

Evotec AG
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Presenters:

Dr Werner Lanthaler (Chief Executive Officer), Dr Klaus Maleck (Chief Financial Officer)

Werner Lanthaler: Good morning, this is Evotec speaking. Welcome to our conference call for our Q1 Results. I hope you have received a presentation which was posted on our webcast and I would like to discuss with you and guide you through the presentation, but also then, of course, answer all your questions. I'm here together with my team especially Klaus Maleck, who will then answer the financial questions.

When a company wants to grow, a company first has to earn the right to grow. That was our message we gave to you about a year ago when we initiated the Action Plan 2012. We wanted to earn the right to grow in order to become a Champions League player in the drug discovery business and I think with the first quarter we delivered for the first time a clear sign that we have earned this right to grow and that we are ready for growth.

With this I would like to guide you to page number 3 of the presentation, but just before we go into too many scientific and too many development promises, just look at the numbers. The numbers tell you that growing a business by close to 20%, with 19.5% without achieving any milestone in the first quarter, which was also not planned by the way, we think that we have not only defined the right game for Evotec but also that we show we are playing the right game.

Even more important when you enter a game is that you know the right performance indicators and here I think it is most important to stress that our close to 20% growth is not sacrificing anything on gross margin. On the contrary we are growing by close to 20% and have a slightly better gross margin. There are not too many businesses that I know that grow close to 20% without sacrificing gross margin. That's very, very important and that will be a key indicator for us also going forward because that is clearly telling you that we are only positioning ourselves into the highly, highly scientifically driven discovery space where it's not about the gross margin in itself but where it comes to clearly superior scientific work.

The other thing I would like to stress here is that for the first time you can see the results of our Action Plan 2012 when it comes to capital efficiency. Many companies promise you a certain percent decrease in SG&A. We have delivered it and all of you who have ever done a cost exercise like this know that this is not going without any pain but I'm very happy to tell you that we have organised our processes very smoothly and are very happy with this SG&A reduction at this stage.

When it comes to our R&D spending we have focused our R&D spending to high value programmes. Yes, you see an enormous reduction here but no, we have not taken out any upside value at this stage that we don't believe in and you will also see that we will catch up in spending, especially in our 100 family and 400 series in the quarters to come so that we will also keep our close to €10 million spending on R&D for the full year.

Our operating result is improving by 93% which is a very nice number where we are for the first time seeing a quarter where we basically had a steady business running

and where without the milestones we come close to the zero line and we expect this to improve significantly in the next quarters because as I already said there was no milestone included in the first quarter.

If you are in the game you have to always find the best team to play together with and I think it is absolutely essential for us that we have assembled a team of alliance partners that is not only making us very comfortable to grow further but which is underlying the quality of our work in the best possible alliances - I don't want to go too deep at this stage but I think it is a great success for the company to have secured an alliance with CHDI for the next years to come, that we have entered into a multi-year strategic alliance with Genentech and that you have also seen other alliances that were formed and that you will see significantly more alliances that will be formed.

When it comes to our development programme I think here it was all about value optimal positioning of our development programme and I think by putting our 100 series into an alliance with Roche, we have now set up where the 100 series can optimally generate value and I'm very comfortable that we will start our Phase II study very soon in the second quarter of this year and then have one of the highest value programmes running but I also want to stress that this is of course a risky programme that we have in our pipeline where all costs are taken by Roche and where the full upside of this programme will go into Evotec. We also have done I think a very optimal step with earlier programmes in our pipelines, for example with our H3 programme in funding debt externally.

We did not this time bring our sales order book into this presentation and I apologise for this but I think it is fair to say that our sales order book is at its strongest stage ever at this time and we have said last time by the end of March it was close to €30 million. It's way beyond €30 million now and I think it would be fair to assume that the sales order book as I said is the strongest ever that we had in the company.

One step back. We have clearly defined and you will see that from page number 7 to exercise our activities in a core business fashion in the drug discovery space. Here we see by defining our drug discovery alliances in the outsourcing space a significantly growing and also significantly moving space. Many of you have seen that for example one of the largest players in the field WuXi Pharma has gone together with Charles River. You have also seen that this discovery space is moving by consolidating one player to the other, but most important is that the sector is growing significantly. Of course it's always easier to grow when the full sector is growing and when you are then the quality leader in the sector and that's especially what we are representing. We are the quality leader in the sector that brings really not only innovation but also best leveraged platform technologies into our alliances.

