

11 August 2010

Phosphagenics (POH)

Reprofiling a failed obesity drug

Analyst

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Authorisation

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Recommendation

Spec Buy

Price

\$0.09

Target (12 months)

\$0.40

Phosphagenics (POH) has been working on adapting its TPM transdermal drug delivery technology to delivery of AOD9604, an anti-fat peptide. We think success in this effort can unlock an OTC market worth hundreds of millions pa by early 2012, with considerable upside for Phosphagenics given the lack of clinically validated competition. Speculative Buy recommendation and 40 cent target price maintained.

Expected Return

Capital growth **344%**

Dividend yield **0%**

Total expected return **344%**

Company Data & Ratios

Enterprise value **\$55.7m**

Market cap **\$66.6m**

Issued capital **739.7m**

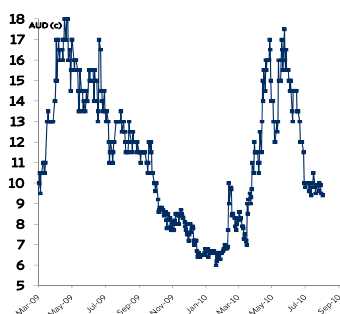
Free float **100%**

12 month price range
\$0.05-\$0.18

GICS sector

Healthcare Equipment and Services

Absolute Price



SOURCE: IRESS

NOTE: In April 2010 Southern Cross Equities was appointed a corporate advisor of POH, with a grant of options associated with this arrangement. For more details see the last page of this note.

Transdermal drug delivery technology that works

Over the last six years POH has demonstrated clinically that its TPM technology, based on phosphorylated Vitamin E, can transdermally deliver therapeutic doses of drugs that until now have had no transdermal option. While the major focus of POH is on using this technology to develop the world's first patch for oxycodone, there is also potential in a project to develop an OTC anti-fat cream using AOD9604, a failed anti-obesity drug.

POH can fix AOD9604's delivery issues

While AOD9604 performed poorly in the clinic as an anti-obesity therapeutic, POH believes that oral delivery of the drug was the key issue rather than the drug's efficacy. Consequently the company has licensed compound and is seeking to develop it as topical anti-fat cream delivered using TPM.

AOD9604 represents a near-term payoff

With overweight and obesity representing a rising global epidemic, there is strong demand for all sorts of products, prescription and over-the-counter, that can combat excess fat tissue. We think that POH's anti-fat cream can be taken to market in early 2012 and can tap into a global market worth potentially hundreds of millions of dollars. We expect the development costs to be only \$100,000 and the regulatory issues to be minimal. With Phosphagenics having disclosed no data on its work AOD9604, we choose not to include any value for AOD9604 in our overall valuation of the stock at this stage. However, a tentative DCF indicates some upside in the order of 8 to 21 cents per share.

Target price 40 cents attainable with clinical data

We value POH at 41 cents base case and 81 cents optimistic case using a probability-weighted DCF valuation. As the near-term nature of TPM becomes apparent, helped by the emergence of further clinical and pre-clinical data on various products including AOD9604, we expect POH to be re-rated by the market.

POH – Reprofileing a failed obesity drug

When we initiated coverage on Phosphagenics on 12 May¹ we took only cursory notice of the company's AOD9604 project, which it has been working on since August 2009. Phosphagenics is exploring the potential to reprofile AOD9604, a failed anti-obesity drug, as an over-the-counter cosmeceutical that can reduce cellulite and subcutaneous fat. The company hopes to bring this product to the market early in 2011. In this note we look at the commercial potential of the AOD9604 project, which suggests further upside in the POH share price beyond our current 41 cents base case / 81 cents optimistic case probability-weighted DCF valuation.

Some people still think AOD9604 has value

What is AOD9604? AOD9604 is a 16 amino acid peptide derived from human growth hormone² that has shown some clinical efficacy as an anti-obesity agent. The drug was developed, from its early stages in the late 1990s through to a Phase IIb clinical failure in early 2007, by the biotech company Metabolic Pharmaceuticals. Metabolic raised around A\$80m in equity capital between IPO and late 2006 using AOD9604 as its lead compound, and it is estimated that around A\$50m was spent directly on the drug before abandonment of the clinical programme. Metabolic subsequently changed its name to Calzada³ and sought new opportunities, but retained control over the AOD9604 intellectual property until it sold these assets to another listed company called ATOS Wellness⁴ in July 2010. Phosphagenics optioned a license on this IP as it related to an anti-fat cosmeceutical in August 2009, and if that option is exercised it will be liable to pay the IP owner – now ATOS Wellness – ‘an undisclosed royalty on future sales of product’. The project arose in part because Esra Ogru, POH's joint CEO, used to work at Metabolic prior to joining POH⁵.

