DRI Healthcare Trust

2024 Third Quarter Earnings Call

Event Date/Time: November 7, 2024 — 8:00 a.m. E.T.

Length: 58 minutes

CORPORATE PARTICIPANTS

Gary Collins
DRI Healthcare Trust — Chairman and Chief Executive Officer

Navin Jacob
DRI Healthcare — Chief Investment Officer

Amit Kapur
DRI Healthcare Trust — Chief Financial Officer

Ali Hedayat
DRI Healthcare — Board Trustee and Acting Chief Executive Officer

CONFERENCE CALL PARTICIPANTS

Doug Miehm
Capital Markets — Analyst

Leszek Sulewski
Truist Securities — Analyst

Michael Freeman
Raymond James — Analyst

George Farmer
Scotiabank — Analyst

Scott Fletcher
CIBC — Analyst

Zachary Evershed
National Bank Financial — Analyst

Justin Keywood
Stifel — Analyst

Tania Armstrong
Canaccord Genuity — Analyst

PRESENTATION

Operator

Good morning, everyone. Welcome to DRI Healthcare Trust's 2024 third quarter earnings call.

Listeners are reminded that certain statements made in this earnings call presentation, including responses to questions, may contain forward-looking statements within the meaning of the safe harbor provisions of Canadian provincial securities laws.

Forward-looking statements involve risks and uncertainties, and undue reliance should not be placed on such statements. Certain material factors or assumptions are applied in making forward-looking statements, and actual results may differ materially from those expressed or implied in such statements.

For additional information about factors that may cause actual results to differ materially from expectations, and about material factors or assumptions applied in making forward-looking statements, please consult the MD&A for this quarter, the Risk Factors section of the Annual Information Form, and DRI Healthcare Trust's other filings with Canadian securities regulators.

DRI Healthcare Trust does not undertake to update any forward-looking statements. Such statements speak only as of the date made.

Today's presentation also references non-GAAP measures. Reconciliation of these measures to measures recognized under IFRS, are included in our earnings press release available on our website and on SEDAR+.

Unless otherwise specified, all dollars amounts discussed today are in US dollars.

I want to remind everyone that this conference call is being recorded today, Thursday, November 7, 2024.

The Trust's quarterly results press release and the slides of today's call will be available on Investor page of the Trust's website at drihealthcare.com.

I would now like to introduce Mr. Gary Collins, Chairman and Chief Executive Officer of DRI Healthcare Trust. Please go ahead, Mr. Collins.

Gary Collins — Chairman and Chief Executive Officer, DRI Healthcare Trust

Thank you, Operator, and good morning, everyone. Thank you for taking the time to join us today. With me are Amit Kapur, Chief Financial Officer of the Trust; Ali Hedayat, Board Trustee and Acting Chief Executive Officer of our manager, DRI Capital Inc., which we refer to as DRI Healthcare; and Navin Jacob, Chief Investment Officer of our manager.

We've made significant improvements since the management changes announced at the beginning of the third quarter, including concrete steps to enhance our internal controls. Transparency, accountability, and good governance are focal points as we continue growing the Trust for the benefit of unitholders.

With the conclusion of the investigation and no further findings to report, we can now turn the page and begin the next chapter in the evolution of the Trust. The new management teams of the Trust and our manager have now been formalized and, along with my role as Chairman of the Board of Trustees, I've taken on the position of CEO of the Trust.

Amit Kapur has recently joined the Trust as CFO. As the independent management group of the Trust, separate from that of the manager, he and I are focused on providing the right governed structures and financial stewardship for the best interest of our unitholders.

We're working alongside the leadership team of our manager, which includes Ali Hedayat, Acting CEO, and Navin Jacob, the CIO. Sandy Kwan and David Plow have been promoted to the roles of CFO and COO, respectively.

Ms. Kwan has been with DRI Healthcare for two years, previously in the role of VP Finance, and then Acting CFO of both the Trust and the Manager.

Mr. Plow was on the investment team of DRI Healthcare from 2010 to 2019, before leaving the organization and then rejoining as Chief of Staff in 2023.

Completing two deals while at the same time making significant progress on our remediation efforts proves that this is a strong leadership team that will continue to deliver results and drive the growth of the Trust within an improved and robust governance framework.

The Trust has been very active since our last earnings call. As Navin will speak to in detail, we completed two innovative transactions for CASGEVY and sebetralstat. In total, we deployed $162 million with a total potential deal size of up to $241 million. These long-dated assets in new therapeutic areas complement the existing assets and increase both the portfolio's duration and diversification.

We also expanded our credit facilities from $500 million to $632 million. And with nearly $300 million still available on the facilities, we have significant additional capital to continue executing our proven strategy, as well as a robust pipeline of opportunities to deploy that capital.

Finally, yesterday, we declared a quarterly distribution of $0.085 for unitholders of record on December 31st that will be paid on January 20, 2025.

I'll now turn the call over to Navin Jacob, Chief Investment Officer of the manager, DRI Healthcare.

Navin Jacob — Chief Investment Officer, DRI Healthcare

Thank you, Gary. These recent transactions are notable because of the structure and the assets. They speak to the innovative and bespoke nature of our deals and our focus on the future of medicine.

