

UBS Investment Research

First Read: Verastem

Proof of Concept Data Presented

■ What's new? Data presentations at EORTC meeting

Verastem presented data for VS-4178 (FAK) and VS-5584 (mTOR/PI3K) at the EORTC meeting in Ireland. Notably, these data show Verastem's continued focus on breast cancer. Both data sets demonstrated a reduction of cancer stem cells (CSCs) in either a xenograft or a triple negative breast cancer mouse model, the latter of which also showed tumor regression in taxane-resistant models.

■ Competitor data establish proof-of-concept for FAK in mesothelioma

Ph1 data for FAK-inhibitor GSK2256098 in mesothelioma pts were presented. While response rates were limited (no CRs or PRs) the PFS data are impressive (17.7wks overall; 24.1wks for merlin negative pts vs. 6wks for historic controls), and establish proof of concept (POC) for FAK-inhibition in meso. While no meso pts were enrolled in the ph1 VS-6063 study, we expect significant activity based on preclinical profile (pivotal trial planned mid-2013e), although we note increased market risk given potential competition in the space.

■ Thoughts: 2013 a key year for advancement

While today's data are supportive of Verastem's CSC-targeted approach, we highlight the translation into the clinic in 2013, with a potential registration study of VS-6063 in mesothelioma planned to start mid-2013. Additionally, ph1 studies for VS-5584 in advanced solid tumors and VS-4178 in patients with tumors enriched for FAK expression (incl mesothelioma and breast cancer) are planned.

■ Valuation: Buy rating with \$20 price target

We derive our price target using a DCF-based analysis.

| Highlights (US\$m) | 12/10 | 12/11 | 12/12E | 12/13E | 12/14E |
|---------------------------|---------------|---------|--------|--------|--------|
| Revenues | 0 | 0 | 0 | 0 | 0 |
| EBIT (UBS) | (1) | (14) | (29) | (31) | (35) |
| Net Income (UBS) | (1) | (14) | (28) | (31) | (34) |
| EPS (UBS, US\$) | (0.92) | (10.58) | (1.47) | (1.44) | (1.35) |
| Net DPS (UBS, US\$) | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |
| Profitability & Valuation | 5-yr hist av. | 12/11 | 12/12E | 12/13E | 12/14E |
| EBIT margin % | - | - | - | - | - |
| ROIC (EBIT) % | - | >500 | >500 | >500 | >500 |
| EV/EBITDA (core) x | - | - | -1.1 | -1.1 | -0.8 |
| PE (UBS) x | - | - | NM | NM | NM |
| Net dividend yield % | - | - | 0.0 | 0.0 | 0.0 |

Source: Company accounts, Thomson Reuters, UBS estimates. (UBS) valuations are stated before goodwill-related charges and other adjustments for abnormal and economic items at the analysts' judgement.

Valuations: based on an average share price that year, (E): based on a share price of US\$7.18 on 08 Nov 2012 19:37 EST

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Global Equity Research

Americas

Biotechnology

12-month rating **Buy**
Unchanged

12m price target **US\$20.00**
Unchanged

Price **US\$7.18**

RIC: VSTM.O BBG: VSTM US

9 November 2012

Trading data

| | |
|--------------------------|----------------|
| 52-wk range | US\$12.01-7.18 |
| Market cap. | US\$0.11bn |
| Shares o/s | 14.7m (COM) |
| Free float | 29% |
| Avg. daily volume ('000) | 10 |
| Avg. daily value (m) | US\$0.1 |

Balance sheet data 12/12E

| | |
|----------------------|------------|
| Shareholders' equity | US\$0.08bn |
| P/BV (UBS) | 1.7x |
| Net Cash (debt) | US\$0.09bn |

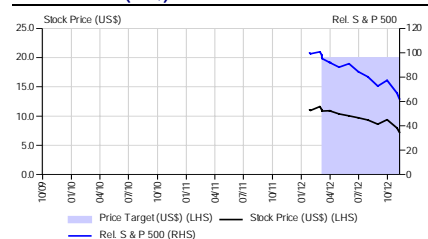
Forecast returns

| | |
|-----------------------------|---------|
| Forecast price appreciation | +178.6% |
| Forecast dividend yield | 0.0% |
| Forecast stock return | +178.6% |
| Market return assumption | 5.3% |
| Forecast excess return | +173.3% |

EPS (UBS, US\$)

| | 12/12E | 12/11 |
|--------|--------|---------------|
| | UBS | Cons. Actual |
| Q1 | (0.47) | (0.47) (1.05) |
| Q2 | (0.34) | (0.34) (1.88) |
| Q3E | (0.38) | (0.36) (2.74) |
| Q4E | (0.31) | (0.35) (4.56) |
| 12/12E | (1.47) | (1.49) |
| 12/13E | (1.44) | (1.61) |

Performance (US\$)



Source: UBS

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This report has been prepared by UBS Securities LLC

ANALYST CERTIFICATION AND REQUIRED DISCLOSURES BEGIN ON PAGE 5.

