

25 February 2009

Avexa

Time to vote

Hold

Important: The above recommendation has been made on a 12 month view and may not suit your investment needs or timeframe. The basis it is prepared on is summarised on the last page of this report. **PLEASE CONTACT YOUR ADVISER TO DISCUSS THIS GENERAL RECOMMENDATION BEFORE ACTING ON IT.**

High Volatility

Target price
A\$0.15

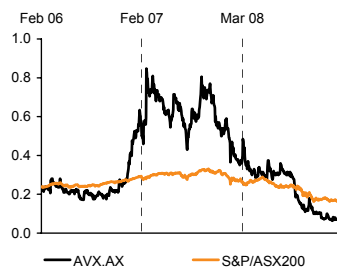
Price
A\$0.069

Short term (0-60 days)
n/a

AVX90225

Price performance

	(1M)	(3M)	(12M)
Price (A\$)	0.07	0.10	0.37
Absolute (%)	-1.4	-31.0	-81.4
Rel market (%)	-1.1	-29.1	-68.9
Rel sector (%)	9.9	-26.4	-76.7



Market capitalisation
A\$28.00m (US\$18.24m)

Average (12M) daily turnover
A\$0.25m (US\$0.22m)

RIC: AVX.AX, AVX AU
Priced at close of business 24 Feb 2009.
Source: Bloomberg

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AVX posted results in line with our expectations. All eyes are on the AVX/Progen merger. Key dates are for Progen shareholders to vote on 11 March and AVX shareholders to vote on 20 March. We make no change to forecasts until the outcome of the merger is known.

Key forecasts

	FY07A	FY08A	FY09F	FY10F	FY11F
EBITDA (A\$m)	-16.7	-40.3	-26.0	-1.32	11.40
Reported net profit (A\$m)	-15.2	-36.1	-23.5	-0.55	11.70
Normalised net profit (A\$m) ¹	-15.2	-36.1	-23.5	-0.55	11.70
Normalised EPS (c) ¹	-3.73	-8.89	-5.53	-0.13	2.77
Normalised EPS growth (%)	-58.7	138.0	-37.8	-97.7	n/a
Dividend per share (c)	0.00	0.00	0.00	0.00	0.00
Dividend yield (%)	0.00	0.00	0.00	0.00	0.00
Normalised PE (x)	n/m	n/m	n/m	n/m	2.50
EV/EBITDA (x)	2.93	0.38	n/m	n/m	0.90
Price/net oper. CF (x)	-1.80	-0.96	-1.06	-7.28	3.10
ROIC (%)	354.6	-196	-147	-6.21	36.60

1. Pre non-recurring items and post preference dividends

year to Jun, fully diluted

Accounting standard: IFRS

Source: Company data, ABN AMRO Morgans forecasts

Phase III trial on track to release results 2QCY09

AVX reported a 1H09 net loss of A\$21.1m, which was in line with our forecast. The cash position at 31 December was A\$20.5m. The first of two Phase III trials has progressed well, with AVX on track to release initial data 2QCY09. Other key milestones to track include the release of 96 week interim data from the Phase IIb extension study in 1QCY09, 144 week final analysis data Phase IIb extension study, conclusion of enrolment of the Phase III study in 2QCY10 and finally the release of 24 week Phase III data in 4QCY10.

Time to vote

AVX and Progen have agreed to an all-scrip merger, to be implemented by a scheme of arrangement. If the merger is implemented, AVX shareholders will be issued one PGL share for every 12.857 AVX shares held. The merged group will be owned 56% by PGL shareholders and 44% by AVX shareholders (post buyback). Both Boards have unanimously agreed to the merger. The key dates are 11 March 2009 for Progen shareholders to vote and 20 March for AVX shareholders to vote. Until the outcome of the vote is known we make no changes to forecasts.

