August 7, 2013

OUTPERFORM

Reason for report:

EARNINGS

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LEERINK SWANN

HEALTHCARE EQUITY RESEARCH

RECEPTOS, INC.

2Q:13 Updates with Pipeline on Track and Bright Future Ahead; Reit OP & $30 PT

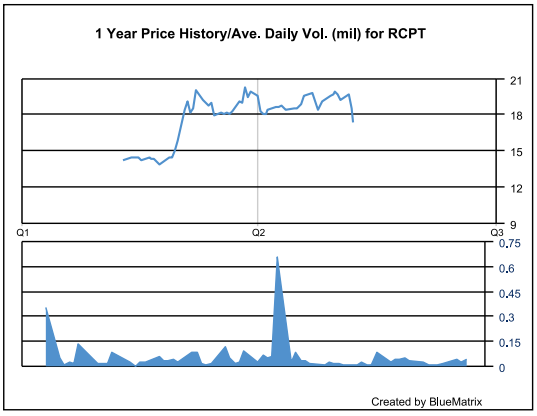
• **Bottom Line:** 2Q:13 updates demonstrate RCPT pipeline programs are advancing steadily and remain on track. We continue to model attractive revenue for lead product RPC-1063 only in Relapsing MS (RMS), leaving potential for significant further upside from potential supplemental indications such as Ulcerative Colitis (UC). Advancement to the clinic of RPC-4046, RCPT's 2nd pipeline candidate, should provide further risk diversification with potential longer-term upside. Multiple catalysts are on target over the next 12 months including: (1) 4Q:13 ECTRIMS Phase I RPC-1063 data; (2) 4Q:13 RPC-1063 interim Phase II RMS analysis triggering initiation of the first Phase III trial; (3) 1H:14 RPC-1063 large pharma partnership; and (4) mid-2014 RPC-1063 top-line Phase II data in UC and RMS. We reiterate our Outperform rating and $30 price target.

• **RCPT reported 2Q:13 collaborative revenue of $1.2M and EPS of ($0.98) vs. our estimates of $0.5M and ($0.51), respectively.** R&D expense was $9.4M, higher than our $7.7M estimate. G&A expense of $1.6M was in line with our expectation. RCPT ended 2Q:13 with ~$91M (~$4.98 cash/share) in cash and cash equivalents.

• **Beyond an attractive base of revenue in RMS (see our MS MEDACorp Survey Industry note), we continue to be very interested in potential upside RPC-1063 could experience in secondary progressive MS (SPMS).** We believe potential pre-2018 approval catalysts that could shape RPC-1063's potential in SPMS include the outcome of Tysabri's SPMS Phase III ASCEND trial and, in 2016, the outcome of NVS's (OP) S1P receptor modulator (S1P-RM) Siponimod Phase III SPMS EXPAND trial. We remain biased that the ASCEND trial will fail (see our Therapeutics Conference MS note) and could begin to erode Tysabri use in the SPMS setting leaving a void for Gilenya (first generation S1P-RM) to fill ~2015. A positive NVS Siponimod (second generation S1P-RM) result in the EXPAND trial would likely lead to FDA approval shortly afterward given no effective therapies for SPMS and reasonably lead to robust market share at least in the SPMS setting. With RPC-1063 demonstrating an emerging "best-in-class" S1P-RM profile, we anticipate it would benefit from use in SPMS with either or both a negative ASCEND and positive EXPAND trial result.

• **While RCPT has a clear path to approval for RPC-1063 in RMS, we believe there is unleveraged opportunity that could emerge based on choice of different active comparator arms in the second Phase III pivotal RMS trial.** Given a dynamic MS market, swapping the current choice of Avonex for Tecfidera (emerging as potential market leader) or Copaxone (possibly generic soon) could have advantages a prospective RPC-1063 partner might appreciate in terms of deal economics.