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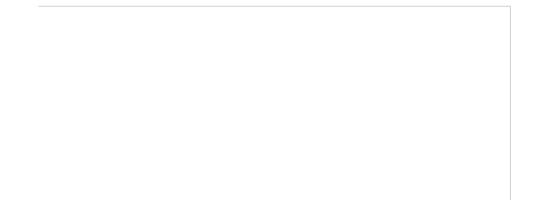
| Income statement (US\$m) | | 12/09 | 12/10 | 12/11 | 12/12E | % ch | 12/13E | % ch | 12/14E | % ch |
|---------------------------------------|---|-------|--------|---------|--------|----------|--------|-------|--------|-------|
| Revenues | - | - | 0 | 0 | 0 | - | 0 | - | 0 | - |
| Operating expenses (ex depn) | - | - | - | - | - | - | - | - | - | - |
| EBITDA (UBS) | - | - | (1) | (14) | (29) | 109.1 | (31) | 9.1 | (35) | 10.5 |
| Depreciation | - | - | 0 | 0 | 0 | - | 0 | - | 0 | - |
| Operating income (EBIT, UBS) | - | - | (1) | (14) | (29) | 109.1 | (31) | 9.1 | (35) | 10.5 |
| Other income & associates | - | - | 0 | 0 | 0 | - | 0 | - | 0 | - |
| Net interest | - | - | 0 | 0 | 0 | 267900.0 | 0 | -45.5 | 0 | 81.5 |
| Abnormal items (pre-tax) | - | - | 0 | 0 | 0 | - | 0 | - | 0 | - |
| Profit before tax | - | - | (1) | (14) | (28) | 107.1 | (31) | 9.6 | (34) | 10.2 |
| Tax | - | - | 0 | 0 | 0 | - | 0 | - | 0 | - |
| Profit after tax | - | - | (1) | (14) | (28) | 107.1 | (31) | 9.6 | (34) | 10.2 |
| Abnormal items (post-tax) | - | - | 0 | 0 | 0 | - | 0 | - | 0 | - |
| Minorities / pref dividends | - | - | 0 | 0 | 0 | - | 0 | - | 0 | - |
| Net income (local GAAP) | - | - | (1) | (14) | (28) | 107.1 | (31) | 9.6 | (34) | 10.2 |
| Net Income (UBS) | - | - | (1) | (14) | (28) | 107.1 | (31) | 9.6 | (34) | 10.2 |
| | | | | | | | | | | |
| Tax rate (%) | - | - | 0 | 0 | 0 | - | 0 | - | 0 | - |
| Pre-abnormal tax rate (%) | - | - | 0 | 0 | 0 | - | 0 | - | 0 | - |
| Per share (US\$) | | 12/09 | 12/10 | 12/11 | 12/12E | % ch | 12/13E | % ch | 12/14E | % ch |
| EPS (local GAAP) | - | - | (0.92) | (10.58) | (1.47) | -86.1 | (1.44) | -2.3 | (1.35) | -6.0 |
| EPS (UBS) | - | - | (0.92) | (10.58) | (1.47) | -86.1 | (1.44) | -2.3 | (1.35) | -6.0 |
| Net DPS | - | - | 0.00 | 0.00 | 0.00 | - | 0.00 | - | 0.00 | - |
| Cash EPS | - | - | (0.92) | (10.58) | (1.47) | -86.1 | (1.44) | -2.3 | (1.35) | -6.0 |
| BVPS | - | - | 2.50 | 45.94 | 4.27 | -90.7 | 2.42 | -43.2 | 3.82 | 57.7 |
| Balance sheet (US\$m) | | 12/09 | 12/10 | 12/11 | 12/12E | % ch | 12/13E | % ch | 12/14E | % ch |
| Cash and equivalents | - | - | 4 | 62 | 86 | 39.3 | 55 | -35.7 | 99 | 79.0 |
| Other current assets | - | - | 0 | 0 | 0 | 109.1 | 0 | 9.1 | 0 | 16.9 |
| Total current assets | - | - | 4 | 62 | 86 | 39.3 | 55 | -35.7 | 99 | 79.0 |
| Net tangible fixed assets | - | - | 0 | 1 | 1 | 104.3 | 2 | 54.5 | 3 | 39.7 |
| Net intangible fixed assets | - | - | 0 | 0 | 0 | - | 0 | - | 0 | - |
