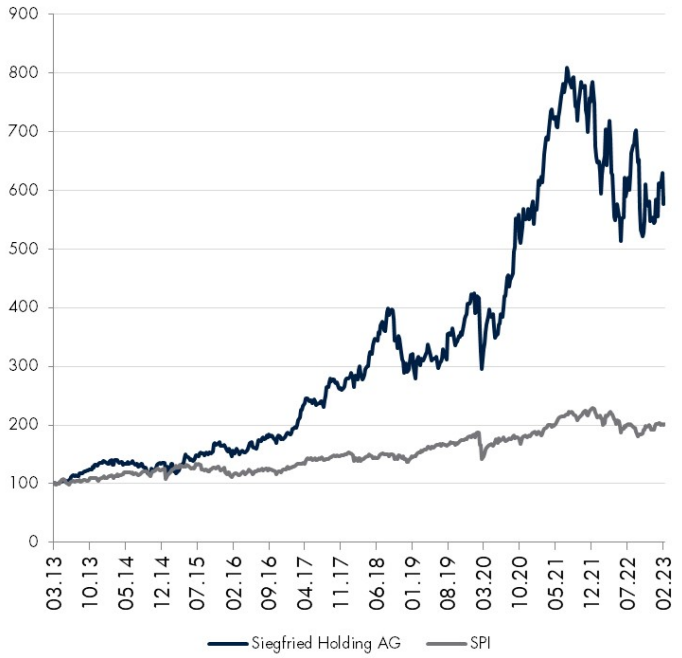
Independent Asset Management

March 2023

Siegfried

Evolution of stock price with respect to benchmark (rebased)
Source: IAM



Market profile

Country	Switzerland
Sector	Specialty & Generic Pharma
Market cap (CHF million)	2'862
52-week high / low (CHF)	818/ 573
Price per share (CHF)	641

Key metrics (CHF)

	2022	2023e	2024e
EPS	29.6	31.7	35.9
PE	21.6	20.2	17.8
P/Book	3.9	2.9	2.5
Dividend yield	0.52%	0.60%	0.62%

Executive summary

Headquartered in Zofingen, Siegfried operates worldwide in life sciences with production facilities in Switzerland, the USA, Malta, China, Germany, France, and Spain. The company's history traces back to 1873 when pharmacist Samuel Benoni Siegfried founded a company with 12 employees as a supplier to pharmacies. Today Siegfried is a worldwide integrated Contract Development and Manufacturing Organization (CDMO). It provides longstanding pharmaceutical and chemical experience, which offers customers with more synergy, expertise, and value. It provides development and manufacturing services, and offers Active Pharmaceutical Ingredients (API), intermediates and finished dosage forms.

Investment case

The CDMO market has been growing faster than the pharmaceutical market itself for quite some time. The depth of knowledge involved, tight regulation and significant investments required create high barriers to entry and also support high profitability margins for CDMOs. The industry is highly fragmented, with the top 10 CDMOs accounting for less than 20% of the total market share. Siegfried has a history of successful acquisitions that have transformed it into a "one-stop-shop" and a management team with a strong record in M&A and private equity. Further, as pharma companies focus their investments into biologic, and cell and gene therapy capabilities, there is a greater number of opportunities to acquire small-molecule manufacturing assets. Siegfried is very well positioned to take advantage of these trends to become a leading company of the fast growing and profitable CDMO market.

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Olivier Aeschlimann, Senior Financial Analyst **March 2023**

Company description and history

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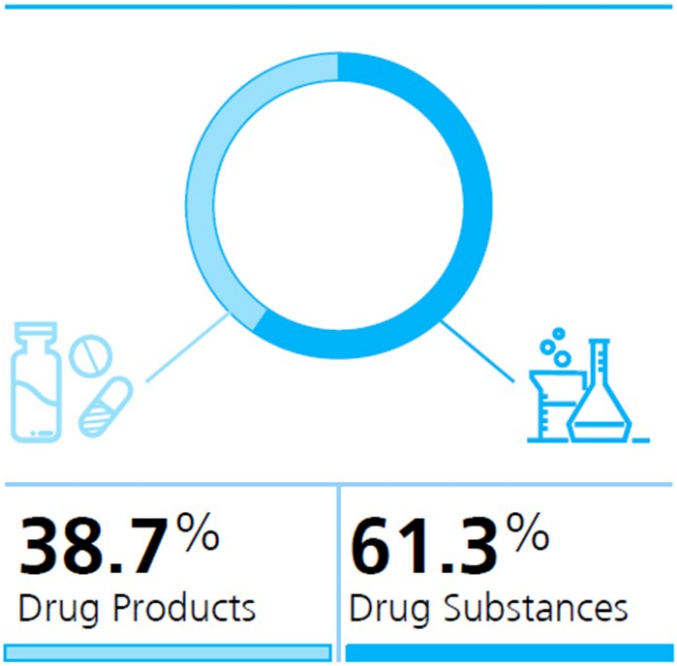
Fig.1: Sales by division, 2022
Source: Siegfried



