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Sirtex Medical Limited

A stronger result than we expected

Sirtex Medical Limited (ASX:SRX) reported their half-year result to 31 December 2014 on 18 February 2015.

According to Portfolio Manager, Russell Muldoon, the result is much stronger across the board, than previously modeled, particularly in dosage sales (volumes), price increases and average selling prices. Sirtex's half-year result is further evidence of our current belief in the business's underlying strength and management's strategy.

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Sirtex Medical Limited is an Australian-based medical device company, providing a radioactive microspheres treatment, called SIR-Spheres, for inoperable liver cancer.

Sirtex is also currently one of the largest positions held in both The Montgomery Fund and The Montgomery [Private] Fund and here we review the company's half year results.

Sirtex reported another half of both revenue and earnings growth.

- Revenue growth of 37.3 per cent
- Earnings growth of 58.9 per cent

Both revenue and earnings growth rates were higher than our estimates as was Sirtex's dosage sales growth of 26.3 per cent, which exceeded of our base case of 21.2 per cent.

At the AGM in 2014, Sirtex reported circa 29 per cent dose sales growth. The recent half yearly result therefore implies circa 24 per cent dose sales growth in the second quarter.

We are particularly impressed, given the company was cycling 19 per cent growth in the prior period. It is also the second strongest result (on a higher base) since we began collecting data. Indeed the dose sales reported represents a step up in growth. We note that sales regionally were not only strong in the United States at +28 per cent, but also in EMEA (Europe, Middle East & Africa). This was primarily driven by the UK with re-inclusion into a stable reimbursement regimen and inclusion by ESMO (European Society for Medical Oncology) into recommended clinical guidelines.

As a side point, sales in this half exceeded total dose sales for all of 2011 reflecting the strong year-on-year-growth Sirtex has achieved. The company has now reported 42 consecutive quarters of dose sales growth.

Further, dose sales are being aided by a ramp up in marketing expenses which are up +39 per cent over the prior period with an additional one-off \$10m to be spent ahead of the SIRFLOX medical trial results (due in a matter of weeks).

Management have also 'accelerated' the recruitment and training of 'active' treatment centres which are up 17.4 per cent over the half. Management confirmed these are quality centres/hospitals with higher than average case loads. New market launches are planned for the second half. This is important as it is Sirtex's distribution channel.

On sales, we noted previously that Sirtex had put through a \$1,000 price rise in the US which appears to have been accepted by clinicians, "*there has been no push back on price with volume growth remaining consistent post.*"

Aided by a declining Australian Dollar with circa 70 per cent of dose sales being in USD, average selling prices improved 8.7 per cent \$14,948 to \$16,253.

Total sales also 'stepped-up' this half with gross profit rising by 1bps (84 per cent GM's).

The operational leverage was somewhat apparent in this result with earnings increasing at a faster rate than sales despite continued and growing investment back into the business.

Clinical Trials Update

Management gave little indication as to the likely outcome of the key SIRFLOX trial which aims to show a Progression Free Survival benefit of circa 3 months when combined with Chemotherapy, the current gold standard of care. The aim of SIRFLOX, as noted previously, is to elevate SIRT to First-Line therapy status.

- We currently expect basic qualitative data to be released in March 2015 with final results, a detailed analysis and full quantitative data (hazard ratios, p-values) to be released at the American Society of Clinical Oncology annual meeting in front of 25,000 US oncologists between 29 May – 2 June 2015 in Chicago.
- Sirtex have a number of other studies either 'recruited' or 'recruiting' at present. One of these is called SARAH and this study has accelerated in terms of recruiting patients onto the trial, which based on our understanding of the past, might be a reflection that oncologists are seeing encouraging results. SARAH is expected to fully recruit within the next few months.

A new slide in the presentation - one that we have not seen before - is how Sirtex plan to manage the transition from a 'salvage' treatment to a first-line therapy (if the results of the SIRFLOX trial are positive).

Summary

We believe that Sirtex's half year result provides further evidence of the company's underlying strength and the efficacy of its strategy. Sirtex is in a strong financial position (46 per cent of the balance sheet is cash) and has a high conversion of accrual earnings to cash flow despite investing heavily in numerous trials and marketing.

We are seeing ever-stronger demand growth for SIR-Spheres Microspheres for the treatment of inoperable Metastatic Colorectal Cancer (MCC) in salvage given "*there is not a lot of transition to first-line use yet*" (implying there is already some), and consider this result to be exceptional and a further reflection of the significant clinical and commercial opportunities that remain, as awareness and demand grows.

Also, other than MCC, Sirtex has the potential to expand into HCC, renal (kidneys) and breast cancer. These markets combined expand the company's market opportunity.