For CASGEVY, rather than acquiring a royalty stream, we acquired a set of payments from Editas Medicine, based on the licence agreement for the Cas9 gene editing technology used in CASGEVY.

The Trust is entitled to a share of the annual license fees that Vertex pays Editas, which range from $5 million to $40 million. Included in this payment range are certain sales-based annual licence fee increases. These increases operated like an incoming milestone, such that when the sales level is achieved, it triggers an additional payment to the Trust. We're entitled to this potential sales-based fee in each calendar year.

Finally, we also purchased a mid-double-digit percentage of Editas' portion of a $50 million contingent payment under the same licence agreement.

Receipts will be collected in the first quarter of the year with the first payment expected in January 2025. We anticipate the term of the payment streams to run until at least 2034. This structure, a first for the Trust, showcases our ability to work constructively with our partners and find a deal that works for the benefit of both parties outside of a traditional royalty deal.

CASGEVY was approved by the FDA in December 2023 and by the EMA in February 2024 for treating sickle cell disease and transfusion-dependent beta thalassemia. These are inherited blood disorders that significantly impact quality of life and shorten life expectancy. Current traditional treatments for sickle cell disease have a 30 percent to 50 percent response rate in preventing vaso-occlusive events, which are extremely painful and potentially deadly.

Transfusion-dependent beta thalassemia patients require frequent blood transfusions. For both diseases, stem cell transplants are a potential curative option, although uptake is low due to the necessity of finding matched donors, making many patients ineligible.

CASGEVY presents a curative option with an over 90 percent success rate. It has better safety and efficacy compared to stem cell transplant and does not require a matching donor. Using the CRISPR/Cas9 technology, CASGEVY is a gene-editing tool that modifies the underlying gene that causes the disease. This is a cutting-edge technology that is helping reshape the future of medicine.

Investing in these types of drugs and helping advanced science is core to our mission at DRI Healthcare. We take a holistic approach to our dealmaking and believe in forming partnerships with our counterparties. We have built a strong working relationship with Editas and hope to work with them again in future transactions.

Turning to Slide 8. We completed our next transaction for sebetralstat less than a month after announcing CASGEVY. The deal size is up to $184 million, with $105 million of that deployed up front.

The sebetralstat deal with KalVista is significant for three reasons. The first is that it is the Trust's first acquisition of a preapproval asset. Second, it is our first synthetic royalty in over three years. Third, we purchased a small equity stake in KalVista, which is another new offering from DRI.

Our team has been evaluating preapproval deals for some time now, and this asset was the best choice to provide accretive value to our portfolio and unitholders while, at the same time, minimizing our downside risk. The robust clinical data leads us to a high-conviction thesis that the drug will be approved.

As noted, the $5 million private placement investment is another new strategy we have implemented for the first time to further enhance our returns and showcase our confidence in the KalVista management team.

Sebetralstat is the first oral medicine for on-demand treatment of acute attacks associated with hereditary angioedema, a rare genetic disorder characterized by recurring episodes of severe swelling in various parts of the body, including the face, extremities, gastrointestinal tract, and airways.

Results from its Phase 3 clinical trial showed significant efficacy and favourable safety. KalVista filed a new drug application, and the FDA has provided a PDUFA date of June 17, 2025, as the deadline by which to approve the asset.

KalVista has also filed a marketing authorization application, which has been validated by the European Medicines Agency, as well as further applications in the UK, Switzerland, Australia, and Singapore.

The transaction entitles us to a reverse-tiered royalty on worldwide net sales, receive a royalty of 5 percent on sales up to and including $500 million, 1.1 percent on sales above $500 million and up to and including $750 million, and 0.25 percent on sales above $750 million.

KalVista is entitled to a potential one-time, sales-based milestone payment of $50 million if annual net sales meet or exceed $550 million before January 1, 2031.

If sebetralstat is approved before October 1, 2025, KalVista will have the option to receive a one-time $22 million payment. If they choose to receive this payment, the first-tier royalty rate will increase from 5 percent to 6 percent, and the potential sales-based milestone payment would increase from $50 million to $57 million, while all other deal terms remain the same.

Royalty receipts will begin the first quarter after approval of the drug and will be collected on a one-quarter lag basis. We anticipate cash receipts through at least 2041. As this is a synthetic royalty, we worked directly with KalVista to structure this deal in a very bespoke fashion and with terms that serve both parties' needs.

Ultimately, these two recent transactions highlight our evolving investment strategy. We will continue looking for ways to increase unitholder value with royalty investing at our core.

Regarding our existing portfolio performance, this table shows the individual royalty receipts for the third quarter of 2024 compared to the same quarter in the previous year and in the previous quarter. Our portfolio performed well in the quarter and with total cash royalty receipts increasing by 54 percent from the previous year.

The 10 percent decrease from the last quarter reflects the normal volatility associated with the annual cycle of biopharma sales. The increase in year-over-year Total Cash Receipts was primarily driven by the royalties on sales of Orserdu and Empaveli, as well as the expansion of the Omidria royalty.

Xenpozyme royalties are only received in the second and fourth quarters. We received our first royalty in the third quarter of last year, but expect to receive semiannual payments going forward.

