marketing and sales	0	0	-1,085	-1,208	-3,500	-5,750
Operating income (EBIT)	-6,912	2,877	-12,834	-12,231	5,760	12,255
Net financial income	-8,148	-8,644	2,877	-1,023	-2,593	-2,338
Pre-tax income (EBT)	-15,060	-5,767	-9,957	-13,254	3,167	9,917
Income taxes	0	0	0	0	0	0
Minority interests	0	0	0	0	0	0
Net income / loss	-15,060	-5,767	-9,957	-13,254	3,167	9,917
Diluted EPS	-0.07	-0.02	-0.02	-0.03	0.01	0.02
EBITDA	-5,992	3,915	-10,477	-11,663	6,862	13,418
Ratios						
Gross margin on revenues	83.8%	83.8%	55.7%	66.3%	85.0%	85.0%
EBITDA margin on revenues	n.m.	18.5%	n.m.	n.m.	15.0%	20.5%
EBIT margin on revenues	n.m.	13.6%	n.m.	n.m.	12.6%	18.8%
Net margin on revenues	n.m.	n.m.	n.m.	n.m.	6.9%	15.2%
Expenses as % of revenues						
Cost of sales	16.2%	16.2%	44.3%	33.7%	15.0%	15.0%
Research and development	149.5%	55.1%	131.0%	120.7%	49.3%	44.4%
General and administrative	36.8%	15.7%	34.6%	33.4%	15.4%	13.0%
Marketing and sales	n.m.	n.m.	10.0%	9.4%	7.7%	8.8%
Y-Y Growth						
Revenues	-35.5%	209.6%	-48.9%	18.8%	254.5%	43.2%
Operating income	n.m.	n.m.	n.m.	n.m.	n.m.	112.8%
Net income/ loss	#BEZUG!	n.m.	n.m.	n.m.	n.m.	213.2%



BALANCE SHEET

All figures in EUR '000	2013A	2014A	2015A	2016E	2017E	2018E
Assets						
Current assets, total	24,599	49,143	51,092	53,587	55,645	66,337
Cash and cash equivalents	16,968	34,185	31,643	25,929	16,885	14,097
Receivables	860	1,554	3,220	5,789	11,400	16,325
Inventories	4,763	13,404	16,229	21,869	27,360	35,915
Other current assets	2,008	0	0	0	0	0
Non-current assets, total	6,809	6,575	6,585	61,143	62,211	63,351
Property, plant & equipment	6,228	5,598	5,661	6,175	7,296	8,489
Goodwill & other intangibles	405	777	724	54,768	54,715	54,662
Other assets	176	200	200	200	200	200
Total assets	31,408	55,718	57,677	114,730	117,856	129,688
Shareholders' equity & debt						
Current liabilities, total	12,925	14,873	13,475	14,932	20,796	23,293
Short term debt	0	0	3,047	5,000	5,000	2,721
Deferred license fee income	2,200	2,200	2,207	2,207	2,207	2,207
Derivative financial liabilities	4,147	4,266	953	953	953	953
Trade and other payables	5,812	7,781	7,005	5,789	11,400	16,325
Finance lease liabilities	766	626	263	983	1,236	1,087
Longterm liabilities, total	13,473	11,002	20,363	44,213	38,309	37,727
Long term debt	0	0	11,757	37,721	32,721	30,000
Deferred license fee income	12,222	10,022	7,808	5,622	4,560	6,530
Finance lease liabilities	1,207	965	798	870	1,028	1,197
Other liabilities	44	15	0	0	0	0
Minority interests	0	0	0	0	0	0
Shareholders equity	5,010	29,843	23,839	55,585	58,752	68,669
Total consolidated equity and debt	31,408	55,718	57,677	114,730	117,856	129,688
Ratios						
Current ratio (x)	1.90	3.30	3.79	3.59	2.68	2.85
Quick ratio (x)	1.53	2.40	2.59	2.12	1.36	1.31
Net gearing	-302.8%	-109.9%	-67.0%	33.2%	39.0%	30.2%
Book value per share (€)	0.01	0.07	0.06	0.09	0.10	0.11
Net cash	-15,171	-32,794	-15,978	18,445	22,899	20,707
Return on equity (ROE)	n.m.	-33.1%	-37.1%	-33.4%	5.5%	15.6%



CASH FLOW STATEMENT

All figures in EUR '000	2013A	2014A	2015A	2016E	2017E	2018E
EBIT	-6,912	2,877	-12,834	-12,231	5,760	12,255
Depreciation and amortization	920	1,038	2,357	568	1,102	1,163
EBITDA	-5,992	3,915	-10,477	-11,663	6,862	13,418
Other adjustments	-2,301	-6,488	-5,945	-12,634	-9,147	-8,923
Operating cash flow	-8,293	-2,573	-16,422	-24,297	-2,285	4,495
CAPEX	241	-654	-898	-55,125	-2,170	-2,303
Free cash flow	-8,052	-3,227	-17,320	-79,423	-4,455	2,192
Debt financing, net	16,023	-682	15,524	28,709	-4,589	-4,980
Equity financing, net	12,178	19,375	483	45,000	0	0
Other changes in cash	-5,454	-1,249	-1,229	0	0	0
Net cash flows	14,695	14,217	-2,542	-5,714	-9,044	-2,788
Cash, start of the year	5,273	19,968	34,185	31,643	25,929	16,885
Cash, end of the year	19,968	34,185	31,643	25,929	16,885	14,097
EBITDA/share	-0.03	0.01	-0.03	-0.03	0.01	0.02
Y-Y Growth						
Operating cash flow	n.m.	n.m.	n.m.	n.m.	n.m.	n.m.
Free cash flow	n.m.	n.m.	n.m.	n.m.	n.m.	n.m.
EBITDA/share	n.m.	n.m.	n.m.	n.m.	n.m.	95.5%

FIRST BERLIN RECOMMENDATION & PRICE TARGET HISTORY

Report No.:	Date of publication	Previous day closing price	Recommendation	Price target
Initial Report	10 November 2009	€0.52	Buy	€0.70
2...30	↓	↓	↓	↓
31	11 March 2016	€0.24	Buy	€1.20
32	20 May 2016	€0.24	Buy	€1.00
33	29 July 2016	€0.22	Buy	€1.00
34	Today	€0.22	Buy	€1.40

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BUY: An expected favourable price trend of more than 25% percent.

ADD: An expected favourable price trend of between 0% and 25%.

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- key sources of information in the preparation of this research report
- valuation methods and principles
- sensitivity of valuation parameters

can be accessed through the following internet link: <http://firstberlin.com/disclaimer-english-link/>

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