

Receptos (RCPT)

Q2 Financials In Line; Cash Runway Through Important Catalysts: Reiterate OUTPERFORM And Increasing Fair Value To \$25 For Time Value

- Q2 financials were in line.** Receptos reported about \$1.2 million in Q2 collaborative revenue (presumably from Ono), which was higher than our \$556,000 estimate. Slightly higher revenues were offset by slightly higher operating expenses (R&D \$9.4 MM vs. our \$8.8 MM; G&A \$1.6 MM vs. our \$1.1MM estimate). EPS (loss) was \$(0.98) (share count 10.2 million) vs. our \$(0.62) (share count 18.9 million). We believe the Q3 share count is likely to be close to 18.9 million since the IPO occurred in May (Q2).
- Management reiterated previous cash runway guidance until Q2:2015—covering major clinical catalysts in 2014.** The company ended Q2 2013 with about \$91.1 million in cash, investments, and equivalents. Cash runway into Q2 2015 includes anticipated mid-2014 releases of transforming top-line Phase 2 results testing RPC1063 treatment of RMS and IBD/UC. Presuming a commercial partner is on board for RPC1063 in RMS and IBD, we project full-year profitability in 2019 after launching RPC1063 in RMS in late 2018, in IBD in 2019, as well as RPC4046 launch in 2019.
- Next: Presentation of positive results from thorough QT Phase 1 at ECTRIMS and IPO lockup expiration in Q4.** Management previously announced top-line results from a Phase 1 thorough QT study which demonstrated that RPC1063 did not show a cardiovascular safety signal and differentiates it from GILENYA®. Details from this study will be presented as a poster at the European Committee for Treatment and Research In Multiple Sclerosis annual conference (ECTRIMS, October 2-5, 2013 Copenhagen). Following this data presentation, the next potential catalyst we see is the 180-day IPO lockup expiration after market close on November 4, 2013. Management does not anticipate significant selling due to investors indicating they are waiting for the mid-2014 Phase 2 data releases for RPC1063 in RMS and IBD/UC.
- We reiterate our OUTPERFORM rating and our increasing our fair value to \$25 for time value.** We calculate RCPT's fair value based on the sum of a 30% annual discount and a 1x-10x premium range on our net peak annual sales estimate for each product and indication in the clinic to reflect risk.

August 7, 2013

Price
\$17.37

Rating
OUTPERFORM

Fair Value Estimate
\$25 (from \$24)

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Company Information

Shares Outst (M)	18.3
Market Cap (M)	\$319
52-Wk Range	\$13.00 - \$25.00
Book Value/sh	\$-28.00
Cash/sh	\$10.36
Enterprise Value (M)	\$300
LT Debt/Cap %	0.00

Company Description

Receptos is developing first- and best-in-class treatments for immune disorders. The lead candidate, RPC1063, is being developed as a safer S1P1 modulator versus GILENYA(TM) for multiple sclerosis as well as for IBD.

FYE Dec	2012E	2013E			2014E		
REV (M)	ACTUAL	CURR.	PREV.	CONS.	CURR.	PREV.	CONS.
Q1 Mar	\$1.3A	\$1.5E		\$0.4E	\$0.2E		N/AE
Q2 Jun	2.2A	1.2E	0.6E	0.4E	0.2E		N/AE
Q3 Sep	2.2A	0.6E		0.4E	0.2E		N/AE
Q4 Dec	2.2E	0.6E		0.4E	0.2E		N/AE
Year*	\$7.8E	\$3.8E	\$3.2E	\$2.0E	\$0.7E		\$5.9E
Change	--	--			--		
EPS	2012E	2013E			2014E		
	ACTUAL	CURR.	PREV.	CONS.	CURR.	PREV.	CONS.
Q1 Mar	(\$3.53)A	(\$5.46)E		(\$0.62)E	(\$0.78)E	(\$0.81)E	N/AE
Q2 Jun	(0.53)A	(0.98)E	(0.62)E	(0.56)E	(0.85)E	(0.88)E	N/AE
Q3 Sep	(0.53)A	(0.62)E	(0.67)E	(0.60)E	(0.89)E	(0.91)E	N/AE
Q4 Dec	(0.53)E	(0.69)E	(0.73)E	(0.72)E	(0.92)E	(0.95)E	N/AE
Year*	(\$2.63)E	(\$3.59)E	(\$3.30)E	(\$3.97)E	(\$3.44)E	(\$3.56)E	(\$3.02)E
P/E	NMx	NMx			NMx		
Change	--	--			--		

Consensus estimates are from Thomson First Call.

