Zacks Small-Cap Research

October 6, 2016
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Aralez Pharmaceuticals Inc. (ARLZ-NASDAQ)

ARLZ: Business Development Activity Continues with Acquisition of Toprol-XL® from AstraZeneca…

Based on our financial model that uses a EV/revenue multiple of 5.0x based on projected 2020 revenues, with a 15% discount rate, ARLZ is valued at $11/share. Additional upside to this valuation is possible from attaining approval for YOSPRALA® in the E.U. and Canada and/or accretive deals.

Current Price (10/6/16)	$5.30
Valuation	**$11.00**

OUTLOOK

On October 4, 2016, Aralez Pharmaceuticals, Inc. (ARLZ) announced the acquisition of Toprol-XL® from AstraZeneca for an upfront payment of $175 million along with a 15% royalty and up to $48 million in potential milestone payments. Aralez is financing the transaction through the previously committed $200 million senior debt facility with Deerfield Management.

Toprol-XL® is a cardiovascular beta-blocker indicated for the treatment of hypertension, the long term treatment of angina, and the treatment of stable, symptomatic heart failure. Revenues for Toprol-XL® and its authorized generic were $91 million, $89 million, and $53 million for 2014, 2015, and the first six months of 2016, respectively. We believe the addition of Toprol-XL® will accelerate Aralez's profitability to 2017 on an adjusted basis.

SUMMARY DATA

52-Week High	**$8.11**
52-Week Low	**$3.12**
One-Year Return (%)	**-13.40**
Beta	**0.77**
Average Daily Volume (sh)	**2,129,466**
Shares Outstanding (mil)	**65**
Market Capitalization ($mil)	**$346**
Short Interest Ratio (days)	**N/A**
Institutional Ownership (%)	**50**
Insider Ownership (%)	**7**
Annual Cash Dividend	**$0.00**
Dividend Yield (%)	**0.00**
5-Yr. Historical Growth Rates	
Sales (%)	**-14.5**
Earnings Per Share (%)	**N/A**
Dividend (%)	**N/A**
P/E using TTM EPS	**N/A**
P/E using 2016 Estimate	**-2.0**
P/E using 2017 Estimate	**-4.2**

Risk Level	**High,**
Type of Stock	**Small-Value**
Industry	**Med-Drugs**

ZACKS ESTIMATES

Revenue

(In millions of $)

	Q1 (Mar)	Q2 (Jun)	Q3 (Sep)	Q4 (Dec)	Year (Dec)
2015	4.4 A	5.2 A	5.8 A	6.0 A	21.4 A
2016	8.1 A	12.6 A	12.7 E	15.8 E	49.1 E
2017					84.5 E
2018					136.8 E

Earnings per Share

(EPS is operating earnings before non-recurring items)

	Q1 (Mar)	Q2 (Jun)	Q3 (Sep)	Q4 (Dec)	Year (Dec)
2015	$0.00 A	$0.50 A	-$0.25 A	-$0.40 A	-$1.16 A
2016	-$0.65 A	-$0.27 A	-$0.32 E	-$0.41 E	-$1.60 E
2017					-$0.68 E
2018					-$0.40 E

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WHAT'S NEW

Aralez Acquires U.S. Rights to Toprol-XL®

On October 4, 2016, Aralez Pharmaceuticals, Inc. (ARLZ) announced it will acquire the U.S. rights to Toprol-XL® and it authorized generic. Toprol-XL® is a cardiovascular beta-blocker indicated for treating patients with hypertension, angina pectoris, and stable, symptomatic heart failure. The acquisition further broadens the company's cardiovascular portfolio and will begin generating meaningful cash, which will move Aralez to profitability on an adjusted basis in 2017.

Toprol-XL®

Toprol-XL® (metoprolol succinate) is a selective β1-receptor blocker, otherwise known as a "beta blocker". This class of drugs is composed of competitive antagonists that block endogenous epinephrine and norepinephrine binding on adrenergic beta receptors. Toprol-XL® is a beta blocker that is selective for β1 receptors, which are mainly located on the heart and kidneys. The drug is formulated to provide a controlled and predictable release of metoprolol succinate from controlled release pellets such that only one dose of drug is required per day.

The FDA originally approved Toprol-XL® in 1992. The MERIT-HF study was a double blind, placebo controlled Phase 3 clinical trial of Toprol-XL® that included 3991 patients (1990 to Toprol-XL®) with NYHA Class II-IV heart failure (MERIT-HF Study Group). The trial was terminated early due to a statistically significant reduction in all-cause mortality (34%, *P*=0.00009). The risk of all-cause mortality plus all-cause hospitalization was reduced by 19% (P=0.00012).

Peak sales of Toprol-XL® were $1.6 billion in 2006, at which point patent protection expired. Sales of both Toprol-XL® and its authorized generic in the U.S. were $91 million, $89 million, and $53 million for 2014, 2015, and the first six months of 2016, respectively. The uptick in 2016 revenues through the first six months of the year was due in part to a contract that AstraZeneca signed with the Veterans Administration for the branded drug.

Upon closing of the deal, Aralez will acquire the U.S. rights to Toprol-XL® for a $175 million upfront payment along with $48 million in potential milestone payments and a 15% royalty on net sales. The upfront payment will be financed through the previously committed debt facility with Deerfield Management. Aralez will also borrow $25 million to replenish the cash that was spent in connection with the recent acquisition of Zontivity®.

