Evotec SE
Transcript of the Conference Call
First quarter 2019 results, 14 May 2019 – 2.00 pm CET

Speakers: Dr Werner Lanthaler (CEO), Dr Cord Dohrmann (CSO), Dr Craig Johnstone (COO), Enno Spillner (CFO)

Operator

Dear Ladies and Gentlemen, welcome to the Evotec SE conference call regarding the Q1 results 2019. At our customer's request, this conference will be recorded. As a reminder, all participants will be in a listen only mode. After the presentation there will be an opportunity to ask questions. If any participant has difficulties in the conference, please press star key followed by zero on your telephone for operator assistance. May I now hand you over to Dr. Werner Lanthaler, who will lead you through this conference. Please go ahead, sir.

Werner Lanthaler

Welcome. This is Werner speaking from Evotec, thank you for taking part in to our Q1 quarterly call. We have uploaded a presentation and we hope that you can follow with the presentation through the discussion of our results, together with my management team which is assembled here in Hamburg. I have Enno Spillner, our CFO, with me, I have Craig Johnstone, our COO, with me and I have Cord Dohrmann, our CSO, with me.

When you go to page number two of this presentation, we want to first say welcome and at the same time, we want to say, like we do it on the cover page of this presentation: one secret of reaching highly aspirational goals, getting fast forward and even getting ahead of plans is to just get started. And if you get started at the right pace then you are up for a good year. With this, we are happy to report that we have started 2019 with a strong first quarter, and we are also happy that there will be three more strong quarters to come in 2019.

When you go page number four of this presentation, we can report that the state of play of the company basically reflects strong scientific and operational progress. You see here some bullets of the activities that we basically report back to you highlighting that we are at this stage following consequently following our strategy to build a world leading external innovation platform. Cord and Craig will then bring you closer to the individual events that you see here, but let me, on page number five, for a second, reflect what we are doing also in numbers. Enno will then give you more details. But what is clear is that you see a strong financial performance which basically reflects in a 20% growth on our top line, that the idea of a macro trend which is just starting is reflected on our platforms from every angle. Translating a fast-growth business also into a profitable business, which you see in our EBITDA growth, is of course making us extremely happy because that gives us the freedom to invest even more than ever before in break-through innovations, which we do in our unpartnered R&D at this stage, which will translate into high value deals at a later point alongside our strategy going forward.

When you go to page number six, let me highlight again, that there is an underlying macro-trend of excellent innovation which is just starting in drug discovery. This is why we are following a strategy that is consequent and where there is a consistent move forward along

this strategy. This is also why we put our strategy in action plans where you have seen three of them already, but there is more to come in the future. With this I hand over to Enno.

Enno Spillner

Thank you, Werner, and welcome everyone on the call also from my side. Happy to take over to provide very positive Q1 2019 numbers in more detail and confirming that Evotec is well on track compared to what was planned and what was guided. Let me start on page number eight. Looking at the group consolidated level, one can observe a 27% uptick in revenues compared to 2019 and on the next slide I'll get into more details regarding revenues and gross margin. So, looking at the R&D efforts here right now, the R&D efforts experience a very significant step up as indicated already during our last call in March, and please bear in mind, that out of this 14.4 million R&D total, 8.1 million are considered unpartnered R&D, which means we are investing significantly more into own projects and own platforms to support our long-term sustainability, for example in the field of metabolic and oncology diseases, as well into our iPSC research, for instance. For comparison in Q1 2018, we had invested about 4.6 million euros at the same time. With regard to SG&A, we are pretty much where we want to be, and SG&A costs are growing, but still, again, like in the previous quarters, under proportionally. Strong growth of the other operating income results from growth in R&D tax credits on the one side and reimbursement of our partnered R&D efforts in context of our Lyon ID activities covered by Sanofi. The letter was not yet in place in Q1 2018, as a reminder, and this also explains one major part of the step up of other operating income in 2019. As a result of the just described, Evotec shows a more than doubling in adjusted EBITDA, and furthermore this positive development is supported by a first time, 3.1 million positive impact through first time application of IFS 16.

