



## **MorphoSys AG – Q1 2011 Conference Call Text**

April 29, 2011

*The spoken word shall prevail.*

### **Dr. Claudia Gutjahr-Löser, Head of Corporate Communications & IR, MorphoSys AG**

#### **Slide 2: Today on the Call**

Good afternoon and welcome, this is Claudia Gutjahr-Löser, Head of Corporate Communications & IR of MorphoSys. With me are Simon Moroney, our CEO, and Klaus de Wall, Head of Finance & Accounting. Jens Holstein, who will join MorphoSys on Monday as our new CFO, is on the call as well.

First, we would like to welcome you to our Q1 conference call and thank you for participating. During the call, we would like to talk about the Company's financial results for the first three months of 2011. Simon will start by giving you an operational overview of the quarter followed by a review of the financial results. Afterwards, we will open the call to your questions.

#### **Slide 3: Safe Harbor**

Before I start, I want to remind you that during this conference call we will present and discuss certain forward-looking statements concerning the development of MorphoSys's core technologies, the progress of its current research programs and the initiation of additional programs. Should actual conditions differ from the Company's assumptions, actual results and actions may differ from those anticipated. You are therefore cautioned not to place undue reliance on such forward-looking statements, which speak only as of the date hereof.

I would now like to hand over to Simon Moroney.

### **Dr. Simon E. Moroney, CEO, MorphoSys AG**

Thank you, Claudia. We've got off to a great start in 2011 with a record quarterly result and I'm very happy to review this quarter for you.

Before we start I would like to take the opportunity to welcome Jens Holstein, who will take over as CFO effective May 1st. Jens wanted to use this call to introduce himself to you all. He'll be happy to answer general questions on his appointment, but I'm sure you'll understand that he's not yet in a position to make any comment on our financial results – Jens.

**Jens Holstein, designated CFO, MorphoSys AG**

Thank you, Simon and thanks for having me on the call.

**Slide 4: New Chief Financial Officer**

Ladies and Gentlemen, it is a great pleasure for me to have the chance to introduce myself to you today. As I am not officially in charge yet, I am not in the position to answer questions on the Company or its results but let me share with you at least a short overview about my professional experience. During the last almost 16 years, I have served in a variety of financial and general management positions within the Fresenius Group. Starting in Dialysis via the hospital project business and the hospital operations business of Fresenius, I moved to Fresenius Kabi, the infusion therapy, nutrition and IV generics business of the Group. From 2006 to 2010, I was Regional Chief Financial Officer of Fresenius Kabi Asia Pacific, based in Hong Kong and most recently I was responsible, as CFO, for the region Europe and Middle East for Fresenius Kabi.

In summary, I have had the chance to work in a broad range of teams within the Fresenius group, notably in healthcare. Prior to Fresenius I have spent a number of years in the consulting industry, with positions in Frankfurt and London, mainly in the fields of mergers & acquisitions.

Personally, I am really excited to join MorphoSys and I am looking forward to using both my financial expertise and healthcare knowledge to help bring this Company to another level. I also look forward to meeting, working and collaborating with all of you in the future. Thank you very much.

**Dr. Simon E. Moroney, CEO, MorphoSys AG**

Thanks, Jens, we look forward to welcoming you on Monday. With that, I'd like to start with the operational review of the quarter.

**Slide 5: Q1 2011: Operational Highlights**

Clearly, the most important event was the successful installation of our technology at Novartis, which triggered a double-digit million euro payment to us. Primarily as a consequence of this milestone payment, we have reported a record quarterly result, both in terms of revenues and profits. It should go without saying, but I'll say it anyway, that you should not extrapolate from this quarter's result to the full year. As always, individual quarters can fluctuate, and the most important orientation we provide is our full-year guidance, which we re-confirm today.

The milestone payment makes a major contribution to our targets for revenues and profits for the year as a whole. Most importantly, the internalization of our HuCAL technology by Novartis underscores once more the commitment they have made to our technology. This is also evident in the productivity of the alliance. Novartis now has five HuCAL antibodies in clinical development with, we hope and expect, many more to come in the years ahead as the earlier-stage programs advance. Overall, based on the number of therapeutic antibodies in clinical development, we believe that HuCAL is the industry's most successful antibody library technology.

