

THE WALL STREET TRANSCRIPT

Questioning Market Leaders For Long Term Investors

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COMPANY INTERVIEW

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Edgemont Capital Partners, LP



DAVID K. BLUME is Managing Director of Edgemont Capital Partners, LP. He has spent his entire 15-year professional career in investment banking, focusing exclusively on health care for the past nine years. He has completed over 50 transactions, representing more than \$25 billion in value, including mergers and acquisitions, fairness opinions, partnerships, joint ventures, public and private equity and debt securities issuance and general strategy and financial advisory services. Mr. Blume's healthcare experience covers a broad range of industry sectors, including pharmaceuticals (large capitalization and specialty) pharmaceutical outsourcing (contract research organizations and pharmaceutical sales and marketing companies) healthcare

information technology, distribution, medical devices, diagnostic equipment, managed care, home healthcare, institutional pharmacy and pharmaceutical benefit management. His clients have ranged in size from startups to Fortune 50 companies. Mr. Blume's transaction experience includes the sell-side representation in the largest CRO transaction to date and buy-side representation in one of the largest non-pharmaceutical healthcare transactions of all time. Prior to co-founding Edgemont Capital Partners, he was a Senior Vice President in Lehman Brothers' Healthcare Group where he led the coverage teams for specialty pharmaceuticals, pharmaceutical outsourcing and healthcare information technology. He joined Lehman Brothers from Bear, Stearns & Co., where he was a Managing Director. At Bear Stearns, he founded the firm's pharmaceutical outsourcing coverage team, which completed five transactions in its first 14 months. Mr. Blume joined Bear Stearns from Prudential Securities Inc. where he worked in the private equity and debt placement group. Prior to this, he was an Associate at Patricof & Co. Capital Corp. where he worked with venture capital-backed companies. He began his career as a Financial Analyst at Salomon Brothers Inc. He graduated from Haverford College with a Bachelor of Arts degree in Philosophy in 1988. Mr. Blume has prior entrepreneurial experience. In college he founded and managed Skeeter's Pizza, a student-operated pizza restaurant and delivery service. Skeeter's quickly became a school institution, delivering to college students on limited budgets. Skeeter's employed 45 students part-time each semester and helped finance his college living expenses. Skeeter's, now in its 17th year of operation, was financed 100% by Mr. Blume and he sold the business to the Haverford College Students Association upon his graduation. Mr. Blume is a Board member of the Rutgers University Venture Action Committee.

SECTOR – PHARMACEUTICALS

(RAJ203) TWST: Would you begin with a capsule summary of Edgemont Capital?

Mr. Blume: Edgemont Capital is a specialty healthcare investment banking advisory firm, focused predominately on the life sciences, working with companies that have either marketed products or products that are in the clinic. We define our clientele as product focused biotech companies through to specialty pharmaceutical marketing companies. We also work with a number of the services companies that have pharma-

ceutical companies as their customers as well, such as contract research organizations and contract sales and marketing companies.

We founded Edgemont about a year and a half ago because of the opportunity that we saw to help emerging and middle market companies in these industries that are not getting the attention from the larger Wall Street firms. Consolidation had eliminated a lot of the traditional middle market investment banking firms such as Montgomery Securities, Robertson Stephens and Hambrecht & Quist.

At Edgemont we essentially provide three categories of services. First, we're a licensed broker-dealer, helping companies raise capital in the private market, from mostly venture capital firms and some other institutional investors. Second, we provide mergers and acquisitions advisory services traditional to a smaller boutique firm. And then the third category of our business that's a little unique and an area that's very active for us is we work with companies around business development pharmaceutical product specific initiatives. For example, we act as an intermediary, advisory and facilitator for the in and out licensing of pharmaceutical products, helping people set up development and commercialization deals, selling NDAs outright or any of the business types of arrangements that are structured between companies around either marketed or pre-approval pharmaceutical products.

TWST: Have others moved into the same niche area that Edgemont is targeted at?

Mr. Blume: We've seen the emergence of a few specialty firms like ourselves focused on health care, but we don't really see anyone that is active around the product-specific business development kinds of initiatives that we work on. These other firms tend to do more traditional M&A advisory services only and perhaps some of them do also help people raise capital, although in this market that's not something that people are doing a lot of. In addition, most do not have the large investment bank experience that qualifies them to provide the full range of services that we offer.

TWST: What were companies doing over the past two years? Did that consolidation you described within the investment banking industry create pent-up demand or did it just mean people stopped doing what they wanted to do?