* Numbers may not add up due to rounding.



Source: Thomson Reuters

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INVESTMENT THESIS

Receptos, located in San Diego, CA, is an emerging biopharmaceutical company developing first-in-class and best-in-class drug candidates for large market opportunities and rare diseases. The company's lead product, RPC1063, is a sphingosine 1-phosphate (S1P1R) receptor modulator being developed as an orally-dosed treatment candidate being tested in a Phase 2/3 clinical trial for relapsing multiple sclerosis (RMS) and in a Phase 2 trial for inflammatory bowel disease (IBD). The second treatment candidate, RPC4046, is an anti-IL13 monoclonal antibody being developed as a potential treatment for an allergic/immune orphan disease called Eosinophilic Esophagitis (EoE). We believe clinical risk is lower than normal as RPC1063 has the same disease target as Novartis's approved RMS treatment Gilenya, but has a better safety profile and best-in-class potential. RPC4046 offers an orphan drug opportunity for Receptos to develop its own sales force. We believe execution risk is lower than normal as we consider management to have higher-than-normal knowledge and experience in the pharmaceutical industry—especially in multiple sclerosis. The CEO was successful at not only developing daclizumab, but also increasing value for FACET and making it an acquisition target for ABT. Additionally, we view the rest of the management team as being top tier. Receptos ended Q1:13 with about \$20 million in cash and along with the IPO funding of about \$72.8 million (excluding shoe), management projects runway into H2 2015, which includes top-line results from the ongoing Phase 2/3 trial testing RPC1063 treatment of RMS as well as IBD in mid-2014. We anticipate RPC1063 is likely to achieve clinical success and regulatory approval and could reach gross peak annual worldwide sales of over \$2 billion for RMS and over \$850 million for IBD. We also project RPC4046 treatment of EoE could reach over \$1 billion in gross peak annual worldwide sales with premium orphan drug pricing.