Overall, Xenpozyme sales continue to show us consistent growth, largely in line with our expectations. Sales increased 53 percent from the same quarter in the previous year, driven by more patients treated across all regions.

Omidria royalty receipts increased 195 percent from the previous year, primarily driven by the second transaction on this asset, which expanded our entitlement and removed the previous annual caps.

Royalty receipts decreased 16 percent from the prior quarter, which is related to quarterly seasonality, but also related to a merit-based incentive payment system program, or MIPS for short, that is used by CMS, the Centers for Medicare & Medicaid Services. CMS likely provided scores to physician groups earlier in the quarter, which affected usage patterns. This MIPS program is likely to have a small impact in Q4.

Importantly though, despite this MIPS program, Omidria is performing in line with our expectations, and we anticipate it returning to low single-digit growth over the coming quarters. Omidria will continue to be a major contributor to our portfolio through the end of the decade.

Orserdu royalties increased 224 percent from the prior-year period, reflecting the addition of the Orserdu II royalty. Orserdu also increased 26 percent from the previous quarter, as it continues to benefit from strong sales, performing ahead of our initial expectations.

Vonjo royalties grew 19 percent from the prior-year period, partly from the addition of the second Vonjo royalty. Vonjo also grew 6 percent from the previous quarter. Products is now showing signs of recovery after a few quarters of weaker-than-expected growth relative to our expectations. Q3 '24 sales quarter-over-quarter growth was 12 percent versus Q2 '24 quarter-over-quarter growth of 5 percent, versus Q1 '24 quarter-over-quarter growth of 1 percent. We anticipate this growth trend to continue as Sobi explores potential international expansion and new indications, opportunities that would represent upside versus our expectations.

Zejula royalty receipts grew by 36 percent from the previous year and 22 percent from the prior period. Sales continued to grow globally across all regions, sustained by increased patient demand and higher volumes, further enhanced by positive price impacts in the US. Several top-line data readouts are expected later this year, potentially leading to additional indications.

Empaveli/Syfovre continues its stable performance. Recall that we did not receive royalties in the prior-year period due to fluctuation in timing of payment from a two-quarter lag to a three-quarter lag. The quarter-over-quarter decline is due to a higher-than-expected Q2 royalties, which was a result of delay in payment from prior periods that was captured in Q2.

Importantly, Empaveli/Syfovre has year-to-date sales of $591 million, which is well above the Empaveli I transaction sales cap of $500 million. Overall, the combined Empaveli I and II transactions are tracking in line with our initial expectations.

Oracea royalty receipts decreased by 47 percent, year over year, and by 26 percent from the previous quarter. We're currently coplaintiffs with Galderma, the marketer of Oracea, in litigation relating to a generic entry. After a lower court decision in favour of the defendants, the defendants launched a generic version of Oracea at risk in the US in April 2024. The plaintiffs have appealed the decision.

Meanwhile, at least one other generic manufacturer of Oracea has launched its product at risk. The Court of Appeals denied the plaintiff's request for an injunction pending appeal and in September the Federal Circuit heard oral arguments on the appeal. We expect a decision within the coming quarters. The reduction in cash flows from Oracea is not anticipated to adversely impact the 2024 revenue guidance we have provided.

Eylea royalties increased slightly by 13 percent, both over the prior period and previous quarter. Regeneron, the marketer of Eylea, has been engaged in patent litigation with Amgen regarding their proposed biosimilar version of Eylea. Given the large step-down in royalty rates for Eylea over the past two years, Eylea now contributes only a de minimis amount of royalties that will continue trending downwards until expiry. Any adverse outcomes from this litigation would not have a meaningful impact to our cash flows.

Spinraza receipts declined 8 percent, year over year, and increased 21 percent over the previous quarter, which is in line with our expectations. Biogen noted some weakness related to one-time events in Russia, but otherwise highlighted global strength for Spinraza. The company specifically highlighted its

effective strategy for finding patients, and Spinraza's excellent efficacy is a differentiating factor amongst the competition.

Xolair sales increased in the third quarter by 12 percent, and Roche expects further growth acceleration in the remainder of 2024, driven by strong performance in the chronic hives segment, as well as for multiple food allergies that was approved earlier this year.

Expected contractual step-downs and expiries in our royalties on Eylea, Rydapt, Stelara, Simponi, and Ilaris partially offset the increases we have seen in our portfolio. As these assets near their expiries, we expect to see minor volatility, generic entry, and subsequent market share erosion, and potentially even litigation, as we've seen with Eylea and Rydapt. These events occur in the normal course as a drug reaches the end of its patent life, and we build these assumptions into our underwriting models.

Turning to our pipeline. Our pipeline remains as robust as ever with well over $3 billion in potential opportunities. This represents the aggregate value of potential opportunities under active evaluation by our investment team, that meet or exceed our qualitative and quantitative investment criteria.

Investors are starting to see signs of recovery in biotech as the market prices in expected cut in interest rates. There is, however, still an immense backlog of companies with significant financing needs. A recent BioCentury study noted that almost two-thirds of unprofitable biotechs listed in the NASDAQ have fewer than 24 months of cash remaining on their balance sheet.