Key Stats:	**(NASDAQ:RCPT)**
S&P 600 Health Care Index:	**1,101.14**
Price:	**$17.37**
Price Target:	$30.00
Methodology:	DCF analysis
52 Week High:	$25.00
52 Week Low:	$13.00
Shares Outstanding (mil):	18.3
Market Capitalization (mil):	$317.9
Book Value/Share:	$0.26
Cash Per Share:	$4.98
Dividend (ann):	NA



Dec Yr	1Q	2Q	3Q	4Q	FY Rev	1Q	2Q	3Q	4Q	FY EPS	P/E
2012A	**--**	**--**	**--**	**--**	**$8.6**	**--**	**--**	**--**	**--**	**($13.73)**	**NM**
2013E - New	**$1.5A**	**$1.2A**	**$1.3**	**$1.2**	**$5.1**	**($5.46)A**	**($0.98)A**	**($0.64)**	**($0.77)**	**($7.85)**	**NM**
2013E - Old	$0.5	$0.5	$0.5	$0.5	$1.9	($0.88)	($0.51)	($0.54)	($0.83)	($2.76)	NM
2014E - New	**--**	**--**	**--**	**--**	**0.0**	**--**	**--**	**--**	**--**	**($2.43)**	**NM**
2014E - Old	--	--	--	--	$0.6	--	--	--	--	($2.16)	NM

Source: Company Information and Leerink Swann LLC Research
Revenues in $000s.

Please refer to pages 5 - 8 for Important Disclosures, Price Charts and Analyst Certification.

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INVESTMENT THESIS

We rate RCPT Outperform. We believe RCPT shares are poised to appreciate near/longer term driven by clinical progress and commercialization of lead compound RPC-1063. Compared to other S1P1 compounds, RPC-1063 is earlier stage but emerging as "best in class." In 2014, RCPT plans to sign an RPC-1063 partnership with large pharma, announce RPC-1063 Phase II data in relapsing MS (RMS) and Ulcerative Colitis (UC) and start two pivotal Phase III RMS trials. We currently assume a 30% probability of approval for RPC-1063 in RMS in 2018. The 2Q13 MEDACorp MS Survey suggests that if approved in 2018, RPC-1063 would take significant market share from Gilenya (~58%), Tecfidera (~13%) and Tysabri (15%) that could be worth $1.2B in U.S. revenue in 2019E. Core RPC-1063 Intellectual Property (IP) expires in 2029 but Gilenya (NVS) currently goes off patent in 2019. Assuming generic pricing starts in 2020, we model peak risk adjusted RPC-1063 WW revenues of ~$640M (or $2.1B non-risk adjusted) which leads to our base case NPV calculation of $520M (including cash), based only on approval and use in RMS.

Change in Estimates

We modified our model based on RCPT's earnings release today. Our full-year 2013E revenue changed from $1.9M to $5.1M and EPS changed from ($2.76) to ($7.85). Our 2014E EPS changed from ($2.16) to ($2.43).

Milestones

Product	Partner	Indication	Phase	Timing	Milestone
RPC-1063 (S1P1)	Proprietary	Relapsing MS	Phase III	4Q13/1Q14	Initiate Phase III portion of 1st pivotal (RPC01-201), (with SPA)
				4Q13	ECTRIMS updates (i.e. TQTc data)
				2014	**Partnership announcement**
				2H14	Initiate 2nd pivotal Phase III RMS trial (with SPA)
				Mid-2014	**Phase II data of 1st pivotal (RPC01-201)**
				2017	2nd pivotal Phase III RMS trial data
				YE17	NDA submission
				2H18	FDA Approval
		Ulcerative Colitis (UC)	Phase II	1H14	Complete trial enrollment
				3Q14	**Phase II UC trial data (might serve as 1 of 2 pivotals)**
				2015	Initiate pivotal trial (possibly maintenance)
				2018	Possible NDA submission
RPC-4046 (IL-13)	ABBV	Eosinophilic Esophagitis (EoE)	Phase II	4Q13/1Q14	Submit IND
				1H14	Initiate Phase II data
				2H15	**Phase II trial data**