| Investments / other assets | - | - | 0 | 0 | 0 | 66.1 | 0 | 6.9 | 0 | 13.1 |
| Total assets | - | - | 4 | 63 | 88 | 40.2 | 58 | -34.0 | 103 | 77.0 |
| Trade payables & other ST liabilities | - | - | 0 | 2 | 5 | 117.5 | 5 | 8.4 | 6 | 11.6 |
| Short term debt | - | - | 0 | 0 | 0 | - | 0 | - | 0 | - |
| Total current liabilities | - | - | 0 | 2 | 5 | 117.5 | 5 | 8.4 | 6 | 11.6 |
| Long term debt | - | - | 0 | 0 | 0 | - | 0 | - | 0 | - |
| Other long term liabilities | - | - | 0 | 1 | 1 | -14.1 | 1 | -34.9 | 0 | -53.5 |
| Total liabilities | - | - | 0 | 3 | 6 | 69.9 | 6 | 0.5 | 6 | 3.9 |
| Equity & minority interests | - | - | 3 | 59 | 82 | 38.5 | 52 | -36.3 | 97 | 84.8 |
| Total liabilities & equity | - | - | 4 | 63 | 88 | 40.2 | 58 | -34.0 | 103 | 77.0 |
| Cash flow (US\$m) | | 12/09 | 12/10 | 12/11 | 12/12E | % ch | 12/13E | % ch | 12/14E | % ch |
| Net income | - | - | (1) | (14) | (28) | 107.1 | (31) | 9.6 | (34) | 10.2 |
| Depreciation | - | - | 0 | 0 | 0 | - | 0 | - | 0 | - |
| Net change in working capital | - | - | 0 | 2 | 2 | 41.4 | 0 | -97.7 | 0 | 804.0 |
| Other (operating) | - | - | 0 | 1 | 1 | 0.0 | 1 | 0.0 | 1 | 0.0 |
| Net cash from operations | - | - | 0 | (11) | (25) | 123.4 | (30) | 19.4 | (33) | 9.0 |
| Capital expenditure | - | - | 0 | (1) | (1) | -0.5 | (1) | 6.7 | (1) | 12.5 |
| Net (acquisitions) / disposals | - | - | 0 | 0 | 0 | - | 0 | - | 0 | - |
| Other changes in investments | - | - | 0 | 0 | 0 | - | 0 | - | 0 | - |
| Cash from investing activities | - | - | 0 | (1) | (1) | -0.5 | (1) | 6.0 | (1) | 11.3 |
| Increase/(decrease) in debt | - | - | 4 | 60 | 0 | - | 0 | - | 0 | - |
| Share issues / (repurchases) | - | - | 0 | 0 | 57 | - | 0 | - | 79 | - |
| Dividends paid | - | - | 0 | 0 | 0 | - | 0 | - | 0 | - |
| Other cash from financing | - | - | 0 | 0 | 0 | - | 0 | - | 0 | - |
| Cash from financing activities | - | - | 4 | 60 | 57 | -5.6 | 0 | - | 79 | - |
| Cash flow chge in cash & equivalents | - | - | 4 | 48 | 30 | - | (31) | - | 45 | - |
| FX / non cash items | - | - | - | 10 | (6) | - | 0 | - | (1) | - |
| Bal sheet chge in cash & equivalents | - | - | - | 58 | 24 | - | (31) | - | 44 | - |
| Core EBITDA | | - | (1) | (14) | (29) | 109.1 | (31) | 9.1 | (35) | 10.5 |
| Maintenance capital expenditure | - | - | 0 | (1) | (1) | -0.5 | (1) | 6.7 | (1) | 12.5 |
| Maintenance net working capital | - | - | 0 | 0 | 0 | - | 0 | - | 0 | - |
| Operating free cash flow, pre-tax | - | - | (1) | (14) | (29) | 103.4 | (32) | 9.0 | (35) | 10.5 |