Investment view: Hold maintained until outcome of merger is known

Our DCF valuation is A\$1.32. Key assumptions include the receipt of A\$30m in milestone payments in FY09 and FY10 upon a licensing deal with a pharmaceutical company, a RFR of 5.25% (was 6.5%), risk premium of 6.0% (was 4.5%), and a WACC of 17.8% (was 15.6%). The share price is unlikely to move until the outcome of the merger is known. Setting the price target is difficult in this environment and therefore we will maintain the price target at A\$0.15. The downside risk to our price target includes delays in the progress of the Phase III trial and the upside relates to securing a partnering deal with a larger pharma company.

Interim result, valuation and price target

AVX reported a net loss of A\$21.1m, which was in line with our forecast. At December 08, AVX had A\$20.5m in cash. Until the outcome of the merger is known we have made no changes to our forecasts.

Our DCF valuation is A\$1.32. The key underlying assumptions underpinning our valuation include:

- In line with the house view, we have reduced our risk-free rate to 5.25% (from 6.5%), and increased the market risk premium to 6.0% (from 4.5%). This has resulted in our WACC increasing to 17.9% (from 15.6%).
- A A\$30m milestone receipt is assumed in FY09 and FY10 upon the execution of a partnering deal. The timing and extent of milestone payments is difficult to estimate and any delay or variation in quantum will have a material negative impact on our valuation.

Setting the price target is difficult in this environment and therefore we will maintain the price target at A\$0.15. The downside risk to our price target includes delays in the progress of the Phase III trial and the upside relates to securing a partnering deal with a larger pharmaceutical company.

Key takeaways of the proposed transaction

The basics – AVX and PGL have agreed to an all-scrip merger, to be implemented by a scheme of arrangement. If the merger is implemented, AVX shareholders will be issued one PGL share for every 12.857 AVX shares held. The merged group will be owned 56% by PGL shareholders and 44% by AVX shareholders (post buyback). The merger ratio is based on AVX's last closing share price prior to the merger of A\$0.105, and an implied value of A\$1.35 per PGL share.

Directors recommend proposal - Both PGL and AVX's board of directors unanimously recommend the proposal.

PGL share buyback – Prior to the merger and subject to shareholder approval, PGL will undertake a voluntary share buyback at A\$1.10 per share for up to A\$20m.

Cash position of merged entity – The merged entity is expected to have a combined A\$60m in cash post completion and following the PGL share buyback. We believe this will be sufficient to fund AVX's clinical program through until the release of 24 week data from the first Phase 3 clinical trial, in 4QCY10.

Hurdles – Among other things, the merger requires both AVX and PGL shareholder approval. There is a A\$0.5m break-fee applicable to both parties.

Independent valuation released - The Independent Expert's Report, prepared by Lonergan Edwards & Associates, was commissioned as part of the proposed merger with Avexa and Progen Pharmaceuticals. The key finding is that after the dilutionary impact of assumed future capital raisings to fund the lead product (ATC) up to the 24 week milestone, the value of AVX shares on a stand-alone basis is in the range of 21cps to 41cps. Our valuation of AVX is higher and the key difference relates to a higher royalty rate assumption (our forecast 30% compared with 12 to 15%).

Benefits and risks for AVX – In our view, the proposed merger provides AVX with sufficient cash to fund the company through to the important 24 week data milestone in 4QCY10. The company recently reiterated that, despite the merger with PGL, it will continue to seek a partner for ATC. We would comment, that to date, partnering discussions have been prolonged, partly impacted by the financial crisis. We believe that topping up its cash position will provide AVX with greater leverage in these discussions. Conversely, if the merger does not proceed, AVX risks eroding its negotiating position with potential partners, given its cash position. We now believe a partnering deal is more likely than M&A with large pharma.

Key voting dates – Progen shareholders will vote on 11 March and Avexa shareholders will vote on 20 March.