Moving to page number nine. Obviously, the positive revenue growth trend observed in the past years could be continued in Q1 of this year. As you can see, this increase was mainly triggered by solid growth of the base business and strong milestone achievements in the EVT Execute and the EVT Innovate segment, for example from Bayer and from Boehringer Ingelheim. This growth of the base business of almost 19%, and it is almost in the same ballpark, in the same range as we saw it in the previous full 2018 average numbers. These two positive revenue effects plus some favorable FX backwinds which are triggering about 1.5 percentage points in our margin, helped increase our gross margin significantly by 7.9 percentage points to now 30.5 percent. To be noted, that also without positive impact of the milestones we can see a positive development of our gross margin.

Slide number ten. Good news on both segments, EVT Execute and EVT Innovate. EVT Execute revenues increased by almost 28% compared to Q1 2018 and EVT innovate is even up over 80% when compared to the same period of the previous year. The significant R&D efforts increased to 16.3 million compared to 5.6 in the EVT Innovate segment in Q1 2018, and this is again a split of an increase in the unpartnered R&D and as described before and new in Q1 2019 the partnered R&D of an amount of 6.3 million euros.

One reason explaining the strong upswing of other operating income are obviously the reimbursement of the R&D costs as I just mentioned by Sanofi. The EVT Execute EBITDA almost doubled compared to Q1 2018, while EVT Innovate improved but remained slightly negative compared also to 2108 Q1.

Slide number eleven is a little bit the exemption from the rule which I will only apply in this quarter. Due to the significant impact through first time application of IFS 16, I would like to draw your attention to a few non-P&L numbers but focusing on balance sheet and cash flow. Balance sheet total went up almost 110 million to a strong 881 million at the end of Q1 of this year for the reasons described on the slide, however the major impact being triggered by the first time application of IFS 16, which is namely an increase in property, plant and equipment following the capitalization of operating leases as now fixed assets according to the new rules. And effected loans and financed leases which are affected significantly by this new measure. Beyond that, Evotec continues to maintain a conservative net debt ratio of roughly 0.8% and we also maintain a strong equity ratio of 51% compared to 55% at the end of last year and maintaining a strong liquidity position of 141.6 million euros at the end of Q1 2019. So, overall presenting a very solid balance sheet and a very strong cash position. Having said that, I would like to hand over to Craig to introduce the EVT Execute part.

Craig Johnstone

Thank you, Enno, and good afternoon to everyone on the call from me. Together, Cord and I will update you on the key aspects of the scientific and operational performance in Q1. On page 13 this diagram simply serves as a reminder of our blended business model through which we offer access to scientific excellence and create value for our partners and ourselves through a range of business models, whether it is through fee-for-service or FT models or indeed by means of advancing technologies and assets internally for partnering later, it is our intention to build up a broad and valuable portfolio of co-owned programs which have built-in quality for survivability and success through the development process.

On the next slide, page 14, we see that the strong financial performance in Q1 already detailed by Enno, has been underpinned by a very strong quarter of scientific progress in major partnerships. By leveraging all our scientific know-how and experience, coupled with advanced technologies, predictive science, machine learning, AI and short cycle times, we drive the highest probability of success in all our projects. Successfully moving projects rapidly through the drug discovery and development process typically drives not only extensions of existing contracts, but often expansion of these partnerships to engage a wider breadth of resources and capabilities. The close integration of all these capabilities under one Evotec roof, enables us to provide our partners with the high flexibility as well as quality throughout, whatever the project needs. Thus, all parts of the business - Evotec, Cyprotex and Aptuit - often working together, have all performed well in this quarter. As ever, we continue to monitor operational efficiency and optimize our infrastructure. We have decided to consolidate our small molecule high-throughput screening site in Basel with our Toulouse operations. Over the coming months, the business will transition to Toulouse, where greater critical mass and co-location of screening and compound management offers optimal efficiency of operation. And of course, we are actively offering support to our 15 affected colleagues there. Pleasingly, we are also witnessing a steady flow of projects moving from the Evotec discovery infrastructure into Indigo, which provides enormous savings of time and complexity for our partners at this very critical stage of a drug's life cycle. As a result, and as you see on page 15, we continue to see a very high return rate, over 90% of our broad and global customer base. Perhaps a couple of noteworthy details here: today we work with 19 of the top 20 pharma while at the same time we create large, long-term strategic partnerships, also with foundations such as CHDI, and many biotech companies around the world: Carna, Tesaro, Abivax, to name just a few. With that, I hand over the next part to Cord.