Source: Company accounts, UBS estimates. (UBS) valuations are stated before goodwill-related charges and other adjustments for abnormal and economic items at the analysts' judgement. Note: For some companies, the data represents an extract of the full company accounts.

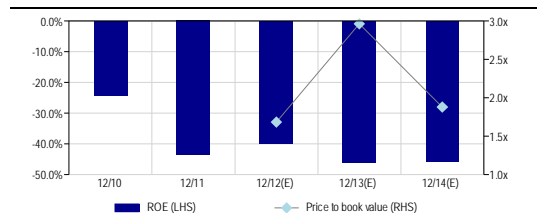
Company profile

Verastem is a Cambridge, Massachusetts-based early-stage biotechnology company focused on the discovery and development of novel small molecule drugs and companion diagnostics targeting cancer stem cells. The proprietary EMT screening platform, licensed from the Whitehead Institute at MIT, has helped select and identify the company's 3 leading candidates (VS-507, a Wnt inhibitor, and two FAK inhibitors VS-4718 and VS-5095). The company plans to begin human trials over the next 12-15 months for VS-507 and one of the two FAK inhibitors, and could be in phase II trials as early as 2015.

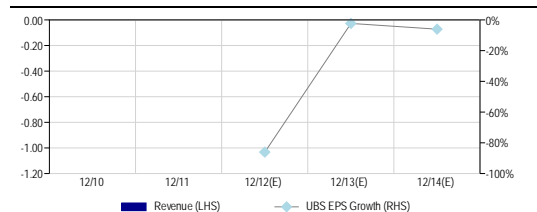
Profitability



ROE v Price to book value



Growth (UBS EPS)



| Valuation (x) | 5Yr Avg | 12/10 | 12/11 | 12/12E | 12/13E | 12/14E |
|-------------------------|---------|-------|-------|--------|--------|--------|
| P/E (local GAAP) | - | - | - | NM | NM | NM |
| P/E (UBS) | - | - | - | NM | NM | NM |
| P/CEPS | - | - | - | NM | NM | NM |
| Net dividend yield (%) | - | - | - | 0.0 | 0.0 | 0.0 |
| P/BV | - | - | - | 1.7 | 3.0 | 1.9 |
| EV/revenue (core) | - | - | - | - | - | - |
| EV/EBITDA (core) | - | - | - | -1.1 | -1.1 | -0.8 |
| EV/EBIT (core) | - | - | - | NM | NM | NM |
| EV/OpFCF (core) | - | - | - | NM | NM | NM |
| EV/op. invested capital | - | - | - | NM | NM | NM |

| Enterprise value (US\$m) | 12/10 | 12/11 | 12/12E | 12/13E | 12/14E |
|---------------------------------|-------|-------|--------|--------|--------|
| Average market cap | - | - | 105 | 105 | 105 |
| + minority interests | 0 | 0 | 0 | 0 | 0 |
| + average net debt (cash) | (4) | (33) | (74) | (71) | (77) |
| + pension obligations and other | 0 | 0 | 0 | 0 | 0 |
| - non-core asset value | 0 | 0 | 0 | 0 | 0 |
| Core enterprise value | - | - | 31 | 35 | 28 |

| Growth (%) | 5Yr Avg | 12/10 | 12/11 | 12/12E | 12/13E | 12/14E |
|--------------|---------|-------|-------|--------|--------|--------|
| Revenue | - | - | - | - | - | - |
| EBITDA (UBS) | - | - | NM | 109.1 | 9.1 | 10.5 |
| EBIT (UBS) | - | - | NM | 109.1 | 9.1 | 10.5 |
| EPS (UBS) | - | - | NM | -86.1 | -2.3 | -6.0 |
| Cash EPS | - | - | NM | -86.1 | -2.3 | -6.0 |
| Net DPS | - | - | - | - | - | - |
| BVPS | - | - | NM | -90.7 | -43.2 | 57.7 |

| Margins (%) | 5Yr Avg | 12/10 | 12/11 | 12/12E | 12/13E | 12/14E |
|----------------------------|---------|-------|-------|--------|--------|--------|
| EBITDA / revenue | - | - | - | - | - | - |
| EBIT / revenue | - | - | - | - | - | - |
| Net profit (UBS) / revenue | - | - | - | - | - | - |

