

February 14, 2013

# Tesaro

(TSRO-NASDAQ)

**Stock Rating:** Outperform**Industry Rating:** Outperform

## Biotechnology

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## Pipeline Visibility Accelerating and CINV Phase 3 Approaches

### Event

Tesaro reported 4Q12 operating results earlier today and provided an update on key initiatives on a call with investors. Non-GAAP loss per share of \$0.70 was generally in line with \$(0.65) consensus, and TSRO ended 2012 with \$125M in cash. With focus on pipeline progress, the rolapitant phase 3 program in chemotherapy induced nausea and vomiting (CINV) remains on track for data release in 2H13 with two studies in patients receiving highly emetogenic chemotherapy (HEC) and one study in patients receiving moderately emetogenic chemotherapy (MEC). Progress with earlier-stage programs was also described with ALK-inhibitor TSR-011 moving into a fourth dosing cohort where inhibition of ALK is expected and where ALK+ patients will be studied, and where phase 3 initiation by mid-year was described for PARP inhibitor niraparib in patients with platinum sensitive, relapsed serous ovarian cancer. The phase 3 study for niraparib was of particular focus on the call, and TSRO described a 360-patient maintenance study randomized 2:1, niraparib vs placebo, in patients achieving response with platinum agent and equally divided between BRAC+ and BRCA- status.

### Impact

We are reiterating our Outperform rating on shares of TSRO, following a better-than-expected 4Q12 update. Progress with niraparib from phase 1 dose escalation to a pivotal phase 3 puts the company ahead of competitors with significant prior validation of PARP inhibition in advanced ovarian cancer. With phase 3 data for rolapitant and early data for ALK+ patients with TSR-011 in 2H13, we see several opportunities for meaningful value appreciation in TSRO shares.

### Forecasts

Our 2013 forecast is for a loss per share of \$2.35.

### Valuation

Our \$22 target is based on 20x our 2017E EPS of \$2.35 discounted 25%.

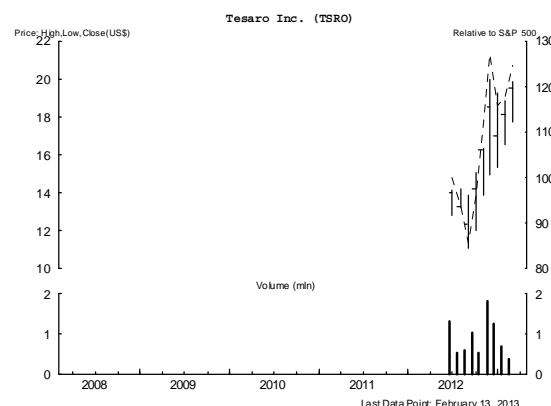
### Recommendation

We rate Tesaro Outperform.

### Securities Info

<b>Price (13-Feb)</b>	<b>\$19.48</b>	<b>Target Price</b>	<b>\$22</b>
52-Wk High/Low	\$20/\$11	Dividend	--
Mkt Cap (mm)	\$520	Yield	--
Shs O/S (mm, BASIC)	26.7	Float O/S (mm)	8.5
Options O/S (mm)	na	ADVol (30-day, 000s)	37

### Price Performance



### Valuation/Financial Data

(FY-Dec.)	2011A	2012A	2013E	2014E
EPS GAAP	-\$31.90	-\$4.51	-\$2.35↓	-\$2.57↓
P/E			nm	nm
First Call Cons.		-\$3.64	-\$2.38	-\$2.13
FCF	-\$14.24	-\$47.73	-\$66.00	na
P/FCF			nm	na
EBITDA (\$mm)	-\$15	-\$62	-\$65	-\$81
EV/EBITDA			nm	nm
Rev. (\$mm)	\$0	\$0	\$0	na
EV/Rev			na	na
<b>Quarterly EPS</b>	<b>1Q</b>	<b>2Q</b>	<b>3Q</b>	<b>4Q</b>
2012A	-\$0.70	-\$21.31	-\$0.52	-\$0.70
2013E	-\$0.53	-\$0.58	-\$0.60	-\$0.65

### Balance Sheet Data (30-Sep)

Net Debt (\$mm)	-\$125	Total Debt/EBITDA	nm
Total Debt (\$mm)	\$0	EBITDA/IntExp	na
Net Debt/Cap.	nm	Price/Book	4.5x

Notes: Quarterly EPS may not sum due to share count. All values in US\$.