Many of these companies saw early signs of recovery at the beginning of this year and were hopeful that their share price would increase to a level where they could effectively access the capital markets. Those higher valuations never materialized, especially for earlier stage, cash flow-negative biotechs. These companies now have burned through another nine months or more of their cash runway

and require significant investment to continue building their R&D or manufacturing and commercial activities.

Taken together, these factors are significant tailwinds for our business and, in part, lead to the tremendous amount of inbound activity we've seen in today's market as we continue funding innovative drug development and commercialization. We are patient investors, and our unique approach to sourcing deals allows us to be selective, executing only on what we believe to be the highest quality transactions.

We invest in cutting-edge and impactful drugs, transact with strong and like-minded counterparties, and craft unique deal structures that fit the needs of both our partners and unitholders. We remain committed to acquiring royalties on products that have the potential to transform patient care and enhance quality of life. Our focus is on therapies backed by strong marketers and durable intellectual property or regulatory protections, aligning with our target of a weighted average portfolio duration of over 10 years.

I will now turn the call over to Amit Kapur, CFO of the Trust.

Amit Kapur — Chief Financial Officer, DRI Healthcare Trust

Thank you, Navin. We posted strong financial results for the quarter. We recorded $38.9 million in normalized Total Cash Receipts, a 54 percent increase over the same quarter in 2023. We recorded $41.6 million in total income, a 22 percent increase over the same quarter in 2023. And we recorded $31.3 million in adjusted EBITDA, a 53 percent increase over the same quarter in 2023. This translates to an adjusted EBITDA margin of 80 percent.

On a run rate, go-forward basis, core margins should be more in line with historic norms. We incurred additional legal and investigation-related costs in the quarter of $2.2 million, which is net of $1.1

million reimbursed by the manager. Excluding these one-time costs, our adjusted EBITDA margin would be 86 percent, which is in line with consensus, as well as our historic average.

Finally, we delivered $0.45 in basic adjusted cash earnings per unit and declared cash distributions of $0.085 per unit.

Moving to Slide 13. We continued to generate strong cash flow from our assets, as Navin outlined earlier. For the last 12 months, ending September 30, 2024, our normalized Total Cash Receipts were $197.6 million, plus cash interest and other income of $2.3 million.

Our operating expenses and management fees totalled $31 million, net of performance fees payable, resulting in adjusted EBITDA of $166.6 million and adjusted EBITDA margin of 84 percent. We also generated adjusted cash earnings per unit of $2.44.

Moving to Slide 14. As at September 30th, we had $89.4 million of cash and cash equivalents, $57 million of which was used to fund the CASGEVY transaction. We also had $45.8 million of royalty receivables. As of close of business yesterday, we had $293.3 million of credit availability from our recently amended syndicated bank facilities. We are well capitalized to act on the attractive opportunities we are seeing in the market.

I will now turn the call over to Ali Hedayat, Acting CEO of our manager, DRI Healthcare.

Ali Hedayat — Board Trustee and Acting Chief Executive Officer, DRI Healthcare

Thank you, Amit. After my first full quarter in the role of Acting CEO, I am more and more confident about the future of our business. We've made significant strides across a number of key areas, including our remediation efforts, capital structure, and engaging with counterparties to complete innovative transactions.

We have a skilled team at all levels and functions of the organization, a renewed and effective governance structure, and valuable partners and stakeholders all around.

We've curated a considerable portfolio with strong assets to continue building upon an exciting pipeline of opportunities to work through, and we have substantial capital to deploy at our disposal. The Trust is much further along its growth path than we could have foreseen at the time of the IPO. With the completion of the sebetralstat transaction, we have now surpassed $1 billion in capital deployment, a large achievement in what has been, in many other ways, a very difficult year.

In addition to our deployment exceeding our expectations at the IPO, we have diversified and extended the tenor of the portfolio and built a platform for sustained cash flow growth. We have also achieved this with a diversified and well-managed funding mix, as our recently upsized bank facility shows. We have the pipeline, the team, and the capital to meet and hopefully exceed our deployment target in 2025.

Our key priorities are long term in nature and remain unchanged from previous quarters. First, our top priority is rebuilding and reinforcing stakeholder confidence. We are taking deliberate steps to enhance our governance practices and strengthen our internal controls. These measures are being implemented with diligence and transparency to ensure long-term trust and stability.

Second, we will continue to invest in our people and build an industry-leading team. Retaining top talent and attracting new expertise is critical to our success. Our team's ability to source and execute accretive transactions is a key driver of our growth, and I am confident that we will continue to deepen our talent pool on our investment team and across the organization. We're also making targeted investments in technology to enhance our deal sourcing and execution capabilities.

Next, we remain focused on executing our proven strategy, supported by one of the largest deal pipelines in the Company's history. The demand for innovative treatments remains high, despite current market challenges for biotech. We have made meaningful strides since our IPO and are well positioned to continue capitalizing on the strong deal flow ahead.

Finally, we're committed to being a key partner in advancing innovation within the life sciences sector. By providing critical funding across the value chain, we aim to create mutually beneficial solutions that both foster innovation and generate value for all of our stakeholders.

With that, we will now take your questions.