When you look at page number 8 I think here on a conceptual note you see that what we try to achieve is to bring core disease biology leveraged with our platform technologies into core disease areas where we build alliances with our partners and we build these alliances along the value chains where we are experts in. So we are not excluding of going with our partners into clinical stage as we for example do it with Roche in our CNS lines, but our main focus is really to bring targets to the stage of R&D and here our value promise is to be not only more efficient but also to be better qualified for many targets. That's the value promise enabling us to form new alliances and retaining existing ones.

Let me give you a few examples on that and let me start with Genentech and let me at this stage apologise because it's not our style as you know to send out press

releases that don't give too much material information as we had to do it recently. At the same time it fits our alliance partner's desire and wish, then that's the law for us and therefore we understand that sometimes people want to know more and we apologise that we cannot send out the full details. What I would like to say is we have announced at the beginning of the year that we want to make one or even two or even more strategic alliances. This one would be large enough to cover two. Nevertheless we will make another one and probably also more. It is not only proof that the best are going together with the best because Genentech clearly is the leader in many, many fields and we are clearly the leader in many of the platform technologies. It also is the proof that not every discovery programme is done at cheap scientific standards in China. It is the proof that there is a superior value paid for superior scientific and innovation alliances. I also would like to say this is a Genentech alliance so this is not an extension of our Roche alliance because there was a bit of misunderstanding on this one. It's an alliance which is multi-years and by multi-years we understand everything which is significantly more than two. We also would like to say that this is an alliance in US dollars which is helpful these days and we would also like to say that we have the intention to grow this alliance significantly over the next years. We have defined this alliance in a disease expertise where Evotec has always been positioned as a clear leader and as you know we are clear leaders when it comes to CNS, pain and oncology fields but especially when it comes to CNS and pain.

Let me highlight also our Roche alliance and I think we have now the situation that all things have been cleared with the FDA, that we are ready to define all protocols and that we will start this Phase II trial shortly, certainly in the second quarter. More details on the trial design will be available following the start of the study. All I can say, this is a trial which is leading to a product and that is the important point that we always want to make here. This is not a quick and dirty biotech trial. This is really leading to a product and that's what Roche and we intend to lead here. You of course also know that this is a high value option when it comes to the results of this trial by triggering a \$65 million going forward up to \$300 million in milestones and significant double digit royalties on treatment resistance depression.

On Huntington's disease we have one type of alliance where I think it is just the optimal situation for a partner that does not wish to build up fixed costs but works with us by basically taking the best of science in a variable cost fashion and I think here we are very happy that the Huntington's Disease Foundation (CHDI) is working very closely together with us to fight this important disease and it's just one kind of alliance where I think it's a very, very good starting point to actually treat Huntington's disease in the future and that's the value promise that we want to bring together forward with our partner.

When it comes to funding opportunities we take all opportunities that we can get only for programmes that we really like, for example the H3 receptor antagonists. That's also something where now through the funding of the BMBF (German Federal Ministry of Research and Technology) we are in a much better position to bring this programme to an optimal value point in the clinic and therefore we are very thankful to the German government that they are supporting this.

If you put this all into a portfolio as you see on page number 13 it just shows you that we are in the process and have already built a very strong portfolio of the best partners thereby significantly reducing our downside risk because we don't work without getting full funding and gross margin on what we do and on top of that we get significant upsides if programmes progress. We have just outlined here and wanted

to show you how this is then included in our top line guidance, where you basically should appreciate that we only give top line guidance on very, very, very secure business where you see that either this business is already reflected in our product sales order book or where we only put into our guidance very certain milestones that we are aware of at this stage. What we don't want to withhold is that there are many targets and many programmes in the company and in our alliances that could lead to additional milestones and additional royalties from products to come. That's also the huge biotech upside which is built into our business model and that makes us so comfortable in not only putting the best platform out there but also putting a very, very good business model out there.