Table 1 : Upcoming milestones

Estimated Date	Milestone	Impact
1QCY07	Release of the first results from Phase 2b clinical trial of Apricitabine	Achieved
2QCY07	Publication of 21 day results at IAS conference (July)	Achieved
3QCY07	Release 24 week data Phase 2b	Achieved
4QCY07	Start first of two Phase 3 clinical trials for ATC	Achieved
1QCY08	Release of 48 week data of Phase 2b study	Achieved
2QCY09	Release of 16 week data from first Phase 3 ATC clinical trial	Positive
1HCY09	Commence second Phase 3 ATC clinical trial	Positive
2HCY10	File NDA with FDA	Major Positive

Source: ABN AMRO Morgans

AVX – financial summaries

Year to 30 Jun (A\$m)	AIFRS 2007A	AIFRS 2008A	AIFRS 2009F	AIFRS 2010F	AIFRS 2011F	Closing price (A\$)	0.069	Price target (A\$)	0.15	
Income statement						Valuation metrics				
Divisional sales	0.2	1.4	25.4	25.4	28.5	Preferred methodology	DCF	Val'n (A\$)	\$ 1.32	
Total revenue	0.2	1.4	25.4	25.4	28.5	DCF valuation inputs				
EBITDA	-16.7	-40.3	-26.0	-1.3	11.4	Rf	5.25%	10-year rate	5.25%	
Associate income	0.0	0.0	0.0	0.0	0.0	Rm-Rf	6.00%	Margin	2.0%	
Depreciation	-0.1	-0.2	-0.1	-0.2	-0.3	Beta	2.09	Kd	7.25%	
EBITA	-16.8	-40.4	-26.1	-1.5	11.1	CAPM (Rf+Beta(Rm-Rf))	17.8%	Ke	17.8%	
Amortisation/impairment	0.0	0.0	0.0	0.0	0.0	E/EV*Ke+D/EV*Kd(1-t)		NPV cash flow (A\$m)	543.7	
EBIT	-16.8	-40.4	-26.1	-1.5	11.1	Equity (E/EV)	100.0%	Minority interest (A\$m)	0.0	
EBIT(incl associate profit)	-16.8	-40.4	-26.1	-1.5	11.1	Debt (D/EV)	0.0%	Net debt (A\$m)	-15.6	
Net interest expense	1.6	4.3	2.6	0.9	0.6	Interest rate	7.25%	Investments (A\$m)	0.0	
Pre-tax profit	-15.2	-36.1	-23.5	-0.5	11.7	Tax rate (t)	30.0%	Equity market value (A\$m)	559.3	
Income tax expense	0.0	0.0	0.0	0.0	0.0	Franking credit	0.0	0.0	0.0	
After-tax profit	-15.2	-36.1	-23.5	-0.5	11.7	WACC	17.8%	Diluted no. of shares (m)	424.6	
Minority interests	0.0	0.0	0.0	0.0	0.0			DCF valuation (A\$)	1.32	
NPAT	-15.2	-36.1	-23.5	-0.5	11.7	Multiples	2008A	2009F	2010F	2011F
Significant items	0.0	0.0	0.0	0.0	0.0	Enterprise value (A\$m)	-15.4	12.4	17.6	10.3
NPAT post abnormal	-15.2	-36.1	-23.5	-0.5	11.7	EV/Sales (x)	-11.3	0.5	0.7	0.4
						EV/EBITDA (x)	0.4	-0.5	-13.2	0.9
Cash flow statement	2007A	2008A	2009F	2010F	2011F	EV/EBIT (x)	0.4	-0.5	-11.9	0.9
EBITDA	-16.7	-40.3	-26.0	-1.3	11.4	PE (pre-goodwill) (x)	-0.8	-1.2	-53.6	2.5
Change in working capital	-0.4	6.6	-4.3	-3.6	-2.6	PEG (pre-goodwill) (x)				
Net interest (pd)/rec	1.6	4.3	2.6	0.9	0.6	At target price	2008A	2009F	2010F	2011F
Taxes paid	0.0	0.0	0.0	0.0	0.0	EV/EBITDA (x)	-0.4	-1.7	-38.1	3.8
Other oper cash items	0.0	0.0	0.0	0.0	0.0	PE (pre-goodwill) (x)	-1.7	-2.7	-116.5	5.4
Cash flow from ops (1)	-15.5	-29.3	-27.6	-4.0	9.5	Comparable company data (x)	2009F	2010F	2011F	
Capex (2)	-0.2	-3.5	-0.2	-1.1	-2.2	Alchemia	EV/EBITDA	-2.0	138.2	0.7