Two other noteworthy events during the quarter relate to our proprietary development segment. First, we strengthened our US patent position on our lead program MOR103. The new patent covers the antibody itself as well as pharmaceutical compositions comprising the antibody and is scheduled to expire in 2026, not including any potential extensions. This newly issued patent complements a US patent granted in 2008 covering medical uses of antibodies against GM-CSF, to which MorphoSys has exclusive access under a license agreement with the University of Melbourne. Together, the two patent families provide strong intellectual property protection for the MOR103 program.

The other highlight in Q1 in the Proprietary Development segment was the manufacturing agreement we signed with Boehringer Ingelheim. This agreement covers process development and manufacturing of MOR208 clinical material, as well as other drug candidates. You'll recall that MOR208 is currently being evaluated in a phase 1 clinical trial in the USA by our partner Xencor. While we're happy with the manufacturing process we're using at present, this deal with BI will help to prevent any bottlenecks in clinical trial supply in the years ahead. Establishing a commercial manufacturing process early in the development of MOR208 will clearly increase the value of this program.

## **Slide 6: Q1 2011: Development Pipeline**

Overall, the current pipeline comprises 74 programs of which 18 programs are now in clinical development. The today reported IND from Oncomed is our 18<sup>th</sup> program in clinical trials. The advancement of a second antibody from our collaboration with Oncomed underlines the success of the collaboration. This is not reflected in our quarterly reporting and the milestone will be booked in Q2 of 2011.

You will see that we have stopped one very early-stage proprietary program during the quarter for reasons relating to the validity of the therapeutic target.

Overall, the programs are developing as expected and we'll keep you posted on their progress as and when information becomes available.

Finally, a few words on the current situation in Japan. We have of course been in close contact with all of our Japanese partners, including Daiichi Sankyo, Astellas and Shionogi, and are happy to report that disruption brought about by the earthquake, tsunami and radiation has been minimal. It is harder to gauge the impact on our AbD business.

With that, I'll now turn to the financial review.

## **Slide 7: Q1 2011: Profit & Loss Statement**

The first quarter was an extraordinary one, financially speaking. Group revenues more than doubled to 48.6 million €. The main reason for the strong increase was the technology milestone payment from Novartis in connection with installation of the HuCAL platform at Novartis's premises in Basel. The payment is of major financial benefit to MorphoSys. Furthermore, this milestone underscores Novartis's commitment to HuCAL and the ongoing success of our collaboration based on the technology.

## **Slide 8: Q1 2011: Segment Reporting**

Looking at the segments individually, you see the strong impact of the milestone payment on the Partnered Discovery segment, both on revenues and profits. Revenues in the Proprietary Development segment doubled to 600,000 €. Those revenues arose from funded research payments relating to our two pre-development programs with Novartis. The performance of the AbD Serotec segment remained below the first quarter of 2010. The unfavorable comparison is due to a large OEM order which was placed in Q1 2010 and had a major effect on revenues as well as on profits. Despite the segment showing a loss in the first quarter, we fully expect to achieve our full year targets.

## **Slide 9: Q1 2011: Profit & Loss Statement**

Coming back to the P&L of the Group, total operating expenses increased by approximately 25% to 19.9 million €. The main reason for this was the increase in R&D expenses. We invested 6.6 million € in proprietary development activities and 0.6 million € in technology development. These are both within budget.

Profit from operations amounted to 28.8 million €, as a result of the above-mentioned milestone payment.

Net profit increased to 18.8 million €, corresponding to diluted earning per share of 81 Cents.

## **Slide 10: Q1 2011: Balance Sheets**

Looking at the balance sheet, our cash position increased to approximately 120 million €. In parallel, the accounts receivable position increased from 15 million € to 38.4 million €, as the milestone payment was still outstanding at balance sheet due date. Once again, our growing cash position shows the strength of our business model. This is a MorphoSys hallmark that distinguishes us from the majority of companies in our sector.

## **Slide 11: Q1 2011: Outlook for 2011**

Before we open the call for your questions, I want to confirm that we are well on track to achieve our full year targets. We continue to anticipate total Group revenues of between 105 million and 110 million €, and an operating profit of between 10 million and 13 million €.

We expect a year rich with newsflow, driven by our proprietary programs as well as the partnered pipeline. We expect to commence the phase 1 trial for MOR202 in the first half of 2011, and can confirm today that we will present some exciting pre-clinical data around MOR202 at this year's ASCO meeting. For MOR103, the RA trial is ongoing, and we are on track to start the safety trial in multiple sclerosis patients in the second half of this year.

For the partnered pipeline, we expect between one and three INDs this year, and potentially some data from ongoing clinical trials. The first of these INDs was the Oncomed one announced this morning. Such updates, of course, will be driven by our partners.