Cord Dohrmann

Thank you Craig and good afternoon to everybody on the call. After a very successful year in 2018, EVT Innovate continues with a strong start into 2019. In the first quarter of 2019, we have already achieved a number of milestones. Most importantly, we have further progressed our partner product pipeline. We added, for example, Galapagos to our long list of partners in a fibrosis-focused partnership. In the anti-infective field, we forged alliances with the Helmholtz Institute for Infectious Diseases and GARDP, a global antibiotic research organization. Furthermore, we added two strategic partnerships in oncology, one with Indivumed in colorectal cancer and another one with the Mark Foundation in immuno-oncology.

On the next page, page 17, you can see that we are well on our way to further broaden and deepen our partner product pipeline. Overall, we have already added five new partnerships and at the same time keep progressing projects on a very broad front. We are very excited about advances in clinical development. Here we already reported two clinical starts, one in chronic cough through our partnership with Bayer and another one in NASH through our partner Second Genome. Unfortunately, not everything is always progressing as planned, so we were recently informed by our partner Second Genome that the NASH trial was put on hold. Although this is unfortunate, this really exemplifies the strength of our EVT Innovate strategy. Having built and continuing to build a very broad pipeline of co-owned projects, one project not moving forward is a setback but is clearly not the end of the world. In this respect we are very much looking forward to Phase II results in chronic cough this summer and hopefully further clinical starts before the end of the year.

With the following page, page 18, we would like to remind you that we continue our efforts to redefine the drug discovery paradigm through focusing on patient-centric approaches and that this puts some of the more recent years in context. Pursuing patient-centric approaches really starts with a better understanding of the disease and the disease-related processes. This can be achieved by extensive profiling of individual patients over time, and in particular conducting molecular profiling through -omics approaches such as genomics, transcriptomics and proteomics. Accessing clinical patient records and combining these with comprehensive molecular profiles through -omics datasets provides new insights into molecular disease processes, which can then be targeted with interventional therapies. In the past we have already made investments into accessing patient data at a larger scale, for example through our NURTuRE consortium and chronic kidney disease, and the most recent collaboration with Indivumed aims at a similar approach, this time just in colorectal cancer.

As you can see on page 19, Indivumed is a company focused on establishing biobanks in the field of oncology. We decided to join forces with Indivumed in the field of colorectal cancer where they have assembled one of the most comprehensive collections of patient samples and have already established molecular profiles using a comprehensive or mixed approach. Together with Indivumed, we will analyze these datasets to select novo mechanisms and targets in order to bring them forward into drug discovery programs. As we are discussing patient-centric approaches, I would like to briefly give you an update on our NURTuRE initiative on page 20. We are continuing to invest into the generation of molecular profiles database for kidney diseases based on the NURTuRE consortium. This project has made great progress in that we were able to demonstrate that molecular profiles are very useful in the stratification of patient populations, the validation of targets and biomarkers and generally the program is generating an increased interest in the industry.

On the next page, page 21, I would also like to briefly update you on our iPSC based drug discovery platform. Once we have generated patient direct molecular disease profiles, the next step is to move these forward into in vitro models. Moving this forward, our iPSC based drug discovery platform is ideally suited to develop patient derived cell based disease models for screening, hit to lead, and lead off campaigns. As you can see on page 22, here we are not only continuing to make progress in our partnerships for Sanofi and diabetes and Celgene neurodegeneration, but also in establishing further cell types. Most recently, we have built a microglia platform which allows us to generate human microglia at a high throughput for screening purposes. This is a great progress as microglia are thought to be highly relevant for many CNS-borne diseases and will open doors for many more project-focused approaches in microglia, including neurodegeneration, neuro developmental disorders and neuro inflammation.

