

The Biotech Growth Trust

Access to major innovation at low valuations

The Biotech Growth Trust's (BIOG's) highly experienced managers, Geoff Hsu and Josh Golomb, are able to draw on the considerable resources of global healthcare specialist OrbiMed. BIOG's performance has been particularly challenging as the managers favour emerging (less mature) biotech companies, which have fared particularly poorly versus the S&P 500 during the longest and largest ever industry drawdown. Hsu and Golomb believe that biotech share price weakness is disconnected from industry fundamentals, as company valuations suggest an industry lacking in innovation, which has historically been the biggest driver of biotech performance. This seems incongruous as the managers believe we are in a 'golden era of innovation' with important technological and medical breakthroughs and a continued high number of new product approvals across multiple disease areas. They believe that sentiment towards the most innovative biotech companies, with robust clinical data, will improve and that BIOG's portfolio is very well positioned to capture this move.

BIOG presentation (February 2025)



Source: BIOG

Why consider BIOG?

BIOG had a strong record of outperformance until Q121. Since then, smaller-cap biotech stocks have experienced what Hsu and Golomb refer to as 'an unprecedented valuation compression'. The managers are confident that emerging biotech stocks will benefit from a performance catch-up to large-cap biotech stocks, due to their high levels of innovation and depressed valuations; however, this move is taking longer than anticipated.

Biotech industry fundamentals remain very favourable, with 65% of the US drug industry pipeline originating from smaller-cap biotech companies across all therapeutic areas and a range of novel/next-generation technologies, which are represented in BIOG's portfolio. New drug approvals by the US Food and Drug Administration (FDA) remain robust, and M&A is expected to accelerate as large pharma companies are seeking reasonably priced products to replace major drugs going off patent (OrbiMed estimates c \$270bn between 2024 and 2030).

In general, investment company discounts remain wider than historical averages. BIOG's 9.3% discount is wider than its historical averages, which range between 5.6% and 8.2% over the last one, three, five and 10 years. A higher valuation could add to what could be considerable capital growth potential.

Investment companies
Biotech equities

18 March 2025

Price 782.00p
Market cap £217m
Total assets £240m

NAV 862.4p

¹At 14 March 2025.

Discount to NAV 9.3%

Current yield 0.0%

Shares in issue 27.8m

Code/ISIN BIOG/GB0000385517

Primary exchange LSE

AIC sector Biotechnology & Healthcare

52-week high/low 1,062.0p 764.0p

NAV high/low 1,156.3p 851.6p

Net gearing 0.0%

¹At 28 February 2025.

Fund objective

The Biotech Growth Trust seeks capital appreciation through investing in the worldwide biotechnology industry. Performance is measured against its benchmark index, the NASDAQ Biotechnology Index (sterling adjusted).

Bull points

- The biotech sector has delivered above-average returns for shareholders over the long term.
- Positive industry fundamentals and valuations, but the sector has been out of favour with investors.
- OrbiMed is a global leader in healthcare research and investment, with more than \$18bn of assets under management.

Bear points

- The focus on emerging biotech stocks was detrimental to performance during the latest sector drawdown.
- Biotech stocks can be volatile.
- Periodic political pressure.

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BIOG: Waiting for the performance gap to close

The trust has a structural bias towards smaller-cap biotech stocks as historically these companies have the better risk/reward profiles in the sector. Despite the recent underperformance of smaller-cap biotech stocks, BIOG has outperformed its benchmark since the fund's inception in June 1997.

Performance of the biotech sector

In Exhibit 1, we illustrate that although BIOG's exposure to large-cap biotech stocks has increased since the end of FY21 (March), which is down to their relative performance, BIOG's portfolio remains biased towards mid- and small-cap biotech companies. The performance of different sized biotech companies is stark: between 31 March 2021 and 31 January 2025, mid-cap biotech stocks trailed large-cap stocks by 27.6pp, while small-caps trailed by an even greater 30.5pp.

Exhibit 1: BIOG's breakdown by market cap and NBI* performance (end March 2021 to end January 2025)

% unless stated	BIOG (end Mar 21)	NBI (end Mar 21)	Delta (pp)	BIOG (end Jan 25)	NBI (end Jan 25)	Delta (pp)	NBI performance
Large cap (>\$10bn)	26	59	(33)	42	66	(24)	0.6
Mid cap (\$2-10bn)	22	29	(7)	37	24	13	(27.0)
Small cap (>\$2bn)	51	13	38	28	11	17	(29.9)

Source: BIOG. Note: NBI = Nasdaq Biotech Index. BIOG's NAV excludes unlisted holdings.

