EDISON

BB Biotech

Strong focus on emerging clinical areas

Investment companies

BB Biotech (BION) is a Switzerland-based closed-end fund focusing on the high-growth opportunities available in the global biotechnology space. Founded in 1993 by industry specialist Bellevue Asset Management, BION holds a concentrated (c 30–35 stocks) portfolio of biotech names, which are diversified across a range of clinical focuses. The fund's strong record of NAV outperformance versus the headline NASDAQ Biotechnology index has suffered a setback in the past 12 months. However, the managers remain optimistic on medium-term clinical catalysts and have recently refreshed the portfolio with a number of new holdings. BION has a policy of paying c 5% of its share price annually as a dividend, which, along with a shift in the shareholder base to include more long-term investors and fewer discount players, has supported a strong re-rating in the shares. The fund has traded at an average 7.1% premium to NAV in the past 12 months.

12 months ending	Share price (%)	NAV (%)	NASDAQ Biotechnology (%)	MSCI World Healthcare (%)	FTSE All-Share (%)
30/09/14	52.4	43.6	38.3	32.6	12.2
30/09/15	44.5	31.1	13.7	5.5	(6.6)
30/09/16	2.2	(6.7)	(4.8)	5.0	(0.6)
30/09/17	36.9	27.7	15.7	12.8	15.4
30/09/18	15.7	0.3	11.4	15.9	3.9

Source: Thomson Datastream. Note: All % on a total return basis in Swiss francs.

Investment strategy: Clinical and financial focus

BION is managed by a team of six life-science specialists, headed by Dr Daniel Koller. The team builds a concentrated, high-conviction portfolio selected from a global universe of c 800 companies, looking for those that blend strong clinical and financial attributes with good management and return potential. Five to eight core holdings typically account for at least 50% of the portfolio.

Market outlook: Long-term positives, short-term risks

Biotech stocks continued to perform strongly in the first nine months of 2018, albeit with some stock-specific setbacks. Average valuations are no longer as compelling as in 2016, although individual pockets of value exist throughout the sector. While global equity markets have seen a sell-off in October, the long-term growth potential of biotech investment remains significant, underpinned by positive fundamentals.

Valuation: NAV dip causes premium to rise

At 24 October 2018, BION's shares traded at a premium of 11.1% to cum-income NAV, below the all-time high of 22.2% seen in early October, but well ahead of the one-year average premium of 7.1%. Over three, five and 10 years, BION's shares have traded at average discounts of 1.6%, 9.0% and 15.6%, respectively. While the recent increase in the premium was largely caused by flat to negative NAV performance (-5% in September) as the share price rose (+5%), the general rerating over recent years has been supported by the 5% annual distribution policy, index inclusion and a shift in the shareholder base.

25 October 2018

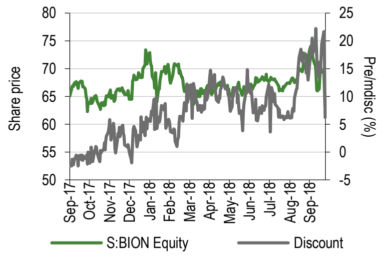
Price	**CHF63.05**
Market cap	**CHF3,493m**
AUM	**CHF3,288m**

NAV*	CHF56.75
Premium to NAV	11.1%

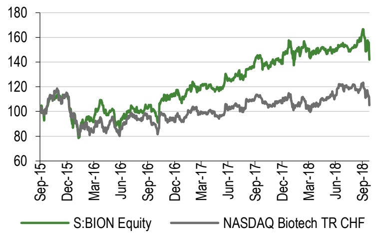
*Including income. As at 23 October 2018.

Yield	5.2%
Ordinary shares in issue	55.4m
Code	BION
Primary exchange	Zurich
AIC sector	N/A
Benchmark	NASDAQ Biotechnology (CHF)

Share price/premium performance



Three-year performance vs index



52-week high/low	CHF74.10	CHF62.30
NAV** high/low	CHF69.80	CHF56.75

**Including income.

Gearing

Gross*	9.2%
Net*	9.2%

*As at 30 September 2018.

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BB Biotech is a research client of Edison Investment Research Limited

Exhibit 1: Company at a glance

Investment objective and fund background

BB Biotech (BION) is a Switzerland-domiciled investment company, targeting long-term capital growth from biotechnology companies that are developing and marketing innovative drugs. At least 90% (currently 98.1%) of the portfolio is invested in listed companies, primarily mid-cap names that are already profitable. BION is benchmarked against the NASDAQ Biotechnology index (in CHF) but is managed bottom-up, with a concentrated 20–35 stock portfolio.

