

Arcus Biosciences

While early, '521 update encouraging as story expands beyond TIGIT; post 4Q takes

Reiterate Rating: NEUTRAL | PO: 24.00 USD | Price: 16.41 USD

Initial glimpse solid but many questions remain; PO to \$24

Arcus' 4Q results were mixed with revenues (+\$3M) ahead though EPS (-\$0.10) missed, but we suspect focus was squarely on HIF-2a inhibitor casdatifan (AB521). To be fair, we think the trends were encouraging albeit very early. Certainly, there was no apparent increase in on-target side effects, with grade 3+ rates of anemia (8%) and hypoxia (8%) seemingly lower than rival Merck's (covered by Geoff Meacham) Welireg (29% and 10%, respectively in LITESPARK-005. That said, how these AEs were distributed among Arcus' dose escalation cohorts was unclear, with implications regarding the dominator. And though the preliminary signals suggest casdatifan may have improved time-to-response in the ongoing dose expansion cohort, whether the PK/PD is meaningfully better was also less apparent to us—with the steady state AUC/ C_{max} looking more similar than not.

In our view, the Arcus narrative has been pivoting to the early pipeline after increasing concerns over TIGIT—including yet another delay in Roche's (Jain/Parry) SKY-01 readout, contributing to the stock's YTD pullback (RCUS -14% vs. NBI +1%). Today's data should give investors some reassurance heading into the expansion cohort update in 2H24, especially given casdatifan's intriguing upside, with Merck highlighting Welireg's blockbuster potential. Still, with uncertainties over whether cas' potentially greater activity can indeed produce significantly better outcomes and legitimate questions over the rest of the pipeline—i.e., quemliclustat ([our PDAC/ ARC-8 takes](#)) and etrumadenant ([our mCRPC/ ARC-6 takes](#))—less clear to us at this point is whether the portfolio absent much/ any contribution from domvanalimab can re-engage investors and/or drive a re-rating. Thus, while we wouldn't be surprised if RCUS shares trade with modest strength near-term, we continue to see the stock as fairly valued. Reiterate Neutral with key de-risking catalysts still a ways away, while lowering our PO from \$25 to \$24 after adjusting our model to account for the company's updated OpEx.

More early pipeline updates ahead as TIGIT ph 3s advance

Beyond the casdatifan dose expansion data, Arcus guided to readouts from ARC-9 (etruma in mCRC) and MORPHEUS-PDAC (etruma in PDAC with Roche) in 1H24 followed by an updates from EDGE-Gastric at ASCO ([our takeaways on initial update](#)). The team also expects STAR-221 (domvanalimab in upper GI) to complete enrollment this year—likely making it the company's first pivotal TIGIT study to readout.

Model Updates

Following today's update, we have adjusted our model and now forecast 2024e EPS of (\$3.40) vs. (\$2.94) prior. See page 3 for further details.

Estimates (Dec) (US\$)	2022A	2023A	2024E	2025E	2026E
EPS	(3.71)	(4.15)	(3.40)	(3.58)	(3.98)
EPS Change (YoY)	NM	-11.9%	18.1%	-5.3%	-11.2%
Consensus EPS (Bloomberg)			(3.42)	(4.08)	(3.32)
DPS	0	0	0	0	0
Valuation (Dec)					
Free Cash Flow Yield*	28.8%	-22.1%	6.9%	-25.2%	-28.1%

* For full definitions of *IQmethod*SM measures, see page 6.

21 February 2024

Equity

Key Changes

(US\$)	Previous	Current
Price Obj.	25.00	24.00
2024E Rev (m)	281.0	502.2
2025E Rev (m)	303.6	524.8
2026E Rev (m)	248.4	532.0
2024E EPS	-2.94	-3.40
2025E EPS	-3.79	-3.58
2026E EPS	-5.30	-3.98

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Stock Data

Price	16.41 USD
Price Objective	24.00 USD
Date Established	21-Feb-2024
Investment Opinion	C-2-9
52-Week Range	12.95 USD - 25.47 USD
Mkt Val (mn) / Shares Out (mn)	1,491 USD / 90.9
Free Float	53.7%
Average Daily Value (mn)	14.46 USD
BofA Ticker / Exchange	RCUS / NYS
Bloomberg / Reuters	RCUS US / RCUS.N
ROE (2024E)	-69.8%
Net Dbt to Eqty (Dec-2023A)	-27.5%
ESGMeter TM	Medium

ESGMeter is not indicative of a company's future stock price performance and is not an investment recommendation or rating. ESGMeter is independent of BofA Global Research's equity investment rating, volatility risk rating, income rating, and price objective for that company. For full details, refer to ["BofA ESGMeter Methodology"](#).

