Alder Biopharmaceuticals (ALDR)

SMALL & MID CAP RESEARCH

Bristol Returns Rights to Clazakizumab - Program's Future Unclear

Regaining rights to clazakizumab removes a source of potential near- and mid-term non-dilutive funding from milestones in the RA and PsA programs. The best case scenario, in our opinion, would be for ALDR to re-partner the clazakizumab program while continuing to focus internal resources on the migraine program. Any plans to move clazakizumab forward without a partner will require us to model new expenses. Changes to our model reflect accelerated recognition of amortized payments from Bristol and a reduction in milestone in 2015.

- **Lowering target to $19 from $20:** While we had relatively modest expectations for clazakizumab and a 40% probability of success, 70% of the value was tied to lucrative milestones from Bristol, including several pre-commercial milestones that we modeled at a much higher probability. Our new target includes $16 for migraine, $2 for clazakizumab, and $1 for NOLs. We ascribe a conservative 55% POS to ALD403 and first sales in 2019, and assume a new partner for clazakizumab in 2015 with a lower 25% POS.
- **Primary driver unchanged:** We continue to view the anti-CGRP drug class as an emerging multi-billion dollar market for migraines. ALDR is advancing both an IV and subcutaneous formulation of ALD403 into Phase IIb trials in H2:14 and H1:15 respectively, with the goal of developing quarterly IV and monthly subcutaneous treatment options.
- **Upcoming Clazakizumab Phase II data:** ALDR expects to report Phase IIb data in psoriatic arthritis by YE:14 and Phase IIb and results in rheumatoid arthritis in H1:15.

Rating	**OUTPERFORM* [V]**
Price (29 Aug 14, US$)	17.04
Target price (US$)	(from 20.00) 19.00[1]
52-week price range	20.34 - 9.91
Market cap. (US$ m)	524.89
Enterprise value (US$ m)	480.67

**Stock ratings are relative to the coverage universe in each analyst's or each team's respective sector.*
[1]Target price is for 12 months.
[V] = Stock considered volatile (see Disclosure Appendix).

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Financial and valuation metrics

Year	12/13A	12/14E	12/15E	12/16E
EPS (CS adj.) (US$)	-0.94	0.09	-2.10	-2.23
Prev. EPS (US$)	—	-1.61	-0.60	-1.85
P/E (x)	-18.1	191.7	-8.1	-7.6
P/E rel. (%)	-101.0	NM	-55.0	-57.4
Revenue (US$ m)	18.8	54.5	9.6	10.3
EBITDA (US$ m)	-19.8	3.4	-69.3	-87.1
OCFPS (US$)	-1.65	-1.58	-0.74	-2.12
P/OCF (x)	—	-10.8	-23.0	-8.1
EV/EBITDA (current)	-22.9	133.4	-6.6	-5.2
Net debt (US$ m)	-23	-44	-149	-65
ROIC (%)	37.60	32.92	210.17	266.90

Number of shares (m)	30.80	IC (current, US$ m)	-55.22
BV/share (Next Qtr., US$)	2.2	EV/IC (x)	56.6
Net debt (Next Qtr., US$ m)	-59.7	Dividend (current, US$)	—
Net debt/tot eq (Next Qtr., %)	-87.9	Dividend yield (%)	—

Source: Company data, Credit Suisse estimates

Bristol Deal was Lucrative for ALDR

Bristol Myers-Squibb was developing clazakizumab, an anti-IL6 antibody, for RA and psoriatic arthritis. Head-to-head Phase II data showed superiority of a clazakizumab-based regimen compared with a Humira regimen in RA, and Phase III trials were expected to start in 2015.

Under the terms of the deal, BMY covered all development costs (a key feature for ALDR), and ALDR was eligible to receive significant milestones ($746M pre-commercial and $500M in sales milestones) and double-digit royalties up to 20%. Importantly, there were $394M in pre-commercial milestones just for the RA program, which we had modeled at a high probability of being earned.

Valuation: $19 vs. Prior $20

Our new valuation includes $16 for ALD403 in migraine (up $1 on discounting calculation), $2 for Clazakizumab (down $2 on lower POS and smaller future deal terms), and $1 for NOLs. Our valuation assumes considerable dilution associated with funding the ongoing ALD403 program, with no additional spending on clazakizumab.

Our valuation includes 55% probability of success for ALD403 and 25% probability of success for clazakizumab. Our clazakizumab assumptions include a new partner in 2015 providing a modest upfront payment, milestones, development funding, and royalties. Our projected milestones and royalties are lower than for the Bristol collaboration and our probability of success is lower (25% vs. 40%), as the clinical success is now dependent on finding a new partner.

