

## AVEO Pharmaceuticals, Inc.

### Partnership A Big Win; Transformative TIVO-1 Data On the Horizon; Raising PT to \$20

Following the removal of a restriction on research publication, we wanted to provide our thoughts on 4Q10 results and Aveo's recent e.x.-Asia partnership with Astellas for tivozanib. On 2/16, Aveo reported a GAAP loss of \$0.30, better than JPM (\$0.77) and Street (\$0.64) estimates on higher collaboration revenues and lower expenses. More importantly, we are very encouraged by the partnership with Astellas, as there is now ample funding for tivozanib to be developed in additional indications, a key to recognizing the full value of the agent. Additionally, we believe the upcoming phase 3 trial (TIVO-1, expected mid-2011) of tivozanib in renal cell carcinoma (RCC) has a high probability of success, and these data are likely to be a transformative catalyst. This would move Aveo from a developmental stage to a pre-commercial company which has clear scarcity value in biotech. We expect AVEO shares to be strong on the partnership news and its favorable terms and we are reiterating our Overweight rating ahead of TIVO-1 data and raising our price target to \$20 from \$16.5 previously.

- **We view the Tivozanib partnership as a big win.** With this partnership, we now believe there is adequate funding to develop tivozanib in additional indications, which was a concern previously. Aveo will receive an initial cash payment of \$125M (\$75M license fee + \$50M in R&D funding), and ~\$1.3B in milestones (\$575M clinical/regulatory + \$780M in commercial). Astellas and Aveo will fund development and commercialization costs equally in North America (NA) and EU, with Aveo leading NA commercialization (Astellas leading EU commercialization). In ROW, Aveo will receive double-digit royalties on sales. Overall, we think the terms are quite good and reflect the value of tivozanib, not just in RCC, but in several other meaningful indications in oncology.
- **We believe Tivozanib in RCC has a high probability of success.** TIVO-1 data is on track for mid-year. On the call, Aveo noted it will have a better gauge of the event-rate in 2Q11. Based on prior phase 2 data, in which a 14.8 month PFS benefit was observed in the phase 3 patient population (clear-cell histology and history of prior nephrectomy), we believe there is a high probability that statistical significance is achieved versus Nexavar (TIVO-1 90% powered to show a 3 month benefit; Nexavar PFS ~5.5 months). In our view, a PFS approaching 12 months with the good tolerability profile that has been seen in phase 2, would mean a very differentiated agent in RCC. The key competitive agent to watch in RCC at this point is Pfizer's axitinib.

#### AVEO Pharmaceuticals, Inc. (AVEO; AVEO US)

	2010E (Old)	2010A (New)	2011E (Old)	2011E (New)	2012E (Old)	2012E (New)
EPS Reported (\$)						
Q1 (Mar)	(2.27)	(2.27)				
Q2 (Jun)	(0.50)	(0.50)				
Q3 (Sep)	(0.60)	(0.60)				
Q4 (Dec)	(0.77)	(0.30)				
FY	(2.92)	(2.31)	(3.41)	(0.45)	(3.56)	0.32

Source: Company data, Bloomberg, J.P. Morgan estimates.

## Overweight

AVEO, AVEO US

Price: \$13.89

▲ Price Target: \$20.00

Previous: \$16.50

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#### Price Performance



#### Company Data

Price (\$)	13.89
Date Of Price	17 Feb 11
52-week Range (\$)	17.93 - 6.01
Mkt Cap (\$ mn)	88.06
Fiscal Year End	Dec
Shares O/S (mn)	6
Price Target (\$)	20.00
Price Target End Date	31 Dec 11

See page 5 for analyst certification and important disclosures.