AOD9604 failed as an anti-obesity drug. In a 536-patient Phase IIb randomised, placebo-controlled trial of AOD9604, results of which were reported in February 2007, the drug:

- failed to achieve a statistically significant weight loss in any dosage group after either 12 weeks or 24 weeks of treatment; and
- showed precious little overall weight loss - even after allowing for the formal diet and exercise programme that had been put in place for this trial (and had not been for previous trials) the weight-loss results were sparse, with less than 1 kg drop across all dose groups⁶ at both measurement points.

...but may work as an anti-cellulite cream. This begs the question as to why Phosphagenics would want to get involved in AOD9604. There are three basic reasons:

¹ In a note headlined 'Unique Drug Delivery Technology'. The stock at the time was 12.5 cents.

² AOD9604 was invented around 1997 in the laboratory of Professor Frank Ng, a biochemist at Monash University in Melbourne who had been studying human growth hormone since the 1960s. In the 1980s Ng et. al. found that a 15-amino acid fragment at one end of the hormone could produce marked weight loss in animal models of obesity. Ng's lab subsequently constructed a number of analogues of the fragment, and picked out the 16 amino acid peptide AOD9604 as the most effective (The AOD stood for 'Advanced Obesity Drug'). *In vitro* and *in vivo* tests on AOD9604 showed that the drug retained all of the fat metabolic properties of growth hormone, without any of the hormone's undesirable effects.

³ ASX: CXD, www.calzada.com.au.

⁴ ASX: ATW

⁵ Esra joined POH in 2001, so had been actively involved in AOD9604 only at its very early clinical stages, before the results of the various Phase IIa trials were available in 2002.

⁶ With the average American adult standing around 169.5 centimetres, such an adult with a BMI of 30, the minimum entry point for the AOD9604 trial, would weigh 87 kilograms, making a 1kg weight loss a drop of only 1.1% of body weight. To be at the top end of 'normal' such an individual needs to lose around 15 kilograms.

- 1) The Phase IIb trial showed that the drug had some efficacy in females who didn't diet or exercise well, suggesting that AOD9604's fat-burning capability was real;
- 2) There is pre-clinical evidence that AOD9604 works well in regulating fat metabolism when it has reached the sites of fat storage;
- 3) Esra Ogru and her colleagues believe that AOD9604, being a peptide derived from a hormone, could have bioavailability/absorption issues that could effect that drug's efficacy, and that TPM can fix this delivery problem by avoiding the gut altogether.

Let's consider each of the above points in turn:

Why Phosphagenics believes AOD9604 can work as anti anti-cellulite cream

AOD9604 did burn fat for at least one trial group. When AOD9604's Phase IIb investigators looked at females in the trial with 'low response to the diet and exercise before randomisation'⁷ the result was 'similar effect sizes to those reported in the previous trial', that trial being a Phase IIb trial which had shown good performance for low doses of the drug. It's well known that physical exercise results in the body producing growth hormone⁸, and that would potentially explain why AOD9604, as a growth hormone derivative, failed to produce much response across most treatment groups where exercise compliance was better – the drug didn't 'synergise' an exercise programme in terms of overall body weight, as Metabolic had hoped prior to initiating the trial. It did, however, burn fat⁹. We think this data partly confirmed what Metabolic had observed in February 2002 when it reported results of its first Phase IIa of AOD9604, where patients registered an increase in fat breakdown 2 hours after AOD9604 dosing compared to placebo. Patients over 35 showing a 25% increase in blood levels of non-esterified fatty acids (NEFA) compared to placebo, with a p value of less than 0.01. This trial, in 23 obese subjects, saw AOD9604 administered intravenously.