Source: BMO Capital Markets estimates, Bloomberg, Thomson Reuters, and IHS Global Insight.

### Changes

#### Annual EPS

2013E -\$2.30 to -\$2.35  
2014E -\$2.51 to -\$2.57

#### Quarterly EPS

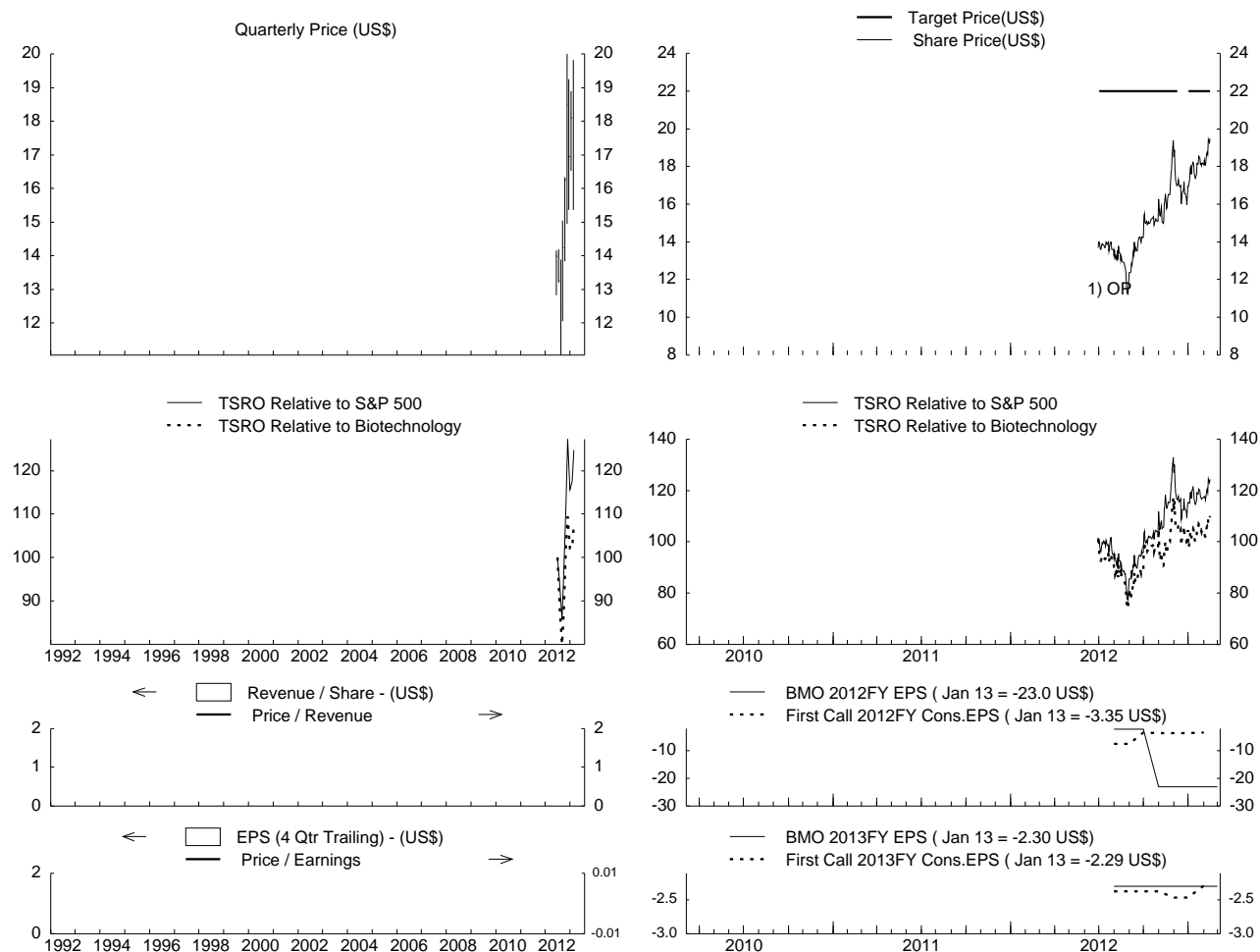
Q1/13E na to -\$0.53  
Q2/13E na to -\$0.58  
Q3/13E na to -\$0.60  
Q4/13E na to -\$0.65