Figure 1: MODEL UPDATE

Receptos, Inc. (NASDAQ: RCPT)							Wedbush Pac Grow Life Sciences						
Historical and Projected Income Statement (In thousands except per share data)							Liana Moussatos, Ph.D. Richard Lau						
	2012A	2013E				2014E	2015E	2016E	2017E	2018E	2019E		
	FY:12A	Q1A	Q2A	Q3	Q4	FY:13E	FY:14E	FY:15E	FY:16E	FY:17E	FY:18E	FY:19E	
Gross Sales													
RPC1063	-	-	-	-	-	-	-	-	-	\$ -	\$ 7,215	\$ 229,723	
RMS	-	-	-	-	-	-	-	-	-	-	7,215	175,010	
IBD	-	-	-	-	-	-	-	-	-	-	-	54,713	
RPC4046	-	-	-	-	-	-	-	-	-	-	\$ -	\$ 46,242	
EoE	-	-	-	-	-	-	-	-	-	-	-	46,242	
Total Gross Sales	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 7,215	\$ 275,965	
Revenues:											72%	70%	
Net Product Sales	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 3,572	\$ 159,382	
RPC1063	-	-	-	-	-	-	-	-	-	\$ -	\$ 3,572	\$ 113,140	
Grant Revenue	-	-	-	-	-	-	-	-	-	-	-	-	
Collaborative Revenue	8,647	1,488	1,238	556	556	3,839	700	1,463	1,463	1,209	1,378	1,350	
Total Net Revenues	\$ 7,810	\$ 1,488	\$ 1,238	\$ 556	\$ 556	\$ 3,839	\$ 700	\$ 1,463	\$ 1,463	\$ 1,209	\$ 4,950	\$ 160,732	
Cost and Expenses:													
Cost of Goods	-	-	-	-	-	-	-	-	-	-	-	11,561	
R&D	22,927	8,020	9,441	10,385	11,424	39,270	55,714	34,643	40,527	47,411	55,464	64,886	
(S)G&A	3,430	1,062	1,589	1,684	1,802	6,138	8,569	10,134	15,060	36,719	62,637	73,277	
Other	-	-	-	-	-	-	-	-	-	-	-	-	
Total Operating Expenses	\$ 24,991	\$ 9,082	\$ 11,030	\$ 12,069	\$ 13,226	\$ 45,407	\$ 64,284	\$ 44,777	\$ 55,588	\$ 84,130	\$ 118,102	\$ 149,723	
Operating Income (Loss)	(17,181)	(7,594)	(9,792)	(11,513)	(12,670)	(41,569)	(63,584)	(43,314)	(54,125)	(82,921)	(113,152)	11,009	
Net Interest Income (Expense)/Other Income	6	1	(126)	52	42	(31)	74	(62)	(183)	(347)	(604)	(784)	
Other Income (Expense)	(40)	(2,056)	-	-	-	(2,056)	-	-	-	-	-	-	
Income Before Income Taxes	\$ (17,215)	\$ (9,649)	\$ (9,918)	\$ (11,461)	\$ (12,627)	\$ (43,656)	\$ (63,510)	\$ (43,376)	\$ (54,308)	\$ (83,268)	\$ (113,756)	\$ 10,224	
Provision (Benefit) for Income Taxes	-	-	-	-	-	-	-	-	-	-	-	-	
Net Income (Loss)	\$ (17,215)	\$ (9,649)	\$ (9,918)	\$ (11,461)	\$ (12,627)	\$ (43,656)	\$ (63,510)	\$ (43,376)	\$ (54,308)	\$ (83,268)	\$ (113,756)	\$ 10,224	
EPS (GAAP, Taxed, Diluted)	(\$2.63)	(\$5.46)	(\$0.98)	(\$0.62)	(\$0.69)	(\$3.59)	(\$3.44)	(\$2.34)	(\$2.91)	(\$4.44)	(\$6.03)	\$0.54	
Weighted Shares Outstanding (Basic and Diluted)	6,552	1,767	10,151	18,363	18,388	12,167	18,450	18,550	18,650	18,750	18,850	18,950	
Total Shares Outstanding (Diluted)	8,367	2,299	10,151	18,920	18,945	12,579	19,008	19,108	19,208	19,308	19,408	19,508	
Cash	\$5,427	\$18,312	\$91,146	\$74,304	\$60,428	\$60,428	(\$3,782)	(\$47,159)	(\$101,466)	(\$184,734)	(\$298,784)	(\$296,623)	
Net Cash per share	\$0.83	\$10.36	\$8.50	\$4.05	\$3.29	\$4.97	(\$0.20)	(\$2.54)	(\$5.44)	(\$9.85)	(\$15.85)	(\$15.65)	
Annual (Burn)/Generation	(\$5,909)					\$55,001	(\$64,210)	(\$43,376)	(\$54,308)	(\$83,268)	(\$114,049)	\$2,161	

Source: Company data, Wedbush Securities, Inc.

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Source: Company data. Wedbush Securities, Inc.

Next: Presentation of positive results from thorough QT Phase 1 at ECTRIMS and IPO lockup expiration in Q4. Management previously announced top-line results from a Phase 1 thorough QT study which demonstrated that RPC1063 did not show a cardiovascular safety signal and differentiates it from GILENYA®. Details from this study will be presented as a poster at the European Committee for Treatment and Research In Multiple Sclerosis annual conference (ECTRIMS, October 2-5, 2013 Copenhagen). Following this data presentation, the next potential catalyst we see is the 180 day IPO lockup expiration after market close on November 4, 2013. Management does not anticipate significant selling due to investors indicating they are waiting for the mid-2014 Phase 2 data releases for RPC1063 in RMS and IBD/UC.

