

July 11, 2012

Market Outperform / Speculative Risk

Looking Ahead to Tomorrow's R&D Update from Verastem

MARKET DATA 7/10/2012

Price	\$10.68
Exchange	NASDAQ
Target Price	\$19.00
52 Wk Hi - Low	\$12.24 - \$8.89
Market Cap(MM)	\$224.9
EV(MM)	\$183.8
Shares Out (MM)	21.1
Public Mkt Float (MM)	21.1
Avg. Daily Vol	16,350
Short Interest	426,046

BALANCE SHEET METRICS

Cash (MM)	\$47.8
LTD (MM)	\$0.0
Total Debt/Capital	NA
Cash/Share	\$30.67
Book Value(MM)	NA
Book Value/Share	\$5.44

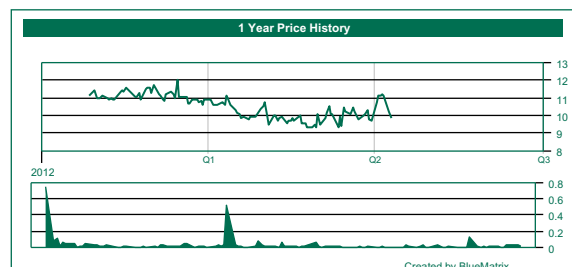
Cash (MM): Includes cash and equivalents, short-term and long-term securities.

EARNINGS DATA (\$)

FY - Dec	2011E	2012E	2013E
Q1 (Mar)	--	(0.47)A	--
Q2 (Jun)	--	(0.49)	--
Q3 (Sep)	--	(0.52)	--
Q4 (Dec)	(4.01)	(0.54)	--
Full Year EPS	(10.59)	(2.04)	(1.64)

INDICES

DJIA	12,653.1
SP-500	1,341.5
NASDAQ	2,585.5
NBI	1,361.9



Tomorrow we will be attending Verastem's first annual Research and Development day (July 12, 9:00am – 12:00pm). While we are sure to follow up with our take immediately after the event, interested investors will be able to join the presentation via webcast here (<http://edge.media-server.com/m/p/ijf69diw/lan/en>).

Here is what to expect. The agenda for tomorrow's event is straightforward with a set of presentations that should be rather familiar to those following the company's progress. Scientific co-founder Dr. Robert A. Weinberg will open the morning with a seminar on the cancer stem cell (CSC) hypothesis, the epithelial-to-mesenchymal transition (EMT), and their implications for not only for cancer metastasis, but tumor resistance to current chemotherapy. Following Dr. Weinberg's presentation, the Company is expected to give an overview of each of its three ongoing development programs in i) Wnt ii) FAK and iii) PI3K/mTOR. As a reminder, VSTM's lead development program is VS-507, a novel inhibitor of Wnt pathway signaling, currently undergoing IND-enabling toxicology assessment and slated to begin Phase I testing by year-end 2012. For the VS-4718/5095 FAK program, scheduled to begin a Phase I trial in 1H13, we hope to learn which the two compounds within the chemical class will form the a basis of an IND. Last, and perhaps most revelatory, the company will outline for the first time development plans for the PI3K/mTOR program, which was acquired through a deal with S*Bio in 1Q12.

New data from VSTM's scientific co-founder subtly underscores the savvy behind VSTM's PI3K/mTOR acquisition. Heading into the VSTM R&D day, it is worth noting some new research from the lab of Dr. Weinberg that was recently published in the journal *Cancer Discovery* (entitled 'Cancer-stimulated mesenchymal stem cells create a carcinoma stem-cell niche via Prostaglandin E₂ signaling'). The paper goes a step further in elucidating the paracrine signaling mechanisms taking place in the stromal microenvironment that can revert differentiated carcinoma cells into a stem-cell like state. In brief, the paper shows that in response to paracrine IL-1 signals from colon carcinoma cells, neighboring mesenchymal stem cells (MSCs) in the stroma express elevated levels of prostaglandin E₂ (PGE₂), which in turn stimulate and coordinate with cytokines secreted by MSCs to influence the carcinoma cells. The net effect to the carcinoma cells are increases in beta-catenin signaling, other CSC markers and tumor initiating potential. Importantly to VSTM, the paper shows that PGE₂'s effect on beta-catenin is mediated by PI3K/AKT activation and is mutable with inhibitors of pathway. In short, the work is perhaps the recent most mechanistic example of how EMT and CSCs could be effectively targeted with PI3K inhibitors – the type of example we expect to see more of from VSTM Thursday.