## Exhibit 1: TSRO Income Statement 2011-2017E

INCOME STATEMENT (\$M)	2012A	1Q13E	2Q13E	3Q13E	4Q13E	2013E	2014E	2015E	2016E	2017E
<b>REVENUES</b>										
Product Revenues	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 43.3	\$ 129.9	\$ 318.4
Collaborative Revenues/Milestones	-	-	-	-	-	-	-	-	-	-
<b>Total Revenues</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$ 43.3</b>	<b>\$ 129.9</b>	<b>\$ 318.4</b>
<b>EXPENSES (GAAP)</b>										
Cost of Goods Sold (COGS)	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 0.2	\$ 0.4	\$ 0.7
R&D Expense	47.2	12.2	13.2	14.0	14.9	54.3	66.2	78.1	90.4	100.4
SG&A Expense	6.7	2.1	2.6	2.6	3.2	10.5	14.5	53.0	69.0	114.0
Acquired In-Process R&D	8.0	-	-	-	-	-	-	-	-	-
<b>TOTAL EXPENSES</b>	<b>61.9</b>	<b>14.3</b>	<b>15.8</b>	<b>16.6</b>	<b>18.1</b>	<b>64.8</b>	<b>80.7</b>	<b>131.2</b>	<b>159.8</b>	<b>215.1</b>
<b>Operating Income</b>	<b>(61.9)</b>	<b>(14.3)</b>	<b>(15.8)</b>	<b>(16.6)</b>	<b>(18.1)</b>	<b>(64.8)</b>	<b>(80.7)</b>	<b>(87.9)</b>	<b>(29.8)</b>	<b>103.3</b>
Depreciation and Amortization	-	-	-	-	-	-	-	-	-	-
EBIT	(61.9)	(14.3)	(15.8)	(16.6)	(18.1)	(64.8)	(80.7)	(87.9)	(29.8)	103.3
Interest Income	0.2	0.2	0.2	0.1	0.1	0.6	0.1	(0.0)	(0.1)	(0.1)
Interest Expense	-	-	-	-	-	-	-	-	-	-
Other Expense	-	-	-	-	-	-	-	-	-	-
Interest and Other (net)	\$ 0.2	\$ 0.2	\$ 0.2	\$ 0.1	\$ 0.1	\$ 0.6	\$ 0.1	\$ (0.0)	\$ (0.1)	\$ (0.1)
Pre-Tax Income	(61.8)	(14.1)	(15.6)	(16.5)	(18.0)	(64.2)	(80.6)	(88.0)	(29.9)	103.2
Income Taxes	-	-	-	-	-	-	-	-	-	15.5
<b>Net Income (GAAP)</b>	<b>(61.8)</b>	<b>(14.1)</b>	<b>(15.6)</b>	<b>(16.5)</b>	<b>(18.0)</b>	<b>(64.2)</b>	<b>(80.6)</b>	<b>(88.0)</b>	<b>(29.9)</b>	<b>87.8</b>
EPS (GAAP) (basic)	\$ (4.51)	\$ (0.53)	\$ (0.58)	\$ (0.60)	\$ (0.65)	\$ (2.35)	\$ (2.57)	\$ (2.60)	\$ (0.85)	\$ 2.35
<b>EPS (GAAP) (diluted)</b>	<b>\$ (4.51)</b>	<b>\$ (0.53)</b>	<b>\$ (0.58)</b>	<b>\$ (0.60)</b>	<b>\$ (0.65)</b>	<b>\$ (2.35)</b>	<b>\$ (2.57)</b>	<b>\$ (2.60)</b>	<b>\$ (0.85)</b>	<b>\$ 2.35</b>
Total of Reconciliation Items	3.0	2.0	2.0	2.0	2.0	8.0	8.0	8.0	8.0	8.0
Net Income (Non-GAAP)	\$ (58.8)	\$ (12.1)	\$ (13.6)	\$ (14.5)	\$ (16.0)	\$ (56.2)	\$ (72.6)	\$ (80.0)	\$ (21.9)	\$ 95.8
Impact of Adjustments to EPS	0.49	0.07	0.07	0.07	0.07	0.29	0.26	0.24	0.23	0.22
EPS (Non-GAAP) (basic)	\$ (22.25)	\$ (0.45)	\$ (0.50)	\$ (0.53)	\$ (0.58)	\$ (2.06)	\$ (2.31)	\$ (2.36)	\$ (0.63)	\$ 2.56
EPS (Non-GAAP) (diluted)	\$ (22.25)	\$ (0.45)	\$ (0.50)	\$ (0.53)	\$ (0.58)	\$ (2.06)	\$ (2.31)	\$ (2.36)	\$ (0.63)	\$ 2.56
Weighted average shares outstanding (basic)	13.7	26.9	27.1	27.4	27.7	27.3	31.3	33.8	35.2	37.2
Weighted average shares outstanding (diluted)	13.7	26.9	27.1	27.4	27.7	27.3	31.3	33.8	35.2	37.2

