Ophthotech

Our Thoughts Post the 4Q Call

Overweight

OPHT, OPHT US
Price: $36.09

Price Target: $40.00

Ophthotech reported 4Q13 EPS, modestly below consensus (-$0.65 vs. -$0.50) on higher opex. More importantly, the company disclosed that it has reached an agreement with EU regulators on the Fovista phase 3 design/dosing reduction schedule, reassuring our confidence in EU timelines (JPMe: launch in FY18). Further, Ophthotech provided incremental granularity on its broader development efforts of Fovista beyond front-line wet AMD as well as for Zimura into wet and dry AMD. These efforts should provide additional news flow and data catalysts in the time leading up to read-out from the pivotal Fovista studies (mid-2016); of note, these indications represent sources of upside value likely not in Street models. We expect a more substantive review of these trials at the company's R&D day next week (Mar 7). Given the commercial opportunity in wet AMD, the existing Fovista datasets, multiple sources of potential upside to current estimates, and the company's strong financial footing, we reiterate our OW on OPHT shares.

- **EU regulatory status:** The company noted that it and the CHMP have reached an agreement regarding the design of the Fovista phase 3 plan. The agreement requires a minor amendment to the dose-reduction schedule in the second-year of therapy in one of the trials; we view this as minor change and positive development, given that the timelines to data read-out remain unchanged.
- **Broader Fovista development:** Ophthotech further delineated a broadening of the Fovista development effort into the treatment of sub-retinal fibrosis associated with wet AMD, reduction of the treatment burden of anti-VEGF resistant wet AMD, and proliferative vitreoretinopathy. We expect to hear more about the scientific rationale and pre-clinical data supporting these trials at the upcoming R&D day. Of note, however, success in these trials would further strengthen the drug's profile and are currently not reflected in our models.
- **Pipeline: Fovista** – Studies assessing the potential for Fovista to (1) reduce the treatment burden in wet AMD and (2) inhibit the formation of sub-retinal fibrosis associated with anti-VEGF therapy in wet AMD are set to initiate in 2014; a study in proliferative vitreoretinopathy is expected to start in 2015. The National Eye Institute (NEI) is also expected to start a study in von Hippel-Lindau in 2014. **Zimura** – Phase 2/3 trial in GA is expected to start in late 2014/early 2015. The company indicated it would likely explore higher/more frequent doses than what was explored in the earlier phase 2 study. A phase 2 study in combination with Fovista plus an anti-VEGF therapy in anti-VEGF resistant wet AMD is also set to start in 2015.

Biotechnology

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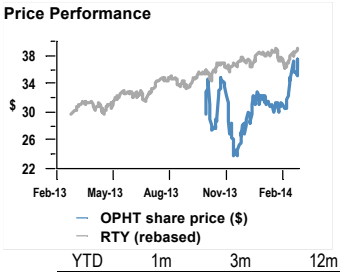

	YTD	1m	3m	12m
Abs	15.3%	19.9%	33.2%	21.5%
Rel	12.6%	16.6%	29.0%	-9.8%

Ophthotech Corp. (OPHT;OPHT US)

FYE Dec	2012A	2013A	2014E (Prev)	2014E (Curr)	2015E (Prev)	2015E (Curr)
EPS ($)						
Q1 (Mar)	-	(6.07)	(0.49)	(0.66)	-	-
Q2 (Jun)	-	(6.07)	(0.51)	(0.73)	-	-
Q3 (Sep)	-	(10.26)	(0.53)	(0.80)	-	-
Q4 (Dec)	-	(0.65)	(0.54)	(0.85)	-	-
FY	(2.52)	(6.34)	(2.07)	(3.04)	(2.26)	(3.65)

Source: Company data, Bloomberg, J.P. Morgan estimates. Note: Q1, Q2 2013 numbers reflect JPMe as co. still to disclose actual numbers; increaed share count plus IPO account for numbers not summing.

Company Data	
Price ($)	36.09
Date Of Price	26 Feb 14
52-week Range ($)	37.93-22.61
Market Cap ($ mn)	1,118.79
Fiscal Year End	Dec
Shares O/S (mn)	31
Price Target ($)	40.00
Price Target End Date	31-Dec-14

See page 5 for analyst certification and important disclosures.

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J.P.Morgan

- **Adjusting estimates.** Based on reported results and an expansion of R&D efforts and associated costs, we are adjusting our EPS estimates. We now forecast FY14 EPS of -$3.04 from -$2.07 and forecast FY15 EPS of -$3.65, from -$2.26.
- **Reiterate Overweight rating**.

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Changes to Our Model

Based on reported results and an expansion of R&D efforts and associated costs, we are adjusting on EPS estimates. We now forecast FY14 EPS of -$3.04 from -$2.07 and forecast FY15 EPS of -$3.65, from -$2.26.

Table 1: Changes to Our Models

	2013A OLD	2013A NEW	2014E OLD	2014E NEW	2015E OLD	2015E NEW
R&D	27.3	33.2	47.1	80.0	58.9	100.0
SG&A	13.1	14.2	16.4	22.0	17.7	26.2
Total Op Ex	40.5	47.4	63.5	102.0	76.6	126.2
Net income	-45.0	-51.1	-66.3	-102.0	-75.6	-125.2
GAAP EPS ($)	**-5.08**	**-6.34**	**-2.07**	**-3.04**	**-2.26**	**-3.65**
shares	10.0	9.0	32.1	33.5	33.5	34.3

Source: J.P. Morgan estimates.