***In vivo* data suggests that AOD9604 can burn fat when it reaches the sites of fat storage.** Two papers from scientists working with Metabolic in Frank Ng's lab established *in vivo* evidence that AOD9604 could stimulate lipolysis:

- **The 2000 *Hormone Research*¹⁰ paper.** This paper looked at oral treatment of obese rats with AOD9604, where the drug reduced weight gain over a 19 day period by over 50% compared to the controls. When the adipose tissues of the rats were studied the scientists found 'an increase in lipolytic activity', that is, it was fat and not some other tissue that was burned.
- **The 2001 *Endocrinology*¹¹ paper.** This paper identified a potential mechanism of action for AOD9604. The drug, when administered to ob/ob mice intraperitoneally over a 14 day period, not only saw marked weight losses in the mice, but also a noticeable increase in the level of expression of B₃ adrenergic receptors whose major function of these receptors is enhancement of lipolysis.

⁷ The politically correct way of describing non-compliers to the diet and exercise regime involved in the trial.

⁸ See, for example, Godfrey et. al., *Sports Med.* 2003;33(8):599-613.

⁹ While it's not clear why non-exercising women enjoyed a good response whereas non-exercising men didn't, one possible explanation is that obese women may have less growth hormone in their systems, on average, than obese men.

¹⁰ See Ng et. al., *Metabolic studies of a synthetic lipolytic domain (AOD9604) of human growth hormone*, *Horm Res.* 2000;53(6):274-8.

¹¹ See Heffernan et. al., *The effects of human GH and its lipolytic fragment (AOD9604) on lipid metabolism following chronic treatment in obese mice and B₃-AR knock-out mice*, *Endocrinology.* 2001 Dec;142(12):5182-9. Esra Ogru was a co-author on this paper. The paper is available in full at <http://endo.endojournals.org/cgi/content/full/142/12/5182>.

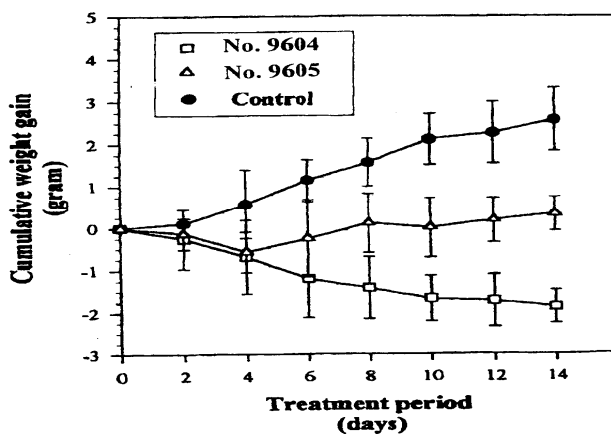
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Oral delivery may have affected AOD9604's performance

AOD9604's delivery could have been the key issue. POH's basic thinking on AOD9604 is that the drug failed because it was made orally available, which likely reduced bioavailability and also potentially resulted in protein denaturation in the gastrointestinal tract, which would have reduced the drug's activity.

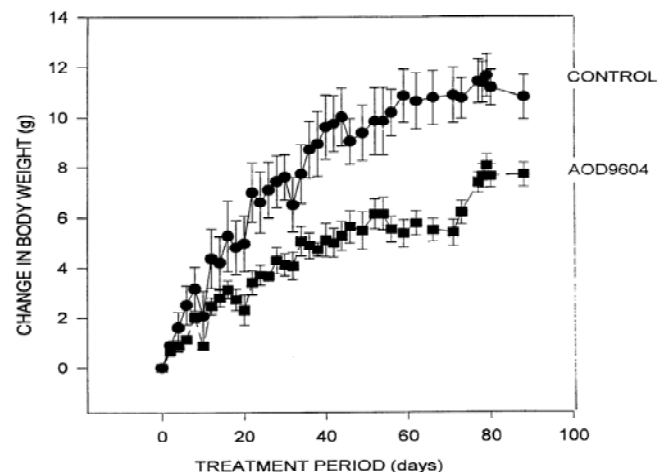
- *The molecule was too unwieldy to be a pill* - At a molecular weight of 1,815 daltons, AOD9604 is a large drug, around five or six times the size of a typical small molecule. Drugs much smaller have low oral bioavailability due to difficulty in getting through the gut wall. For example, leuprolide is a synthetic nine amino acid peptide with a 1,200 dalton molecular weight used in the treatment of prostate cancer in men and endometriosis in women. That drug has virtually no oral bioavailability and has to be delivered through injectable, injectable depot or subcutaneous implant formats. Even if AOD9604 was only a small peptide, it would still be susceptible to enzymatic degradation in the gut, being derived as it is from a naturally occurring protein¹².
- *Some drug, but probably not enough, got through* - For AOD9604, large molecule size wouldn't have reduced bioavailability to zero, and the use of polyethylene glycol as an excipient may have increased bioavailability slightly¹³, however there is the distinct possibility that not enough of the drug got through the gastrointestinal tract to make a therapeutic difference.
- *There is evidence that injecting the drug works better* - Looking at the charts which Ng et al. disclosed on AOD9604's activity in WO 99/12969 (the basic patent application for the drug), it appears that intraperitoneal injections of the drug were more effective than oral gavage, with injections showing weight losses, and oral gavage showing merely slowing of weight gain¹⁴.
- POH would further argue that if insulin, three times the size of AOD9604, can be delivered transdermally via TPM, then successful transdermal delivery of AOD9604 is not a problem¹⁵.