Q&A

Operator

Thank you. Ladies and gentlemen, we will now begin the question-and-answer session. Should you have a question, please press *, followed by the 1 on your telephone keypad. You will hear a prompt that your hand has been raised. And should you wish to cancel your request, please press *, followed by the 2. If you are using a speakerphone, please lift the handset before pressing any keys.

One moment, please, for your first question.

Your first question comes from the line of Doug Miehm from RBC Capital Markets. Please go ahead.

Doug Miehm — Capital Markets

Thank you very much and good morning, everyone. Navin, and maybe Ali, you could both expand on this. What I'm curious about is you did sort of signal a shift in terms of the types of deals you're willing

to do, adding a bit more risk, but certainly increasing the duration of the portfolio, in this case, by about 10 percent.

Could you tell us if, as we think about the future strategically, if you're going to continue to do those types of deals? Or are we going to continue to see a mix with a small proportion of those potentially at-risk deals?

Ali Hedayat

Hey, Doug.

Navin Jacob

I'll—yeah. Go ahead, Ali. Sorry.

Ali Hedayat

Doug, I'll just jump in, and then I'll let Navin elaborate. But I think, probably, the right way to think about this is we're going to take some steps in the direction of taking a little bit of what I would describe as managed preapproval risk.

When you look at this transaction, it's a transaction that obviously is very far along in terms of the approval process. It has a PDUFA date. We have all the data on the trials and such. And it's not in the same sort of category of risk that you've seen some of our competitors take in the preapproval space, so I think it's a very managed way to start approaching some of those transactions.

You will likely see us do some mix of that on a go-forward basis. Alongside some of the more regular-way transactions, you will also see us continue to innovate structural considerations like the equity component that we did this year. But the core of the business will remain cash-flowing royalties. I think that's something that we have reiterated and will remain very clear on.

I would view this step as a step along the path that we have voiced in the past about innovating our structures and the range of things that we're willing to do as a counterparty.

Doug Miehm

Okay. Thank you. And, Navin, maybe you can just expand a tiny bit on the competitive marketplace for that drug, particularly thinking about Pharvaris? And I know they're behind, but the data look reasonable. And maybe the competitive space for that drug looking forward? And I'll leave it there. Thank you.

Navin Jacob

Yeah. So currently, well, number one, Pharvaris is a couple years behind. That's first. But before we even get to Pharvaris, let's just be clear. Sebetralstat is going to be the first and only oral medication for the treatment of HAE. It's a tremendous advancement for patients living with HAE attacks.

And as I've said this to you before, Doug, but personally, as an individual who has severe food allergies, walking around with an EPIPEN can be very challenging and—or versus walk around with a bottle of pills would be significantly easier. And so if you think about HAE attacks, I think about it in a very similar manner, walking around with an injection or having to go and get it administered if it's an IV, which is the current—which is one of the treatments that are in the marketplace for HAE attacks, treating HAE attacks.

Sebetralstat provides the exact same efficacy as those injectables with the significant convenience of an oral. So we're tremendously excited about the asset. KalVista's management team—KalVista's built a strong management team that has a very strong commercial team that we anticipate will provide—will optimize the potential of this asset.

And with regards to the competition that's coming down the road, deucrictibant does look very interesting. It's a solid asset that's being developed for both the on-demand setting and as well as the

prophylactic setting. But it is a couple years behind. There is some value; there is some branding and some stickiness to the market that occurs. And so we think that we'll have—that, that'll have a lot of staying power for sebetralstat.

Furthermore, let's see how the phase 3 for deucrictibant plays out. The phase 3 is solid, but sebetralstat was at least as good as that deucrictibant data. Let's see what happens in phase 3. Phase 3s typically tend to trend down relative to phase 2s. So we're going to have to see what exactly happens there before we can make a judgment.

But regardless, as you know, Doug, we're a conservative organization. We take into consideration all competition, not just a quick event, but any activities that are not just in that on-demand setting, but also in the prophylactic setting, that may have any potential impact to the overall market for the on-demand setting. We've assumed extremely conservative assumptions in our forecast.

And at the end of the day—and this is an important point—it's not about what competition is coming down the road, but what have we assumed about that competition? We've assumed that deucrictibant launches. We've assumed that they take share from the—into the overall market and so—and we underwrite our deals according to those assumptions.

Doug Miehm

Excellent. Thank you very much.

Operator

Thank you. And your next question comes from the line of Leszek Sulewski from Truist Securities. Please go ahead.

Leszek Sulewski — Truist Securities

And good morning. Thank you for taking my questions. Navin, just on that note, appreciate the portfolio overview and the other Orserdu and Vonjo. Are you seeing any unexpected outperformers or underperformance across your portfolio of products that are beyond your initial expectations?

And then just to kind of follow up on the previous comments, sebetralstat gets you into treatment of HAE attacks on demand. Are there, you know, we're looking at other expansion opportunities within this indication, specifically on the prophylactic side, with other products facing upcoming approval. Are those of interest to you? And kind of just walk us through that reasoning there. Thank you.

Navin Jacob

Yeah. So I'll answer your first question, which is with regards to other products in the portfolio that are performing—either under or overperforming. As I noted, Omidria, there's been a little bit of lumpiness the past couple of quarters, but we've spoken about that before. I think what's important is that we're seeing some recovery there; the same for Vonjo as well.

