

AVEO Pharmaceuticals, Inc.

2Q10 Update and Model Adjustments

2Q results for Aveo were largely uneventful, with the company reporting non-GAAP EPS of (\$0.50) with \$16M in collaboration revenues. In the pipeline, the ongoing TIVO-1 pivotal trial comparing Aveo's tivozanib with Nexavar in advanced renal cell carcinoma (RCC) is on track with enrollment ahead of schedule (top-line data YE11). In addition, Aveo expects to report incremental phase 1b tivozanib data in CRC at the ESMO conference (Milan; Oct 8-12) and phase 1b mBC data at the San Antonio Breast Cancer Conference (Dec 8-12). We note that opportunities in colon and breast cancer are free call options, in our view, and they are not assumed in our AVEO model. With TIVO-1 on track in RCC and data for new indications emerging, as well as a potential partnership, we are bullish on AVEO and are maintaining our Overweight rating.

- 2Q Results.** Collaborative revenues of \$16M for 2Q were modestly above the Street and our estimates (JPMe: \$10M, cons: \$14M), and include \$8.5M of milestone payments received from Merck (related to AV-299 ph 2 trial initiation) during the quarter. Operating expenses came in \$7M above the Street (+\$3M vs. JPMe), largely due to one-time purchase of Nexavar for TIVO-1 trial, but expected to come down to normal run rate in coming quarters. The company maintained its guidance of year-end cash balance of at least \$50M.
- TIVO-1 on track; Orphan drug designation by EMA.** Aveo noted that enrollment is ahead of schedule in the ongoing phase 3 TIVO-1 trial, with 86 sites active to date. We expect top-line data released by YE11 if not sooner. Additionally, in another positive development, European Medicines Agency (EMA) granted orphan drug designation for Tivozanib in RCC last month.
- Potential partnership opportunities in colon and breast.** Future tivozanib expansion in breast, and colon could be significant value drivers, in our view. Efficacy signals in the Phase I trials (data expected in 4Q) could very well accelerate partnership discussions in US and OUS.
- Pipeline updates.** AV-299 (partnered with Merck), a monoclonal antibody targeting HGF, advanced into a phase 2 trial in NSCLC this quarter. AV-203 (partnered with Biogen) targeting Erb3 demonstrated significant tumor growth inhibition in preclinical studies for solid tumors and we believe offer additional value to investors.

Overweight

AVEO, AVEO US

Price: \$7.15

Price Target: \$14.00

US Biotechnology

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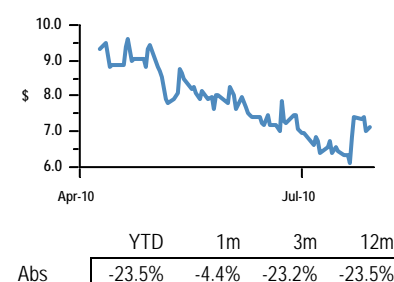
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Price Performance



AVEO Pharmaceuticals, Inc. (AVEO; AVEO US)

	2008A	2009A	2010E (Old)	2010E (New)	2011E
EPS Reported (\$)					
Q1 (Mar)			(2.27)A	(2.27)A	
Q2 (Jun)			(0.57)	(0.50)	
Q3 (Sep)			(0.65)	(0.63)	
Q4 (Dec)			(0.67)	(0.65)	
FY	(0.46)	(2.03)	(2.95)	(2.80)	(1.81)

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

Company Data	
Price (\$)	7.15
Date Of Price	29 Jul 10
52-week Range (\$)	9.91 - 6.01
Mkt Cap (\$ mn)	45.33
Fiscal Year End	Dec
Shares O/S (mn)	6
Price Target (\$)	14.00
Price Target End Date	31 Dec 10

See page 4 for analyst certification and important disclosures, including non-US analyst disclosures.

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Changes to Our Model

We have updated our model to reflect the quarterly results. Our 2010 non-GAAP EPS estimate is \$(2.80) now. We have not made changes to 2011-12. Please see Table 1 for details.

Table 1: AVEO: Changes to Our Model

	2010E	2010E	2011E	2011E	2012E	2012E
	OLD	NEW	OLD	NEW	OLD	NEW
Total Revenue	40.9	46.5	75.0	75.0	108.7	108.7
R&D	95.1	98.6	115.0	115.0	135.0	135.0
SG&A	16.8	16.1	22.5	22.5	55.0	55.0
Total Op Ex	111.9	114.7	137.5	137.5	194.7	194.7
Net income	(70.7)	(69.3)	(63.2)	(63.2)	(85.8)	(85.8)
EPS (excl. FAS123R)	(2.95)	(2.80)	(1.81)	(1.81)	(2.20)	(2.20)

Source: JPMorgan estimates, Bloomberg, and Company data.

Valuation, Rating and Price Target Analysis

We arrive at our \$14 price target for AVEO by applying a 5x revenue multiple to our 2013 revenue estimate of \$178M, the second full year we expect Tivozanib to be on the market, and discounting back to the present at 25% per year. Our 5x multiple is at the lower end of the range of 4-7x 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). Our price target represents significant upside potential from current levels, and thus supports an Overweight rating.

