

AFT Pharmaceuticals

Financial update

On the cusp

Pharma & biotech

31 May 2017

Price **NZ\$2.30**
Market cap **NZ\$223m**

NZ\$0.68/US\$

Net debt (NZ\$m) at March 2017 7.45

Shares in issue 97.1m

Free float 24.3%

Code AFT

Primary exchange NZX

Secondary exchange ASX

Share price performance



% 1m 3m 12m

Abs (6.3) (19.1) (23.3)

Rel (local) (6.6) (20.7) (24.4)

52-week high/low NZ\$3.22 NZ\$2.25

Business description

AFT Pharmaceuticals is a specialty pharmaceutical company that operates primarily in Australasia but has product distribution agreements across the globe. The company's product portfolio includes prescription and over-the-counter drugs to treat a range of conditions and a proprietary nebuliser.

Next events

Maxigesic launches 2017

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AFT Pharma recently reported its FY17 results. Operating revenue grew 8.1% compared to FY16, mainly due to 19% growth in the Australian market, which currently comprises 53% of company revenue. New Zealand was weak due to Metoprolol issues and weak pharmacy demand. Maxigesic continues to do well internationally and is now launched in eight countries. Additionally, a licence agreement was recently announced in France, the world's second largest market for similar products.

Year end	Revenue (NZ\$m)	PBT* (NZ\$m)	EPS* (NZ\$)	DPS (NZ\$)	P/E (x)	Yield (%)
03/16	64.0	(10.8)	(0.11)	0.0	N/A	N/A
03/17	69.2	(18.5)	(0.19)	0.0	N/A	N/A
03/18e	97.7	(0.6)	(0.01)	0.0	N/A	N/A
03/19e	124.2	14.7	0.15	0.0	15.3	N/A

Note: *PBT and EPS are normalised, excluding amortisation of acquired intangibles, exceptional items and share-based payments.

Australian market leads the way

Revenue in Australia was up 19% in FY17 compared to FY16, thanks in large part to Maxigesic sales doubling as well as successful launches of Crystaderm and Restoranail. Growth is expected to continue to be robust as patients switch from codeine containing products (which will no longer be available over the counter after 1 February 2018 due to re-scheduling) to Maxigesic.

Maxigesic marketing expanding globally

Maxigesic is currently sold and launched in eight countries and distribution agreements are in place in a total of 112, including a recent licence deal in France, which has a US\$900m market for paracetamol/acetaminophen and ibuprofen tablets (the second largest in the world, behind the US). AFT is targeting between 30-40 launches for Maxigesic in FY18.

R&D programmes progressing

The FDA has accepted the application for registration for the oral version of Maxigesic and a decision is pending (likely in CY18). AFT is currently completing a 275-patient pivotal study for Maxigesic IV (filing expected in CY17) and recently completed a 200-patient study for Maxigesic Oral Liquid. A 275-patient pivotal study of Maxiclear PE is expected to complete this calendar year as well. NasoSURF is now in distribution and human factor studies with pharmacokinetic and clinical studies are expected to begin in FY18.

Valuation: NZ\$461m or NZ\$4.75 per share

We are adjusting our valuation from NZ\$461m or NZ\$4.76 per share to NZ\$461m or NZ\$4.75 per share. We have reduced our FY18 and FY19 revenue projections by NZ\$1.4m and NZ\$2.0m, respectively, but the effect of this reduction is offset by advancing our NPVs to the most recent period. We expect to update our valuation following additional information regarding the status of Maxigesic launches as well as results of clinical trials.

Making progress

AFT Pharmaceuticals is a specialty pharmaceutical company with over 130 prescription, over the counter and hospital products across an array of indications. In recent years, it has been involved in the international launch of a series of products outside of its home territory in New Zealand. It has successfully built a commercial infrastructure in Australia where the market for its products continues to grow. It is currently in the early stages of a launch across South-East Asia, and has recently signed multiple out-licensing partners across Europe and the Middle East. The company's lead product is Maxigesic, a co-formulation of acetaminophen and ibuprofen at a specific ratio (3.3 to 1) that has been clinically proven to increase potency. AFT is using Maxigesic as its flagship product for international expansion and it currently accounts for the majority of overseas revenue.

Australian revenue growth a highlight of FY17 results

AFT recently reported operating revenue of NZ\$69.2m for FY17, ending on 31 March 2017. This marks an 8.1% increase over FY16. The loss for the period was NZ\$18.3m, compared to an FY16 loss of NZ\$13.3m.