I also want to stress at this point that there are still many unpartnered projects in the company, which are fully funded by us because there's a very strong rationale to believe in them and to create either own alliances or own developments with these programmes going forward, just to mention here EVT 401, P2X₃, H3, ASiCs, B1 and others.

When it comes to building this portfolio let me stress again that we don't differentiate at this stage which is the partner that we put most of the effort behind or which is the partner we are valuing the most. You also don't make a differentiation when you have children, which of the children you do like most. We at this stage really differentiate in the sense that we only create partnerships with companies that fit to us, where there is a synchronisation of understanding, of making scientifically driven best discovery alliances. Here, we see a market, where there are many opportunities out there, and here we have the great situation that we can actually build alliances on the basis of where the best fit to our company is, which also at this stage puts us in a situation that basically all capabilities and capacities of Evotec are filled. So that's a very good situation, which also puts us into a situation that we are building more capabilities basically in the sites that are representing the centres of excellence for building these discovery alliances, so it's a good situation to have a company that is hiring people and that is building more because that's the only way to increase our top line.

With this I would like to hand over to Klaus who will give you an outlook for our current numbers.

Klaus Maleck: Thanks Werner and hello everybody. Moving to page 15, given the good development of our business that Werner just described we can confirm our guidance. We will grow our revenues by more than 15% in 2010 and our R&D costs will come in below €10 million and on a year end liquidity we will exceed the €64 million. Finally we are on track to bring our company to a sustainable profitability at the latest in 2012.

Moving on to page 16 - our path here is clearly reflected in our first quarter results. When we compare the first quarter 2009 - before restructuring - with the past first quarter 2010 after restructuring we see a strong revenue growth of 19%, in both years without milestones. The gross margin has slightly improved despite unfavourable foreign exchange effects that have cost us 2.2 percentage points. The restructuring becomes very visible when we compare R&D and SG&A costs. R&D has reduced by 83% and SG&A by 30%. Finally in 2009 we had an impairment and in the context of our restructuring we had restructuring expenses of €1.4 million. In 2010 clearly we don't expect to have those charges, and also as a consequence of that, operating income improved by 93% and we believe we have now a cost

structure in place that allows us to reach profitability, €-1.5 million operating income and net income of €-1.2 million.

On page 17 you see that the reduced net loss is also reflected in the cash flow statement. Our operating activities consumed approximately €5.2 million cash and that is due to bonus payments and other early year payments such as insurance and maintenance contracts and so on. The cash outflow is expected to decline significantly over the next quarters. We have been actively managing our cash reserves and have invested €5.3 million, visible as an increase in the balance sheet in investments of €5.1 million. Altogether our liquidity has decreased by €3.8 million in the past first quarter while we used €13.4 million just a year ago in the same period. We currently have a liquidity of €67 million.

On the balance sheet we are continuously strong on our equity ratio, on page 18, of 78.3%. We have a comfortable liquidity position of €57 million, composed of €25 million cash and €32 million short term investment, plus €10 million invested in auction rate securities. Auction rate securities will be liquid by the end of June again at the latest, some of them are actually already now popping up and becoming liquid and we are well financed for our future growth with this cash position and liquidity position.

I hand over to Werner.

Werner Lanthaler: Let me thank you again for that because it's a situation where we have invited you all to follow our path and control it and page number 19 shows you all the key indicators that we have put forward to you at the beginning of Action Plan 2012 and I think it's fair to say that we are monitoring this very closely and overall I think we are even faster on our way than we had initially anticipated and we are very happy that we can report that back to you.

When it comes to the next months and the next quarters one should be aware that making an excellent start is a good thing but always think about it that you have to go in for something in the long run. We are in this for the long run. We see many milestones to come. We see many news flow points to come and I would just like to highlight a few of them. For example we have shown with building the Genentech alliance that this is an optimal way of creating value going forward. We think that it will be possible going forward to show more of the synchronisation of target identification, platform technologies and development programmes within Evotec and our partners. Here it's most important for us to first secure all existing alliances and here the feedback is very good from all our partners at this stage in building new alliances also by potentially opening new fields of disease areas that we want to grow in and here I think it's always very important that we want to for example get into metabolic diseases or that we want to step into more biology driven disease areas.

