Pharma Drivers: Money for Nothing

BY AMY BROWN, EDWIN ELMHIRST & ELIZABETH CAIRNS | MARCH 2023

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Introduction

In the current environment, all routes to the public markets for biopharma or medtech companies are likely to be pretty tough.

Gone are the days when an IPO was a walk in the park. The process currently is more akin to wading through a raging river, swerving a treacherous ditch and skirting the edges of a field containing a large, ill-tempered bull. And still finding that your destination is a huge disappointment anyway.

Companies determined to realise their ambitions of public ownership need to employ some creative approaches. This isn't new. Spacs had their moment over the past couple of years but most failed to deliver – with a handful of exceptions. Reverse mergers are now looking like a feasible, if not auspicious approach.

Observers and investors are sniffy about these routes to market, implying that a "proper" IPO is still considered the gold standard. Except, of course, the bull market of a few years ago saw some companies of pretty dubious quality sail through the open IPO window.

To get to the truth of the matter, the Evaluate Vantage team has looked at the numbers behind the tough realities of the public markets for pharma and biotech in 2023. Were Spacs as bad as people claimed? Did any late-peak IPOs meet expectations? Are reverse mergers just another nonsense route to market or a pragmatic response to some dire straits?

One thing is for sure. Plenty of cash has been splashed in the past few years – but was it money for nothing?

Contents

The ink dries on the blank cheque craze

BY EDWIN ELMHIRST AND AMY BROWN | MARCH 08, 2023

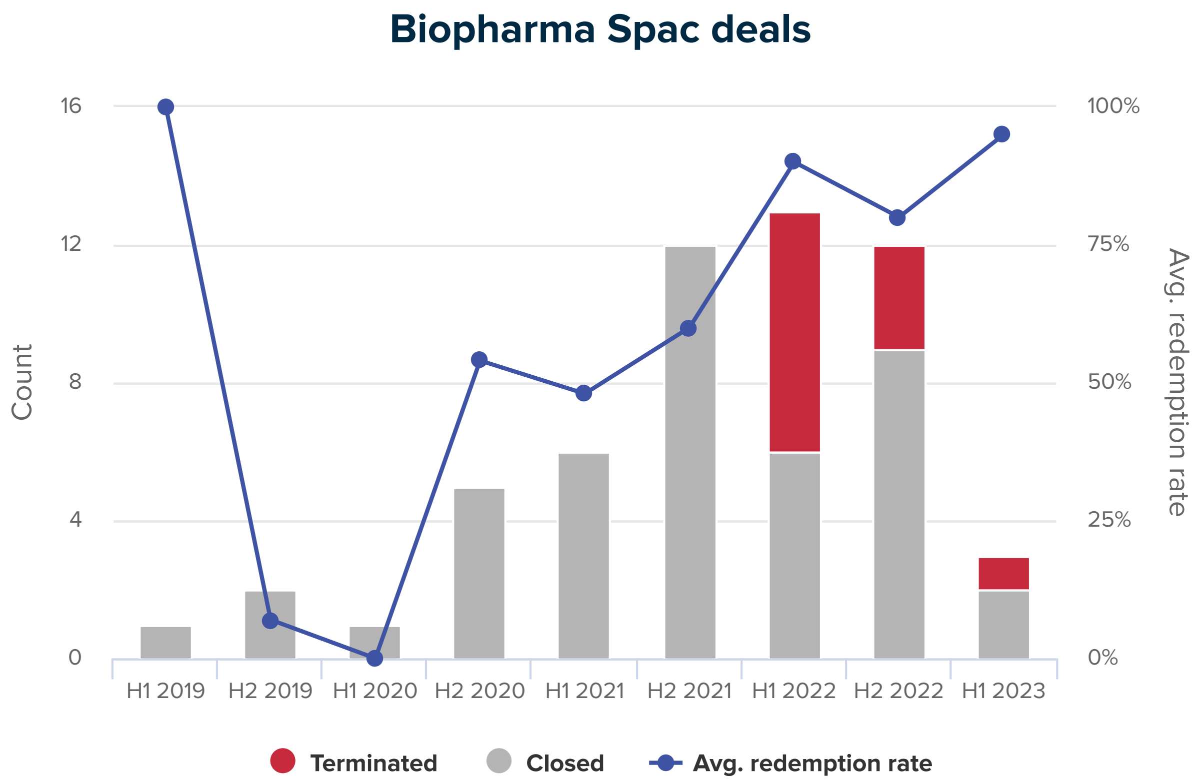
As Apexigen throws in the towel six months after listing, can any bright spots be found in the stats on Spacs?