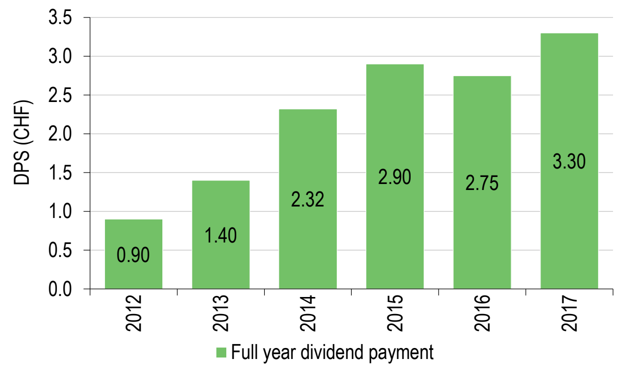
Recent developments

- 19 October 2018: Results for the three months ended 30 September 2018. Share price TR +7.8% in CHF, +9.4% in EUR and +8.8% in USD, versus NAV total returns of +7.3%, +8.9% and +8.3%, respectively. NASDAQ Biotechnology index +11.2% in USD terms.
- 20 July 2018: Results for the six months ended 30 June 2018. Share price TR +8.4% in CHF, +8.2% in EUR and +6.6% in USD, versus NAV total returns of -2.5%, -1.3% and -4.1%, respectively. NASDAQ Biotechnology index +2.9% in USD terms.

Forthcoming		Capital structure		Fund details	
AGM	March 2019	Total expense ratio	1.33% (30 September)	Group	Bellevue Asset Management
Annual results	15 February 2019	Net gearing	9.2% (30 September)	Manager	Team-managed
Year end	31 December	Annual mgmt fee	1.1% of market cap	Address	Seestrasse 16, 8700 Küsnacht, Switzerland
Dividend paid	March (out of capital)	Performance fee	None		
Launch date	November 1993	Company life	Indefinite	Phone	+41 44 267 67 00
Continuation vote	None	Loan facilities	See page 9	Website	www.bbbiotech.com

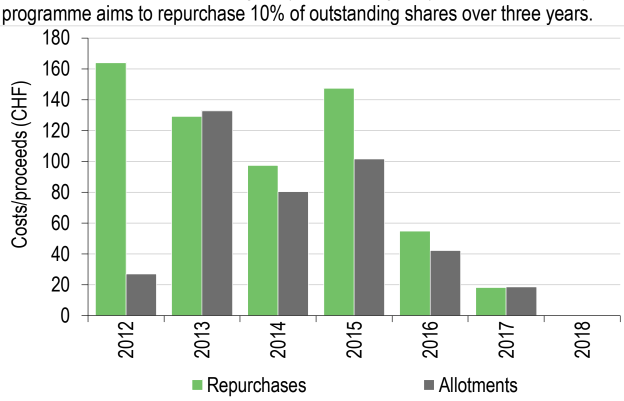
Dividend policy and history (financial years)

A new distribution policy was put in place from the year ended 31 December 2012, whereby BION makes a cash distribution equivalent to approximately 5% of its volume-weighted average December share price. Dividends restated to take account of five-for-one stock split in March 2016.

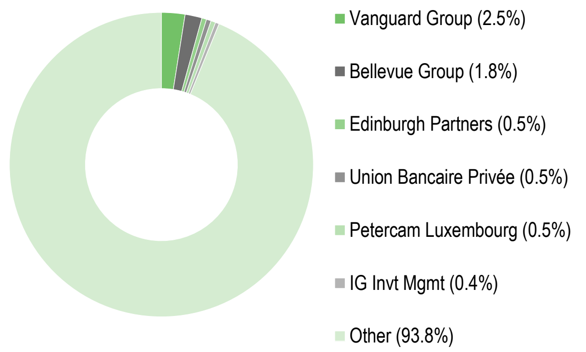


Share buyback policy and history (financial years)

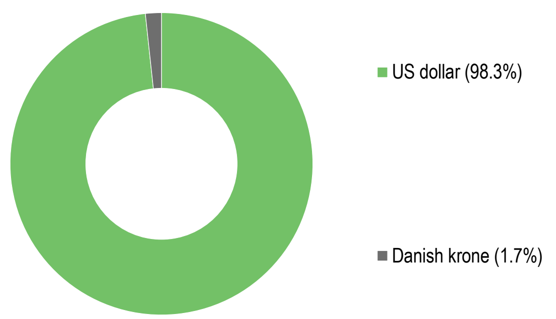
BION has the authority, renewed annually, to repurchase up to 10% of its issued share capital. As part of the distribution policy announced in 2012, it may return up to 5% of its share price through buybacks during the year. The current buyback programme aims to repurchase 10% of outstanding shares over three years.



