

# HBM Healthcare

Switzerland | Pharma & biotech | MCAP CHF 1.3bn

22 July 2019

## Buy

<b>Target Price</b>	<b>CHF 220.00</b> (151.00)
Current Price	CHF 184.80
Up/downside	19.0%
Change in TP	45.7%
Change in EPS	up nm 19E / up nm 20E

Q.

## Does the current discount to NAV hamper the potential of HBM's shares?

HBM's shares are up 20% since the beginning of the year, beating the performance of the US biotech market over the same period (+12%). This great performance relies on an improvement of the NAV, but most importantly on the gradual decline in HBM's share price discount to NAV. The current discount is therefore limited to 8%, well below its three-year average (16%). One might wonder whether this trend is sustainable.

A.

## No, there is enough room for further appreciation

Pharma trends and dynamics remain solid, and HBM has demonstrated its ability to identify the value of promising biotechs early on. HBM has a well-balanced portfolio of public and private companies, and a successful long-term exit strategy (IPO or trade sale). Furthermore, shareholders benefit from an attractive return (a dividend in the range of 5% per year and share buyback), leading to sustainable performance. As a result, HBM's shares posted one of the best five-year performances among its peers. Despite this, the current share price discount to NAV is still 8%, while some laggards trade at a premium. Lastly, the non-listed investments could hide interesting value, as they are valued at their acquisition cost in our model. We update our model and henceforth apply a conservative 10% discount to NAV (vs. 20% previously) to take into account the portfolio's positive advancement. Accordingly, we lift our TP to CHF220, implying 19% upside, and maintain a Buy rating.

Kepler Cheuvreux and the issuer have agreed that **Kepler Cheuvreux** will produce and disseminate investment research on the said issuer as a service to the issuer.

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### Pharma & biotech research team

Biographies at the end of the report

# Beyond the Q.

## Investment Case

### Pharma trends still set the pace

HBM Healthcare is a Swiss investment company managed by HBM Partners. Its investment focus is private and public healthcare companies, mainly in Europe and North America. Among the various segments of the healthcare industry, the biotech sector is well positioned to sustain its dynamic growth in the years ahead, thanks to its track record of innovation. Despite increasing pressure on healthcare, the sector offers solid fundamentals, supported by an ageing population, innovation, and emerging economies.

No other sub-sector in healthcare generates as high a return as the biotech sector. HBM has gradually built a strong track record of investment, targeting and delivering an annual return of at least 5% of net assets (+129% on the last five years). This regular outperformance gives the company an edge over peers.

### Enough room for further appreciation

Thanks to wise choices and relevant stock-picking, HBM's long-term performance (three to five years) is among the best of its peers. Hence, over the last year, due to an increase in investors' confidence in HBM's investment strategy, the fund's discount to NAV has decreased to 8%, well below the three-year average discount (16%). However, some of its peers with worse performances are currently trading at a premium to their NAV. Hence, we think that HBM's discount to NAV is likely to shrink again. Moreover, HBM Healthcare's portfolio of private companies that are still at a relatively early stage of development could hide promising value, as HBM has already demonstrated its ability to elicit the value from these investments (through an IPO or trade sale).

### Valuation model

Our valuation of HBM Healthcare is based on the NAV of all investments, minus a discount. Henceforth, we use a conservative 10% discount to NAV (vs. 20% previously) to take into account the positive advancement of the portfolio and higher confidence from investors. We expect the NAV of HBM's public company portfolio to reach the value implied by analysts' and consensus' target prices. The valuation of investments in private companies and funds are included in our valuation, at their acquisition costs or the price of the last round of financing. Our valuation points to a NAV per share of CHF247, implying a target price of CHF220. Any IPO or trade sale of companies in the private equity portfolio offer upside to our scenario.

**Company summary**

HBM Healthcare is a Swiss investment company managed by HBM Partners. It was founded in 2001 and listed on the Swiss Stock Exchange in February 2008. Its investment focus is private and public healthcare companies, mainly in Europe and North America. The investment portfolio is made up of stakes in about 50 companies (its largest investment is less than 10% of the portfolio). It also has investments in healthcare-dedicated funds to diversify outside of its core expertise.

**Management**

Andreas Wicki, CEO  
Erwin Troxler, CFO  
Hans Peter Hasler, Chairman of the Board

**Key shareholders**

Nogra Pharma Invest 15.0%

**Market data**

Bloomberg	HBMN SW
Reuters	HBMN.S
Market cap (CHF)	1.3bn
Free float (%)	100.0
No. of shares outstanding (m)	7
3m avg. daily vol (CHFm)	1.2
YTD abs. performance	18.9%
52-week high (CHF)	186.40
52-week low (CHF)	147.60

**Strengths**

- Highly skilled investment team with long-standing expertise
- Diversified portfolio of late-stage assets, both private and public
- Active role in value creation within portfolio companies
- Listed private healthcare equity fund

**Opportunities**

- Invested in emerging and innovative therapies
- Substantial clinical newsflow from holding companies
- Intense M&A activity in the global healthcare sector
- Favourable environment for healthcare IPOs

**Weaknesses**

- Persistent wide discount to NAV
- Mature portfolio, which needs to be rebalanced
- Mixed performance over the years
- Size could be an obstacle to investing in small- and mid-caps

**Threats**

- Competition from listed healthcare equity funds or ETFs
- Venture is an industry that does not scale well
- The biotech boom coming to an end
- Sector rotation with healthcare outflows

**Key financials** (please see the end of this report for full financials)

Income Statement (CHFm)	2015	2016	2017	2018	2019E	2020E	1 year performance
Sales	0.0	0.0	0.0	0.0	0.0	0.0	
% Change	na	na	na	na	na	na	
EBITDA adjusted	0.0	0.0	0.0	0.0	0.0	0.0	
EBIT adjusted	0.0	0.0	0.0	0.0	0.0	0.0	
Adjusted EBIT margin (%)	na	na	na	na	na	na	
Net profit reported	23.1	134.6	113.8	209.1	194.7	208.8	
Net profit adjusted	23.1	134.6	113.8	209.1	194.7	208.8	

**Cash flow statement (CHFm)**

Levered post tax CF before capex	-44.0	119.3	72.5	171.9	141.8	163.0
Capex	0.0	0.0	0.0	0.0	0.0	0.0
Free cash flow	-44.0	119.3	72.5	171.9	141.8	163.0

**Balance sheet (CHFm)**

Intangible assets	0.0	0.0	0.0	0.0	0.0	0.0
Tangible assets	0.0	0.0	0.0	0.0	0.0	0.0
Fin. & other non-current assets	1,007.6	1,126.8	1,193.6	1,262.4	1,507.0	1,766.8
Total shareholders' equity	1,019.9	1,086.9	1,150.5	1,302.6	1,596.5	1,919.1
Pension provisions	0.0	0.0	0.0	0.0	0.0	0.0
Liabilities and provisions	102.7	259.4	266.8	229.0	229.0	229.0
Net financial debt	-15.9	36.6	40.6	-43.1	-92.4	-155.2
IFRS16 debt	0.0	0.0	0.0	0.0	0.0	0.0
Invested capital	-3.6	-3.3	-2.5	-2.9	-2.9	-2.9

**Per share data (CHF)**

EPS adj and fully diluted	3.06	19.01	16.40	30.05	27.99	30.02
Cash flow per share	-5.82	16.86	10.45	24.71	20.39	23.43
Book value per share	135.09	153.51	165.71	187.23	229.48	275.85
DPS	5.50	5.80	7.00	7.50	7.66	8.04

**Ratios**

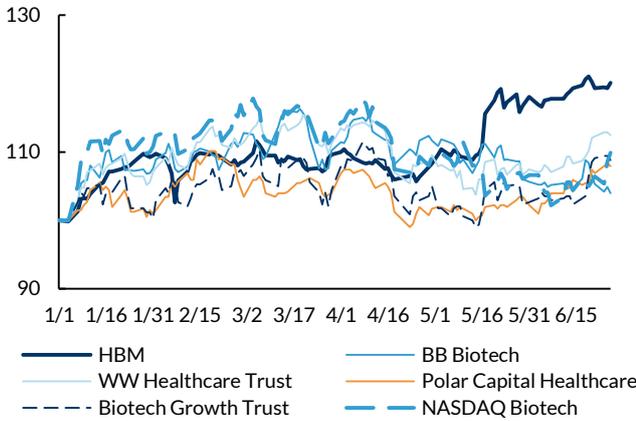
ROE	2.2%	12.8%	10.2%	17.0%	13.4%	11.9%
ROIC	na	na	na	na	na	na
Gearing	-1.6%	3.4%	3.5%	-3.3%	-5.8%	-8.1%

**Valuation**

P/E adjusted and fully diluted	32.6	5.3	7.5	5.5	6.6	6.2
P/CF	na	5.9	11.8	6.6	9.1	7.9
P/BV	0.7	0.7	0.7	0.9	0.8	0.7
Dividend yield (%)	5.5%	5.8%	5.7%	4.6%	4.1%	4.4%
FCF yield (%)	-5.8%	16.8%	8.5%	15.1%	11.0%	12.7%
EV/Sales	na	na	na	na	na	na
EV/EBITDA	na	na	na	na	na	na
EV/EBIT	na	na	na	na	na	na
EV/IC	na	na	na	na	na	na

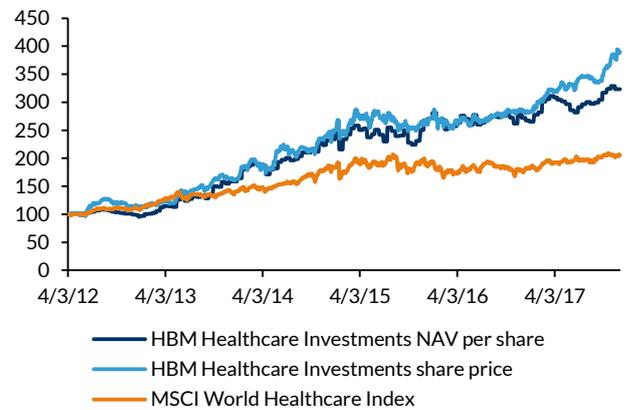
# Q&A in six charts

**Chart 1: Share price performance since the beginning of 2019**



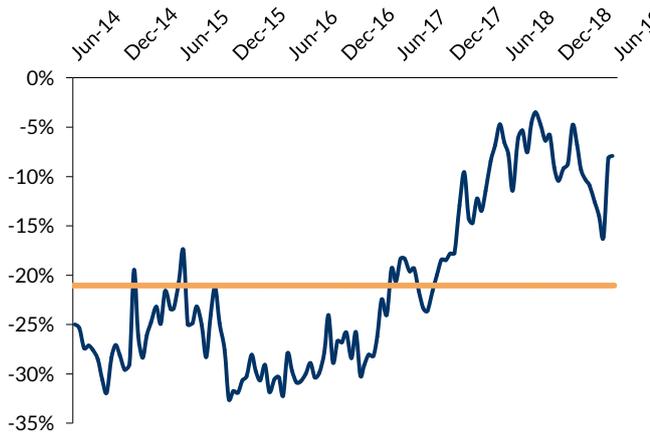
Source: Factset Partners

**Chart 2: Share price and NAV performance versus index**



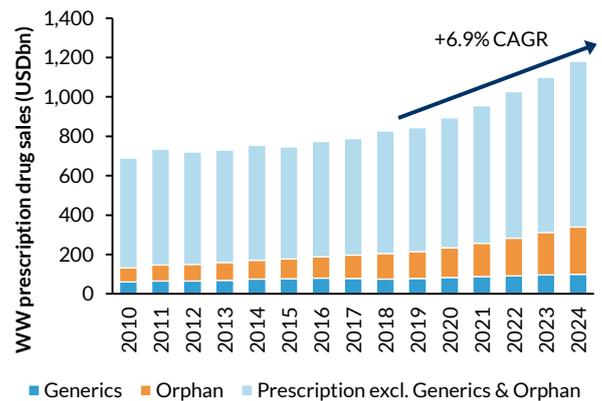
Source: Factset Partners, Kepler Cheuvreux