The public markets might have little appetite for IPOs, but hunger for Spacs is even smaller. A poor track record at delivering strong companies into investors' laps has not helped the so-called blank-cheque space, with news from Apexigen providing another sorry example.

The cancer antibody company is "exploring strategic alternatives" six months after arriving on Nasdaq, a sticky situation of the sort that many other ex-Spacs are surely grappling with. Half of the 43 drug developers that floated via these vehicles since 2019 have enterprise values of less than $30m, Evaluate Vantage research finds.

Proposed Spac acquisitions are falling apart in increasing numbers, and redemption rates of close to 100% are now far from rare. This rate refers to the proportion of the Spac's original investors who decide not to support the proposed target acquisition and ask for their money back, a move that drains the pot of cash available to the private company with its eyes on the Spac's public listing.

The analysis below, based on data provided by SpacResearch, lays bare the state of play. Only pure-play drug developers are considered; *Vantage* has separately looked at device companies that floated via Spacs.



Source: Evaluate Vantage analysis of SpacResearch data

In Apexigen's case, the developer never really stood a chance as a listed entity, particularly in a bear market. A 92% redemption rate meant that it arrived on Nasdaq last July with very little cash; a $50m equity line and warrants attached to its stock added to the prospect of substantial dilution down the road for shareholders.

Making the investment case even harder, the developer was betting on CD40 agonism, an immuno-oncology mechanism that has yet to prove itself. A private placement in January raised $2.8m, but this was apparently not enough to carry on.

Other Spac developers must be in similarly dire financial situations. Of the 43 identified for this analysis, one has already gone bankrupt and another delisted – 4D Pharma and Xynomics respectively.

All of which makes it surprising that private developers are still pursuing this route, particularly when reverse merger opportunities abound. Calidi Biotherapeutics, Psyence and Longevity all announced proposed Spac deals this year. With the IPO window barely open, perhaps some consider this the best option available.

Oculis, for example, closed its deal last week, though a $91m Pipe financing run concurrently with the Spac deal provided most of the $104m transaction proceeds. The Spac with which it merged, European Biotech Acquisition Corp, was sponsored by LSP, a European venture fund that also anchored the Pipe. Oculis presumably had to pay LSP twice, both Spac and Pipe fees; in this instance the developer will arrive on Nasdaq with a respectable bank balance, but the route to that listing cannot have come cheap.

According to SpacResearch there are 12 drug developers with open Spac deals, awaiting finalisation. Most of these were announced in 2022; the most elderly of these, a deal between the UK developer Zura Bio and a Spac named JATT Acquisition that was triggered back in June, took one of the final steps towards completion last week.

EXCEPTIONS TO THE RULE

Despite some of these gloomy stats there are success stories to be found in the Spac space. One way of measuring success is comparing the enterprise value proposed at the time of the deal with current enterprise value; the former measure assumes no redemptions, so is perhaps an unfair baseline, although this number is touted to investors at the time of the proposed Spac transaction.

Notwithstanding this, on this basis Cerevel, Immunovant and Newamsterdam stand out. All have current enterprise values at least three times higher than their initial target enterprise values.

Of the 43 ex-Spacs identified, seven currently trade with an enterprise value of more than $1bn, led by Roivant, Alvotech and Prokidney.

