Pacific Edge

RESEARCH INSIGHTS#

1H20 Result and Capital Raise

Pacific Edge (PEB) announced a fully underwritten NZ$20m capital raise alongside its 1H20 result, as it continues to work towards commercial milestones in the US market to drive a step-change for the business. Post raise, this provides ~20 months cash on hand using 1H20 cash burn rates, with upside risk given cash burn has historically been seasonally higher in 1H, and should test receipts continue to grow.

What's changed?

- **Our forecasts for FY20E and beyond have not been updated following the 1H20 result and capital raise announcement.**

1H20 result — strong growth in NZ, costs controlled, US modest

PEB reported 1H20 operating revenue of NZ$2.3m, up +12%, with a modest increase in operating costs lifting the net loss to -NZ$9.4m (from -NZ$8.7m).

- **US:** 1H20 revenue of NZ$2m, up +8%. PEB is cash accounting its US segment, with material potential revenue not being reported through the accounts (for example ~47% of current US tests are for customers of public health insurer, CMS. Until commercial sign-off is achieved, PEB is not recognising any revenue despite being 'billable' tests).
- **Rest of World:** Revenue of NZ$0.3m (up +54% from NZ$0.2m), primarily underpinned by strong momentum in the small NZ market following an array of recent success with coverage and inclusion within the standard of care. Lab throughput is up +50% to 1,896 tests (including NZ, Australia and Singapore) given momentum in NZ and User Programmes in Singapore.

Aside from updated financials, there was little new insight on commercial milestones in the result.

Capital raise — lifting cash balance to NZ$24.7m

PEB announced a fully underwritten NZ$20m capital raise, via an initial placement and subsequent 1 for 4.25 pro-rata renounceable rights offer.

- **Placement:** NZ$7m at NZ$0.15/share on 21 November 2019.
- **Rights offer:** 1 for 4.25 rights offer, to raise NZ$13.1m at NZ$0.10/share. This is a 34% discount to the theoretical ex-rights placement adjusted price of NZ$0.152. Record date is 29 November; settlement 18 December 2019.

PEB reported a net cash position of NZ$4.7m at 30 September 2019, lifting to NZ$24.7m post capital raise (~20 months of cash at 1H20 burn rates).

Near-term milestones PEB has called out

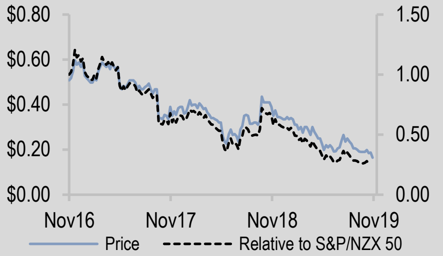
- **Additional peer reviewed papers:** Due 2H20 "supporting clinical utility"
- **Coverage decision from public health insurer, CMS:** PEB has submitted a dossier of evidence for review and is expecting to know the outcome in 1Q21 (based on expert opinion). 19,361 tests have been provided to CMS customers since inception (up +19% on FY19). When/if a coverage decision is achieved, tests to date may be partially reimbursed. The price for CMS was set at US$760/test (effective 1 January 2019).

Investment View

The success of PEB will be determined by the commercial success of Cxbladder in the US. Investors continue to require patience, with the large US market challenging to secure reimbursement, albeit the prize is large.

NZX Code	PEB
Share price	NZ$0.17
Issued shares	467.1m
Market cap	NZ$77.1m
Average daily turnover	187.0k (NZ$45k)

Share Price Performance



Financials: March	19A	20E	21E	22E
NPAT* (NZ$m)	-17.9	-14.2	-8.2	-0.5
EPS* (NZc)	-3.7	-2.8	-1.6	-0.1
EPS growth* (%)	20.3	25.0	42.4	93.6
DPS (NZc)	0.0	0.0	0.0	0.0
Imputation (%)	0	0	0	0

Valuation (x)	19A	20E	21E	22E
EV/EBITDA	n/a	n/a	n/a	n/a
EV/EBIT	n/a	n/a	n/a	n/a
PE	n/a	n/a	n/a	n/a
Price / NTA	5.8	n/a	n/a	n/a
Cash dividend yield (%)	0.0	0.0	0.0	0.0
Gross dividend yield (%)	0.0	0.0	0.0	0.0

* Our forecasts for FY20E and beyond have not been updated following the 1H20 result and capital raise announcement

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FORSYTH BARR IS A LEAD MANAGER AND AN UNDERWRITER OF THE CAPITAL RAISING AND WILL RECEIVE FEES IN CONNECTION WITH THOSE ROLE.S

#Forsyth Barr **RESEARCH INSIGHTS** targets selected smaller cap stocks or those under transitional coverage and focuses on qualitative rather than quantitative assessments. We do not provide investment ratings or target prices on these stocks.