Source: Company Reports, Leerink Swann LLC estimates

VALUATION

We calculate a $30 DCF price target for RCPT in the next 12 months based on a discounted cash flow (DCF) analysis. We apply a discount rate of 11% and a terminal growth rate of 1% which translates to a 10x terminal multiple which we believe is comparable to biotechnology companies in a similar development stage. We currently assume a 30% probability of approval for RPC-1063 in RMS in 2018. The 2Q13 MEDACorp MS Survey suggests that if approved in 2018, RPC-1063 would take significant market share from Gilenya (~58%), Tecfidera (~13%) and Tysabri (15%) that could be worth $1.2B in U.S. revenue in 2019E. Core RPC-1063 Intellectual Property (IP) expires in 2029, but Gilenya (NVS) currently goes off patent in 2019. Assuming generic pricing starts in 2020, we model peak risk adjusted RPC-1063 WW revenues of ~$640M (or $2.1B non-risk adjusted) which leads to our base case NPV calculation of $520M (including cash), based only on approval and use in RMS.

RISKS TO VALUATION

An investment in RCPT is fundamentally a high-risk, high-reward investment, in our opinion. RCPT may face significant clinical, regulatory, and commercial risks for pipeline products. Most important is risk associated with potential failure of RPC-1063 (Relapse Remitting Multiple Sclerosis) to obtain regulatory approvals and capture market share in the MS treatment paradigm. RPC-1063 is also the earliest among other S1P receptor modulators. There is also risk that evolving therapeutic landscapes could render RCPT pipeline compounds non-competitive or less valuable once approved.

RCPT P&L ($000s, except per share data)	2012A	1Q13A	2Q13A	3Q13E	4Q13E	2013E	2014E	2015E	2016E	2017E	2018E	2019E	2020E	2021E	2022E	2023E	2024E	2025E
Revenues																		
RPC1063 WW Revenue											$316,680	$1,088,253	$569,241	$768,848	$1,003,905	$1,257,093	$1,470,700	$1,664,873
Risk Adjusted RPC1063 WW Revenue											**$95,004**	**$326,476**	**$170,772**	**$230,654**	**$301,171**	**$377,128**	**$441,210**	**$499,462**
RPC4046																		
Collaborative Revenue	$8,647	$1,488	$1,238	$1,250	$1,150	$5,126	-	-	-	-	-	-	-	-	-	-	-	-
Total Revenue	**$8,647**	**$1,488**	**$1,238**	**$1,250**	**$1,150**	**$5,126**	**-**	**-**	**-**	**-**	**$95,004**	**$326,476**	**$170,772**	**$230,654**	**$301,171**	**$377,128**	**$441,210**	**$499,462**
Costs and Expenses																		
Probability Adjusted COGS	-	-	-	-	-	-	-	-	-	-	$14,251	$48,971	$25,616	$41,518	$54,211	$67,883	$79,418	$74,919
R&D	$22,927	$8,020	$9,441	$11,114	$13,250	$41,825	$50,190	$85,323	$110,919	$124,230	$134,168	$138,193	$142,339	$146,609	$149,541	$152,532	$155,583	$158,694
SG&A (Risk Adjusted from Time of RPC1063 Launch)	$3,430	$1,062	$1,589	$1,900	$2,100	$6,651	$7,316	$8,048	$8,852	$30,984	$39,000	$43,400	$45,570	$47,849	$50,241	$52,753	$55,391	$58,160
Total Costs and Expenses	**$26,357**	**$9,082**	**$11,030**	**$13,014**	**$15,350**	**$48,476**	**$57,506**	**$93,370**	**$119,772**	**$155,213**	**$187,419**	**$230,564**	**$213,525**	**$235,975**	**$253,993**	**$273,168**	**$290,391**	**$291,774**
Operating Income (EBIT)	**($17,710)**	**($7,594)**	**($9,792)**	**($11,764)**	**($14,200)**	**($43,350)**	**($57,506)**	**($93,370)**	**($119,772)**	**($155,213)**	**($92,415)**	**$95,912**	**($42,752)**	**($5,321)**	**$47,179**	**$103,960**	**$150,819**	**$207,688**
Y/Y growth																		
Income Before Taxes	**($17,710)**	**($9,649)**	**($9,918)**	**($11,764)**	**($14,200)**	**($45,531)**	**($57,506)**	**($93,370)**	**($119,772)**	**($155,213)**	**($92,415)**	**$95,912**	**($42,752)**	**($5,321)**	**$47,179**	**$103,960**	**$150,819**	**$207,688**
Provision for Taxes							-	-	-	-	-	-	-	-	-	-	-	(16,192)
Net income	**($17,710)**	**($9,649)**	**($9,918)**	**($11,764)**	**($14,200)**	**($45,531)**	**($57,506)**	**($93,370)**	**($119,772)**	**($155,213)**	**($92,415)**	**$95,912**	**($42,752)**	**($5,321)**	**$47,179**	**$103,960**	**$150,819**	**$223,880**
EPS (LPS) Basic	**($13.73)**	**($5.46)**	**($0.98)**	**($0.64)**	**($0.77)**	**($7.85)**	($2.43)	($2.75)	($2.87)	($3.68)	($2.17)	$2.23	($0.98)	($0.12)	$1.06	$2.32	$3.34	$4.90
Y/Y growth																		
Basic Shares* (000)	**1,290**	**1,767**	**10,151**	**18,300**	**18,483**	**5,801**	**23,668**	**33,905**	**41,744**	**42,161**	**42,583**	**43,008**	**43,439**	**43,873**	**44,312**	**44,755**	**45,202**	**45,654**