Shareholder base (as at 31 May 2018)



Portfolio exposure by currency (as at 30 September 2018)



Top 10 holdings (as at 30 September 2018)

			Portfolio weight %	
Company	**Country**	**Main clinical focus**	**30 September 2018**	**30 September 2017**
Ionis Pharmaceuticals	US	Genetic diseases	11.4	10.5
Neurocrine Biosciences	US	Neurological diseases/women's health	9.9	5.6
Celgene	US	Oncology	6.8	12.2
Vertex Pharmaceuticals	US	Orphan diseases	6.7	5.9
Incyte	US	Oncology	6.7	11.2
Alexion Pharmaceuticals	US	Orphan diseases	4.7	5.0
Agios Pharmaceuticals	US	Oncology	4.3	4.8
Sage Therapeutics	US	Neurological diseases	3.9	1.8
Gilead	US	Infectious diseases	3.8	5.9
Halozyme Therapeutics	US	Oncology	3.8	3.9
Top 10 (% of portfolio)			**62.0**	**70.7**

Source: BB Biotech, Edison Investment Research, Bloomberg, Morningstar

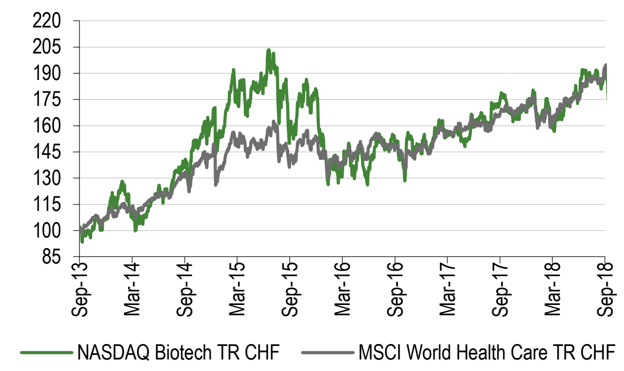
Market outlook: Fundamentals remain solid

Biotech and healthcare stocks have performed steadily and with less volatility since early 2016 (Exhibit 2, left-hand chart), and over five years Swiss franc-based investors would more or less have doubled their money in either sector, although the road for investors in the NASDAQ Biotechnology index has been a little bumpier than for those following the broader MSCI World Health Care index (c 16% of which is made up of biotech stocks). Healthcare stocks in general and biotech stocks in particular have benefited from a more accommodative regulatory regime, with fast-track approval for innovative treatments, as well as clinical successes driven by major advances in the understanding of disease processes and human biology. Demographic factors also underpin the investment case; with life expectancy increasing worldwide and growing prosperity outside the West, there is greater demand globally for treatments to address previously intractable health issues. Advances are beginning to be made in areas such as dementia, which is a growing problem in an ageing population where previously fatal conditions such as cancer and heart disease are increasingly treatable.

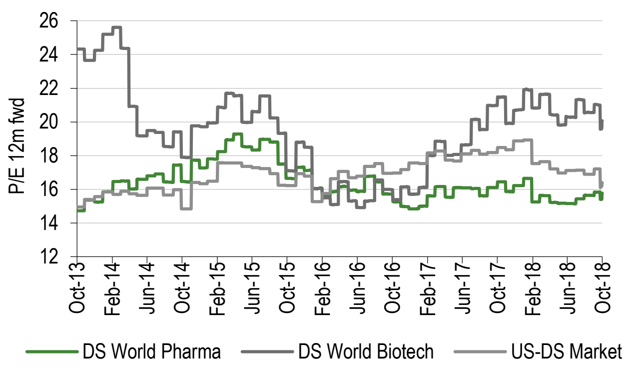
As shown in the right-hand chart, 12-month forward P/E valuations for biotech stocks have risen from the low levels of 2016 (when, unusually, they were below the forward P/E of both the pharmaceutical sector and the US stock market), and the 20.7x forward P/E for the Datastream World Biotechnology index is now c 3% above its five-year average, albeit c 19% below its five-year peak of 25.6x in March 2014. While the Datastream US and Datastream World Pharmaceutical indices may look more reasonably valued at forward P/E ratios of 16.4x and 15.8x, respectively, biotech valuations have held up better than those of the broad US index in the market volatility seen so far in 2018, suggesting that investors are more optimistic on their growth prospects. Biotech stocks may be vulnerable to swings in sentiment and tend to sell off in periods of risk aversion, but the positive industry fundamentals and the long-term growth of the sector (total returns of 312% in CHF terms for the NASDAQ Biotechnology index over 10 years to 30 September 2018, a period that includes some of the darkest days of the global financial crisis) suggest that patient investors may be well served by an allocation to the sector.

Exhibit 2: Biotech and healthcare market performance and valuations

Biotech and healthcare indices, total returns in CHF over five years



12m forward P/E valuations of pharma, biotech and US equity indices



Source: Thomson Datastream, Edison Investment Research. Valuation data at 18 October 2018, using Datastream indices.

Fund profile: Concentrated biotech specialist

BB Biotech (BION), launched in 1993, is a Switzerland-based specialist biotechnology fund that aims to achieve capital growth by investing in innovative biotech companies. Its primary (Swiss franc) listing is on the Swiss SIX Exchange, with secondary, euro-denominated listings in Germany and Italy. It has been included in the Stoxx 600 index of leading European shares since 2014, and as of 24 September 2018 is included in the SMIM index, which comprises the next 50 largest and most liquid companies listed in Switzerland after the 20 blue-chip constituents of the SMI index.

