

PDL BioPharma

Financial update

Q318 results

PDL reported Q318 revenues of \$67.9m, up 8.2% compared to Q317 and up 45.8% sequentially, with that growth mainly due to an increase in the fair value of the Assertio (formerly Depomed) royalty rights. Noden Product revenue of \$17.8m was up 17.9% compared to Q317 but was down 31.2% sequentially, mainly due to the bulk purchasing by distribution partner Orphan Pacific for the Japanese market launch in Q218. Importantly, PDL recently announced a \$100m stock repurchase program which at current prices would buy back approximately 25% of the common shares outstanding.

Year end	Revenue (\$m)	PBT* (\$m)	EPS* (\$)	DPS (\$)	P/E (x)	Yield (%)
12/16	244.3	175.5	0.78	0.10	3.6	3.5
12/17	320.1	200.3	0.81	0.00	3.5	N/A
12/18e	189.4	66.1	0.46	0.00	6.2	N/A
12/19e	126.9	34.9	0.21	0.00	13.5	N/A

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

Cost cutting at Noden improves profitability

In August, PDL announced that Noden would discontinue its 60+ person contract salesforce and instead contract with Archer Healthcare to focus on email, direct mail and telesales. As a result, Noden reduced sales and marketing expenses by \$1.6m in Q318, while net income increased to \$4.1m, up from \$1.1m in Q317.

Continuing to look for acquisitions

The company is continuing to look for additional product acquisitions with a focus on commercial assets but also stated that it is looking at products that are still in development. The latter would represent a big change in strategy as the company has avoided such products and the large R&D expenditures that go with them. In our view, this move is unlikely as the company has historically been conservative in its acquisitions and price conscious even when it has liked an asset.

\$100m stock repurchase program

In September, PDL announced a \$100m share repurchase program, a course of action that has been promoted by certain investors. At current prices the program would enable PDL to repurchase around 25% of the common shares outstanding. Since March 2017, the company has bought back \$55m worth of shares via share repurchase programs.

Valuation: \$786m or \$5.39 per share

We have adjusted our valuation from \$783m or \$5.39 per basic share to \$786m or \$5.39 per share. The increase in the total valuation is mainly due to a higher level of net cash, mitigated by slightly lower valuations for Noden and AcelRx. The value per share is unchanged due to a slightly higher number of shares.

Pharma & biotech

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Price **US\$2.84**
Market cap **US\$414m**

Net cash (\$m) at 30 September 2018	251.0
Shares in issue	146.0m
Free float	90.6%
Code	PDLI
Primary exchange	NASDAQ
Secondary exchange	N/A

Share price performance



Business description

PDL BioPharma is reinventing itself as a healthcare-focused finance company through a three-pronged strategy: investing in royalty streams; providing high-yield financing to life science companies with near-term product launches; and specialty pharmaceutical sales through Noden Pharma.

Next events

China Rasilez launch	H119
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Earnings

PDL reported Q318 revenues of \$67.9m, up 8.2% compared to Q317 and up 45.8% sequentially. The growth in revenues was mainly due to an increase in the fair value of the Assertio (formerly Depomed) royalty rights following PDL's purchase of Assertio's remaining interest in those assets for \$20m. Revenue associated with royalty rights totalled \$42.2m during the quarter with \$17.5m due to Assertio cash royalties and \$31.6m due to a change in fair value of the Assertio royalty rights. The company also lowered its fair value estimates for AcelRx by \$9.2m during the quarter to \$68.3m due to lower expectations for that royalty stream.

Noden Product revenue of \$17.8m was up 17.9% compared to Q317, but down 31.2% versus Q218. The sequential decline was mainly due to a \$6.8m drop in Asian sales as the bulk purchasing by distribution partner Orphan Pacific for the Japanese market launch in Q218 subsided. As a reminder, Lee's Pharmaceutical Holdings, which has licensed the rights to Tekturna/Rasilez in China, Hong Kong, Macau and Taiwan, is expected to launch in China in H119. Our current forecasts do not include any revenues for Tekturna/Rasilez in China, so any meaningful sales there could provide additional upside.

