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Biomedical stocks racing to solve a $40bn problem

Companies making cancer therapy drugs offer scope

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A CURE for cancer remains one of the biggest mysteries in the medical world. Immuno-oncology is one of the more recent and revolutionary approaches to treating the disease. Moreover, it may be the most promising of all treatments yet seen.

A substantial amount of work in immuno-oncology is being done in the private sector, very often by listed stockmarket companies dotted around the world.

The beauty of an immuno-oncological approach is the lack of toxicity and deadly side effects that plague many other chemical-based cancer therapies. Some industry analysts estimate that over the next 10 years, up to 60 per cent of cancers may be treated in this manner compared with only 3 per cent today.

It has been recently reported that researchers at the Melanoma Institute Australia are successfully treating melanoma patients using drugs to awaken the body's immune system using what is called the PD-1 receptor, a key regulator of cell activity.

With most cancers, the body's immune system fails to recognise the tumour as a threat because the tumour is able to mask itself using the PD-1 receptor. But the new immuno-oncology drugs have the potential to stop that process. If these treatments become mainstream, the investment implications are huge with an estimated $US35 billion ($40bn) a year revenue stream at stake.

It is also likely that if this approach is successful for one type of cancer (say melanoma) it may well work for a number of other deadly cancers.

There are several publicly traded pharmaceutical and biotechnology companies in the US and Europe that are using this approach via checkpoint agents, vaccines, and cell therapies to try to achieve breakthroughs in the treatment of the most common and deadly cancers — melanoma, and cancer of the lung, brain, breast and colon.

In the large cap space, I believe Bristol-Myers Squibb and Roche are best placed given their advanced pipelines using PD-1 checkpoints and deep expertise in cancer therapies. US-based Bristol-Myers Squibb (market cap $US97bn) develops, licenses, and manufactures biopharmaceutical products worldwide.

It has a diverse product range covering chemically synthesised drugs and biologies in various therapeutic areas, including virology, human immunodeficiency, virus infection (HIV), oncology, neuroscience, immunoscience, and cardiovascular.

Bristol-Myers has the most PD-1 based indications in clinical trials (more than 35 at last count) and for a wide range of cancers. Bristol trades at more of a "biotech" multiple 32 times 2014 EPS but has a medium-term growth rate of more than 20 per cent.

Roche is my favourite European pharmaceutical company for immune-oncology and a good choice for investors wishing for diversification in an Australian or US-centric equity portfolio.

Swiss-based Roche (market cap 238bn Swiss francs, or $282bn) is a global healthcare company with interests in pharmaceuticals and diagnostics.

The pharmaceuticals division is the world leader in anti-cancer medicine.

The diagnostics division is the world's largest with expertise in blood glucose monitoring and blood virus testing.

The investment case for Roche is based on the fact that the company and its fully owned subsidiary Genentech have one of the most extensive portfolios of immunotherapy indications in the world.

A much smaller company that it is involved in immuno-oncology is Celldex Therapeutics (market cap $US1.2bn), a US-based biotechnology company. Much riskier than the large capitalisation names mentioned previously, it is a pure play on the theme. Celldex has developed an impressive pipeline comprising antibody and protein-based therapies that "modulate" the immune system and target tumours.

Rindopepimut is company's most advanced drug and is currently in phase three trials with 700 patients enrolled for the most common and deadly form of brain cancer, glioblastoma multiforme (or GBM.)

In phase 2 trials, Rindo (as we'll call it) achieved impressive longer-term survival rates for a disease whose survival rate is literally 0 per cent.

If phase two results are successful then Food and Drug Administration approval can be sought via a regulatory submission. Of course, not all phase three trials pass the scrutiny of the FDA.

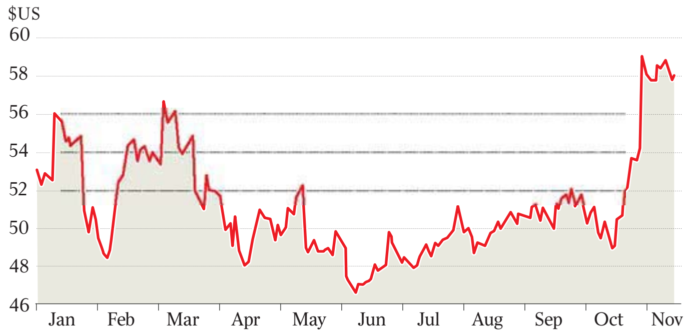
If it passes, estimates vary widely as to the revenue potential of Rindo. It could be $US500 million, $US1bn, or even more. At any rate, if it's approved Celldex stock is going higher since Celldex is not profitable and had revenues of only $US4.1m in FY13. The company is also working on Glenba, a breast cancer drug.