For a list of abbreviations, please see page 3

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Timestamp: 21 February 2024 09:59PM EST

iQprofileSM Arcus Biosciences

iQmethodSM – Bus Performance*

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Return on Capital Employed	-18.4%	-26.1%	-28.2%	-46.1%	-213.4%
Return on Equity	-35.6%	-54.9%	-69.8%	-152.3%	NM
Operating Margin	-250.0%	-290.6%	-56.7%	-57.4%	-63.1%
Free Cash Flow	429	(330)	103	(375)	(419)

iQmethodSM – Quality of Earnings*

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Cash Realization Ratio	NM	NM	NM	NM	NM
Asset Replacement Ratio	1.5x	3.0x	1.5x	1.6x	1.5x
Tax Rate	0.4%	2.0%	NM	NM	NM
Net Debt-to-Equity Ratio	-31.4%	-27.5%	-309.6%	-599.3%	NM
Interest Cover	NA	NA	NA	NA	NA

Income Statement Data (Dec)

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Sales	112	117	502	525	532
% Change	-70.7%	4.5%	329.2%	4.5%	1.4%
Gross Profit	112	117	502	525	532
% Change	-70.7%	4.5%	329.2%	4.5%	1.4%
EBITDA	(274)	(332)	(278)	(294)	(327)
% Change	NM	-21.2%	16.4%	-5.9%	-11.3%
Net Interest & Other Income	14	39	26	28	29
Net Income (Adjusted)	(267)	(307)	(258)	(274)	(307)
% Change	NM	-15.0%	15.8%	-6.0%	-12.0%

Free Cash Flow Data (Dec)

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Net Income from Cont Operations (GAAP)	(265)	(295)	(258)	(274)	(307)
Depreciation & Amortization	6	8	7	7	8
Change in Working Capital	623	(71)	281	(183)	(197)
Deferred Taxation Charge	NA	NA	NA	NA	NA
Other Adjustments, Net	74	52	84	86	89
Capital Expenditure	(9)	(24)	(11)	(12)	(13)
Free Cash Flow	429	-330	103	-375	-419
% Change	NM	NM	NM	NM	-11.6%
Share / Issue Repurchase	0	25	0	0	0
Cost of Dividends Paid	0	0	0	0	0
Change in Debt	0	0	0	0	0

Balance Sheet Data (Dec)

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Cash & Equivalents	206	127	862	487	68
Trade Receivables	NA	NA	NA	NA	NA
Other Current Assets	861	704	37	39	41
Property, Plant & Equipment	35	51	55	59	63
Other Non-Current Assets	243	216	132	129	133
Total Assets	1,345	1,098	1,086	714	305
Short-Term Debt	NA	NA	NA	NA	NA
Other Current Liabilities	193	184	364	377	386
Long-Term Debt	0	0	0	0	0
Other Non-Current Liabilities	495	449	444	256	66
Total Liabilities	688	633	808	633	452
Total Equity	657	462	278	81	(147)
Total Equity & Liabilities	1,345	1,095	1,086	714	305

* For full definitions of iQmethodSM measures, see page 6.

Company Sector

Biotechnology

Company Description

Arcus is a clinical stage, oncology-focused biopharma. The company is building a novel portfolio of cancer treatments it intends to formulate into novel combinations for the treatment of both solid tumors and hematological malignancies. Currently, six assets are in the clinic. The company has entered into a number of partnerships with established oncology players, which are providing financial, technical, and eventually, potentially commercial support.

Investment Rationale

Despite the breadth and depth of the late-stage pipeline, we are cautious on the near-term trial read-outs given questions we--and KOLs we spoke with--have about the clinical potential and market opportunities. Ahead of several de-risking events, we believe more compelling opportunities exist elsewhere in SMid-cap Biopharma

Stock Data

Average Daily Volume 881,047

Quarterly Earnings Estimates

	2023	2024
Q1	-1.09A	NA
Q2	-1.02A	NA
Q3	-0.95A	NA
Q4	-1.08A	NA

Model Updates

We've updated our Arcus model to reflect the 4Q print (see Exhibit 1 below).