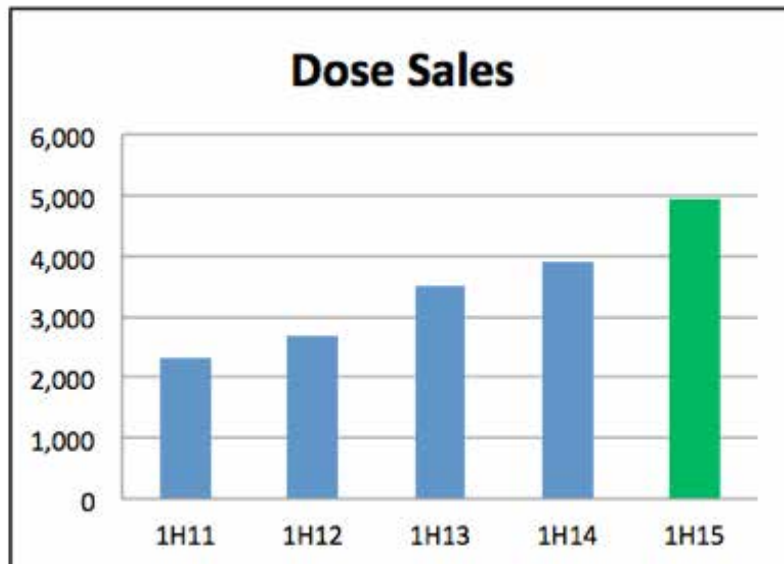
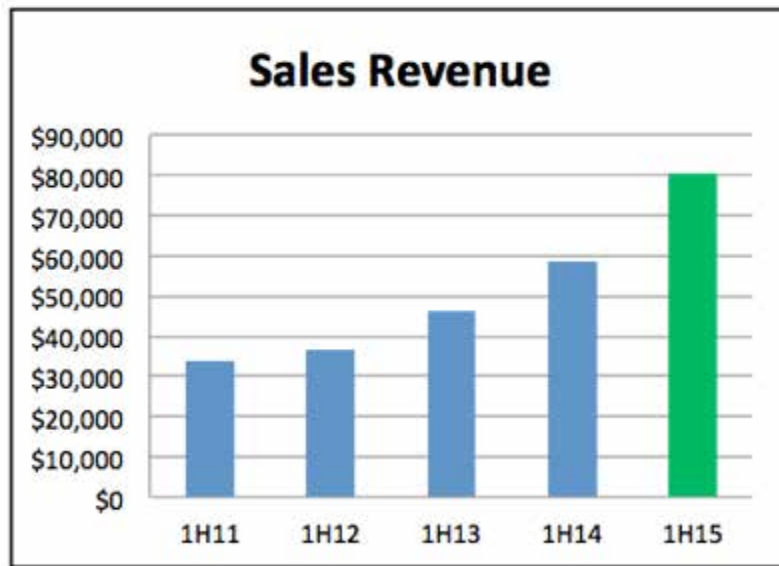
To quote management:

- *"It is an exciting time for Sirtex"*
- *"Dose sales growth is representative of our devices growing reputation and efficacy"*
- *"We have a robust and profitable global business set to reach new levels of growth"*

In the Press













Jessica Gardner from the Australian Financial Review wrote an in depth piece about Sirtex and its growth potential in 2015. She mentions Montgomery's Russell Muldoon and his views on the liver cancer treatment drug and the approaching trial. You can read this article [here](#).

Appendix 1



Study name	Start	Total patients	% recruited			Type of liver cancer ⁽¹⁾
			31 Dec 2013	30 Jun 2014	31 Dec 2014	
SIRFLOX	2006	532	100%	100%	100%	mCRC
FOXFIRE & FOXFIRE Global	2010	>560	68%	94%	100% ⁽²⁾	mCRC
SARAH	2012	460	67%	92%	96%	HCC
SORAMIC	2010	375	53%	63%	75%	HCC
SIRveNIB	2011	360	64%	69%	78%	HCC

Appendix 2

1H15 Result	1H 2014	1H 2015	Delta	Delta %	Trend	
Dose Sales	3,919	4,950	1,031	26.3%	— 	Sales stepped up
Total Revenue	\$58,581	\$80,452	\$21,871	37.3%	— 	US price rise + currency benefits
Avg Selling Price	\$14,948	\$16,253	\$1,305	8.7%	— 	
Gross profit	\$49,347	\$67,816	\$18,469	37.4%	— 	
Gross profit margin	84%	84%		0.1%	— 	
Marketing Expenses	\$21,194	\$29,464	\$8,270	39.0%	— 	Ramp-up ahead of SIRLOX result
Underlying PAT	\$11,170	\$17,655	\$6,485	58.1%	— 	
Operational Cash Flow	\$15,892	\$21,948	\$6,056	38.1%	— 	Strong cash conversion
Balance Sheet						
Cash Balance	\$47,850	\$55,455	\$7,605	15.9%	— 	
Capitalised Intangible Assets	\$9,899	\$10,255	\$356	3.6%	— 	Relates to ongoing trial costs.
Shareholders Equity	\$107,583	\$119,455	\$11,872	11.0%	— 	
% Cash	44%	46%		4.4%	— 	Cash building. M&A activity flagged

Quarterly Dose Sales Growth (no longer being reported)				
	1st Qtr	2nd Qtr	3rd Qtr	4th Qtr
2015	29%	24%		
2014	4%	19%	18%	27%
2013	37%	25%	6%	13%
2012	11%	22%	34%	26%
2011	16%	17%	21%	19%