

BioPharma Credit

Reinvesting proceeds from loan prepayments

BioPharma Credit (BPCR) has recently made good progress in deploying its cash balance due to drawdowns of second tranches of senior secured loans provided to Sarepta Therapeutics and Global Blood Therapeutics and funding of an additional tranche to Epizyme. Meanwhile, the trust has delivered a solid three-year NAV total return (TR) to end-October 2020 of c 8% per year and its targeted dividend is covered in the near term.

Proceeds from recent prepayments partially deployed

In recent months, BPCR has received three large loan prepayments, including Amicus Therapeutics (US\$150m), Novocure (US\$150m) and Lexicon Pharmaceuticals (US\$124.5m). As a result, its cash balance at end-October 2020 reached US\$538.3m (or c 39% of NAV). However, the recent drawdowns and additional Epizyme investment should reduce BPCR's end-October 2020 cash figure to c US\$250m. The trust also has some minor US\$21.0m outstanding commitments to fund additional tranches as part of existing loan agreements.

Dividend covered by income in the near term

We estimate that BPCR's cash balance still represents around 18% of its NAV. We believe it has to deploy part of it to cover its dividend payments from recurring coupon/royalty income in the long run. However, we estimate that the recently earned 'make-whole' and prepayment fees, together with BPCR's revenue reserve, provide full dividend cover until at least end-Q121. We also note BPCR was able to increase the funding fee on the second Sarepta Tranche from 1.75% to 2.95% and the additional Epizyme tranche has similar terms to the previous tranches. This suggests BPCR is still able to pursue deals on attractive terms in line with its previous investments.

Returns remaining intact in the short term

BPCR's 12-month NAV TR to end-October 2020 reached 6.8%, which compares with the Credit Suisse HY Index at -10.2%. Here it is important to flag that while BPCR's loan investments are carried at fair value, they are not actively traded in the market. We also note that BPCR's three-year NAV TR in sterling terms (29.5%) is clearly ahead of the average for listed debt funds included in the AIC sectors direct lending (13.1%) and loans and bonds (-3.5%). BPCR's shares trade close to the trust's NAV per share and offer a c 7% dividend yield (excluding the last special dividend), in line with its target.

Investment trusts
Debt: direct lending

24 November 2020

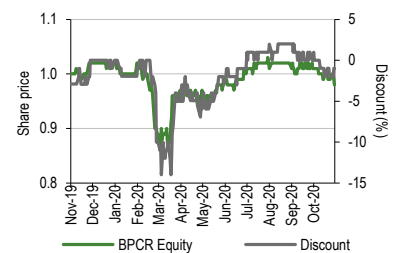
Price US\$0.98
Market cap US\$1,346.4m
NAV* US\$1,389.4m

Premium/(discount) to NAV (3.3%)

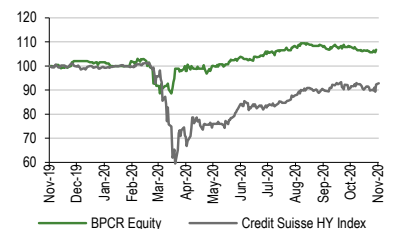
*As at end-September 2020

Yield 8.4%
Ordinary shares in issue 1,373.9m
Code BPCR
Primary exchange LSE
AIC sector Debt – Direct Lending
Benchmark N/A

Share price/discount performance



Three-year performance vs index



52-week high/low US\$1.03 US\$0.86

NAV** high/low US\$1.03 US\$1.00

**Including income.

Gearing

Gross* 0.0%

Net cash* 39%

*As at end-September 2020.

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Exhibit 1: Company at a glance

Investment objective and fund background

BioPharma Credit was incorporated in the UK in October 2016 and aims to generate predictable income for shareholders over the long term through a diversified portfolio of loans and other instruments backed by royalties or other cash flows derived from sales of approved life sciences products. This includes senior secured notes, royalty debt instruments and priority royalty tranches. BPCR may also invest in unsecured debt (up to 35% of gross assets) as well as credit-linked notes. It can also have an equity exposure of up to 15% of GAV.