Mr. Blume: No, I think it's created a greater sense of need and urgency among some of

these firms to try to find advisors who can be helpful to them to advise on strategic initiatives, provide the valuation expertise and the transaction facilitation that a number of those banks used to provide. You see it starkly among the small cap public companies, a number of which have, as a result of this consolidation, lost so many banking relationships, which is evidenced by the fact that they have no research coverage, which is something that is very important for them. Now, while we're not in that line of business today, I think it is evidence of the crying need that these firms have for additional support. For public companies with market caps of \$100-\$200 million up to \$500 million to not have a single firm providing equity research cover is really astounding. I think it impacts on a significant number of companies these days, and given the overall conservative nature of the investor community today and reluctance to get into new names without having an advocate or two on your behalf in communicating with these constituencies, I think is a real handicap.

TWST: Have you been able to breach that divide?

Mr. Blume: I think that we are able to address it in terms of providing quality banking advisory services. As I said, we're not really in the research part of the business currently, but what it has done I think is highlight for us that these firms have a need for help and I think that they are open to working with firms that have good ideas, that have smart people who are committed to helping them further their business initiatives and that they are open to dialoguing with firms, such as Edgemont, that can add value. We receive a very warm reception pretty much across the board in approaching these companies and find that we're able to engage in a healthy dialogue by showing up with ideas that can potentially add value for these firms.

TWST: It would seem that given that environment you also can be very selective in whom you include under the Edgemont umbrella. What are you using as your current criteria?

Mr. Blume: We look for companies that offer one or both of the following characteristics: There are companies that are bringing products through the clinical development that we think will have a significant impact upon approval in the market that they are addressing, whether it's reformulations of existing compounds or new chemical entities altogether. We look for companies that have innovation as a focus. On the other hand, we also look for companies that have a commercialization capability that makes them somewhat unique.

One of the attractions to us of the specialty pharmaceutical sector is the good opportunity and the compelling business model that's been demonstrated by a significant number of companies in marketing products to certain physician specialties that you can reach with a modest size sales force and a smaller internal organization and still be very effective and compete alongside or heads up against some of the largest pharmaceutical companies within those specialties. And, in the best of all worlds, having both capabilities makes for a fairly formidable company in this sector. So those are some of the key criteria that we look for in the companies that we seek out as clients.

TWST: What is the special expertise or the ways in which you've changed the analysis that you have to do in valuing companies?

Mr. Blume: The most dramatic change is, over the last several years up until to about 18 to 24 months ago, there was an arbitrage that was very much in favor of selling equity versus looking at the sum of your parts, or said another way, the value of your portfolio and pipeline together probably was valued at a discount to your valuation on

an overall equity basis. I think that, given that we are in a very illiquid capital markets environment, the arbitrage has swung entirely in the other direction. We're now in a situation where values of products, portfolios and pipelines exceed where the overall equity values that are being accorded these firms. So where that impacts on valuation is being able to assess what is the value of the marketed products as well as the pre-approval products and the intellectual property that a number of our clients have, as well as perhaps the value of their commercialization capabilities and expertise and being able to look at those parts in total, with respect to where the equity valuations are for companies in the category.

TWST: That said, it seems that the compass has been pointing to platform companies which were in vogue and perhaps even some of the tools and medical device companies more so than the true development of discovery companies.

Mr. Blume: I think you had a lot of excitement around a number of those companies as part of the heady equity capital markets environment than public market valuations of a couple of years past. I think now there is much more comfort with valuations of companies that have products on the market or late stage products. We've seen a real premium change toward an emphasis on companies that have products and that people are far less comfortable with development risk and FDA approval risk and, to some extent, even marketing risk than they were in the past. Things that are earlier stage such as raw discovery or even tools companies helping raw discovery have come under a lot of pressure and, as a result you've seen them turn toward big cap pharma again as a means to access capital and to sort of grow their businesses, whereas a couple of years ago the capital was available for them to try to go it alone.

TWST: How many total clients is Edgemont working with at this point? And are there any specific examples there as far as what you have provided in each of those three service areas that you could provide?

Mr. Blume: Last year we represented a Cromedica, one of the leading central nervous system CNS CROs in the world, in a sale to PRA International, which is the largest privately held CRO in the world today and probably the third or fourth largest overall. And that would be representative of our M&A advisory services. Also last year we represented Hollister Steir Laboratories in the sale of one of their pharmaceutical products, TwinJect, which is a product that will compete with the Epi-Pen, an auto injector of epinephrine for anaphylactic shock, when it's approved. We represented them in a divestiture of that product line, as well as some ongoing business relationships with the party that acquired TwinJect. That would be representative of some of our product specific business development services.