Group Structure

Siegfried has two operating divisions: Drug Substances and Drug Products. The Drug Substance division focuses on the development and production of customer-specific APIs and intermediates, as well as controlled substances (narcotics and analgesics) such as methadone and nicotine. The Drug Products division specializes in the sterile filling of drugs and oral dosage forms, which are offered to customers as a separate portfolio for licensing or as contract development through contract manufacturing.

Drug Substances

Siegfried's chemical expertise centers on the development and production of active pharmaceutical ingredients and intermediates. API are used in the production of a medication. APIs are the key ingredient of a finished product that is ready for administration with a direct effect concerning treatment. Intermediates are created in the course of a multi-step chemical reaction. They are not final products but the result of the previous step and the initial product for the following reaction step.

Drug Products

Siegfried's capabilities are covering the entire lifecycle of a product from development phase to commercial supply as well as taking care of sourcing of raw materials, quality and regulatory services. Siegfried offers from manufacturing to final packaging services according to target-market specific requirements. Siegfried is offering the following technology platforms:

- Oral solid dosage forms.
- Sterile dosage forms – Injectables – aseptic processing and terminal sterilization.
- Ophthalmic (ointments, gels, suspensions, and solutions in tubes, bottles, vials, ampoules, car-

tridges, and pre-filled syringes.

- Inhalation Capsules based Dry Powder Inhaler (DPI) products.

Siegfried Business Model: from API to the finished product

As a fully integrated pharmaceutical company, Siegfried is today one the few suppliers that can carry out both the development of active ingredients and finished formulated drugs under one roof. This combination of experience and know-how is unique in the CDMO market. Below is a simplified framework of the Siegfried's business model.

- The customer's Research and Development discovers a new API.
- API Synthesis: in this phase, the process is developed by Siegfried and then scaled up to ensure that it can be used in large-scale production.
- Particle Processing: by using bridging technologies such as milling, micronization or spray dying, Siegfried can offer the production of active ingredients and finished formulations from a single source.
- Finished Dosage Forms: in the phase, solid oral dosage forms are produced by means of dosage formulation, or active ingredients are sterilely or aseptically filled and packaged.
- Marketing and Distribution: the finished product is delivered to the customer for his further commercial use.

The CDMO market

The market to supply active pharmaceutical ingredients (CDMO: Customer Development and Manufacturing Organization) to the pharmaceutical and biotech industries has been growing faster than the pharmaceutical market itself for quite some time.

Pharmaceutical suppliers are enjoying high momentum thanks to the trend in the pharmaceutical industry to fulfil