Pacific Edge (PEB)	Priced as at 21 Nov 2019: NZ$0.17	March year end

Research Insights

Forsyth Barr Research Insights focuses on qualitative rather than quantitative assessments of an equity investment.
We do not provide valuation, target prices or investment ratings for companies in the Research Insights series. It is targeted at selected smaller cap stocks with typically higher risk attributes, or those under transitional coverage.
Our earnings and cashflow forecasts, together with key valuation and ratios provided on this page should assist investors in determining the relative valuation merits of the company.

Profit and Loss Account (NZ$m)	2018A	2019A	2020E	2021E	2022E
Sales revenue	4.6	4.8	7.8	18.6	34.1
Normalised EBITDA	**(19.7)**	**(18.0)**	**(14.2)**	**(7.9)**	**(0.2)**
Depreciation and amortisation	(0.3)	(0.2)	(0.2)	(0.2)	(0.2)
Normalised EBIT	**(20.0)**	**(18.2)**	**(14.4)**	**(8.1)**	**(0.4)**
Net interest	0.2	0.3	0.1	(0.1)	(0.2)
Associate income	-	-	-	-	-
Tax	-	(0.0)	-	-	0.1
Minority interests	-	-	-	-	-
Normalised NPAT	**(19.8)**	**(17.9)**	**(14.2)**	**(8.2)**	**(0.5)**
Abnormals/other	0.0	(0.0)	-	-	-
Reported NPAT	**(19.7)**	**(17.9)**	**(14.2)**	**(8.2)**	**(0.5)**
Normalised EPS (cps)	(4.7)	(3.7)	(2.8)	(1.6)	(0.1)
DPS (cps)	-	-	-	-	-

Growth Rates	2018A	2019A	2020E	2021E	2022E
Revenue (%)	7.6	3.6	62.4	>100	83.4
EBITDA (%)	n/a	n/a	n/a	n/a	n/a
EBIT (%)	n/a	n/a	n/a	n/a	n/a
Normalised NPAT (%)	n/a	n/a	n/a	n/a	n/a
Normalised EPS (%)	n/a	n/a	n/a	n/a	n/a
DPS (%)	n/a	n/a	n/a	n/a	n/a

Cash Flow (NZ$m)	2018A	2019A	2020E	2021E	2022E
EBITDA	**(19.7)**	**(18.0)**	**(14.2)**	**(7.9)**	**(0.2)**
Working capital change	1.5	-	1.2	0.6	(1.3)
Interest & tax paid	0.1	0.4	0.1	(0.1)	(0.2)
Other	(0.1)	0.2	-	-	0.1
Operating cash flow	**(18.1)**	**(17.5)**	**(12.8)**	**(7.5)**	**(1.6)**
Capital expenditure	0.3	0.2	0.2	0.2	0.2
(Acquisitions)/divestments	-	-	-	-	-
Other	-	-	-	-	-
Funding available/(required)	**(17.8)**	**(17.4)**	**(12.6)**	**(7.3)**	**(1.4)**
Dividends paid	-	-	-	-	-
Equity raised/(returned)	21.3	14.6	-	-	-
Increase/(decrease) in net debt	**(3.6)**	**2.8**	**12.6**	**7.3**	**1.4**

Balance Sheet (NZ$m)	2018A	2019A	2020E	2021E	2022E
Working capital	(1.1)	(0.5)	(1.7)	(2.2)	(1.0)
Fixed assets	0.9	0.8	0.8	0.8	0.8
Intangibles	0.3	0.2	0.2	0.2	0.2
Other assets	0.5	0.6	0.6	0.6	0.6
Total funds employed	**0.5**	**1.1**	**(0.1)**	**(0.6)**	**0.6**
Net debt/(cash)	(16.2)	(12.8)	0.2	7.8	9.6
Other non current liabilities	0.1	0.1	0.1	0.1	0.1
Shareholder's funds	16.6	13.9	(0.3)	(8.5)	(9.0)
Minority interests	-	-	-	-	-
Total funding sources	**0.5**	**1.1**	**(0.1)**	**(0.6)**	**0.6**