Disposals/(acquisitions)	-12.9	-0.8	0.0	0.0	0.0	Year to 30 Jun	EV/EBIT	-1.6	-10.0	0.8
Other investing cash flow	0.0	0.0	0.0	0.0	0.0		PE	-2.6	19.9	0.6
Cash flow from invest (3)	-13.1	-4.2	-0.2	-1.1	-2.2		PEG	-0.7	5.7	0.2
Incr/(decr) in equity	85.3	0.0	0.0	0.0	0.0	Peplin	EV/EBITDA	0.0	0.5	-0.2
Incr/(decr) in debt	0.0	0.0	0.0	0.0	0.0	Year to 30 Jun	EV/EBIT	0.0	0.5	-0.2
Ordinary dividend paid	0.0	0.0	0.0	0.0	0.0		PE	-0.1	-0.2	-0.4
Preferred dividends (4)	0.0	0.0	0.0	0.0	0.0		PEG			
Other financing cash flow	0.0	0.0	0.0	0.0	0.0	Per share data	2008A	2009F	2010F	2011F
Cash flow from fin (5)	85.3	0.0	0.0	0.0	0.0	No. shares	406.0	424.6	424.6	424.6
Forex and disc ops (6)	0.0	0.0	0.0	0.0	0.0	EPS (cps)	-8.9	-5.5	-0.1	2.8
Incr/(decr) cash (1+3+5+6)	56.7	-33.5	-27.8	-5.1	7.3	EPS (normalised) (c)	-8.9	-5.5	-0.1	2.8
Equity FCF (1+2+4)	-15.7	-32.7	-27.8	-5.1	7.3	Dividend per share (c)	0.0	0.0	0.0	0.0
						Dividend payout ratio (%)	0.0	0.0	0.0	0.0
Balance sheet	2007A	2008A	2009F	2010F	2011F	Dividend yield (%)	0.0	0.0	0.0	0.0
Cash & deposits	76.9	43.4	15.6	10.4	17.7	Growth ratios	2008A	2009F	2010F	2011F
Trade debtors	0.1	0.4	6.6	5.2	5.9	Sales growth	531.7%	1767.0%	0.1%	12.2%
Inventory	0.0	0.0	0.0	0.0	0.0	Operating cost growth	146.3%	23.4%	-48.0%	-36.1%
Investments	16.5	20.0	20.0	20.0	20.0	EBITDA growth	141.4%	-35.4%	-94.9%	na
Goodwill	0.0	0.0	0.0	0.0	0.0	EBITA growth	141.3%	-35.5%	-94.3%	na
Other intangible assets						Operating performance	2008A	2009F	2010F	2011F
Fixed assets	0.3	0.9	1.0	2.0	3.8	Asset turnover (%)	0.4	11.7	15.7	16.7
Other assets	0.1	0.1	0.1	0.1	0.1	EBITDA margin (%)	-2962.0	-102.5	-5.2	40.1
Total assets	94.0	64.8	43.3	37.7	47.5	EBIT margin (%)	-2975.8	-102.9	-5.8	39.0
Short-term borrowings	0.0	0.0	0.0	0.0	0.0	Net profit margin (%)	-2655.8	-92.6	-2.2	41.2
Trade payables	2.2	8.4	10.4	5.4	3.5	Return on net assets (%)	-72.5	-80.9	-4.7	25.6
Long-term borrowings	0.0	0.0	0.0	0.0	0.0	Net debt (A\$m)	-43.4	-15.6	-10.4	-17.7
Provisions	0.0	0.0	0.0	0.0	0.0	Net debt/equity (%)	-77.8	-48.2	-32.9	-40.8
Other liabilities	0.5	0.6	0.6	0.6	0.6	Net interest/EBIT cover (x)	9.3	10.0	1.6	-17.7
Total liabilities	2.7	9.0	11.0	6.0	4.0	ROIC (%)	-196.4	-147.8	-6.2	36.6
Preference shares						Internal liquidity	2008A	2009F	2010F	2011F
Hybrid equity						Current ratio (x)	4.9	2.0	2.7	5.9
Share capital	137.2	137.2	113.7	113.2	124.9	Receivables turnover (x)	5.4	7.3	4.3	5.1
Other reserves	0.0	0.0	0.0	0.0	0.0	Payables turnover (x)	7.8	5.4	3.4	3.8
FCTR										
Unrealised gains/losses										
Retained earnings	-45.9	-81.5	-81.5	-81.5	-81.5					
Other equity	0.0	0.0	0.0	0.0	0.0					
Total equity	91.3	55.8	32.3	31.7	43.5					
Minority interest	0.0	0.0	0.0	0.0	0.0					
Total shareholders' equity	91.3	55.8	32.3	31.7	43.5					
Total liabilities & SE	94.0	64.8	43.3	37.7	47.5					