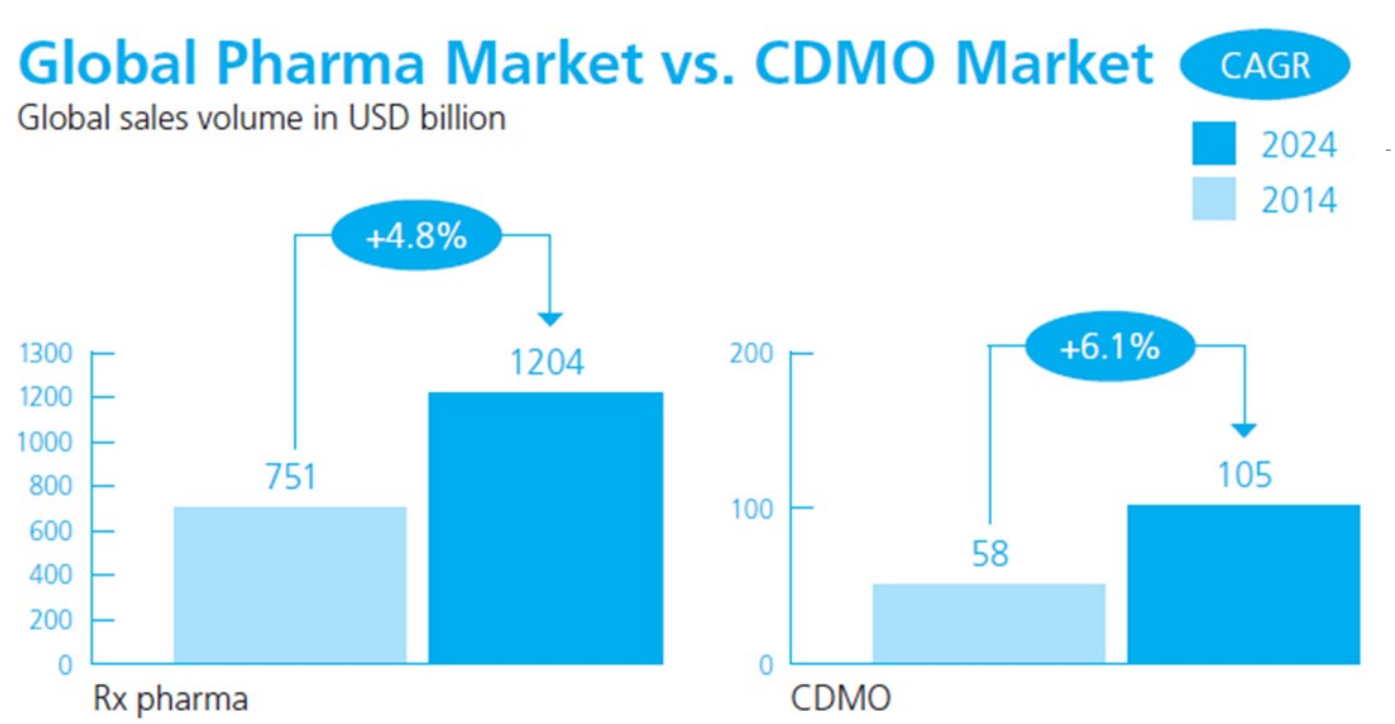
Fig2.: Global distribution of production facilities
Source: Siegfried

only basic demand for products through in-house active ingredient production capacity. Peaks in demand, market fluctuations, and above all growth in product sales are met by outsourcing production of active ingredients to suppliers. The idea is to transfer working capital and capex risk to external suppliers and concentrate instead on research. At present, the share of outsourced active pharmaceutical ingredients production (Drug Substance) and formulations (Drug Products) is only around 50%, so this area offers considerable growth potential over the next few years.

High barriers to entry

The depth of knowledge involved, tight regulation and significant investments required create high barriers to entry and also support high profitability margins for CDMOs. Pharma companies are exposed to strict regulatory criteria during the development process and for the commercial supply once their drugs are approved, and as such, require their suppliers to adopt stringent quality and monitoring standards. In order to qualify as suppliers and win relevant contracts, supply companies therefore need to earn their reputation over time, making a rapid industry entrance by a new company more difficult. Moreover, once a company is approved as a supplier, it must ensure that it maintains high quality standards and proves itself reliable, as the products are critical for the clinical and commercial success of the pharma/biotech customer's drug. Access to capital is another hurdle faced by companies looking to enter the pharma supply industry. API manufacturing and packaging typically requires major investments in physical property, plant and equipment, and the upfront capital expenditure can be quite substantial. However, for established suppliers, drug companies show some degree of willingness to participate in financing, especially for drug-specific manufacturing lines, and in general financing is relatively inexpensive currently. Once a drug approaches commercialization, the ability of suppliers to scale up processes securely and reliably is another differentiation factor. For the lifetime of the drug, suppliers and pharma companies usually enter long-term contracts, and the costly and time-consuming nature of switching manufacturing suppliers due to renewed certification and validation requirements makes the business sticky.