The fund has a concentrated portfolio of c 30–35 stocks (the official range is 20–35), with a bias towards fast-growing mid-cap names. There are usually five to eight core holdings that account for around half to two-thirds of the total (currently five companies and 41.5% of the portfolio, a lower level than average). The portfolio blends earlier-stage businesses with those that already have products on the market and are profitable, and may hold up to 10% of its assets (currently c 2%) in unlisted companies.

BION is managed by Bellevue Asset Management, a specialist healthcare investment manager headquartered in Switzerland, with portfolio managers based in Zurich and New York, and has an executive board of healthcare industry specialists who oversee major investment decisions. The fund uses the NASDAQ Biotechnology index (in Swiss francs) as a performance benchmark, although its focus on the mid-cap sector and its concentrated nature mean its portfolio weightings tend to diverge markedly from those of the index.

The fund manager: Bellevue Asset Management

The manager's view: More optimistic than the street

BION's lead manager Daniel Koller says that the dominant US biotech market is "full steam ahead" in terms of the industry and regulatory environments, with a business-friendly head at the Food and Drug Administration (FDA), and an ex-Eli Lilly executive now in charge of the Department of Health and Human Services (HHS). Koller argues that these developments, among others, lead the Bellevue team to have a more optimistic outlook for the sector than is the case within the wider investment community. "We will continue to rebalance our portfolio to focus on leading companies pursuing effective, safe and cost-effective treatments that can make a big difference to patients and healthcare systems," he adds. The recent FDA approval of the AbbVie/Neurocrine Biosciences endometriosis treatment elagolix (to be marketed as Orilissa) provides support for this view, as would the expected approval in Q418 of Sage Therapeutics' post-partum depression treatment, brexanolone (Zulresso). However, the regulator's 'refusal to file' in February 2018 for Celgene's multiple sclerosis candidate ozanimod has caused a 12–18 month setback for BION's third-largest holding, and indicates the FDA is prepared to be tough with companies that provide incomplete information. Koller says that while there is talk of the US midterm elections in November as the next potential big drawdown for the sector, the Bellevue team sees Donald Trump's protectionist trade wars as more significant.

Company-specific issues in the BION portfolio over the past 12 months have highlighted the long-term horizon necessary for investment in biotechnology. As well as the setback for Celgene (whose share price was down 19.5% year-to-date at 18 October), fifth-largest holding Incyte (-30.8% ytd) was badly hit by the Phase III failure of its cancer immunotherapy drug epacadostat in combination with Merck's Keytruda; Esperion (-24.7% ytd) suffered another filing delay for its cholesterol-lowering bempedoic acid; and Prothena (-67.0% ytd) was sold after its candidate for treating AL amyloidosis failed to meet its primary or secondary end points. Koller argues that Celgene still has a pipeline – he believes that ozanimod remains a good candidate, and the company is also developing a treatment for myelodysplastic syndrome in partnership with Acceleron. Meanwhile, he says, Incyte has support from products already on the market as well as further pipeline potential, and Esperion has suffered more from poor sentiment than poor prospects for bempedoic acid. Prothena suffered a straightforward failure and will have to start from scratch again, but "will be a completely different company in a year or two", at which point the Bellevue team may reassess it.

One area that has proved a disappointment so far in 2018 is mergers and acquisitions (M&A). "I am puzzled to see hardly any M&A if you exclude the big deals [Celgene's takeover of Juno Therapeutics, the purchase of AveXis by Novartis, and Sanofi's recent acquisition of Ablynx]," says Koller. He argues that while the market is expecting the primary driver of M&A to be cash repatriated as a result of recent US tax reforms, there is ample scope for large companies to make acquisitions to bolster their pipelines without waiting for overseas cash to arrive. The manager points out that although big pharma companies may cynically make bids around key political events such as elections, when biotech stock prices may be depressed, in the main it pays acquirers not to wait. "Deals are becoming more expensive," says Koller. "Roche made a [failed] bid for Illumina at $48 a share in 2012, and it is now at $360. It feels like a lot of companies are talking about M&A – AbbVie has said it has a $20-30bn war chest – but I don't know why they don't act."

This is made more puzzling, the manager says, by the current low level of some biotech company valuations. "Valuations are rock-bottom for large-caps, and for small and mid-caps, our price targets in many cases are multiples of the current price," he explains. Koller says big biotech company valuations tend to be modelled out on one or two marketed products, with no residual value when patents expire, and no credit is given for new product development or potential pipeline-bolstering acquisitions. He points out that if big pharma company valuations were modelled on the same basis, their valuations would be even lower. However, the arguably lesser growth potential and poorer performance record of big pharma mean investors do not see the sector as an irresistible bargain: "Particularly in continental Europe, investors are making a shift from big pharma, which has underperformed for years," says Koller. "It resonates with them more loudly these days that large-cap is not the space to be in, and BION is seen as one of the potential alternatives when people do not dare to go into single names."

