



## Pharmaceuticals &amp; Biotechnology



Source: Refinitiv

## Market data

EPIC/TKR	ARIX
Price (p)	163
12m High (p)	165
12m Low (p)	59
Shares (m)	135.6
Mkt Cap (£m)	220.3
NAV/share (p)	247
Premium/discount to NAV	-34%
Free Float	71%
Market	Main

## Description

ARIX is a publicly listed biotechnology venture capital company. It provides an opportunity for all investors to participate in a balanced portfolio of diverse biotech innovation via a single stock. With a global portfolio of 16 companies and five IPOs achieved since launch in 2016, Arix is a dynamic and modern approach to life sciences venture capital investing.

## Company information

Exec. Chairman	Naseem Amin
MD	Jonathan Tobin
MD	Christian Schetter
COO	Robert Lyne
Finance Director	Marcus Karia

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[www.arixbioscience.com](http://www.arixbioscience.com)

## Key shareholders

Directors	0.1%
Link Fund Solutions	19.8%
Fosun	8.2%
Ruffer	6.1%
Takeda Ventures	5.5%

## Diary

Nov'20	Listed companies' 3Q'20 results
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## ARIX BIOSCIENCE

## Hitting the jackpot

Arix Bioscience (ARIX) is a listed global venture capital (VC) company that presents an opportunity for institutional and retail investors to participate in the high risk-return profile of early-stage biotech investing. ARIX minimises risk through a combination of an expert investment team and portfolio diversification. Along with its 2020 interim results, management provided the market with some aspirational targets for the next three years, which would see the NAV double to ca.£500m. News that Merck & Co is to acquire portfolio company, VelosBio, for \$2.75bn cash, giving ARIX >12x return on its investment, will help to smash these targets.

- **Strategy:** ARIX sources investments from an established network and a strong scientific reputation. The portfolio is diversified by therapeutic area, treatment modality, stage of discovery/development and geography to balance the risk-reward profile. Value is realised when ARIX successfully exits its investments.
- **Acquisition of VelosBio:** Major pharmaceutical company, Merck & Co (MRK), has announced the acquisition VelosBio for \$2.75bn cash, to boost its position in oncology and provide it with another breakthrough technology in this field. The transaction, subject to approval under the Hart-Scott-Rodino Antitrust Improvements Act, is expected to close by the end of 2020.
- **Return on investment:** VelosBio was introduced to ARIX by its strategic partner, Takeda Ventures. ARIX co-led the company's Series A funding round in 2018, committing \$11m/£8.6m, and made a further investment of \$4.0m/£3.2m in VelosBio's Series B in July 2020. ARIX is expecting to receive \$185m/£142m for its stake, representing a 12.3x return.
- **Market reaction:** Although the market responded favourably to this news, with the shares rising 55%, this equates to an increase in market capitalisation of only £74m compared with the £121m valuation uplift from the VelosBio consideration, and has expanded the discount to NAV from 31% to 34%. This suggests that the shares have much further to go.
- **Investment summary:** The principal reason that ARIX has been trading on a discount to its NAV has been the "lack of a track record". Management tried to allay the market's concern with its interim results when it highlighted the portfolio's IRR of 20% since inception and set itself some ambitious targets for the next three years. The trade sale of VelosBio means that these targets should be easily met and the market should be giving far more credit to the company.

## Financial summary and valuation

Year-end Dec (£m)	2017	2018	2019	2020E	2021E	2022E
Change in FV of investments	5.5	51.2	-58.6	*136.7	-	-
Other income	1.9	1.3	0.5	0.2	0.2	0.0
Administrative expenses	-11.0	-11.7	-9.7	-7.0	-5.5	-5.6
Operating profit/(loss)	-7.2	37.5	-70.6	130.5	-7.2	-7.6
Profit/(loss) before tax	-7.7	38.2	-69.9	130.7	-6.9	-7.3
Underlying EPS (p)	-9.5	27.2	-49.9	88.9	-4.7	-5.0
Net cash/(debt)	74.9	91.2	53.7	32.1	167.8	156.0
Capital increase	105.1	83.5	0.0	0.0	0.0	0.0
NAV/share (p)	152.3	200.4	149.1	246.7	-	-

\*Based on share prices and forex at close of business on 5 November 2020

Source: Hardman &amp; Co Life Sciences Research

# Merck & Co to buy VelosBio

## Cash offer for portfolio company

Merck & Co (MRK.N) has announced that it has entered into a definitive agreement to acquire the outstanding share capital of VelosBio, a private company in ARIX's investment portfolio, for \$2.75bn in cash. This will be the first trade exit for a company in ARIX's portfolio, valuing its stake at ca.\$185m/£142m, which represents a >12x return on its \$15m/£12m investment, validating its investment strategy and capability.