Source: Leerink Swann estimates and company reports.
** Basic shares for 2012A and 1Q13E are pro forma for IPO priced on 5/8/13.*

DCF Calcuation

Discount rate	*11%*
Terminal Growth Rate	*1%*
Valuation	**$520,094**
Valuation / Share	**$30**

Source: Leerink Swann estimates.

RCPT DCF Valuation Sensitivity Analysis ($M)

Terminal Growth Rate \ Discount Rate	9.0%	10.0%	11.0%	12.0%	13.0%
0.0%	$45	$35	$27	$21	$16
1.0%	$50	$38	**$30**	$23	$17
2.0%	$56	$42	$32	$25	$19
3.0%	$64	$47	$36	$27	$21
4.0%	$75	$54	$40	$30	$23

Source: Leerink Swann estimates.

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Disclosures Appendix

Analyst Certification

I, Marko Kozul, M.D., certify that the views expressed in this report accurately reflect my views and that no part of my compensation was, is, or will be directly related to the specific recommendation or views contained in this report.

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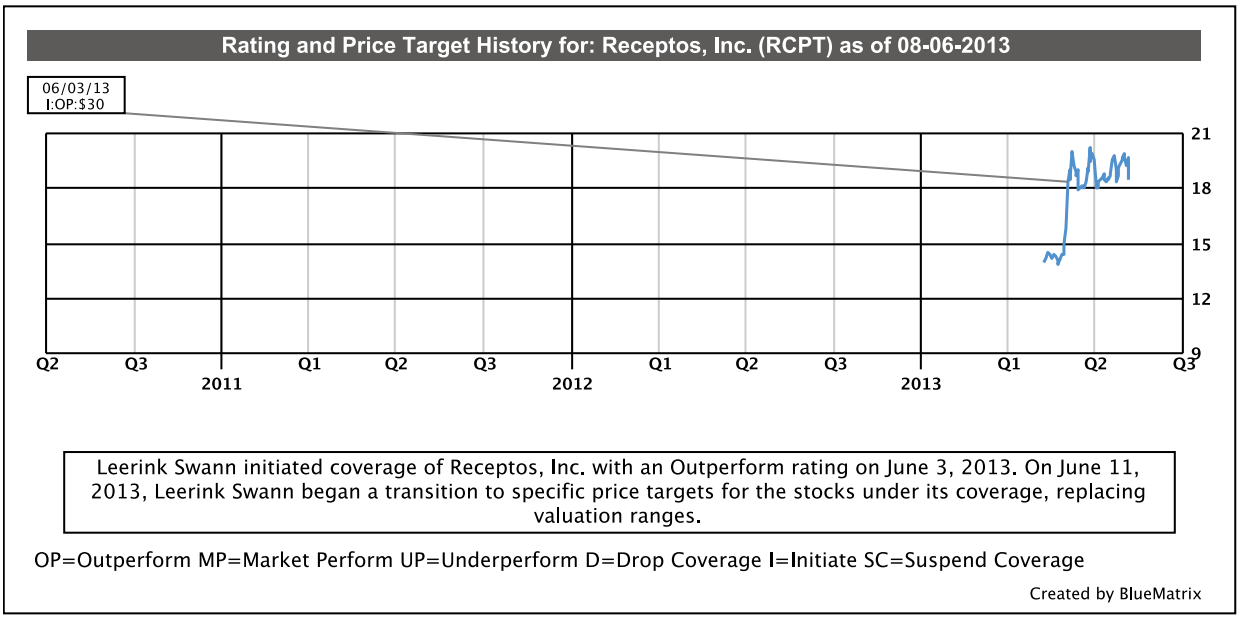