Asset allocation

Investment process: Focused and specialist approach

BION's portfolio management team is made up of six investment professionals with a variety of scientific specialisms. The head of the team, Dr Daniel Koller, has been involved with BION's management since 2004. An understanding of the clinical landscape is fundamental to the fund's investment approach, and in order to achieve this, the managers spend time monitoring medical journals, attending industry conferences, and meeting clinicians and biotech company executives.

The fund's investment universe numbers c 800 established and developing biotech companies globally, and BION's managers focus on those clinical areas where scientific advances coincide with strong market potential, in order to filter the opportunity set to c 300-400 companies. This is further refined to a 'long list' of c 150 potential investments by applying a variety of quantitative and qualitative screens. The managers then assess candidate stocks for factors such as innovation, intellectual property ownership (there is a strong preference for wholly owned assets), pharmacoeconomics and quality of management. Screening criteria are weighted towards clinical factors, although the team also builds detailed financial models, and prefers to invest in companies that have the potential to achieve above-average growth in sales and profits.

An investment proposal is produced for companies that make it through all the stages of the process, including clinical data, financial models, estimates of potential upside/downside, and recommendations on purchase price and position size. The team presents the proposals to the executive board, which signs off on all new positions, exits and major changes in weighting. The size range for a new position is c 0.5-4.0% of the portfolio, with earlier-stage companies tending to be at the lower end of the range. BION's portfolio is made up of c 30-35 companies, drawn from around the world and representing a wide range of market capitalisations and development stages. There is a heavy bias towards the US, as this is the base for most of the world's biotechnology companies. The portfolio is concentrated, with five to eight core holdings (currently five) accounting for around half to two-thirds of total assets. There is a strong sell discipline; holdings may be trimmed to keep positions from becoming too large, or sold completely if they reach valuation targets, or if the original investment thesis is called into question by poor clinical data or regulatory setbacks.

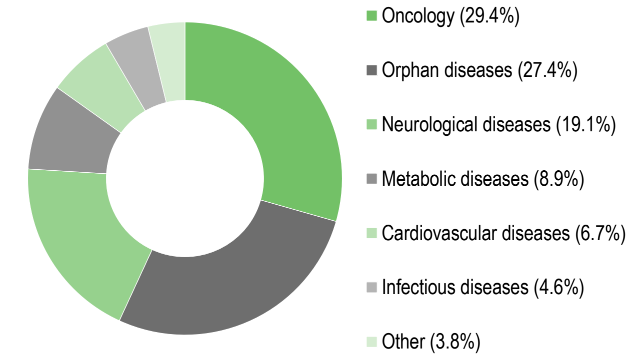
Current portfolio positioning

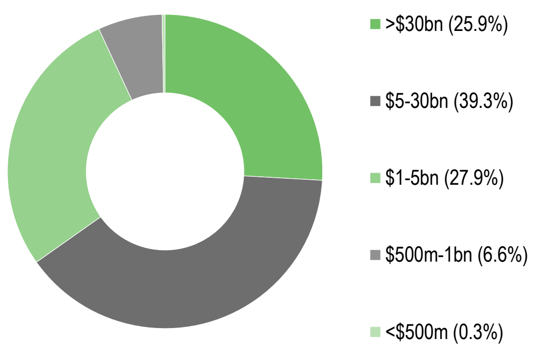
At 30 September 2018, there were 34 companies in BION's portfolio, up from 33 at the 31 December 2017 year-end and towards the top end of the indicative 20-35 stock range. Concentration in the top 10 holdings (see Exhibit 1, page 2) has fallen from c 70% to c 60% over the past 12 months. The top five positions are currently viewed as the core holdings. While oncology remains the largest clinical area (Exhibit 3, left-hand chart), exposure to this indication has fallen by 10.6pp over the last 12 months, with neurological disease exposure rising by 9.7pp. An emerging focus that spans several disease categories is RNA-based therapies, which BION said made up 19% of the portfolio at the end of Q118. BION remains biased towards small- and mid-caps (right-hand chart), with liquid large-cap holdings such as Gilead (the ninth-largest position) seen more as a potential source of funds to invest in new ideas, although gearing may also be used to fund new positions.

Ten new holdings have been added to the portfolio in the past 12 months, with seven complete exits. Juno Therapeutics and AveXis were taken over, respectively by Celgene in Q118, and Novartis in Q218. The long-standing holding in Swedish Orphan Biovitrum was sold in Q417 at a substantial profit, while in Q218 a small position in Actelion spinoff Idorsia was also exited at a profit, and the holding in Prothena was sold after the failure of its lead candidate for AL amyloidosis in a Phase IIb trial. Residual positions in Five Prime Therapeutics and Probiodrug were sold in Q318.