While Spacs have not lived up to some of the grander promises made by certain proponents, they have delivered promising stories for biopharma. These are exceptions, however, so it is not surprising that enthusiasm for these vehicles has petered out with the bull market.

The current stats on Spacs		
Company (date deal closed)	**Current enterprise value ($m)**	**Target enterprise value ($m)**
Ranked on current enterprise value (highest)		
Roivant (Sep 2021)	5,286	5,000
Alvotech (Jun 2022)	4,245	2,250
Cerevel (Oct 2020)	3,453	847
Ranked on delivered enterprise value vs target enterprise value		
Cerevel (Oct 2020)	3,453	847
Immunovant (Dec 2019)	1,799	555
Newamsterdam (Nov 2022)	1,022	326
Ranked on % destruction of target enterprise value		
Vincera Pharma (Sep 2020)	-38	77
Pardes Biosciences (Jun 2021)	-118	339
Surrozen (Apr 2021)	-43	203
Ranked on current enterprise value (lowest)		
EQRX (Dec 2021)	-301	3,538
Nuvation Bio (Oct 2021)	-235	1,319
Pardes Biosciences (Dec 2021)	-118	339
Sum of all 43 ex-Spacs since 2019	**29,861**	**21,909**

Source: SpacResearch for target enterprise value, Pitchbook for current enterprise value.

The slow death of the medtech Spac deal

BY ELIZABETH CAIRNS | FEBRUARY 06, 2023

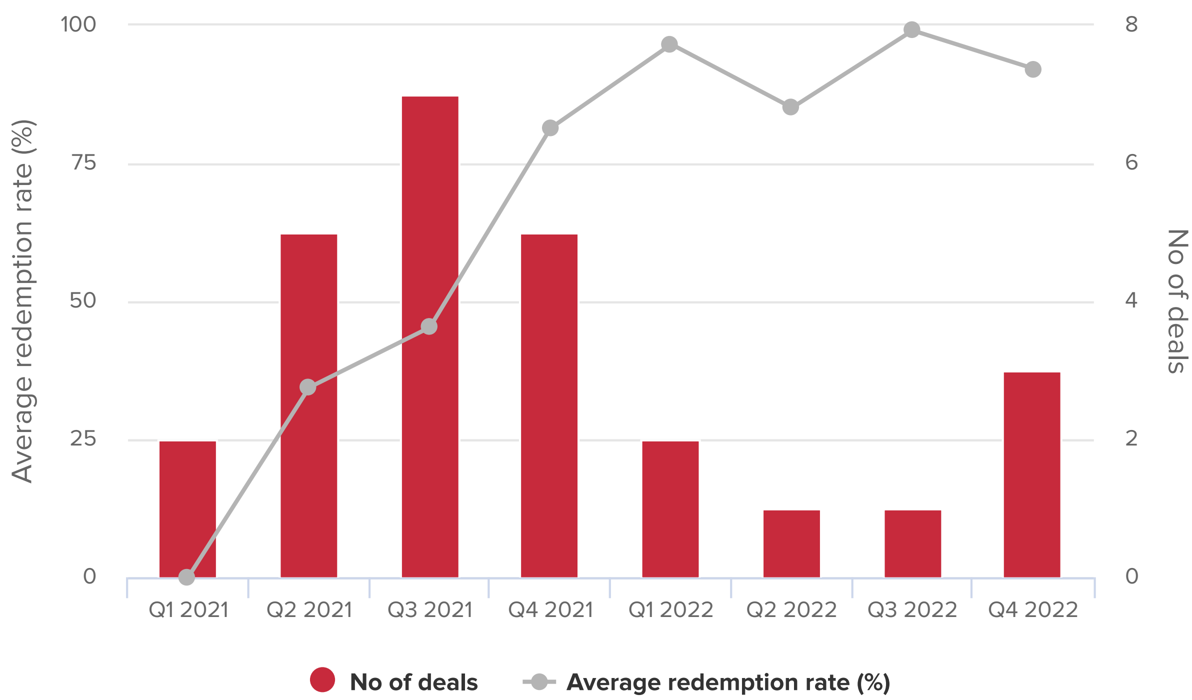
The remarkable thing is that these tie-ups are still occurring, so atrocious is their track record.