Hsu and Golomb believe that the size performance gap will close given emerging biotech companies' high levels of innovation and attractive valuations. They note that small-cap underperformance is not unique to the biotech sector. Between the end of March 2021 and the end of January 2025, the US 1000 large cap index rallied by 48.4%, while the US 2000 SMID-cap index was only 3.0% higher. During this period the US 2000 small-cap biotech index underperformed the S&P 500 Index by more than 110pp, which the managers suggest offers a very timely opportunity for investors considering smaller-cap biotech stocks. They reiterate the positive emerging biotech prospects by looking at analysis by Morgan Stanley. Between 31 March 2024 and 31 January 2025, a basket of commercial (large-cap) biotech stocks outperformed a basket of clinical (emerging) biotech stocks by 34.4pp.

They highlight that biotech valuations reached record lows during the latest sector drawdown, with more than 150 companies (25% of the sector) trading below the level of net cash on their balance sheets; so far, there has only been limited normalisation. Higher interest rates were a major factor in the devaluation of biotech stocks as the Federal Reserve aggressively tightened monetary policy in response to rising inflation. Inflation has moderated but remains sticky and there are concerns that tariffs are inflationary, which has meant that interest rate reductions are currently on hold, but may resume in the future, which should be supportive for the valuation of growth stocks, including biotech names.

Favourable biotech industry fundamentals

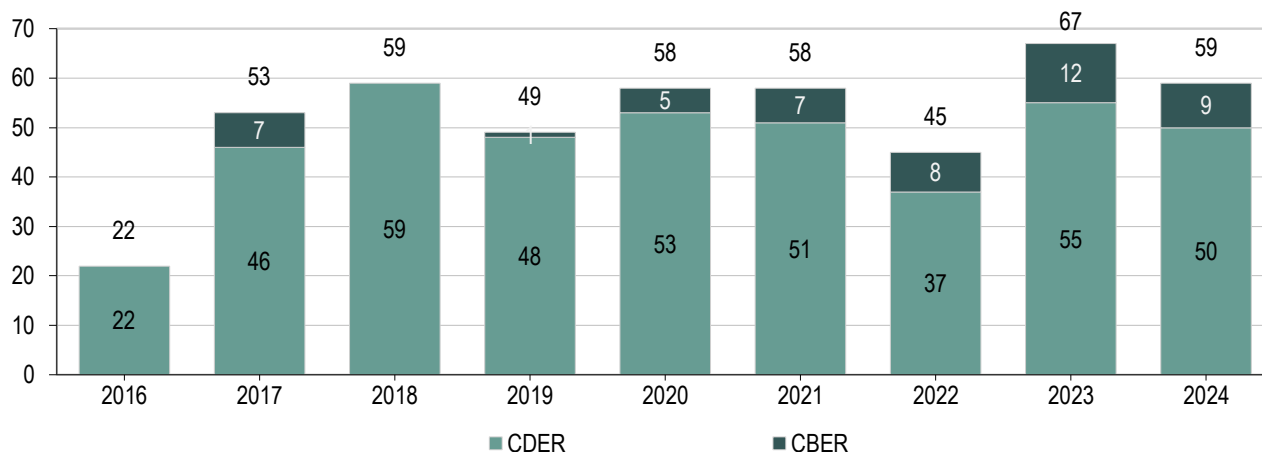
Hsu and Golomb focus on innovation, highlighting a series of important biotech breakthroughs over the last 24 months, including Insmed's Brensocatib (DPP1 inhibitor). Its positive Phase III data was the first successful study in the treatment of bronchiectasis. This is a lung disease where thickened and/or scarred enlarged airways can cause mucus build up in the lungs, leading to chronic cough, shortness of breath and chest pain. Another breakthrough was the world's first approval of a CRISPR therapy. CRISPR Therapeutics and Vertex Pharmaceuticals have developed Casgevy (CASPR Cas9 gene-editing therapy) for the treatment of sickle cell disease and beta thalassaemia, which are inherited blood disorders.