We were recently licensed by the NASD as a member broker-dealer firm and we are actually in the process of ramping up on our first private placement assignment. Currently we are working on four mandated assignments and, as I have said, we have completed the couple of transactions that I mentioned earlier. By the end of 2003, I estimate we will have completed six transactions. We look to work on anywhere between three and six transactions at any given time.

TWST: Touching briefly on a conference topic itself, can there be a viable rapid growth company in that universe you work with?

Mr. Blume: Absolutely. And I think the quickest way to that path is obviously having in your portfolio or the marketing rights for a product with high growth potential. If you are able to

bring a truly differentiated product to the market, particularly in the specialty world, and are able to reach the key influencing physician prescribers quickly, you can achieve rapid growth. Nothing accelerates the growth of these companies more quickly than building a portfolio of products to a given specialty. Once you have a commercialization infrastructure set up and are detailing a product to a physician, the marginal profitability of adding yet a second or third product to that commercialization capability is enormous because there are very little marginal incremental marketing expenses required to bring additional products into your sales organization.

TWST: The sales and marketing aspect then is critical, and most companies in this space generally are more science than business oriented. What should be brought to the table for most of these companies on that business side?

Mr. Blume: I think those companies need to make a determination at some point whether or not they believe that it makes sense for them to have the commercialization capability or they should partner to achieve it. What's changed dramatically in my opinion over the last number of years is that the number of potential partners has increased several-fold. Going back five or 10 years, if you had developed a product, there was a pretty short list of people that you could approach to potentially partner with and commercialize your product, and they usually had all the leverage. As a result, people got stuck doing fairly traditional deals where you got a little bit of an expense reimbursement and maybe some milestone payments and gave the majority if not the lion's share of the economics to your partner. In the current environment, there are a large enough number of specialty firms out there calling on the requisite physician universe that it makes for more creative kinds of

structures allowing the innovator company to capture a greater proportion of the overall economics.

So companies that seem primarily as drug developers, have, in this environment, more leverage given the premium that's been placed on products to cut a more favorable economic deal for themselves. So they are able to approach it in much more of a competitive fashion. And, if you will, that is exactly what we help these companies do is create a much more efficient market for partnering their products.

Historically, if there were a limited number of people you could approach, you went and you hoped you could do the best deal with one of them and whatever terms they put on the table was probably as good as you were going to get. What we help companies do is approach this process much in the same way they would conduct an overall M&A divestiture assignment which is that we help put together an information package, approach a universe of people that we think are good quality potential partners and essentially attempt to establish an auction process, if you will, the opportunity to create a "market" whereby having a large number of potential parties evaluate the opportunity sets up a competitive dynamic that allows our client to optimize the terms that they are able to achieve at the end of the process.

TWST: And yet you mentioned that the key was getting the attention of the practitioner, getting a foot in the door. Has anyone figured out how to solve the problem of getting your product into the practitioner's hands so that he actually then uses it, prescribes it, recommends it?

Mr. Blume: I think that the specialty companies that are successful have found a number of creative ways to be effective in marketing products. Physician detailing has still predominately proven to be the most effective way of doing that. There is a lot of competition for physician time. A

number of the strategies that these firms use is to focus on specialties that haven't necessarily received as much volume of physician details historically and other creative strategies and techniques for getting visibility on the products. The advantage that they have is that their cost infrastructure is so much far lower than large pharma companies — in part because they don't invest in the same level of R&D down to the discovery level, but rather focus on reformulations and less costly R&D efforts. They don't have to achieve the same enormous level of revenues to make the returns that they target. Said a different way, for these companies, given their infrastructure, big product could be \$50 million or \$100 million in revenue, whereas for large cap pharma anything less than \$1 billion in revenue these days is considered small.

TWST: From the investor's point of view, what has changed as far as their parameters, the timeline to the exit point, the time involved in commercialization, the slope of the ramp-up of sales?

Mr. Blume: I think investors overall obviously are very conservative in the current environment. I think what goes hand in hand with that is a healthy dose of skepticism. And, as a result, companies that talk about timelines to FDA approval as being key milestones need to be cognizant of the fact that investors are going to discount those milestones and build in a healthy amount of cushion. Things that are earlier in the pipeline are being valued at a greater discount. I think investors want to see the companies meet the goals that they set for themselves as far as revenue and profit and earnings projections to build credibility and that hopefully translates into development pipeline credibility.