Two years ago private device makers' ardour for going public via a merger with a special purpose acquisition company was at fever pitch. As market sentiment sank into despondency over the course of last year, enthusiasm slackened and medtech Spac deals slowed from a flood to a trickle.

The performance of the 26 medtechs that went public via Spac deals over the last two years has been woeful. Only one has seen its enterprise value exceed the figure promised when the Spac merger was announced, and four now trade at a negative enterprise value, indicating that these groups are trading below cash.

Device makers started stepping away from Spac deals in the final quarter of 2021, but signs were already mounting that some investors were getting cold feet. A big signal here is redemption rates. Investors in a pre-merger Spac can redeem their shares, essentially asking for their money back, if they do not like the look of the proposed merger.

Medtech Spac deals - quarterly redemption rates



Source: Vantage and spacresearch.com

Redemptions were almost unknown at the beginning of 2021, but grew swiftly thereafter and remained high throughout 2022, data collected by Spac Research show. One explanation is that Spac shareholders had seen how poorly previous deals had done – as early as the summer of 2021 it was clear that the vast majority of transactions had disappointed – and decided to exit while they could.

DEAL WITH THE DEVIL

An analysis of post-Spac medtechs' enterprise value shows how poor the returns have been.

With one exception, all the medtechs that closed deals with Spacs in 2021 or 2022 have haemorrhaged value. This cohort has seen an average 79% decrease in enterprise value, from the EV that was promised in each company's merger announcement to their current EV.

These 26 companies are collectively responsible for $29bn in undelivered EV.

Broken promises: the catastrophic value destruction of medtech Spacs					
Target	**Focus**	**Closing date**	**Promised EV ($m)**	**Current EV ($m)**	**% EV change**
Top 5 best performers					
Seastar Medical	Cell therapy	Oct 2022	122	132	8%
Docgo	Telehealth	Nov 2021	900	870	-3%
Hims & Hers Health	Telehealth	Jan 2021	1,592	1,384	-13%
Prosomnus	Respiratory	Dec 2022	199	142	-29%
Alpha Tau Medical	Radiology	Mar 2022	660	168.4	-74%
Top 5 worst performers					
Hyperfine	Imaging/patient monitoring	Dec 2021	581	-72	-112%
Quantum-Si	Proteomics	Jun 2021	946	-45	-105%
Akili	Digital health	Aug 2022	906	-28	-103%
Talkspace	Telehealth	Jun 2021	1,400	-23	-102%
Cardio Diagnostics	Diagnostics	Oct 2022	104	1	-99%
Total (26 medtech spacs since 2021)			**35,222**	**6,214**	**Avg -79%**

Note: only deals that closed in 2021 and 2022. EV=enterprise value.

Source: spacresearch.com & Pitchbook.

Times are hard, and many high-risk stocks are suffering, not just in the medtech sector. But could the performance of these Spac groups spell the end to these vehicles?

It is not quite time to schedule the post-mortem. Medtechs are still pursuing the blank-cheque route in 2023, with one deal closed so far this year – Orchestra Biomedical's – and two more announced.

But 25 healthcare-focused Spacs are known to have been liquidated, having been unable to find a suitable target by their self-imposed deadline, which is usually set two years after the Spac floats. 21 of these liquidations occurred in the fourth quarter of 2022.

More are on the cards. 39 Spacs are currently shopping for a healthcare-focused company, and 22 of them have less than six months to find one, according to Spac Research. With investors increasingly disillusioned with this mechanism, Spac deals are going to become rare, if not actually extinct.