Within the 2024 biotech approvals there was a series of important 'firsts', in terms of disease treatment, new technologies or novel mechanism of action. Oncology remains the largest therapeutic area in biotech and big pharma drug development (c 25% share), primarily driven by ongoing unmet medical needs. It is also the largest-growing disease area, with sales projected to reach c \$351bn, an increase of c \$163bn from 2023, according to Evaluate Pharma. Going back 25 years, the only options for cancer patients were surgery and radiation or chemo therapies. Now there are multiple innovative approaches to treat different tumours, intended to provide improved patient outcomes, by offering more effective solutions to target disease, while mitigating unpleasant side effects associated with older approaches. These include cellular therapies, antibody-drug conjugates, bispecific antibodies, targeted therapies, radiopharmaceuticals and cancer vaccines. All these areas have demonstrated successful clinical trials and five out of six have products approved and in the market.

In the central nervous system (CNS) area, there are many companies working on therapies for both psychiatric and neurological conditions, including Alzheimer's disease, multiple sclerosis, Parkinson's disease and schizophrenia, which offer large chronic market opportunities. CNS is the second-largest therapeutic area behind oncology, and major pharma companies are showing increased interest in the space. In the last 18 months there have been four multi-billion dollar acquisitions of biotech players: Cerevel Therapeutics (by AbbVie at a 22% premium); Intra-Cellular Therapies (by Johnson & Johnson at a 39% premium); Karuna Therapeutics (by Bristol Myers Squibb at a 53% premium); and Longboard Pharmaceuticals (by Lundbeck at a 54% premium). CNS is widely considered one of the most complicated areas of drug discovery, with high levels of complexity. However, as reflected in the rate of advancements in the last year alone, it is also a field that is ripe for clinical innovation, and since it may be viewed as less competitive than oncology, there is a lot of opportunity for value creation.

Biotech innovation is well reflected in BIOG's portfolio, including antibody-drug conjugates (16.1% of NAV); gene therapy and gene editing (12.1%); cell therapy (16.0%); multispecific antibodies and T-Cell engagers (22.3%); and oligonucleotide therapeutics (36.0%). We note that there is some overlap of NAV exposure between the novel technologies.

Exhibit 2: FDA new molecular entity approvals



Source: BIOG, Edison Investment Research

Within the US FDA there are different departments for drug and biologics approvals: the Center for Drug Evaluation and Research (CDER) and the Center for Biologics Evaluation and Research (CBER). There have been around 450 approvals in the last eight years; they started to increase in 2017, which was the beginning of President Trump's first term in office. Hopefully, this will continue through Trump's second term. In 2024, there were 59 approvals of new molecular entities: 50 drugs and nine biologics. Interestingly, 48% of the CDER approvals represent first-in-class drugs (those with novel pharmacological effects), up from 36% in 2023. Notable 2024 approvals included: Karuna Therapeutics' new schizophrenia treatment KarXT (acquired by Bristol Myers Squibb in late-2023 for US\$14bn), representing a resurgence in what has been a relatively stagnant field; Eli Lilly's donanemab for Alzheimer's disease, highlighting the importance of CNS; and Acceleron Pharma's Sotatercept for pulmonary arterial hypertension (acquired by Merck in late-2021 for US\$1.5bn). Two of these three highlighted drug approvals were developed by smaller biotechnology companies before being acquired by big pharma companies, illustrating that innovation in the healthcare sector often stems from biotech.

The financing environment is improving for biotech companies. Volumes started to pick up in 2024; although there are still a muted number of IPOs, there has been steady follow-on financing. OrbiMed has good access to deals because of its size and expertise. Pharma companies are looking to acquire due to a massive patent cliff between now and 2030, when more than \$270bn of the 2024-based sales of branded drugs will be going off patent. As an example, Merck had around \$30bn of Keytruda sales in 2024, and the product loses patent exclusivity in 2028. BIOG has benefited from some of its holdings being taken over, typically at a meaningful premium.

Hsu and Golomb believe that overall the US political environment is positive. The Inflation Reduction Act Medicare price negotiations are due to start in 2026, but with the Republicans controlling Congress, drug price reform could be amended or repealed and pricing exclusivity for small-molecule drugs could be extended from nine to 13 years. The change in the Federal Trade Commission leadership should be positive for M&A as the outgoing commissioner blocked some proposed transactions. Trump's economic policy should be positive for the sector with potential extension of tax cuts or a reduction in corporate tax.