Figure 1 - Performance of injected AOD9604 in ob/ob mice



SOURCE: WO 99/12969, FIGURE 12

Figure 2 - Performance of oral AOD9604 in ob/ob mice



SOURCE: WO 99/12969, FIGURE 13

¹² Some synthetic peptides can avoid enzymatic degradation in the gut, whereas natural peptides generally cannot.

¹³ The two excipients in the AOD9604 pill were the sugar mannitol and a polyethylene glycol formulation called PEG 3550.

¹⁴ Intraperitoneal delivery would be subject to potential hepatic first-pass losses, but not intestinal first-pass losses, so bioavailability of AOD9604 would greatly increase under this model.

¹⁵ Chinese-sourced AOD9604 is apparently being sold around the world by firms such as Peptide Warehouse (see <http://peptidewarehouse.com>), in spite of the patents granted or pending, for use by bodybuilders who, by injecting the product, receive adequately sized doses to burn fat. See *Bulk up on this fat-fighting firm* by Tim Boreham, *The Australian*, 2/3/2010. We came across no online evidence of bodybuilders advocating AOD9604.

The time to market for Phosphagenics' cream is fairly short

POH believes that, should the research be successful, a commercial cosmetic cream can be launched by the first half of calendar 2011. The development costs of this product will likely be mild – only \$100,000 for pre-clinicals and a short clinical trial before product release.

Human testing is starting on an AOD9604 anti-fat cream

What has been achieved to date. In order to get an AOD9604 cream ready for the market, POH has achieved the following:

- Sourced the AOD9604 peptide from a low-cost Chinese manufacturer;
- Formulated the peptide into a TPM cream;
- Established that AOD9604 is compatible with TPM; and
- Fielded numerous requests from potential commercial and scientific partners for information on product development.

What is being done. Currently POH is working on:

- Franz cell testing¹⁶ to show that the peptide is deliverable across the skin. Human skin is being used for these experiments;
- Optimisation of active concentration levels;
- Development of a bioanalytical assay to detect if the peptide has made it through human tissue – we understand that the POH team has made significant progress towards this; and
- Protocols for 'cosmetic testing' of the cream¹⁷ - POH intend to start recruitment for cosmetic testing around November 2010.

We think the cosmetic testing will be completed before the end of 2011, allowing the product to be brought to market early in 2012 either by Phosphagenics directly, or with partners in the cosmetics industry.

Tapping a huge market opportunity

Around 68% of American adults are overweight and 34% are obese¹⁸, and while the US sits at the extreme most Western countries are experiencing an epidemic in which more adults are moving into the overweight or obese categories. This has fuelled significant markets for anti-fat products. Consider two examples:

A lot of money gets spent on anti-fat creams

The existing cosmetic market is significant. Around US\$3bn pa is spent worldwide on cosmetic products that are either 'firming' or 'anti-cellulite' in nature. The anti-cellulite products generally come with little, if any, studies demonstrating efficacy¹⁹. While the vast majority of this is probably firming creams it indicates the kind of potential market for a well-validated anti-cellulite cream which, by burning fat, would help to smooth out wrinkled skin.