Figure 3: VALUATION

Source: Company data. Wedbush Securities, Inc.

We reiterate our OUTPERFORM rating and our increasing our fair value to \$25 for time value. We calculate RCPT's fair value based on the sum of a 30% annual discount and a 1x-10x premium range on our net peak annual sales estimate for each product and indication in the clinic to reflect risk.

Risks to Attainment of Our Fair Value

Clinical Risk: We believe clinical risk is low in 2013, but likely to increase in 2014 with release of Phase 2 clinical results. Receptos is a developmental stage emerging pharmaceutical company which has completed Phase 1 and is conducting a Phase 2 trial for their lead product candidate, RPC1063 for the treatment of relapsing multiple sclerosis (RMS) with top-line results expected in mid-2014. As will all clinical candidates, RPC1063 is susceptible to inherent risks of failure at any stage of drug development, which may include unexpected adverse events; however, the S1P1 target has been validated by Novartis' GILENYA™ and RPC1063 appears to have a better safety profile. The company is also developing RPC1063 as a treatment candidate for inflammatory bowel disease (IBD) which is currently in a Phase 2 clinical trial with initial results expected in mid-2014. A second clinical candidate, RPC4046 is being developed as a treatment candidate for Eosinophilic Esophagitis (EoE) and is expected to start Phase 2 in 2014. Because the company is not expected to release initial top line results from mid-to-late stage clinical candidates, we do not believe clinical risk to our fair value is high in 2013.

Regulatory Risk: We consider regulatory risk to be low in 2013; however, in general, we believe if RPC1063 successfully completes clinical development, we believe regulatory risk is likely to be lower than average. That the FDA approved Novartis' GILENYA™ in 2011 despite safety issues including potential mortality upon initial dosing due to cardiovascular adverse events, suggests to us that a safer drug candidate with a similar efficacy profile is also likely to obtain approval. Receptos has never obtained marketing approval for a drug candidate and we do not anticipate NDA filing for the lead drug candidate (RPC1063) until 2017. Upon completion of regulatory review, if the FDA requires additional studies or data, the resulting increased costs and delays in the marketing approval would likely increase financing risk. Even after conducting such trials and submitting new data, the FDA may find these to be insufficient or may not agree with the analysis and still may not approve the NDA. Any delay in obtaining, or an inability to obtain, marketing approvals would increase financing risk by delaying commercialization as well as potential profitability. Regulatory risk can involve turnover in regulatory decision-makers, which can change policy and approval criteria after the trial is conducted. Agency statisticians may choose a different analytical process than was conducted in the NDA and conclude that the trials failed to achieve statistical efficacy. Changes in standard-of-care occurring while the trial is ongoing may also result in the design being found to be obsolete during regulatory review. Even if a product is approved, the designated patient population may be much smaller than expected, which could limit sales potential. Post-approval clinical studies may be required as well as limits on sales and marketing practices and materials. If unexpected adverse effects emerge the drug can be withdrawn from the market. Regulatory requirements also vary among different countries and may result in requirements for additional clinical trials.

Manufacturing Risk: We consider manufacturing risk to be low in 2013, but higher than normal for the future as Receptos lacks manufacturing capability and plans to continue relying on third parties to supply its product candidates. In addition, the company does not have any executed agreements for long-term commercial supply for any of its drug candidates, but plan to do so for RPC1063 prior to commercial launch. For RPC4046, AbbVie has agreed to manufacture enough for preclinical and clinical trials and may continue to or may choose to engage a third party following the planned Phase 2 results in EoE, after which, AbbVie may choose to execute an option to collaborate with Receptos for RPC4046 development and commercialization. Multiple improvements to the manufacturing process for RPC4046 have been made and a comparability assessment of the material used in the completed Phase 1 study versus the new process must be filed prior to the initiation of the Phase 2 in EoE.