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- **Pipeline.** Related to Tivozanib, Aveo plans to move forward in breast and colorectal cancer. This is not surprising, in our view, given the encouraging early data observed in both indications. Additionally, enrollment in the phase 2 trial of AV-299 (ficlatuzumab) + gefitinib in NSCLC is expected to complete this year, with data expected in early-2012. AV-299 also brings significant value to Aveo given that it is unpartnered and it could benefit down the road commercially from existing sales / marketing infrastructure in North America.
- **Reiterate Overweight rating.**

## Changes to Our Model

Based on the partnership with Astellas, we are making changes to our model to account for expenses and milestones. Our 2011, 2012, and 2013 EPS estimates change to (\$0.45), \$0.32, and \$0.50, respectively, from (\$3.41), (\$3.56), and (\$2.53).

Table 1: AVEO: Changes to Our Model

	2011E	2011E	2012E	2012E	2013E	2013E
	OLD	NEW	OLD	NEW	OLD	NEW
Total Revenue	37.5	71.1	70.3	126.3	138.0	171.5
R&D	120.0	52.0	145.0	62.4	150.0	71.8
SG&A	35.0	34.0	55.0	40.8	60.0	46.9
Total Op Ex	155.0	86.0	207.9	111.1	240.0	148.5
Net income	(119.6)	(17.0)	(139.2)	13.6	(103.0)	21.9
EPS (excl. FAS123R)	(3.41)	(0.45)	(3.56)	0.32	(2.53)	0.50

Source: JPMorgan estimates, Bloomberg, and Company data.

## Valuation, Rating and Price Target Analysis

We have raised our December 2011 price target to \$20 from \$16.50 based on applying a 3x revenue multiple to our 2014 revenue estimate of \$400M, the third full year we expect Tivozanib to be on the market, and discounting back to the present at 25% per year. Our 3x multiple is conservatively at the lower end of the range of 3-5x revenue multiple for SMid biotechs over the last three years. Our discount rate is consistent with the rate afforded by many SMids with phase 3 trials (having de-risked phase 2 data).

## Risks to Our Rating and Price Target

We see four primary risks to our Overweight rating on AVEO: 1) the failure of key later-stage clinical program of tivozanib in RCC; 2) AVEO has not developed a commercial team, and the RCC market is quite competitive with more than 6 players in the space, including major pharma with deep pockets – hence, even with differentiated data for tivozanib, AVEO may not be able to compete effectively in the US market; 3) regulatory risk for FDA approval of tivozanib in RCC; and 4) there is risk the AVEO could seek to raise capital through an equity offering, which could dilute shareholders.