Cosmetic surgery also indicates the market potential. The market for cosmetic procedures related to excess fat, while declining over the last couple of years in the US, also provides a good indicator of the size of the opportunity. In 2009 around US\$600m was spent on suction-assisted lipoplasty. In a good year (ie one with less unemployment than currently) the lipoplasty market is a billion dollar opportunity.

¹⁶ This involves running TPM/AUD9604 through a Franz Cell, an apparatus consisting of two primary chambers separated by human skin as a membrane. The peptide is applied to the membrane via the top chamber. The bottom chamber contains fluid from which samples are taken at regular intervals for analysis. This testing determines the amount of active that has permeated the membrane at various time points.

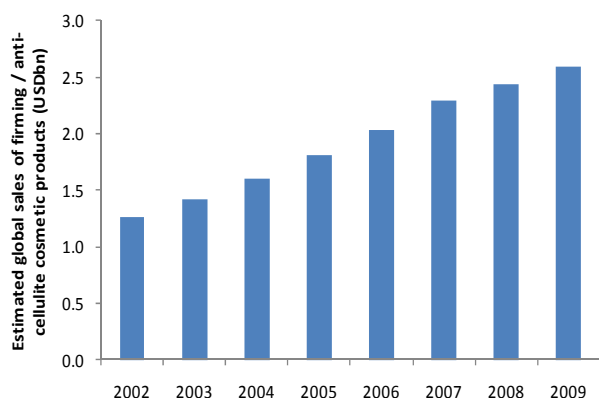
¹⁷ Animal testing of cosmetics is generally frowned on today. A 2005 MORI poll in the UK commissioned by the Coalition for Medical Progress, a pro-animal testing organisation, found that only 10% of those questioned supported animal testing for cosmetics.

¹⁸ Source: CDC NHANES data.

¹⁹ Notable products in the space include Nivea Good-Bye Cellulite and L'Oreal Paris Sublime Slim. Generally anti-cellulite creams have natural actives such as caffeine, ginkgo biloba or ivy, or amino acids such as L-Carnitine, where the compound in question has some known lipolytic properties.

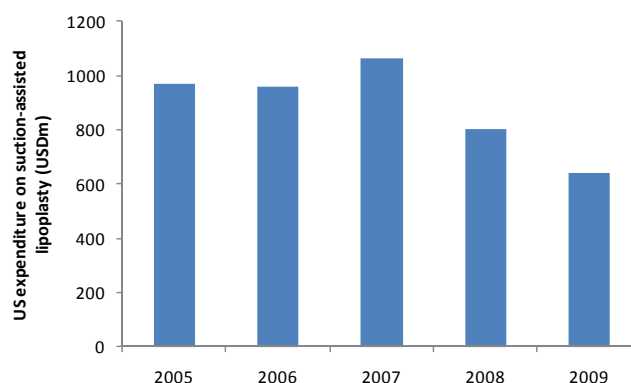
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Figure 3 - The market for 'firming' and 'anti-cellulite cosmetics' is growing



SOURCE: SOUTHERN CROSS EQUITIES ESTIMATES

Figure 4 - US\$600m was spent on suction-assisted lipoplasty in the US in 2009



SOURCE: AMERICAN SOCIETY FOR AESTHETIC PLASTIC SURGERY

Valuing the AOD9604 project

With Phosphagenics having disclosed no data on the efficacy of its proposed TPM/AOD9604 product, we choose not to include any value for AOD9604 in our overall valuation of the stock at this stage. However, a tentative DCF indicates some upside. We assume:

- Base case – A fourteen year patent life²⁰, a royalty to Phosphagenics of 15%, peak sales growth in year 3, global sales that year of US\$200m, sales growth thereafter of 5%; and
- Optimistic case – A fourteen year patent life, a royalty to Phosphagenics of 25%, peak sales growth in year 3, sales that year of US\$300m, 5% sales growth thereafter.

In each case we assume that a royalty to ATOS can be negotiated to be paid by the licensee without recourse to payments made to Phosphagenics, so that it is not a factor in valuing cash flows to Phosphagenics. Discounting those cash flows at 25% and using a 30% tax rate indicates a potential valuation for AOD9604 of 8 cents to 21 cents per share.