Conditions are ripe for reverse mergers

BY AMY BROWN AND EDWIN ELMHIRST | FEBRUARY 23, 2023

Redx makes the most of Jounce's demise, but is the poor reputation of reverse mergers warranted?

With the IPO window barely open, investors sick of Spacs, and increasing numbers of cash-rich and pipeline-poor developers, conditions are ripe for reverse mergers. Four such transactions have emerged so far this year and, unless the public markets become more conducive to flotations, more will surely follow.

A reverse merger typically involves a private company taking over a public group's listing, with the latter party all but wound up. In reality these transactions follow variations on a theme, as with the deal announced today that will see London-listed Redx take over Jounce's Nasdaq listing.

The combined entity will be majority owned by the UK company's investors and run by Redx's chief executive, but 47 of Jounce's R&D team, plus its biologics research base in Massachusetts, will be retained. Jounce's clinical pipeline is abandoned – this was a casualty of the failed Icos mechanism – but some latent value is apparently seen in the immuno-oncology researcher's early work.

Biopharma's reverse mergers of 2023 so far			
Acquirer (private/listing)	**Target**	**Combined cash**	**Resulting ownership**
Redx (Aim London)	Jounce (Nasdaq)	$170m* (to H2 2025)	Redx shareholders: 63.0%
Pherecydes (Euronext Growth)	Erytech (Nasdaq & Euronext)	€41m (to Q3 2024)	Pherecydes shareholders: 49.5%
Flame (private)	Leap (Nasdaq)	$115m (to mid-2025)	Flame shareholders: 47.4%
Elicio (private)	Angion (Nasdaq)	$25m**	Elicio shareholders: 65.5%

*Includes Evaluate Vantage's estimate of Redx current cash.
**Minimum net cash requirement.

Source: company statements.

Another deal last week, between Erytech and Pherecydes, also involved a Europe-listed developer using the reverse merger mechanism to gain a Nasdaq foothold. This suggests that while financing conditions in the US are considered dire they are still thought more attractive than in Europe.

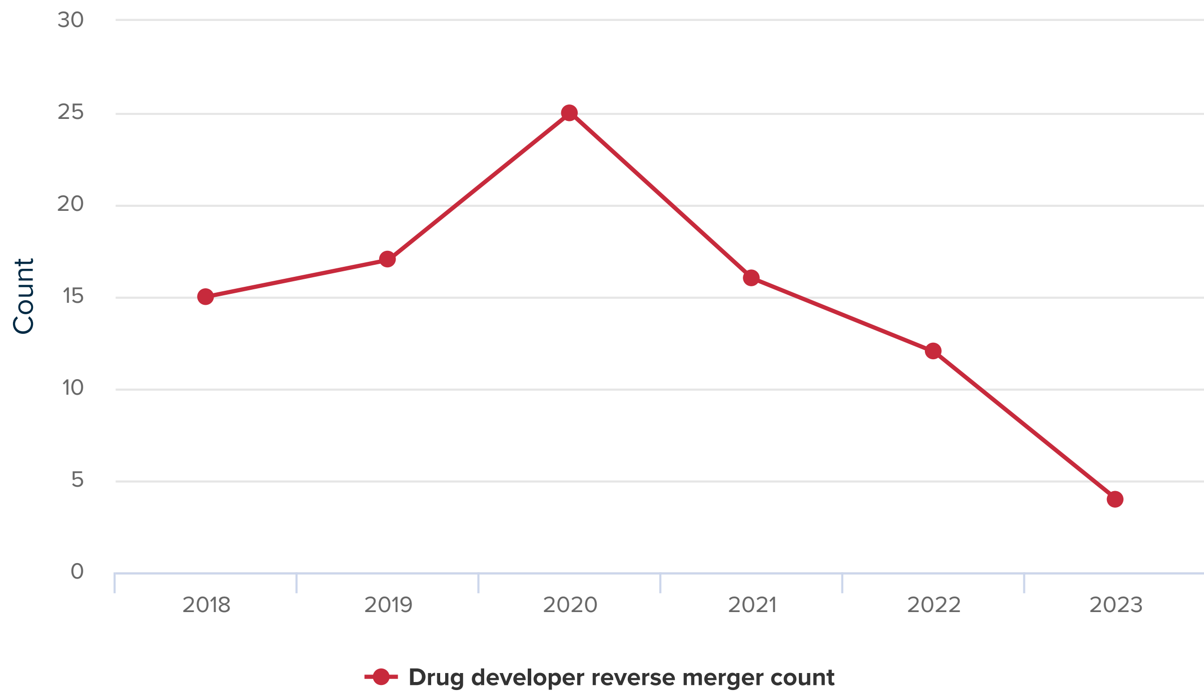
With the number of developers "exploring alternatives" growing longer every day, private developers and those listed outside the US will have plenty of zombie companies to choose from, if Nasdaq represents the promised land.