Fig.3: Growth prospects of the CDMO market
Source: Siegfried



Advancement into the top CDMO group

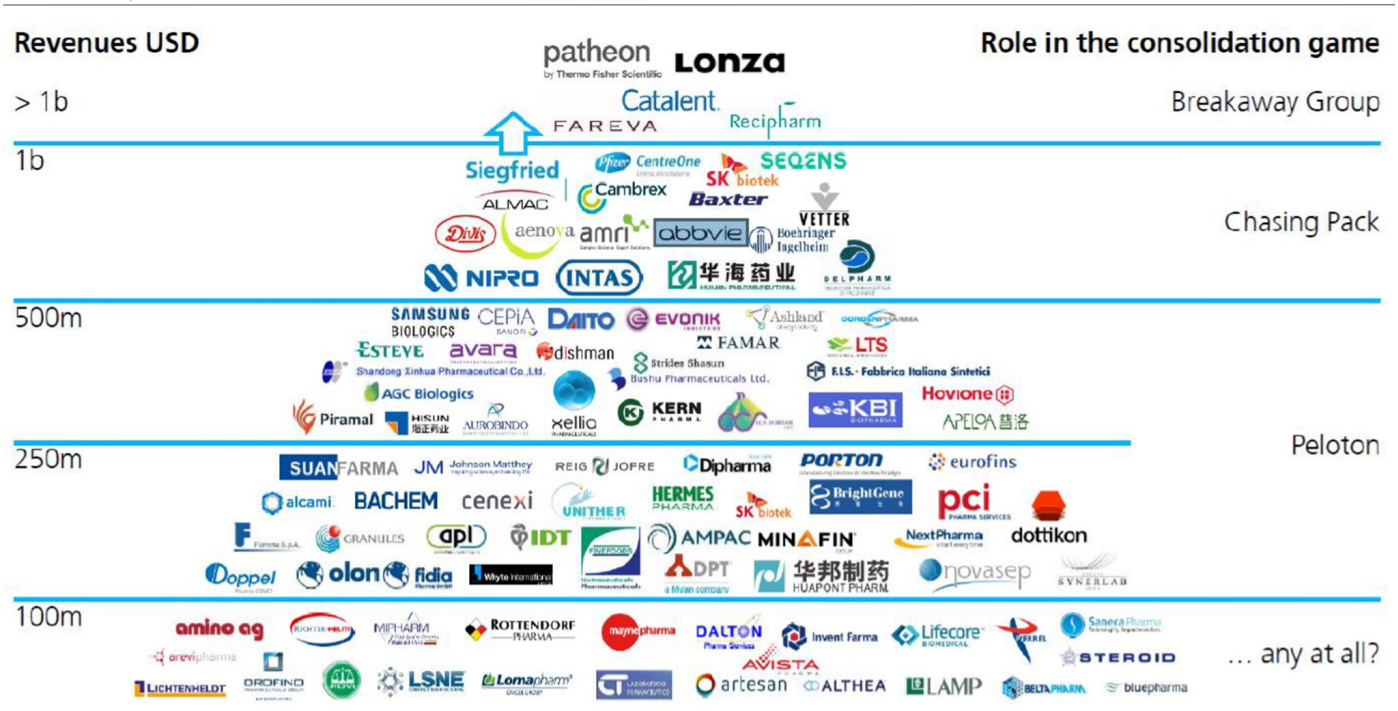
The industry is highly fragmented, with the top 10 CDMOs accounting for less than 20% of the total market share. However, the market is consolidating through strong M&A activity and an injection of capital from public market and private equity firms. Big pharma continues to divest non-core assets to reduce their manufacturing footprint, which is also an attractive acquisition opportunity for CDMOs. These assets are often of high quality with an experienced workforce in place, and CDMOs benefit from taking over supply agreements for products that continue to be manufactured. Siegfried has a history of successful acquisitions that have transformed it into a "one-stop-shop" and a management team with a strong record in M&A and private equity. Further, as pharma companies focus their investments into biologic, and cell and gene therapy capabilities, there is a greater number of opportunities to acquire small-molecule manufacturing assets.

In autumn 2020, Siegfried purchased two Novartis production sites in Spain. These transactions propelled the company into the league of the world's largest CDMOs with annual sales of over USD 1 billion. The additional sales improve the absorption of the idle costs associated with open capacity. This improvement has a correspondingly positive effect on profitability. Deliberately maintaining open capacity is the basic prerequisite for gaining sustained market share in the CDMO sector. This approach to capacity utilization enables the acquisition of interesting new projects to expand the existing customer and project portfolio.