So, in conclusion, all in all, we have had a very strong start into 2019 for EVT Innovate and expect to continue on this path going forward. With this I would like to thank you for your attention and hand over to Werner.

Werner Lanthaler

Thank you so much. When you go to page 24, let's round up. It is about getting started, but for us it is about creating a long-term consistent strategy. And with this we are well on our way for a strong 2019. With this we confirm comfortably our guidance for 2019 by basically growing about 10% on our group revenues, by growing about 10% on our adjusted EBITDA and keeping our unpartnered R&D expenses at between 30 and 40 million euros, which is the highest investment that we have ever done in the history of the company to create long-term partnerable projects out of these R&D investments.

On the last page you see important dates coming up. And with this let us thank you for following Evotec from quarter to quarter and growing together with us. Thank you so much. We are open for all questions.

Sami Devani (Arrex Securities)

Thanks for taking my questions. Congrats on another good quarter. I have just got a couple, just on the Second Genome project. Just wondering, have you got any other backup p2x7 inhibitors that you are working on with Second Genome or anywhere else in the portfolio? So, I guess that is the first question. And just, within the statement you talk about a seasonal high cash outflow. I am just wondering if you could just perhaps provide a bit more color on that because it is not apparent, at least to me, it's in the Q1 for 2018 and 17 with seeing that. So, could you just give a bit more detail on that. Thanks very much.

Werner Lanthaler

I think that is a fair question. So, on p2x7, yes there are other p2x7 projects in our portfolio, but not together with Second Genome. So that is the answer to your first question. And on the cash outflow I will hand it back to Enno.

Enno Spillner

Yes, pleasure. Sami. So at the end of 2018 we had a cash position of roughly 149 million, which then to the end of Q1 reduced to 142, so not a huge change; however, in the meantime paying back another 15 million euros of debt of our Deutsche Bank bridge loan of the Aptuit acquisition in Q1 and another 15 million immediately after, closing Q1 completely winding this loan down, driving it back to zero, so in this regard there have not been any major changes with the exception of having twice a payback of this loan.

Brigitte de Lima (Goetzpartners)

Hello. Good afternoon. I will ask silly questions, if I may. So, the first one is maybe just some clarity on the EVT Innovate revenues. Just, really, to understand, I mean, the numbers are very high, to start with, it is a very strong result for the EVT Innovate business. How can we understand what the balance is if we take one side, the milestones you disclosed, what was the rest of the revenue related to, and that would, I think, help us understand. The second would be on the Indivumed collaboration. I am just wondering, how it is actually structured from a financial point of view, without asking for specifics. Do the companies both invest in working on something and then if Evotec develops molecules Indivumed retains some sort of royalty? And then the last question would be on the Bayer chronic cough. There are now two projects in Phase II, and I was just curious to understand how the two molecules differ in terms of the chemical series they come from, do they have the same target, is the expectation that they would be positioned in different ways or is it a way for Bayer to reduce the risk, to make sure that at least one of those will eventually go all the way through the development? Thank you.

Werner Lanthaler

Maybe starting with your third question because the second question will go to Cord, the first question will go to Enno. The philosophy behind all our large partnerships is to create a portfolio of options to basically master a disease. That is what we are doing also in the field of endometriosis, like we do it in chronic cough together with Bayer. So you should assume that there are different molecules coming from different chemical series in different mechanisms where we always try to go through one bottleneck, which very often is a predictive model, and then we say okay, if there are two compounds than we try it with two compounds to see which one ultimately is better serving the indication. Then, as you also know, many indications have different ways of treatment within the indication. That is, at this stage, too early to tell and unclear, and that is the reason why we are in these indications together with our partners in the large collaborations like Celgene neurodegeneration or Bayer in the metriosis in cough, going here for multiple options. At the end, of course, you will be happy if you have one compound going into a large Phase III, because that is where the cost of running a Phase III ultimately has to be taken into consideration and account. But that is just the philosophy behind the P2X3'sPhase 2s and Phase 3s that you see in this collaboration and also an important guidance point. We expect from these ongoing Phase II's by the end of 2019 the first data points which I think also guides us very nicely into a potential royalty coming out of these projects, hopefully. Question number two goes back to Cord and is on the Indivumed partnership.