You will also see that our value promise will become true in the sense that we are faster in delivering clinical entry points so we hope that still in 2010 we meet clinical entry points within our alliances thus sharing the product upside within our alliances. We are very happy that our 100 series is well on track to get into a significant development programme and we are very comfortable that we will exceed our goals that we have promised to you when it comes to our financial guidance by delivering at least 15% growth for the whole year on a gross margin which is at least constant. We will optimally invest in R&D on a number which is around €10 million, probably a bit below that and we will keep our cash tight in our hands because we think it's very optimal to have a situation in days like this where liquidity puts us in a strong strategic

situation and with our close to €70 million, that's what we think that we are at this stage.

Thank you very much and we are more than happy to take all questions.

Operator: Thank you. Ladies and gentlemen, we are starting the question and answer session. The question and answer session will be conducted electronically. If you'd like to ask a question please press the star or asterisk key followed by the digit 1 on your telephone keypad. Please ensure that the mute function on your telephone is switched off to allow your signal to reach our equipment. The operator will announce your name when it is your turn to ask a question. If you wish to cancel your question please press *2.

We will now take our first question from Hanns Frohnmeier of LBBW. Please go ahead sir.

Hanns Frohnmeier: Good morning and congratulations to these good results. I have two questions, one is, could you remind me on the amount of milestones you expect in 2010? Did you ever disclose that, what is approximately the number you are expecting for that? Then on the second question I understand on the Genentech deal that you are very restricted and limited to give us any more precise perspectives, but could you give us an influence on your figures maybe next year? Was the deal already included with respect to your plan to become profitable in 2010? Thanks.

Werner Lanthaler: On the first question we have not given guidance on the milestones, because it's very important for us to see this as an upside for our shareholders, but I think that a number that you should keep in mind here is that last year we have received around €8 million in upfront payments and milestones. The year before it was also in that magnitude. So I think assuming that there should be a minimum of this year would be right because all programmes are progressing very nicely. On the Genentech collaboration, I think it's fair to assume that we have had a very good feeling in making this alliance also when we started the year, and you know it takes months to close these things, so it was part of our Action Plan 2012 to have alliances like that. Is it now a bit better than we have originally assumed? Yes, so I think it's certainly nothing that would lead us to have any downside on that. It's clearly upside at this stage to our original plans. Sorry I cannot say more. I think on the pattern of this alliance you should always keep in mind how we have structured for example the CHDI alliance, that these are long term things and once you start these things it's also our intention to make it very, very long term. That's by the way also something that at this stage we really go for this quality of top line because it makes a huge difference if you have a quality of top line that is just more or less booked in for a few years than if you have to struggle for every screen that you can get out there anywhere. We also do that of course.

Operator: Our next question comes from Elmar Kraus of DZ Bank. Please go ahead.

Elmar Kraus: Good morning everybody and congrats also from me. I've got two or three questions, one is actually on the status of partnering with your other projects, whether you can bring some news on that? The other one is actually on the status on one project which I think is somewhere in the middle which is the EVT 302. There were some plans to develop it in a different indication, so what are your plans about that? Last but not least with CHDI there was recently announced also an alliance with Galapagos with the very same foundation. Can you just briefly outline where the differences are between those two big players in that field? Thanks.

Werner Lanthaler: On the first one I think we are aware of the fact that for our R&D spending we have to bring something back and either we create value points on our own by progressing these programmes or we clearly show that we have external commercial buy-in of these programmes, so we are very aware of that and very conscious of that and I think it is something to be expected in 2010 that we want to make at least one licensing deal for one asset that is in our current portfolio and I'm at this stage comfortable confirming that. On your second question, developing some of our existing programmes also into other indications like for example Alzheimer's disease, yes, there are opportunities, yes, there are options, but no, we will not go there alone and we certainly will not go there without a strong alliance partner. It's not only about risk sharing here, it's really about defining the game that we are in. We are defining the game that we are in, in bringing assets to our partners in creating alliances and for example when it comes to Alzheimer development, if you really do this seriously for products then you need a bigger wheel to turn than we could do this and want to do this in the short run here. So therefore we are active on that but we will not spend money on that alone. The CHDI is actually doing something which is absolutely in line with our strategy that they are building a portfolio of partners and it's their mission to try everything and to test every potential target out there, not only with us but also with other companies. So it's actually very good news for us that there are more targets than they can bring into our alliance and also bring them to others and it just shows you that there's such a strong need for finding a cure against Huntington's disease that there's enough research funds within the CHDI to try everything, and the best thing here is to try it in not building up their own fixed cost structure but by defining it with outsourced partners as we represent it, so this is absolutely fine and fully in line with our portfolio thinking.

