

InnoCare Pharma (9969 HK)

Breakup with Biogen on orelabrutinib for the treatment of autoimmune diseases

- **Biogen terminated partnership with InnoCare.** On 15 Feb, Biogen terminated the collaboration with InnoCare on orelabrutinib for the treatment of multiple sclerosis (MS) and other autoimmune diseases. The two parties started the collaboration in Jul 2021, and since then, InnoCare has received US\$125mn upfront payment, and was eligible to receive up to US\$812.5mn milestone payment and future sales royalties according to the original agreement. However, due to the current termination, future payment will not happen, while InnoCare doesn't need to return the upfront payment.
- **Ph2 MS trial of orelabrutinib partially on hold by US FDA due to liver toxic problem, while no real liver injury observed as per management.** Last Dec, the US FDA placed the Ph2 trial (NCT04711148) of orelabrutinib in R/R MS partially on hold based on drug-induced liver injury cases observed. However, before the pause, the majority (80+%) of enrolled patients had completed at least 70 days of treatment and could continue the study. According to InnoCare management, there were no actual liver injuries, but only a very limited number of liver transaminase increases. The increases were transitory, only happened during the first two months of treatment, and were revisable. Compared to the MS trial of Sanofi's evobrutinib - ~26% patients had raised liver enzymes and 11% discontinued the study, the liver toxic problem of orelabrutinib seems minimal.
- **InnoCare targets to continue the MS study.** An interim analysis (12 weeks of treatment) of the ongoing Ph2 MS trial was performed, while the results were not released. The trial was mainly led by InnoCare from start. InnoCare has amended and submitted the revised protocol to the US FDA in January. Monitoring frequency and enrolment inclusion criteria would be the major protocol revisions. InnoCare plans to release the data of the MS trial in 2Q23E (24 weeks of treatment), and if positive, to initiate a Ph3 trial. In the future, InnoCare still expects to collaborate with a global partner.
- **Concern remains regarding the liver toxic problems of orelabrutinib in treating MS.** There are concerns that Biogen could have made its decisions based on the results of the first interim analysis of the ongoing MS trial, which were not released and only accessible to a few people from Biogen/InnoCare. However, orelabrutinib, as a successful oncology therapy widely used for the treatment of CLL and MCL, doesn't have liver toxic effects based on treating thousands of patients with hematologic malignancies. We look forward to the data readout of the Ph2 MS trial in 2Q23E.
- **Maintain BUY.** Orelabrutinib is also under assessment for the treatment of other autoimmune diseases, including SLE, ITP, and NMOSD. Particularly, based on positive PoC data on SLE, a potentially registrational Ph2b study of SLE has been started. We are still interested in orelabrutinib's potential for autoimmune disease, besides its success in oncology. InnoCare has a sufficient RMB7.7bn net cash as of Sep 2022. We revised our TP from HK\$20.14 to HK\$10.84 (WACC: 10.11%, terminal growth rate: 3.0%).

Earnings Summary

(YE 31 Dec)	FY20A	FY21A	FY22E	FY23E	FY24E
Revenue (RMB mn)	1	1,043	598	941	1,509
Net profit (RMB mn)	(391)	(65)	(907)	(581)	(354)
EPS (Reported) (RMB)	(0.40)	(0.05)	(0.51)	(0.33)	(0.20)
R&D expenses (RMB mn)	(403)	(722)	(570)	(600)	(600)
Admin expenses (RMB mn)	(89)	(140)	(179)	(254)	(362)
CAPEX (RMB mn)	(251)	(166)	(400)	(200)	(100)

Source: Company data, Bloomberg, CMBIGM estimates

BUY (Maintain)

Target Price HK\$10.84
 (Previous TP) HK\$20.14
Up/Downside 22.5%
Current Price HK\$8.85

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Stock Data

Mkt Cap (HK\$ mn)	15,614.2
Avg 3 mths t/o (HK\$ mn)	13.1
52w High/Low (HK\$)	15.50/7.49
Total Issued Shares (mn)	1,764.3