The company previously announced the decision to eliminate its 60+ person contract salesforce, and instead has contracted Archer Healthcare to focus on email, direct mail and telesales. As the contract salesforce had made little headway in reversing the exponential decline in prescriptions, the impact on prescriptions has been minimal but profitability has improved. The change took effect in August and in Q318 the company saved \$1.8m in sales and marketing expenses. Net income for the Noden subsidiary increased to \$4.1m during the quarter, up from \$1.1m in Q317.

Additionally, LENSAR generated revenues of \$6.6m in Q318, up 12% compared to Q218 with seven systems sold during the quarter. Profitability also improved with a quarterly loss of \$0.9m versus \$1.9m last quarter.

CEO retiring

The company announced that John McLaughlin, the CEO since December 2008, intends to retire at the end of 2018. He will be replaced by Dominique Monnet, PDL's president, who has been with the company since September 2017. Mr Monnet was previously senior vice president and chief marketing officer at Alexion Pharmaceuticals, a now \$28 billion company and prior to that he was at Amgen for 10 years where he held various commercial positions. It is unclear if the new CEO will lead to a change in strategy although at the results the company stated that it intends to look at potentially acquiring development stage assets, which is a change as PDL has previously focused on commercial stage assets. However, on the Q318 conference call, Mr Monnet reiterated that the company "will advance very cautiously in this area."

Valuation

We have adjusted our valuation from \$783m or \$5.39 per basic share to \$786m or \$5.39 per share. The higher total valuation was mainly due to a higher level of net cash but was mitigated by slightly lower valuations for Noden and AcelRx. The value per share is unchanged as a slightly higher number of shares offsets the total valuation increase.

Exhibit 1: PDL valuation

Royalty/Note	Type	Expiration year	PDL balance sheet carrying value (\$m)	NPV (\$m)
Queen et al	Royalty	2015	N/A	N/A
Assertio (formerly Depomed)	Royalty on Glumetza and other products	2024	\$265.7	\$281.8
VB	Royalty on Spine Implant	Undisclosed	\$13.9	\$16.5
University of Michigan	Royalty on Cerdelga	2022	\$27.5	\$14.4
Wellstat	Note (Impaired)	Unknown	\$50.2	\$50.2
Hyperion	Note (Impaired)	Unknown	\$1.2	\$1.2
Lensar	Equity		N/A	\$53.1
Acelrx	Royalty on Zalviso	2027	\$68.3	\$73.4
Careview	Note	2022	\$19.4	\$20.5
Noden	Equity	N/A	\$40.1	\$23.5
Kybella	Royalty	Unknown	\$2.9	\$0.9
Total				\$535
Net cash (Q318) (\$m)				\$251.0
Total firm value (\$m)				\$786
Total basic shares (m)				146.0
Value per basic share (\$)				\$5.39
Total options				0.0
Total number of shares (m)				146.0
Diluted value per share (\$)				\$5.39

Source: Edison Investment Research, company reports

Financials

We have increased our estimated FY18 revenues to \$189.4m from \$176.1m, but decreased our estimated FY19 revenues to \$126.9m from \$145.5m. The increase in FY18 revenue estimates was due to the increase in the fair value of the Assertio royalties, partially offset by a lower than expected run rate for Noden. The decrease in FY19 revenues is due to our more conservative revenue forecasts for Noden. We have decreased our SG&A estimates to \$69.6m from \$74.0m for FY18, and to \$72.4m from \$76.9m for FY19, mainly due to cost cutting at Noden. The company ended the quarter with \$401.0m in cash (\$251.0m in net cash).