**Chart 3: HBM's share discount to NAV (average level: -21%)**



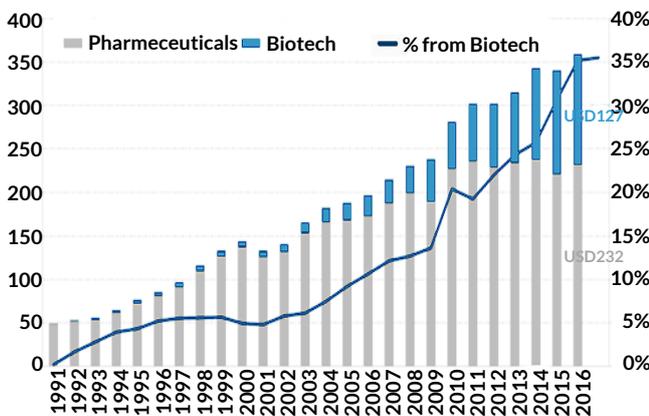
Source: HBM, Kepler Cheuvreux

**Chart 4: Worldwide total prescription drug sales (2010-24)**



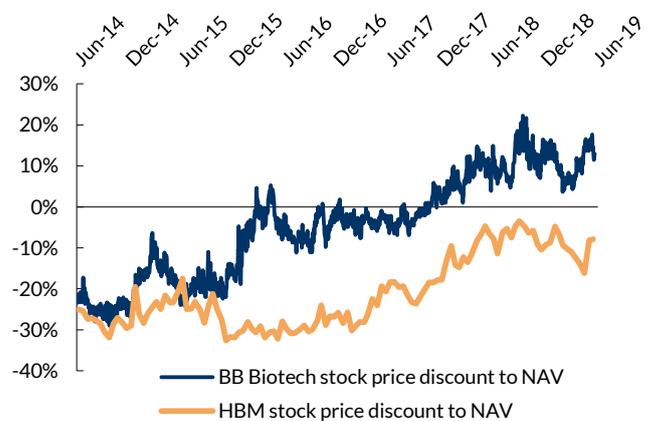
Source: Evaluate Pharma,

**Chart 5: Revenue contribution from biotech (USDbn)**



Source: S&P Capital IQ, HBM Research, 2017

**Chart 6: HBM and BB Biotech stock price discount to NAV**



Source: Factset Partners, Kepler Cheuvreux

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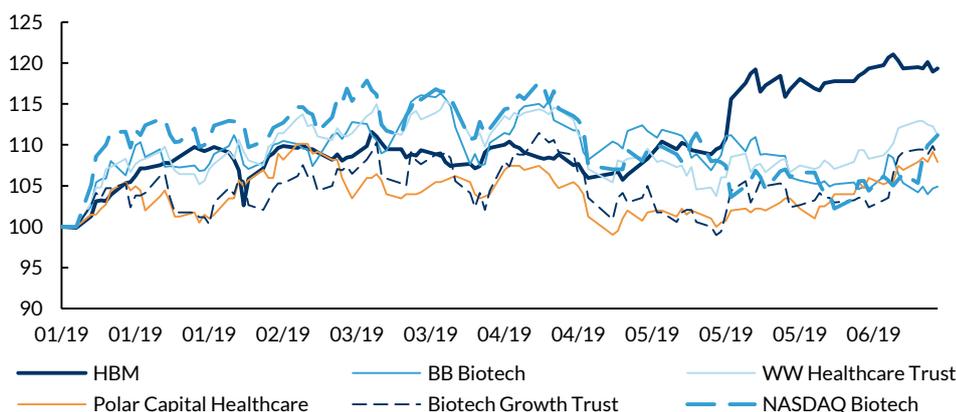
## Does the current discount to NAV hamper the potential of HBM's shares?

Since the beginning of the year, the stock has grown by more than 20%. This is well above the performance of the US biotech market. HBM's share price discount to NAV has shrunk and is currently well below its historical level (-21% on a long-term basis and -16% on a three-year basis). Regarding the current valuation, one might wonder if this trend can continue.

### A strong performance since the beginning of the year

HBM Healthcare Ltd was founded in 2001 and has been listed on the Swiss Exchange since 2008. The company has gradually developed expertise in investing in private and public companies with an exit-driven strategy, leading to an impressive performance over time. Since its inception, HBM's stock performance has regularly outpaced the market.

Chart 7: Share price performance of healthcare/biotech funds since the beginning of 2019



Source: Factset Partners

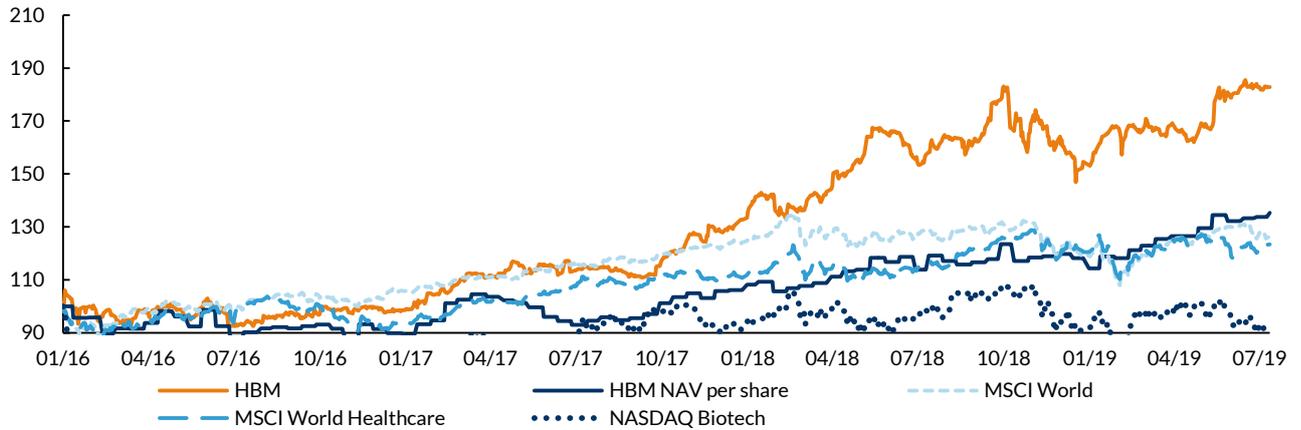
Since the beginning of the year, HBM's share price has increased by +20%, significantly more than the NASDAQ Biotech index (+10%) or its European peers such as BB Biotech (+8%) or American (+10% on average).

### Discount to NAV has melted

Despite its lower exposure to the US market compared to its peers, thanks to wise choices, HBM Healthcare's long-term performance (three to five years) is among the best of its peer group.

Accordingly (and thanks to an increase of investors' confidence in HBM's investment strategy since the beginning of the year), the fund's NAV increased by +14%, while HBM's share price increased by +19%, significantly more than the MSCI World (+16%) or the MSCI World Healthcare Index (+14%).

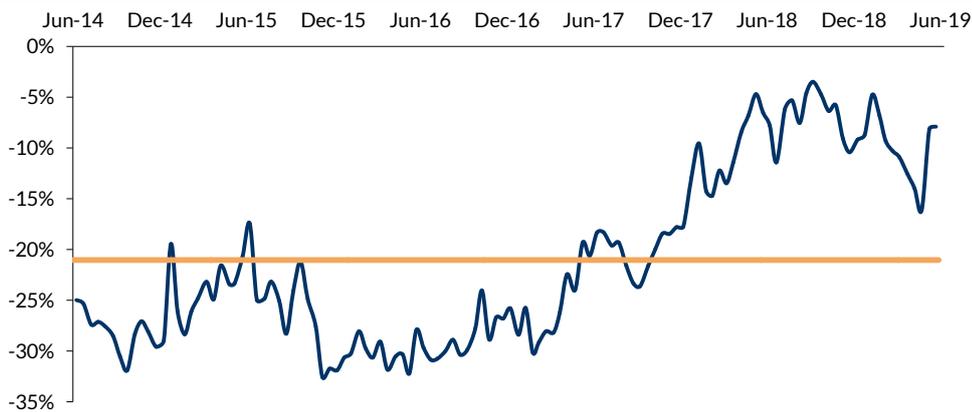
**Chart 8: Share price and NAV performance versus indexes**



Source: Factset Partners, Kepler Cheuvreux

Moreover, nowadays HBM's stock price discount to NAV has reduced considerably to 8%, far below its average historical level (-21%).

**Chart 9: HBM's stock price discount to NAV (average historical level: -21%)**



Source: HBM, Kepler Cheuvreux

# Pharma trends remain solid

The healthcare industry represents annual expenditures worth an average of 9% of GDP across OECD countries (with large discrepancies between countries). Global demand for healthcare products and services will sustain this strong trend in the coming years, thanks to robust fundamentals. These include ageing populations (and the related increase in drug consumption), changes in lifestyle (eating habits and low levels of physical activity), emerging-country expansion, and the innovation cycle within pharma/biotech companies in a more favourable regulatory climate. This positive trend is led by the dynamism of biotech companies.

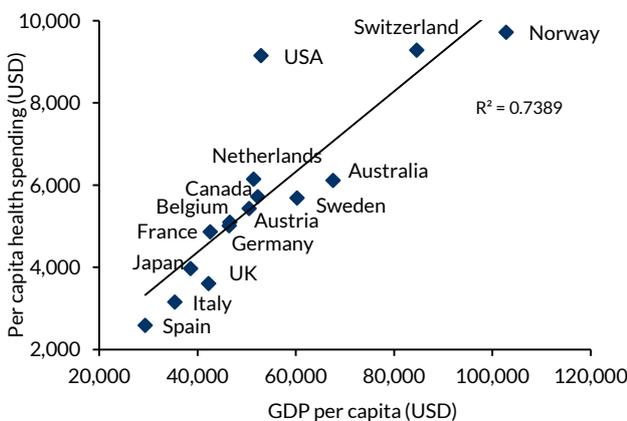
HBM has developed a strong expertise in investment along the healthcare value chain in private and public companies that are focused on biotech or medical devices.

## Increasing healthcare expenditures

The trend of the pharmaceutical industry's growth is astonishing. The OECD estimates that, in 2018, health spending accounted for 9% of GDP on average across OECD countries. Spending on inpatient and outpatient care combined represents the largest part of health spending. Medical goods (mainly pharmaceuticals) accounted for 19% of health spending, mostly driven by the US.

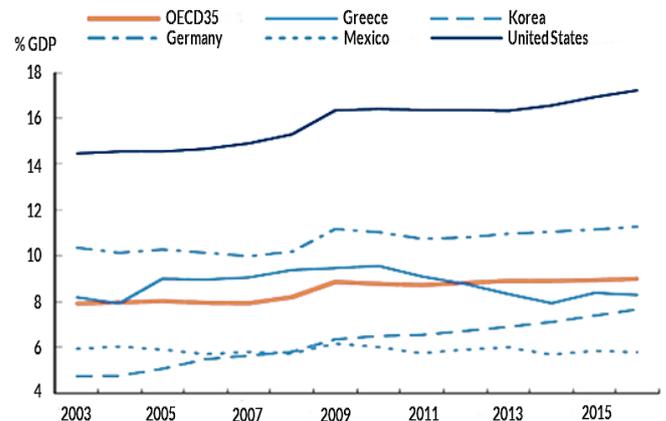
Looking at changes over time, average health spending grew at a faster rate than the overall economy in the 1990s and 2000s, with some discrepancies between countries. In the US, healthcare expenditures represented 16.9% of US GDP in 2018, but only 7.0% in Ireland.

**Chart 10: Total health expenditure per capita and GDP per capita (2013), selected countries**



Source: Kepler Cheuvreux

**Chart 11: Healthcare expenditure as a share of GDP, selected OECD countries, 2003-16**

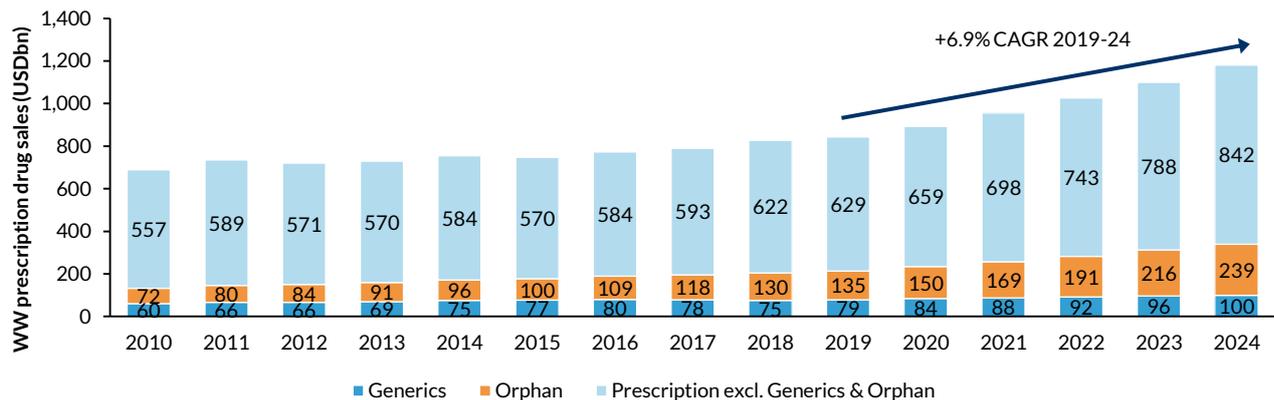


Source: OECD Health Statistics 2017

The Center for Medicare and Medicaid Services (CMS) expects healthcare spending in the US to represent c. 20% of GDP by 2022E. According to the World Bank, healthcare expenditure is growing in all countries regardless of income level.

Turning our attention to pharmaceutical spending, worldwide sales of prescription drugs are still growing faster than healthcare expenditures. This spending covers both prescription (Rx) and over-the-counter medication (OTC) corresponding to a USD827m market in 2018. According to EvaluatePharma, the pharmaceutical industry is set to post a 6.5% CAGR and is likely to reach USD1.2bn by 2024E.

