

BioLight Life Sciences

Binding agreement reached to sell IOptima

Update on sale

Pharma & biotech

BioLight's subsidiary IOptima Ltd (of which BioLight holds a 70% ownership stake) entered into a binding agreement for it to be acquired in a four-stage process by Chengdu Kanghong Pharmaceutical Group Co. (Chengdu). The total cash proceeds that BioLight is anticipated to receive, by mid-2021, would be between \$23m and \$27.3m; we estimate it would receive about \$12m by mid-2018. We now obtain an rNPV valuation of NIS112.5-134.3m (up from NIS109.7-130.7m, previously).

Year end	Revenue (NISm)	PBT* (NISm)	EPS* (NIS)	DPS (NIS)	P/E (x)	Yield (%)
12/15	1.4	(25.1)	(6.96)	0.0	N/A	N/A
12/16	2.1	(26.3)	(5.55)	0.0	N/A	N/A
12/17e	2.2	(30.1)	(6.88)	0.0	N/A	N/A
12/18e	3.6	(27.9)	(7.50)	0.0	N/A	N/A

Note: *PBT and EPS are normalised, excluding amortisation of acquired intangibles, exceptional items and share-based payments.

Initial cash proceeds to BioLight by mid-2018

The initial tranche, expected within 60 days, calls for Chengdu to invest \$7m directly in IOptima for a 19% stake, reducing the stake of existing shareholders (BioLight's will be lowered to 55-57%). In the three subsequent stages of the deal, Chengdu will purchase the remaining IOptima shares from BioLight and the other shareholders. The second stage, expected within six months of the first, would involve Chengdu purchasing 41% of total outstanding shares for \$17.2m. As BioLight's equity stake would be reduced to c 27-28%, we estimate that it would receive c \$12m at this point. In the two remaining stages, scheduled for Q219 and Q221, respectively, Chengdu would acquire the remaining shares in IOptima (acquiring 20% in each stage), with the pricing to be determined based on IOptima's performance.

Deal likely to proceed but contingent on conditions

Execution of each stage is contingent on the fulfilment of several predefined conditions, including the approval by the applicable Chinese authorities to permit flows of investment capital outside China and the associated forex conversions that are needed. The second stage requires the renewal of IOptiMate's registration with the Chinese Food & Drug Authority (CFDA) to occur by April 2018. As IOptiMate previously received CFDA approval, we do not expect challenges for this renewal. We view most of the conditions as customary for a deal of this nature, and we assign a 12.5% pa discount rate on the anticipated proceeds.

Valuation: rNPV of NIS112.5-134.3m

While we previously used a probability-weighted relative NPV (rNPV) analysis for the anticipated cash flows from IOptiMate (which provided a pre-tax rNPV contribution of NIS107.7m), we are replacing this with a discounted cash flow analysis of the projected proceeds from the sale of BioLight's IOptima stake, which we value at \$21.6m (NIS75.8m). After making forex, working capital and tax adjustments, and rolling forward our forecasts, we obtain an rNPV of NIS112.5-134.3m (up from NIS109.7-130.7m, previously). We expect that the firm has sufficient funds into early 2018 and we model it will raise NIS15m in early 2018.

28 November 2017

Price* **NIS14.74**

Market cap **NIS54m**

*Priced as at 24 November 2017.

NIS3.51/US\$

Net cash (NISm) at Q417e 12.9

Shares in issue 3.6m

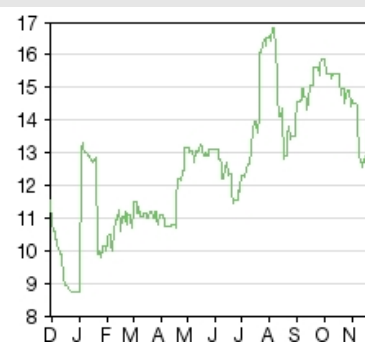
Free float 43%

Code BOLT

Primary exchange TASE

Secondary exchange N/A

Share price performance



% 1m 3m 12m

Abs 1.7 9.8 32.1

Rel (local) 1.1 5.1 26.7

52-week high/low NIS16.8 NIS8.4

Business description

Based in Israel, BioLight Life Sciences is an emerging ophthalmic company focused on the development and commercialisation of product candidates that address ocular conditions. VS-101 is directed towards the treatment of glaucoma and TeaRx is intended for use in dry eye diagnostics.

