

Biotechs begin to look much

B iotechnology stocks have been gaining support from investors looking for quick gains as commodity prices have fallen.

Novogen, Progen Industries and industry heavyweight ResMed were among the best performers in the small-cap arena in a week in which most of the worst performing stocks were small-cap miners. The ASX/S&P 300 Resources Index fell almost 10 per cent.

Novogen's stock rose almost 3 per cent during the week, mainly because its 87 per cent-owned US company Marshall Edwards, which is producing a drug called Phenoxodiol, announced the drug was eligible for early regulatory approval, shortening the time it takes to go into production. Phenoxodiol is aimed at a broad range of cancers but initially is being developed for ovarian cancer.

Novogen research director Alan Husband said Marshall Edwards should have approval to market Phenoxodiol within 18 months.

But the bounce in Novogen's share price comes after a 38 per cent fall during the past year as investors deserted a sector that failed to live up to its promise as many firms listed too early, according to many analysts.

"We call them 'gunna' stocks, because they're gunna have some earnings in 2010 because they haven't got any now," said Smalco Investment Manager managing director Rob Hopkins.

He said there was still huge risk in investing in the sector, with the obvious exception of CSI.

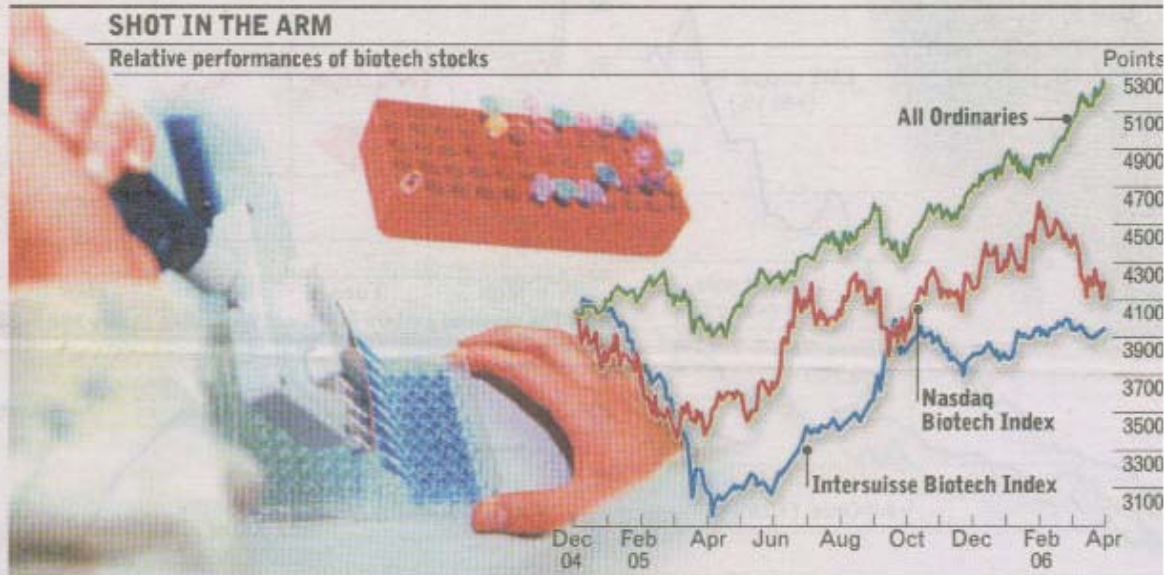
This week, Progen announced that the US Food and Drug Administration was assisting it in accelerating approval of its PI-88 drug, aimed at treating liver cancer. Progen has risen almost 11 per cent since the start of April.

Meanwhile, ABN Amro has raised \$30 million for two biotechs, Chemgenex and Avexa.

Chemgenex is developing a leukaemia drug called Ceflatonin, which has completed a Phase 2 trial, meaning it poses no danger and is being tested on a sample population to see if it works.

ABN Amro estimates the newly raised funds will see Chemgenex through to the end of 2007 and registration of Ceflatonin.

Avexa is developing a drug to



Many biotech stocks have let investors down due to companies listing too early and with little prospect of decent cash flow, but now analysts say value is emerging in the sector and sentiment is slowly becoming positive.

treat HIV. Its market launch, according to ABN Amro, is expected to begin in fiscal 2009.