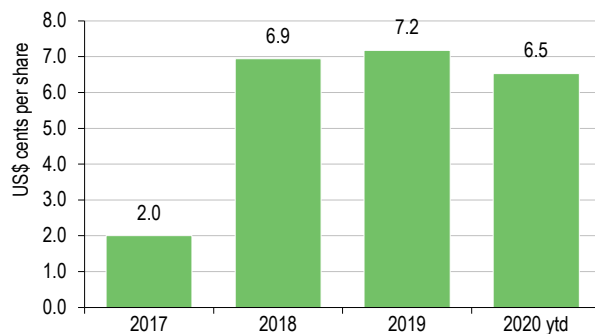
Recent developments

- 9 November 2020: additional debt investment in Epizyme
- 28 September 2020: amendment to Sarepta Therapeutics loan agreement
- 16 September 2020: half-year report and appointment of Rolf Soderstrom as a new non-executive director
- 9 September 2020: Lexicon Pharmaceuticals loan prepayment
- 7 August 2020: Novocure notice of prepayment and GBT notice of intention to draw the second tranche

Forthcoming		Capital structure		Fund details	
AGM	June 2021	Ongoing charges	1.2% (LTM ending June 2020)	Group	BioPharma Credit
Final results	March 2021	Net gearing	None	Manager	Pharmakon Advisors
Year end	31 December	Annual mgmt fee	1.0% of NAV less US\$100k	Address	110 East 59th Street 3300, New York, NY 10022
Dividend paid	Quarterly	Performance fee	10% of NAV accretion	Phone	+1 (212) 883-1006
Launch date	24 October 2016	Company life	Indefinite	Website	www.bpcruk.com
Continuation vote	2022	Loan facilities	US\$200m (undrawn)		

Dividend policy and history (calendar years)

BPCR pays quarterly dividends in US dollars and aims to pay a US\$0.07 annualised dividend per share and deliver a 7% dividend yield for investors. During 2020, total DPS so far has amounted to 6.53c, which included a special dividend of 1.28c.



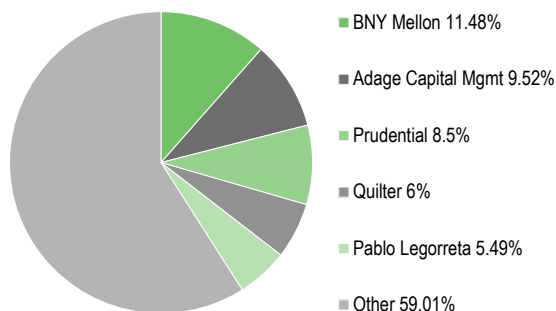
Share buyback policy and history

BPCR's board may perform share buybacks to limit the discount volatility and potentially provide an additional source of liquidity at attractive price levels. If the shares trade at an average discount over 5% (10% during a three-month (six-month) rolling period, subject to meeting its target dividend, the trust will use 50% (100%) of capital and income proceeds generated after this rolling period for buybacks, at least until the shares start trading at an average discount of 1% or less to NAV over a two-week rolling period. The company has activated its discount control mechanism in June 2020, repurchasing 59,694 shares (representing 0.004% of its issued share capital).

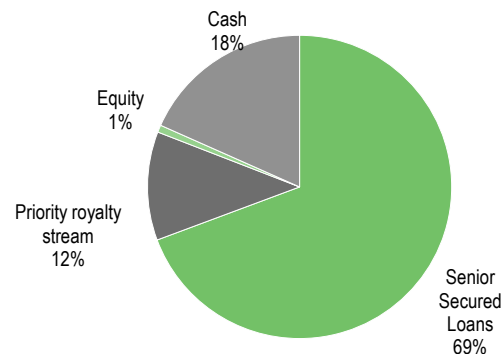
If, during the last month of a performance period, BPCR's shares have, on average, traded at a discount of 1% or more to the NAV per share, BPCR's investment manager shall use 50% of any performance fee paid by BPCR for share buybacks until the shares have, on average, traded at a discount of less than 1% to NAV per share over a period of five business days.

BPCR is authorised to execute share repurchases up to 14.99% of total shares in issue immediately after admission from the date of the resolution and the first AGM.

