

**SMALL CAPS BRENDON LAU**

# New drugs point to winners

The small-cap health-care sector has been one of the best performing in the Small Ordinaries Index this year, and many market watchers believe further near-term upside is possible as several biotech firms are close to commercialising new drugs.

The health-care sector of the S&P/ASX Small Ordinaries Index has returned minus 12.9 per cent year to date, compared with minus 20.99 per cent for industrials and minus 42.81 per cent for financials. Out of all the Small Ordinaries sectors, only consumer goods ranked higher, with a return of minus 12.4 per cent.

While investing in biotech stocks is generally regarded as a speculative endeavour due to the high rate of new drug failures, investors can minimise some of the risks by looking at companies with drugs undergoing final phase-three clinical trials. Wilson HTM health-care and biotech analyst Graeme Wald said drugs in this trial phase had an average success rate of 80 per cent and Australian investors had an unprecedented range of choices.

"If you look at biotech, there are a number of companies in late-stage development, and that is something that has never happened before in Australia," Mr Wald said.

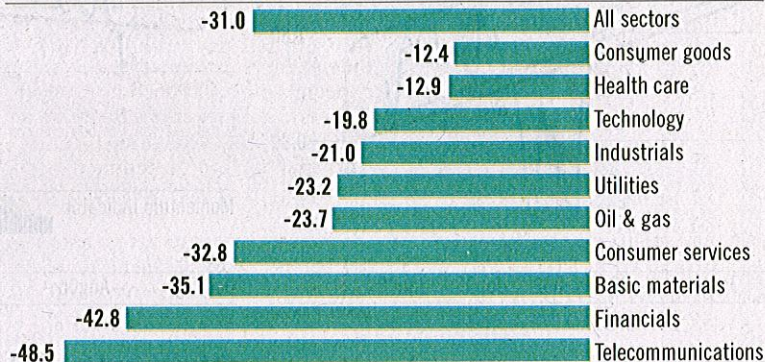
Stocks he considers likely to see big returns on their innovations include **Chemgenex Pharmaceuticals**, for leukaemia; **Avexa**, for HIV; and medical device maker **Universal Biosensors**, for its diabetes glucose-meter.

However, the stock he particularly likes is **Pharmaxis**. The group has been making steady progress in getting its blockbuster drug **Bronchitol** approved for the treatment of cystic fibrosis and bronchiectasis, and Mr Wald believes this can come as early as next year.

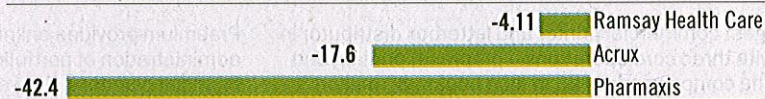
"Bronchitol is probably the best drug in the world to treat cystic fibrosis and the only approved drug that works against bronchiectasis,"

## Rude health

Year to date performances of S&P/ASX Small Caps sectors (%)



Year to date performances of three small health care stocks (%)



SOURCE: BLOOMBERG

he said. Bronchiectasis causes localised irreversible dilatation of part of the bronchial tree in the lung.

Despite the stock's strong upside potential, it has been one of the worst performers in the health-care space and has tumbled by about 45 per cent since the start of the year.

"The reason why it has underperformed is because the company has no earnings yet," Mr Wald said. "In times when there

### There are a number of companies in late-stage development.

is a lack of confidence in the market, these are the sorts of companies that suffer the most."

The stock closed up 11¢ at \$2.43 on Monday and Wilson HTM has a 12-month price target of \$4.41 on it. Acrux is another stock winning support from brokers. It has one advantage over Pharmaxis: it already has a product on the market in the US, called **Estradiol**, which is

used to treat menopausal symptoms. Acrux normally out-licenses its technologies but it will take **Estrodiol** to market on its own.

WilsonHTM is bullish on the stock, while Morningstar is urging risk-tolerant investors to buy the stock under \$1.10 as Acrux is forecast to receive significant royalty payments after 2010. Acrux, which develops delivery technologies that allow patients to spray on treatments as opposed to swallowing drugs, hit a 21-month low in March this year of 76¢ as investors lost their taste for high-risk stocks and on news that a director's shares were entangled with the **Opes Prime** debacle. The stock has bounced around 50 per cent since then but is still down around 18 per cent this year. The stock closed 5¢ higher at \$1.15 yesterday.

Investors looking for a less risky option might prefer to consider **Ramsay Health Care**.

The stock has performed relatively strongly this year, delivering a negative total return of about 6 per cent.