**Chart 12: Worldwide total prescription drug sales (2010-24, USDm)**



Source: Evaluate Pharma, May 2019

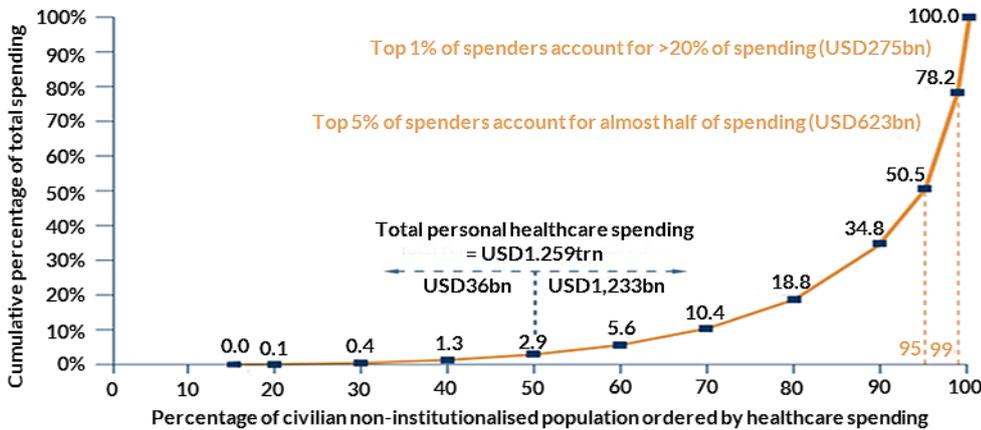
Underlying factors driving this growth include the ageing population, improvements in quality of life in emerging countries, a new cycle of innovation in pharma companies, and the new possibility of a shortened pathway to Food and Drug Administration (FDA) approval for treatments of specific diseases.

### Ageing demographics

Healthcare expenditure is concentrated on a relatively small number of people. According to data from the US Department of Health and Human Services, a small number of people account for a significant share of healthcare expenses. Conversely, a large portion of the population has very low levels of healthcare spending. Thus, almost half of healthcare spending was used to treat just 5% of the US population.

As the population ages, global healthcare consumption increases. Hence, high spending occurs near the end of many patients' lives. In the US, people over 64 years of age represent 13% of the population, but they account for 40% of the top 5% highest spenders on healthcare.

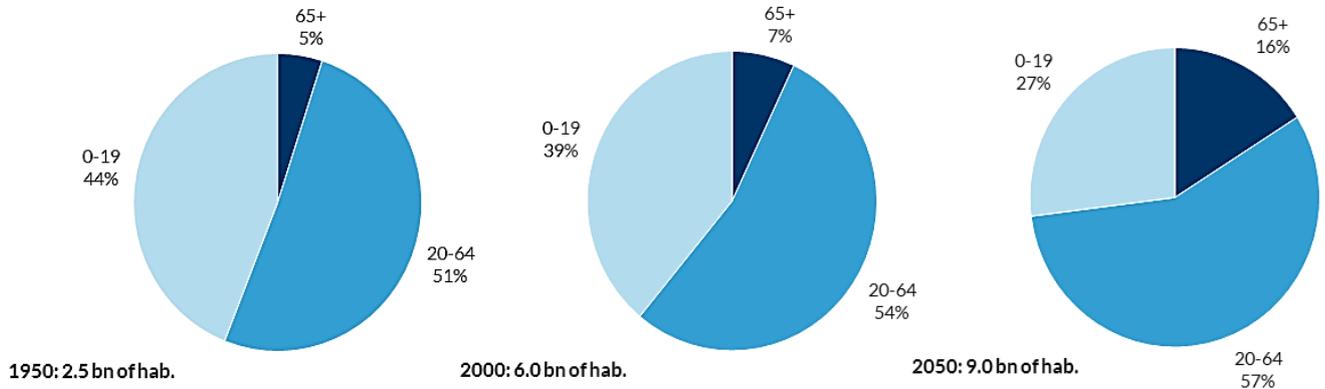
Chart 13: Distribution of personal healthcare spending, 2009



Source: NIHCM Foundation analysis of data from the 2009 Medical Expenditure Panel Survey

The population is ageing more than ever. According to the UN, the number of people aged 65 and over is set to double as a percentage of the global population, from 7% in 2000 to 16% in 2050. By then, the number of people over 85 years of age is set to have doubled from the current level of c. 2-4%.

Chart 14: The ageing of the world population 1950-2050



Source: OECD

Life expectancy across OECD countries increased by over five years between 1990 and 2012. According to OECD statistics, the share of the population aged over 65 is set to increase from 7% of the population to 16% in 2050. Hence, the growth in pharmaceutical spending is likely to continue in the coming years.

### Lifestyle and obesity

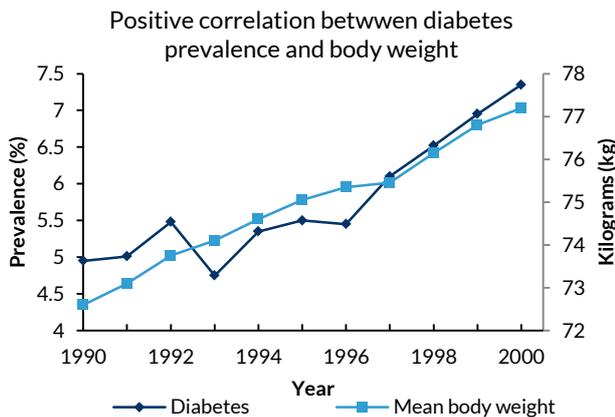
According to the World Health Organisation (WHO), low fruit and vegetable consumption and low levels of physical activity increase the risk factors in terms of years of healthy life lost.

The rise in sedentary lifestyles is raising obesity<sup>1</sup> rates, leading to increased risk of coronary heart disease, strokes, and certain types of cancer.

A study conducted by S. Sabharwal *et al.*<sup>2</sup> shows that obese patients have a 15% higher chance of musculoskeletal injury or fractured bones in their lifetime compared to people with healthy weights. According to the WHO, worldwide obesity rates almost doubled between 1980 and 2008. Moreover, a study from the Centers for Disease Control and Prevention (CDC) established that more than one-third of US adults (c. 36%) and c. 17% (12.5m) of children and adolescents aged 2-19 are obese. This global trend is set to continue, with significant shifts in eating habits and more sedentary lifestyles.

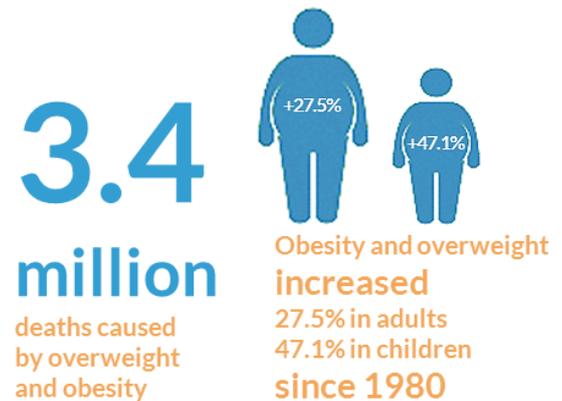
In 2014, more than 1.9bn adults over 18 years of age were overweight (39% of adults), and of these, over 600m were obese (13%).

Chart 15: Diabetes - the ongoing epidemic



Source: Kepler Cheuvreux, AH Mokdad *et al.*, JAMA 1999

Chart 16: Obesity increasing worldwide



Source: Kepler Cheuvreux

Healthcare expenditure is significantly correlated with the rise in risk factors such as obesity, and the increased prevalence of chronic diseases linked to these risk factors such as hypertension, diabetes, and hypercholesterolemia.

All regions are affected by this broad trend. Once considered a high-income-country issue, obesity today also affects lower- and middle-income countries. Due to the complications caused by obesity (diabetes, high cholesterol, high blood pressure, etc.), being obese kills more people than being simply overweight.

### Make innovation great again

Healthcare innovation can be evaluated by its impact on stakeholders as either non-disruptive or disruptive. While non-disruptive innovation refers to evolutionary or incremental improvements (improvements in something that already exists), disruptive innovations refer to innovations that fundamentally disrupt old systems or create new markets and deliver new value opportunities.

<sup>1</sup> Obesity is characterised by a body mass index of over 30 (body mass index, or BMI, is a ratio between height and weight. BMI = kg/m<sup>2</sup>)

<sup>2</sup> S. Sabharwal *et al.*, *Impact of obesity on orthopaedics* - Bone Joint, 2012

### Advanced medical device technology

Thanks to advanced technology, enormous progress has been made in the development of medical devices for different end-users. Some are used by healthcare professionals to treat patients (such as devices that emit low-level electrical pulses to treat ADHD or robotic surgical systems), while others are worn by patients (like insulin pumps) or operate inside their bodies (like artificial heart pumps and hip implants).

### Immuno-oncology

Immuno-oncology (IO) refers to therapies that boost or restore the ability of the immune system to fight cancer. The four main active IO categories are immune checkpoint inhibitors (ICIs), therapeutic cancer vaccines, oncolytic viruses, and adoptive cell therapies (CAR T cell therapies). ICIs, which are by far the largest category of IO by value, aim to re-establish the anti-tumour activities of immune cells. ICIs do not work for all tumour types on their own, but combining them with other treatments to “turn cold tumours hot” (i.e. make tumours responsive to ICIs) looks promising and is leading to numerous developments.

IO’s commercial history began in the early 2010s, but it really took off in 2014 with the launch of the ICIs Keytruda and Opdivo. Each recorded sales of more than USD7bn in 2018, leading to an IO market of over USD18bn. The number of developments in this field has been impressive, with more than 1,000 ongoing trials. Deal activity is twice that of any other class of cancer drugs.

### Gene editing and gene therapies

Thanks to the rapid development of DNA sequencing, this field is likely to have the biggest impact in the coming years on the way physicians treat and categorise patients depending on their disease.

According to the WHO, more than 10,000 diseases are caused by a mutation in a single gene. Two approaches to treat such diseases show a lot of promise: gene editing and gene therapy.

- **Gene editing** is the insertion, deletion, or replacement of DNA at a specific site in the genome of an organism or cell. It is usually achieved in the lab using engineered nucleases, also known as molecular scissors. Gene editing treatment is not yet available to patients, but several biotechnology companies are developing gene editing treatments for various genetic diseases such as haemophilia, myopathy, and sickle cell disease.
- **Gene therapy** involves the insertion of a healthy gene into cells. Several gene therapies have proven successful in late-stage trials, while a few have already been approved in the US. Gene therapy is currently in vogue, leading to intense M&A activity. In February 2019, Roche acquired Spark Therapeutics for USD4.8bn (haemophilia). In March 2019, Biogen bought Nightstar Therapeutics for USD800m (choroideremia, a rare genetic form of blindness).

### Other innovations

Autoimmune diseases and CNS drugs also represent a great investment opportunity, as the unmet medical needs for the related diseases are still important.

Autoimmune diseases encompass more than 80 chronic disabling conditions affecting between 7% and 9% of the global population, with a sharp increase over the last decades. They are caused by a dysfunction of the immune system, which produces an inappropriate response to its own cells, tissues, and/or organs, resulting in inflammation and damage.

### However, there are some headwinds

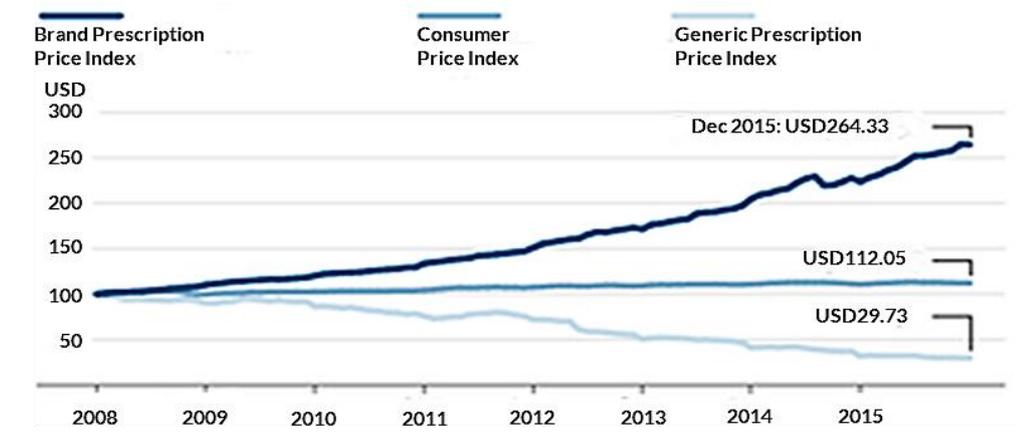
Beyond the outcomes of clinical trials and regulatory hurdles, a pharma/biotech company is sensitive to several themes, in particular the rise of healthcare costs, which has become a significant issue for both developed and developing countries. This situation leads to harsher price controls all over the world for every new drug, and fosters the promotion of generics/biosimilars. However, as pharma companies need to renew their pipeline, biotech companies represent key M&A targets.