ARIX investment in VelosBio					
Date	Round	Amount invested		Cumulative investment	
		\$m	£m	\$m	£m
Oct'18	Series A – tranche 1	6.5	5.1	6.5	5.1
Jan'20	Series A – tranche 2	4.5	3.5	11.0	8.6
Jly'20	Series B	4.0	3.2	15.0	11.8
<b>Total</b>		<b>15.0</b>	<b>11.8</b>		
MRK bid		185.0	142.0		
<b>Return</b>			<b>12.3x</b>		

Source: Hardman & Co Life Sciences Research

## VelosBio

VelosBio is a clinical-stage biopharmaceutical company committed to developing first-in-class cancer therapies targeting receptor tyrosine kinase-like orphan receptor 1 (ROR1) for the treatment of patients with haematologic malignancies and solid tumours. VelosBio's lead drug candidate is VLS-101, an antibody-drug conjugate (ADC), which is currently in a Phase I trial in patients with refractory haematological tumours. This trial is expected to report data by the end of the year.

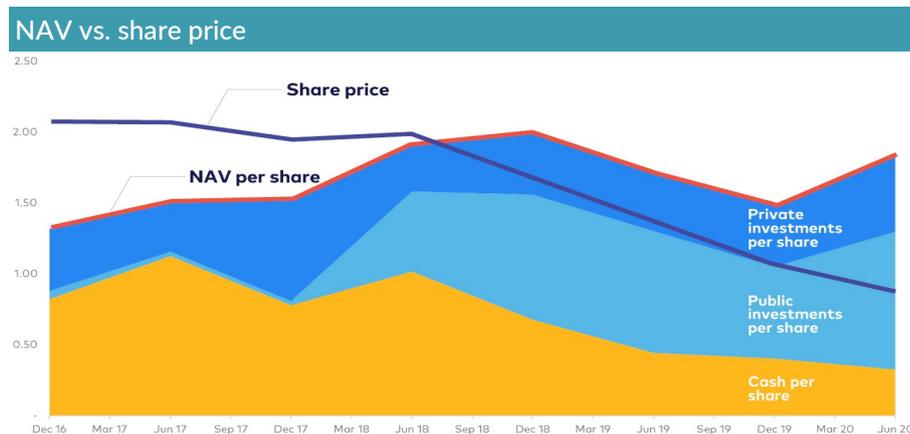
In October 2020, VelosBio announced the initiation of a Phase II clinical trial (NCT04504916) to evaluate VLS-101 in the treatment of patients with solid tumours, including patients with triple-negative breast cancer (TNBC), hormone receptor-positive and/or HER2-positive breast cancer, and non-squamous non-small-cell lung cancer (NSCLC).

MRK is a major player in oncology, particularly some of the breakthrough technologies aimed at improving patient outcomes. It believes that the addition of VelosBio with its ADC technology will strengthen its position.

VelosBio was sourced through ARIX's strategic partnership with Takeda Ventures and the two companies co-invested in 2018. In October 2018, ARIX led a Series A funding round with an investment of \$6.5m/£5.1m in the first tranche and a commitment to make a further investment of \$4.5m/£3.5m in the second tranche, which completed in January 2020. This was followed in July 2020 with a \$137m Series B round, which received support from a top-tier syndicate of investors as a significant valuation uplift compared with the Series A round. The proposed takeover of VelosBio by MRK is providing all these investors with a substantial, and quick, return. The deal is expected to close around the end of 2020.

## Generating a track record

In September 2020, ARIX reported strong interim results showing a 24% increase in NAV to £251.0m. However, this highlighted the enormous valuation disconnect between the NAV and its market capitalisation.<sup>1</sup>



The key reason for the discount was considered to be the “lack of a track record”. The new management team attempted to allay these fears by highlighting that, since inception, ARIX had deployed £149m (currently increased to £155m) into its portfolio, realised £13m through opportunistic divestments, and generated an IRR of 20% (realised and unrealised). Moreover, with a number of upcoming clinical events, the company set an aspirational target to make an annual IRR of 15%-25%, and to generate an NAV of £500m by the end of 2023. The market responded very positively to this by marking up its shares by about 35%.

Subsequent to this, there has been some volatility in the share prices of the listed companies in its portfolio, such that the NAV at the closing prices on 4 November was estimated to be £212m. Despite the share price uplift following its interim results, ARIX was still trading at a 31% to this updated NAV.

The proposed purchase of VelosBio by MRK completely removes the key reason for ARIX’s discount. Unsurprisingly, the market responded positively to this news, with the share price rising 55%. But is this enough? ARIX will be receiving ca.£142m for its stake in VelosBio when the deal closes in about two months’ time, which represents a £121m (89p per share) valuation uplift in NAV, yet the increase in its market capitalisation was only £74m. Consequently, the discount has actually increased from 31% to 34%. As an aside, the cash coming from MRK equates to 92% of investments made by ARIX into all of its portfolio companies.

### Impact of VelosBio returns

Current NAV* (Hardman & Co estimate)	£212m
ARIX market capitalisation*	£146m
Discount at close on 4 November	31%
Investments into portfolio companies since inception	£155m
NAV of investment into VelosBio	-£12m
Return from VelosBio investment	£142m
Revised NAV	£334m
ARIX market capitalisation at close on 5 November	£220m
Updated discount	34%

\*Share prices and forex taken at close of business on 4 November 2020

Source: Hardman & Co Life Sciences Research

<sup>1</sup> <https://www.hardmanandco.com/research/corporate-research/realising-the-valuation-disconnect/>

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