Cord Dohrmann

Thank you for your question. So, the Indivumed partnership is in line with many other partnerships that we have structured with academia and smaller partners. Here, essentially, Indivumed invested heavily already into the collection of patient-derived colorectal samples

and the characterization of these samples via a panomics approach. Here now at this point in time we are coming in to help analyze these data sets and identify novel targets and mechanisms to pursue and bring them forward into drug discovery programs. Here primarily Evotec will invest in these steps going forward and Indivumed will participate in royalty rate from whatever we will ultimately, when we commercialize, what Evotec will be getting, they will get a share depending a little bit on how much we have actually invested before the partnership is signed.

Werner Lanthaler

Thank you. Question number one goes back to Enno.

Enno Spillner

Yes, coming back to the segment revenues of EVT Innovate, which indeed increased at about 80% as I described before. This is a mix of an increase in the field of milestones, up fronts and licenses which, if you take a look at that part is about triple compared to Q1 2018. 2018 was relatively low in that regard. And then it's also in the normal course of business, just growing our collaborations and here is just one example: the Celgene onco deal was struck last year in Q2 and was not in as a comparison in Q1 of 2018, and these large collaborations make a significant difference compared to the previous year.

Werner Lanthaler

Does this answer your questions, Brigitte?

Brigitte de Lima (Goetzpartners)

Yes, mostly. I am still a bit puzzled about EVT Innovate, because my understanding was that it is mainly deferred revenue and licensing revenue. So, the Celgene onco deal, is that, are we talking about deferred revenue or is it an ongoing license fee that they are paying you, or what exactly are we looking at there? I am really just trying to get to grips with what is in there apart from the milestones that we heard about.

Enno Spillner

Well, you have just a normal collaboration ongoing, where we have received the cash in already in May of last year and now it is being deferred over the period of the collaboration triggering revenues over the quarters that we are working in.

Brigitte de Lima (Goetzpartners)

Okay, so it was the deferred revenues. that is what I was after. Thank you very much indeed. Very clear.

Michael Higgins (Ladenburg)

Thank you operator and congratulations guys on the continued execution. A couple of questions if we could. Regarding the unpartnered R&D: how does it compare to the partnered R&D expenses for the quarter. Also, on the unpartnered iPSC expenses: is that work that is

conducted on a partnered program or work toward reaching other iPSC collaboration agreements? Thanks.

Werner Lanthaler

Welcome to New York City. Hi Michael. Maybe first on the iPSC platform because that is simple. Everything at this stage is partnered is within the partnerships that you see out of the Celgene neurodegeneration partnership or within the Sanofi beta cell collaboration. All the rest of our R&D investments is in unpartnered protocols out of the iPSC platform. If you want to give this a number it is somewhere between five, or probably even a larger number of ongoing larger projects within this platform that we are preparing here for future partnering, which can be in the next two to three years. On R&D overall, I hand back to Enno.

Enno Spillner

So, out of the split where the total was 14.4 million, the partnered R&D is about 6.3 million euros, so that is the part that is being reimbursed by Sanofi under other operating income and then logically about 8.1 million is the part which is unpartnered, so that is the effort into our own platforms and product candidates.

Werner Lanthaler

Does that answer your questions, Michael?

Michael Higgins (Ladenburg)

Yes, that is very helpful, thank you. If I could ask one more: I am trying to understand the consolidation of the Basel activities and to the Toulouse site. How many employees do you have there now, what programs are being worked on there and how has this changed since the Sanofi agreement? Thanks.