Source: FactSet

Shareholding Structure

Hillhouse Capital	11.8%
King Bridge Investments	9.2%

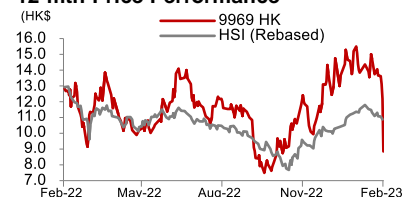
Source: Company data

Share Performance

	Absolute	Relative
1-mth	-42.9%	-40.8%
3-mth	-28.6%	-37.9%
6-mth	-26.3%	-30.3%

Source: FactSet

12-mth Price Performance



Source: FactSet

Figure 1: Risk-adjusted DCF valuation

DCF Valuation (in RMB mn)	2022E	2023E	2024E	2025E	2026E	2027E	2028E	2029E	2030E	2031E	2032E	2033E	2034E	2035E
EBIT	(1,037)	(711)	(473)	(335)	(495)	(184)	176	679	1,125	1,619	1,969	2,302	2,525	2,699
Tax rate	0%	0%	0%	0%	0%	0%	15%	15%	15%	15%	15%	15%	15%	15%
EBIT*(1-tax rate)	(1,037)	(711)	(473)	(335)	(495)	(184)	150	577	956	1,376	1,674	1,957	2,146	2,294
+ D&A	13	13	13	13	13	13	13	13	13	13	13	13	13	13
- Change in working capital	218	82	223	375	317	312	331	304	262	190	126	60	(90)	(131)
- Capex	(400)	(200)	(100)	(100)	(100)	(100)	(100)	(100)	(100)	(100)	(100)	(100)	(100)	(100)
FCFF	(1,206)	(815)	(337)	(47)	(265)	42	394	794	1,131	1,479	1,713	1,930	1,970	2,076
Terminal value														30,090
FCF + Terminal value	(1,206)	(815)	(337)	(47)	(265)	42	394	794	1,131	1,479	1,713	1,930	1,970	32,166
Present value of enterprise (RMB mn)	9,536													
Net Debt	-6,767													
Minorities	44													
Equity value (RMB mn)	16,259													
Corporate value (HK\$ mn)	19,128													
# of shares outstanding (mn)	1,764													
TP per share (HK\$)	10.84													
Terminal growth rate	3.00%													
WACC	10.11%													
Cost of Equity	12.8%													
Cost of Debt	4.50%													
Equity Beta	0.90													
Risk Free Rate	2.00%													
Market Risk Premium	12.00%													
Target Debt to Asset ratio	30.00%													
Effective Corporate Tax Rate	15.00%													

Source: CMBIGM estimates

Figure 2: Sensitivity analysis (HK\$)

		WACC				
		9.11%	9.61%	10.11%	10.61%	11.11%
Terminal growth rate	4.00%	14.20	12.86	11.75	10.83	10.04
	3.50%	13.42	12.25	11.26	10.43	9.72
	3.00%	12.77	11.73	10.84	10.09	9.43
	2.50%	12.22	11.28	10.48	9.78	9.18
	2.00%	11.75	10.89	10.15	9.52	8.96

Source: CMBIGM estimates

Figure 3: CMBIGM estimates revision

RMB mn	New			Old			Diff (%)		
	FY22E	FY23E	FY24E	FY22E	FY23E	FY24E	FY22E	FY23E	FY24E
Revenue	598	941	1,509	655	1,416	2,065	-9%	-34%	-27%
Gross Profit	449	744	1,199	530	1,161	1,714	-15%	-36%	-30%
Operating Profit	(855)	(587)	(361)	(946)	(168)	281	NA	NA	NA
Net profit	(916)	(590)	(364)	(965)	(172)	235	NA	NA	NA
EPS (RMB)	(0.51)	(0.33)	(0.20)	(0.54)	(0.09)	0.14	NA	NA	NA
Gross Margin	79.00%	79.00%	79.50%	82.00%	82.00%	83.00%	-3.00 ppt	-3.00 ppt	-3.50 ppt

Source: Company data, CMBIGM estimates

Figure 4: CMBIGM estimates vs consensus

RMB mn	CMBIGM			Consensus			Diff (%)		
	FY22E	FY23E	FY24E	FY22E	FY23E	FY24E	FY22E	FY23E	FY24E
Revenue	598	941	1,509	607	1,294	2,030	-1%	-27%	-26%
Gross Profit	449	744	1,199	496	1,119	1,736	-10%	-34%	-31%
Operating Profit	(855)	(587)	(361)	(817)	(445)	(100)	NA	NA	NA
Net profit	(916)	(590)	(364)	(795)	(338)	11	NA	NA	NA
EPS (RMB)	(0.51)	(0.33)	(0.20)	(0.47)	(0.23)	(0.05)	NA	NA	NA
Gross Margin	75.00%	79.00%	79.50%	81.72%	86.50%	85.51%	-6.72 ppt	-7.50 ppt	-6.01 ppt

Source: Company data, CMBIGM estimates

Financial Summary

INCOME STATEMENT	2019A	2020A	2021A	2022E	2023E	2024E
YE 31 Dec (RMB mn)						
Revenue	1	1	1,043	598	941	1,509
Cost of goods sold	0	0	(66)	(150)	(198)	(309)
Gross profit	1	1	977	449	744	1,199
Operating expenses	(440)	(594)	(1,212)	(1,481)	(1,494)	(1,713)
Selling expense	(3)	(68)	(298)	(422)	(640)	(951)
Admin expense	(64)	(89)	(140)	(179)	(254)	(362)
R&D expense	(213)	(403)	(722)	(570)	(600)	(600)
Others	(160)	(34)	(52)	(310)	0	200
Other income	104	271	218	177	164	153
Other expense	(2)	(1)	(3)	(4)	(4)	(4)
Gain/loss on financial assets at FVTPL	(1,814)	(69)	0	(30)	0	0
Share of (losses)/profits of associates/JV	0	0	(1)	(18)	0	0
Pre-tax profit	(2,150)	(392)	(20)	(916)	(590)	(364)
Income tax	0	0	(47)	0	0	0
After tax profit	(2,150)	(392)	(67)	(916)	(590)	(364)
Minority interest	9	0	2	10	10	10
Net profit	(2,141)	(391)	(65)	(906)	(580)	(354)