TWST: What are the sweet spots today? What are the exciting investment opportunities, if any, out there now?

Mr. Blume: I think a lot of the potential exciting upside opportunities are the resurgence of companies that fell off people's radar screens. There are a good number of companies in the sub-\$500 million market cap range that have very exciting products in development or that have recently started to market products. These products have terrific potential but, because these companies are under followed, investors have paid less attention to them.

I also think a number of these companies have lost credibility with investors because they set milestones or approvals were expected that didn't occur and once you lose that credibility it takes a long time and is very hard to regain it. I think a number of those companies have learned those lessons over the last few years. In several cases you've seen companies that have products that received non-approval letters or were on track to get not non-approval withdraw those products from the FDA, go back and redesign Phase III trials, put the products back into the clinic and either get them approved or get them back on track to be approved. I think there is the potential for healthy returns by revisiting a good number of these companies that fell out of favor with Wall Street over the last two to three years that are worth taking a good look at again.

TWST: What interest, if any, do you see in some of the international-based companies?

Mr. Blume: I think you're seeing several trends in Europe. One, over a very slow period of time, is a trend toward more pan-European coverage. You know, Europe much more than the US, has a number of mid-cap companies and then a large number of smaller, more regional or country focused companies. And I think you're seeing slowly through consolidation the emergence over time of companies that can cover all of Europe. A

lot of these companies do have products that have very long safety records in Europe and have potential use here in the US. And they increasingly are looking for US partners to help them get through the development process here in the US and then ultimately commercialize the products. These companies tend to be among the most conservative and slower moving that we see, so I think that will be a long process. But culling through the portfolios of European pharma today, I would expect to see a number of those products on the market in the US in the foreseeable future.

TWST: As a summary, what's the agenda for Edgemont? What would make the next 12 months a success from your perspective?

Mr. Blume: I think our goals are several-fold. One is we would like to expand our coverage and universe to include other areas in health care. Medical devices is an area that we're particularly focused on building and growing. I think we are going to look to add a small merchant banking fund to invest alongside of a number of the advisory assignments that we work on. One of the advantages we have is that we find a lot of exciting investment opportunities that we would like to be able to take advantage of as a principal, so that is another key growth objective of ours. And then finally we continue to be intrigued with offering more services to our clients, particularly around perhaps research and institutional selling capabilities. But again, given the current capital markets environment and an unclear regulatory picture on that front, I think that's a little more of a longer-term proposition for us.

Overall the opportunity is that health care is a fairly large industry and life sciences is significantly underserved by advisory firms such as ourselves. We can grow just addressing the need of our current coverage universe.

TWST: A lot has been said lately with the lack of distinction between the various operational units with investment bank firms that do give analysis and advice and firms that work with the companies directly. Do you feel that at your size, with the audience that you have, that any of those concerns are critical at this point? Do you feel you can walk the thin line that perhaps investors are anticipating?

Mr. Blume: For us the dramatic advantage is that we aren't in the investment advisory or investment research business today. And while we do think that there is an opportunity there, for us it's longer term. What allows us to offer today is completely non-conflicted quality advice without the potential for any sort of conflict emerging because we're not in the research business. And as a result we can give completely unbiased advice to our clients and don't have a lot of the conflicts that the larger investment banks have encountered and a number of which have gotten them into difficulty because of our focus only on the banking and corporate finance side of the business.

TWST: What have I overlooked?

Mr. Blume: The only other point that I would underscore is that the investment banking industry overall has suffered a little bit, I think, by focusing too much on building their own businesses. The advantage that I think a number of the smaller firms such as ourselves have and will continue to enjoy for some time to come is a pretty healthy universe of companies that are not being

adequately served by the larger investment banks; and the ability to give the best quality advice as a true advisor the way the banking business used to be in the past.

Investment banks, many of which are public and are trying to meet their own earnings objectives on a quarterly basis, always find themselves under pressure to try to get the transactions done that are in their best interest and to meet their timing objectives, and not always necessarily that are in the best interest of their clients. As a specialty private partnership such as ourselves, we have the ability to really act in concert with our clients as true partners and to give them the best advice. If that means telling clients to postpone a transaction until their business recovers, a major regulatory or clinical milestone is achieved or until the financing or deal climate is better, then we have the flexibility to do so and can really function in the role of the true advisor in the best sense of the word.

TWST: Thank you. (DWA)

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