

## UBS Investment Research

### Verastem

## Ovarian Program to Start Earlier

### ■ What's new? Ovarian clinical path outlined at UBS Life Sciences Conf.

At the 2012 UBS Global Life Sciences Conference, Verastem management offered a (new) accelerated clinical development plan in ovarian and breast cancer for FAK inhibitor VS-6063. A ph1 dose escalating trial in combination with paclitaxel in platinum-resistant ovarian cancer patients is now expected to start 1H13 (vs. 1H14 outlined at recent R&D day), and a proof-of-concept ph2 can now begin as early as 2014. While the ph1 trial may also enroll a subset of breast cancer patients, the ph2 portion will focus on ovarian cancer, potentially a significant opportunity.

### ■ Fast-to-market mesothelioma indication is still the lead program

While the company has not yet finalized the ph2 trial design in mesothelioma, we believe by targeting a disease highly enriched in cancer stem cells and with a clear link/biomarker to FAK expression, the strategy presents a viable fast to market path forward. Further, given the high unmet medical need, a well-designed ph2 trial would likely be registerable in our view. We look to near-term data from both Verastem and GlaxoSmithKline on FAK inhibition to support use in this setting.

### ■ Thoughts: VS-6063 charging ahead; remaining pipeline interesting as well

Although FAK inhibition is clearly the lead program, we believe the core R&D focus on cancer stem cells through the proprietary screening platform will continue to yield interesting targets (e.g. PI3K/mTOR inhibitor VS-5584) and could be expanded into other CSC rich tumor types and related pathways.

### ■ Valuation: Buy with \$20 price target

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

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	-	-	-2.5	-2.4	-1.9
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\$9.84 on 19 Sep 2012 18:41 EST

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## Global Equity Research

Americas

Biotechnology

12-month rating **Buy**  
**Unchanged**

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

Price **US\$9.84**

RIC: VSTM.O BBG: VSTM US

19 September 2012

### Trading data

52-wk range	US\$12.01-8.02
Market cap.	US\$0.14bn
Shares o/s	14.7m (COM)
Free float	29%
Avg. daily volume ('000)	13
Avg. daily value (m)	US\$0.1

### Balance sheet data 12/12E

Shareholders' equity	US\$0.08bn
P/BV (UBS)	2.3x
Net Cash (debt)	US\$0.09bn

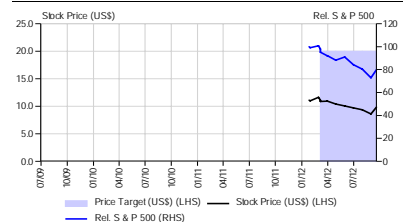
### Forecast returns

Forecast price appreciation	+103.3%
Forecast dividend yield	0.0%
Forecast stock return	+103.3%
Market return assumption	5.3%
Forecast excess return	+98.0%

### 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)	(0.36) (4.56)
12/12E	(1.47)	(1.50)
12/13E	(1.44)	(1.60)

### Performance (US\$)



Source: UBS

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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	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

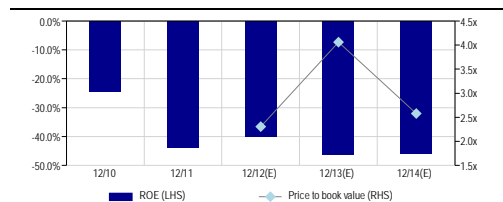
Source: Company accounts, UBS estimates. (UBS) valuations are stated before goodwill-related charges and other adjustments for abnormal and economic items at the analysts' judgement. Note: For some companies, the data represents an extract of the full company accounts.

## Company profile

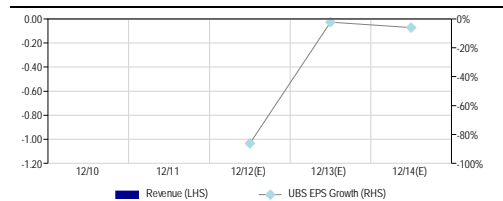
Verastem is a Cambridge, Massachusetts-based early-stage biotechnology company focused on the discovery and development of novel small molecule drugs and companion diagnostics targeting cancer stem cells. The proprietary EMT screening platform, licensed from the Whitehead Institute at MIT, has helped 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	-	-	-	2.3	4.1	2.6
EV/revenue (core)	-	-	-	-	-	-
EV/EBITDA (core)	-	-	-	-2.5	-2.4	-1.9
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	-	-	145	145	145
+ 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	-	-	71	74	67

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	(96.0)	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\$9.84 on 19 Sep 2012 18:41 EST Market cap(E) may include forecast share issues/buybacks.

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## ■ Verastem

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.

## ■ 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.

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UBS 12-Month Rating	Rating Category	Coverage <sup>1</sup>	IB Services <sup>2</sup>
Buy	Buy	55%	33%
Neutral	Hold/Neutral	37%	31%
Sell	Sell	8%	16%
UBS Short-Term Rating	Rating Category	Coverage <sup>3</sup>	IB Services <sup>4</sup>
Buy	Buy	less than 1%	0%
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 June 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.

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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 <sup>2, 4, 6, 16</sup>	VSTM.O	Buy	N/A	US\$9.84	19 Sep 2012

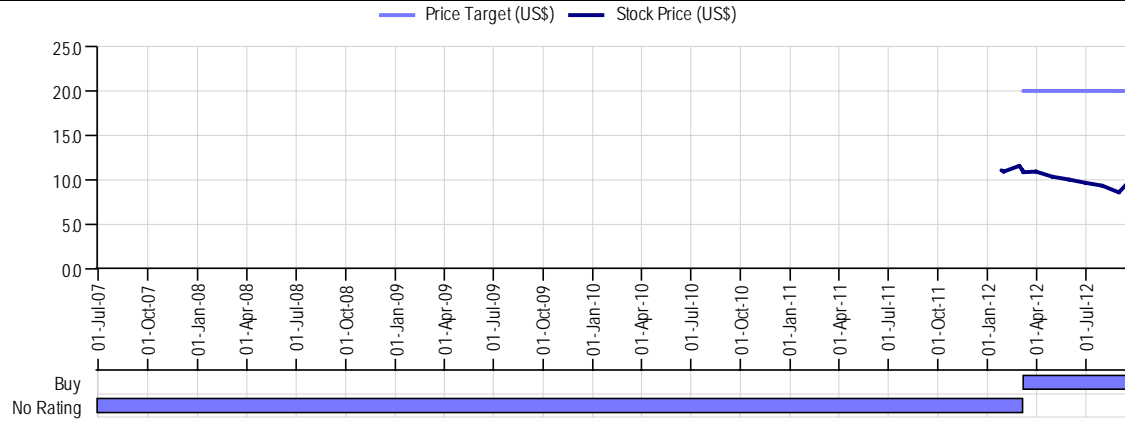
Source: UBS. All prices as of local market close.

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

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

Verastem (US\$)



Source: UBS; as of 19 Sep 2012



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