Exhibit 1: FY17 results by segment				
NZ\$000s	Revenues (2017)	Revenues (2016)	Loss before tax (2017)	Loss before tax (2016)
Australia	37,064	31,224	(3,663)	(3,233)
New Zealand	29,168	31,135	(5,782)	(4,902)
Asia	1,005	648	(689)	(1,015)
Rest of World	1,968	1,007	(8,226)	(4,159)
Total	69,205	64,014	(18,330)	(13,309)

Source: AFT Pharmaceuticals

The Australian segment reported particularly strong results, thanks to Maxigesic revenues more than doubling (due to less stringent scheduling for Maxigesic as well as the announcement that products containing codeine would no longer be available without a prescription) and the launch of Crystaderm and Restoranail. The outlook for Maxigesic in Australia remains strong, as market research conducted by the company suggests that 40-47% of current consumers who buy 750 million OTC codeine analgesics each year in Australia would switch to another OTC analgesic rather than get a doctor's prescription, which they will be forced to do as of 1 February 2018.

Maxigesic momentum

Maxigesic is now sold and launched in a total of eight countries – Australia, New Zealand, Brunei, Italy, Serbia, Singapore, United Arab Emirates and the United Kingdom – with total tablet sales more than tripling from 22m to 74m. In total there are licence agreements in 112 countries. AFT is targeting one-third of these areas to have launches in FY18, one-quarter in FY19, another one-quarter in FY20 and the rest in FY21. If AFT executes on this plan successfully, Maxigesic could be available in over 40 countries by the end of the fiscal year, including much of Europe. The major rate-limiting step will be the ability of the company to successfully traverse the registration applications in all of these different countries in a timeline manner.

Exhibit 2: Current and upcoming Maxigesic launches outside Australia/New Zealand

Country	Status
Spain	Launch pending
Portugal	Launch pending
UK	Launched, sales ahead of expectations
Belgium	Launch pending
Luxembourg	Launch pending
France	Launch pending
Nordics	Launch pending
Eastern Europe & Balkans	Launch pending
Serbia	Launched
Italy	Launched, sales increased sixfold
Kuwait & Iraq	Launch pending
United Arab Emirates	Launched, sales tripled
Singapore/Brunei	Launched, reason for 55% growth in South-East Asia Revenue
Malaysia	Launch pending

Source: AFT Pharmaceuticals

New Zealand still a work in progress

New Zealand continues to be a bit of a problem area, falling 6.3% in FY17. Approximately half of the decline (~NZ\$1m) was due to ongoing issues with Metoprolol, which AFT had been sole supplier of for the New Zealand market. As a reminder, Metoprolol is a beta blocker used to treat angina, high blood pressure and heart failure. Since November 2015, there has been an ongoing global shortage of the active ingredient, metoprolol succinate, due to a manufacturing issue. The New Zealand government pharmaceutical buying agency, PHARMAC, and AFT have agreed that AFT will no longer supply Metoprolol to the New Zealand market from approximately mid-FY18 onwards as PHARMAC has enlisted other sources. We believe the total additional downside from this lost contract will be between NZ\$1m and NZ\$2m.

The other half of the New Zealand decline was due to weakness in the Pharmacy channel, especially in the first half of the year. The reason for the weakness is difficult to discern but may be due to a mild cold/flu season in the winter months and then a disappointing allergy season due to wet weather in the spring.

Spending driven by increased investment

The company reported R&D expenses increased 38.7% to NZ\$11.2m as the company has ramped up its development programmes. AFT is currently completing a 275-patient pivotal study for Maxigesic IV (filing expected in CY17) and recently completed a 200-patient study for Maxigesic Oral Liquid. A 275-patient pivotal study of Maxiclear PE is expected to complete this calendar year as well.

NasoSURF completed Class I Medical Device registration in the US and is now in distribution and human factor studies with pharmacokinetic and clinical studies (including a 300-patient trial in its first indication) expected to begin in FY18. AFT is also preparing to file an IND with the FDA this year.

Selling and distribution expenses increased 32.2% to NZ\$26.0m, thanks primarily to the launch of OTC products in Australia and Singapore as well as the cost of advertising of Maxigesic following its rescheduling on 1 July 2016 in Australia.

Valuation

We are adjusting our valuation from NZ\$461m or NZ\$4.76 per share to NZ\$461m or NZ\$4.75 per share. We have reduced our FY18 and FY19 revenue projections by NZ\$1.4m and NZ\$2.0m, respectively, (mainly due lower expectations in the New Zealand market) but the effect of this reduction is offset by advancing our NPVs to the most recent period. We have also eliminated the tax liability for 2019 and part of 2020 due to carried forward tax losses. We expect to update our valuation following additional information regarding the status of Maxigesic launches as well as results of clinical trials.

Exhibit 3: DCF sensitivity table (NZ\$/share)

Terminal Revenue Growth	Terminal EBIT Margin				
	15%	25%	34%	38%	42%
-2%	2.36	3.05	3.67	3.95	4.23
-1%	2.43	3.19	3.87	4.17	4.47
0%	2.53	3.36	4.10	4.44	4.77
1%	2.64	3.56	4.39	4.76	5.13
2%	2.78	3.82	4.75	5.16	5.58
3%	2.96	4.14	5.21	5.68	6.16
4%	3.20	4.58	5.82	6.38	6.93
5%	3.54	5.19	6.68	7.34	8.01

Source: Edison Investment Research

Financials

AFT reported NZ\$16.0m in cash as of 31 March 2017, down from NZ\$28.1m a year ago. It raised NZ\$9.1m in March 2017 with the issue of redeemable preference shares to two major shareholders. The company is currently in the midst of a share purchase plan being offered to a broader group of eligible shareholders, which is looking to raise up to NZ\$1.25m. The offer opened on 24 May 2017 and closes on 12 June 2017.