Uncertainties include the appointment of Robert F Kennedy Junior as head of the US Health and Human Services, as he

is a vaccine sceptic, although he has toned down his rhetoric. FDA commissioner nominee Martin Makary is expected to continue the trend of a high number of new drug approvals. Although Trump is focusing on cost reduction, FDA drug reviewers are paid for by pharma company PDUFA (Prescription Drug User Fee Act) fees, so should not be affected. Interest rates could stay higher for longer as although Trump wants lower 10-year bond yields, his tariff policy is likely to be inflationary.

The managers' strategy and outlook

Hsu and Golomb will continue to favour emerging over large-cap biotech stocks, aiming to fully capture the anticipated rebound in the shares of less-mature biotech companies. The managers believe that the very low valuation of emerging biotech stocks offers significant upside potential, and is the result of the largest and longest drawdown ever versus the S&P 500. Valuations are below the levels seen during the bursting of the dot.com bubble and the global financial crisis and there are a meaningful number of biotech companies that are trading below the level of cash on their balance sheets. If the US economy weakens, lower interest rates should be supportive for the performance of biotech stocks, which tend to outperform during a recession. Hsu and Golomb believe that biotech valuations remain disconnected from favourable industry fundamentals. Also, M&A should accelerate due to low valuations and the need for large pharma companies to replenish their product pipelines ahead of a steep multi-year patent cliff.

Portfolio breakdown

At the end of February 2025, BIOG's top 10 holdings made up 51.1% of the portfolio. This was a higher concentration compared with 43.1% a year earlier and three names were common to both periods. The portfolio had 59 positions, which was three less than 12 months earlier, while the active share increased to 77.6% from 70.5% (this is a measure of how the fund compares with its benchmark, with 0% representing full index replication and 100% no commonality).

Exhibit 3: Top 10 holdings

Company	Country	Industry	28 February 2025	28 February 2024
Gilead Sciences	US	Major biotech	12.9	N/A
Sarepta Therapeutics	US	Emerging biotech	6.1	4.0
Neurocrine Biosciences	US	Emerging biotech	5.0	3.9
Argenx	Europe	Emerging biotech	5.0	N/A
Amgen	US	Major biotech	4.2	6.8
Avidity Biosciences	US	Emerging biotech	3.9	N/A
Xenon Pharmaceuticals	US	Emerging biotech	3.7	N/A
Cytokinetics	US	Emerging biotech	3.5	N/A
Amicus Therapeutics	US	Emerging biotech	3.4	N/A
Alnylam Pharmaceuticals	US	Emerging biotech	3.4	N/A
Top 10			51.1	43.1

Source: BIOG, Edison Investment Research. Note: N/A is not in 28 February 2024 top 10.

There are just modest changes in BIOG's geographic exposure in the 12 months to the end of February 2025, with lower weightings in unquoted and North American stocks and higher allocations to continental Europe and Chinese quoted companies.

Exhibit 4: Portfolio geographic breakdown (%)

Country/region	Portfolio end February 2025	Portfolio end February 2024	Change (pp)
North America	86.0	88.0	(2.0)
Continental Europe	7.1	4.8	2.3
China (quoted)	6.1	3.9	2.2
Unquoted*	0.8	3.3	(2.5)
Total	100.0	100.0	

Source: BIOG, Edison Investment Research. Note: Adjusted for gearing. *Of the 0.8% unquoted investments at end-February 2024, 0.3% was in China and 0.5% was in Asia.

Performance: Awaiting a return to historical form

Of the seven funds in the AIC Biotechnology and Healthcare sector, three are biotech specialists: BIOG, International Biotechnology Trust (IBT) and RTW Biotech Opportunities (RTW). BIOG's strategy of favouring smaller-cap biotech stocks means that its NAV total returns lag those of its peers over the periods shown. The trust's other peers are broader healthcare specialists: Bellevue Healthcare Trust (BBH), Polar Capital Global Healthcare Trust (PCGH) and stablemate Worldwide Healthcare Trust (WWH), along with Syncona (SYNC), which is an early-stage healthcare investor. These companies have also mostly generated better NAV total returns than BIOG over the periods shown.

However, this is a recent phenomenon. Looking back to the BIOG review we published in [March 2021](#), which was when smaller-cap biotech stocks started to underperform large-cap biotech stocks, the trust had the highest NAV total returns of the then six funds in the AIC Biotechnology and Healthcare sector over one, three, five and 10 years.

