

AVEO Pharmaceuticals, Inc.

Significant 3Q10 Progress; Focus on Mid-2011 TIVO-1 Data

This morning, Aveo reported a 3Q loss per share of (\$0.60) versus our estimate of (\$0.63) and consensus of (\$0.62). We believe Aveo continues to make excellent pipeline progress with Tivozanib, the company's main value driver. Indeed, the pivotal phase 3 trial of Tivozanib in RCC (TIVO-1) completed enrollment in August, which was 6 months ahead of schedule (data mid-2011). Aveo also noted, with the recent private placement, the company will accelerate development plans for Tivozanib in breast and colon cancer, which are very attractive call options, in our view. Additionally in 3Q10, Aveo regained rights to AV-299 from Merck, but our sense is this development program will likely take a backseat to Tivozanib in the near term. We're maintaining our Overweight rating on AVEO shares, given near term TIVO-1 data and a strengthened balance sheet.

- **3Q results.** Lower collaborative/R&D revenues of \$6.2M (JPMe: \$10M; consensus: \$9M) were more than offset by lower OPEX of \$24M (JPMe: \$30M; consensus: \$19M). With the recent private placement of \$57M, Aveo expects to end-2010 with ~\$100M in cash (sufficient to mid-2012). Indeed, we are no longer assuming a partnership for Tivozanib given a dramatically improved balance sheet.
- **TIVO-1 in RCC.** Data from TIVO-1 now is expected mid-2011. Recall, in phase 2 Tivozanib produced 11.8 month PFS (Nexavar-5.5 month PFS; also the active comparator in phase 3) and an attractive safety profile. Based on this, we continue to believe there is a high probability of success for TIVO-1.
- **Pipeline updates.** Perhaps the most interesting data points from the call were that Aveo will now also accelerate development of Tivozanib in breast and colon. Update data from early ongoing Tivozanib trials in both indications are expected by year-end and should increase visibility for the agent's potential beyond RCC (*Tivozanib+FOLFOX6 in GI cancers and CRC*: EORTC (Nov. 16-19; Berlin, Germany); *Tivozanib+paclitaxel in mBC*: San Antonio Breast Cancer Symposium (Dec. 8-12; San Antonio, Texas))
- **Reiterate Overweight rating.** We believe TIVO-1 has a high probability for success in phase 3, and we view the breast and colon indications as attractive call options. We continue to like Aveo shares, and would opportunistically add to positions on any share pull backs ahead of mid-2011 TIVO-1 data.

Overweight

AVEO, AVEO US

Price: \$15.86

Price Target: \$16.50

US Biotechnology

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Price Performance



AVEO Pharmaceuticals, Inc. (AVEO; AVEO US)

| | 2010E (Old) | 2010E (New) | 2011E (Old) | 2011E (New) | 2012E (Old) | 2012E (New) |
|-------------------|----------------|----------------|----------------|----------------|----------------|----------------|
| EPS Reported (\$) | | | | | | |
| Q1 (Mar) | (2.27)A | (2.27)A | | | | |
| Q2 (Jun) | (0.50)A | (0.50)A | | | | |
| Q3 (Sep) | (0.63)A | (0.60)A | | | | |
| Q4 (Dec) | (0.65) | (0.77) | | | | |
| FY | (2.80) | (2.92) | (1.81) | (3.41) | (1.79) | (3.56) |

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

Company Data

| | |
|-----------------------|--------------|
| Price (\$) | 15.86 |
| Date Of Price | 03 Nov 10 |
| 52-week Range (\$) | 16.25 - 6.01 |
| Mkt Cap (\$ mn) | 100.55 |
| Fiscal Year End | Dec |
| Shares O/S (mn) | 6 |
| Price Target (\$) | 16.50 |
| Price Target End Date | 31 Dec 11 |

See page 4 for analyst certification and important disclosures.

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Changes to Our Model

Based on updates on the 3Q10 call and the recent financing, we are updating our model. Given the recent financing, we are no longer assuming a partnership for Tivozanib and we are increasing our R&D (due to accelerated development in breast and colon cancer) and SG&A (pre-commercial launch activities). As a results, our 2010, 2011 and 2012 loss per share estimates change to \$2.92, \$3.41 and \$3.56 respectively, from \$2.80, \$1.81, \$1.79.

Table 1: Table 1: AVEO: Changes to Our Model

| | 2010E | 2010E | 2011E | 2011E | 2012E | 2012E |
|---------------------|--------|--------|--------|---------|--------|---------|
| | OLD | NEW | OLD | NEW | OLD | NEW |
| Total Revenue | 46.5 | 35.7 | 75.0 | 37.5 | 127.8 | 70.3 |
| R&D | 98.6 | 90.9 | 115.0 | 120.0 | 135.0 | 145.0 |
| SG&A | 16.1 | 14.2 | 22.5 | 35.0 | 55.0 | 55.0 |
| Total Op Ex | 114.7 | 105.1 | 137.5 | 155.0 | 197.9 | 207.9 |
| Net income | (69.3) | (72.2) | (63.2) | (119.6) | (69.8) | (139.2) |
| EPS (excl. FAS123R) | (2.80) | (2.92) | (1.81) | (3.41) | (1.79) | (3.56) |

Source: JPMorgan estimates, Bloomberg, and Company data.

Valuation, Rating and Price Target Analysis

Our 2011 price target is \$16.50 for AVEO shares, based on applying a 5x revenue multiple to our 2013 revenue estimate of \$181M, the second full year we expect Tivozanib to be on the market, and discounting back to the present at 25% per year. We are pushing up the launch of Tivozanib slightly given revised timelines. 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).