Valuation Ratios	2018A	2019A	2020E	2021E	2022E
EV/EBITDA (x)	n/a	n/a	n/a	n/a	n/a
EV/EBIT (x)	n/a	n/a	n/a	n/a	n/a
PE (x)	n/a	n/a	n/a	n/a	n/a
Price/NTA (x)	4.4	6.0	n/a	n/a	n/a
Free cash flow yield (%)	-22.4	-21.9	-15.9	-9.1	-1.8
Net dividend yield (%)	0.0	0.0	0.0	0.0	0.0
Gross dividend yield (%)	0.0	0.0	0.0	0.0	0.0
Imputation (%)	0	0	0	0	0
Pay-out ratio (%)	0	0	0	0	0

Capital Structure	2018A	2019A	2020E	2021E	2022E
Interest cover EBIT (x)	86.6	56.4	>100x	n/a	n/a
Interest cover EBITDA (x)	85.3	55.8	>100x	n/a	n/a
Net debt/ND+E (%)	-4,080.9	-1,208.6	-95.7	-1,087.6	1,761.1
Net debt/EBITDA (x)	0.8	0.7	n/a	n/a	n/a

Key Ratios	2018A	2019A	2020E	2021E	2022E
Return on assets (%)	-101.7	-110.1	-87.7	-45.0	-2.0
Return on equity (%)	-118.8	-128.8	4,535.6	96.3	5.8
Return on funds employed (%)	0.0	0.0	0.0	0.0	0.0
EBITDA margin (%)	-424.4	-375.2	-181.5	-42.7	-0.7
EBIT margin (%)	-430.9	-379.3	-184.0	-43.7	-1.2
Capex to sales (%)	-7.2	-3.2	-2.4	-1.0	-0.6
Capex to depreciation (%)	-201	-131	-168	-168	-168

Key assumptions	2018A	2019A	2020E	2021E	2022E
NZDUSD cross rate	0.71	0.68	0.66	0.66	0.66
US market assumptions (US$)					
Test - average sale price	n/a	n/a	950	900	900
Cost of test	n/a	n/a	100	100	100
Gross profit of test	n/a	n/a	850	800	800
Gross margin (%)	n/a	n/a	89.5	88.9	88.9
Revenue breakdown (NZ$m)					
Cxbladder sales	3.4	3.8	7.3	18.1	33.6
Other	1.2	1.0	0.5	0.5	0.5
Total revenue	**4.6**	**4.8**	**7.8**	**18.6**	**34.1**
Total billable tests	11,866	12,744	18,522	40,046	63,872

Potential market size - bladder cancer ('000 pa)	US	Australasia
Est number of urologists	10,000	300
New patients who present with haematuria	1,000.0	50.0
New incidences of bladder cancer	74.7	3.0
Diagnosed with bladder cancer		
Year 1 (4 tests)	298.8	12.0
Year 2 (2 tests)	149.4	6.0
Year 3 (2 tests)	149.4	6.0
Year 4 (2 tests)	149.4	6.0
Year 5 (2 tests)	149.4	6.0
Total tests recommended	896.3	36.0
Total potential market	**1,896.3**	**86.0**

* Forsyth Barr target prices reflect valuation rolled forward at cost of equity less the next 12-months dividend

Our forecasts for FY20E and beyond have not been updated following the 1H20 result and capital raise announcement.

Investment summary

Pacific Edge (PEB) is a cancer diagnostics company in the early stages of commercialising its first product, Cxbladder. Investors continue to require patience, with the large US market challenging to secure reimbursement. Changing established clinical processes takes time, however, the prize is large. PEB is a speculative risk stock, reliant on converting key groups to commercial customers, with timing highly unpredictable.

Key drivers

- **Market awareness in the US:** PEB's primary focus is on the US market, given the large potential opportunity and global credibility gained through acceptance. The market is sizeable, indicative test prices highly attractive, albeit commercialisation is challenging and slow given a highly complex reimbursement landscape.
- **Lab throughput:** Shows evidence of growing market awareness, albeit off a low base. It includes both commercial and User Programme tests. Billable test numbers also continue to show positive momentum.

Other key company and industry issues

- **South East Asia:** PEB is in the early stages of looking into the market, supported by a grant. At this stage we have not yet included the opportunity in our forecasts.

Upcoming catalysts/events

- **CMS reimbursement (public health insurer, Centre for Medicare and Medicaid Services):** Getting Cxbladder approved for reimbursement will be a key milestone.
- **Kaiser Permanente — signing a commercial contract:** The results from its User Programme were strong, providing another credibility tick and leg of support for clinical adoption. The timeframe for investors for Kaiser to become a commercial customer is still unknown and out of PEB's control.

