Pharming Group NV

Netherlands / Biotechnology
Primary exchange: Euronext Amsterdam /
Secondary exchange: Frankfurt
Bloomberg: PHARM NA
ISIN: NL0010391025

Q3 results

RATING	**BUY**
PRICE TARGET	**€1.40**
Return Potential	516.7%
Risk Rating	High

HEADING FOR PROFITABILITY IN 2017

Q3/16 results were close to our expectations and showed Pharming at breakeven at the operating level on a proforma basis (assuming ownership of US marketing rights to lead product Ruconest). We expect Pharming to close the acquisition of the US marketing rights to Ruconest from Valeant before the end of November. Completing this transaction will give the company full access to the market for treatment of acute hereditary angioedema attacks, which is currently worth over USD750m worldwide. Meanwhile, excellent preliminary results of a phase II study with Ruconest in the prophylaxis of hereditary angioedema suggest that Pharming will be able to tap a market worth an additional USD800m before the end of this decade. We expect the sharper focus entailed by Pharming's marketing of its own lead drug as well as increased resources to enable the company to make the case for the advantages of the 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. We continue to see fair value for the Pharming share at €1.40.

Valeant transaction expected to close in November Pharming has published Q3 results as shown in figure 1 overleaf. The numbers were close to our expectations – in part because the company had already released results for the first two months of the quarter on 3 October. Q3 sales came in at €3.4m (Q3/15: €3.2m; FBe: €3.5m) while EBIT was €-3.2m (Q3/15: €-3.0m; FBe: €-3.1m) These numbers were released two days ahead of the AGM on 5 October at which shareholders voted in favour of the capital raise necessary to implement the acquisition of the north American marketing rights to Ruconest. Management expects this transaction to close in November.

Annualised Ruconest sales run rate up 29% since June US Ruconest sales increased 10% y-o-y to €2.3m in Q3/16 (Q3/15: €2.1m). (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

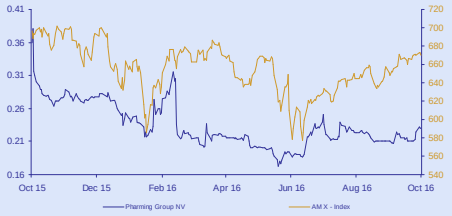
Pharming develops and produces therapeutic proteins from the milk of genetically modified rabbits. Pharming and Chinese SIPI signed a collaboration agreement in 2013, which will accelerate the addition of new projects to the firm's R&D pipeline. Lead drug Ruconest received EMA approval in 2010 and FDA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

MARKET DATA

As of 27 Oct 2016	
Closing Price	€ 0.23
Shares outstanding	412.61m
Market Capitalisation	€ 93.66m
52-week Range	€ 0.17 / 0.38
Avg. Volume (12 Months)	2,614,236

Multiples	2015	2016E	2017E
P/E	n.a.	n.a.	44.2
EV/Sales	8.5	7.1	2.0
EV/EBIT	n.a.	n.a.	16.0
Div. Yield	0.0%	0.0%	0.0%

STOCK OVERVIEW



COMPANY DATA

As of 30 Sep 2016	
Liquid Assets	€ 16.76m
Current Assets	€ 41.02m
Intangible Assets	€ 0.69m
Total Assets	€ 48.86m
Current Liabilities	€ 18.29m
Shareholders' Equity	€ 14.98m

SHAREHOLDERS

Kingdon Capital Management LLC	3.1%
Free Float	96.9%

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US Ruconest sales continue to be affected by turmoil at marketing partner Valeant. In the course of a refocusing of its business, Valeant halved the sales force dedicated to Ruconest. Pharming has undertaken to restore the US sales team to its former size in a stepwise fashion and also to hire several medical liaison personnel if it succeeds in acquiring the Ruconest marketing rights. Looking at the development of Ruconest in the US over recent quarters, sales have continued to recover from the low point of €1.2m reached in Q4/15. Q1/16 sales were €1.5m, Q2 sales were €2.0m and Q3 sales came in at €2.3m as stated above. Proforma figures (assuming ownership of the US marketing rights to Ruconest and that Pharming therefore receives 100% of the product's US revenues compared with the 30% it receives currently) showed worldwide Ruconest revenues of €20.5m at the nine months stage compared with €12.4m for H1/16. We estimate that US revenues accounted for ca. 95% of both these figures. Annualised worldwide Ruconest sales were €32m based on September numbers compared with €24.8m based on the H1/16 numbers.

Figure 1: First nine months results (€000's)

	A Proforma 9M 2016	B Actual 9M 2016	Δ A vs. B	C Actual Q3/2016	D Actual Q3/2015	Δ C vs. D	Proforma Q3/2016	Proforma H1 2016	E Actual 9M 2015	Δ B vs. E
Revenue	21,200	8,690	139%	3,416	3,249	5%	7,700	13,500	8,484	2%
License fees	700	1,656	-53%	552	541	2%	-400	1,100	1,655	0%
Product sales	20,500	7,034	186%	2,864	2,698	6%	8,100	12,400	6,829	3%
of which:										
Ruconest N. America (€m)	19.3	5.8	233%	2.3	2.1	10%	7.6	11.7	5.0	16%
Ruconest ex-N. America (€m)	1.2	1.2	0%	0.6	0.6	0%	0.5	0.7	1.8	-33%
Gross profit	18,000	5,459	228%	2,189	1,868	228%	6,500	11,500	4,752	15%
margin (%)	84.9%	62.8%		64.1%	57.5%		84.4%	85.2%	56.0%	
Costs	-21,400	-15,111	n.m.	-5,435	-4,949	n.m.	-6,700	-14,700	-13,929	n.m.
EBIT	-3,100	-9,387	n.m.	-3,176	-3,008	n.m.	0	-3,100	-9,070	n.m.
EPS (€)	-0.010	-0.025	n.m.	-0.009	-0.005	n.m.	0.003	-0.013	-0.014	n.m.

