Q&A with James R. Neal, CEO of XOMA Corporation discussing their New Focus as a Royalty Aggregator to complement their Asset Generating Antibody Discovery Platform and their Portfolio of Programs Licensed with Biotech and Big Pharma Partners

James R. Neal
Chief Executive Officer and Member of the Board of Directors
XOMA Corporation (Nasdaq: XOMA)
http://www.xoma.com/

Interview conducted by:
Bud Wayne, Editorial Executive
CEOCFO Magazine

“
We offer a unique way for investors to participate and get exposure to the upside that biotech can bring, but without necessarily exposing themselves to the binary outcomes that are so characteristic of biotech.” - James R. Neal

CEOCFO: Mr. Neal, you joined XOMA Corporation in 2009. What did you like about XOMA at that time and what in your background and experience did you bring to the table for XOMA that would enhance its growth?

Mr. Neal: What I was particularly impressed by at XOMA when I joined the company, were a couple of things. I was a big fan of the lead asset, gevokizumab, which was in clinical development at the time that I joined. Gevokizumab is an IL-1 beta inhibitor for broad spectrum anti-inflammatory indications. I was very excited about what gevokizumab as a drug candidate could represent to patients and the ultimate commercial possibilities there. The other thing I liked about XOMA was the antibody discovery platform and capabilities that we have here as a company, really based on some foundational scientific work and intellectual property that the company has going back many, many years. Since its inception, the antibody discovery platform has been the foundation for the company and the engine which could produce assets like gevokizumab. When I looked at the company, I thought that there were a great number of possibilities here – both drug candidate assets and the technology platform and capabilities. From my personal perspective, what XOMA was looking for and I thought I could contribute was business development and commercial capability. I had come through various roles in business development in biotech, and prior to that in a larger company setting. Those experiences, of having done multiple licenses on platforms and on drug candidates assets was something I felt I could bring to XOMA that could enhance the growth of the company. XOMA was eager to do licensing deals to be able to get partners for its discovery programs. I felt I could play an important role in being able to secure those types of arrangements.

CEOCFO: XOMA has recently changed its focus as well as brought on new leadership. Would you tell us the reason for the change? Was the change your brainchild?

Mr. Neal: One of the strengths of the company as I mentioned has been our discovery capabilities. The platform has been the core XOMA over
time. But, we have struggled to take those discovery candidates all the way through clinical development and ultimately to commercialization. Drug development is a challenge in itself, and for XOMA it had been a particular challenge throughout our history. Therefore, the former business model seemed like a risky prospect from the point of view of both the novel science, but also the amount of capital called for. Hundreds of millions of dollars are required to do these late stage clinical trials. It is actually kind of crazy to keep doing the same things over and over again, taking the next lead candidate and bring it into development and expecting a different outcome. Hence, it felt like an appropriate thing to do was to think about the business very differently and change things up. What was underappreciated about XOMA was the depth and the breadth of the licenses that it had put in place as a result of its 30 years of existence. These licenses had a great potential to provide royalty and milestone revenues if we allowed the drugs to develop in the hands of our licensees. We thought if we could embrace this history and capitalize on this portfolio of licenses that had already been done, we could have a very successful and very, very different business from anything the company had done before. It was essentially concluding that we should focus on the things we had done well in terms of the technology and the platform capabilities that had turned into licenses. These have resulted in partner programs at both biotech and big pharma companies where we could enjoy downstream economics from the advancement of those programs.

In terms of how we got to this place, it was something we discussed with external advisors and on a strategy sub team. There was probably an 18 or 24-month period before we actually made the change. Though we were intrigued by this strategy, what we could not figure out was how to get the company to that new point. It would require a very different orientation and a financial bridge to launch the strategy. We were able to build this bridge in the recapitalization of the company by BVF Partners. This provided us with the ability to align this strategy with the capability to execute. As a background, we really had the three elements that we believe were really necessary to come together for us to succeed. First, we had an existing portfolio of over two dozen fully funded programs. Secondly, our management team in myself and Tom Burns, our Senior Vice President, Finance and Chief Financial Officer, was willing to run a lean organization with a strong deal orientation. And finally, we believed this should be housed in a publicly traded entity where ultimately revenues could produce earnings and attract an exceptionally high earnings multiple in terms of valuation. Those elements were all there, but what the BVF financing did was to provide a short-term bridge and an aligned long-term partner focused on the royalty aggregator strategy. Their investment and belief in us was critical to our launch of the new strategy in March 2017.

