

Sector: Pharmaceutical

Hemispherx Biopharma, Inc.

Analyst: Florian Homm

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Fundamental outlook: Reinforced through recent developments

Recommendation: Strong Buy recommendation reiterated

VALUE MANAGEMENT & RESEARCH AG

Bear raid likely to provide first-rate buying opportunity

The upcoming (September 28th) *Business Week* article already available through the Internet features a brief article on Hemispher_x. The article quotes a well-known short seller who believes Hemispher_x major product, Ampligen, is both ineffective and highly toxic and (what a surprise) says that the stock is going to zero. Dr. Carter, Hemispher_x's CEO, calls the claims frivolous and wrong. We would simply call the comments as superficial, self-serving and poorly researched. For one, Ampligen has undergone the most rigorous testing by the Food and Drug Administration regarding safety and efficacy. The product sailed through phase one and two trials and has been awarded Treatment IND status by the FDA. This special FDA status is awarded to treatments involving diseases which cause severe hardship and suffering and where the treatment shows evidence of being superior to any other treatment alternative. To date 100% of those treatments which have gone all the way through this approval process have been approved. In other words, no treatment accorded Treatment IND status has ever been refused FDA approval. The short sellers seem to be making a poorly analysed bet against huge odds in this case!

The short sellers also claim that share dilution from preferred stock issues and warrants is likely to increase shares outstanding to 41 million. Serving, their own best interests, they fail to mention that an increase in shares outstanding would further strengthen the outstanding balance sheet of Hemispher_x. The company currently reports to hold net cash of about US\$ 13.5 million. This sum alone would support the company's operations for about four years given the current burn rate. Moreover, should certain outstanding warrants be converted in the coming weeks, we expect a further \$20 to \$24 million of cash to come into the company. Share dilution is public information and has always been factored into our share price and earnings calculations. Yes, there will be dilution, but if all options, warrants and preferred stock were exercised the company would receive \$55 million of additional paid in capital.

The short sellers and VMR however agree on one subject matter. The stock has performed well, much to the chagrin of short sellers. Conversations with short sellers, major broker/dealers and half a dozen stock-lending desks confirm that Hemispher_x's shares are virtually unborrowable. Much more significant for the short sellers, lawyers have been analysing and reviewing illegal short sales of Hemispher_x's stock. Selling shares that have not been borrowed in advance and sold naked can ultimately not be delivered. As a consequence, illegal short sellers attempt to delay delivery as long as possible hoping the share price goes down so that they can buy the shares back in the open market for delivery. If the share price however moves up (as in Hemispher_x), the shares are bought in by their brokers because buyers demand delivery. There are apparently so many naked shorts in Hemispher_x that the first rounds of forced buy-ins are already taking place. In the meantime, if the shares do not decline on their own accord, the short sellers frequently work with media contacts to negatively influence the share price development.

Given the precarious and rather desperate position of certain short sellers (the share price has more than doubled this year, and naked short buy-ins are imminent) a bear raid has to be organised through increased and negative media exposure. The short sellers are now hoping that their attempt at discrediting the company through media contacts will lead to a precipitous price fall allowing them to cover both the legal and illegal short positions in a few days. Should these efforts by short sellers lead to a sharp price decline due to investor uncertainty we would see this as an excellent buying opportunity.

Back to Basics

In light of complex investor and media manipulation strategies it makes sense to revisit the basic investment case. It also makes sense to monitor the company's progress since initiating coverage. Whether Hemispher_x will go to zero or sixty dollars will probably be decided by the middle of next year. Given the company's ample cash position and low burn-rate the former will not likely be the case. The battle between bears and bulls will have to be resolved so fasten your seat belts. Here are the facts:

- The company is in excellent financial health.
- Evidence from successfully completed FDA Phase one and two trials strongly supports both efficacy and safety.
- The emergence of a reliable diagnostic test for Chronic Fatigue Syndrome (Professor Suhaldonik, Temple University) could substantially enhance the identification of this condition with greater ease. This is a recent and important development in addressing this potentially billion-dollar market.
- Treatment IND status is only awarded to a highly select and exclusive set of treatments. To emphasise at the risk of repetition, no treatment accorded this status has ever been refused final FDA approval!
- There is presently no effective alternative treatment.
- Commercialisation (along with substantial revenue and profits) is expected next year.
- CFS treatment is potentially a multi-billion dollar market.
- The company is known to be working on a significant licensing agreement relating to Hepatitis B and C treatments, itself a potential multi-billion dollar market,
- Short sellers are finding themselves between a rock and a hard place and are trying to manipulate investors and the media by issuing misleading statements in order to trigger a sell-off and turn a quick profit.

Conclusion:

This time the short sellers have obviously not done their homework. Share price declines will be the result of uninformed panic selling triggered by a desperate bear raid in the face of an impending short squeeze. Should the current bear raid on Hemispher_x result in sharp share price declines, we recommend that this opportunity will be used by new investors to buy shares and for existing investors to increase their holdings. We reiterate our Strong Buy recommendation with a two-year price target of US\$ 50.

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