In a diversified global equity portfolio, I would hold all three companies. Bristol-Myers and Roche have broad and diversified therapeutic portfolios and are in the lead to commercially develop the immune oncology approach.

The FDA seems more inclined to approve novel immunotherapies given the much better response rates seen in early trials. Celldex is speculative, loss-making, and may never commercialise its pipeline but that the risk you take in small biotechnology companies. In terms of position size, my Celldex holding would be modest relative to Bristol-Myers and Roche.

Clay Carter writes on global equities for Eureka Report. He holds shares in Celldex Technologies.

Bristol-Myers Squibb this year



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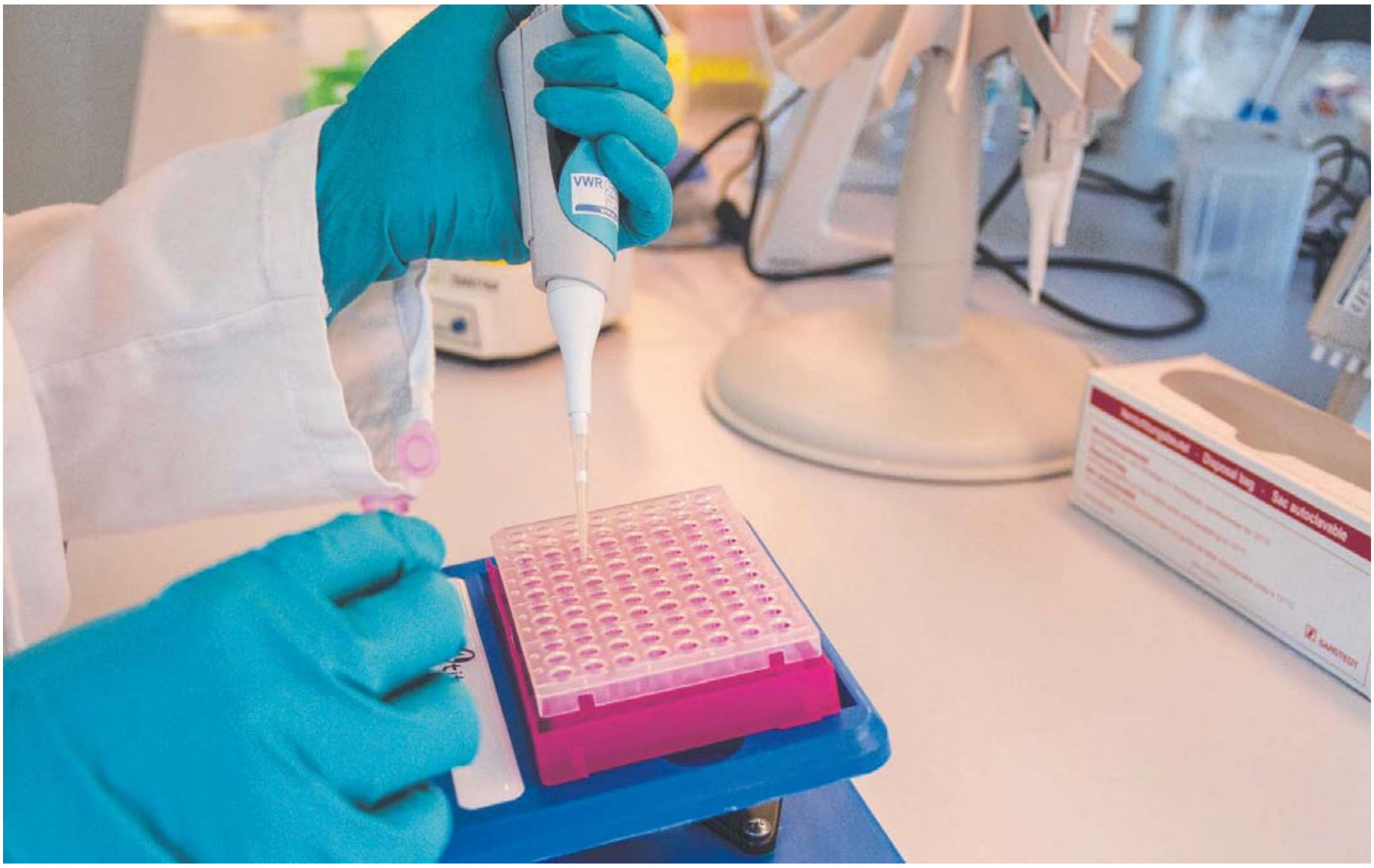

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