Only today Evofem, which had failed to make a commercial success of its spermicide product Phexxi, announced it was considering strategic alternatives, including a reverse merger. Graphite made a similar statement yesterday, as it formally discontinued its lead sickle cell project.

True, reverse mergers have something of a bad reputation as a route for companies too weak to undertake a full IPO, but financing options are pretty limited right now.

Spacs offered an alternative route to market in recent years, although these vehicles' poor track record at finding strong target companies soured investors to the blank cheque movement. The Spac craze probably explains the dip in reverse mergers seen last year, in the *Evaluate Vantage* analysis below.

Biopharma in reverse



Note: 2022 to February 23.

Source: Evaluate Pharma and Pitchbook

But is this poor reputation warranted? Of the 89 reverse merger deals identified in the graph above, 13 no longer seem to have a market listing, and 43 have a market cap of less than $50m. 10 are worth more than $250m, and the top five are listed below.

Those stats feel like a damning indictment, but it is worth remembering the abysmal state of the wider markets. Around 20% of global biotech companies are currently trading at negative enterprise values, and 77% of them are worth less than $250m, according to the investment bank Torreya's latest analysis of S&P Capital IQ data.

Bucking the trend?		
Company	**Current market cap**	**Reverse merger target (year of deal)**
Rocket Pharmaceuticals	$1.5bn	Inotek (2018)
Chinook Therapeutics	$1.4bn	Aduro (2020)
Immunitybio	$1.1bn	Nantkwest (2021)
Compass Therapeutics	$489m	Olivia Ventures (2020)
Disc Medicine	$431m	Gemini Therapeutics (2022)

Source: Evaluate Pharma & Pitchbook.

Flotations versus blank cheques

BY AMY BROWN AND EDWIN ELMHIRST | MARCH 09, 2023

Neither route to the stock market covered itself in glory in the recent bull market. But how do returns really stack up?

Spacs are whack and IPOs are the gold standard, the former merely being a route to market for weak companies. That commonly held belief was challenged by the recent biotech bull market, when a wide-open IPO window allowed a flood of developers of dubious quality to list.