Source: Pharming, First Berlin Equity Research

Q3/16 operating result at breakeven The reported gross profit climbed to €2.2m (Q3/15: €1.9m) equivalent to a margin of 64.1% (Q3/15: 57.5%). The gross margin widened because of a shift in the product mix towards higher margin US revenues. However, the reported operating loss widened to €3.2m (Q3/15: €3.0m) mainly due to a €300k increase in R&D expenditure. On a proforma basis, the operating result was a loss of €3.1m at both the H1/16 and 9M/16 stage. The proforma Q3/16 operating result was thus breakeven.

Excellent preliminary results from phase II prophylaxis trial Preliminary results of the phase II clinical trial of Ruconest for prophylaxis of HAE published in July were excellent. The primary efficacy endpoint was the number of HAE attacks per 28 day treatment period and the secondary endpoint was clinical response, defined as a ≥ 50% reduction in the number of attacks from treatment with placebo to treatment with Ruconest. Patients who received Ruconest twice weekly had a mean of 2.7 attacks per four week treatment period, compared with a mean of 7.2 attacks for the placebo group. Meanwhile, among the per-protocol population of patients who completed the study without any major deviations (n=23), 96% of patients who received Ruconest twice weekly had at least a 50% reduction in their attack frequency. The study also confirmed a high level of tolerability for Ruconest. No patients withdrew from the study due to adverse events and no thrombotic or thromboembolic events were observed. In addition, there were no hypersensitivity or anaphylactic reactions and no neutralizing antibodies were detected.

Value of US HAE prophylaxis market projected to reach USD800m in 2017 Management tell us that comprehensive peer-reviewed results of the phase II prophylaxis trial will be presented at the Annual Scientific Meeting of the American College of Allergy, Asthma and Immunology from 10-14 November in San Francisco.

Pharming will then begin discussions with the FDA on further steps towards approval of Ruconest for prophylaxis of HAE. We expect a phase III study to begin before the end of this year. Results are likely to be available in 2017 and first revenues before the end of this decade are realistic. The US market for prophylaxis of HAE is expected to be worth USD800m in 2017 (up from USD500m in 2014). The only product currently approved for HAE prophylaxis in the US is Shire's Cinryze. If Ruconest is approved for HAE prophylaxis in the US, it will be the only product approved for both acute attacks and prophylaxis. The availability of one product for both indications has the potential to simplify management of the disease.

We maintain our Buy recommendation and price target of €1.40 Our 2016 numbers are based on the assumption that the Valeant transaction will not close until the end of the year. However, management now expects closing during November. If the December P&L includes 100% of North American Ruconest revenues rather than just the 30% which Pharming is currently booking, our numbers are likely to be exceeded. The structure of the transaction (the split between straight debt, convertibles and straight equity) has still to be finalised, but management has indicated that minimisation of shareholder dilution is a priority. Pending publication of this information, we are leaving our forecasts and valuation unchanged. We maintain our Buy recommendation and price target of €1.40.

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%	10%	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%	15%	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 PV[4)]		€994.5M									
NPV		€864.3M									
Milestones PV		-€26.9M									
Net Cash (pro-forma)		€59.8M									
Fair Value		€897.2M									
Share Count (fully diluted)		647,246K									
Fair value per share		€1.39									

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

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**	**-11,871**	**-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	n.m.	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	963	568	1,102	1,163
EBITDA	**-5,992**	**3,915**	**-11,871**	**-11,663**	**6,862**	**13,418**
Other adjustments	-2,301	-6,488	-4,551	-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	29 July 2016	€0.22	Buy	€1.00
32	30 August 2016	€0.22	Buy	€1.40
33	7 October 2016	€0.22	Buy	€1.40
34	Today	€0.23	Buy	€1.40

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INFORMATION PURSUANT TO SECTION 34B OF THE GERMAN SECURITIES TRADING ACT [WPHG], TO REGULATION (EU) NO 596/2014 OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL OF APRIL 16, 2014, ON MARKET ABUSE (MARKET ABUSE REGULATION) AND TO THE GERMAN ORDINANCE ON THE ANALYSIS OF FINANCIAL INSTRUMENTS [FINANV]

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First Berlin's system for asset valuation is divided into an asset recommendation and a risk assessment.

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The recommendations determined in accordance with the share price trend anticipated by First Berlin in the respectively indicated investment period are as follows:

STRONG BUY: An expected favourable price trend of more than 50% combined with sizeable confidence in the quality and forecast security of management.

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

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

REDUCE: An expected negative price trend of between 0% and -15%.

SELL: An expected negative price trend of more than -15%.

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The First Berlin categories for risk assessment are low, average, high and speculative. They are determined by ten factors: Corporate governance, quality of earnings, management strength, balance sheet and financial risk, competitive position, standard of financial disclosure, regulatory and political uncertainty, strength of brandname, market capitalisation and free float. These risk factors are incorporated into the First Berlin valuation models and are thus included in the target prices. First Berlin customers may request the models.

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Legally required information regarding

- **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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