Late-cycle opportunities in new cancer treatment

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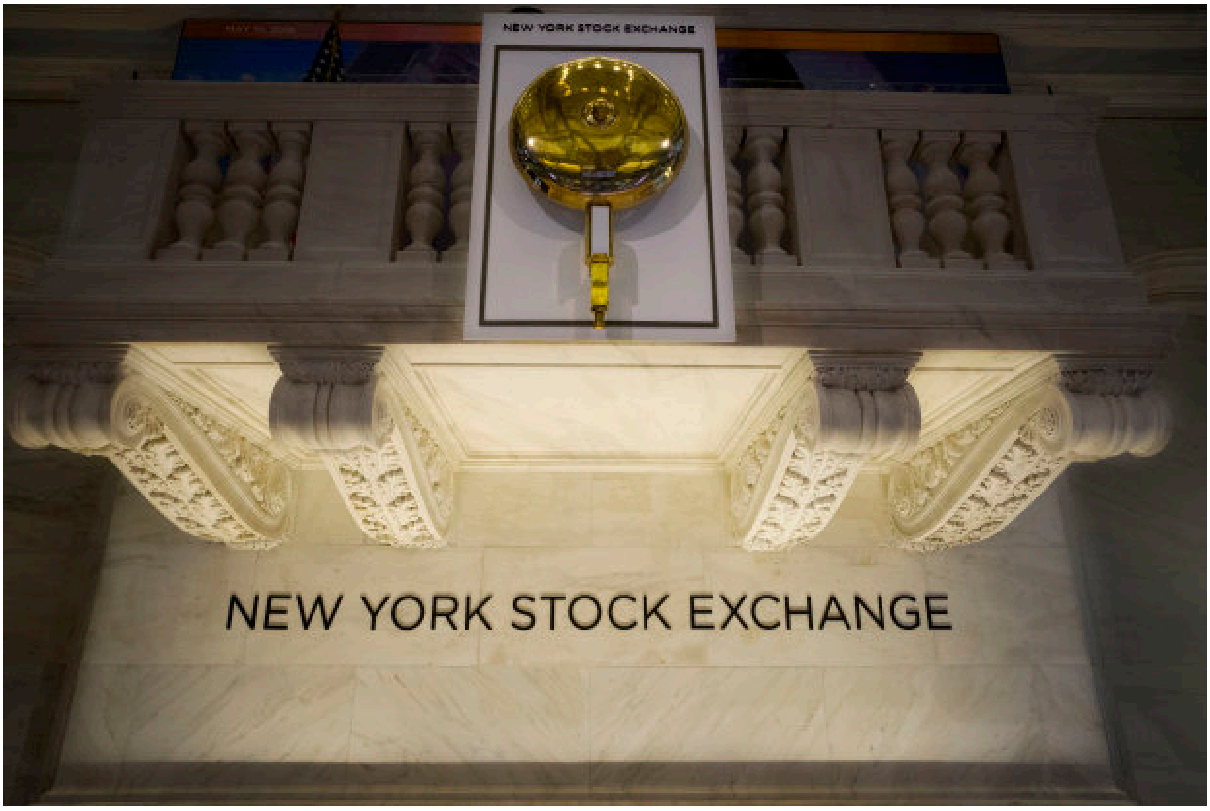
Whatever one's view of where we are in the collective global cycle, pretty much everyone can agree that 2019 is long in the tooth and can safely be dubbed "late cycle".

Late cycles display some very particular attributes. Traditionally there is a flurry of merger and acquisition "megadeals" within incumbent industries, as well as a barrage of new upstarts, reflected in initial public offering (IPOs).



In 2019, only 75 IPOs have come to market in the leading global sharemarkets. *AP Photo*

But 2019 continues to be an unusual year, reflected in the fact that in the leading global sharemarkets – the US' New York Stock Exchange plus the technology-centric NASDAQ – there have, as at the time of writing, been only 75 IPOs coming to market.

That's 325 offerings short of the tech bubble average of 400 IPOs aggregated annually between 1995 to 2001.

Absolute valuations for the IPOs completed in 2019 have been lower than previously, and investors have assigned a greater valuation premium than usual to IPOs with the fastest expected sales growth. IPO statistics for 2019 highlight that the sales growth in these listed entities is 50 per cent higher during the first three years than IPOs in the late-1990s.

Fifteen years ago Australia experienced similar off-market to on-market turbulences with the disruption of then nascent private equity conglomerates delisting Australian darlings and bringing to market privately held companies.

In 2019, domestically but also globally, this shift is being seen in venture capital (VC) private companies being brought to market or existing listed entities receiving capital injections from VC, private equity and passively managed ETF mega-conglomerates.

One well-publicised example of this in recent weeks has been the saga surrounding e-cigarette manufacturer Juul, known for its popular flavoured e-cigarette range, which represents 80 per cent of sales.

This month not only has the company's CEO stepped down as merger talks between its biggest investor, Altria Group, and Philip Morris International collapsed in the face of a regulatory backlash, but one of its largest passive investors, Fidelity, took the brunt of the volatility both financially and in the public relations forum.

The reason behind this particular fracas being noticed by those keeping an eye on late-cycle opportunities (and risks) is because there has been anticipation that oncology and health sciences opportunities leading into 2020 and potentially 2021 may be where the last uplift of the current bull cycle will be seen.

Healthcare deal flow has remained relatively subdued, but the silver lining is that this may be an opportunity to bring to listed markets IPO-worthy opportunities in oncology, healthcare and related services.

According to the American Cancer Society, during the 1940s – before all the technology and innovation we now enjoy – only one in 16 people got cancer. By the 1970s, that number fell to one in 10.

Today, one in two males is at risk of developing some form of cancer and for women, the chances are one in three.

Treating cancer as a category generated $US9.9 billion in annual venture capital funding in 2019, with a compound annual growth rate (CAGR) of 30 per cent over five years. Late-cycle pundits are investigating whether this may overlay into IPO opportunities.

According to Goldman Sachs, new hopes and opportunities may be found in what is being pre-emptively (still requiring a proof of concept) referred to as the "fourth wave in cancer treatment", found in the emerging field of chromatin biology.

Although this is a new area of oncology for many, since 1910, six Nobel Prizes have been awarded to molecular biologists who have shed light on important aspects of chromatin bioscience.

Academic research has unveiled the role that mutations in chromatin, the regulatory system for our DNA, play in the development of a wide variety of cancers and other diseases.

Based on this understanding, there are a variety of potential therapeutic approaches that could treat cancer through targeting mutated chromatin.

Trailblazing this path are two US funds, Flagship Pioneering and OrbiMed Advisors, which are investing heavily into dedicated chromatin-remodelling companies.

One of these is Foghorn Therapeutics, a portfolio company of Flagship Pioneering, which is trying to commercialise chromatin regulation and present it as a foundational approach to treating not only cancer but other diseases including arthritis and lupus.

According to Goldman Sachs, global spending on oncology therapeutics and supportive care was $US133 billion in 2017 and estimated to rise to $US200 billion by 2022 (10-13 per cent CAGR), with US spending expected to reach $US100 billion in 2022 (12-15 per cent CAGR).

Chromatin regulation offers a novel approach to cancer therapeutics and could command a significant share of this global market and it may answer the question as to where growth can be found this late in the cycle.

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