#### Rise of healthcare costs...

The rapid growth of healthcare expenditure has become a great concern for both households and governments, leading to increased price pressure on pharmaceutical drugs.

According to Express Scripts, prescription costs have dramatically increased for US patients in recent years. The Affordable Care Act, which provides uninsured patients access to affordable drugs, is part of the reason for this rise.

Chart 17: Soaring drug prices



Source: Express Scripts

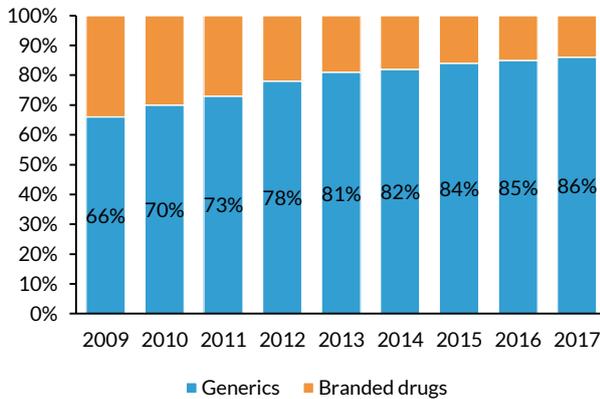
Other reasons include the introduction of new drugs into the market which are sold at a higher price in some therapies (cancers, rare or chronic diseases). For instance, in less than 15 years, the average monthly price of cancer drugs has almost tripled to USD13,000, while insulin prices have spiked by 8x in 20 years.

#### ...leads to increased use of generics...

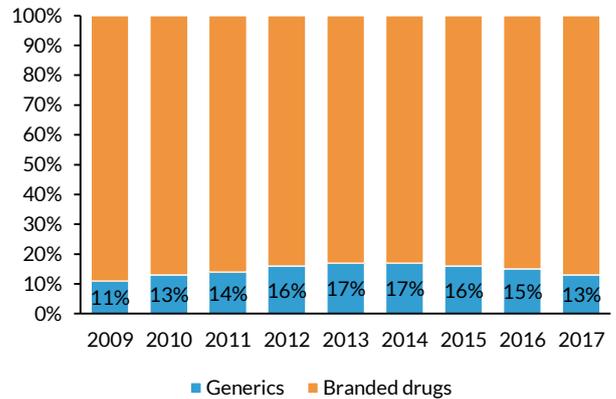
The introduction of generic medicines has helped sustain the US healthcare system by improving patient access and generating savings for taxpayers, employers, and insurance providers. Thus, the use of generics is growing when available. While their weight as a percentage of all prescription drugs is growing, they represent

only a small percentage of total drug expenditure. For instance, in 2017, US generics accounted for only 13% of overall drug spending, but 86% of prescriptions dispensed by volume.

**Chart 18: Volume share of generics (in %)**



**Chart 19: Value share of generics (in %)**

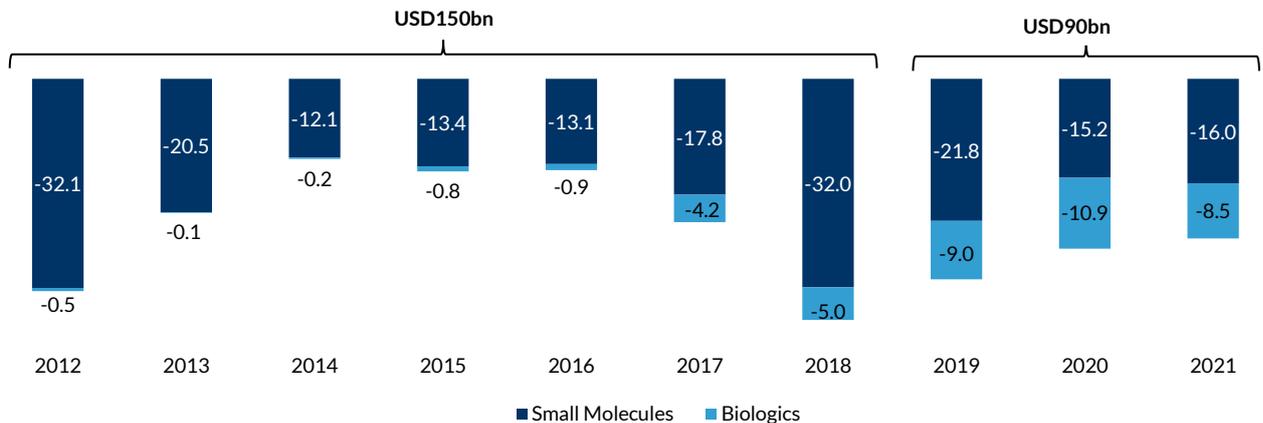


Source: IQVIA, National sales perspectives, National prescription Audit, 2018

Source: IQVIA, National sales perspectives, National prescription Audit, 2018

Patent cliffs and budgetary constraints are the main factors behind slower sales growth in the pharmaceutical sector. In ten years, the patent cliff is set to wipe c. USD240bn off pharma's revenues. The next wave will be the rise of biosimilars<sup>3</sup>.

**Chart 20: Revenue loss due to loss of exclusivity (USDbn)**



Source: Quintiles IMS Market Prognosis, National Sales Perspectives, March 2017, Kepler Cheuvreux

The expiration of the patents of various blockbuster biologics in the 2000s heralded the era of biosimilars, new drugs that mimic original biologic medicines. Because it is easier to copy than create, developing a biosimilar is cheaper, quicker, and less risky than developing a new biologic drug, although it is more complex than developing generics, due to their manufacturing process, which uses biological sources.

<sup>3</sup> Biosimilars are biologic medicines that are highly similar in terms of structure, efficacy, safety, and immunogenicity profile (i.e. their ability to cause an immune response) but not identical to already approved drugs called "reference medicines"

As biosimilars are marketed at between 65% and 70% of the cost of branded biologics, we believe that they will increasingly play a crucial role in delivering more affordable treatments to patients while simultaneously providing much-needed savings to healthcare systems worldwide.

The global biosimilars market, estimated to be worth USD6.0bn in 2017, is projected to post a CAGR of c. 45.0% over the next five years, reaching USD36.0bn in 2022E. This trend is supported by the increasing number of blockbuster biologics coming off patent. From 2017, around USD75bn worth of biologic sales will lose exclusivity, including USD52.0bn between 2019E and 2022E.

All these patent expirations leading to a growing market for generics and biosimilars will put mounting pressure on pharma/biotech companies to innovate as cheaper versions of already approved molecules are launched.

### **...and tight price controls**

The main consequence of these regular price increases is growing pressure on pharma/biotech companies to grant rebates to the Health Maintenance Organisation or Pharmacy Benefit Managers (PBM<sup>4</sup>).

The high price of drugs is one of the biggest hurdles to wide-ranging access to healthcare. This is as true in emerging countries as it is in developed ones, where payers consider high prices a real barrier to accessing new medicines, given budgetary constraints. Hence, many drugs are not available to all the patients who need them. In particular, the economic justification for orphan drug prices is difficult to validate (cost-effectiveness) unless we look at the small size of the population targeted.

However, governments and payers are still willing to pay for innovation. Hence, the latest prices for innovative treatments like Opdivo (nivolumab, BMS) or Keytruda (pembrolizumab, Merck), which can cure specific cancers, were up to USD150,000 for a course of therapy.

### **Biotechs are at the forefront**

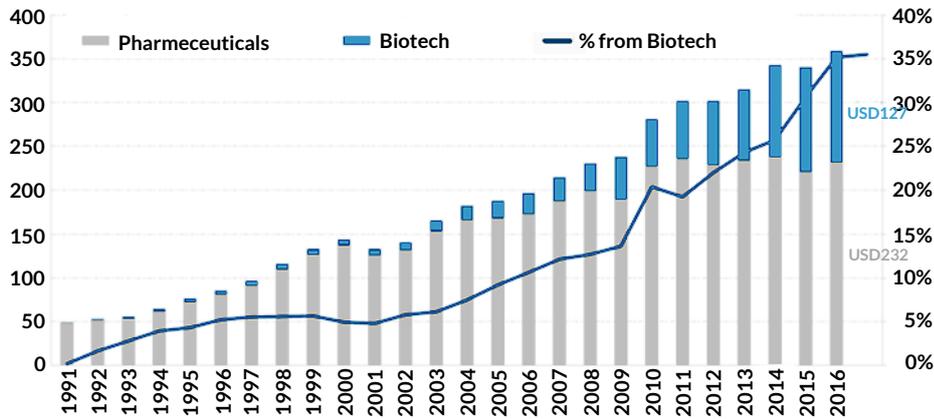
While HBM Healthcare is a leading investment company in healthcare, the company invests mainly in biotechs with high visibility.

US revenues from publicly traded drug companies have been growing year after year. They now represent more than 35% of the healthcare industry's revenues.

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<sup>4</sup> PBM negotiates prices on behalf of private corporations (health insurers, Medicare, private unions) and ask for rebates and discounts which vary depending on the added value of a drug

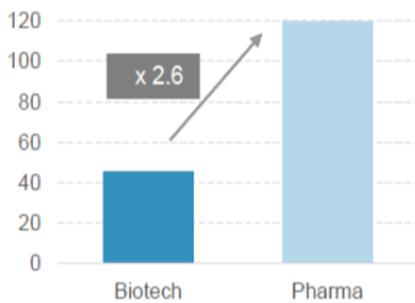
Chart 21: Revenue contribution from biotech (USDbn)



Source: S&P Capital IQ, HBM Research, 2017

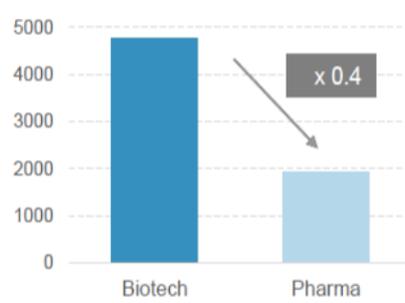
Innovation is crucial to pharma companies (particularly for biotechs) and will almost certainly continue to drive the sector. Despite constraints, there has been a clear acceleration in the number of drugs in development in recent years. However, biotech companies seem more agile than big players. Indeed, while they spend 2.6 times less money on average in R&D, they carry out most clinical trials, and they manage to get twice as many approvals as large pharma players.

Chart 22: R&D spending (USDbn, 2017)



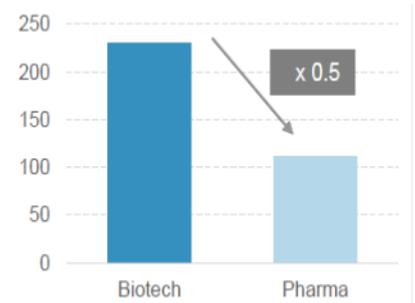
Source: Evaluate Pharma World Preview, 2018

Chart 23: Pipeline (clinical trials)



Source: Biotechnology Innovation Organisation Report, 2018

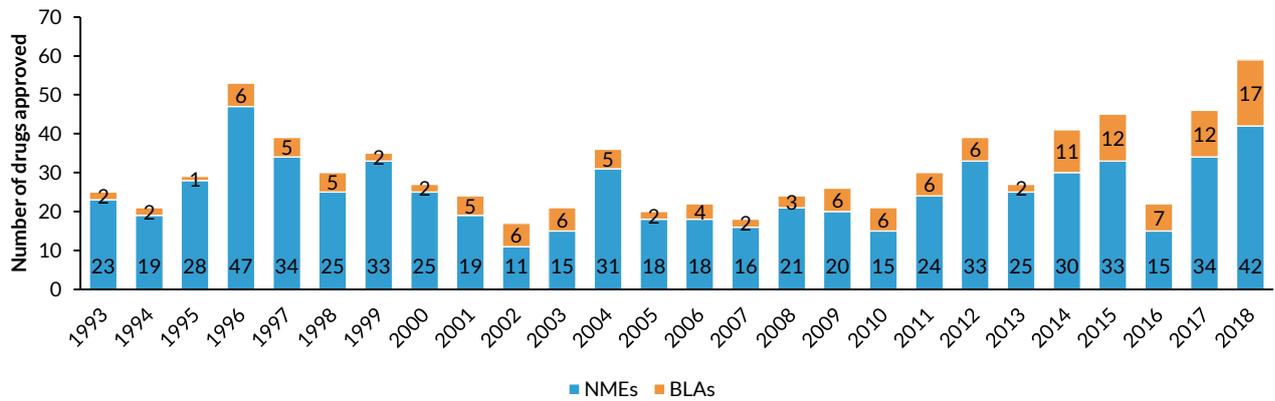
Chart 24: Approvals by origin (count)



Source: HBM Biopharma Drug Approval Report, 2018

Recent years have seen the emergence of new tools that will facilitate the approval of upcoming innovative treatments (development incentives like breakthrough therapy designation, priority review vouchers, or the 21<sup>st</sup> Century Cures Act).

Chart 25: Novel FDA approvals since 1993



Source: FDA, CDER

One of the missions of the head of the FDA is to slash regulations and speed up drug approval at the agency. The Trump administration is set to increase the competitive environment for generic drugs while facilitating the approval of innovative drugs.