Exhibit 1: Sum of the Parts Valuation

Program	NPV ($M)	Sales ($M)	POS	Per share (current)	per share (future)
ALD403	$791	$1,057	55%	$24	$16
Clazakizumab	$80	$510	25%	$2	$2
NOLs (future)	$65			$2	$1
Total	**$935**			**$29**	**$19**

Source: Company data, Credit Suisse estimates

Exhibit 2: ALDR Pipeline

Drug	Target	Indication	Stage	Partner
ALD403	CGRP	Migraine	Phase II	Proprietary
Clazakizumab	IL-6	Rheumatoid Arthritis	Phase IIb	Proprietary
		Psoriatic Arthritis	Phase II	Proprietary
4 preclinical programs	TBA	TBA	Preclinical	Proprietary

Source: Company data, Credit Suisse estimates

Exhibit 3: ALDR News Flow

Product	Catalyst	Expected Date
ALD403	Start Phase IIb dose ranging study in chronic migraine patients	H2:14
New target	Select new clinical stage candidate	H2:14
Clazakizumab	Phase II data in psoriatic arthritis	YE-2014
Clazakizumab	Phase IIb dose exploration data in RA	H1:15
ALD403	Start Phase IIb dose ranging study in frequent episodic migraine patients	H1:15
ALD403	Phase IIb data	H2:15
New target	First clinical study start (one or more)	H2:15
Clazakizumab	Phase III start	2015
Clazakizumab	Phase III start	2015
ALD403	End of Phase II meeting with FDA	YE:15
ALD403	Start Phase III in migraine	2016

Source: Company data, Credit Suisse estimates.

Exhibit 4: ALDR Model

	2012A	2013A	Q1:14A	Q2:14A	Q3:14E	Q4:14E	2014E	2015E	2016E	2017E	2018E	2019E	2020E
Revenues													
US sales of ALD403												29.7	154.6
Ex-US royalies on ALD403													0.7
Royalties on Clazakizumab												1.4	3.1
Collaboration and license agreement	**20.1**	18.8	4.8	4.7	45.0		54.5	9.6	10.3	10.3	65.7	94.8	12.0
Total Revenues	**20.1**	**18.8**	**4.8**	**4.7**	**45.0**		**54.5**	**9.6**	**10.3**	**10.3**	**65.7**	**125.9**	**170.3**
Expenses													
Cost of goods												3.0	15.5
Research and development	**30.7**	31.9	7.0	9.4	10.0	12.0	38.4	58.5	74.0	90.0	92.0	87.0	77.0
Sales, general, administrative	**7.2**	7.7	3.2	2.7	3.5	4.0	13.4	21.0	24.0	24.0	26.0	35.0	40.0
Total Operating Expenses	**37.9**	**39.6**	**10.2**	**12.1**	**13.5**	**16.0**	**51.8**	**79.5**	**98.0**	**114.0**	**118.0**	**122.0**	**117.0**
Operating income (loss)	**(17.8)**	(20.8)	(5.4)	(7.4)	31.5	(16.0)	2.7	(69.9)	(87.7)	(103.7)	(52.3)	3.9	53.3
Total Other Income (Expense)	**0.0**	0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.2	0.2	0.2
Pre Tax Income	**(17.8)**	(20.6)	(5.4)	(7.4)	31.5	(16.0)	2.8	(69.9)	(87.7)	(103.7)	(52.1)	4.1	53.5
Income tax													
Net Income	**(17.8)**	**(20.6)**	**(5.4)**	**(7.4)**	**31.5**	**(16.0)**	**2.8**	**(69.9)**	**(87.7)**	**(103.7)**	**(52.1)**	**4.1**	**53.5**
EPS - basic (proforma)	**($3.55)**	($3.84)	($5.38)	($0.40)	$1.02	($0.51)	$0.13	($2.10)	($2.23)	($2.20)	($1.09)	$0.08	$1.09
EPS - diluted (proforma)	**($3.55)**	($3.84)	($5.38)	($0.40)	$0.95	($0.51)	$0.09	($2.10)	($2.23)	($2.20)	($1.09)	$0.08	$1.02
Shares outstanding - basic (proforma)	**5.01**	21.89	1.00	18.56	31.04	31.20	20.45	33.34	39.31	47.16	47.99	48.47	48.95
Shares outstanding - diluted (proforma)	**5.01**	21.89	1.00	18.56	33.24	31.20	30.93	33.34	39.31	47.16	50.97	51.60	52.24

Source: Company data, Credit Suisse estimates

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Companies Mentioned *(Price as of 29-Aug-2014)*

Alder Biopharmaceuticals (ALDR.OQ, $17.04, OUTPERFORM[V], TP $19.0)

Disclosure Appendix

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3-Year Price and Rating History for Alder Biopharmaceuticals (ALDR.OQ)

ALDR.OQ	Closing Price	Target Price	
Date	(US$)	(US$)	Rating
02-Jun-14	12.26	20.00	O *

** Asterisk signifies initiation or assumption of coverage.*

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Price Target: (12 months) for Alder Biopharmaceuticals (ALDR.OQ)

Method: Our rounded $19 target includes $16 for ALD-403, $2 for Clazakizumab, and $1 for its NOLs. Our $19 valuation is justified by a fully-taxed, probability weighted, product level DCF for each of the two clinical stage programs plus the value of future NOLs. We assume an ex-US partner for ALD403 and significant dilution from future equity raises prior to profitability. For our DCF analysis, we use a 12% discount rate and 35% tax rate.

Risk: Risks to our $19 TP include: 1) unexpected negative result for proprietary or partnered clinical program, 2) financing risk from expected future equity raises, 3) unexpected strong clinical result(s) from the competition in the migraine and RA settings, and 4) significant delay in one or more clinical programs that pushes potential approval timeline(s) out.

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