Next events

Start VS-101 Phase IIb study H118

2017 financial results March 2018

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Definitive agreement reached to sell IOPTima

BioLight announced on 21 November 2017 that its subsidiary IOPTima Ltd. has entered into a binding agreement for it to be acquired in a four-stage process by Chinese pharmaceutical company Chengdu Kanghong Pharmaceutical Group Co. (Chengdu). This arrangement follows the term sheet that both parties entered into in April 2017 and that was detailed in an earlier [research note](#). Prior to any Chengdu investment, BioLight (through its wholly-owned XL Vision Sciences Ltd. subsidiary) owns about 70% of IOPTima's share capital, and two investment funds hold the majority of the remaining c 30%.

Initial cash proceeds to BioLight anticipated by mid-2018

The initial tranche of the Chengdu transaction calls for it to invest \$7m directly in IOPTima for a 19% stake in the company, which would value IOPTima (including Chengdu's stake) at about \$37m. This first stage of the transaction is expected to occur within 60 days of the signing of the formal agreement between both parties; hence we expect it have occurred by the end of January 2018. Following this initial investment, Chengdu will become the exclusive distributor for IOPTima's main product, IOPTiMate,¹ in China (historically the product's largest market) for at least three years, and BioLight's ownership stake will be reduced to about c 55-57%. In the three subsequent stages of the acquisition transaction, Chengdu will purchase the remaining IOPTima shares from the remaining shareholders (including BioLight).

The second stage of the transaction has been guided to occur within six months of the first stage. In this second stage, Chengdu would acquire additional shares in IOPTima from the existing shareholders (reflecting 41% of total shares outstanding) for \$17.2m (about NIS60m), thereby raising its stake to 60%. Based on such metrics, IOPTima would be valued at about \$42m at this point, and BioLight's equity ownership stake in IOPTima would be reduced to c 27-28%. Execution of the second stage is contingent on the fulfilment of several predefined conditions, including the completion of certain IOPTima operational objectives including the renewal of IOPTiMate's registration with the Chinese Food and Drug Authority (CFDA) by April 2018. Given that IOPTiMate previously already received approval by CFDA and has been sold in China, we do not expect challenges to renewing this registration. If this and all other conditions are met, as we expect, we estimate that BioLight will receive approximately \$12m in cash proceeds as part of this stage.

Up to \$27.3m in total proceeds for IOPTima sale by mid-2021

In the two remaining stages, scheduled for Q219 and Q221, respectively, Chengdu would acquire the remaining shares in IOPTima (acquiring 20% in each stage), with the price to be paid determined using a pricing formula dependent on IOPTima's profitability and operational results (and that is calculated separately for each stage), and that can reflect an IOPTima valuation of between \$40.5m to \$56.25m. By the end of the fourth stage, Chengdu will have full ownership and control of IOPTima. If the transaction is completed in its entirety, BioLight expects that it will generate gross cash flow proceeds between \$23m and \$27.3m (i.e. by mid-2021).

BioLight indicates that execution of each stage of the transaction is contingent on clauses, terms, and conditions, including ensuring the approval by the applicable Chinese authorities to permit the outflow of investment capital (and the associated forex conversions) to purchase assets outside of China (to allow for the payment by Chengdu for the acquisition of IOPTima shares at each stage).

¹ IOPTiMate is a proprietary carbon-dioxide laser-assisted sclerectomy (CLASS) device marketed by IOPTima for the treatment of glaucoma.

Accordingly, management indicates that there is no guarantee of the completion of any of the four stages of the agreement.

Valuation

The signing of a binding agreement between IOptima and Chengdu prompts us to revise our analysis for IOptima in our valuation for BioLight. While there are conditions attached to the transaction, including operational objectives that must be met for the second (and subsequent) stages to proceed, we view most of these as customary for a transaction of this nature and in our view it is likely that the transaction will proceed as planned or guided by the company. That said, we believe it would only be prudent to attach a discounted-factor analysis to the expected cash flows to BioLight as part of the different parts of the transaction.

Altogether, whereas we previously applied a probability-weighted relative net present value (rNPV) analysis for the expected cash flows from IOptiMate (adjusted for BioLight's 70% ownership stake in IOptima), sales in US and ex-US markets (which provided an rNPV contribution of NIS107.7m on a pre-tax basis), we now feel it is more appropriate to replace this assessment with a discounted cash flow analysis of the projected proceeds from the Chengdu acquisition of BioLight's IOptima stake. The table below provides a summary analysis of the expected proceeds to BioLight and timing for stages two through four of the purchase transaction. We apply a 12.5% discount rate to these cash flows (for illustrative purposes only, the final column also shows the present value if a higher 25% discount rate is used). For stages three and four, for the assumed sales of BioLight's remaining IOptima shares, we assume the mid-point of the IOptima firm value range provided by the terms of the transaction (\$48.38m, or midway between \$40.5m to \$56.25m figures provided by the firm). Based on this analysis, we estimate that the total non-discounted proceeds to BioLight from the sale of its IOptima stake would be \$25.3m. Using a 12.5% annual discount rate, that the discounted proceeds would be \$21.6m (NIS75.8m).