## Enough room for further appreciation

HBM actively invests in private and listed biotech and pharmaceutical companies. HBM prioritises revenue-generating companies, companies with products at an advanced stage of development (phase II or phase III), and cash flow-neutral companies that require funding to expand leading to lower clinical risk. Moreover, HBM focuses on promising therapeutic areas where medical needs are unmet or unsatisfied (oncology, CNS, or autoimmune diseases). Thanks to its significant expertise and intelligent stock-picking, HBM has had a successful investment strategy with a regular return over 10% per year. Moreover, its well-balanced portfolio allows the fund to be less sensitive to single-company issues in its portfolio.

Moreover, HBM set up an attractive policy of returning cash to its shareholders through dividends (in the range of 5% per year) and share buybacks. Thus, in a five-year period HBM posted the best performance compared to its peers. Despite these outcomes, HBM's share discount to NAV is higher than some peers who performed worse over the same period. However, things appear to be changing, as investors seem to have more confidence in HBM's successful stock-picking strategy.

Lastly, part of the future performance will come from investments in private companies for which the value recorded in the fund (NAV) is the acquisition price. Hence, the exit-driven strategy (trade sales and IPOs) should help to materialise the hidden value of these investments.

### A successful investment strategy backed by expertise

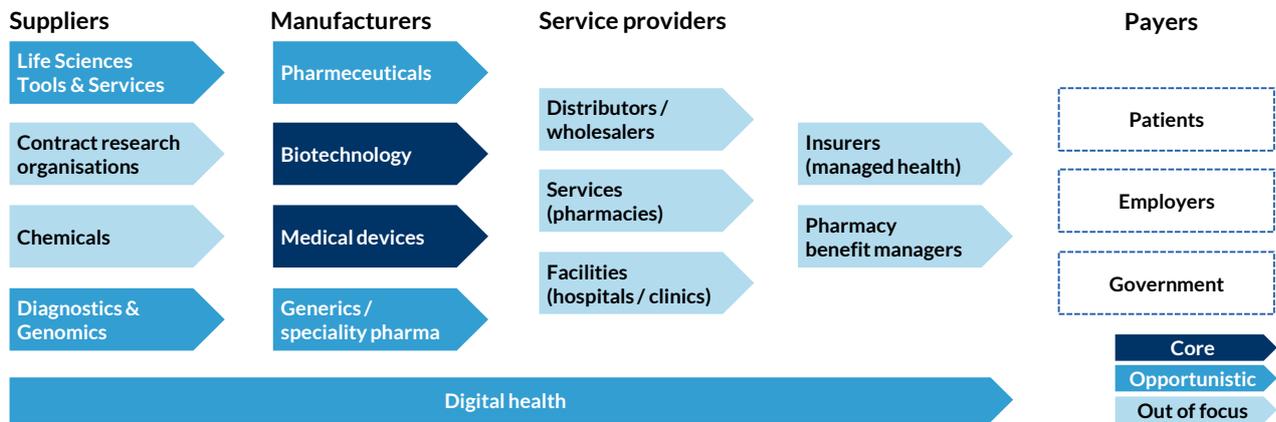
HBM Healthcare is a long-term shareholder in emerging healthcare companies and actively contributes to performance. Healthcare investing requires a multifaceted approach to understand the underlying drivers. HBM Healthcare Investments has many years of investment expertise with private and public companies. Its portfolio focus on biotechs and medical devices is diversified and well balanced (drug candidates at different stages of development).

#### Focus on healthcare

HBM Healthcare Investments invests primarily in more mature private companies with an attractive valuation and a convincing business model including its product pipeline, technology, and management.

The primary focus is on biotechs and medical devices, while the company can invest opportunistically in pharmaceuticals, speciality pharma, and diagnostic companies.

Chart 26: HBM's investment focus



Source: HBM Healthcare

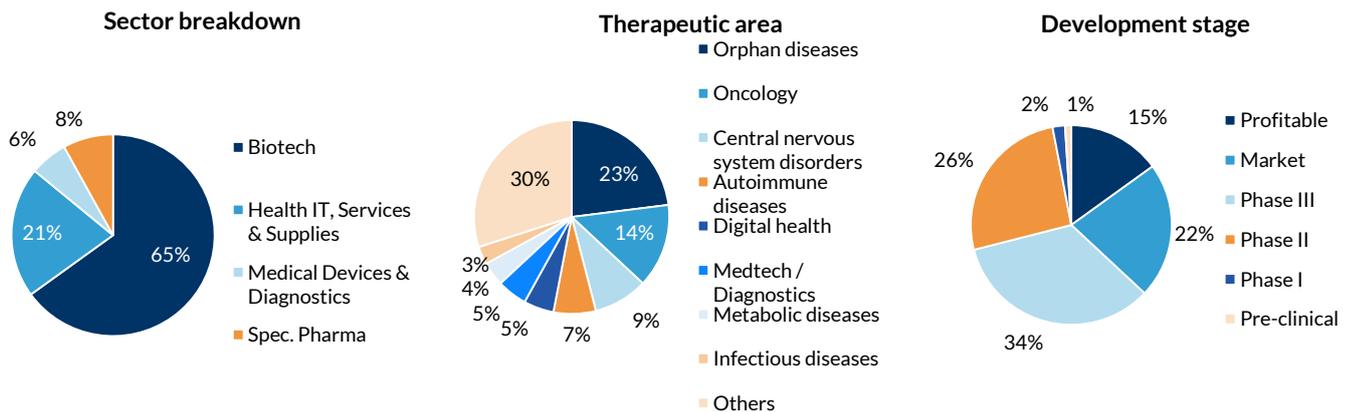
Once an investment opportunity is identified, the company conducts its due diligence and makes an evaluation of the investment potential.

**A well-balanced and diversified portfolio...**

HBM Healthcare has a well-balanced and diversified portfolio of private and public companies. The US represents the lion's share of the portfolio, while Europe and Asia represent only 20%. Emerging countries and in particular Asia encompass several promising late-stage biotech companies.

HBM's portfolio has a clear focus on biotech companies, although it is well balanced in terms of therapeutics areas and development stages of drug candidates.

Chart 27: Portfolio breakdown by sector, therapy, and stage



Source: HBM Healthcare's portfolio as of 31/03/2019

**Sector**

As of the end of March 2019, biotech investments represented the main part of HBM Healthcare's portfolio (65%), while the company also invested in medical devices companies, health services companies, and health IT (digital health, which uses technology to help improve individuals' health and wellness).

### Therapeutic area

HBM Healthcare invests in fast-growing healthcare areas where medical needs are important. Hence, more than one-third of HBM's portfolio is made up of companies involved in orphan diseases or oncology.

While half of the drugs approved in 2015 were developed for orphan diseases, more and more biotech companies are engaging in R&D related to such diseases. Indeed, this involvement in the rare disease business allows biotech companies to develop drugs more quickly (orphan drug designation) and charge higher prices for many rare disease drugs.

The rationale for oncology is different. Oncology is one therapeutic class where science has made huge progress in recent years, thanks to innovative IO treatment. Thus, numerous companies have developed targeted therapies for multiple solid and liquid tumours. However, despite all these medical advances, there are still huge unmet medical needs. Much of the growth in pharma is set to come from new cancer medicines, in particular immunotherapies expected to generate sales over USD130bn by 2022E.

### Development stage

The value of a healthcare/biotech portfolio increases with the advancement of its underlying pipeline. Whereas the development of a new drug is a high-risk, high-reward business, the likelihood of approval (LOA) is defined for each stage of development. According to Bio and Biomedtracker, these probabilities of success are based on a statistical analysis of records from the last ten years for each new drug (from January 2006 to December 2015).

**Table 1: Phase transition success rate and LOA, all modalities**

	POS* (%)	LOA** (%)
Ph. I --> Ph. II	63.2%	9.6%
Ph. II --> Ph. III	30.7%	15.2%
Ph. III --> Regulatory	58.1%	49.6%
NDA/BLA --> Market approval	85.3%	85.3%

\*Probability of success; \*\*LOA

Source: BIO Industry Analysis, Kepler Cheuvreux

Thus, on average, LOA increases from 9.6% for a new drug in phase I to 49.6% for a drug in phase III. The valuation of the drug increases as the LOA increases.

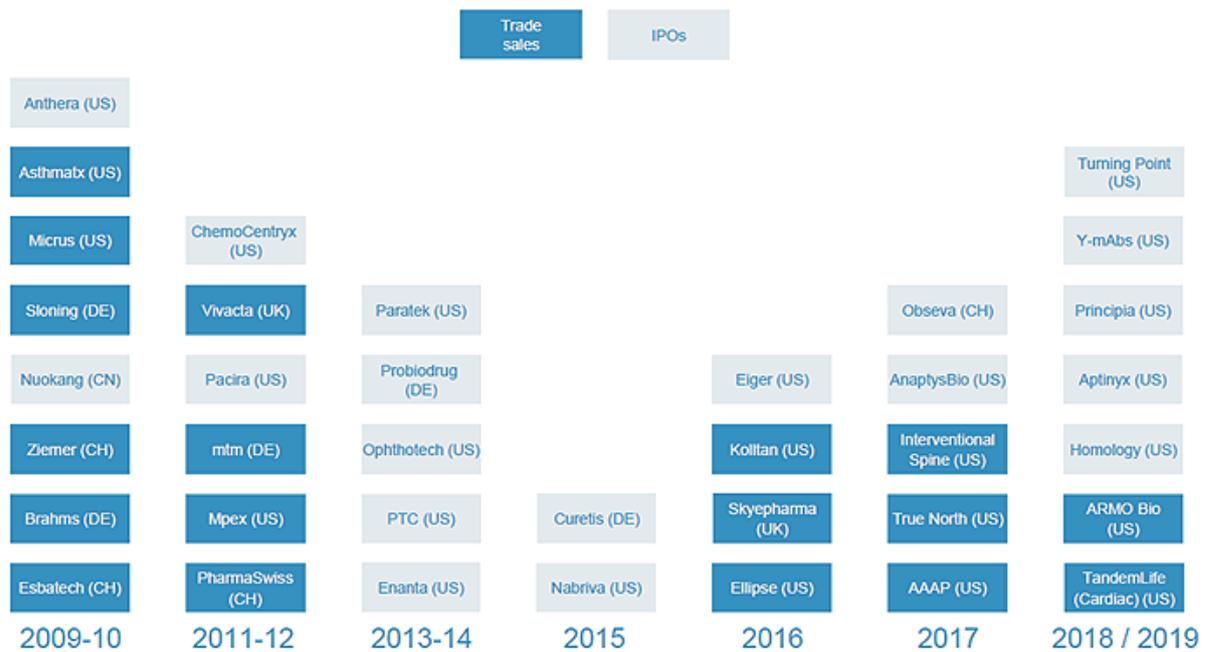
In HBM's portfolio, about half of all assets are exposed to companies with lead phase II and phase III drugs.

### ...with a successful exit strategy

While HBM Healthcare is known as a long-term investor, an exit strategy mindset is always present. Hence, HBM Healthcare wants to be able to influence its portfolio companies, particularly with regard to an exit. However, HBM can increase its level of investment in subsequent financing rounds if the potential for value creation remains intact.

Thus, HBM has been a strong contributor to value creation for its portfolio companies, and the fund has a proven track record of exits, validated by over 50 trade sales or public offerings since 2001.

Chart 28: Trade sales and IPOs



Source: HBM Healthcare

### And attractive dividend policy

Since 2013, HBM's strategy has evolved, and the company has decided to set up an attractive dividend policy. Thus, on average the dividend yield is in the range of 3-5% per year.

Table 2: Distribution

	2014	2015	2016	2017	2018	2019
Net dividend per share (CHF)	3.00	5.50	5.50	5.80	7.00	7.50
Shares outstanding	8.5	7.8	7.4	7.1	7.0	7.0
Distribution (CHFm)	25.5	42.9	40.7	41.2	49.0	52.5
Distribution yield (%)	4.0%	5.1%	5.1%	5.2%	4.9%	-

Source: HBM Healthcare, Kepler Cheuvreux

This policy allows HBM to gain shareholder loyalty and thus avoid a potential important sell-off in difficult periods.

### Share buyback programme

Besides dividends, HBM Healthcare regularly uses share buybacks as a way to return money to shareholders. Thus, on 24 June 2016, a share buyback programme of up to 730,000 shares was approved at the AGM. This programme ended in 23 June 2019.

In late June 2019, HBM Healthcare launched a new share buyback programme. This new programme was approved earlier in the month during the company's AGM and will lead to the potential cancellation of up to 696,000 shares (10% of the shares issued). This programme will last until 27 June 2022 at the latest.

## The best performance among its peer group

Despite its lower investment exposure to the US market (more dynamic, higher valuation) thanks to its wise choices, HBM Healthcare's medium- and long-term performance (one, three, and five years) is the best in its peer group. While some peers posted a better performance on a one-month basis, HBM has outperformed them over the long term.