**CEOCFO: Would you introduce us to the new members of your team and tell us what they bring to XOMA?**

**Mr. Neal:** I mentioned Tom Burns, who is our CFO. He has a strong financial background and has been with the company for over 10 years. He knows the investor community really well and has strong relationships with bankers and analysts. He was part of the small team that outlined this new strategy, as he and I particularly were the architects that defined this new strategy for the company. In addition, we have Kirk Johnson, PhD, who is our Vice President of Technology and Development. Kirk is leading our small technical team that supports both
the out-licensing efforts and the acquisition efforts from a scientific and clinical perspective. We have a small team. This is core to the strategy and our team focuses on transactions, legal, corporate governance, IP and licensing strategy, and maintaining our public listing.

CEOCFO: XOMA is now focused on driving shareholder value by combining revenue from a portfolio of partner-funded programs with a lean cost structure. With an operating cash burn cut by over 50%, what did you do to bring this about?

Mr. Neal: We are really intensely focused on the core strategy of driving shareholder value by combining the revenue from this portfolio of partner-funded programs with a lean cost infrastructure. We made some difficult decisions to restructure the size and nature of the organization, but they were really important and reflected the strategy. Ultimately, what we had to do was eliminate some resource intensive functions here at the company, such as manufacturing and even our core research and clinical development. These were not part of what we are about in this new world as we embraced these historical partnership arrangements and as we begin to acquire additional milestone and royalty assets. We eliminated manufacturing, discovery research and clinical development. The net effect was a very dramatic reduction in the size of the company as we went from several hundred employees to our current size of less than 20. Naturally, we were able to outsource some functions such as HR and IT, and we moved to a much smaller physical space. The strategy really is designed for us to see our revenues become cash flow positive by combining them with a lean cost infrastructure.

CEOCFO: Would you tell us about your partner-funded programs? What is your involvement? Are you out-licensing and your partners taking the products through the clinics and providing you with milestones?

Mr. Neal: As I said, one of the keys of the company is that we already have over a couple of dozen partner-funded programs in the portfolio today and that number continues to climb. The key in this whole structure is that our partners bring the financial investment capital to these programs, so we do not have to do that. However, as the programs advance we receive economic reward in terms of milestone payments and ultimately royalties as these assets advance through clinical development and into commercialization.

Essentially, we are a passive partner in the process once we have done the out-licensing, and so we do not really control the pace or the path of the development of these drug candidates. However, we do get to enjoy the economic benefits as those assets advance and it really does come at no cost to us. We think of these programs as being fully funded, because 100% of the investment is really done by our partners. This is the key to this whole strategy. The really heavy lifting is actually done by people who are much more financially capable and have the scientific and intellectual wherewithal to be able to advance these programs much more effectively than we could.

CEOCFO: What does the payment structure look like?

Mr. Neal: There are payments that we get as these candidate drugs advance through clinical development, from Phase 1 to Phase 2 to Phase 3. Then if our partner gets to the point of commercialization we expect to receive royalty payments.
CEOCFO: Would you tell us about your gevokizumab and IL-1 beta IP portfolio program with Novartis? How did your relationship with Novartis come about?

Mr. Neal: We have had a long standing relationship with Novartis, having done several licensing deals with them over time. For example, prior to doing the gevokizumab license agreement, we had 3 other major programs already advanced and in their hands from prior interactions with Novartis. They are a major pharmaceutical with a great many initiatives in many diseases in many countries. This was a broad relationship we have had with them. The gevokizumab, IL-1 beta license was really transformational for us and sort of highlighted some key components of our overall strategy in a single transaction. It allowed us to build on our portfolio of fully funded programs. Gevokizumab became one more of the fully funded programs we have on our list, now being advanced by Novartis. The IL-1 beta intellectual property was also out-licensed to Novartis on a non-exclusive basis, so in the event that their IL-1 inhibitor canakinumab, produces revenues in cardiovascular indications, we would enjoy some royalties from those sales.