During the summer, we expect the first diagnostic kit based on a HuCAL antibody to be launched. We regard this as a significant milestone for AbD Serotec.

Lastly, we plan to publish an update on our latest technology development activities. All in all, we expect an exciting year.

That concludes my review for the first quarter of 2011, and I'll hand back now to Claudia for the Q&A session.

**Dr. Claudia Gutjahr-Löser, Head of Corporate Communications & IR**

Thank you. We will open the call now for your questions.

**Cornelia Thomas, WestLB:** Hello, good afternoon, and thank you for the short presentation. I've got a question on how you're planning to distribute the R&D costs over the remainder of the year. I'm currently assuming that there's going to be a ramp up towards the end of the year to prepare for further clinical trials, but just wanted to double check that that is correct; and then on the AbD segment, so are you expecting this to go into profitability again with the launch of the diagnostics kit or do you have any other plans to bring this back into profitability, and maybe if you could explain why it was non-profitable in the first quarter, please. Thank you.

**Simon Moroney:** Okay, thanks, Cornelia. First of all, regarding the R&D cost, yes, these were certainly ramped. Bear in mind that we currently have two proprietary clinical programs ongoing, namely MOR103 in the phase 1/2-trial in rheumatoid arthritis and MOR 208 in phase 1 for cancer. By the end of the year we expect to have five clinical programs ongoing so that means there are three more still to come; so that will, of course, be associated with a significant ramp up in R&D cost, and that's the reason why we stand by our guidance for R&D, for proprietary R&D investment of somewhere between 40-45 million for the full year.

Regarding AbD, as we said, and certainly in comparison to Q1 of last year, the product mix was certainly lower margin this quarter in comparison to the first quarter of last year, and we've also taken the opportunity to make some investments. We expect particularly on the OEM side of the business to secure some larger orders during the course of the year which will change the product mix and the margin balance if you like, and that's why we're able again to confirm our original guidance for that segment for the full year, which is revenues of between €22-23 million and a profit margin of around 4% of the operating level.

**Cornelia Thomas:** Thank you.

**Daniel Wendorff, Commerzbank:** Good afternoon, and thanks for taking my questions: two I have remaining now. Maybe one question for Mr Holstein and my line was not really good at the beginning so if you already said that, my apologies, but my question would be what made you move to MorphoSys? I was wondering whether you can give us a bit more color on that, and a follow-up question on AbD Serotec: can you potentially tell us what the underlying development, excluding the one-off in 2010, has been, and how the demand at the moment is developing in the different regions in the world? You mentioned Japan at one point, but how's the situation in North America and Europe? That would be helpful, thank you.

**Simon Moroney:** So perhaps we'll start with the first question: Jens, do you want to answer that directly?

**Jens Holstein:** Yes, sure, I can do that. Thanks very much, Daniel, for the question. I didn't actually explain it so it's fair to do that; basically, quite honestly, it has been a combination of the prospects of the company which I saw and I've heard about the team. It's always a combination of all those things. For me it was clearly not a decision against Fresenius: it was one for MorphoSys, and for me the opportunity to develop this company, which in my view has a very convincing and proven business model as well as the dedication and the spirit of the team, and the industry knowledge of the supervisory board as well were all aspects which I was impressed of when I made my decision, so I felt that MorphoSys would be the right environment offering the right opportunities and challenges for me. That's basically the reason.

**Daniel Wendorff:** Thank you.

**Simon Moroney:** And Daniel, your second question regarding AbD, I think the general trends we're seeing are currently that Europe is essentially flat, it's definitely a more challenging environment than it perhaps was in the past, and that's been counter balanced, if you like, by the US, which is proceeding extremely well for us at the moment, and so we're seeing good growth in the US. Japan is always a small part of our total market and it's also probably a little bit early to say in regard to Japan.

I think the other significant thing for us is that the first, as we mentioned, the first diagnostic products based on HuCAL are expected onto the market this year. These we think should be the first of a number of diagnostic products based on the HuCAL technology that we expect to see come into market and, of course, that should also help in terms of the profit margin of that part of the business. So although we can't right now on the call give you the exact impact of, or corrected for, the one-off event that we had in Q1 of last year, I hope that this general qualitative guidance that we give you on the various geographical areas is of help.