Figure 5 - A tentative valuation of AOD9604

	Base case	Optimistic case
NPV (USDm)	69.8	174.6
NPV (AUDm)	76.0	190.0
NPV per diluted share (AUD cents)	8.4	21.0
Fully diluted shares on issue ²¹	903.4	

SOURCE: SOUTHERN CROSS EQUITIES ESTIMATES

AOD9604 could be used to fund oxycodone. This kind of valuation suggests the potential for Phosphagenics to fund its pivotal trial of TPM/oxycodone and other projects through sale of the project to the right commercial partner.

²⁰ Basic patent protection of AOD9604 runs to roughly 2017. We assume that POH can file for patent protection of its TPM/ AOD9604 combination.

²¹ As per our 12 May assumption.

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Glossary

Adipose tissue – Fat tissue ('adeps' is Greek for fat)

AOD9604 – A peptide drug originally developed for the treatment of obesity. The drug is a modified peptide fragment of Human Growth Hormone. AOD stands for 'Advanced Obesity Drug'.

Amino acid - The building blocks of proteins. A peptide is a string of amino acids and a peptide or several peptides together makes up a protein.

Analogues – Chemical compounds that are based on a known substance but where various elements of the original compound have been changed. Scientists often create analogues of known compounds when looking for new drugs that have similar properties to the compound but are better as drugs.

B₃ adrenergic receptors – Receptors located mainly in adipose tissue involved in the regulation of lipolysis.

Bioavailability – The quantity of a drug that is able to make it to its target once inside the body. High bioavailability is an important component in a drug's prospects for commercial success. High oral bioavailability is even more desirable because then the drug can be administered in pill form. Some drugs have high bioavailability when injected intravenously but low bioavailability orally.

Cellulite - The dimples and bumps in the skin, usually around the thighs and buttocks, caused when the natural structure of the skin is stretched by fat tissue.

C-terminal – The right hand side of an amino acid sequence. AOD960-4 comes from the C terminal of Human Growth Hormone.

Dalton – See molecular weight.

Excipient – An inert substance used to prepare a drug for administration rather than being an active part of the drug itself.

Gavage – Force feeding through a tube inserted through the mouth or nose into the stomach.

Growth hormone – A hormone naturally synthesised by the body to stimulates growth and cell reproduction. AOD9604 is a modified peptide fragment of human Growth Hormone.

Hormone – A protein that serves as chemical messenger from one cell or group of cells to another.

Intraperitoneal – Injections into the peritoneum, the serous membrane that forms the lining of the abdominal cavity.

In vitro – Testing in the test tube.

In vivo – Testing in animal models.

Lipolysis – Breakdown of fat tissue.

Molecular weight – The size of a drug molecule, the standard unit of measurement of which is the dalton.

Non-Esterified Fatty Acids – Fatty acids whose blood levels increase during the breakdown of fats in the body.

Ob/Ob – A mouse model of obesity based on a gene called Ob.

Obesity – A state where a person's body mass index (BMI) is 30 or more, BMI being one's weight in kilograms divided by the square of one's height in metres. Obesity is a chronic health problem in the Western world, it being estimated that perhaps 4% of the world's population suffers from a severe weight problem.

Peptide – A string of amino acids. A protein is simply a structured collection of

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peptides.

Phase II – A clinical trial to test the efficacy of a drug in a small number of patients.

Polyethylene glycol – A material often used as an excipient for drug delivery.

Pre-clinical – The stage of a drug's development in which a candidate drug has been selected and it is being tested for its safety ahead of human trials.

Proteins – A class of fairly common molecules in the living things that includes antibodies and enzymes. Protein-based drugs have a high molecular weight compared to small molecules. A hormone is a protein.

p-value – A measure of statistical significance. Generally a p-value below 0.05 is considered statistically significant.

Reprofiling – The process of taking a drug that has failed in one indication and retrialling it in another where it has shown promise.

Small molecules – Drugs that have a low molecular weight, making them easier to penetrate cell membranes and the blood-brain barrier. Protein drugs are not small molecules.

Statistical significance – A statistic that is considered by statisticians to be unlikely to be the product of chance. Traditionally statistical significance is measured by a 'p value' of less than 0.05.

Subcutaneous – Under the subcutis, that is, the layer of skin that follows the outermost layers, the epidermis and the dermis.