Exhibit 1: Assessment of cash flows to be received as part of IOptima sale to Chengdu

Transaction stage	Period	Estimated ownership (%) of IOptima held by BioLight before sale*	Estimated change in BioLight's IOptima stake (%)*	Non-discounted cash proceeds (\$m)	Proceeds (\$m) discounted at 12.5% pa	Proceeds (\$m) discounted at 25.0% pa
2	Q318	56	28.5	12.0	11.3	10.7
3	Q219	27.5	13.75	6.65	5.7	5.0
4	Q221	13.75	13.75	6.65	4.5	3.2
Total			56	25.30	21.6	19.0

Source: Edison Investment Research. Note: *Expressed as a percentage of total IOptima shares outstanding.

Our estimates for BioLight's remaining product lines (TeaRx and Eye-D VS-101) are unchanged, although we have rolled forward our forecasts by one quarter.

Exhibit 2: BioLight Life Sciences rNPV assumptions

Product contributions (net of R&D costs)	Indication	rNPV (NISm)	rNPV/share (NIS)	Probability of success	Launch year	Peak sales (US\$m)
VS-101 (97% weighted)	Glaucoma	125.1	34.43	30.0%	2020	\$69.8m in 2026
TeaRx (80% weighted)	DES diagnosis	26.7	7.36	50.0%	2017	\$19.8m in 2025
Corporate costs & expenses						
SG&A expenses		(60.2)	(16.56)			
Net capex, NWC & taxes		(56.6)	(15.58)			
Discounted value of future IOptima sale proceeds		75.8	20.87			
Value of Micromedic shares (MCTC, TASE)*		3.6	0.99			
Total rNPV		114.5	31.50			
Net cash (debt) (Q417e) excluding net cash held by IOptima subsidiary		6.4	1.76			
Total equity value**		120.9	33.26			
FD shares outstanding (000) (H117)		3,634				

Source: Edison Investment Research. Note: *5.29m shares held with 22 November 2017 price of NIS0.683 per share. **Excludes the impact from any dilution resulting from any future equity offerings.

We continue to apply a risk-adjusted net present value (rNPV) model with a 12.5% cost of capital. For both Eye-D VS-101 and TeaRx, we provide a weighted rNPV based on BioLight's ownership of the associated subsidiary company. After including the discounted proceeds from the IOptima sale (in lieu of our probability-weighted rNPV forecasts for the subsidiary) in our valuation, rolling forward our forecasts, adjusting forex assumptions (and the public market value of held Micromedic shares), and lowering working capital needs and future tax expenses (since IOptima-related profits are now excluded), we now obtain an rNPV of NIS112.5-134.3m (up from NIS109.7-130.7m, previously). We assume that that none of the cash currently held at IOptima will be returned to BioLight following the completion of the Chengdu transaction. Hence, the net cash position (NIS6.4m at Q417e) used in our equity valuation calculation now excludes the amount of net cash held at the IOptima subsidiary (NIS6.5m at Q417e).

Financials

BioLight expects to cease consolidating its financial reports with those of IOptima once the second stage of the transaction is completed. Accordingly we have removed IOptima-related revenues and expenses from our forecasts starting in Q318.

We continue to believe that BioLight will need to raise funds imminently, as it will not receive any proceeds from the IOptima sale until mid-2018. BioLight finished Q217 with NIS25.5m in net cash (NIS25.1m cash and equivalents and NIS0.4m in short-term deposits). However, NIS11.6m of this cash is held at IOptima and other BioLight subsidiaries (NIS9.9m at IOptima, NIS1.3m at Micromedic and NIS0.5m at other subsidiaries), and BioLight prefers to avoid inter-corporate cash transfers to the parent company.

Hence, the parent company (BioLight) only had c NIS13.5m in net cash available at Q217. BioLight had an H117 operating cash burn rate (including all subsidiaries) of NIS12.8m, and we forecast its H217 burn rate will be similar. We estimate that without any additional cash raising, the company, including its subsidiaries, will only have NIS12.9m at YE17. We assume that IOptima will have NIS6.5m net cash at YE17, and thus BioLight's consolidated net cash excluding IOptima will be NIS6.4m. The parent company will likely need funds in early 2018 to sustain its operations and R&D projects (such as for Eye-D VS-101). We now model that BioLight will raise NIS15.0m in H118. For modelling purposes, we assign this financing to long-term debt.



Once proceeds are received from the second tranche of the IOptima sale, we do not expect further fund raising will be necessary to support BioLight's development programs (we expect VS-101 to be launched in 2020 and BioLight would subsequently generate sustainable positive cash flows).