Three of the new holdings – Akcea Therapeutics, Wave Life Sciences (both added in Q417) and Moderna Therapeutics (added in Q118) are involved in RNA-based therapies. Akcea (an affiliate of BION's largest holding, Ionis Pharmaceuticals), which is focused on rare diseases, and Wave, which specialises in neurological disorders, both use RNA to inhibit the expression of disease-causing proteins. Conversely, Moderna, a rare investment in a private company, is developing a technology platform to use messenger RNA as a medicine to transport information into cells to produce proteins, "effectively switching on a patient's machinery to build new proteins," says Koller. It is targeting a variety of indications in oncology, infectious diseases, liver disorders and cardiovascular diseases.

Exhibit 3: Portfolio distribution by clinical focus (left) and market capitalisation (right)





Source: BB Biotech, Edison Investment Research. Note: As at 30 September 2018.

Other new holdings include small-molecule oncology specialists G1 Therapeutics and Exelixis (both added in Q218), neurology-focused gene therapy play Voyager Therapeutics (added in Q417), platform company Nektar Therapeutics, targeting a range of indications in oncology, autoimmune disorders and chronic pain (Q218), Argenx, active in antibody therapeutics for autoimmune diseases and cancer (Q118), and Myokardia, which is developing a precision medicine approach to treating rare genetic cardiovascular disorders (Q218). One new investment, in growth factor specialist Scholar Rock, was initiated in Q318. The initial indication for its lead compound SRK-015 is in late-onset spinal muscular atrophy and BION says it may also target anaemia in 2019 with another compound, BMP6.

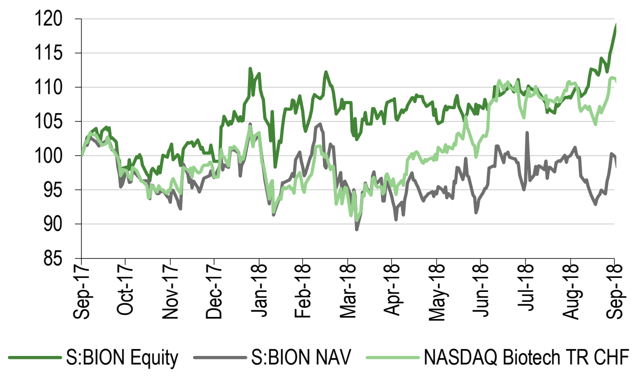
While BION's geographical exposure by currency remains overwhelmingly tilted towards the US (see Exhibit 1 – US dollar investments were 98.3% of the portfolio at 30 September 2018), one of the new holdings, Argenx (1.6% of the BION portfolio at 30 September 2018) is a Belgian company, which trades in the US through an American depositary receipt (ADR). Koller comments that new positions tend to come into the portfolio at 0.5-2.0%, with the team waiting to see how milestones develop before topping up holdings. The Q417 investments in Akcea and Wave have been added to since their initial purchases, and respectively made up 2.3% and 1.9% of the BION portfolio at 30 September 2018, compared with 0.6% and 0.8% respectively at 31 December 2017. In Q318 BION also added to its new investments in Argenx, Exelixis and Nektar, which now collectively make up 4.5% of the portfolio, compared with 2.3% at 30 June 2018.

BION's managers generally prefer companies that develop and commercialise their own products, rather than in-licensing or out-licensing, where either the intellectual property is not wholly owned, or the potential revenues will be shared with another party. While some companies with platform technologies may not be developing their own products, Koller says that many begin with licensing but their ultimate goal is their own commercial products. Having a platform (as is the case with holdings including Ionis, Alnylam, Macrogenics and Moderna) means there tends to be a larger known pipeline of products, which reduces risk compared with companies with a single lead candidate, such as Prothena.

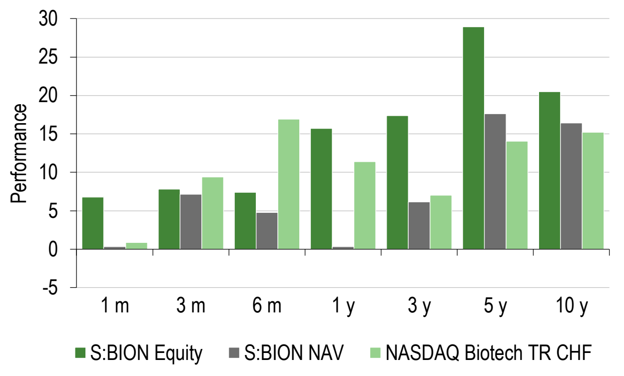
Performance: Recovering from short-term NAV dip

Exhibit 4: Investment company performance (in CHF terms) to 30 September 2018

Price, NAV and benchmark total return performance, one-year rebased



Price, NAV and benchmark total return performance (%)



Source: Thomson Datastream, Edison Investment Research. Note: Three, five and 10-year performance figures annualised.