We expanded the portfolio of fully funded programs, and we also received about $45 million worth of liquidity from Novartis in this transaction in the form of cash and debt forgiveness and a $5 million equity investment. Therefore, we strengthened the balance sheet through this transaction. We also, as I suggested, anticipate milestones and royalties for future revenues from the gevokizumab license of up to $438 million worth of milestone payments, and then high-single to mid-teens royalties. Then, as I mentioned, single digit royalties in the case of canakinumab sales in cardiovascular indications. So that whole idea of milestones and royalties for future revenue was embedded in this transaction as well. What it did for us as well, was remove our financing overhang. We are now projecting 4+ years of cash runway. As well, our other programs in the portfolio to continue to advance in the hands of our partners. In addition, we do not have any debt repayment due until 2022. All of these things were part of that single transaction with Novartis and was really transformational for us.

CEOCFO: Where is Novartis in the development process?

Mr. Neal: Novartis has essentially 4 assets of ours that are in their hands. We have the anti-CD40 antibody program, which is really in multiple ongoing clinical studies and has completed Phase 2 development in several different diseases including Sjogren’s Syndrome. That program is advancing nicely in mid-stage clinical development. The TGF beta program is in immune-oncology, which is a very hot area of drug development. Novartis licensed this program from us in 2015, and it is in Phase 1 stage at this point. We mentioned gevokizumab, which is basically a Phase 2 or Phase 3 asset depending on how you think about it, so it is also in late stage clinical development. Then canakinumab is actually already commercial, and Novartis is anticipating to expand the label for canakinumab to include cardiovascular uses.

CEOCFO: You have had an impressive list of companies that you have and have had partner programs with, such as J&J and Lilly. What is your strategy for outreach and is building those relationships a major focus for you as CEO?

Mr. Neal: The strategy is really interesting and goes back to one of the things that attracted me to XOMA in the beginning. That is all about the science and the strength of the XOMA capabilities in the area of
monoclonal antibody drug discovery. That is the key. Without that foundation these relationships do not take place and there is no reason for J&J, Lilly or others like them to talk to us. We really do have some great science that we can represent to these potential partners.

As for what is really important here, it is still the science and the foundational platform that produces these drug candidates. As CEO, with my business background, I place great value in these relationships and we work hard as to ensure that we are a good partner for these companies with whom we have licenses and collaborations. It is really their efforts that are going to produce the milestones and royalties for us in the future, so it is important for us to interact with them and maintain good relationships with these companies.

CEOCFO: Would you tell us about commercial products with XOMA IP and are there any other products that are near-term?
Mr. Neal: There are multiple examples of commercial products developed with XOMA IP. There is an oncology drug, RITUXAN®, an anti-inflammatory drug, CIMZIA®, and LUCENTIS®, which is a product from Genentech for ophthalmology. These are examples of commercial stage assets, and on-market drugs that have been touched by XOMA intellectual property. We do have multiple drug candidates at late stages in clinical trials which have potential to show positive results in these studies. Again, all of these are in the hands of our partners. We have not provided guidance to the market as to which might make it to approval and when we might expect that to occur.

CEOCFO: How many partnered programs do you currently have and are there any others that are producing milestones that we should be aware of such as your program with FivePrime and the recent XOMA 358 exclusive license agreement with Rezolute, Inc.?
Mr. Neal: Today we have over 2 dozen fully funded partner programs and the majority of these have the potential to produce additional milestones for us in the future and all of them have the potential to produce royalties for us – typically with a ten year post commercialization term. Therefore, they are all very, very valuable to us, and they are at various stages from pre-clinical to early stage clinical, to late stage clinical development. As you suggest, we continue to add to our fully funded programs with license arrangements such as what we just were able to recently announce with Rezolute, Inc. for XOMA 358. XOMA 358 is an asset that we also had developed here as a company. This compound, for example, is in Phase 2 stage and we anticipate it moving to the later stage development in the next little while. With over 2 dozen programs in place, we have a strong portfolio of opportunities for us to continue to deliver milestone and royalty revenue. What we have said publicly is we anticipate up to $60 million worth of potential milestone payments could accrue to us over the course of the next 36 months.