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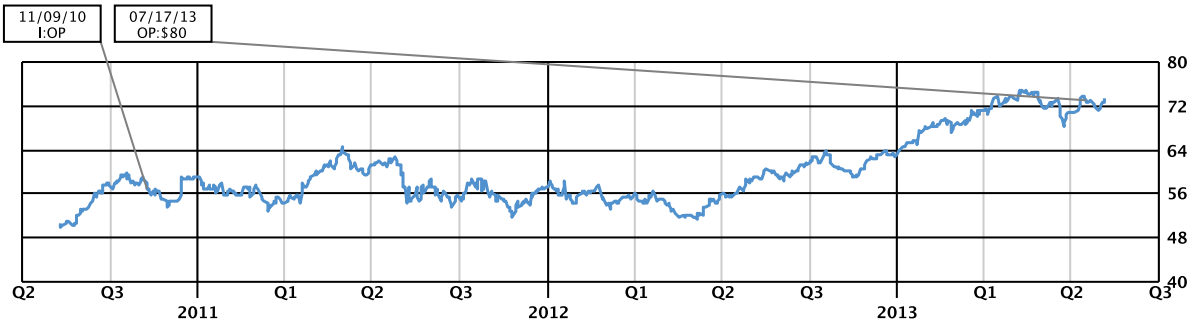
Rating and Price Target History for: Novartis AG (NVS) as of 08-06-2013



On June 11, 2013, Leerink Swann began a transition to specific price targets for the stocks under its coverage, replacing valuation ranges.

OP=Outperform MP=Market Perform UP=Underperform D=Drop Coverage I=Initiate SC=Suspend Coverage

Created by BlueMatrix

Distribution of Ratings/Investment Banking Services (IB) as of 06/30/13				
			IB Serv./Past 12 Mos.	
Rating	Count	Percent	Count	Percent
BUY [OP]	103	62.80	30	29.00
HOLD [MP]	61	37.20	2	3.00
SELL [UP]	0	0.00	0	0.00

Explanation of Ratings

Outperform (Buy): **We expect this stock to outperform its benchmark over the next 12 months.**

Market Perform (Hold/Neutral): **We expect this stock to perform in line with its benchmark over the next 12 months.**

Underperform (Sell): **We expect this stock to underperform its benchmark over the next 12 months.The degree of outperformance or underperformance required to warrant an Outperform or an Underperform rating should be commensurate with the risk profile of the company.**

For the purposes of these definitions the relevant benchmark will be the S&P 600® Health Care Index for issuers with a market capitalization of less than $2 billion and the S&P 500® Health Care Index for issuers with a market capitalization over $2 billion.

Important Disclosures

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Like all Firm employees, analysts receive compensation that is impacted by, among other factors, overall firm profitability, which includes revenues from, among other business units, the Private Client Division, Institutional Equities, and Investment Banking. Analysts, however, are not compensated for a specific investment banking services transaction.

Leerink Swann Consulting LLC, an affiliate of Leerink Swann LLC, is a provider of evidence-based strategy and consulting to the healthcare industry.

In the past 12 months, the Firm has received compensation for providing investment banking services to Receptos, Inc.

Leerink Swann LLC makes a market in Receptos, Inc.

Leerink Swann LLC is willing to sell to, or buy from, clients the common stock of Novartis AG on a principal basis.

In the past 12 months, an affiliate of the Firm, Leerink Swann Consulting LLC, has received compensation for providing non-securities services to: Novartis AG.

Leerink Swann LLC has acted as a co-manager for a public offering of Receptos, Inc. in the past 12 months.

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