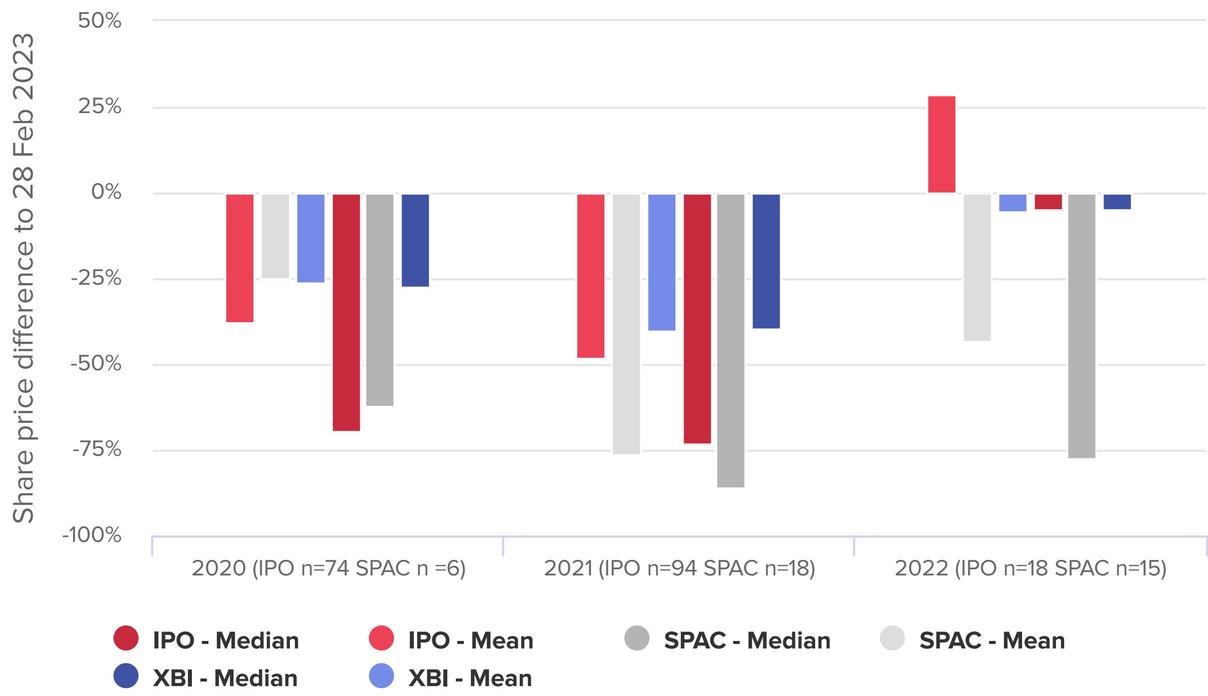
Spacs, also known as blank-cheque companies, still have a worse reputation than IPOs, however. Deservedly so, according to an analysis of returns versus IPOs, although developers that listed via the more traditional route have also performed poorly. Both cohorts substantially underperformed the wider market, *Evaluate Vantage* finds.

The chart below shows the average returns delivered by pure-play drug makers that listed on Nasdaq via either IPO or Spac, to the end of February this year. The comparator chosen was the XBI, a closely followed exchange-traded fund that tracks small biotechs. For a more detailed methodology, see below.

Cut the data almost any way, and negatives emerge. The only exception is the mean return on 2022 IPOs, thanks to incredibly strong performances from Belite Bio in particular, and Nuvectis Pharma.

Perhaps this finding can be explained by a more exacting IPO market last year, when only lower-risk developers were able to float. However, it is also true that these groups have had less time to reach, and potentially miss, important targets, compared with previous years' cohorts.

Average returns



Source: Evaluate

It is also worth remembering that considerably more developers list via IPO than via Spac. In 2021, for, example, the relative numbers were 94 and 18.

That year the peak of the bull market was reached, and this cohort of IPOs and Spacs is the worst performing, even against similarly terrible returns on the XBI. This finding surely confirms that investing at the peak of the market rarely ends well.

While this analysis paints ex-Spacs as stocks to avoid, success stories can be found in this group, as detailed in our deep dive into this space. And if all three years are amalgamated the median returns are not that different between IPOs and Spacs, at -69% and -78% respectively. This compares with a 27% fall for the XBI.

Methodology: For IPOs flotation price to close on 28 February 2023 was used to calculate return. For acquired companies the per-share takeout price was used where possible. For reverse merger targets the share price immediately before deal announcement was used.

For Spacs return was calculated from $10, which is the price at which these vehicles float, and where they typically trade until the acquisition of the target company closes.

The average closing price over each year was used to calculate the XBI return, also to 28 February 2023.

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