While BION's share price performance has been well ahead of the benchmark NASDAQ Biotech index over one, three, five and 10 years (Exhibit 4), NAV performance has been less positive in both relative and absolute terms over periods of three years and less. This has largely been driven by company-specific events at some of BION's core holdings, such as poor performance by Celgene in late 2017, and a major clinical trial failure by Incyte early in the second quarter of 2018. In the third quarter, the market was underwhelmed by developments at key BION holdings Radius Health, Alnylam and Tesaro. The manager points out that large, short-term swings in one direction or another are a natural outcome of running a concentrated portfolio in a volatile sector, but that BION's solid record of medium- to long-term share price and NAV performance has come about by sticking to its strategy. As shown in Exhibit 5, over five and 10 years (and three years for the share price), BION has beaten the NASDAQ Biotech and MSCI World Health Care indices by a substantial margin, as well as massively outperforming the UK FTSE All-Share index (all in CHF terms). BION's share price has substantially outperformed the index in September and October to date, buoyed by investor demand as a result of its inclusion in the Swiss SMIM and SPI indices.

Exhibit 5: Share price and NAV total return performance (in CHF terms), relative to indices (%)

	One month	Three months	Six months	One year	Three years	Five years	10 years
Price relative to NASDAQ Biotech	5.8	(1.5)	(8.1)	3.9	31.9	84.8	56.8
NAV relative to NASDAQ Biotech	(0.6)	(2.0)	(10.4)	(10.0)	(2.5)	16.8	11.1
Price relative to MSCI World Health Care	3.6	(1.8)	(8.3)	(0.1)	17.9	85.6	131.4
NAV relative to MSCI World Health Care	(2.7)	(2.4)	(10.6)	(13.4)	(12.9)	17.3	64.0
Price relative to FTSE All-Share	4.6	11.9	4.6	11.4	35.8	185.4	324.7
NAV relative to FTSE All-Share	(1.7)	11.2	2.0	(3.4)	0.4	80.4	201.0

Source: Thomson Datastream, Edison Investment Research. Note: Data to end September 2018. Geometric calculation.

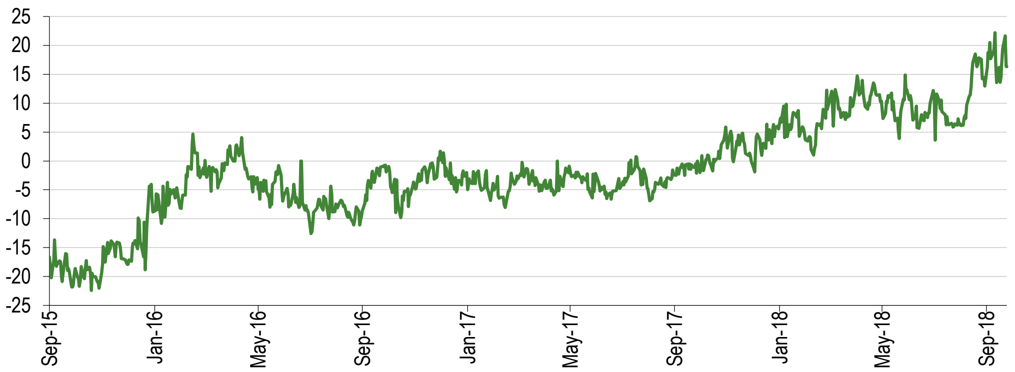
Exhibit 6: NAV total return performance relative to benchmark (in CHF) over five years

Source: Thomson Datastream, Edison Investment Research

Discount: Moving to a premium in recent months

Having traded close to par since mid-2016, BION's shares have moved to a premium to NAV in recent months, reaching an all-time high of 22.2% on 10 October 2018. At 24 October 2018 the premium was 11.1%. This compares with an average premium of 7.1% over one year, and average discounts of 1.6%, 9.0% and 15.6% respectively over three, five and 10 years. Index inclusion (first in the Stoxx 600 index in 2014, and more recently in the Swiss SMIM and SPI indices) has been instrumental in the move from a persistent discount to NAV, to the current high level of premium. Koller explains that the shareholder register now includes more committed long-term holders who like BION's investment story and high distributions, and fewer discount-focused investors. This has meant that in the more difficult recent period of stock market performance, the share price has held up while the NAV has been flat to negative, causing a premium to the value of the underlying assets.

Exhibit 7: Share price premium/discount to NAV (including income) over three years (%)



Source: Thomson Datastream, Edison Investment Research

Capital structure and fees

BION is a closed-end investment company, incorporated in Switzerland with a primary listing on the SIX Swiss Exchange and secondary, euro-denominated listings in Germany and Italy. It has 55.4m shares in issue, following a five-for-one stock split in March 2016. A buyback authority is in place whereby it can repurchase up to 10% of the shares; to date (since it was put in place in 2016), this facility has not been used. Gearing is available via a short-term loan at an interest rate of 0.40% a year, of which CHF325m was drawn at 30 September 2018, equivalent to c 9.3% of net assets. (Reported gearing at 30 September was 9.2%).