| Return on capital (%) | 5Yr Avg | 12/10 | 12/11 | 12/12E | 12/13E | 12/14E |
|-----------------------|---------|--------|--------|--------|--------|--------|
| EBIT ROIC (UBS) | - | - | NM | NM | NM | NM |
| ROIC post tax | - | - | NM | NM | NM | NM |
| Net ROE | - | (24.2) | (43.7) | (40.0) | (46.1) | (45.8) |

| Coverage ratios (x) | 5Yr Avg | 12/10 | 12/11 | 12/12E | 12/13E | 12/14E |
|---------------------------------|---------|-------|-------|--------|--------|--------|
| EBIT / net interest | - | - | - | - | - | - |
| Dividend cover (UBS EPS) | - | - | - | - | - | - |
| Div. payout ratio (% , UBS EPS) | - | - | - | - | - | - |
| Net debt / EBITDA | - | 4.6 | 4.5 | 3.0 | 1.8 | 2.9 |

| Efficiency ratios (x) | 5Yr Avg | 12/10 | 12/11 | 12/12E | 12/13E | 12/14E |
|--------------------------------|---------|-------|-------|--------|--------|--------|
| Revenue / op. invested capital | - | - | 0.0 | 0.0 | 0.0 | 0.0 |
| Revenue / fixed assets | - | - | 0.0 | 0.0 | 0.0 | 0.0 |
| Revenue / net working capital | - | - | 0.0 | 0.0 | 0.0 | 0.0 |

| Investment ratios (x) | 5Yr Avg | 12/10 | 12/11 | 12/12E | 12/13E | 12/14E |
|-----------------------|---------|-------|-------|--------|--------|--------|
| OpFCF / EBIT | - | 1.0 | 1.1 | 1.0 | 1.0 | 1.0 |
| Capex / revenue (%) | - | - | - | - | - | - |
| Capex / depreciation | - | - | - | - | - | - |

| Capital structure (%) | 5Yr Avg | 12/10 | 12/11 | 12/12E | 12/13E | 12/14E |
|--------------------------------|---------|-------|-------|--------|--------|--------|
| Net debt / total equity | - | NM | NM | NM | NM | NM |
| Net debt / (net debt + equity) | - | NM | NM | NM | NM | NM |
| Net debt (core) / EV | - | - | - | NM | NM | NM |

Source: Company accounts, UBS estimates. (UBS) valuations are stated before goodwill-related charges and other adjustments for abnormal and economic items at the analysts' judgement.

Valuations: based on an average share price that year, (E): based on a share price of US\$7.18 on 08 Nov 2012 19:37 EST Market cap(E) may include forecast share issues/buybacks.

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■ Verastem

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■ Statement of Risk

We see several risks to our Buy rating on VSTM shares. We see risk to our Buy rating if VS-705, VS-4718 and/or VS-5095 have unforeseen safety, tolerability or toxicity signals or fail to yield positive phase 1b clinical results. We also see downside risk if the companion diagnostic fails to identify the appropriate population or biomarkers to better quantify benefit/risk. Finally, we see further downside risk if competition shows better data with CSC-targeting therapies, which would potentially lessen the strategic value of Verastem's assets.

■ Analyst Certification

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UBS Investment Research: Global Equity Rating Allocations

| UBS 12-Month Rating | Rating Category | Coverage ¹ | IB Services ² |
|-----------------------|-----------------|-----------------------|--------------------------|
| Buy | Buy | 50% | 31% |
| Neutral | Hold/Neutral | 41% | 31% |
| Sell | Sell | 9% | 20% |
| UBS Short-Term Rating | Rating Category | Coverage ³ | IB Services ⁴ |
| Buy | Buy | less than 1% | 33% |
| Sell | Sell | less than 1% | 0% |

1:Percentage of companies under coverage globally within the 12-month rating category.

2:Percentage of companies within the 12-month rating category for which investment banking (IB) services were provided within the past 12 months.

3:Percentage of companies under coverage globally within the Short-Term rating category.

4:Percentage of companies within the Short-Term rating category for which investment banking (IB) services were provided within the past 12 months.

Source: UBS. Rating allocations are as of 30 September 2012.

UBS Investment Research: Global Equity Rating Definitions

| UBS 12-Month Rating | Definition |
|-----------------------|---|
| Buy | FSR is > 6% above the MRA. |
| Neutral | FSR is between -6% and 6% of the MRA. |
| Sell | FSR is > 6% below the MRA. |
| UBS Short-Term Rating | Definition |
| Buy | Buy: Stock price expected to rise within three months from the time the rating was assigned because of a specific catalyst or event. |
| Sell | Sell: Stock price expected to fall within three months from the time the rating was assigned because of a specific catalyst or event. |

KEY DEFINITIONS

Forecast Stock Return (FSR) is defined as expected percentage price appreciation plus gross dividend yield over the next 12 months.