Werner Lanthaler

So, maybe Craig is, as he is the site head of Toulouse, the best to give you information about the Toulouse site.

Craig Johnstone

Sure. Thank you for the question, Michael. So, today Evotec is operating three high throughput screening centers. You'll understand the business is very intensive, very investment intensive and so on. The Basel site was brought into Evotec as part of the acquisition of Aptuit. So, what we are doing is consolidating the work from Basel into Toulouse, where we have co-location of both a very broad and large high throughput screening facility alongside very important compound management, compound dispensing capabilities. And these work together in tandem to optimize the efficiency of high throughput screening and hit finding operations. So, we have decided to move the work from Basel to Toulouse and bring to an end the operations in the Basel site around quarter 3 of this year. It affects 15 members of staff.

Werner Lanthaler

Which are invited to go to any other site. That is one additional information, the other information is that when you look at Toulouse, we took over Toulouse in 2014 with 208 staff and by the middle of 2019 we will be above 480 people who are operating in our Toulouse site now, which makes this in itself a highly productive, highly efficient and a great site where we continue to grow because the footprint and the capacity available in Toulouse is there. The site was built for even larger capacities in the past. The other point about Toulouse is that France is an excellent recruitment ground because the scientific talent we can attract in France to Toulouse is outstanding and as we are one of the faster growing companies in the field of life science in the south of France, we are a highly attractive employer in that region so that is why many, many positives are coming together in Toulouse for us.

Michael Higgins (Ladenburg)

Okay. That is very, very helpful. That is great, thank you. Just one brief follow-up, if I could, is the potential expansion that you could incur organically in that Toulouse facility. You are about 480 or so now, how many employees and how much operationally could you expand to there? Thanks.

Werner Lanthaler

So, at this stage, we are growing at every site within the footprint of Evotec. I think that is an important message as well. We are growing very strongly, for example, in our Verona site, we are growing very strongly in our German sites, we are growing very, very strongly in our US operations and of course we are also growing massively in our Manchester, in our Abingdon operations in the UK. The capacity limitation for Toulouse is something where again, this is a former pharma site, which was hosting more than 1,000 people on that site, so there would be enough capacity and space to grow, that is not limiting organically at this stage the growth of the Toulouse site.

Victoria English (Ever Now Publishing)

Yes, Werner, I have two questions: the first concerns your activity in the area of antibiotics. Cord quickly mentioned that in connection with the infectious, I think it was a consortium or a group that you are working with. If you could just tell us a little bit about what you are contributing to that. And the second question concerns the microglia, the comments about the iPSCs and what could be done here in understanding CNS diseases. The question is whether this has application to Alzheimer's and the sub-question to early stage Alzheimer's and the reason I mention this is that SI has just started or set up an agreement to work with a number of US institutions to try to work on early stage, an indication for the two drugs that it is taking through Phase III.

Werner Lanthaler

Thank you so much. Hello, Victoria. Both questions I direct to Cord.

Cord Dohrmann

More generally speaking, what are we doing? So, we have a number of ongoing projects in the antibiotics field and are constantly trying to grow this portfolio going forward. We have

built, for example, and announced a partnership with the Helmholtz Centre here on a new class of natural products that have brought spectrum activity on microbes and particularly multi-drug resistant microbes. We are highly excited about this; this could lead to a whole platform of new potential first-in-class antibiotics and we are currently evaluating further opportunities to expand the portfolio here. I think that is all I can say at this point in time about the antibiotics franchise. When it comes to microglia, microglia is a cell type that is thought to be high relevance to many CNS-borne diseases, and it has just been very difficult to access because it has not been possible to drive human microglia in in vitro and use them for screening purposes. Microglia, as you mentioned, is clearly relevant for neurodegenerative diseases including Alzheimer's disease and here in particular the neuroinflammation angle is an angle that is of great excitement. But it is also highly relevant to neurodevelopmental disorders and other neurological diseases which are not in the scope of the Celgene collaboration. This is also why I called it a platform, because it really can be leveraged in all sorts of directions, and we are just very excited about having been able to put this platform in place and making it work and now we will try to exploit it going forward.