And the Omidria is largely in line with our expectations, despite some lumpiness in the quarter. Vonjo, we had noted before, had been, for a couple of quarters, a little bit below our expectations but it's trending back nicely, back towards our initial expectations.

With regards to potential other opportunities in HAE, we look at everything, and we're open to any counterparty or partner that has an interesting asset. At the end of the day, we are therapeutic area agnostic. We are modality agnostic. And ultimately, we have certain investment criteria with regards to the quality of the asset and the value creation that we can provide to unitholders, and that's what drives our decisions.

Operator, I think we can take the next question.

Operator

Thank you. And your next question comes from the line of Michael Freeman from Raymond James. Please go ahead.

Michael Freeman — Raymond James

Hey. Good morning, Ali, Gary, Amit, Navin. Congratulations on the quarter. Congratulations on a great deal cadence of late. I wanted to ask more questions about the KalVista drug.

As the recent deal contemplates royalties on sales, sort of on sales up and over $500 million, and where KalVista talks about a global market for on-demand HAE drugs in the $900 million range total, according to the calculations we've done back here, in order to drive an IRR well over 10 percent, it kind of looks like this drug needs to do about $500 million or more. What gives you such confidence in these sales? And like, there might be discrepancies between our calculations, but what gives you confidence in the sales of this drug?

Navin Jacob

Well, I can't—that's a very sophisticated way of trying to get to our peak sales and our IRR calculations. I like that question, Mike, but I'm not going to fall into that trap.

But I will—what I will say is that, if you looked back in 2018, the branded market prior to FIRAZYR going generic was roughly a billion-dollar market. If you then assume some small pharmaceutical price inflation over a 10-year period and you can get to—and then assume some small increase in the treatment rate of HAE attacks, which is very reasonable based on all the payer analysis we've done, the claims database analysis we've done, the KOL interactions we've had, interviews, as well as the position surveys that we've conducted, all of those, and the literature reviews that we've conducted—it is clear that the

market can get to—on a branded perspective, remember, because firazyr is generic now, so the dollar market is smaller than it actually can be.

But if you apply a branded price to that FIRAZYR market share, then you can get to a place where the market can conceivably be a $1.2 billion to $1.5 billion market and kind of—yeah, call it in the 2030-plus period.

Having said all that, that is … you know, we are a conservative company. We have made some assumptions around the product that are, we feel, very fair and assumes a fair amount of competition from other entrants down the road, as well as impact from the prophylactic setting applying to the treatment setting. And despite that, we found that we are able to get to sales that are interesting.

And importantly, the structure of our deal provides which, you know, it's unclear what you're—what exactly you're calculating, Michael, and happy to talk about that offline—but we get to a place where our IRRs and, even more importantly, at the multiple should be very attractive for unitholders.

Ali Hedayat

Mike, I would just echo what Navin said there. I think the structural consideration in terms of (unintelligible) that our Roche (phon) deal was tiered at various sales levels is one thing that really works well for us in terms of returns.

And what I would also say is just echoing the comment on sort of IRRs and duration. This transaction is sort of in line with the broad range of IRRs that we have done in the past. But very importantly, when you take those IRRs and play them out over the duration of this asset, what you're getting is a very good multiple on money.

And I think we've spoken about in the past, that sort of balancing act between near-term cash flows and duration and IRRs and multiples that's sort of embedded in that. And I think you will see us

continue to be tactical about that going forward in terms of balancing the shape of the portfolio between those high-multiple, longer-duration-type assets and near-term cash flow that allows us more investing flexibility and debt capacity.

Michael Freeman

Thank you. Thank you, Ali and Navin. And very quickly, I wonder if you could touch on anticipated milestone schedules. Looking back at agreements, it kind of looks like Orserdu and Vonjo might be on the cusp of a couple of milestones. I wonder if you could share any colour.

Navin Jacob

Yeah. As far as Orserdu's concerned, we've achieved most of the milestones that we were anticipating. We are eligible for more, but we have achieved all that we were anticipating from a base case perspective; potentially, can achieve more from an upside case perspective. But the deal that we underwrote to, we have achieved the milestones that we had—already, that we had anticipated.

With Vonjo, there are some other milestones that we assume that will hit down the road, but I can't comment further than that.

Ali Hedayat

Mike, and again, it's Ali, just to add a little layer to that. Generally speaking, when we underwrite a transaction, the payment of outgoing milestones, here, we're talking a little bit about a mix of receipt of milestones and payment of milestones. But generally speaking, the payment of outgoing milestones is something that is a good event for us in that it's sort of enhancing the return of the deal.

We're not getting ourselves into a situation, by and large, where those milestones or outbound payments are subtracted from our IRRs. So if we find ourselves in a situation where we're paying

milestones, that's generally a happy moment for us, as well as our counterparty. On the inbounds, I think that was broadly covered by what Navin spoke about earlier.

Michael Freeman

All right. Thanks very much. I'll pass it on.

Operator

Thank you. And your next question comes from the line of George Farmer from Scotiabank. Please go ahead.