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 six 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; 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 | FY09A | FY10E | FY11E | FY12E | Income Statement - Quarterly | 1Q10A | 2Q10A | 3Q10A | 4Q10E |
|-------------------------------------|--------|--------|--------|--------|-----------------------------------|----------|----------|----------|----------|
| Revenues | 21 | 36 | 38 | 70 | Revenues | 11 | 16 | 6 | 3 |
| Cost of products sold | 0 | 0 | 0 | 8 | Cost of products sold | 0 | 0 | 0 | 0 |
| Gross profit | 21 | 36 | 38 | 62 | Gross profit | 11 | 16 | 6 | 3 |
| SG&A | 10 | 14 | 35 | 55 | SG&A | 3 | 4 | 4 | 4 |
| R&D | 52 | 91 | 120 | 145 | R&D | 23 | 26 | 20 | 22 |
| Operating Income | (41) | (69) | (118) | (138) | Operating income | (14) | (14) | (18) | (23) |
| Note: EBITDA | (41) | (69) | (118) | (138) | Note: EBITDA | (14) | (14) | (18) | (23) |
| Net interest income / (expense) | (3) | (3) | (2) | (2) | Net interest income / (expense) | (1) | (1) | (1) | (1) |
| Other income / (expense) | (0) | 0 | 0 | 0 | Other income / (expense) | 1 | (1) | 0 | 0 |
| Pretax income | (44) | (72) | (120) | (139) | Pretax income | (14) | (15) | (19) | (24) |
| Income taxes | 0 | 0 | 0 | 0 | Income taxes | 0 | 0 | 0 | 0 |
| Net income - GAAP | - | - | - | - | Net income - GAAP | - | - | - | - |
| Net income - recurring | (44) | (72) | (120) | (139) | Net income - recurring | (14) | (15) | (19) | (24) |
| Diluted shares outstanding | 22 | 25 | 35 | 39 | Diluted shares outstanding | 6 | 31 | 31 | 31 |
| EPS - excluding non-recurring | (2.03) | (2.92) | (3.41) | (3.56) | EPS - excluding non-recurring | (2.27) | (0.50) | (0.60) | (0.77) |
| EPS - recurring | (2.03) | (2.92) | (3.41) | (3.56) | EPS - recurring | (2.27) | (0.50) | (0.60) | (0.77) |
| 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% | 68.6% | 69.5% | 17.1% |
| Inventories | - | - | - | - | EPS growth | 343.4% | 43.5% | 16.8% | 4.5% |
| Other current assets | 1 | 2 | 2 | 2 | Gross margin | 100.0% | 100.0% | 100.0% | 88.8% |
| Current assets | 53 | 68 | 28 | (5) | EBIT margin | (197.9%) | (194.1%) | (313.3%) | (195.8%) |
| PP&E | 4 | 3 | 1 | (0) | EBITDA margin | (197.9%) | (194.1%) | (313.3%) | (195.8%) |
| Total assets | 60 | 73 | 31 | (3) | Tax rate | 0.0% | 0.0% | 0.0% | 0.0% |
| Total debt | 20 | 12 | 12 | 12 | Net margin | (212.4%) | (202.0%) | (318.8%) | (198.0%) |
| Total liabilities | 230 | 64 | 64 | 64 | Debt / EBITDA | - | - | - | - |
| Shareholders' equity | (170) | 10 | (32) | (66) | Debt / Capital (book) | (13.1%) | 55.9% | (61.9%) | (22.7%) |
| Net income (including charges) | (44) | (72) | (120) | (139) | Return on assets (ROA) | (73.8%) | (98.6%) | (380.9%) | 5011.3% |
| 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 | 2.0 | 1.9 | 1.0 |
| Cash flow from operations | (10) | (66) | (110) | (126) | Enterprise value / EBITDA | - | - | - | - |
| Capex | (2) | 0 | 0 | 0 | Free cash flow yield | (19.7%) | (111.7%) | (186.1%) | (212.3%) |
| Free cash flow | (12) | (66) | (110) | (126) | | | | | |
| 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

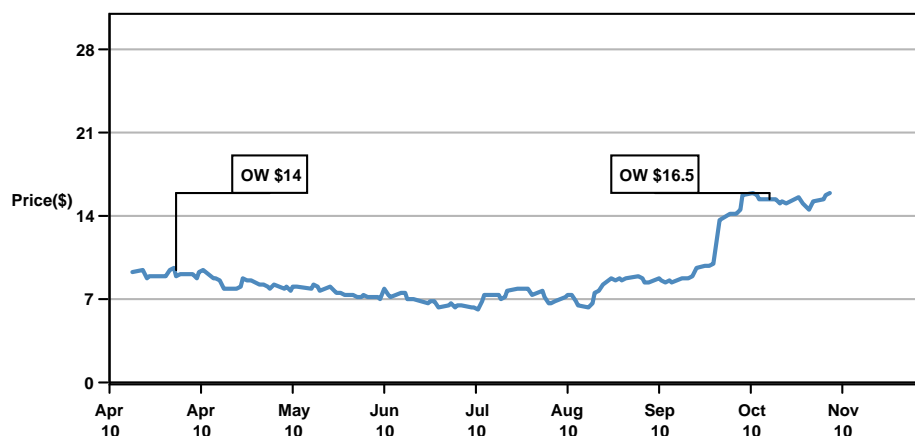
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AVEO Pharmaceuticals, Inc. (AVEO) Price Chart



| Date | Rating | Share Price (\$) | Price Target (\$) |
|-----------|--------|------------------|-------------------|
| 21-Apr-10 | OW | 9.39 | 14.00 |
| 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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|---|-----------------------------|---------------------------|-------------------------------|
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04 November 2010

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