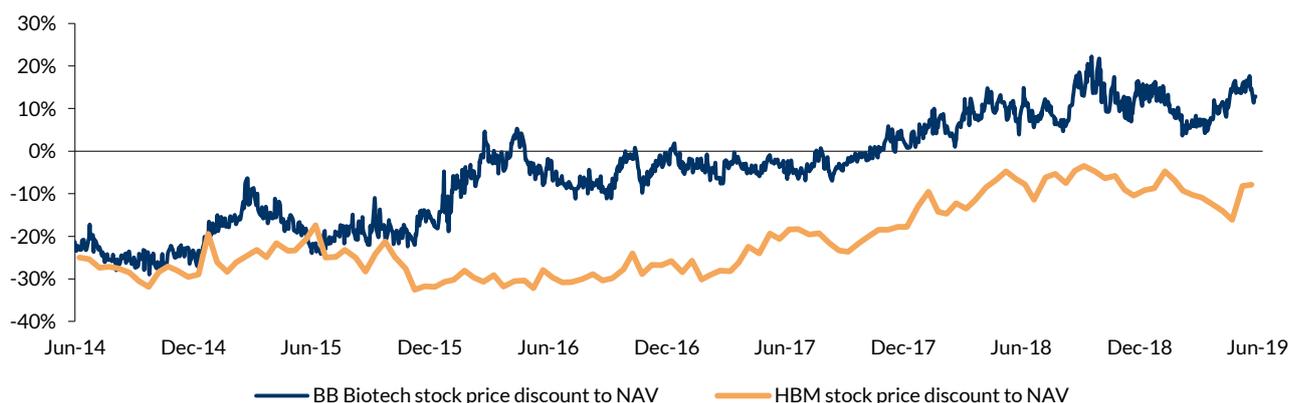
**Table 3: Performance of peer group – as of 07 July 2019**

	Country	Perf. 1M	Perf. 1Y	Perf. 3Y	Perf. 5Y	Price (LC)	NAV/share	Price to NAV
BB Biotech	CH	2.5%	-0.8%	41.4%	122.6%	67.9	59.8	14%
Biotech growth trust	UK	9.8%	-10.7%	11.7%	31.1%	9.6	10.8	-10%
BlackRock Health Sciences	US	2.8%	-5.8%	8.0%	20.0%	38.6	38.2	1%
<b>HBM Healthcare</b>	<b>CH</b>	<b>1.5%</b>	<b>18.4%</b>	<b>96.2%</b>	<b>128.8%</b>	<b>184.2</b>	<b>200.3</b>	<b>-8%</b>
International Biotechnology Trust	UK	4.0%	-6.3%	27.7%	85.0%	8.1	8.2	0%
Polar Capital Global Healthcare	UK	3.5%	2.3%	10.1%	22.0%	2.8	3.0	-8%
Tekla Healthcare Investors	US	2.6%	-13.3%	-19.6%	-17.6%	19.7	22.1	-11%
Tekla Healthcare Opportunities	US	3.2%	0.1%	7.2%	na	17.7	19.5	-9%
Worldwide Healthcare Trust	UK	4.4%	-6.1%	30.2%	73.5%	34.3	34.3	0%
<b>HBM Healthcare ranking versus peers</b>		<b>9</b>	<b>1</b>	<b>1</b>	<b>1</b>			<b>5</b>

Source: Kepler Cheuvreux

Despite the fact that it regularly and solidly outperforms its peers, HBM's share price discount to NAV is still in the middle of our selected peers. This discount to NAV has decreased in the past ten months, resulting in growing investor confidence in HBM's management and investments. However, we think there is room for further improvement. Indeed, BB Biotech, a Swiss peer, trades at a double-digit premium to NAV, while its medium- and long-term performances are below that of HBM.

**Chart 29: HBM Healthcare and BB Biotech stock price discount to NAV**



Source: Eikon

With an 8% discount to NAV currently, HBM's shares are trading at the same level as Polar Capital Global Healthcare, despite the fact that its shares have risen 5-8x more than the latter's (depending on the period: one, three, or five years).

## Investments in private companies could hide value

HBM Healthcare invests in a mix of private and public companies involved in healthcare at different stages of development. In private companies, HBM acts as a lead or co-lead investor with board representation. The recent performance of the fund has been boosted by several successful exits (IPOs and M&A activity) from the private portfolio. The current average return on investment of exits coming from the private portfolio since 2017 is 106%. This indicates the relevance of HBM's strategy (a greater focus on private companies).

**Table 4: An important return on investment**

Year	Exit	Company	Activity	HBM's investment (EURm)	Value at exit (EURm)	Current value (EURm)	Return on investment	Remark
2019	IPO	Turning Point (US)	Oncology	14.5	31.9	46.7	222%	Still in portfolio
2018	Trade sale	TandemLife (US)	Cardiology	4.4	33.9	-	670%	Sold
2018	Trade sale	ARMO Bio (US)	Oncology	22.2	42.3	59.3	167%	Sold
2018	IPO	Homology (US)	Rare genetic diseases	10	16.8	17.4	74%	Still in portfolio
2018	IPO	Aptinyx (US)	Neurologic disorders	8.5	18.55	2.6	-69%	Still in portfolio
2018	IPO	Principia (US)	Immuno-oncology	19.2	41.1	29.9	56%	Still in portfolio
2018	IPO	Y-mAbs (US)	Immunotherapy	32.6	73.8	62.0	90%	Still in portfolio
2017	Trade sale	AAAP (US)	Oncology, neurology	85.3	164.9	-	93%	Sold
2017	Trade sale	True North (US)	Haematology	10	10.3	-	3%	Sold
2017	Trade sale	Interventional Spine (US)	Implantable devices	18	26.9	-	49%	Sold
2017	IPO	AnaptysBio (US)	Inflammatory diseases	7	21.0	14.3	104%	Still in portfolio
2017	IPO	ObsEva (CH)	Woman's reproductive health and pregnancy	9.9	31.2	29.1	194%	Still in portfolio

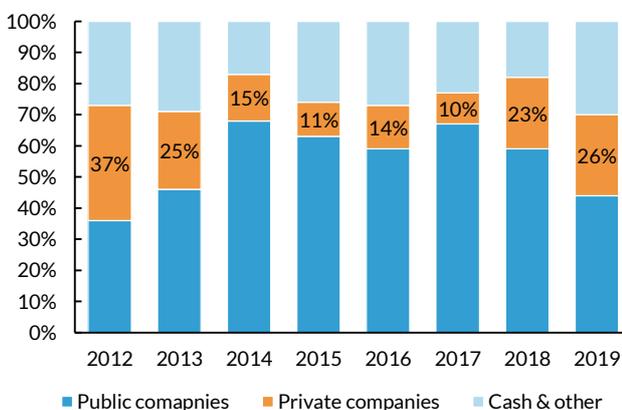
Source: Kepler Cheuvreux, HBM Healthcare

On the flipside, it is always difficult to correctly assess companies from the private portfolio, due to the lack of information. The fair value of these investments is either equal to their acquisition price or the value determined during the last financing round. Hence, their real valuation potential is more difficult to estimate.

## Increasing the weight of the private portfolio

HBM Healthcare's private portfolio has grown in recent years with the addition of new and follow-on investments.

**Chart 30: Asset allocation over time**



Source: Kepler Cheuvreux

**Chart 31: Largest private investment over the last five years**



Source: HBM

Currently, private companies represent 26% of HBM's asset allocation, and this is set to increase over the coming months.

### **An important bet in the private portfolio: Cathay Industrials Biotech**

HBM Healthcare is a long-term shareholder. When an investment opportunity is identified, the company conducts its due diligence and evaluates the investment potential. The company regularly reassesses its investment and can be a long-term investor that supports value creation over several years if it considers the investment undervalued. However, in specific cases (disappointing clinical results, changes of control, etc.) the holding period may be shorter.

An interesting example of this long-term strategy is the investment in Cathay Industrial Biotech. HBM Healthcare invested in this innovative company more than ten years ago, and it currently owns 7.9% of Cathay. This investment represents the group's largest investment (12.1% of the entire investment portfolio and 30% of the private portfolio). Despite some setbacks at Cathay's inception, HBM Healthcare has strongly supported its management. Currently, HBM Healthcare is one of the main shareholders in the company. Cathay is likely to go public, which could lead to an interesting and significant exit for HBM Healthcare.

**Table 5: A long-term investor**

	03/2013	03/2014	03/2015	03/2016	03/2017	03/2018	03/2019
Valuation of Cathay's investment (USDm)	28	28	14	44	44	92	126
Ownership	12.6%	12.6%	12.6%	9.5%	9.3%	8.5%	7.9%
% of HBM's portfolio	4.4%	2.7%	1.3%	4.1%	4.0%	7.5%	12.1%

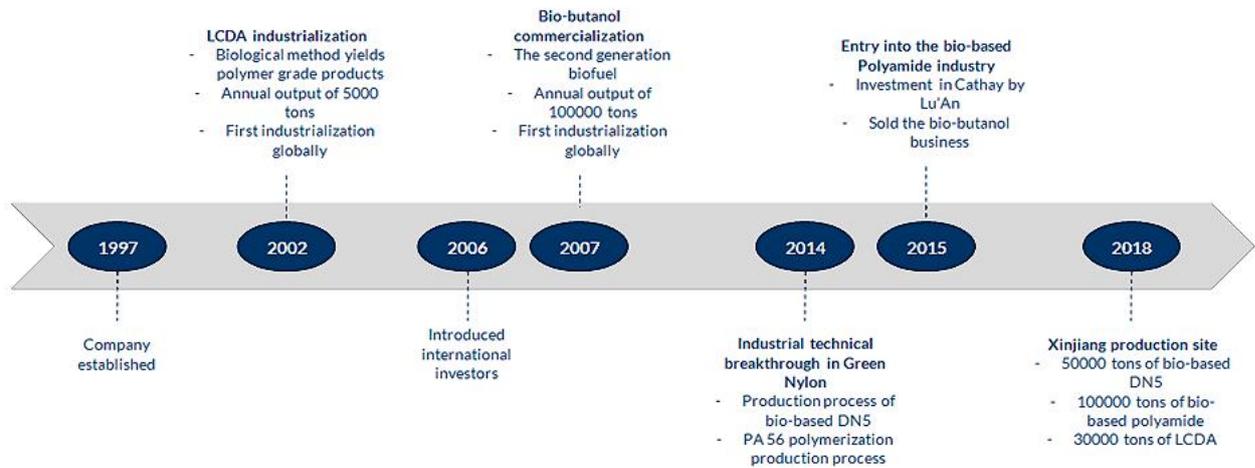
Source: Kepler Cheuvreux, HBM Healthcare

Cathay was founded in 1997. It was HBM Healthcare's first investment in China (Shanghai).

Cathay's goal is to replace conventional production processes with biotechnological methods. It uses biotechnological processes to produce chemicals, fuels, and polymers.

Cathay is an industrial biotechnology firm that produces long chain dibasic acids (LCDAs). LCDAs are mainly used as chemical replacements for nylons, polyesters, adhesives, and bio-solvents. Cathay offers environmental solutions, as the raw material for polyamide comes from renewable starchy plants. It is considered to be the most advanced bio-manufacturing material since the invention of petrol-based PA66 and PA6.

Chart 32: Cathay's history



Source: Kepler Cheuvreux

Cathay's bio-based polyamide has had a lot of success in the textile and plastic industries as an environmental alternative, but also as a unique and new polymer. For customers, Cathay's products are of interest to various industries, including chemicals, automobiles, and textiles. DuPont, Evonik, Arkema, Novo Nordisk, and Akzo Nobel are all customers, for instance.

Cathay currently has two production sites and one R&D centre in China (Shanghai): Zhanjiang Hi-Tech Park. The latter is mainly focused on research in molecular biology, fermentation process engineering, polymer materials, etc.

Cathay aims to become the first company to produce the bio-based diamine 5 on a commercial scale. The company is now profitable and had more than USD150m in turnover in 2018. In the medium term, Cathay is targeting an IPO to finance long-term growth. The IPO would help improve HBM's valuation and would be an important trigger to establish the "real" value of this promising company.

## We update our model and lift our TP

We update our model for HBM Healthcare, taking into account the advancement of its portfolio. We lift our TP to CHF220, implying 19% upside, based on the assumption that NAV will reach the value implied by analysts and consensus target prices for HBM's public company holdings, while we do not include valuation upside from the private equity part of the portfolio or the funds. Lastly, we apply a conservative 10% discount to NAV to obtain our TP (vs. 5% currently and a three-year average of 16%).

### NAV-based pricing model

A peer comparison is not appropriate, as the investment theme for each fund is different, as are their returns. However, in the medium to long term, HBM Healthcare's discount to NAV could shrink again and even switch to a premium.

#### Target price lifted to CHF220

Our HBM valuation is based on the NAV of the company portfolio, with a discount applied by the market.

HBM publishes the net asset value per share of its fund twice a month. This NAV is calculated from the share price of publicly traded portfolio companies, while the fair values of the funds and investments in private companies are included at their acquisition costs or at the value determined during the last financing round.