George Farmer — Scotiabank

Hi. Good morning. Thanks for taking my questions. Wondering if you could just kind of elaborate more on the dynamics of the marketplace now. Certainly two very creative deals you recently did. Do you think that this is a direction that this marketplace is going in, kind of combination of synthetic royalty/equity investments?

And then also, just to bring up something from the beginning of the year, you did issue guidance of $153 million to $155 million in royalty income at the beginning of the year. You're clearly exceeding that or on track to do so. Does it make sense to update that guidance? Or do you think this isn't a good exercise going forward? Thanks.

Ali Hedayat

George, I'll take the guidance point, and then Navin maybe can speak about the market conditions and deal structures. On guidance, I think we've gotten a bit of a cadence of updating guidance with every transaction. I think that's something that we'll take a step back from and probably update periodically through the year. And I think that will help both encapsulate the transactions that we've done and also the projections of asset performance.

And I think that's just more helpful and talks about the scale of the business. I think the transaction-by-transaction guidance updates were maybe a bit more appropriate when the portfolio was subscale and we were building it up. I think this deal was pretty transformative to the shape of our cash flows. On a go-forward basis, I think we'll sort of go to something like a normal company cadence of guidance updates.

Navin Jacob

George, with regards to the broader marketplace, what I'll say is that I'm not sure how other folks will—our competitors or colleagues or however you want to describe them—will be reacting or acting. This is—the move towards conducting more synthetic royalties, participating in small pipes as part of a broader royalty deal, that was a very—it did not happen overnight. It did not happen randomly. It was a very well-thought-out process, and there was extreme diligence that went into whether we should do this, why we should do this, pros and cons, how we do it, implement it.

It was an 18-month—or we had—the first time we formally met to discuss it, we were bandying it about for more than 18 months, but formally kicked off the process with it 18 months ago and went through a six- to eight-month process of diligencing newer avenues of royalty investing before we started even attempting to go out to the marketplace to see if there was appetite.

And as we suspected, there was a significant appetite, and we are happy to be implementing our first such transaction with KalVista, who we feel very good about and have a wonderful asset that we are happy to participate and help fund.

But I think, more broadly speaking, what we're excited about is not this one type of transaction. We're just broadly more excited about royalty investing. And we've spoken about this for several quarters over and during analyst meetings and so on and so forth.

One of the medium-term trends that—I've spoken about three trends that are driving our business, short-term trend driven by weakness in equity capital markets; longer-term trends, driven by the need of R&D funding, or just funding in general for the biopharmaceutical space, driven by innovation, which is clearly inflecting up over the long term.

But the medium-term trend, which I've spoken about, which you're kind of asking about, is just this need for—or it—there should be, very clearly, a place for royalty investing as a third leg in the financing stool that CFOs and CEOs of biotech companies should have access to, in order to best optimize the value for their products and their shareholders, respectively. And we want to be one of the drivers of pushing royalty investing, or royalty financing, as not just an esoteric means of financing, but a mainstream way of raising capital.

Ali Hedayat

George, it's Ali here. The one thing that's pretty clear to me in the time that I've been here is that we have a very large amount of white space to grow that business, and I think synthetics is a key element of that, especially with some of the small and midsize product types that are having difficulty funding.

And as Navin said, I think we'd like to see a world where they look at their various funding options and understand that on the road to managing dilution and achieving their aims, royalty financing is as viable or better in many cases than equity or some of the structured debt-type deals that you see out there, in response to their funding needs. So I think we're at a very, very early stage of the share of what royalty funding could be in terms of the biotech funding stack.

George Farmer

Okay. Great. Thanks very much.

Operator

Thank you. And your next question comes from the line of Scott Fletcher from CIBC. Please go ahead.

Scott Fletcher — CIBC

Hi. Good morning. Just one question for me on the debt and the new capacity. It seems like, now, that the leverage ceiling would be more of the limit to what you can spend. Could you just give us an update on sort of where you're willing to take leverage to? And sort of—and if there's a willingness to sort of take that up to the ceiling in the near term, given that some of the recent royalties aren't cash-flowing immediately?

Ali Hedayat

Yeah. It's Ali. Look, I think I'll just reiterate what we've said in the past, which is this is not a levering-up exercise in the sense that the multiples of EBITDA that sort of bind our debt agreement are the same. Right? So we're not levering up in terms of terms of leverage. What you're seeing is the dollars of leverage available to us, at the same leverage multiple, are going up, and I think that's just a reflection of the business growing.

So broadly speaking, our intent is, as the business grows, to increase the dollars of debt available to us, but not to lever up in terms of the EBITDA terms that we have on the portfolio. And I think that's a very prudent way to manage it.

With regards to where we're at on that journey, I'd say that, as you alluded to, some of the transactions we've done are a little bit more back-end loaded in terms of their cash flows. So the ability to fully access our leverage ceilings will obviously be bound by the EBITDA that we're generating, and I think the EBITDA of the portfolio will continue to grow and sort of unlock that capacity.

And I think, as I said in the past, we're going to be reasonably dynamic about the types of deals we do. And we did some pretty long-range deals that extended duration and provided us with high multiples, and we could certainly, in the future, look at some deals that have more current cash flow and balance that out in terms of unlocking capacity in the debt facility.