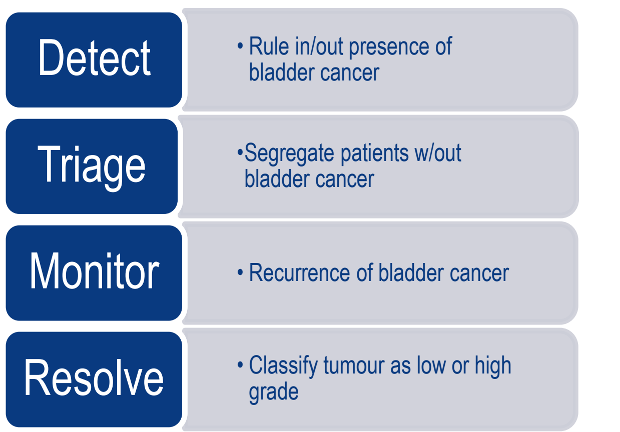
Key risks

- **Long adoption curve:** Gaining acceptance and reimbursement from the medical community is critical to success but takes time.
- **New test / competing product:** Or a shift away from molecular diagnostics.

Company description

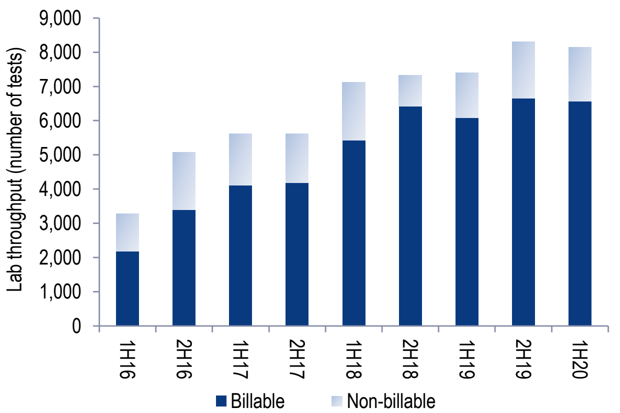
Pacific Edge is a cancer diagnostics company in the early stages of commercialisation of its first product, Cxbladder, after 10 years of research into genetic markers. Cxbladder is a suite of non-invasive urine tests to detect the presence of bladder cancer in patients presenting with haematuria. PEB has four Cxbladder products in the market: Detect, Triage, Monitor and Resolve.

Figure 1. Cxbladder products and timing



Source: Company reports, Forsyth Barr analysis

Figure 2. Lab throughput (includes commercial & User Programmes)



Source: Company reports, Forsyth Barr analysis

Figure 3. Substantial Shareholders

Shareholder	Latest Holding
Harbour Asset Management	16.5%
Salt Funds Management	12.0%
AMP Capital Investors NZ	5.5%

Source: NZX, Forsyth Barr analysis, NOTE: based on SSH notices only

Figure 4. International Compcos

Company	Code	Price	Mkt Cap	PE		EV/EBITDA		EV/EBIT		Cash D/Yld
(metrics re-weighted to reflect PEB's balance date - March)			(m)	2020E	2021E	2020E	2021E	2020E	2021E	2021E
Pacific Edge	**PEB NZ**	**NZ$0.17**	**NZ$77**	**<0x**	**<0x**	**<0x**	**<0x**	**<0x**	**<0x**	**0.0%**
Exact Sciences Corp	EXAS US	US$82.77	US$12,186	<0x	<0x	<0x	<0x	<0x	<0x	n/a
Cancer Genetics Inc	CGIX US	US$6.58	US$14	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Genomic Health Inc	GHDX US	US$63.44	US$2,385	38.2x	33.9x	21.4x	17.9x	33.3x	n/a	n/a
Myriad Genetics Inc	MYGN US	US$24.96	US$1,857	>50x	20.5x	18.9x	15.1x	>75x	16.9x	n/a
			Compco Average:	**38.2x**	**27.2x**	**20.1x**	**16.5x**	**33.3x**	**16.9x**	**n/a**
EV = Current Market Cap + Actual Net Debt			**PEB Relative:**	**n/a**	**n/a**	**n/a**	**n/a**	**n/a**	**n/a**	**n/a**

Source: *Forsyth Barr analysis, Bloomberg Consensus, Compco metrics re-weighted to reflect headline (PEB) companies fiscal year end

Figure 5. Consensus EPS Momentum

n/a

Source: Forsyth Barr analysis

Figure 6. 12 Month Forward PE

n/a

Source: Forsyth Barr analysis