Shareholder base (at 11 November 2020)



Portfolio exposure by security type (at 23 November 2020*)



Holdings (at 31 October 2020)

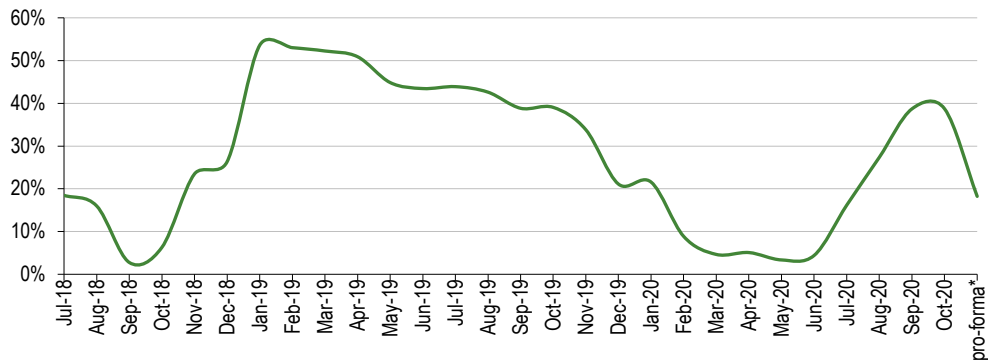
Company/borrower	Security type	Key underlying products	% of NAV	
			31 Oct 2020	31 Oct 2019**
Sarepta Therapeutics	Senior secured loan	Exondys 51, Vyondys 53	13%	N/A
Bristol Myers Squibb	Priority royalty stream	Onglyza, Farxiga	12%	9%
Collegium Pharmaceutical	Senior secured loan	Xtampza, Nucynta	10%	N/A
Sebela Pharmaceuticals	Senior secured loan	Suprep, Brisdelle, Analpram, Naftin, Lotronex	7%	11%
BDSI	Senior secured loan + equity	Belbuca, Bunavil, Symproic	6%	6%
Optinose	Senior secured loan	Xhance, Onzetra	4%	3%
Global Blood Therapeutics	Senior secured loan	Oxbryta	3%	N/A
Akebia Therapeutics	Senior secured loan	Auryxia	3%	N/A
Epizyme	Senior secured loan	Tazverik	3%	N/A
Total			61%	61%

Source: BioPharma Credit, Edison Investment Research, Bloomberg. Note: *including November drawdowns. **N/A where not in end-September 2019 top 10.

Recent good progress in cash deployment

After BPCR entered a definitive agreement to provide a US\$165m single-tranche senior secured loan to Collegium Pharmaceutical in February 2020 and funded all the purchased payments related to its Bristol-Myers Squibb royalties, its new investment activity became muted for several months (BPCR only funded the second US\$20m BDSI tranche in May), as the trust was close to being fully invested (see Exhibit 2). Meanwhile, three of its existing loans (Amicus, Novocure and Lexicon) with an aggregate volume of US\$424.5m have been prepaid since July 2020, which (together with the Sebelo and Collegium Pharmaceutical loan amortisation) brought BPCR's cash position to US\$538.3m at end-October 2020 (39% of NAV).

Exhibit 2: BioPharma Credit's cash position as % of NAV



Source: Company data; Note: *After accounting for the Sarepta and Global Blood Therapeutics drawdowns, as well as the additional Epizyme tranche.

More recently, however, BPCR made good progress in its cash deployment, with the drawdown of the second tranche of the Sarepta (US\$175m, with a higher funding fee at 2.95%) and Global Blood Therapeutics (US\$41.3m) loans. Both tranches have been funded in November 2020. Furthermore, in November BPCR and BioPharma V fund agreed to provide an additional US\$150m tranche to Epizyme (with US\$75m attributable to BPCR). BioPharma Credit made the initial senior secured loan investment in Epizyme in November 2019 and subsequently funded two further tranches following the FDA approval of TAZVERIK (an oral EZH2 inhibitor for selected oncology indications, which is Epizyme's lead product) for treating epithelioid sarcoma and follicular lymphoma. The new tranche has been drawn in full on 18 November 2020 and has the same coupon and fees as the previous ones (coupon rate LIBOR +7.75% and funding fee of 2.0%). It brings BPCR's total investment in Epizyme to US\$110m (with a further US\$110m provided by BioPharma V). The facility remains expandable by up to an additional US\$150m, subject to mutual agreement between the lenders and Epizyme. Additionally, BPCR has already received or is due to receive funding fees from Sarepta, GBT and Epizyme (c US\$7.2m in total by our calculations).