But all that said, we're in a great place in terms of capital availability. We have a lot of unused capacity in the facility, even at our current run rate EBITDA levels. We have a lot of cash flow that we're generating right now that feeds into our investing capacity, and I think we don't see that being at all an impediment to achieving or even exceeding our '25 deployment guidance.

Scott Fletcher

That's great. Thank you.

Ali Hedayat

Are there any more questions—

Operator

Thank you. And your—apologies. Your next question comes from the line of Zachary Evershed from National Bank Financial. Please go ahead.

Zachary Evershed — National Bank Financial

Good morning, everyone. Just a quick one for me. Could you give us maybe more detail on the tech investments that will help sourcing and execution for deals?

Ali Hedayat

Yeah. We hired a data science specialist. He's a PhD from Columbia. He's been working on a number of different initiatives. Internally, he also has a biotech background in addition to his computer science work.

He's been working on a number of initiatives. Some of those are basically what I would broadly describe as taking the existing information that we have available internally and allowing us to optimize the way that we lever it to streamline our processes. And a lot of that is sort of building bridges to openly available LLMs and machine-learning type of constructs and running our data through those and optimizing our ability to search and create conclusions.

From that data, I think the second leg of that is going to be, maybe, a step beyond efficiency and speed improvements and seeing if we can create insights into what we should be looking at.

But for now, what we're really doing is freeing up the research team's time to focus on sourcing and executing investments by taking a lot of the background work and just making it more efficient through automation.

Zachary Evershed

That's great colour. Thanks. I'll turn it over.

Operator

Thank you. And your next question comes from the line of Justin Keywood from Stifel. Please go ahead.

Justin Keywood — Stifel

Good morning. Thanks for taking my call. Just had a question. With the new US administration coming in, do you anticipate any impact directionally on the portfolio of assets or new pursuits? Any puts or takes to note?

Ali Hedayat

It's too early. Sorry—

Navin Jacob

Yeah, I was going to say the exact same thing. I think we just have to see, Justin. What exactly the platform is for the new administration is a bit of a question as it relates to healthcare. There have been some various names that have been thrown around that are associated with the new administration that may have a very different view of how the biopharmaceutical space and drugs should be approved and which drugs should be approved.

All of that is not necessarily a bad thing, quite frankly, for our business. I think it adds that, plus any potential for inflation, which most macroeconomists believe will occur under the new administration and will translate into higher interest rates. All of that is, quite frankly, not a negative thing, probably exactly the opposite, actually, for our industry, i.e., the royalty industry, insofar as volatility in or lack of understanding of pricing and/or higher interest rates makes for challenging equity capital markets for the biotech sector, which should be very positive for the royalty investing sector.

Justin Keywood

Thank you for the initial views.

Operator

Thank you. And your next question comes from the line of Tania Armstrong from Canaccord Genuity. Please go ahead.

Tania Armstrong — Canaccord Genuity

Good morning, gentlemen. A couple for me, and apologies if I missed this in your early remarks. Could you provide an update on where things stand with the potential internalization of DRI Capital, the manager? I know this is something you've talked about in the past.

Ali Hedayat

Yeah. I'll chime in there for a second, and then I think Gary will probably want to say some words about it as well. But look, we are actively exploring all sorts of avenues to think about an optimal structure that's the best outcome for our unitholders. I think in the broad range of that, internalization is certainly one of the things that has been looked at and discussed.

As you know, there are a number of tax issues we need to work through, and then there's some sort of earnings impact work that we're doing and weighing those two things against each other and seeing where that comes out versus where potential sort of multiple impacts would offset that or not.

I think we're decently advanced in terms of that assessment. I think it's something that we'll probably really, really take a hard look at likely in the first quarter of next year. And I think that is a dynamic discussion in the sense that some of the parameters that may or may not make it viable now are constantly in flux with the growth of the business and various other factors.

So having done that work, whether or not it's something that we engage in, in terms of actually consummating it in early part of next year, it'll really be work that's available to us and we'll be able to reassess dynamically as the business grows and circumstances evolve.

Gary Collins

Yeah. And I wouldn't add too much to that other than that we're just—we're going through that process. We've talked about it before. We're looking at a number of different structures, trying to get an assessment of what's the best for unitholders, and we'll follow that path where it leads us.

Tania Armstrong

Okay. Excellent. And then just secondly, I know a question on guidance came up previously. But I'm wondering if you can provide updated royalty income CAGR guidance. I know this is something you've

typically given us a little bit of light on, heading out to 2030. Is this something you'll be updating? Or that you can provide more colour on?

Ali Hedayat

We'll likely update that in the fourth quarter.

Tania Armstrong

Okay. Excellent. Thank you, guys.

Ali Hedayat

Thank you.

Operator

Thank you. There are no further questions at this time. I will now hand the call back to Mr. Gary Collins for any closing remarks.

Gary Collins

Well, thank you, everyone, for taking the time to be with us this morning. We look forward to discussing our Q4 results with you later in March. And thank you for your continued support of DRI Healthcare Trust.

Operator

Thank you. And this concludes today's call. Thank you for participating. You may all disconnect.