Peer comparison

There are four other CDMOs listed on the Swiss market besides Siegfried. Lonza, by far the biggest company, also has better margins than Siegfried as the firm is involved in the more demanding biologics business. Bachem and Polypeptides are market leader in the very specific business of sophisticated peptides, with which significantly higher margins can be achieved due to their complexity in production involving a disproportionately higher number of process steps (however, that complexity may be difficult to deal with as exemplified by the production problems recently experienced by Polypeptides). Finally, Dottikon, which focuses on specialties and serves its customers with selected performance chemicals and exclusive active ingredients that often involve chemical safety-critical reactions.

Fig.4: Structure of the CDMO market
Source: Siegfried

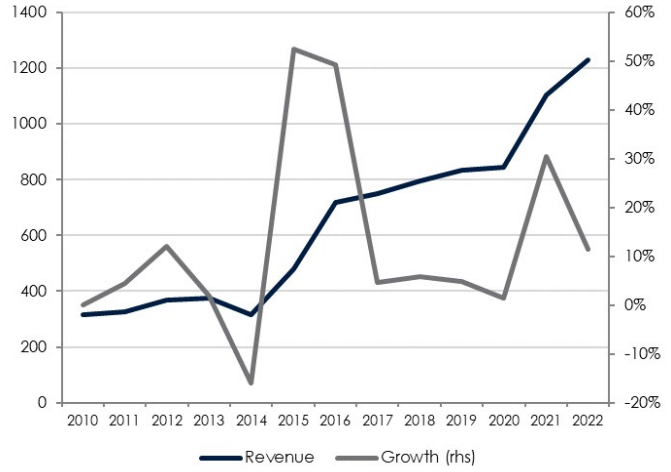


Financial analysis

Revenues

Sales have increased by 11.5% in 2022 (+15.6% in local currencies) to reach CHF 1.229 billion. Sale growth was supported by both Drug Substances and Drug Products. The two pharmaceutical manufacturing sites acquired from Novartis at the beginning of 2021 have been fully integrated into the Siegfried network during the financial year 2022 and contributed to the growth in the period.

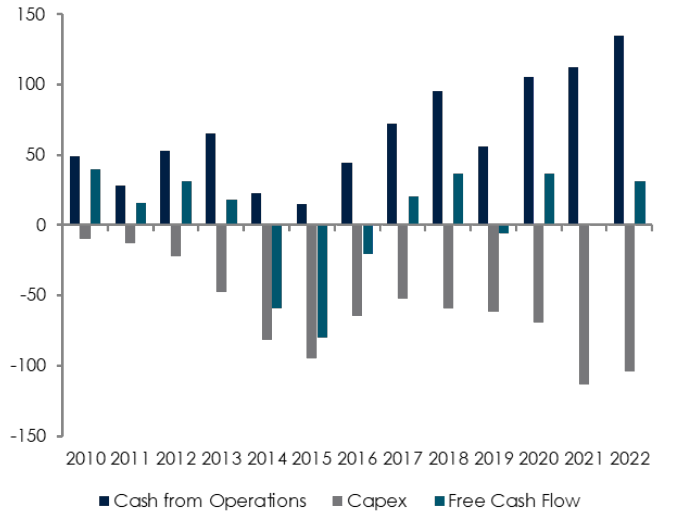
Fig.5: Evolution of revenue
Source: Siegfried



Capex and cash flow

Since 2021, Siegfried has substantially increased its capex. In 2022, the company continued to invest in its global network to further strengthen its innovation and technological capabilities. Siegfried started the construction of a new world-class large-scale production plant for innovative Drug Substance for a total investment of up to CHF 100 million. However, thanks to a very strong operating cash flow generation, Siegfried was free cash flow positive in 2022.