Kepler Cheuvreux's healthcare/biotech team does not cover any companies in HBM Healthcare Investments' public portfolio (except Argenx). Hence, our NAV is based on the following assumptions:

- For public companies, we apply consensus target prices from Bloomberg when more than four analysts cover the stock. Otherwise, we apply valuations based on the most recent update.
- For private companies and funds, we apply the last disclosed fair value reported (as of 31 March 2019) despite the solid track record on exits.
- A discount to NAV of 10%, which is lower than the current discount to NAV but higher than the average seen over the last three years. This discount to NAV aims to reflect the positive advancement of HBM's portfolio.

Accordingly, we derive a target NAV per share of CHF247 and a TP of CHF220 including a discount to NAV of 10%, leading to 19% upside to the last listed price. At the current price of HBM shares and taking into account the market value of the public portfolio, HBM's share discount to NAV is around 7%.

**Table 6: Valuation – Part I – Public portfolio**

Name	Currency	HBM holding (%)	Current share price (LC)	Market cap (LC in m)	Current value (CHFm)	TP (consensus)	TP range	Analysts	Valuation at TP (CHFm)
Y-mAbs Therapeutics	USD	8.4%	22.95	785	64.6	35.0	30-40	5	98.5
Vectura	GBP	6.3%	83.15	554	42.8	117.3	94-160	11	59.8
Pacira Pharmaceuticals	USD	2.3%	40.86	1,687	38.2	52.9	15-85	16.0	49.4
Galapagos	USD	0.5%	152.45	8,358	49.1	132.4	91-180	15	42.8
Ultragenyx Pharm.	USD	0.8%	58.62	3,369	26.0	75.5	51-89	19	33.4
Principia Biopharma	USD	3.5%	39.59	945	32.5	47.0	40-55	6	38.6
Zogenix	USD	1.2%	47.24	2,003	61.0	61.9	50-73	12	79.9
Immunomedics	USD	0.7%	14.22	2,724	18.4	25.0	14-40	10	32.3
Alnylam	USD	0.3%	72.79	7,755	19.0	116.6	62-150	20	30.5
Argenx	USD	0.5%	143.48	5,408	29.2	158.1	143-182	16	32.2
Argenx (ADS)	USD	0.5%	143.48	5,408	26.3	158.1	143-182	16	28.9
Esperion Therapeutics	USD	2.1%	45.61	1,228	25.6	94.5	56-153	13	53.1
RA Pharmaceuticals	USD	2.0%	33.18	1,404	27.7	41.0	32-48	10	34.2
Acadia Pharmaceuticals	USD	0.5%	26.72	3,852	18.4	33.5	21-60	12	23.1
AnaptysBio	USD	0.9%	55.66	1,504	13.5	116.3	79-146	11	28.2
ObsEva	USD	3.1%	10.15	442	13.9	30.6	23-44	8	41.7
Arena Pharmaceuticals	USD	0.7%	62.07	3,077	22.3	69.0	60-79	10	24.8
Amicus Therapeutics	USD	0.5%	12.53	3,119	13.1	19.0	15-31	12	19.8
Retrophin	USD	1.4%	21.22	879	12.3	43.4	35-57	8	25.1
Divis Laboratories	INR	0.2%	1,648.6	437,652	11.0	1,751.1	1445-1925	17	11.8
Coherus Biosciences	USD	1.2%	18.86	1,308	15.2	29.0	25-35	7	23.3
Nicox	USD	5.6%	4.98	149	9.3	10.5	10-11	3	19.4
Idorsia	USD	0.5%	23.62	3,098	15.6	18.9	16-24	6	12.5
Uniqure	USD	0.5%	69.65	2,633	12.1	86.2	63-175	13	15.0
Albireo Pharma	USD	2.7%	28.84	347	9.1	59.8	41-87	8	18.8
Arrowhead Pharm.	USD	0.6%	27.8	2,636	15.0	28.1	24-33	5	15.2
Spring Bank Pharm.	USD	4.0%	4.73	78	3.1	23.4	10-29	6	15.2
Beigene	HKD	0.1%	73.2	57,100	6.5	100.6	62-125	10	8.9
Beigene (ADR)	USD	0.1%	122.91	7,375	6.0	178.3	146-214	15	8.8
Jubilant Life Science	INR	0.4%	465.65	74,169	4.1	732.4	620-915	13	6.4
Assembly Biosciences	USD	1.1%	13.59	348	3.9	47.6	30-74	6	13.6
Dermira	USD	0.8%	8.61	462	3.4	22.5	14-29	10	8.9
Xenon Pharmaceuticals	USD	2.0%	10.51	271	5.4	20.0	16-23	3	10.3
Myokardia	USD	0.2%	50.22	2,314	4.9	80.0	70-90	10	7.9
Collectis (ADR)	USD	0.6%	15.73	668	4.2	44.0	21-73	11	11.7
Nabriva Therapeutics	USD	2.6%	2.41	175	4.4	7.8	5-13	7	14.0
Viking Therapeutics	USD	0.6%	8.24	594	3.2	24.6	12-41	11	9.7
Paratek Pharmaceuticals	USD	2.2%	3.67	119	2.6	21.3	7-44	8	14.8
Rubius Therapeutics	USD	0.3%	14.78	1,181	3.0	33.8	25-40	6	6.9
Alimera Sciences	USD	4.9%	0.87	62	3.0	2.8	2-3	6	9.5
Solara Active	INR	2.5%	428.95	11,056	3.8	650.0	650-650	0	5.7
Hansa Medical	SEK	0.4%	183.3	7,466	2.9	352.5	320-400	6	5.6
Laurus Labs	INR	0.6%	349.4	37,189	3.0	456.0	410-515	6	4.0
Vicore Pharma	SEK	4.6%	18	763	3.7	41.5	41-42	2	8.5
Aptinyx	USD	2.2%	3.81	128	2.8	11.5	7-15	5	8.3
Other					18.8				18.8
<b>Total public companies</b>					<b>733.5</b>				<b>1,089.7</b>

Source: Kepler Cheuvreux

The group's portfolio of public company investments is well balanced (more than 30 positions), leading to a valuation that is less sensitive to any particular event in its portfolio. However, HBM has strong convictions on certain investments. Its five largest investments represent 20% of the portfolio. Accordingly, the five main upsides in this public portfolio represent one-third of the total upside (based on consensus estimates).

**Table 7: Valuation – Part II – Private portfolio and Funds**

Name	Currency	HBM holding (%)	Current value (CHFm)	Valuation at TP (CHFm)
<b>Total public companies</b>			<b>733.5</b>	<b>1,089.7</b>
Cathay Industrial Biotech	USD	7.9%	125.1	125.1
Neurelis	USD	15.0%	37.5	37.5
Harmony Biosciences	USD	7.6%	32.5	32.5
Amicus	EUR	29.0%	22.3	22.3
1mg	INR	10.5%	20.9	20.9
SAI Life Sciences	INR	5.3%	19.3	19.3
Jianke Pharmaceutical	USD	3.3%	14.8	14.8
Westmed Holding	USD	25.2%	12.4	12.4
SpringWorks Therapeutics	USD	3.6%	11.9	11.9
Turning Point Therapeutics	USD	3.3%	10.0	10.0
Vascular Dynamics	USD	13.1%	9.7	9.7
FarmaLatam	USD	70.2%	8.8	8.8
Valcare	USD	8.4%	7.0	7.0
ConnectRN	USD	20.2%	6.6	6.6
Shape Memory Medical	USD	17.4%	6.0	6.0
Sphingotec	EUR	7.1%	5.0	5.0
Cardialen	USD	17.8%	5.0	5.0
Galera Therapeutics	USD	2.0%	5.0	5.0
Forbuis (Formation Biologics)	CAD	9.6%	4.8	4.8
Vitaeris	USD	18.7%	4.0	4.0
<i>Other</i>			17.7	17.7
<b>Total private companies</b>			<b>409.6</b>	<b>409.6</b>
HBM BioCapital II	EUR		23.0	23.0
MedFocus Fund II	USD		18.7	18.7
WuXi Healthcare Ventures II	USD		28.4	28.4
6 Dimensions Capital	USD		14.0	14.0
BioMedInvest II	CHF		7.0	7.0
Hatteras Venture Partners III	USD		5.9	5.9
Tata Capital HBM Fund I	USD		8.2	8.2
Galen Partners V	USD		4.9	4.9
Nordic Biotech	DKK		1.6	1.6
BioMedInvest I	CHF		5.1	5.1
HBM Genomics	USD		11.5	11.5
BioVeda China	USD		1.3	1.3
C-Bridge Capital IV	USD		1.2	1.2
<i>Other</i>			1.9	1.9
<b>Total funds</b>			<b>132.6</b>	<b>132.6</b>
<b>Total investments</b>			<b>1,230.4</b>	<b>1,631.8</b>
Cash and other assets less liabilities (net)			87.9	87.9
<b>Net Asset Value</b>			<b>1,318.3</b>	<b>1,719.7</b>
Number of shares (m)			7.0	7.0
<b>NAV per share (CHF)</b>			<b>196.0</b>	<b>247.2</b>
Discount				10%
<b>Fair value (CHF)</b>				<b>222.5</b>

Source: Kepler Cheuvreux

Note that the “cash less liabilities” item includes among other things the cash available in the fund for new investment (CHF263m as of the end of March 2019), as well as CHF100m in bond liabilities (two straight bond tranches, each with a par value of CHF50m and maturing on 10 July 2021 and 10 July 2023).

**Table 8: Sensitivity analysis**

Discount to NAV	0%	5%	10%	15%
Fair value (CHF)	247.2	234.8	<b>222.5</b>	210.1

Source: Kepler Cheuvreux

### **Upside to our valuation**

Our valuation only includes the potential of public companies based on their target prices. This valuation does not include valuation upside from private companies or funds. Indeed, these investments are valued at their acquisition costs or the price of the last financing round. Hence, their valuation does not change before either an exit or a new financing round. In particular, the most upside should come from Cathay Industrial Biotech.

Thus, these investments represent the hidden value of HBM's portfolio. Before investing in a private company, HBM assesses the potential exit strategy. The main exit for private companies is an IPO or acquisition.

# Valuation

FY to 31/03 (CHF)	03/14	03/15	03/16	03/17	03/18	03/19	03/20E	03/21E
<b>Per share data (CHF)</b>								
EPS adjusted	40.98	32.58	3.06	19.01	16.40	30.05	27.99	30.02
% Change	445.2%	-20.5%	-90.6%	521.5%	-13.7%	83.3%	-6.9%	7.3%
EPS adjusted and fully diluted	40.98	32.58	3.06	19.01	16.40	30.05	27.99	30.02
% Change	445.2%	-20.5%	-90.6%	521.5%	-13.7%	83.3%	-6.9%	7.3%
EPS reported	40.98	32.58	3.06	19.01	16.40	30.05	27.99	30.02
% Change	445.2%	-20.5%	-90.6%	521.5%	-13.7%	83.3%	-6.9%	7.3%
EPS Consensus								
Cash flow per share	39.40	30.61	-5.82	16.86	10.45	24.71	20.39	23.43
Book value per share	106.68	135.46	135.09	153.51	165.71	187.23	229.48	275.85
DPS	3.00	5.50	5.50	5.80	7.00	7.50	7.66	8.04
Number of shares, YE (m)	8.6	7.9	7.6	7.1	6.9	7.0	7.0	7.0
Number of shares, fully diluted, YE (m)	8.6	7.9	7.6	7.1	6.9	7.0	7.0	7.0
<b>Share price</b>								
Latest price / year end	75.5	108.0	99.5	111.4	144.0	168.8	184.8	184.8
52 week high	80.0	112.5	111.5	113.1	144.0	184.0	186.4	
52 week low	49.3	70.3	92.0	92.0	111.3	145.0	162.8	
Average price (Year)	64.2	89.1	99.8	100.2	123.6	163.9	184.8	184.8
<b>Enterprise value (CHFm)</b>								
Market capitalisation	554.1	706.4	753.3	709.4	857.9	1,140.4	1,285.7	1,285.7
Net financial debt	-46.9	-76.9	-15.9	36.6	40.6	-43.1	-92.4	-155.2
Pension provisions	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
IFRS 16 debt	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Market value of minorities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Market value of equity affiliates (net of tax)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Others	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Enterprise value	507.2	629.5	737.4	746.0	898.6	1,097.2	1,193.2	1,130.4
<b>Valuation</b>								
P/E adjusted	1.6	2.7	32.6	5.3	7.5	5.5	6.6	6.2
P/E adjusted and fully diluted	1.6	2.7	32.6	5.3	7.5	5.5	6.6	6.2
P/E consensus								
P/BV	0.6	0.7	0.7	0.7	0.7	0.9	0.8	0.7
P/CF	1.6	2.9	na	5.9	11.8	6.6	9.1	7.9
Dividend yield (%)	4.7%	6.2%	5.5%	5.8%	5.7%	4.6%	4.1%	4.4%
Dividend yield preference shares (%)	4.7%	6.2%	5.5%	5.8%	5.7%	4.6%	4.1%	4.4%
FCF yield (%)	61.3%	34.4%	-5.8%	16.8%	8.5%	15.1%	11.0%	12.7%
ROE (%)	46.5%	25.9%	2.2%	12.8%	10.2%	17.0%	13.4%	11.9%
ROIC (%)	na	na	na	na	na	na	na	na
EV/Sales	na	na	na	na	na	na	na	na
EV/EBITDA	na	na	na	na	na	na	na	na
EV/EBIT	na	na	na	na	na	na	na	na
EV/NOPAT	na	na	na	na	na	na	na	na
EV/IC	na	na	na	na	na	na	na	na
ROIC/WACC	na	na	na	na	na	na	na	na
EV/IC over ROIC/WACC	na	na	na	na	na	na	na	na