Source: Company data, ABN AMRO Morgans forecasts

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Absolute performance, long-term (fundamental) recommendation: The recommendation is based on implied upside/downside for the stock from the target price. A Buy/Sell implies upside/downside of 10% or more and a Hold less than 10%. The target price is the level the stock should currently trade at if the market accepted the analyst's view of the stock, provided the necessary catalysts are in place to effect the change in perception. If it is felt that the catalysts are not fully in place to effect a re-rating of the stock to its warranted value the target price will differ from 'fair' value. Given the volatility of share prices and our pre-disposition on not to change recommendations frequently, these performance parameters should be interpreted flexibly. Performance in this context only reflects capital appreciation and the horizon is 12 months.

For listed property trusts (LPTs) the recommendation is based upon the target price plus the dividend yield, ie total return. A Buy implies a total return of 10% or more; a Hold 5-10%; and a Sell less than 5%.

Absolute performance, short-term (trading) recommendation: The Trading Buy/Sell recommendation implies upside/downside of 3% or more. The trading recommendation time horizon is 0-60 days.

Each stock has been assigned a Volatility Rating to assist in assessing the risk of the security. The rating measures the volatility of the security's daily closing price data over the previous year relative to other stocks included in either the S&P/ASX200 Index (large caps) or the Small Ordinaries Index (small caps) of which it is a member. This rating is a quantitative (objective) measure provided as an additional resource and is independent of the qualitative research process undertaken by our research analysts.

A rating of Low indicates very little movement in price over the previous year (Coefficient of Variation < 4 for small caps or < 5 for large caps). A Moderate rating implies average price movement over the previous year (Coefficient of Variation of 9 - 21 for small caps or 7.25 - 15 for large caps). A High rating implies significant price movement over the past year (Coefficient of Variation greater than 25 for small caps or 35 for large caps).

REGULATORY DISCLOSURES

Subject companies: AVX.AX, ACR.AX, CXS.AX

ABN AMRO Morgans corporate acted as a lead manager to the share placement and rights issue for AVX and received fees in this regard.: AVX.AX

CXS.AX

ABN AMRO Morgans Limited was the Underwriter to the renounceable rights issue of shares by Aveva Limited in March 2007 and received fees in this regard: AVX.AX

ABN AMRO Morgans Limited is the Lead Manager to the current ChemGenex Pharmaceuticals Limited placement and SPP and may receive fees in this regard.: CXS.AX

ABN AMRO Morgans was the Lead Manager to the rights issue and placement of shares by Chemgenex Pharmaceuticals Limited in February 2007 and received fees in this regard.: CXS.AX

ABN AMRO Morgans Limited is the Lead Manager to the ChemGenex Pharmaceuticals Limited placement and SPP in September 2008 and may receive fees in this regard.: CXS.AX.

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