Source: Company reports and BMO Capital Markets

## Tesar Inc. (TSRO)



FYE (Dec.)	EPS US\$	P/E Hi - Lo	DPS US\$	Yield% Hi - Lo	Payout %	BV US\$	P/B Hi - Lo	ROE %	TSRO - Rating as of 23-Jul-12 = OP		
Range*:		na na		NC		>15 >15			Date	Rating Change	Share Price
Current*	ND	NC	0.00	0.0	na	2.6	7.2	na	1 23-Jul-12	NR to OP	\$13.90

\* Current EPS is the 4 Quarter Trailing to Q3/2012.

\* Valuation metrics are based on high and low for the fiscal year.

\* Range indicates the valuation range for the period presented above.

Last Price ( February 13, 2013): \$19.48  
Sources: IHS Global Insight, Thomson Reuters, BMO Capital Markets.

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**Methodology:** We arrive at our price target by applying a 20x multiple to 2017 GAAP EPS estimate of \$2.35 and discounting 25%.

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Rating Category	BMO Rating	BMOCM US Universe*	BMOCM US IB Clients**	BMOCM US IB Clients***	BMOCM Universe****	BMOCM IB Clients*****	Starmine Universe
Buy	Outperform	37.0%	17.7%	52.9%	38.5%	50.5%	54.0%
Hold	Market Perform	60.7%	9.6%	47.1%	57.3%	48.4%	40.6%
Sell	Underperform	2.4%	0.0%	0.0%	4.2%	1.0%	5.4%

\* Reflects rating distribution of all companies covered by BMO Capital Markets Corp. equity research analysts.

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OP = Outperform - Forecast to outperform the market;

Mkt = Market Perform - Forecast to perform roughly in line with the market;

Und = Underperform - Forecast to underperform the market;

(S) = speculative investment;

NR = No rating at this time;

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