

Equity Research

December 16, 2013

Price: \$14.00 (12/16/2013)

Price Target: \$16.00

OUTPERFORM (1)

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Company Quick Take

Veracyte GEC Receives Positive Coverage Decision From Cigna

The Cowen Insight

VCYT's Afirma GEC received a positive coverage decision from Cigna, expanding total covered lives to >115MM. We believe the announcement is demonstrative of continued momentum towards more covered and eventually contracted lives heading into 2014.

Summary: Today after the close, Veracyte (VCYT – Outperform, \$14.00) announced that Cigna (CI – Outperform/Arnold, \$83.95) issued a positive coverage policy for the company's Afirma Gene Expression Classifier (GEC) test. The new policy applies to ~13MM lives covered by Cigna, effective immediately, and expands the Afirma GEC's total covered lives to >115MM in the US.

The Afirma GEC test is used to reduce the number of unnecessary thyroid surgeries in patients suspected of having thyroid cancer.

Building Momentum Towards More Covered And Contracted Lives

Today's announcement is consistent with previous positive coverage decisions made by several other public and private payers, including Medicare (January 2012), United Healthcare (March 2012), Aetna (June 2013), and Humana (July 2013). We believe these existing coverage decisions, coupled with positive guideline recommendations from the National Comprehensive Cancer Network (NCCN) obtained in January 2013, will help Veracyte to continue to expand GEC coverage and use over the next 12-18 months.

Additional catalysts over the next 12 months include the potential for Veracyte to enter into contracts with one or more payers with existing positive coverage policy. As noted in our initiation report ([Link](#)), Veracyte has only entered into contracts with pre-determined test prices with Medicare so far, and entering into similar contracts with private payers will allow those additional volumes to be accrued, therefore increasing revenue predictability and also accelerating revenue growth due to a shift in accounting from cash-based to accrual-based. We believe today's Cigna announcement will help build momentum towards adding contracted lives heading into 2014.

Valuation Methodology And Risks

Valuation Methodology

Life Science & Diagnostic Tools:

Price targets are based on several methodologies which may include: analysis of market risk, growth rate, revenue stream, discounted cash flows (DCF), EBITDA, EPS, cash flow (CF), free cash flow (FCF), EV/EBITDA, P/E, PE/growth, P/CF, P/FCF, premium (discount) / average group EV/EBITDA, premium (discount) / average group P/E, sum of the parts, net asset value, dividend returns, and return on equity (ROE) over the next 12 months.

Investment Risks

Life Science & Diagnostic Tools:

Risks to the Medical and Life Science Tools sector may include: reduction or delay in research and development budgets and government funding, reduced or delayed purchasing from health care / hospital customers, increased or extended regulatory hurdles or processes for regulated products, increased dependence on volatile emerging markets for revenues and profitability, and general macroeconomic challenges.

Risks To The Price Target

Risks include but are not limited to: difficulty in expanding payer coverage and entering into payer contracts; reimbursement prices lower than expected; delays or weaker than expected clinical data in support of new products; competition from other potential molecular diagnostic players; weaker than expected uptake in international markets; Genzyme partnership could become "relatively" expensive; and delivering on margin / profitability targets.

Addendum

Stocks Mentioned In Important Disclosures

Ticker	Company Name
CI	Cigna
VCYT	Veracyte

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Cowen and Company Rating System effective May 25, 2013

Outperform (1): The stock is expected to achieve a total positive return of at least 15% over the next 12 months

Market Perform (2): The stock is expected to have a total return that falls between the parameters of an Outperform and Underperform over the next 12 months

Underperform (3): Stock is expected to achieve a total negative return of at least 10% over the next 12 months

Assumption: The expected total return calculation includes anticipated dividend yield

Cowen and Company Rating System until May 25, 2013

Outperform (1): Stock expected to outperform the S&P 500

Neutral (2): Stock expected to perform in line with the S&P 500

Underperform (3): Stock expected to underperform the S&P 500

Assumptions: Time horizon is 12 months; S&P 500 is flat over forecast period

Cowen Securities, formerly known as Dahlman Rose & Company, Rating System until May 25, 2013

Buy – The fundamentals/valuations of the subject company are improving and the investment return is expected to be 5 to 15 percentage points higher than the general market return

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Hold – The fundamentals/valuations of the subject company are neither improving nor deteriorating and the investment return is expected to be in line with the general market return

Cowen And Company Rating Definitions

Distribution of Ratings/Investment Banking Services (IB) as of 09/30/13

Rating	Count	Ratings Distribution	Count	IB Services/Past 12 Months
Buy (a)	394	58.72%	54	13.71%
Hold (b)	255	38.00%	5	1.96%
Sell (c)	22	3.28%	1	4.55%

(a) Corresponds to "Outperform" rated stocks as defined in Cowen and Company, LLC's rating definitions. (b) Corresponds to "Market Perform" as defined in Cowen and Company, LLC's ratings definitions. (c) Corresponds to "Underperform" as defined in Cowen and Company, LLC's ratings definitions.

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Veracyte Rating History as of 12/13/2013

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Cigna Rating History as of 12/13/2013

powered by: BlueMatrix



Legend for Price Chart:

I = Initiation | 1 = Outperform | 2 = Market Perform | 3 = Underperform | UR = Price Target Under Review | T = Terminated Coverage | \$xx = Price Target | NA = Not Available

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