We estimate that as a result of all the above, BPCR's cash position will be reduced to nearly US\$250m (c 18% of NAV). In Exhibit 3, we present BPCR's pro-forma portfolio composition at end-October 2020. We note that BPCR has outstanding commitments to fund additional tranches as part of existing loan agreements (which could bring BPCR's cash down further) of US\$21.0m, including Akebia (US\$10.0m available until end-2020) and OptiNose (US\$11.0m available until September 2021).

Exhibit 3: Pro-forma portfolio composition*

Counterparty /borrower	Asset	Underlying products	Fair value (US\$m)	Expected maturity	Coupon/royalties	Fees and other	% of net assets
Sarepta Therapeutics	Senior secured loan	Exondys 51, Vyondys 53	350.0	Tranche A (US\$175m) December 2023; Tranche B (US\$175m) December 2024 Make-whole: 2 years	8.5% (fixed)	Funding fee 1.75%/2.95% (tranche A/B); exit fee 2%; prepayment fee at 2% on or prior to the third anniversary and 1% thereafter	25%
Bristol-Myers Squibb	Priority royalty stream	Onglyza, Farxiga	162.0	31 December 2059 or such other date TBA	No coupon; Expected high single-digit return	N/A	12%
Collegium Pharmaceutical	Senior secured loan	Xtampza, Nucynta	144.4	February 2024	Libor 3M + 7.5% (2.0% Libor floor)	Funding fee 2.5%	10%
Epizyme	Senior secured loan	Tazverik (Tazemetostat)	110.0	Tranche A (US\$12.5m), B (US\$12.5m), and C (US\$10m) November 2024; Tranche D (US\$75m) November 2026	Libor + 7.75%	Funding fee 2%; subject to certain prepayment and make-whole fees. Quarterly amortisation starts around four years since drawdown of each tranche	8%
Sebel	Senior secured loan	Suprep, Brisdelle, Analpram, Naftin, Lotronex	101.6	December 2022	High single-digit floating coupon (uncapped)	Quarterly amortisation starts post-Q318; funding fee 1.5%; other fees were not disclosed, but are in line with comparable deals according to BPCR	7%
BDSI	Senior secured loan (US\$80m) + equity	Belbuca, Bunavail, Symproic	88.5	28 May 2025	Libor 3M + 7.5%	Amortisation: 30 months interest only, then quarterly; funding fee 2%; prepayment fee not disclosed but in line with comparable deals according to BPCR	6%
Global Blood Therapeutics	Senior secured loan	Oxbryta	82.5	December 2025	Libor 3M + 7% (2.0% Libor floor)	Funding fee 1.75%; exit fee of 2%	6%
OptiNose	Senior secured loan	Xhance, Onzetra	60.7	12 September 2024	10.75% (fixed)	Amortisation: 39 months interest only, then quarterly; funding fee 0.75% of drawn and undrawn + three-year warrants on OptiNose shares at zero cost; prepayment fee not disclosed but in line with comparable deals according to BPCR	4%
Akebia	Senior secured loan	Auryxia	40.0	November 2024; Make-whole: 2 years	Libor 3M + 7.75% (2.0% Libor floor)	Funding fee 2%; prepayment fee at 2% and 1% prior to the third and fourth anniversary and 0.5% thereafter	3%
Cash and other	-	-	256.4**	-	-	-	18%

Source: BioPharma Credit, Edison Investment Research; Note: *Accounting for the Sarepta and Global Blood Therapeutics drawdowns, as well as the additional Epizyme tranche. **Edison estimate.

Dividend fully covered in the near term

We have examined the extent to which BPCR's income from recent transactions and its current investment portfolio covers the targeted dividend payout. BPCR aims to deliver an annualised dividend of 7c per share (paid quarterly), which implies a payout of c US\$96.2m per year (US\$24.0m per quarter). At the same time, its operating expenses stand at US\$2.2m pa (c 0.2% of average NAV) based on LTM (last 12 months) results at end-June 2020. Furthermore, the trust pays a management fee of 1% of NAV less US\$100,000 (paid quarterly), which based on BPCR's last reported NAV implies c US\$13.8m per year. On top of this, BPCR pays a performance fee at 10% NAV accretion subject to a hurdle rate of 6%. Finally, BPCR entered a US\$200m credit facility agreement with JPMorgan Chase Bank in May 2020 that remains undrawn but involves a non-utilisation fee of 200bp (or US\$0.4m pa).