Norris Johan (Intrinsic House)

Hi there, it is Norris Johan, from Intrinsic House. I have a few questions please. Can you give us some sense of the size of the milestones that you negotiated on some of the more recent partnerships in EVT Innovate, as well as a nearer number of new clinical starts? How should we be thinking about the size of any potential milestones relative to what we have seen in the past? And then last year we saw you spent more money on R&D as your revenues surpassed your initial expectations through the year. This year looks like we could be in a similar position from a revenue perspective, and so, philosophically, do you see the need to accelerate some programs or invest more heavily in 2019? And then I have a couple more if you could come back to me please.

Werner Lanthaler

So, I think the first, on the design of our partnerships. I think here, on our milestone and co-ownership driven partnerships, you should see that of course it always comes down to what is the first-in-class situation of a certain target that we are partnering, what is the competitive situation, so there is an individual life behind every contract of our 100 co-owned EVT Innovate projects. The average number of milestones is around 200 million milestones per co-owned project, that is the first thing. The average number of royalties that is behind every one of these partnerships is on average 8%. Coming to your specific question, how does this look in recent years, compared to 5 years ago, it also comes down to where does the partnership originate? If, for example, a partnership originates from our iPS platform, we have always been able to negotiate double-digit royalties and milestones that are significantly higher than the 200 million that I have just described as an average. And that is, I think, a pattern where it comes down to what is the first-in-class potential and what is platform and the competitive situation, that we can bring together into a partnership for these types of transactions. When it comes to our R&D "need" going forward, that is the way I interpret your question, I think you should see that for us it is not driven by how much R&D do we want to spend or can we spend, it is really driven by what project is exciting us and where do we see a first-in-class opportunity to invest in. I think that is a situation where at this stage we are not able to invest in everything that is exciting us because of capacity limitations. That is also why we are planning for the very long run, because many of the things will not just go away in drug discovery this year or next year or the year after. We are at the beginning of our R&D

efforts in drug discovery because we are at the beginning of curing or going to cure certain disease areas and that is why limiting this to the view of one year is probably not enough. That is why it is such a great situation to have a profitable company going forward and that is why we are "capital market independently" able to tailor our R&D investments on the platform. Sorry for a philosophical answer on that question, but that is really how we operate.

Norris Johan (Intrinsic House)

Okay, thanks. And then a couple more, just following on from that, are there any programs derived from the iPSC platform that are nearing entry in the clinic that could help us validate the platform? And then on the iPSC platform, it is clearly a very sound technology, but we haven't seen any major new partnerships for a while. Is that because you are still working on things like the microglia work or is it that the two most obvious applications where one is Sanofi and one is Celgene is signed up and so you've got anti-compete clauses that prevent you from signing new deals. Just some kind of insights as to where that platform is going and what the opportunity is in the near to medium term, I think would be helpful.

Werner Lanthaler

So, I think to the second part of your question, nothing would hold us back given the existing partnerships to sign new partnerships. I can also disclose there is enough interest in the market to make new partnerships with us. There is more excitement than ever on our iPSC platform for the projects that we are bringing forward here. Having said that, we are just value optimizing here, while sometimes investing a bit more in kick-starting the project, building on the platform, making them even more robust than we have been able to do in the past. That is why not signing new iPSC deals I think is a good sign. It is not a sign of a non-availability of partnerships here. And on your first question, we will report once we are there in the clinic. All I can say at this stage, that the portfolio of targets nearing the clinic out of both collaborations, the beta cell collaboration but also the neurodegenerative collaboration looks good. And at the same time I just don't want to make specific guidance to specific dates.

Norris Johan (Intrinsic House)

Thanks. Could I just sneak one more in? Which is on the margin guidance. You have kept your margin guidance the same, despite the currency tailwind on the gross margin. So, should we expect these currency tailwinds to ease through the year and therefore can expect a slightly weaker margin as we go through the year?