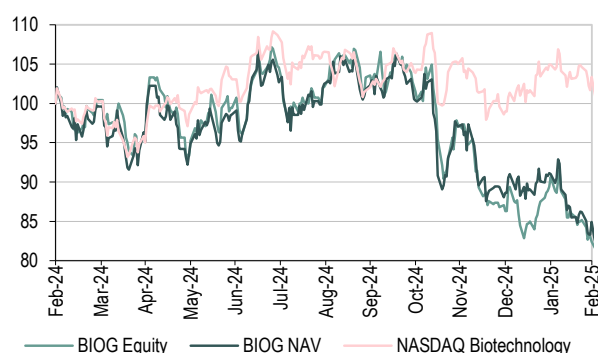
BIOG currently has the third-highest valuation in the sector (all the funds are trading at a discount), and an ongoing charge that is modestly below the mean. The trust is currently ungeared and does not receive sufficient income to pay a dividend; biotech peer IBT can pay its dividend out of capital.

Exhibit 5: AIC Biotechnology and Healthcare sector at 14 March 2025*

% unless stated	Market cap (£m)	NAV TR 1Y	NAV TR 3Y	NAV TR 5Y	NAV TR 10Y	Discount	Ongoing charge	Performance fee	Net gearing	Dividend yield
Biotech Growth	216.6	(19.8)	(8.4)	(5.2)	2.2	(9.3)	1.2	Yes	100	0.0
Bellevue Healthcare	305.3	(12.8)	(15.4)	26.8		(4.3)	1.0	No	100	4.8
International Biotechnology	230.5	1.0	25.0	44.3	64.0	(10.5)	1.2	Yes	114	4.4
Polar Capital Global Healthcare	414.7	(8.9)	15.4	67.4	107.1	(4.8)	0.9	Yes	100	0.7
RTW Biotech Opportunities	327.2	(3.2)	32.7	50.9		(33.3)	2.0	Yes	100	0.0
Syncona	567.8	(4.7)	(10.0)	(9.8)	60.3	(48.8)	2.0	No	100	0.0
Worldwide Healthcare	1,517.9	(7.4)	7.3	27.6	85.0	(11.5)	0.9	Yes	100	0.9
Average (7 funds)	511.4	(8.0)	6.7	28.8	63.7	(17.5)	1.3	0	102	1.5
Rank	7	7	5	6	5	3	5	0	2	5

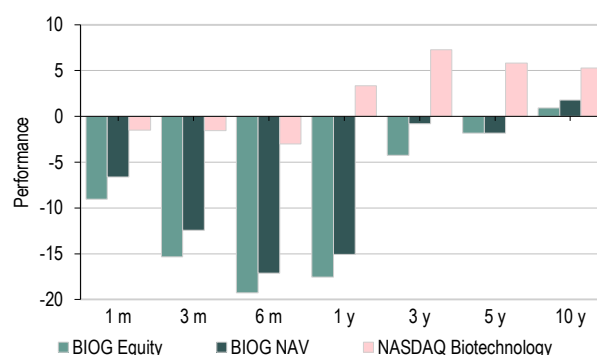
Source: Morningstar, Edison Investment Research. Note: *Performance at 13 March 2025. TR = total return.

Exhibit 6: Rebased one-year share price, NAV and index total return performance to 28 February 2025



Source: LSEG Data & Analytics, Edison Investment Research

Exhibit 7: Share price and NAV total return performance, relative to indices (%)



Source: LSEG Data & Analytics. Note: Three-, five- and 10-year figures annualised.

Exhibit 8: Five-year discrete performance data

12 months ending	Share price (%)	NAV (%)	NASDAQ Biotech (%)	World-DS Pharma & Bio (%)	MSCI World (%)	CBOE UK All-Cos (%)
28/02/21	69.2	52.8	26.6	11.3	18.8	2.8
28/02/22	(38.6)	(38.9)	(15.0)	7.4	15.9	16.7
28/02/23	(2.3)	5.7	14.0	11.8	3.2	8.2
29/02/24	8.9	8.7	4.9	12.7	20.2	0.7
28/02/25	(17.6)	(15.1)	3.3	7.2	16.7	18.6

Source: LSEG Data & Analytics. Note: All % on a total return basis in pounds sterling.