We expect that AFT will have sufficient capital to reach profitability, which it guides to the FY18/19 timeframe (we are currently expecting a break-even FY18 and a profitable FY19). It is important to note that our estimates for profitability are heavily dependent upon growth in the Maxigesic franchise, especially in the ROW segment. Whether or not AFT is able to meet or beat these estimates will depend on whether the company is able to execute on the estimated 30-40 launches it is targeting in FY18.

Exhibit 4: Financial summary

	NZ\$000	2015	2016	2017	2018e	2019e
March		NZ GAAP	NZ GAAP	NZ GAAP	NZ GAAP	NZ GAAP
PROFIT & LOSS						
Revenue		56,241	64,014	69,205	97,731	124,214
Cost of Sales		(35,083)	(40,435)	(43,207)	(49,383)	(56,779)
Gross Profit		21,158	23,579	25,998	48,348	67,435
EBITDA		(9,659)	(7,821)	(15,125)	1,260	16,519
Operating Profit (before amort. and except.)		(9,530)	(7,667)	(14,982)	1,403	16,662
Intangible Amortisation		99	114	183	183	183
Exceptionals		0	0	0	0	0
Other		(546)	(618)	2,245	2,357	2,475
Operating Profit		(9,977)	(8,171)	(12,554)	3,943	19,320
Net Interest		(1,908)	(3,145)	(3,531)	(2,000)	(2,000)
Profit Before Tax (norm)		(11,438)	(10,812)	(18,513)	(597)	14,662
Profit Before Tax (reported)		(11,885)	(11,316)	(16,085)	1,943	17,320
Tax		282	42	(58)	0	0
Profit After Tax (norm)		(11,156)	(10,770)	(18,571)	(597)	14,662
Profit After Tax (reported)		(11,603)	(11,274)	(16,143)	1,943	17,320
Average Number of Shares Outstanding (m)		1.2	96.8	97.1	97.1	97.1
EPS - normalised (NZ\$)		(9.46)	(0.11)	(0.19)	(0.01)	0.15
EPS - normalised fully diluted (c)		(945.74)	(11.12)	(19.12)	(0.61)	15.10
EPS - (reported) (NZ\$)		(9.84)	(0.12)	(0.17)	0.02	0.18
Dividend per share (c)		0.00	0.00	0.00	0.00	0.00
Gross Margin (%)		37.6	36.8	37.6	49.5	54.3
EBITDA Margin (%)		N/A	N/A	N/A	1.3	13.3
Operating Margin (before GW and except.) (%)		N/A	N/A	N/A	1.4	13.4
BALANCE SHEET						
Fixed Assets		2,488	3,249	4,171	5,516	6,915
Intangible Assets		1,669	2,111	2,548	3,698	4,848
Tangible Assets		411	407	386	581	830
Investments		408	731	1,237	1,237	1,237
Current Assets		30,725	62,055	54,060	54,171	69,515
Stocks		14,686	17,686	18,718	21,494	24,713
Debtors		11,251	16,288	19,362	19,795	22,759
Cash		4,700	28,055	15,980	12,882	22,043
Other		88	26	0	0	0
Current Liabilities		(10,148)	(13,511)	(15,019)	(16,623)	(18,521)
Creditors		(10,148)	(13,511)	(15,019)	(16,623)	(18,521)
Short term borrowings		0	0	0	0	0
Long Term Liabilities		(20,739)	(23,161)	(23,426)	(23,426)	(23,426)
Long term borrowings		(20,739)	(23,161)	(23,426)	(23,426)	(23,426)
Other long term liabilities		0	0	0	0	0
Net Assets		2,326	28,632	19,786	19,638	34,483
CASH FLOW						
Operating Cash Flow		(11,479)	(11,326)	(15,473)	763	13,342
Net Interest		(1,908)	(3,145)	(3,531)	(2,000)	(2,000)
Tax		282	42	(58)	0	0
Capex		(483)	(694)	(1,598)	(1,671)	(1,724)
Acquisitions/disposals		0	0	0	0	0
Financing		12,859	38,357	9,042	0	0
Dividends		(763)	(1,652)	0	0	0
Net Cash Flow		(1,492)	21,582	(11,618)	(2,908)	9,617
Opening net debt/(cash)		11,889	16,039	(4,894)	7,446	10,544
HP finance leases initiated		0	0	0	0	0
Other		(2,658)	(649)	(722)	(190)	(456)
Closing net debt/(cash)		16,039	(4,894)	7,446	10,544	1,383

Source: Edison Investment Research

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