



Stock Research | 03 May 2010

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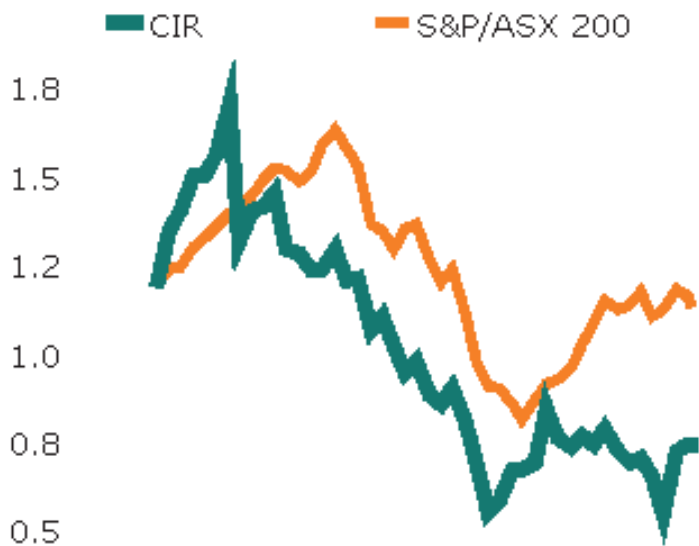
## Circadian Technologies Limited CIR

03 May 2010 | Encouraging results in animal studies

Recommendation: **Speculative Buy**



Note: marker indicates price of \$0.75 at publication date. Price date based on previous close.



\$ Price	6/06(a)	6/07(a)	6/08(a)	6/09(a)
NPAT	-6.5	-16.5	-1.1	-9.9
EPS	-16.1	-40.8	-2.9	-22.2
EPS % Chg	-129.7	--	--	--
DPS	0.0	0.0	0.0	0.0
Franking %	--	--	--	--
Div yield %	0.0	0.0	0.0	0.0
P/E	0.0	0.0	0.0	0.0

### Investment Rating

CIR is now focused on the development of VEGF-based therapies for the treatment of cancers and other diseases. Licensing deals already in place

Fair Value (\$)	<b>2.20</b>
Morningstar Style Box	
Moat Rating	None
Business Risk	--
Mkt Cap (\$m)	\$33.00
Previous Close	<b>\$0.74</b>
52 Wk \$ High/Low	\$0.88 / \$0.53
ROE (2009/06)	-25.6
Net Interest Cover	5.28%
Ex-Dividend	04 Feb 2005
Payable	24 Feb 2005
Company Beta	0.70
Sector Beta	0.71

provide a degree of validation of the technology. At present the share price recognises negligible value for CIR's intellectual property. The biotech sector is inherently speculative and CIR's share price highly volatile. The stock has the potential to generate strong returns but can remain depressed for long periods while risk aversion remains high. Investors should only direct small proportions of their portfolios to the stock and then only if comfortable with high risk and share price volatility.

## Result Description

- CIR recently completed studies in mice that demonstrated significant synergistic effects between its candidate VGX-100 and Avastin and the chemotherapy agent docetaxel in prostate and brain cancers and a similar effect to Avastin in pancreatic cancer. CIR is hopeful these and toxicology studies in animals later this year will pave the way for human trials in 2011.

## Impact

- CIR holds cash of around \$33m and legacy investments in Antisense Therapeutics and Optiscan worth roughly \$4m. This compares with a market capitalisation of only \$34m at the time of writing.
- CIR has over 500 granted and pending patents worldwide pertaining to the VEGF family of proteins that promote blood and lymphatic vessel development which in turn are involved in cancer tumour growth and spread.

## Recommendation Impact (Last Updated: 03 May 2010)

While unarguably speculative, CIR's cash and extensive IP position relative to its market capitalisation suggest an attractive risk/return ratio for investors experienced in the multiple pitfalls that can accompany R&D investment.

## Event Analysis

CIR is Australia's oldest listed biotech company. Around two years ago it changed its primary character from investment fund to developer of its own intellectual property in the area of biological cancer therapy. CIR holds cash of around \$33m and legacy investments in Antisense Therapeutics and Optiscan worth roughly \$4m. This compares with a market capitalisation of only \$34m at the time of writing. CIR has over 500 granted and pending patents worldwide pertaining to the VEGF family of proteins that promote blood and lymphatic vessel development which in turn are involved in cancer tumour growth and spread. VEGF stands for Vascular Endothelial Growth Factor. While unarguably speculative, CIR's cash and extensive IP position relative to its market capitalisation suggest an attractive risk/return ratio for investors experienced in the multiple pitfalls that can accompany R&D investment.

Antibody drug technology is relatively new and a number of antibody drugs are multi-billion dollar revenue generators. The best known of these is Avastin. The drug enjoys annual sales of around US\$6bn even though a significant proportion of treated patients derive little or no benefit from the drug. Only 30%-50% of patients respond to the drug of which 25%-50% become resistant within 12-18 months. Avastin is an anti-angiogenic. Drugs in this class inhibit the formation of tumour blood supply. A major shortcoming is that Avastin does not appear to impact the metastatic process (cancer spread).

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CIR's technology is similar to Avastin in that it blocks growth of blood supply in tumours, but it does so by blocking different growth promoting proteins. It also appears to retard cancer spread, a function, which if proven, would represent a significant benefit over Avastin. If CIR successfully develops an antibody cancer treatment it is unlikely to displace but rather be used in combination with Avastin and other drugs. Combination therapies are used to combat the disease's pernicious ability to rapidly combat a particular drug's mode of attack. Like Avastin the technology also has potential to be used in therapies to treat eye disease.

CIR is working on three drug candidates internally and has out-licensed a candidate to ImClone, now wholly owned by Eli Lilly. In addition CIR is partnering with Healthscope to develop a diagnostic for Cancers of Unknown Primaries (CUP), scheduled for launch later in 2010. We estimate this

will generate \$2-3m in royalties to CIR 3-4 years after launch.

While CIR's development work is yet to reach human clinical trials, there have been a number of potentially very valuable deals done in the antibody therapy space at similarly early stages of development. CIR will not attempt to develop its first candidate beyond Phase 1. It will prefer to leverage the drug-trial, regulatory expertise and marketing clout of a much larger partner. We consider a partnering deal in the next 12-18 months that leads to roughly a trebling of CIR's current market capitalisation quite likely. Such a deal hopefully will generate the funds and technology credibility that enable CIR to develop one of its other candidates to a more advanced and therefore value generating level.

With its current cash reserves and potential to begin earning revenue in 2011 from its collaboration with Healthscope and from possible partnering deals over the next 18 months we do not anticipate significant dilution of existing shareholders.

We stress though the dangers of R&D. There is the real possibility of CIR's research failing to generate significant medical and therefore shareholder value. Another market meltdown could also retard progress by for example impacting the development or commercial strategy of a large partner. At best a good measure of patience is likely to be required to enjoy significant fruits from a position in the stock.

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