AOD9604-related patents and patent applications

- 1 **Treatment of obesity**, U.S Patent 5,869,452, priority date 15 November 1994. Invented by Frank Ng, Siria Natera and Woei-Jia Jiang and applied for by Monash University. U.S. patent 6,335,319 is a divisional of this patent.
- 2 **Treatment of obesity**, WO 99/12969, priority date 13 November 1997. Invented by Frank Ng and Woei-Jia Jiang and applied for by Metabolic Pharmaceuticals. Granted in the U.S. as Patent No. 6,737,407.
- 3 **Product and method for control of obesity**, WO 01/33977, priority date 5 November 1999. Invented by Chris Belyea, Paul Vaughan and Frank Ng and applied for by Metabolic Pharmaceuticals. Granted in the U.S. as Patent No. 7,098,029.
- 4 **Product and method for control of obesity**, WO 02/18436, priority date 1 September 2000. Invented by Chris Belyea, Roger Summers and Mark Heffernan and applied for by Metabolic Pharmaceuticals.
- 5 **Insulin potentiating peptides**, WO 01/72770, priority date 31 March 2000. Invented by Frank Ng and Woei-Jia Jiang and applied for by Metabolic Pharmaceuticals.
- 6 **Method for control of depression using C-terminal Growth Hormone (GH) fragment**, WO 03/092725, priority date 3 May 2002. Invented by Gary Wittert and Chris Belyea and applied for by Metabolic Pharmaceuticals²².
- 7 **Methods for Preventing or Treating Bone Disorders**, WO 2005/105132, priority date 4 May 2004. Invented by Evert Vos and applied for by Metabolic Pharmaceuticals.

²² In the Phase IIa trials of AOD9604 clinical investigators noted a feeling of euphoria in several of the trial participants, potentially indicating that the drug had anti-depressant properties.

Phosphagenics (POH)

Phosphagenics

COMPANY DESCRIPTION

The Melbourne-based Phosphagenics (POH) is an early stage biotechnology company commercialising a drug delivery technology known as TPM, which allows drugs that previously could only be injected to be delivered transdermally in gel or patch form. We see potential for TPM to be licensed for use in delivering the analgesic drug oxycodone while a number of other drugs, including insulin, the acne drug tretinoin and the anti-inflammatory diclofenac, have also shown promise using TPM.

INVESTMENT STRATEGY

We see a payoff to shareholders arising from favourable clinical outcomes, followed by a licensing of the technology to pharmaceutical and biotechnology companies looking to expand their product range. We also see POH benefiting from improved sentiment towards Australian biotech stocks. The end of the Global Financial Crisis came at a time when many Australian biotech companies had reached late stage maturity.

VALUATION

We value POH at 41 cents base case and 81 cents optimistic case using a probability-weighted DCF approach. Our target price of 40 cents sits at our base case valuation. We assume that POH can be re-rated by the market as the near-term nature of TPM becomes apparent, helped by the further clinical and pre-clinical data.

RISKS

We see the main risk in POH as being clinical risk – ie that products fail to perform in human trials. Another major risk facing the company is that prospective licensing partners may drive too hard a bargain for POH shareholders to enjoy a strong return. A third significant risk is burn rate. At 31 December 2009 POH had \$10.9m cash but has burned around \$700,000 per month since early 2004 when it began to focus solely on development of TPM. The company has raised \$51m in equity capital over the last six years. It may have to make further capital raisings to fund its burn rate until the clinical programmes yield licensable products.

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Recommendation structure

Spec Buy: Expect >30% total return on a 12 month view but carries significantly higher risk than its sector

Buy: Expect >15% total return on a 12 month view

Accumulate: Expect total return between 0% and +15% on a 12 month view

Reduce: Expect -15% and 0% total return on a 12 month view

Sell: Expect <-15% total return on a 12 month view

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Southern Cross Equities Ltd and its associates hold 276,000 shares in POH as at the date of this report. This position is subject to change without notice. In April 2010 Southern Cross Equities was appointed a corporate advisor to POH. As part of this arrangement Southern Cross has been granted 5 million options exercisable at 14.2 cents expiring 31/3/2013. These options vest immediately. In the event that the corporate advisory role continues, being terminatable by POH at any time, Southern Cross Equities may potentially be granted another 5 million options in April 2011 and 5 million in April 2012 with the same exercise price and expiry date. In the event that POH stock trades at or above 50 cents for 20 consecutive business days all options shall vest immediately.



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