Commercialization Risk: We consider commercialization risk to be low in 2013, but higher than average in general due to Receptos's small size and development stage. Receptos's business model is to develop and commercialize clinical candidates; however, for small development-stage companies, we view commercialization risk in general as higher than normal until/unless the company partners commercialization with an appropriate larger pharmaceutical company—especially for large indications such as multiple sclerosis. We anticipate Receptos is likely to partner commercial activities for large markets globally. For rare diseases such as EoE, the company may hire a small specialty sales force for the US, but we anticipate the company will partner commercialization for primary care globally as well as for all physicians outside the US. We consider this commercial plan to be optimal for leveraging potential profits from sales for a small company.

Competition Risk: We view competition risk as low in 2013 but, in general, higher than average unless Receptos partners with an appropriate global pharmaceutical company for commercialization. In general, we believe a small development-stage emerging pharmaceutical company with limited resources has higher-than-average competition risk. In the situation with RPC1063, while we believe large pharmaceutical companies with large marketing budgets, such as Novartis and Biogen-Idec may counter-detail RPC1063 after potential launch in late 2018, if its emerging profile of equal efficacy to GILENYA™, but improved safety while maintaining once-daily oral dosing is maintained through clinical development, we believe physicians treating MS patients are likely to prefer it over the currently approved oral therapies. In addition, physicians treating MS have commented that twice-daily dosing such as for Biogen-Idec's Tecfidera™ may have reduced real-world efficacy as their patients may forget to take the evening dose.

Intellectual Property Risk: We consider intellectual property risk to be low in 2013 and, in general, as the company has an exclusive license for the RPC1063 composition of matter patent which expires in May 2029 and could be extended into 2032. In addition, intellectual property protection for RPC4046 also has a long runway with expiration in 2028 and may be extended up to 5 years.

Financing Risk: Receptos ended Q2:13 with about \$91.1 million in cash and investments and reiterated their runway guidance until Q2 2015. We consider financing risk to be low in 2013, but likely to increase in H2 2014.

Analyst Biography

Liana Moussatos joined Wedbush from Pacific Growth Equities where she was a Senior Research Analyst. Prior to that she came from UBS Global Asset Management where she was Director and portfolio manager of the UBS Global Biotech Funds for five years. Previously, Liana was with Bristol-Meyers Squibb where she was a manager in University and Government Licensing, External Science and Technology and she also worked with Sloan-Kettering Cancer Institute in the Office of Industrial Affairs and the National Cancer Institute in the Office of Technology Development. Liana received a BS in Entomology and a MS in Zoology and Biochemistry from Clemson University. She also earned a Ph.D. in Plant Pathology from the University of California, Davis and completed a postdoctoral research fellowship in Cellular and Molecular Physiology at the Yale School of Medicine.

Analyst Certification

I, Liana Moussatos, Ph.D., Richard Lau, certify that the views expressed in this report accurately reflect my personal opinion and that I have not and will not, directly or indirectly, receive compensation or other payments in connection with my specific recommendations or views contained in this report.

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Rating Distribution (as of June 30, 2013)	Investment Banking Relationships (as of June 30, 2013)
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Company	Disclosure
Receptos	1,3,5,7

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Price Charts

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RCPT

1) 06/03/13	2) 06/21/13
OUTPERFORM \$23	OUTPERFORM \$24



* WS changed its rating system from (Strong Buy/Buy/Hold/Sell) to (Outperform/ Neutral/Underperform) on July 14, 2009. Please access the attached hyperlink for WS' Coverage Universe: <http://www.wedbush.com/services/cmg/equities-division/research/equity-research> Applicable disclosure information is also available upon request by contacting Ellen Kang in the Research Department at (213) 688-4529, by email to ellen.kang@wedbush.com, or the Business Conduct Department at (213) 688-8090. You may also submit a written request to the following: Business Conduct Department, 1000 Wilshire Blvd., Los Angeles, CA 90017.

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