Consequently, we estimate that to sustain its dividend policy, BPCR has to generate an income of at least US\$113m per year (excluding any performance fee). We also estimate that based on its current pro-forma portfolio at end-October 2020 (after reflecting the drawdown of the second Sarepta Therapeutics and Global Blood Therapeutics tranches and the additional investment in

Epizyme), BPCR now generates a coupon/royalty income (including amortised funding fees) of c US\$100–105m, with a weighted average coupon rate on its loan portfolio close to c 9%. In this context, we note that at least c 70% of its investments have a fixed coupon rate or a floating rate based on USD LIBOR, but subject to a floor (normally at 2.0%).

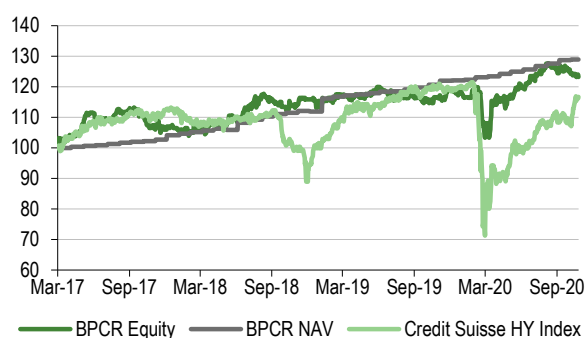
While we believe BPCR needs to deploy at least part of its remaining cash for its portfolio income to fully cover its dividend in the long run, we note it has received make-whole and prepayment fees of US\$13.6m in total from three loan prepayments in recent months (Amicus, Novocure and Lexicon). We estimate that after accounting for a performance fee in FY20 (calculated assuming no further deals and in line portfolio performance), as well as BPCR's revenue reserve at end-June 2020 (US\$14.9m), this should cover the income shortfall at least until the end of Q121. Consequently, we believe BPCR has a relatively comfortable position to gradually deploy its remaining dry powder in the coming months to maintain full dividend cover based on recurring coupon/royalty income.

Performance: Solid return of c 8% pa over three years

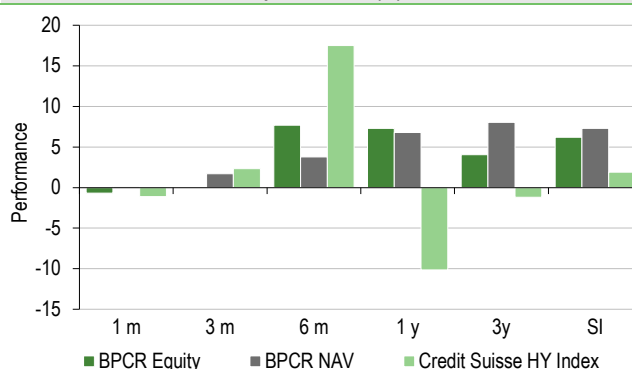
BPCR's NAV TR over the 12 months ended October 2020 is 6.8% (in US\$ terms), which is slightly below the targeted 8–9% NAV TR. We note, however, this covers Q419 when BPCR had a significant cash drag (cash as percentage of NAV at 20–40%, see Exhibit 2). This followed a large Tesaro prepayment in January 2019, which generated significant make-whole and prepayment fees (resulting in an IRR of 28.8%, see our [previous note](#) for details). BPCR's three-year NAV TR is 8% per year (in line with target) and its year-to-date NAV TR to end-October 2020 reached c 5.6%, which includes the make-whole and prepayment fees received from Amicus, Novocure and Lexicon.

Exhibit 4: Investment trust performance to 31 October 2020

Price, NAV and benchmark TR performance, since IPO rebased



Price, NAV and benchmark TR performance (%)



Source: Refinitiv, Edison Investment Research. Note: Since IPO and three-year performance figures annualised. Inception date is 24 October 2016. BPCR equity performance measured based on ordinary shares.

Peer group comparison

As we have not identified any close listed peers for BPCR, we compare its performance against two broader AIC sectors: direct lending and loans and bonds (see Exhibit 5), which contain funds with a wide variety of credit investment strategies, although none focuses on the life sciences credit market. Nevertheless, we believe these are a reasonable reference point in terms of the performance of the broader corporate debt market.