Bellevue Asset Management is paid an all-in management fee of 1.1% a year, with no performance fee. The total expense ratio at 30 September 2018 (Q318) was 1.33% (FY17: 1.24%).

Dividend policy and record

The biotechnology sector contains many companies that are at an early stage of developing treatments and may be several years away from making a profit. Even for those that have products on the market and generating revenues, the focus may be more on growth than on rewarding shareholders through dividends. However, as capital growth from holdings can be significant, BION has a longstanding policy of paying out part of this as an annual distribution to shareholders, equal to 5% of its market capitalisation based on the volume-weighted average share price in December. In respect of FY17, a distribution of CHF3.30 was paid to shareholders in March 2018, a 20% increase on the CHF2.75 paid in respect of FY16. Distributions may rise or fall from one year to the next because of the volatile nature of the biotech sector combined with the fixed percentage distribution policy, but over five years to FY17, BION's annual distribution has grown at a compound rate of 29.7% (adjusting for the FY16 stock split). Based on the current share price and the FY17 distribution, BION has a yield of 5.2%, comfortably the highest in its peer group.

Peer group comparison

Exhibit 8: Biotech and healthcare peer group (in CHF terms) as at 24 October 2018*

% unless stated	Market cap £m	NAV TR 1 year	NAV TR 3 year	NAV TR 5 year	NAV TR 10 year	Ongoing charge	Perf. fee	Discount (ex-par)	Net gearing	Dividend yield
BB Biotech AG	**3,493.0**	**(11.2)**	**3.6**	**109.2**	**352.6**	**1.3**	**No**	**16.3**	**109**	**5.2**
BB Healthcare	532.5	17.8	--	--	--	1.4	No	5.2	106	3.0
Biotech Growth Trust	490.3	(13.0)	(1.9)	57.3	358.3	1.1	Yes	(4.0)	113	0.1
HBM Healthcare Investments AG	1,282.8	13.8	60.2	136.7	141.7	1.2	Yes	(5.0)	100	4.2
International Biotechnology Trust	291.3	0.5	11.9	88.2	225.3	0.9	Yes	1.7	100	4.5
Polar Capital Global Healthcare	333.0	9.7	19.9	54.3	--	1.4	Yes	(5.6)	100	1.6
Syncona	2,130.1	18.2	42.0	62.1	--	1.6	No	29.7	100	0.9
Worldwide Healthcare Trust	1,700.9	0.9	29.9	102.3	290.0	0.9	Yes	4.7	110	0.7
Peer group average	**1,281.7**	**4.6**	**23.7**	**87.2**	**273.6**	**1.2**		**5.4**	**105**	**2.5**
BION rank in sector	**1**	**7**	**6**	**2**	**2**	**4**		**2**	**3**	**1**

Source: Morningstar, Edison Investment Research. Note: *Performance to 22 October 2018. TR=total return. Net gearing is total assets less cash and equivalents as a percentage of net assets (100 = ungeared).

In Exhibit 8 above we show BION in a peer group that includes the members of the AIC specialist Biotech & Healthcare sector, as well as Switzerland-listed HBM Healthcare Investments. The group contains a mix of biotech specialists and healthcare generalists. In terms of short- to medium-term performance, the biotech funds have lagged the healthcare funds, although over the long term the biotech specialists have generally done better. In line with this trend, BION's NAV total returns are below the sector average over one and three years (ranking seventh of eight and sixth of seven funds respectively), but above average over five and 10 years (ranking second of seven and a close second of five). Ongoing charges (which BION expresses as a total expense ratio) are a little above average, but BION is one of only three peers without a performance fee. The level of gearing is above average, while the dividend yield is comfortably the highest in the group. Possibly as a result of the high yield as well as the strong long-term performance record, BION currently trades at a premium to NAV, while most of the peers (with the notable exception of Syncona, at a 29.7% premium) trade close to par or at a discount.

The board

There are currently three directors on BION's executive board, all of them highly qualified industry specialists. Dr Erich Hunziker, a former CEO of Roche, has served on the board since 2011 and was appointed chairman in 2013. The longest-serving director (appointed in 2003) is Dr Clive Meanwell, founder and CEO of The Medicines Company. Professor Dr Klaus Strein joined the BION board in 2013 and has held senior R&D roles at Roche and Boehringer Mannheim. The directors sign off on major investment decisions, although day-to-day portfolio management is Bellevue's responsibility. On 19 October, BION announced it will propose Dr Thomas von Planta for election to the board at its next shareholder meeting in March 2019, increasing the number of directors to four. Dr von Planta's background is in investment banking and he is currently the chairman of the board of Bellevue Group, a position from which he will retire before joining BION's executive board.

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