Conclusion and Valuation

The addition of Toprol-XL® is a smart strategic move for Aralez, which management was able to complete at a reasonable price (upfront payment ~2X 2015 revenues). This follows the recently announced acquisition of Zontivity® and the FDA approval of YOSPRALA®, thus along with Fibricor, Aralez now has a full suite of complementary cardiovascular product offerings.

Following completion of the Toprol-XL® deal, Aralez will have fully drawn down the $200 million credit facility that was originally entered into with Deerfield Management upon the formation of the company. As a reminder, this credit facility bears an interest rate of 12.5% and may be repaid at any time following the end of the sixth month following the funding date of each draw. However, Aralez can continue to look for additional business development opportunities, as Deerfield has agreed to allow up to an additional $250 million in capital to fund any future acquisitions under similar terms as the original credit facility. Management has indicated that the current credit facilities are a bridge to a more permanent financing situation at some point in the future when the company has significant EBITDA and a leverage ratio that will allow them to receive more favorable financing conditions.

We have updated our financial model to incorporate potential revenues for Toprol-XL®. We are currently forecasting for sales of Toprol-XL® in 2017 of $80 million, which will then slightly decrease in subsequent years. We derive a valuation for Aralez using an enterprise value (EV)/revenues multiple of 5.0x based on forecasted 2020 revenue and a 15% discount rate. We now forecast 2020 revenues will be approximately $306 million. The company currently has $275 million in debt and we estimate approximately $78 million in cash as of the end of 3Q16. This leads to a valuation of $11 per share. We note potential upside to the model exists based on better than anticipated sales of the company's products and any additional accretive deals.

PROJECTED FINANCIALS

Aralez Pharmaceuticals Inc.
Income Statement

Aralez Pharmaceuticals, Inc.	2015 A*	Q1 A	Q2 A	Q3 E	Q4 E	2016 E	2017 E	2018 E
Vimovo (royalty)	**$21.4**	**$4.5**	**$5.2**	**$5.3**	**$5.3**	**$20.3**	**$20.0**	**$20.0**
YOY Growth		-	-	-	-	*-5.1%*	*-1.5%*	*0.0%*
Yosprala	**$0.0**	**$0.0**	**$0.0**	**$0.0**	**$3.0**	**$3.0**	**$30.0**	**$75.0**
YOY Growth	-	-	-	-	-	-	-	-
Zontivity	**$0.0**	**$0.0**	**$0.0**	**$0.0**	**$0.0**	**$0.0**	**$4.0**	**$6.0**
YOY Growth	-	-	-	-	-	-	-	-
Toprol XL	**$0.0**	**$0.0**	**$0.0**	**$0.0**	**$0.0**	**$0.0**	**$80.0**	**$75.0**
YOY Growth	-	-	-	-	-	-	-	-
Other Products	**$27.4**	**$3.6**	**$7.4**	**$7.4**	**$7.5**	**$25.8**	**$24.5**	**$24.8**
Total Revenues	$48.8	$8.1	$12.6	$12.7	$15.8	$49.1	$158.5	$200.8
YOY Growth	-	-	-	-	-	*0.7%*	*222.6%*	*26.7%*
Cost of Goods Sold	$10.7	$2.5	$3.4	$2.8	$3.3	$12.0	$35.0	$42.0
Product Gross Margin	*78.0%*	*68.5%*	*73.3%*	*78.0%*	*79.1%*	*75.6%*	*77.9%*	*79.1%*
SG&A	$54.5	$37.5	$22.7	$26.0	$33.0	$119.2	$120.0	$135.0
% SG&A	*111.6%*	*464.9%*	*180.7%*	*204.7%*	*208.9%*	*242.6%*	*75.7%*	*67.2%*
R&D	$8.5	$4.4	$1.5	$1.5	$1.5	$8.9	$8.5	$8.8
% R&D	*17.4%*	*54.8%*	*11.7%*	*11.8%*	*9.5%*	*18.1%*	*5.4%*	*4.4%*
EBITDA	($24.9)	($36.4)	($15.0)	($17.6)	($22.0)	($90.9)	($5.0)	$15.0
Operating Margin	*-51.1%*	*-451.2%*	*-119.2%*	*-138.6%*	*-139.2%*	*-185.1%*	*-3.2%*	*7.5%*
Interest, Income Net and Other	($8.5)	$4.5	($0.9)	($0.9)	($2.0)	$0.7	($27.0)	($27.0)
Amortization Expense	($8.6)	($1.3)	($2.1)	($2.1)	($2.1)	($7.6)	($10.0)	($10.0)
Pre-Tax Income	($42.0)	($33.1)	($18.0)	($20.6)	($26.1)	($97.8)	($42.0)	($22.0)
Taxes	$2.6	$0.7	($0.5)	$0.5	$0.5	$1.1	$3.0	$5.0
Net Income	($44.6)	($33.8)	($17.5)	($21.1)	($26.6)	($99.0)	($45.0)	($27.0)
YOY Growth	-	-	-	-	-	*121.8%*	*-54.5%*	*-40.0%*
Net Margin	*-91.4%*	*-419.4%*	*-138.9%*	*-166.1%*	*-168.4%*	*-201.4%*	*-28.4%*	*-13.4%*
Reported EPS	($0.70)	($0.65)	($0.27)	($0.32)	($0.41)	($1.60)	($0.68)	($0.40)
Avg. Weighted Shares Outstanding	63.4	52.2	64.4	65.0	65.4	61.7	66.0	67.0

Source: Zacks Investment Research, Inc. *David Bautz, PhD*
**Pro Forma Aralez Combined*

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