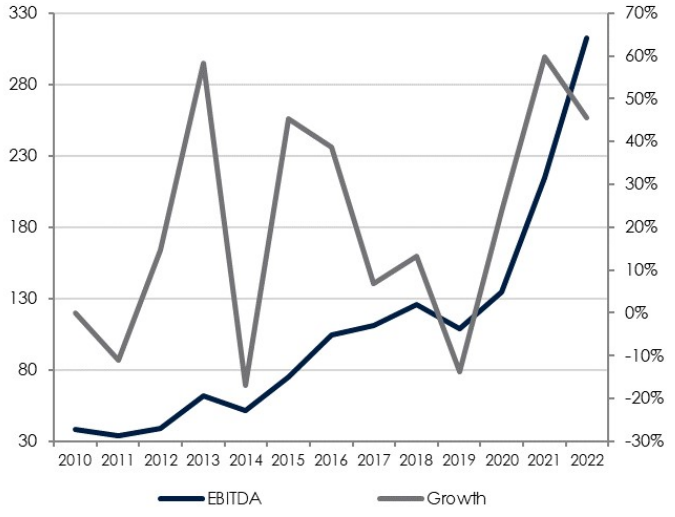
Fig.6: Cash flow
Source: Siegfried



Profitability

EBITDA grew from CHF 215 million to 313 million in 2022, a 25.4% increase from the previous year. This resulted in an EBITDA margin of 25.4%, exceeding the 20% mark for the first time on a full year basis.

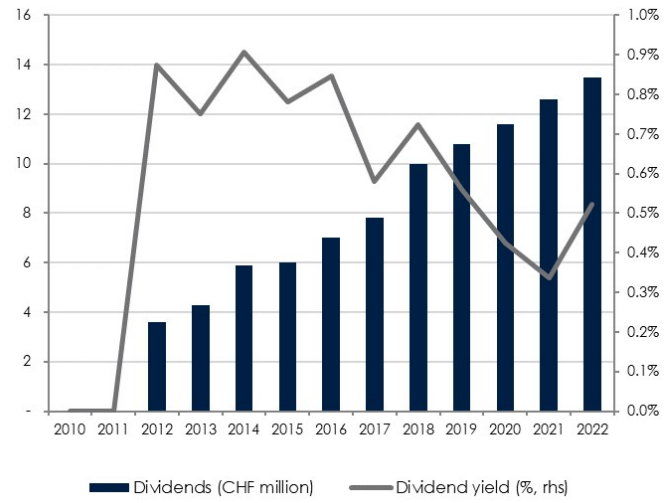
Fig.7: Evolution of EBITDA
Source: Siegfried



Capital distribution

In 2022, the dividend yield was about 0.52%. The company has always managed to increase its dividend since it has started serving one in 2012. However, as Siegfried is currently investing for growth, serving a big dividend is not a priority.

Fig.8: Dividends and dividend yield
Source: Georg Fischer



Strong balance sheet

Although the debt metrics have deteriorated somewhat since the acquisition of the two Novartis assets, the balance sheet is still very strong with a total debt to equity ratio of 64.5 %. Net debt to EBITDA has started to decrease and is now at 1.59X. That said, the interest cover ratio defined as EBIT/interest expense is over 30X, which is extremely comfortable.