# Income statement

FY to 31/03 (CHF)	03/14	03/15	03/16	03/17	03/18	03/19	03/20E	03/21E
<b>Sales</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>
Gross profit	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
EBITDA reported	0.0	0.0	0.0	0.0	0.0	-4.0	-4.1	-4.2
<b>EBITDA adjusted</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>
Depreciation and amortisation	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Goodwill impairment	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other financial result and associates	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
EBIT reported	0.0	0.0	0.0	0.0	0.0	-4.0	-4.1	-4.2
<b>EBIT adjusted</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>
Net financial items	0.0	-0.3	-2.1	-2.6	-2.4	-2.4	-2.4	-2.4
Associates	353.5	258.6	25.2	137.1	116.2	215.5	201.3	215.5
Others	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Earnings before tax	353.5	258.4	23.1	134.6	113.8	209.1	194.7	208.8
Tax	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Net profit from continuing operations	353.5	258.4	23.1	134.6	113.8	209.1	194.7	208.8
Net profit from discontinuing activities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Net profit before minorities	353.5	258.4	23.1	134.6	113.8	209.1	194.7	208.8
Minorities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
<b>Net profit reported</b>	<b>353.5</b>	<b>258.4</b>	<b>23.1</b>	<b>134.6</b>	<b>113.8</b>	<b>209.1</b>	<b>194.7</b>	<b>208.8</b>
Adjustments	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
<b>Net profit adjusted</b>	<b>353.5</b>	<b>258.4</b>	<b>23.1</b>	<b>134.6</b>	<b>113.8</b>	<b>209.1</b>	<b>194.7</b>	<b>208.8</b>
Sales % Change	na	na	na	na	na	na	na	na
EBITDA reported % Change	na	na	na	na	na	na	na	na
EBITDA adjusted % Change	na	na	na	na	na	na	na	na
EBIT reported % Change	na	na	na	na	na	na	na	na
EBIT adjusted % Change	na	na	na	na	na	na	na	na
Earnings before tax % Change	427.6%	-26.9%	-91.1%	482.9%	-15.4%	83.7%	-6.9%	7.3%
Net profit from continuing operations % Change	427.6%	-26.9%	-91.1%	482.9%	-15.4%	83.7%	-6.9%	7.3%
Net profit reported % Change	427.6%	-26.9%	-91.1%	482.9%	-15.4%	83.7%	-6.9%	7.3%
Net profit adjusted % Change	427.6%	-26.9%	-91.1%	482.9%	-15.4%	83.7%	-6.9%	7.3%
Gross profit margin (%)	na	na	na	na	na	na	na	na
EBITDA margin (%)	na	na	na	na	na	na	na	na
EBIT margin (%)	na	na	na	na	na	na	na	na
Net profit margin (%)	na	na	na	na	na	na	na	na
Tax rate (%)	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
Payout ratio (%)	7.3%	16.9%	179.8%	30.5%	42.7%	25.0%	27.4%	26.8%
EPS reported (CHF)	40.98	32.58	3.06	19.01	16.40	30.05	27.99	30.02
EPS adjusted (CHF)	40.98	32.58	3.06	19.01	16.40	30.05	27.99	30.02
EPS adj and fully diluted (CHF)	40.98	32.58	3.06	19.01	16.40	30.05	27.99	30.02
DPS (CHF)	3.00	5.50	5.50	5.80	7.00	7.50	7.66	8.04
DPS,preference shares (CHF)	3.00	5.50	5.50	5.80	7.00	7.50	7.66	8.04
EPS reported % Change	445.2%	-20.5%	-90.6%	521.5%	-13.7%	83.3%	-6.9%	7.3%
EPS adjusted % Change	445.2%	-20.5%	-90.6%	521.5%	-13.7%	83.3%	-6.9%	7.3%
EPS adj and fully diluted % Change	445.2%	-20.5%	-90.6%	521.5%	-13.7%	83.3%	-6.9%	7.3%
DPS % Change	100.0%	83.3%	0.0%	5.5%	20.7%	7.1%	2.1%	5.0%
Consensus Sales (CHFm)								na
Consensus EBITDA (CHFm)								na
Consensus EBIT (CHFm)								na
Consensus EPS (CHF)								na
Consensus DPS (CHF)								na

# Cash flow statement

FY to 31/03 (CHF)	03/14	03/15	03/16	03/17	03/18	03/19	03/20E	03/21E
Net profit before minorities	353.5	258.4	23.1	134.6	113.8	209.1	194.7	208.8
Depreciation and amortisation	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Goodwill impairment	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Change in working capital	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Others	-13.6	-15.6	-67.1	-15.2	-41.3	-37.1	-52.9	-45.8
<b>Levered post tax CF before capex</b>	<b>339.9</b>	<b>242.8</b>	<b>-44.0</b>	<b>119.3</b>	<b>72.5</b>	<b>171.9</b>	<b>141.8</b>	<b>163.0</b>
% Change	508.8%	-28.6%	na	na	-39.2%	137.0%	-17.5%	14.9%
Capex	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
<b>Free cash flow</b>	<b>339.9</b>	<b>242.8</b>	<b>-44.0</b>	<b>119.3</b>	<b>72.5</b>	<b>171.9</b>	<b>141.8</b>	<b>163.0</b>
% Change	508.8%	-28.6%	na	na	-39.2%	137.0%	-17.5%	14.9%
Acquisitions	-309.8	-323.3	-395.9	-405.0	-556.5	-534.0	0.0	0.0
Divestments	329.8	461.7	476.5	444.9	661.6	710.8	146.8	155.9
Dividend paid	0.0	-23.6	-42.3	-39.2	-40.8	-38.1	-53.3	-56.0
Share buy back	-20.6	-78.9	-35.9	-29.1	-9.9	-6.1	0.0	0.0
Capital increases	5.0	6.0	7.0	8.0	9.0	10.0	11.0	12.0
Others	-349.4	-190.8	-1.0	6.2	-125.9	-266.3	-197.0	-212.1
<b>Change in net financial debt</b>	<b>-5.2</b>	<b>93.9</b>	<b>-35.6</b>	<b>105.2</b>	<b>10.1</b>	<b>48.3</b>	<b>49.3</b>	<b>62.8</b>
Change in cash and cash equivalents	-6.1	93.5	-25.6	104.2	4.2	45.5	49.3	62.8
Attributable FCF	339.9	242.8	-44.0	119.3	72.5	171.9	141.8	163.0
Cash flow per share (CHF)	39.40	30.61	-5.82	16.86	10.45	24.71	20.39	23.43
% Change	529.1%	-22.3%	na	na	-38.0%	136.5%	-17.5%	14.9%
FCF per share (CHF)	39.40	30.61	-5.82	16.86	10.45	24.71	20.39	23.43
% Change	529.1%	-22.3%	na	na	-38.0%	136.5%	-17.5%	14.9%
Capex / Sales (%)	na	na	na	na	na	na	na	na
Capex / D&A (%)	na	na	na	na	na	na	na	na
Cash flow / Sales (%)	na	na	na	na	na	na	na	na
FCF / Sales (%)	na	na	na	na	na	na	na	na
FCF Yield (%)	61.3%	34.4%	-5.8%	16.8%	8.5%	15.1%	11.0%	12.7%
Unlevered FCF Yield (%)	67.0%	38.6%	-5.7%	16.3%	8.3%	15.9%	12.1%	14.6%

# Balance sheet

FY to 31/03 (CHF)	03/14	03/15	03/16	03/17	03/18	03/19	03/20E	03/21E
Cash and cash equivalents	46.9	140.4	114.8	219.0	223.2	268.7	318.0	380.7
Inventories	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Accounts receivable	0.2	0.2	0.2	0.4	0.4	0.6	0.6	0.6
Other current assets	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
<b>Current assets</b>	<b>47.1</b>	<b>140.6</b>	<b>115.0</b>	<b>219.4</b>	<b>223.6</b>	<b>269.2</b>	<b>318.5</b>	<b>381.3</b>
Tangible assets	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Goodwill	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other Intangible assets	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Financial assets	878.6	1,050.6	1,007.6	1,126.8	1,193.6	1,262.4	1,507.0	1,766.8
Other non-current assets	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
<b>Non-current assets</b>	<b>878.6</b>	<b>1,050.6</b>	<b>1,007.6</b>	<b>1,126.8</b>	<b>1,193.6</b>	<b>1,262.4</b>	<b>1,507.0</b>	<b>1,766.8</b>
Short term debt	0.0	63.5	0.0	156.5	164.6	126.1	126.1	126.1
Accounts payable	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other short term liabilities	1.5	3.1	3.8	3.8	3.0	3.5	3.5	3.5
<b>Current liabilities</b>	<b>1.5</b>	<b>66.6</b>	<b>3.8</b>	<b>160.3</b>	<b>167.5</b>	<b>129.6</b>	<b>129.6</b>	<b>129.6</b>
Long term debt	0.0	0.0	98.9	99.1	99.2	99.4	99.4	99.4
Pension provisions	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
IFRS16 Debt	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other long term provisions	3.8	50.4	0.0	0.0	0.0	0.0	0.0	0.0
Other long term liabilities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
<b>Non-current liabilities</b>	<b>3.8</b>	<b>50.4</b>	<b>98.9</b>	<b>99.1</b>	<b>99.2</b>	<b>99.4</b>	<b>99.4</b>	<b>99.4</b>
Shareholders' equity	920.3	1,074.2	1,019.9	1,086.9	1,150.5	1,302.6	1,596.5	1,919.1
Minority interests	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
<b>Total equity</b>	<b>920.3</b>	<b>1,074.2</b>	<b>1,019.9</b>	<b>1,086.9</b>	<b>1,150.5</b>	<b>1,302.6</b>	<b>1,596.5</b>	<b>1,919.1</b>
<b>Balance sheet total</b>	<b>925.7</b>	<b>1,191.2</b>	<b>1,122.7</b>	<b>1,346.2</b>	<b>1,417.3</b>	<b>1,531.6</b>	<b>1,825.5</b>	<b>2,148.1</b>
% Change	53.8%	28.7%	-5.8%	19.9%	5.3%	8.1%	19.2%	17.7%
Book value per share (CHF)	106.68	135.46	135.09	153.51	165.71	187.23	229.48	275.85
% Change	58.2%	27.0%	-0.3%	13.6%	7.9%	13.0%	22.6%	20.2%
Net financial debt	-46.9	-76.9	-15.9	36.6	40.6	-43.1	-92.4	-155.2
IFRS16 Debt	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Pension provisions	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Others	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Net debt	-46.9	-76.9	-15.9	36.6	40.6	-43.1	-92.4	-155.2
Net debt / EBITDA (x)	na	na	na	na	na	na	na	na
Trade working capital	0.2	0.2	0.2	0.4	0.4	0.6	0.6	0.6
Net working capital	-1.4	-2.9	-3.6	-3.3	-2.5	-2.9	-2.9	-2.9
NWC/Sales	na	na	na	na	na	na	na	na
Inventories/sales	na	na	na	na	na	na	na	na
Invested capital	-1.4	-2.9	-3.6	-3.3	-2.5	-2.9	-2.9	-2.9
Net fin. debt / FCF (x)	-0.1	-0.3	0.4	0.3	0.6	-0.3	-0.7	-1.0
Gearing (%)	-5.1%	-7.2%	-1.6%	3.4%	3.5%	-3.3%	-5.8%	-8.1%
Goodwill / Equity (%)	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%

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Stock	ISIN	Currency	Price
Argenx	NL0010832176	EUR	131.30
HBM Healthcare	CH0012627250	CHF	184.80
Merck KGaA	DE0006599905	EUR	92.68

Source: Factset closing prices of 17/07/2019

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Rating Breakdown	A	B
Buy	50%	56%
Hold	33%	30%
Reduce	14%	9%
Not Rated/Under Review/Accept Offer	3%	5%
Total	100%	100%

Source: Kepler Cheuvreux

A: % of all research recommendations

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Argenx (EUR)	13/06/2019 07:27	Equity Research	Buy	140.00	107.00
Merck KGaA (EUR)	19/10/2018 07:04	Equity Research	Buy	105.00	92.64
	15/11/2018 08:20	Equity Research	Buy	108.00	98.00
	14/03/2019 09:33	Equity Research	Buy	110.00	98.92
	22/05/2019 08:36	Equity Research	Buy	108.00	90.84

Credit research does not issue target prices. Left intentionally blank.

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