Elmar Kraus: Thanks.

Operator: Our next question comes from Mike Aitkenhead of Piper Jaffray. Mr. Aitkenhead, please go ahead.

Mike Aitkenhead: Good morning and thanks for taking my questions. Just two quick questions, firstly on the gross margin. I see gross margin at 38% was pretty good for the first quarter. Can we reasonably expect gross margin to stay at those levels for the rest of the year? Secondly just on the auction rate securities: what is the status of those?

Werner Lanthaler: On the first question we don't sacrifice those margins at this stage. It's a very comfortable position to be in that we have enough business opportunities that we don't have to do that. We are always evaluating the best opportunities for us but at this stage it's not an issue. It's also very important, we want to grow more than 15% year on year by not sacrificing the gross margin going forward. That's the clear goal here. On the auction rate securities in June, this basically will fall away. Klaus will just elaborate in a second.

Klaus Maleck: We acquired the auction rate securities in the context of the Renovis acquisition. They became illiquid during the financial crisis 18 months ago. Our bank, UBS, gave us a put option at face value for June 2010 and until then we enjoy high interest rates. However, there is some liquidity now already in the market and we have seen today a market opening for a \$1.5 million security. Two weeks ago another contract became liquid again.

Mike Aitkenhead: Excellent. Finally could I just clarify something on the guidance for 2010? The 15% revenue growth that you've indicated, am I correct in assuming that is excluding the recognition of the up front payments for the EVT 101 programme, i.e. that we're expecting a 15% underlying growth in the research services business including both the research fee income and potential milestones.

Klaus Maleck: The upfront payment was recognised as deferred revenues in 2010, over 24 months. The corresponding portion of the \$10 million that we got for 101 is included in the revenues of Q1. What is not included is the \$65 million, that potentially comes through in 2011.

Mike Aitkenhead: Brilliant, thanks.

Operator: Our next question today comes from Howard Rowe of Gsquare. Please go ahead.

Howard Rowe: Thank you gentlemen. Just a quick question on the order book. Without getting into any particular names are you able to describe for us what trend you're seeing in the growth of the order book and by that I mean in particular, is it pharma dominated, is it biotech dominated, is it a mix? Then, in addition to that, are you also noticing any difference in the mix of that composition versus previous quarters?

Werner Lanthaler: First of all again apologies for not disclosing the full number at this stage but as already said it's the strongest order book ever, significantly above 30, close to €40 million at this stage. It's a mix of pharma and biotechs and I think here it's also fair to say that we are always very carefully evaluating the opportunities that we have. So for example we don't want to take on businesses where our scientists don't believe in the programme, because it doesn't help us strategically to have done a short term revenue and then never have a potential upside or a programme that moves forward from screening into chemistry. We last year of course had many biotechs and many pharmas that were very hesitant because of the world economic situation overall, so we see clearly here faster decisions in 2010 than they were taken in 2009 and we also see that we have a mix of Europe and the United States which is from our key customers more or less 50-50. When it comes to biotechs it's more European biotechs and less US biotechs and always the biotechs - and that's also very important - they don't go for Indian or Chinese integrated experiences alone. So there are always companies that are aware of the fact that if you go to Evotec you pay more, but you also get a significantly better and more valid investment decision proposal or stop-loss decision proposal for your compounds.

Howard Rowe: Great, thank you.

Operator: As there are no more questions we will conclude the question and answer session now.

Werner Lanthaler: I would like to thank you very much on this and would like to wish you all the best. I hope to hear you soon and I hope also that you will read from us soon. All the best, bye-bye.