Risks to Our Rating

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 pharmas 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. Lastly, 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	FY09A	FY10E	FY11E	FY12E	Income Statement - Quarterly	1Q10A	2Q10E	3Q10E	4Q10E
Revenues	21	47	75	109	Revenues	11	16	10	10
Cost of products sold	0	0	0	5	Cost of products sold	0	0	0	0
Gross profit	21	47	75	104	Gross profit	11	16	10	10
SG&A	10	16	22	55	SG&A	3	4	4	5
R&D	52	99	115	135	R&D	23	26	25	25
Operating Income	(41)	(68)	(62)	(86)	Operating income	(14)	(14)	(20)	(20)
Note: EBITDA	(41)	(68)	(62)	(86)	Note: EBITDA	(14)	(14)	(20)	(20)
Net interest income / (expense)	(3)	(1)	(1)	0	Net interest income / (expense)	(1)	(1)	0	0
Other income / (expense)	(0)	0	0	0	Other income / (expense)	1	(1)	0	0
Pretax income	(44)	(69)	(63)	(86)	Pretax income	(14)	(15)	(19)	(20)
Income taxes	0	0	0	0	Income taxes	0	0	0	0
Net income - GAAP	-	-	-	-	Net income - GAAP	-	-	-	-
Net income - recurring	(44)	(69)	(63)	(86)	Net income - recurring	(14)	(15)	(19)	(20)
Diluted shares outstanding	22	25	35	39	Diluted shares outstanding	6	31	31	31
EPS - excluding non-recurring	(2.03)	(2.80)	(1.81)	(2.20)	EPS - excluding non-recurring	(2.27)	(0.50)	(0.63)	(0.65)
EPS - recurring	(2.03)	(2.80)	(1.81)	(2.20)	EPS - recurring	(2.27)	(0.50)	(0.63)	(0.65)
Balance Sheet and Cash Flow Data	FY09A	FY10E	FY11E	FY12E	Ratio Analysis	FY09A	FY10E	FY11E	FY12E
Cash and cash equivalents	45	-	-	-	Sales growth	-	-	-	-
Accounts receivable	0	0	0	0	EBIT growth	31.3%	65.9%	(8.4%)	37.7%
Inventories	-	-	-	-	EPS growth	343.4%	37.9%	(35.6%)	21.8%
Other current assets	1	2	2	2	Gross margin	100.0%	100.0%	100.0%	95.6%
Current assets	53	71	87	108	EBIT margin	(197.9%)	(146.7%)	(83.3%)	(79.2%)
PP&E	4	3	1	(0)	EBITDA margin	(197.9%)	(146.7%)	(83.3%)	(79.2%)
Total assets	60	76	91	110	Tax rate	0.0%	0.0%	0.0%	0.0%
Total debt	20	12	12	12	Net margin	(212.4%)	(149.0%)	(84.3%)	(78.9%)
Total liabilities	230	64	64	64	Debt / EBITDA	-	-	-	-
Shareholders' equity	(170)	13	27	46	Debt / Capital (book)	(13.1%)	49.4%	31.2%	21.0%
Net income (including charges)	(44)	(69)	(63)	(86)	Return on assets (ROA)	(73.8%)	(91.0%)	(69.8%)	(78.1%)
D&A	1	1	2	2	Return on equity (ROE)	-	-	-	-
Change in working capital	29	(0)	(0)	(0)	Return on invested capital (ROIC)	-	-	-	-
Other	-	-	-	-	Enterprise value / sales	1.3	1.5	1.0	0.7
Cash flow from operations	(10)	(63)	(54)	(72)	Enterprise value / EBITDA	-	-	-	-
Capex	(2)	0	0	0	Free cash flow yield	(19.7%)	(106.8%)	(91.1%)	(122.2%)
Free cash flow	(12)	(63)	(54)	(72)					
Cash flow from investing activities	3	0	0	0					
Cash flow from financing activities	31	81	70	93					
Dividends	-	-	-	-					
Dividend yield	-	-	-	-					

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

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

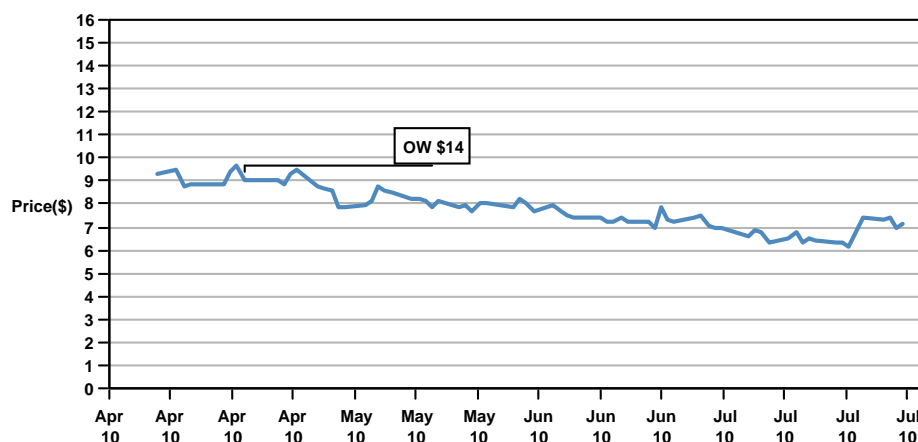
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AVEO Pharmaceuticals, Inc. (AVEO) Price Chart



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

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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