Exhibit 2: Financial summary

	\$000s	2016	2017	2018e	2019e
Year end 31 December		US GAAP	US GAAP	US GAAP	US GAAP
PROFIT & LOSS					
Revenue		244,301	320,060	189,361	126,862
Cost of Sales		(4,065)	(30,537)	(45,163)	(19,742)
Gross Profit		240,236	289,523	144,198	107,120
General & Administrative		(43,287)	(63,324)	(69,614)	(72,399)
EBITDA		193,129	218,818	71,757	31,894
Operating Profit (before amort. and except.)		193,129	218,818	71,757	31,894
Intangible Amortisation		(12,028)	(24,689)	(15,831)	(15,831)
Other		0	0	0	0
Exceptionals		(51,699)	(349)	(129,897)	0
Operating Profit		129,402	193,780	(73,971)	16,063
Net Interest		(17,679)	(18,562)	(5,676)	2,972
Other		(2,353)	9,309	0	0
Profit Before Tax (norm)		175,450	200,256	66,081	34,866
Profit Before Tax (FRS 3)		109,370	184,527	(79,647)	19,035
Tax		(45,711)	(73,826)	1,490	(3,997)
Deferred tax		(0)	(0)	(0)	(0)
Profit After Tax (norm)		129,739	126,430	67,571	30,868
Profit After Tax (FRS 3)		63,659	110,701	(78,157)	15,037
Minority interest		(53)	(47)	0	0
Profit After Tax less Minority Interest (FRS 3)		63,606	110,654	(78,157)	15,037
Average Number of Shares Outstanding (m)		163.8	155.4	146.5	149.5
EPS - normalised (\$)		0.78	0.81	0.46	0.21
EPS - FRS 3 (\$)		0.39	0.71	(0.53)	0.10
Dividend per share (c)		10.03	0.00	0.00	0.00
Gross Margin (%)		98.3	90.5	76.1	84.4
EBITDA Margin (%)		79.1	68.4	37.9	25.1
Operating Margin (before GW and except.) (%)		79.1	68.4	37.9	25.1
BALANCE SHEET					
Fixed Assets		818,949	611,827	448,927	342,571
Intangible Assets		228,542	215,823	51,318	51,318
Tangible Assets		1,631	16,369	12,430	14,348
Royalty rights		402,318	349,223	348,525	250,938
Other		186,458	30,412	36,654	25,968
Current Assets		395,147	631,296	540,657	641,099
Stocks		0	0	0	0
Debtors		40,120	31,183	15,437	15,437
Cash		147,154	527,266	446,407	546,849
Other		207,873	72,847	78,813	78,813
Current Liabilities		(130,315)	(193,109)	(46,672)	(46,672)
Creditors		(7,016)	(19,785)	(9,011)	(9,011)
Short term borrowings		0	(126,066)	0	0
Other		(123,299)	(47,258)	(37,661)	(37,661)
Long Term Liabilities		(329,649)	(204,124)	(200,202)	(200,202)
Long term borrowings		(232,443)	(117,415)	(124,614)	(124,614)
Other long term liabilities		(97,206)	(86,709)	(75,588)	(75,588)
Net Assets		754,132	845,890	742,710	736,797
Minority Interests		0	0	0	0
Shareholder equity		754,132	845,890	742,710	736,797
CASH FLOW					
Operating Cash Flow		101,718	40,624	(9,700)	(5,187)
Net Interest		0	0	0	0
Tax		0	0	0	0
Capex		(109,963)	(1,297)	(5,367)	(1,269)
Acquisitions/disposals		13,082	128,415	76,581	102,410
Financing		0	0	0	0
Dividends		(16,583)	(222)	0	0
Other		(47,629)	212,592	(15,926)	4,488
Net Cash Flow		(59,375)	380,112	45,588	100,442
Opening net debt/(cash)		38,918	85,289	(283,785)	(321,793)
HP finance leases initiated		0	0	0	0
Exchange rate movements		0	0	0	0
Other		13,004	(11,038)	(7,580)	(0)
Closing net debt/(cash)		85,289	(283,785)	(321,793)	(422,235)

Source: PDL BioPharma accounts, Edison Investment Research

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