Exhibit 1: RCUS Model Changes for 2024E and 2025E

We've provided our model changes for 2024e and 2025e below

	2024E		2025E	
\$ in millions (ex. per share items)	Prior	Current	Prior	Current
Net Product Sales	\$0	\$0	\$0	\$0
Collaboration/ Licensing Revenues	\$281	\$502	\$304	\$525
Total Revenue	\$281	\$502	\$304	\$525

	2024E		2025E	
\$ in millions (ex. per share items)	Prior	Current	Prior	Current
Revenue	\$281	\$502	\$304	\$525
COGS	-	-	-	-
Gross Profit	281	502	304	525
R&D	382	658	451	691
SG&A	134	129	155	135
Operating Income	(235)	(285)	(303)	(301)
Other income, net	17	26	19	28
Taxes	-	-	-	-
GAAP Net Income	(\$218)	(\$258)	(\$284)	(\$274)
GAAP EPS	(2.94)	(3.40)	(3.79)	(3.58)
Shares Outstanding - Diluted	74	76	75	77

Source: BofA Global Research estimates

BofA GLOBAL RESEARCH

Abbreviations:

HIF-2a: hypoxia-inducible factor 2a

TIGIT: T cell immunoreceptor with Ig and ITIM domains

OS: overall survival

PDAC: pancreatic ductal adenocarcinoma

mCRPC: metastatic castrate resistant prostate cancer

mCRC: metastatic colorectal cancer

ASCO: American Society of Clinical Oncology meeting

AUC: area under the curve

C_{max}: peak concentration

GI: gastrointestinal



Price objective basis & risk

Arcus Biosciences (RCUS)

Our 12-month price objective (PO) is based on our NPV analysis of revenue forecasts and estimated margin assumptions. We forecast sales of dom (anti-TIGIT), etruma (anti-A2a/A2b receptor), and zim (anti-PD-1), with profits and royalties distributed in accordance with partnership agreements. This includes sales of dom adjusted by an LOS range of 25-35% by indication, etruma (LOS: 5-10%) and zim (LOS: 5-30%). Given a WACC of 12% and a terminal growth rate ranging from 0% to -50%, we estimate a value of \$8/ share for the partnerships (\$4/sh for dom, \$1/sh for zim, \$0/sh for etruma, \$3/sh for licenses/ milestones). Together with \$16/sh for net cash and <\$1/sh for the pipeline, our PO is \$24/ share.

Upside risks to our PO: 1) validation of clinical targets, 2) clear signals of clinical efficacy with good tolerability, 3) similar robust signals from the early pipeline, 4) expansion of collaboration deals for these assets, 5) accelerated regulatory timelines, and 6) strong commercial support from payers and providers

Downside risks to our PO: 1) clinical trial failures, 2) emergence of meaningful safety risks likely to pose regulatory and/or commercial headwinds, 3) limited signs of synergistic efficacy of combo regimens, 4) regulatory delays, 5) competition from other players, 6) financial risks due to available cash to fund activities, 7) commercial pushback from payers and providers, and 8) current partners opting to discontinue their collaborations.

Analyst Certification

I, Jason Zemansky, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.

US - Biopharmaceuticals Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
BUY				
	89bio, Inc	ETNB	ETNB US	Geoff Meacham
	Acumen Pharma	ABOS	ABOS US	Geoff Meacham
	Agios Pharmaceuticals	AGIO	AGIO US	Greg Harrison, CFA
	Amylyx Pharmaceuticals	AMLX	AMLX US	Geoff Meacham
	BioMarin	BMRN	BMRN US	Geoff Meacham
	BioXcel Therapeutics	BTAI	BTAI US	Greg Harrison, CFA
	BridgeBio Pharma	BBIO	BBIO US	Greg Harrison, CFA
	Caribou	CRBU	CRBU US	Geoff Meacham
	CRISPR Therapeutics	CRSP	CRSP US	Geoff Meacham
	Eli Lilly and Company	LLY	LLY US	Geoff Meacham
	Gilead Sciences Inc.	GILD	GILD US	Geoff Meacham
	HUTCHMED	HCM	HCM US	Alec W. Stranahan
	Immatics	IMTX	IMTX US	Alec W. Stranahan
	Insmed Incorporated	INSM	INSM US	Jason Zemansky
	Intellia Therapeutics	NTLA	NTLA US	Greg Harrison, CFA
	Janux Therapeutics	JANX	JANX US	Alec W. Stranahan
	Keros	KROS	KROS US	Greg Harrison, CFA
	Kiniksa Pharmaceuticals, Ltd.	KNSA	KNSA US	Geoff Meacham
	Krystal Biotech	KRYS	KRYS US	Alec W. Stranahan
	Kura Oncology	KURA	KURA US	Jason Zemansky
	Liquidia Corporation	LQDA	LQDA US	Greg Harrison, CFA
	Lyell Immunopharma	LYEL	LYEL US	Geoff Meacham
	MeiraGTx	MGTX	MGTX US	Alec W. Stranahan
	Merck & Co.	MRK	MRK US	Geoff Meacham
	Mineralys Therapeutics	MLYS	MLYS US	Greg Harrison, CFA