## AVEO Pharmaceuticals, Inc.: Summary of Financials

Income Statement - Annual	FY10A	FY11E	FY12E	FY13E	Income Statement - Quarterly	1Q11E	2Q11E	3Q11E	4Q11E
Revenues	45	71	126	172	Revenues	-	-	-	-
Cost of products sold	0	0	8	30	Cost of products sold	-	-	-	-
Gross profit	45	71	118	142	Gross profit	-	-	-	-
SG&A	15	34	41	47	SG&A	-	-	-	-
R&D	86	52	62	72	R&D	-	-	-	-
Operating Income	(56)	(15)	15	23	Operating income	-	-	-	-
Note: EBITDA	(56)	(15)	15	23	Note: EBITDA	-	-	-	-
Net interest income / (expense)	(3)	(2)	(2)	(1)	Net interest income / (expense)	-	-	-	-
Other income / (expense)	1	0	0	0	Other income / (expense)	-	-	-	-
Pretax income	(59)	(17)	14	22	Pretax income	-	-	-	-
Income taxes	0	0	0	0	Income taxes	-	-	-	-
Net income - GAAP	-	-	-	-	Net income - GAAP	-	-	-	-
Net income - recurring	(59)	(17)	14	22	Net income - recurring	-	-	-	-
Diluted shares outstanding	25	38	42	44	Diluted shares outstanding	-	-	-	-
EPS - excluding non-recurring	(2.31)	(0.45)	0.32	0.50	EPS - excluding non-recurring	-	-	-	-
EPS - recurring	(2.31)	(0.45)	0.32	0.50	EPS - recurring	-	-	-	-
Balance Sheet and Cash Flow Data	FY10A	FY11E	FY12E	FY13E	Ratio Analysis	FY10A	FY11E	FY12E	FY13E
Cash and cash equivalents	-	-	-	-	Sales growth	-	-	-	131.1%
Accounts receivable	0	0	0	0	EBIT growth	37.2%	(73.6%)	(202.0%)	51.5%
Inventories	-	-	-	-	EPS growth	13.4%	(80.7%)	(172.4%)	55.7%
Other current assets	2	2	2	3	Gross margin	100.0%	100.0%	93.8%	82.6%
Current assets	81	144	264	300	EBIT margin	(126.3%)	(21.0%)	12.0%	13.4%
PP&E	3	1	(0)	(2)	EBITDA margin	(126.3%)	(21.0%)	12.0%	13.4%
Total assets	87	147	266	300	Tax rate	0.0%	0.0%	0.0%	0.0%
Total debt	12	12	12	12	Net margin	(131.6%)	(23.9%)	10.8%	12.8%
Total liabilities	64	64	64	64	Debt / EBITDA	-	-	-	-
Shareholders' equity	23	84	202	236	Debt / Capital (book)	34.7%	12.8%	5.7%	4.9%
Net income (including charges)	(59)	(17)	14	22	Return on assets (ROA)	(67.9%)	(11.5%)	5.1%	7.3%
D&A	1	2	2	2	Return on equity (ROE)	-	-	-	-
Change in working capital	(0)	(0)	(0)	(0)	Return on invested capital (ROIC)	-	-	-	-
Other	-	-	-	-	Enterprise value / sales	1.6	1.0	0.6	0.4
Cash flow from operations	(53)	(8)	27	35	Enterprise value / EBITDA	-	-	-	-
Capex	0	0	0	0	Free cash flow yield	(89.1%)	(13.1%)	45.4%	59.6%
Free cash flow	(53)	(8)	27	35					
Cash flow from investing activities	0	0	0	0					
Cash flow from financing activities	81	70	93	0					
Dividends	-	-	-	-					
Dividend yield	-	-	-	-					

Source: Company reports and J.P. Morgan estimates.

Note: \$ in millions (except per-share data). Fiscal year ends Dec

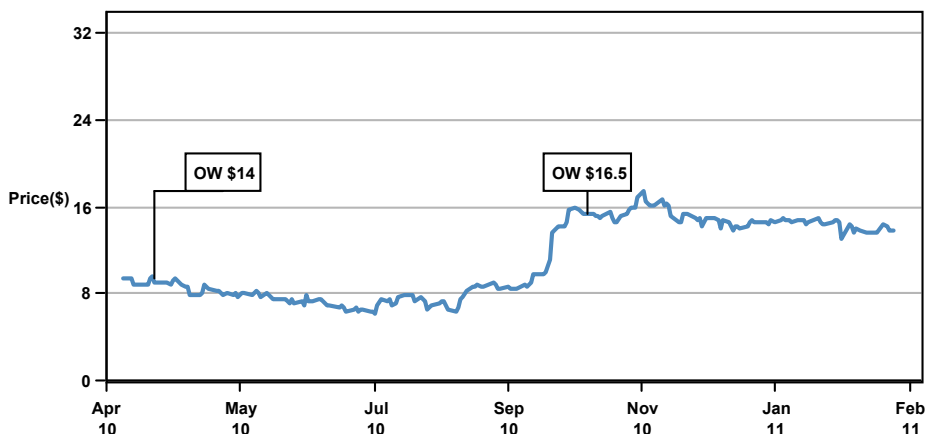
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#### AVEO Pharmaceuticals, Inc. (AVEO) Price Chart



Date	Rating	Share Price (\$)	Price Target (\$)
21-Apr-10	OW	9.39	14.00
15-Oct-10	OW	15.35	16.50

Source: Bloomberg and J.P. Morgan; price data adjusted for stock splits and dividends.  
Initiated coverage Apr 21, 2010. This chart shows J.P. Morgan’s continuing coverage of this stock; the current analyst may or may not have covered it over the entire period.  
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