BPCR's one-year NAV TR in sterling terms of 6.9% is ahead of the direct lending peer group average of 3.4%, and clearly ahead of the loans and bonds peer group (average return of -6.3%). We note that while BPCR's loan investments are carried at fair value, they are not actively traded in

the market (as opposed to investments held by several peers within the loans and bonds peer group) and thus are revalued only in response to triggers at underlying companies (with no impact from market sentiment). More importantly, however, BPCR's three-year NAV TR of 29.5% is clearly ahead of both the direct lending (13.1%) and loans and bonds (-3.5%) peer group average. In this context, we note that BPCR recently won the Debt category for investment company of the year 2020 (from Investment Week in association with the AIC).

Exhibit 5: Selected peer group at 23 November 2020* in sterling terms

% unless stated	Market cap £m	NAV TR one year	NAV TR three year	NAV TR five year	Discount (ex-par)	Ongoing charge (%)	Perf. fee	Net gearing	Dividend yield (%)
BioPharma Credit	1,018.2	6.9	29.5	N/A	(3.3)	1.2	Yes	100	8.4
Debt - Direct Lending									
Alternative Credit Investments	643.6	2.9	9.4	19.6	(5.9)	1.5	Yes	148	5.5
GCP Asset Backed Income	406.7	5.2	21.4	36.3	(7.4)	1.2	No	100	7.0
Honeycomb Investment Trust	329.7	10.4	28.8	N/A	(8.2)	1.8	Yes	100	8.6
RDL Realisation	10.3	(0.9)	(17.9)	3.5	(38.1)	9.8	Yes	255	26.9
Riverstone Credit Opportunities Income	47.9	5.6	N/A	N/A	(35.0)	1.6	No	100	N/A
RM Secured Direct Lending	96.3	0.3	13.1	N/A	(12.4)	1.9	No	104	6.1
Secured Income Fund	35.0	(4.0)	4.7	16.1	(16.8)	2.4	Yes	100	10.5
SME Credit Realisation Fund	96.3	(4.8)	(0.7)	N/A	(28.7)	1.0	No	120	8.9
VPC Specialty Lending Investments	191.4	16.1	45.9	50.6	(32.5)	2.0	Yes	100	11.8
Direct Lending average	206.3	3.4	13.1	25.2	(20.6)	2.6	-	125	10.7
Debt - Loans & Bonds									
Alcentra Eur Floating Rate	4.2	(12.1)	(8.1)	3.0	(6.8)	1.1	No	100	5.6
Axiom European Financial Debt Fund	77.2	3.5	8.0	N/A	(11.6)	1.4	Yes	100	7.1
City Merchants High Yield	191.8	3.2	11.0	34.6	0.3	1.0	No	106	5.3
CQS New City High Yield	214.2	(11.9)	(5.1)	17.5	4.8	1.2	No	100	9.1
CVC Credit Partners Euro Opps GBP	181.8	(1.7)	0.8	19.8	(4.3)	1.2	No	100	5.7
Eurocastle Investment	319.7	(22.7)	(15.1)	75.1	(25.3)	5.5	No	142	N/A
Henderson Diversified Income	173.1	4.7	14.1	32.9	(0.7)	0.9	No	114	4.9
Invesco Enhanced Income	122.1	4.9	13.6	45.0	(4.7)	1.0	No	122	7.1
M&G Credit Income Investment	124.8	1.9	N/A	N/A	(12.3)	0.7	No	100	2.4
NB Distressed Debt Inv Extended Life	27.6	(16.9)	(22.5)	(10.3)	(40.3)	2.4	Yes	100	2.5
NB Distressed Debt New Glb	19.9	(31.7)	(35.9)	(23.9)	(16.4)	2.4	Yes	100	N/A
NB Distressed Debt	8.3	(14.7)	(27.4)	(15.8)	(6.4)	2.4	Yes	100	N/A
NB Global Monthly Income Fund GBP	197.7	(0.8)	6.2	16.0	(14.1)	1.2	No	100	6.0
TwentyFour Select Monthly Income	188.7	6.1	14.8	37.5	(8.0)	1.1	No	100	7.5
Loans & Bonds average	132.2	(6.3)	(3.5)	19.3	(10.4)	1.7	-	106	5.7
Peer group average	161.2	(2.5)	2.8	21.0	(14.4)	2.0	-	114	7.8
Trust rank in group	1	3	2	N/A	4	13	-	9	7

Source: Morningstar, Edison Investment Research. Note: *Performance to 31 October 2020. Net gearing is total assets less cash and equivalents as a percentage of net assets, where 100=ungeared. BPCR performance measured based on ordinary shares.

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