BALANCE SHEET	2019A	2020A	2021A	2022E	2023E	2024E
YE 31 Dec (RMB mn)						
Current assets	2,409	4,092	6,417	8,804	8,162	7,828
Cash & equivalents	2,292	3,970	5,929	6,541	5,845	5,417
Account receivables	0	0	45	15	26	45
Inventories	0	2	10	13	18	28
Financial assets at FVTPL	80	0	317	2,167	2,167	2,167
Other current assets	37	121	116	68	107	171
Non-current assets	207	445	980	1,350	1,537	1,624
PP&E	48	306	430	820	1,009	1,099
Right-of-use assets	86	97	136	134	132	130
Investment in JVs & assos	1	1	21	4	4	4
Intangibles	37	37	34	34	33	33
Goodwill	3	3	3	3	3	3
Other non-current assets	31	1	356	356	356	356
Total assets	2,616	4,538	7,398	10,153	9,699	9,452
Current liabilities	66	104	329	472	609	926
Short-term borrowings	0	0	0	0	0	0
Account payables	8	6	85	103	136	212
Other current liabilities	51	92	218	343	446	686
Lease liabilities	6	7	20	20	20	20
Contract liabilities	0	0	7	7	7	7
Non-current liabilities	5,498	1,273	1,409	2,149	2,149	1,949
Long-term borrowings	0	0	0	0	0	0
Convertible bonds	1,117	1,150	1,201	1,941	1,941	1,741
Deferred income	157	100	124	124	124	124
Other non-current liabilities	4,223	23	85	85	85	85
Total liabilities	5,563	1,377	1,739	2,622	2,758	2,875
Share capital	0	0	0	0	0	0
Other reserves	(3,005)	3,104	5,605	7,487	6,907	6,553
Total shareholders equity	(3,005)	3,104	5,605	7,487	6,907	6,553
Minority interest	57	56	54	44	34	24
Total equity and liabilities	2,616	4,538	7,398	10,153	9,699	9,452

CASH FLOW	2019A	2020A	2021A	2022E	2023E	2024E
YE 31 Dec (RMB mn)						
Operating						
Profit before taxation	(2,150)	(464)	(20)	(916)	(590)	(364)
Depreciation & amortization	1	2	10	10	10	10
Tax paid	0	0	0	0	0	0
Change in working capital	21	(57)	120	218	82	223
Others	2,048	346	57	238	(118)	(306)
Net cash from operations	(80)	(173)	167	(450)	(615)	(437)
Investing						
Capital expenditure	(75)	(251)	(166)	(400)	(200)	(100)
Net proceeds from disposal of short-term investments	19	(889)	(1,637)	(1,848)	0	0
Others	103	33	73	125	124	113
Net cash from investing	47	(1,107)	(1,730)	(2,124)	(76)	13
Financing						
Dividend paid	0	0	0	0	0	0
Net borrowings	(50)	(9)	0	0	0	0
Proceeds from share issues	422	2,253	2,562	3,189	0	0
Others	(9)	(6)	(17)	(4)	(4)	(4)
Net cash from financing	363	2,238	2,545	3,186	(4)	(4)
Net change in cash						
Cash at the beginning of the year	1,245	1,594	2,301	5,929	6,541	5,845
Exchange difference	18	(252)	(45)	0	0	0
Cash at the end of the year	1,594	2,301	5,929	6,541	5,845	5,417
GROWTH	2019A	2020A	2021A	2022E	2023E	2024E
YE 31 Dec						
Revenue	(22.9%)	9.4%	76,368.7%	(42.6%)	57.3%	60.3%
Gross profit	(22.9%)	9.4%	71,554.4%	(54.1%)	65.7%	61.3%
PROFITABILITY	2019A	2020A	2021A	2022E	2023E	2024E
YE 31 Dec						
Gross profit margin	100.0%	100.0%	93.7%	75.0%	79.0%	79.5%
Return on equity (ROE)	na	(788.3%)	(1.5%)	(13.8%)	(8.1%)	(5.3%)
GEARING/LIQUIDITY/ACTIVITIES	2019A	2020A	2021A	2022E	2023E	2024E
YE 31 Dec						
Current ratio (x)	36.7	39.2	19.5	18.6	13.4	8.5
Receivable turnover days	0.0	0.0	9.9	12.9	13.9	14.9
Inventory turnover days	0.0	0.0	32.8	32.8	32.8	32.8
Payable turnover days	0.0	0.0	250.5	250.5	250.5	250.5
VALUATION	2019A	2020A	2021A	2022E	2023E	2024E
YE 31 Dec						

Source: Company data, CMBIGM estimates. Note: The calculation of net cash includes financial assets.

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