**Daniel Wendorff:** Yes, it certainly does, thank you.

**Sachin Soni, Kempen & Co.:** Good afternoon, everyone, my question is on the outlook. Two points. First you said data from ongoing trials of partnered programs: can you please specify which one we should wait for, for this year out of all those partnerships you have? And then you say further technology announcements: can you please specify something, in which direction we should be thinking that more technology announcements could happen, going forward? Thank you.

**Simon Moroney:** Sure, Sachin. Again, just to be very clear about the data from partners, we're really in the hands of the partners here. If they choose to say something great, if they choose

not to say something; of course, that's something that we can't influence. However, the most likely data that we could expect this year comes from a number of Centocor programs, particularly CNTO888, which is currently in phase 2-trials in lymphatic pulmonary fibrosis: that one probably won't report this year because we know that it is due to run on into next year, but the phase 2 cancer trial for that program may read out this year and Centocor may choose to publish data there.

The other two where we may see something, Centocor CNTO1959 and CNTO3157: these are programs in asthma and psoriasis, both currently in phase 1, due to be completed this year, and again, which we could potentially expect some data from, from Centocor during the course of this year.

In terms of the technology we don't want to pre-empt what we want to say here. As you know we continue to invest in technology in-house. A lot of what we're interested in here and what we've been investing is really making the ability to make better antibody based drugs, so you shouldn't be surprised that it will be an antibody based technology. But we think it will enhance our ability both our own and together with partners to make even better antibody based drugs; and I think more than that at this stage I wouldn't want to say for fear of pre-empting the announcement itself.

**Sachin Soni:** Thank you.

**Hanns Frohnmeyer, LBBW:** Good afternoon. I have just two small questions on your Q1 figures and then maybe one more on the prospectus. So your organic growth of the Partnered Discovery section in Q1, excluding milestones, could you give us a number for this: how high was organic growth and the second question is, just what interests me, is: what is behind this other non-operating expenses of roughly €1.3 billion accounted in the first quarter, and can we expect that this is a kind of run rate for the rest of the year or is it a one-time item? And maybe, in addition, more on your future: can we... you bought Sloning last year and pretty soon after that we found that nice contract with Pfizer and at that time you said you will probably have at least one or probably more than one deal coming up in the next quarters. So is it realistic to assume that we will find other Sloning technology-based deals in 2011? Thanks.

**Simon Moroney:** Thanks for those questions. First of all, in terms of the organic growth in the Partnered Discovery segment once you strip out the milestone: maybe a general comment here first is that, remember that we had always anticipated and planned for the fact that a number of the partnerships other than Novartis would expire, and obviously that means that revenues, collaborative revenues from those collaborations will also expire. The... essentially the trend between 2010 and 2011 in the first quarter's roughly flat. At about 13.7 million in the first quarter of last year versus 13.3 million in the first quarter of this year. As I said that was expected, and it

has to do with the fact that certain of these partnerships are expiring and that's something that we planned for. Can you just remind me about the second question?

**Hanns Frohnmeyer:** It was on these non-operating financial expenses, your account is 1.3 million in the financial results and I was just wondering because I haven't read anything on that.

**Simon Moroney:** Yes, I'm going to ask Klaus to answer that in one second. Let me just start by addressing your third question regarding Sloning. Yes indeed, we do anticipate doing deals around the Slonomics technology. Some of those deals may be Slonomics in isolation as was the Pfizer deal, but more importantly for us, we anticipate doing deals where the Slonomics technology is part of a package which may include specific, obviously antibody based, technologies.

As always, I don't want to comment on the timing of any potential deals but we do definitely see the Sloning technology as being a key part of our platform and should be definitely a key part of the deals and the partnerships that we do in the years ahead.

**Hanns Frohnmeyer:** Maybe just to add on this: is it right to assume that the current deal of Novartis, with Novartis, is not including the Slonomics technology, right?

**Simon Moroney:** That's correct. We've certainly had a discussion with Novartis, as we always do, about whether the technology is of interest, whether it can be added somehow to the collaboration, and those discussions are ongoing. So I hope that helps and I would now like to hand over to Klaus de Wall for the answer to the second one of your questions.

**Klaus de Wall:** Yes, this item of other expenses which you mentioned, 1.3 million: this mainly includes fx losses of approximately 1.2 million of this total amount, and this relates to cash inflows which came in foreign currency.

**Hanns Frohnmeyer:** Thank you.

**Thomas Schiessle, EQUI.TS:** Yes, hi, this is Thomas Schiessle from EQUI.TS in Frankfurt calling. Question to Simon if I may, concerning your collaboration with Boehringer Ingelheim regarding the production of antibody material. Is this because of reducing cost in the production, so changing technology leads to lower cost of goods, or is it because of spreading the risk when it comes to the production of clinical or commercial material? Thank you.