Werner Lanthaler

We are, unfortunately, or fortunately, not in the situation to predict where currencies will go, but I think the good situation in Evotec is that there is a kind of a natural hedge in the company. So, we have a cost base, we have a cost base in the US, we have a cost base in Europe, we have a cost base in the UK, so there are three currencies affected by that. We have a revenue base coming out of the US, increasingly coming out of the US, increasingly signed up in US dollars and we have a cost base in Europe, so that is why there is a natural hedge that is good. Our exposure over all to SX is kind of limited. Having said that, we then use all tools to get the smoothening of the FX into our P&L and I think that is the daily bread and butter of our finance teams here to optimize that.

Frank Gregorie (Trinity Delta)

Hello gentlemen, good afternoon to you. Let me ask a provocative question: your revenues are rising, your margins are expanding, your cash flows are very solid, your debt position is very controlled. Is it time to start paying dividends?

Werner Lanthaler

It is actually a technical situation where given the loss carried forward that are in our group at this stage are still existing, so therefore technically we are not, and legally we are not allowed to pay dividends. Having said that, that is a situation which will come, which is fantastic for a company to have the optionality to think about these things, especially for biotech companies because, as you know, there are 4,400 biotech companies out there. Less than 2% of them are profitable, and we are one of them Having said that, the synchronization that we want to get with our shareholders and investors is that we want to dividend in to our EVT Innovate segment because here the value creation is disproportionately higher. And by dividending out on short term cash dividend that we would give at this stage to the company. That is the long-term potential that we see arising from the platform. Having said that, it is a fantastic situation to also being able to not only on an abstract level but on a very specific long-term plan, also to think about cash dividends in the long-term future.

Brigitte de Lima (Goetzpartners)

Hi, just one question: I noticed that the revenue coming from biotech now stands at 46% which I think is the highest, at least that I can see in my model. So I think that is quite telling of the broader environment, it really seems to be biotech that seems to be outsourcing and potentially also increasing their spend the most, but is this now, has this group now firmly become your largest customer group going forward as well or was it a one off and if biotech is your biggest customer group, does that change the average structure of the contracts and the duration, are these sort of long-term clients or is it more piece meal, does it make the business harder to manage or is this a very positive thing that you are having to cater to more and more biotechs?

Werner Lanthaler

I think that it is a situation where ultimately the idea of virtualization and capital elasticity will drive all of our partners. Of course, the group that stands out here is virtual biotechs, especially coming from the east coast of the United States, where you have a very good funding environment for the last years which will also drive our long-term growth here. But again, having said that, we see for all institutions that do drug discovery, a trend towards virtualization and using companies like Evotec in partnership with them. The other thing I want to highlight here is that it is not biotechs only. Let me stress the importance of foundations in our business model going forward. Going back here between five or ten years, foundations did not exist as active players in the drug discovery world. Now, this year we will make significant revenues with foundations where you see an element of virtualization really in its best practice, because you come from the patient, have money that is on the drug discovery platform, immediately put to work and then goes back on to clinical platforms and allows many, many foundations to get into the market. Just to give you here a number, there are more than 400 patient foundations out there who want to definitely do something in their mission and that includes also drug discovery work. That is also just starting as a process and

here a platform like Evotec is ideally suited for this customer type. So yes, biotech is growing also given the business mix that we are creating through our Aptuit acquisition that we brought in two years ago because here we are providing, for example, Indigo, for example, so marching in to a clinical trial, packages which are of course ideally suited for this kind of customers and that is why you seen biotechs growing, you will see foundations growing and you will also see an increased virtualization, and capital elasticity driven pharma market. Sorry for a long answer to a short question, but yes, we love biotech.

Werner Lanthaler

If there are no further questions, let me thank you again. It is our pleasure to work for our partners, it is our pleasure to drive R&D forward and it is also our pleasure to serve our long-term shareholders, who build Evotec together with us. Thank you so much.