Salmat feels the pinch

Fund managers are running their rulers over direct marketing company Salmat after its share price fall of more than 30 per cent this week. The decline came after Salmat said Coles Myer would not be renewing its advertising catalogue distribution contract when it expired in August.

Analysts estimated the contract was worth between \$30 million and \$35 million. The business was lost to the other major competitor in junk mail distribution, PMP.

But a fear for Salmat chief executive Philip Salter is that costs in this duopoly industry are reaching ridiculous levels.

According to Mr Salter, PMP won the contract because it promised to provide each of its "walkers" – those who deliver the junk mail – with a portable navigational device, also known as a GPS system, that ensures the catalogues get delivered to each destination. Mr Salter says he can't understand how PMP can

deliver on its pledge when Salmat alone has more than 30,000 walkers on its books.

He says Salmat's strategy, which will be announced in the next four to six weeks, is to use the GPS device to monitor whether or not the junk mail has been delivered.

Trading on a P/E ratio of just under 13 times for fiscal 2006 versus the average small-cap multiple of just under 20 times, Salmat is looking much better value to small-cap fund managers such as Paradise Investment's Matt Riordan.

"Because the market's been weak there has probably been an over-reaction in the stock, but long term there is an issue over the levels of competition their businesses are facing," he said. Mr Riordan is contemplating investing but doesn't own the stock.

Goldman Sachs JBWere media analyst George Batsakis downgraded his valuation to \$4.25 from \$4.72 after the announcement and said he expected the stock to continue to underperform in the next six months "given potential earnings risks and margin pressure" in the

direct marketing business.

But Mr Batsakis's view is that the stock is worth holding for the long term because its business model is strong. The stock closed on Friday at \$2.95.

Buyback boosts shares

Mining and construction engineer Structural Systems shone this week when most stocks linked to the commodity boom fell.

The shares soared by more than 11 per cent after the company said it would buy back up to 10 per cent of its stock. It also announced that profit for this financial year would be about \$6 million, more than double the net profit of \$2.9 million for fiscal 2005. The company is clearly generating cash, and pays out 50 per cent of earnings in dividends, but it is benefiting from tax losses, of which it has left \$10 million, or about two years' worth.

Finance director David Perry envisages further growth in the company's UK and Middle East operations, which account for 25 per cent of its earnings. The construction operations in Australia are also growing.

healthier

according to Mr Perry.

But his comments that current profitability is principally due to "not doing anything wrong" are revealing. Trading on a P/E ratio of 10 times for fiscal 2006 and with a market cap of less than \$41 million, the stock still looks cheap, but the company's earnings have been vulnerable to disruptions in the past.

It first listed in 1987 and after initial success it has performed poorly since 2000 due to non-performing businesses and expensive contractual disputes. Structural Systems lost \$8.6 million in fiscal 2004 but its recent announcements should give shareholders much to look forward to.

Mexican gold

As with many miners, the upward ride for shareholders in prospective silver and gold producer Bolnisi Gold faltered this week. The silver price has fallen more than 14 per cent during the past two weeks, while gold has fallen about 4.5 per cent in the past five trading sessions. But most analysts say silver's price fall isn't surprising considering it has almost doubled this year, while gold has risen by about 65 per cent.

Bolnisi has fallen about 28 per cent since its record high in late April, but investors who have been in the stock for the past year have quadrupled their money. On Friday the stock closed at \$2.15, up from less than 50¢ a year ago. Three years ago the stock was worth 16.5¢.

The company, through a 79 per cent Canadian offshoot, owns the Palmarejo Project in Mexico, which is scheduled for production in the middle of next year. Company secretary Peter Nightingale said he expected the mining permit to come through this month or in June. Should all go to plan, Bolnisi estimates it will produce 11 million ounces of silver and 110 ounces of gold from the mine each year.

Mr Nightingale said the gold production alone should pay all of the mine's operating costs.

Assuming silver contributes 30 per cent of the operating costs, he said the Palmarejo project was forecast to produce an operating surplus of \$US110 million a year, equivalent to almost 40¢ a share.