**Simon Moroney:** Thank you, Thomas. So first of all the prime driver for this collaboration was not purely about cost: it's really to ensure that we have a second source for the MOR208 program and also a source that we're confident could provide a commercial supply of material once a product comes to market or goes into late stage clinical trials and then comes to market. We're also delighted to have a relationship with BI who we regard as very much champions league, if not world champions when it comes to antibody manufacture, being located relatively close to us, of course, in Biberach... is also an advantage, so really from a number of points of view, including risk mitigation as you mentioned, diversifying the sources of supply, geographical proximity, those are all good arguments for us to be working with BI. And we foresee that this relationship will not just be limited to MOR208 although that's the initial focus, but we could foresee running future programs beyond MOR208 together with BI.

**Thomas Schiessle:** Is it the plan to spread the collaboration across the whole portfolio of future products at MorphoSys. So, that it will be your main producer of antibody material?

**Simon Moroney:** It's certainly an option. The decision there will be made case-by-case but we see this really as the start of what we hope will be a long and fruitful relationship with, as I say, clearly one of the world's leaders, if not the leader, in antibody manufacture.

**Thomas Schiessle:** When it comes to the commercial terms, is everything done in Euros or is there any foreign exchange risk in between from your point of view?

**Simon Moroney:** I'm 99% sure, not a 100% sure, but 99% sure that everything is in Euros.

**Thomas Schiessle:** Thanks so far.

**Daniel Wendorff, Commerzbank:** Yes, hi again, mainly a follow-up question on the proprietary clinical programs. You mentioned that there are two programs currently ongoing, and mentioned the ones which are ongoing: that's fine. You pointed towards five proprietary programs being active at the end of 2011. Can you remind me again, what are the three new clinical programs to start during the course of this year? Thank you.

**Simon Moroney:** Yes, Daniel, just to be absolutely clear here, we referred to clinical studies.

**Daniel Wendorff:** Yes, sorry, yes, that's what...

**Simon Moroney:** And the difference between the two that you know of and the five is: first of all a subcutaneous study of MOR103 so testing a subcutaneous formulation. Remember the current formulation in the phase I, II trial is an intravenous formulation, so that's one. The second one is the MOR103 study in multiple sclerosis, and the third one is the initiation of MOR202 in multiple myeloma.

**Daniel Wendorff:** Yes, perfect, thank you.

**Thomas Schiessle EQUI.TS:** Thanks. Thomas Schiessle, once again. When it comes to your partner, is there anything new on the Absynth collaboration or with Galapagos? To my knowledge there should be some milestones to be reached in 2011 so is there anything ahead of us?

**Simon Moroney:** So first of all both of those collaborations, both Absynth with the infectious disease focus remember, and Galapagos with the co-development of bone and joint targets are both proceeding well, but of course both are also at a phase that we would characterize as being discovery, so early stage, and as a policy essentially we don't comment on those early stage programs. Essentially because it's early and there's really not a lot we can say at this stage.

**Thomas Schiessle:** But there should be something coming out of these programs in the current year?

**Simon Moroney:** There are constantly results being generated. Whether we choose to say anything or publish any of those results is another matter, but you shouldn't plan on it, or you shouldn't assume it, and essentially that's because the stage programs, as is really commonplace throughout the industry, are largely not commented on.

**Thomas Schiessle:** Fair enough. Thank you.

**Mick Cooper, Edison Investment Research:** Just a quick question on the subcutaneous study. Will it look at safety and tolerability or is it going to be another trial in RA?

**Simon Moroney:** Thanks, Mick. This is a PK study, essentially looking at the bioavailability of the drug and its formulation versus the bioavailability in the intravenous formulation.

**Mick Cooper:** In patients?

**Simon Moroney:** In health volunteers.

**Mick Cooper:** Thank you.



**Dr. Simon E. Moroney, CEO, MorphoSys AG**

Thank you. I'd like to close by reminding you of the key messages to take away from this call.

The quarter was dominated by the milestone payment we received from Novartis, which sets us up well to achieve our financial objectives for the full year. Operationally we're well on track, and look forward to updating you further on our pipeline programs as the year progresses.

**Dr. Claudia Gutjahr-Löser, Head of Corporate Communications & IR**

That concludes the call. Should any of you wish to follow up with us directly, we are all in the office for the remainder of the day. Thank you again for joining the call and goodbye.

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