US - Biopharmaceuticals Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
	Neumora Therapeutics	NMRA	NMRA US	Geoff Meacham
	Rani Therapeutics	RANI	RANI US	Geoff Meacham
	Regenxbio, Inc.	RGNX	RGNX US	Alec W. Stranahan
	Revolution Medicines	RVMD	RVMD US	Alec W. Stranahan
	Rocket Pharmaceuticals, Inc.	RCKT	RCKT US	Greg Harrison, CFA
	Royalty Pharma	RPRX	RPRX US	Geoff Meacham
	Sana Biotechnology	SANA	SANA US	Geoff Meacham
	SpringWorks	SWTX	SWTX US	Alec W. Stranahan
	Syndax Pharmaceuticals	SNDX	SNDX US	Jason Zemansky
	Traverse Therapeutics Inc	TVTX	TVTX US	Greg Harrison, CFA
	Turnstone Biologics	TSBX	TSBX US	Geoff Meacham
	Vertex Pharmaceuticals Inc.	VRTX	VRTX US	Geoff Meacham
	Werewolf Therapeutics	HOWL	HOWL US	Jason Zemansky
	Xencor	XNCR	XNCR US	Alec W. Stranahan
NEUTRAL				
	AbbVie	ABBV	ABBV US	Geoff Meacham
	Alector, Inc	ALEC	ALEC US	Greg Harrison, CFA
	Amgen Inc.	AMGN	AMGN US	Geoff Meacham
	Arcus Biosciences	RCUS	RCUS US	Jason Zemansky
	Beam Therapeutics	BEAM	BEAM US	Greg Harrison, CFA
	Biogen Inc.	BIIB	BIIB US	Geoff Meacham
	Bristol-Myers Squibb	BMJ	BMJ US	Geoff Meacham
	Cytokinetics, Incorporated	CYTK	CYTK US	Jason Zemansky
	Editas Medicine	EDIT	EDIT US	Greg Harrison, CFA
	Erasca	ERAS	ERAS US	Alec W. Stranahan
	Esperion	ESPR	ESPR US	Jason Zemansky
	Exscientia	EXAI	EXAI US	Alec W. Stranahan
	IGM Biosciences	IGMS	IGMS US	Greg Harrison, CFA
	Johnson & Johnson	JNJ	JNJ US	Geoff Meacham
	Kymera Therapeutics	KYMR	KYMR US	Geoff Meacham
	Moderna	MRNA	MRNA US	Geoff Meacham
	Pfizer	PFE	PFE US	Geoff Meacham
	Recursion Pharmaceuticals, Inc.	RXRX	RXRX US	Alec W. Stranahan
	Tyra Biosciences	TYRA	TYRA US	Greg Harrison, CFA
	Vir	VIR	VIR US	Alec W. Stranahan
	Y-mAbs Therapeutics, Inc	YMAB	YMAB US	Alec W. Stranahan
UNDERPERFORM				
	AlloVir, Inc.	ALVR	ALVR US	Jason Zemansky
	CureVac	CVAC	CVAC US	Geoff Meacham
	Day One Biopharmaceuticals	DAWN	DAWN US	Alec W. Stranahan
	Novavax	NVAX	NVAX US	Alec W. Stranahan
	Regeneron Pharmaceuticals Inc.	REGN	REGN US	Geoff Meacham
	Reneo Pharmaceuticals	RPHM	RPHM US	Jason Zemansky
	TG Therapeutics	TGTX	TGTX US	Alec W. Stranahan
	United Therapeutics Corporation	UTHR	UTHR US	Greg Harrison, CFA



iQmethodSM Measures Definitions

Business Performance

Return On Capital Employed

Return On Equity

Operating Margin

Earnings Growth

Free Cash Flow

Quality of Earnings

Cash Realization Ratio

Asset Replacement Ratio

Tax Rate

Net Debt-To-Equity Ratio

Interest Cover

Valuation Toolkit

Price / Earnings Ratio

Price / Book Value

Dividend Yield

Free Cash Flow Yield

Enterprise Value / Sales

EV / EBITDA

Numerator

$\text{NOPAT} = (\text{EBIT} + \text{Interest Income}) \times (1 - \text{Tax Rate}) + \text{Goodwill Amortization}$