We maintain our Market Outperform rating for VSTM shares and \$19 price target. We derive our price target through a combination of methodologies, including a DCF-based valuation of \$17 and a CAGR valuation of \$22. Risks to our valuation include the risk of clinical failure with VS-507 and/or VS-4718/5095 for reasons of safety or inactivity. In our view, the value of VSTM shares will be primarily milestone-driven over the next six to twelve months, as VS-507 completes IND tox assessment.

Table 1. Upcoming Milestones

Milestone	Date
• Peer-review scientific journal publication	2H 2012
• IND filing of VS-507 with FDA and initiation of Phase I trial	2H 2012
• IND filing of VS-4718/VS-5095 with the FDA and initiation of Phase I trial	1H 2013

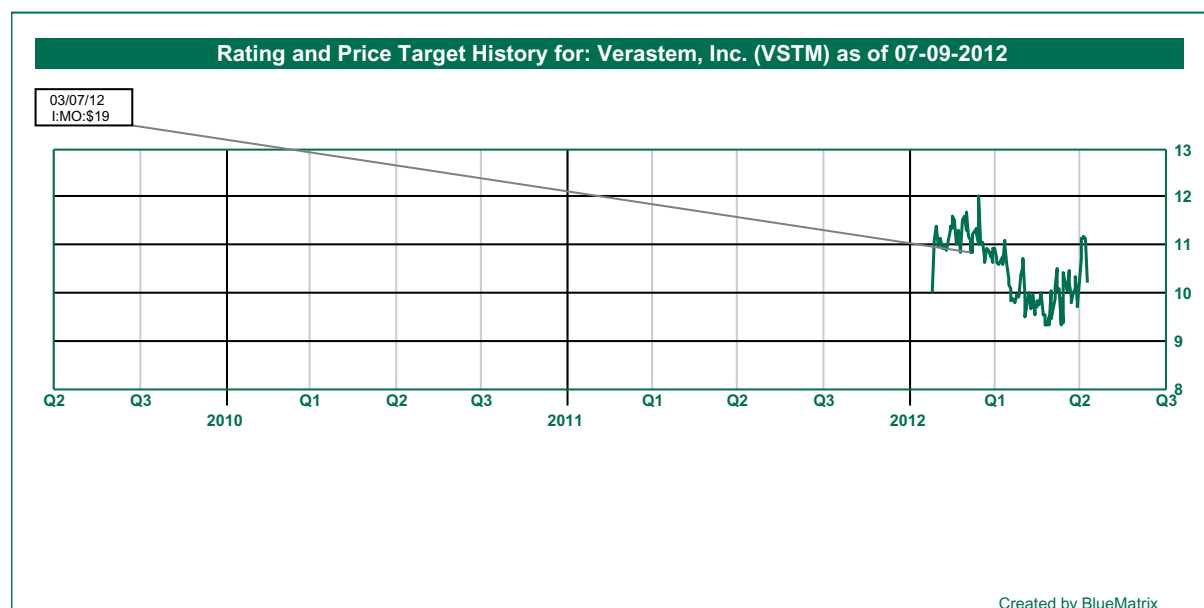
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RETURN ASSESSMENT

- **Market Outperform (Buy):** The common stock of the company is expected to outperform a passive index comprised of all the common stock of companies within the same sector, as defined by First Call.
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- **Speculative -** The common stock risk level is significantly greater than market risk. The stock price of these equities is exceptionally volatile.
- **Aggressive -** The common stock risk level is materially higher than market level risk. The stock price is typically more volatile than the general market.
- **Moderate -** The common stock is moderately risky, or equivalent to stock market risk. The stock price volatility is typically in-line with movements in the general market.



RATING SUMMARY

Distribution of Ratings Table				
Rating	Count	Percent	IB Serv./Past 12 Mos	
			Count	Percent
Market Outperform(MO)	27	31.40%	3	11.11%
Market Perform(MP)	14	16.28%	0	0.00%
Market Underperform(MU)	3	3.49%	0	0.00%
Under Review(UR)	42	48.84%	9	21.43%
Total	86	100%	12	100%

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