Exhibit 3: Financial summary

	NIS000s	2014	2015	2016	2017e	2018e	2019e
Year end 31 December		IFRS	IFRS	IFRS	IFRS	IFRS	IFRS
PROFIT & LOSS							
Revenue		941	1,391	2,111	2,210	3,585	5,026
Cost of Sales		(538)	(734)	(996)	(1,169)	(1,613)	(2,262)
Sales, General & Administrative		(8,529)	(11,956)	(10,360)	(10,233)	(8,122)	(8,633)
Research & Development		(18,560)	(13,045)	(10,982)	(18,010)	(19,500)	(13,200)
EBITDA		(26,686)	(24,344)	(20,227)	(27,202)	(25,650)	(19,068)
Depreciation		(3,884)	(1,306)	(3,190)	(1,329)	(2,400)	(2,400)
Amortization		0	0	0	0	0	0
Operating Profit (before exceptionals)		(30,570)	(25,650)	(23,417)	(28,531)	(28,050)	(21,468)
Exceptionals		(5,886)	(2,475)	(7,357)	241	0	0
Other		0	0	0	0	0	0
Operating Profit		(36,456)	(28,125)	(30,774)	(28,290)	(28,050)	(21,468)
Net Interest		448	543	(2,836)	(1,557)	107	233
Profit Before Tax (norm)		(30,122)	(25,107)	(26,253)	(30,088)	(27,943)	(21,236)
Profit Before Tax (FRS 3)		(36,008)	(27,582)	(33,610)	(29,847)	(27,943)	(21,236)
Tax		0	0	0	0	0	0
Profit After Tax and minority interests (norm)		(17,216)	(16,784)	(14,467)	(23,220)	(27,275)	(21,375)
Profit After Tax and minority interests (FRS 3)		(23,102)	(19,259)	(21,824)	(22,979)	(27,275)	(21,375)
Average Number of Shares Outstanding (m)		1.9	2.4	2.6	3.4	3.6	3.6
EPS - normalised (NIS)		(8.91)	(6.96)	(5.55)	(6.88)	(7.50)	(5.88)
EPS - normalised and fully diluted (NIS)		(8.91)	(6.96)	(5.55)	(6.88)	(7.50)	(5.88)
EPS - (IFRS) (NIS)		(11.96)	(7.98)	(8.37)	(6.80)	(7.50)	(5.88)
Dividend per share (NIS)		0.0	0.0	0.0	0.0	0.0	0.0
BALANCE SHEET							
Fixed Assets		8,002	9,832	5,282	4,910	(31,382)	(50,730)
Intangible Assets		7,106	6,869	3,910	3,910	(38,222)	(61,570)
Tangible Assets		896	2,963	1,372	1,000	6,839	10,839
Current Assets		32,432	53,439	30,031	15,505	32,473	30,852
Short-term investments		6,408	385	417	382	382	0
Cash		22,196	50,697	25,057	12,492	31,490	27,028
Other		3,828	2,357	4,557	2,631	601	3,823
Current Liabilities		(6,552)	(6,605)	(6,988)	(7,121)	(71)	(478)
Creditors		(6,552)	(6,605)	(6,988)	(7,121)	(71)	(478)
Short term borrowings		0	0	0	0	0	0
Long Term Liabilities		(8,144)	(9,605)	(11,915)	(11,653)	(26,653)	(26,653)
Long term borrowings		0	0	0	0	(15,000)	(15,000)
Other long term liabilities		(8,144)	(9,605)	(11,915)	(11,653)	(11,653)	(11,653)
Net Assets		25,738	47,061	16,410	1,641	(25,634)	(47,009)
CASH FLOW							
Operating Cash Flow		(27,435)	(24,580)	(24,106)	(22,875)	(30,001)	(21,643)
Net Interest		448	543	(2,836)	(1,557)	107	233
Tax		0	0	0	0	0	0
Capex		(402)	(182)	(370)	(1,066)	(8,239)	(6,400)
Acquisitions/disposals		0	(837)	(227)	(192)	42,132	23,348
Financing		38,374	47,320	2,554	11,479	0	0
Net Cash Flow		10,985	22,264	(24,985)	(14,211)	3,999	(4,462)
Opening net debt/(cash)		(17,901)	(28,604)	(51,082)	(25,474)	(12,874)	(16,872)
HP finance leases initiated		0	0	0	0	0	0
Other		(282)	214	(623)	1,611	0	0
Closing net debt/(cash)		(28,604)	(51,082)	(25,474)	(12,874)	(16,872)	(12,410)

Source: BioLight Life Sciences reports, Edison Investment Research. Note: The reported financial results consolidate Micromedic's financials, and forecast financial results (2017e and beyond) do not include Micromedic operations.

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