Fig.10: Profitability ratiosSource: Georg Fischer

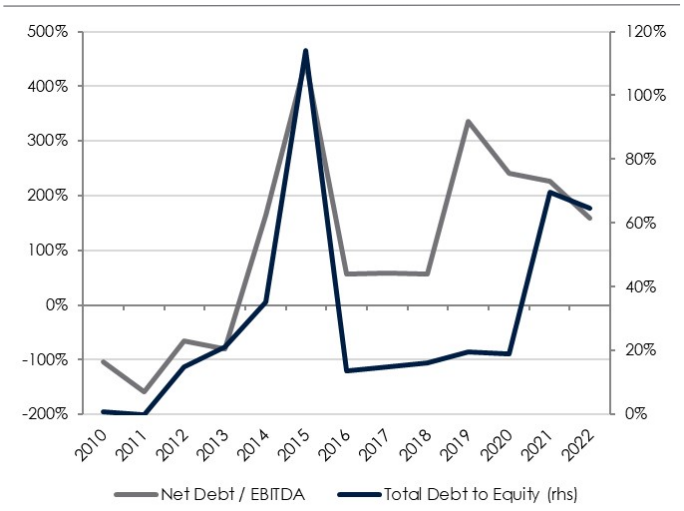
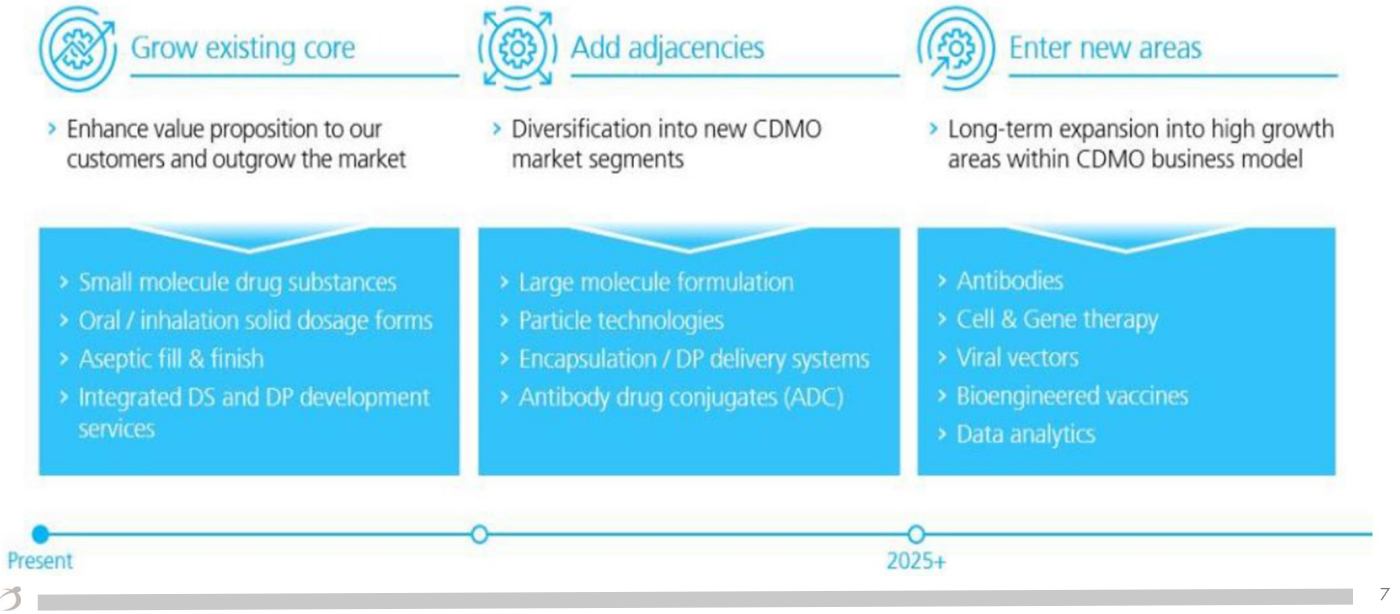


Fig.9 Siegfried's value proposition and growth perspectives
Source: Siegfried



Investment case

Siegfried focuses on the production of active ingredients (Drug Substances) and downstream formulation of products for health and well-being. The company operates six sites to produce active ingredients. These sites, which are located in Europe, The US and China, are coordinated with each other. The production network for the manufacture of chemically based active ingredients (small molecules) is unparalleled worldwide. The market to supply active pharmaceutical ingredients (CDMO: Customer Development and Manufacturing Organization) to the pharmaceutical and biotech industries has been growing faster than the pharmaceutical market itself for quite some time. The depth of knowledge involved, tight regulation and significant investments required create high barriers to entry and also support high profitability margins for CDMOs. The industry is highly fragmented, with the top 10 CDMOs accounting for less than 20% of the total market share. Siegfried has a history of successful acquisitions that have transformed it into a "one-stop-shop" and a management team with a strong record in M&A and private equity. Further, as pharma companies focus their investments into biologic, and cell and gene therapy capabilities, there is a greater number of opportunities to acquire small-molecule manufacturing assets. Siegfried is very well positioned to take advantage of these trends and progress to become a leading company of the fast growing and profitable CDMO market.

SWOT analysis

Strengths

- Balanced regional distribution of production facilities
- Solid balance sheet ensures competitive strength and allows for larger investments and acquisitions.
- Strong management team and corporate governance
- Strong customer loyalty thanks to reliability an high quality standards

Weaknesses

- Dependent on decisions by regulatory authorities
- Project business involves order volatility

Opportunities

- Increasing outsourcing tendency of the global pharmaceutical industry
- Enhancement of finished formulations, particularly in the field of sterile filling of syringes, including entry into the filling of biologics
- Use of cost advantages through the new production site in Nantong (China)

Threats

- Unplanned interruption of operations due to accident, cyber attacks or regulatory requirements
- Price pressure (particularly for generic drugs) and significant competition from emerging countries
- Shortage of raw materials, rising raw material prices or unfavorable exchange rate developments