CEOCFO: Given your recent licensing agreement with Rezolute, XOMA now currently has only 3 programs ready for partnering. Would you tell us about those, where they are in development and why they should interest a potential partner?
Mr. Neal: We do have 3 assets currently available for licensing. XOMA 213 is a clinical stage program for the treatment of hyperprolactinemia. We also have our very interesting asset for immuno-oncology, our IL-2 program, which has the potential to expand the therapeutic index of Proleukin® (aldesleukin), which is a very powerful, but quite toxic
oncology drug. Then we have the Anti-PTH1R program, which is a pre-clinical stage program anticipated for the treatment of hypercalcemia endocrine and oncology indications; showing some interesting reductions in calcium levels.

**CEOCFO: A $25 Million BVF Partners investment with no debt repayment until 2022 is pretty impressive? Do you feel set for the near term for further acquisitions?**

**Mr. Neal:** Bud, you have hit the nail on the head. The engine for growth for us is actually acquisition of additional milestone and royalty assets, and we do see those being a critical focus in the forthcoming year and onward. We have made some significant progress in 2017, in strengthening our balance sheet, to a point where just over a year ago where we had over $40 million of debt, but we are now at a point where we have 4 plus years of projected cash runway and this does not include the possible $60 million worth of cash receipts coming from anticipated milestone payments over the next 3 years. We have dramatically changed the financial health of the company and are now in a position to do some monetization transactions. That said, for us to really successfully execute the strategy it is important that we work on strengthening the balance sheet even further in order to be viewed as a credible, viable provider of capital for companies wishing to monetize their royalty streams. We need to have cash on the balance sheet. Therefore, we continue to focus on capital access as a key component of our strategy of expanding our portfolio of fully funded programs. We have seen many opportunities to be able to acquire milestones and royalties. We are thinking about capital sources for the company to execute on our strategy, either through debt or equity, or a hybrid combinations thereof.

**CEOCFO: As CEO do you spend a great deal of time on the road with investor outreach and attending conferences, both investor and healthcare/industry/product related conferences?**

**Mr. Neal:** Yes, and it is important, even more so than at this stage of our company’s life. As CEO I do spend a great deal of time on the road with external stakeholders such as investors or prospective investors at investor and healthcare industry conferences. In fact, there is a big healthcare conference that occurs every year in San Francisco, in the January timeframe, the J.P. Morgan Healthcare Conference. It is a big event, and kind of a kickoff event for the industry for the year. We have probably about 40 or 50 meetings booked over the course of the 3 or 4 days of that conference. We will use this conference to build awareness in our ecosystem of the new XOMA, with the various companies who might benefit from what we are now doing such as venture capital firms, or investment banks. We could benefit small biotech companies by providing them with non-dilutive capital that could be helpful for them to advance their programs in exchange for future milestones and royalties that we would receive from those companies. It is a good event for us to evangelize and create awareness of what we are doing within both the investment community and the broader healthcare ecosystem.

**CEOCFO: Final thoughts. Why is XOMA Corporation’s new focus a winning strategy?**

**Mr. Neal:** That is a great question. We get all wrapped up in biotech stuff, pathways and biology and disease indications. However, the way to think about XOMA is first and foremost we believe we offer a unique way for investors to participate and get exposure to the upside that biotech
can bring, but without necessarily exposing themselves to the binary outcomes that are so characteristic of biotech. It is a nice way to play in biotech without necessarily taking on that same risk profile of having drug failures be the constant theme you are worried about. We are still to this day in an industry where more drug candidates fail than make it to the marketplace, and by this portfolio of opportunities that we have, we think we could benefit by being strongly positioned to see the successes, without the huge negative of the failures. The chance of a drug candidate making it all the way from discovery all the way through to commercialization is less than a 10% probability. However, we have a portfolio of assets where the chance of none of them making it to commercialization is significantly lower than that. There is actually a really high chance that at least a few of the assets in our portfolio will make it to the marketplace. I could not tell you today which ones it might be, but the portfolio is really the key to success. We’re building on and expanding our portfolio so that over the time we will have multiple shots on goal to produce royalty revenues for us in the future.