Market Return Assumption (MRA) is defined as the one-year local market interest rate plus 5% (a proxy for, and not a forecast of, the equity risk premium).

Under Review (UR) Stocks may be flagged as UR by the analyst, indicating that the stock's price target and/or rating are subject to possible change in the near term, usually in response to an event that may affect the investment case or valuation.

Short-Term Ratings reflect the expected near-term (up to three months) performance of the stock and do not reflect any change in the fundamental view or investment case.

Equity Price Targets have an investment horizon of 12 months.

EXCEPTIONS AND SPECIAL CASES

UK and European Investment Fund ratings and definitions are: Buy: Positive on factors such as structure, management, performance record, discount; Neutral: Neutral on factors such as structure, management, performance record, discount; Sell: Negative on factors such as structure, management, performance record, discount.

Core Banding Exceptions (CBE): Exceptions to the standard +/-6% bands may be granted by the Investment Review Committee (IRC). Factors considered by the IRC include the stock's volatility and the credit spread of the respective company's debt. As a result, stocks deemed to be very high or low risk may be subject to higher or lower bands as they relate to the rating. When such exceptions apply, they will be identified in the Company Disclosures table in the relevant research piece.

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UBS Securities LLC: Matthew Roden, PhD; Leah Batkiewicz, PhD; Andrew Peters.

Company Disclosures

| Company Name | Reuters | 12-mo rating | Short-term rating | Price | Price date |
|---------------------------------|---------|--------------|-------------------|----------|-------------|
| Verastem ^{2, 4, 6, 16} | VSTM.O | Buy | N/A | US\$7.18 | 08 Nov 2012 |

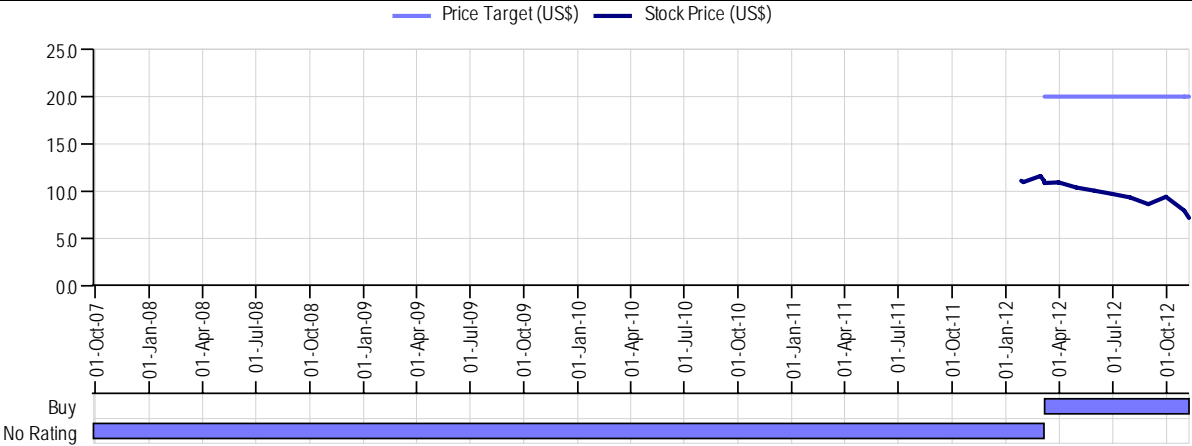
Source: UBS. All prices as of local market close.

Ratings in this table are the most current published ratings prior to this report. They may be more recent than the stock pricing date

2. UBS AG, its affiliates or subsidiaries has acted as manager/co-manager in the underwriting or placement of securities of this company/entity or one of its affiliates within the past 12 months.
4. Within the past 12 months, UBS AG, its affiliates or subsidiaries has received compensation for investment banking services from this company/entity.
6. This company/entity is, or within the past 12 months has been, a client of UBS Securities LLC, and investment banking services are being, or have been, provided.
16. UBS Securities LLC makes a market in the securities and/or ADRs of this company.

Unless otherwise indicated, please refer to the Valuation and Risk sections within the body of this report.

Verastem (US\$)



Source: UBS; as of 08 Nov 2012

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