Net Income

Operating Profit

Expected 5 Year CAGR From Latest Actual

Cash Flow From Operations – Total Capex

Numerator

Cash Flow From Operations

Capex

Tax Charge

Net Debt = Total Debt – Cash & Equivalents

EBIT

Numerator

Current Share Price

Current Share Price

Annualised Declared Cash Dividend

Cash Flow From Operations – Total Capex

$\text{EV} = \text{Current Share Price} \times \text{Current Shares} + \text{Minority Equity} + \text{Net Debt} +$

Other LT Liabilities

Enterprise Value

Denominator

$\text{Total Assets} - \text{Current Liabilities} + \text{ST Debt} + \text{Accumulated Goodwill}$

Amortization

Shareholders' Equity

Sales

N/A

N/A

Denominator

Net Income

Depreciation

Pre-Tax Income

Total Equity

Interest Expense

Denominator

Diluted Earnings Per Share (Basis As Specified)

Shareholders' Equity / Current Basic Shares

Current Share Price

$\text{Market Cap} = \text{Current Share Price} \times \text{Current Basic Shares}$

Sales

Basic EBIT + Depreciation + Amortization

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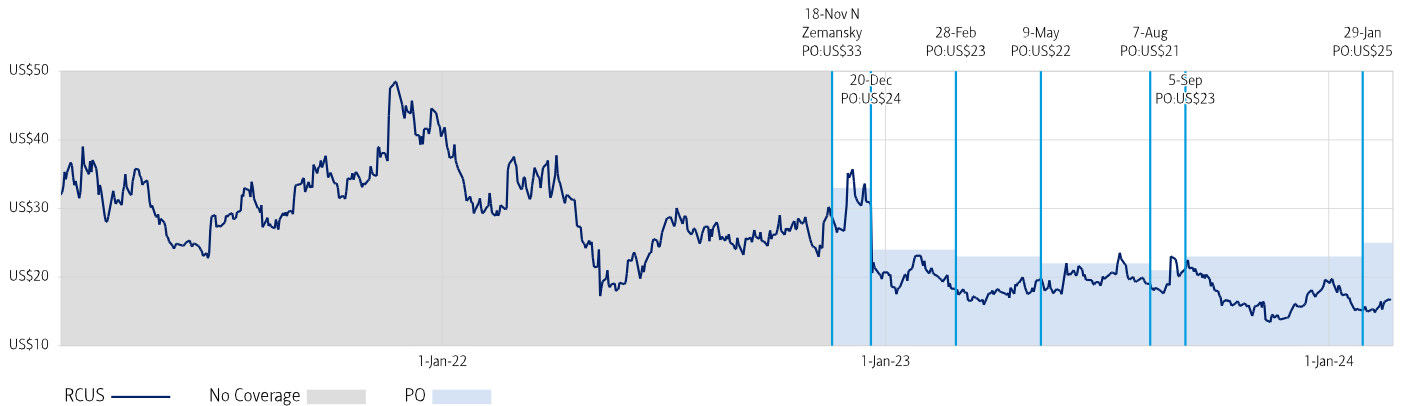
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Disclosures

Important Disclosures

Arcus Biosciences (RCUS) Price Chart



B: Buy, N: Neutral, U: Underperform, PO: Price Objective, NA: No longer valid, NR: No Rating

The Investment Opinion System is contained at the end of the report under the heading "Fundamental Equity Opinion Key". Dark grey shading indicates the security is restricted with the opinion suspended. Medium grey shading indicates the security is under review with the opinion withdrawn. Light grey shading indicates the security is not covered. Chart is current as of a date no more than one trading day prior to the date of the report.

Equity Investment Rating Distribution: Health Care Group (as of 31 Dec 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships ^{R1}	Count	Percent
Buy	234	60.94%	Buy	115	49.15%
Hold	80	20.83%	Hold	36	45.00%
Sell	70	18.23%	Sell	29	41.43%

Equity Investment Rating Distribution: Global Group (as of 31 Dec 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships ^{R1}	Count	Percent
Buy	1895	53.62%	Buy	1083	57.15%
Hold	832	23.54%	Hold	454	54.57%
Sell	807	22.84%	Sell	383	47.46%

^{R1} Issuers that were investment banking clients of BofA Securities or one of its affiliates within the past 12 months. For purposes of this Investment Rating Distribution, the coverage universe includes only stocks. A stock rated Neutral is included as a Hold, and a stock rated Underperform is included as a Sell.

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Investment rating	Total return expectation (within 12-month period of date of initial rating)	Ratings dispersion guidelines for coverage cluster ^{R2}
Buy	≥ 10%	≤ 70%
Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

^{R2} Ratings dispersions may vary from time to time where BofA Global Research believes it better reflects the investment prospects of stocks in a Coverage Cluster.

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