

MARC SINATRA'S BIOGUIDE TO THE CRASH ... ER ... CORRECTION

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[MARC SINATRA'S BIOGUIDE: THE AUGUST 2007 CORRECTION](#)

So, Billy-Ray-Bob and Tammy-Faye-Sue default on their mortgage somewhere in Alabama and all of a sudden your Australian biotech portfolio has fallen by 30 percent. You didn't see that one coming, did you?

Surely their default should only affect the housing market, shouldn't it?

Unfortunately, the answer to that question is, no.

When we calculate the values of biotech stocks, we use a discount rate to convert all of the future cash flows we believe a company will make into one nice neat dollar figure that represents what we believe the true value of the stock to be.

This discount rate is determined by how risky the general market is and how leveraged the particular stock is to the market. The more risky the market, the higher the discount rate, the lower we value the stock.

The link between the US sub-prime mortgage market and our biotech's stocks is an indirect one that goes through general market risk.

The sub-prime market's poor performance makes the general market more risky, which, in turn, causes us to give our biotech stocks lower valuations.

Since biotech stocks are seen as being highly leveraged to the general market, they can cop a pretty good kicking, as they have today.

Most market commentators seem to think that the sub-prime issue won't be around for too long and that the bottom is not too far away.

Certainly, there do appear to be some very good buys emerging among the biotech's. Acrux, Alchemia, Avexa, Chemgenex, Circadian and Peptech all look to have been oversold.

Even poor old Metabolic could be worth a bit of a punt, given it is trading below its cash backing. That is, its cash holding of \$18 million is more than its current market capitalization of \$16 million.

At the end of the day smart investors buy shares when there is value and up to one quarter of the Biotech Daily Top 40 represent extremely good value and many others are looking like good buys.

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