Exhibit 9: Share price and NAV total return performance, relative to indices (%)

	1 month	3 months	6 months	1 year	3 years	5 years	10 years
Price relative to NASDAQ Biotechnology	(7.6)	(14.0)	(16.8)	(20.2)	(28.9)	(31.4)	(34.4)
NAV relative to NASDAQ Biotechnology	(5.2)	(11.1)	(14.5)	(17.8)	(21.0)	(31.4)	(28.7)
Price relative to WORLD-DS Pharm & Bio	(11.7)	(19.1)	(15.8)	(23.1)	(35.0)	(43.5)	(53.6)
NAV relative to WORLD-DS Pharm & Bio	(9.4)	(16.4)	(13.5)	(20.7)	(27.7)	(43.6)	(49.5)
Price relative to MSCI World	(7.2)	(16.3)	(26.1)	(29.3)	(39.4)	(54.2)	(66.8)
NAV relative to MSCI World	(4.7)	(13.4)	(24.2)	(27.2)	(32.6)	(54.3)	(63.9)
Price relative to CBOE UK All Companies	(10.2)	(19.9)	(23.6)	(30.5)	(32.1)	(41.2)	(40.4)
NAV relative to CBOE UK All Companies	(7.9)	(17.2)	(21.5)	(28.4)	(24.5)	(41.3)	(35.3)

Source: LSEG Data & Analytics, Edison Investment Research. Note: Data to end-February 2025. Geometric calculation.

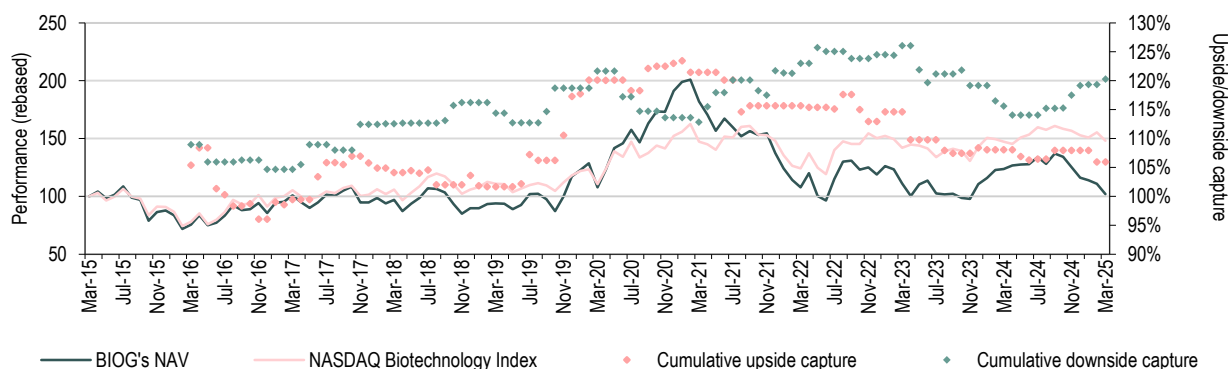
As discussed earlier in the report, BIOG's relative performance was negatively affected by its bias to emerging versus large-cap pharma stocks during the latest major biotech industry sell-off. Unfortunately, recently there have been some company-specific developments that have hurt the trust's performance, including disappointing trial data.

Exhibit 10: BIOG's NAV versus the benchmark over the last 10 years


Source: LSEG Data & Analytics, Edison Investment Research

BIOG's upside/downside capture

Exhibit 11 shows BIOG's performance versus the NASDAQ Biotechnology Index over the last decade. The trust's upside capture rate of 109% is much lower than its 123% downside capture rate, suggesting that BIOG will underperform by more in a market when biotech stocks are falling than it will outperform when biotech shares are rising. This feature of the trust should not be a surprise given BIOG's bias to emerging biotech stocks, which are inherently more risky than large-cap biotech stocks.

Exhibit 11: BIOG's upside/downside capture


Source: LSEG Data & Analytics, Edison Investment Research.

Note: Cumulative upside/downside capture calculated as the geometric average NAV total return (TR) of the fund during months with positive/negative reference index TRs, divided by the geometric average reference index TR during these months. A 100% upside/downside indicates that the fund's TR was in line with the reference index's during months with positive/negative returns. Data points for the initial 12 months have been omitted in the exhibit due to the limited number of observations used to calculate the cumulative upside/downside capture ratios.

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