Investment Thesis, Valuation and Risks

Ophthotech *(Overweight; Price Target: $40.00)*

Investment Thesis

Fovista is the key value driver for OPHT shares. Based on the efficacy data from the phase 2b, the combination of an anti-PDGF and anti-VEGF offers potentially best-in-class efficacy with meaningful improvements against the traditional regulatory endpoints of visual acuity, as well as an underappreciated endpoint, regression of neovascularization lesions, against which traditional therapy had minimal effect. As such, we view the phase 3 results as being significantly de-risked and believe Fovista will find use in both treatment-naïve AMD patients, and those requiring monthly anti-VEGF injections. Further, we believe Fovista has a two- to three-year head start over other anti-PDGF therapies in development.

Valuation

Our December 2014 $40 price target is based on our sum-of-the-parts NPV analysis. Our analysis is based on projected Fovista sales from a projected launch in 2017 through 2025. We conservatively modeled a 12.5% WACC and zero terminal values for the drug in the US and EU. Based on the above projections and assumptions, as well as probability of success adjustments, we derive a valuation of $40/share, comprising US sales of Fovista of $21/sh, OUS sales of Fovista of $14/sh, and $5/sh for net cash. Zimura is not built into our valuation or forecasts.

Risks to Rating and Price Target

Key downside risks include to our price target include (1) clinical risk associated with outcome of the phase 3 studies of Fovista, (2) commercial risk that the drug will offer meaningful benefit over the current treatment paradigm as well as the impact of competing agents risk, and (3) reimbursement risk for Fovista.

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Ophthotech: Summary of Financials

Income Statement - Annual	FY13A	FY14E	FY15E	FY16E
Revenues	0	0	0	-
Cost of products sold	0	0	0	-
Gross profit	-	-	-	-
SG&A	(14)	(22)	(26)	-
R&D	(33)	(80)	(100)	-
Operating income	(47)	(102)	(126)	-
EBITDA	(47)	(102)	(126)	-
Net interest (income) / expense	-	-	-	-
Other income / (expense)	(4)	0	1	-
Income taxes	0	0	0	-
Net income - GAAP	(57)	(102)	(125)	-
Net income - recurring	(57)	(102)	(125)	-
Diluted shares outstanding	9	34	34	-
EPS - excluding non-recurring	(6.34)	(3.04)	(3.65)	-
EPS - recurring	(6.34)	(3.04)	(3.65)	-

Balance Sheet and Cash Flow Data	FY13A	FY14E	FY15E	FY16E
Cash and cash equivalents	164	104	85	-
Accounts receivable	0	0	0	-
Inventories	-	-	-	-
Other current assets	0	0	0	-
Current assets	165	104	86	-
PP&E	0	0	0	-
Total assets	165	104	86	-
Total debt	11	11	11	-
Total liabilities	128	128	128	-
Shareholders' equity	36	(24)	(43)	-
Net income (including charges)	(57)	(102)	(125)	-
D&A	0	0	0	-
Change in working capital	0	0	0	-
Other	0	0	0	-
Cash flow from operations	(57)	(102)	(125)	-
Capex	(0)	(0)	(0)	-
Free cash flow	(57)	(102)	(125)	-
Cash flow from investing activities	(0)	(0)	(0)	-
Cash flow from financing activities	217	42	107	-
Dividends	-	-	-	-
Dividend yield	-	-	-	-

Income Statement - Quarterly	1Q14E	2Q14E	3Q14E	4Q14E
Revenues	0	0	0	0
Cost of products sold	0	0	0	0
Gross profit	-	-	-	-
SG&A	(5)	(5)	(6)	(6)
R&D	(17)	(19)	(22)	(23)
Operating income	(22)	(24)	(27)	(29)
EBITDA	(22)	(24)	(27)	(29)
Net interest (income) / expense	-	-	-	-
Other income / (expense)	0	0	0	0
Income taxes	0	0	0	0
Net income - GAAP	(22)	(24)	(27)	(29)
Net income - recurring	(22)	(24)	(27)	(29)
Diluted shares outstanding	33	34	34	34
EPS - excluding non-recurring	(0.66)	(0.73)	(0.80)	(0.85)
EPS - recurring	(0.66)	(0.73)	(0.80)	(0.85)

Ratio Analysis	FY13A	FY14E	FY15E	FY16E
Sales growth	-	-	-	-
EBIT growth	246.6%	115.1%	23.7%	-
EPS growth - recurring	151.1%	(52.0%)	19.9%	-
Gross margin	-	-	-	-
EBIT margin	-	-	-	-
EBITDA margin	-	-	-	-
Tax rate	0.0%	0.0%	0.0%	-
Net margin	-	-	-	-
Net Debt / EBITDA	323.1%	90.9%	58.7%	-
Net Debt / Capital (book)	131.3%	79.4%	63.5%	-
Return on assets (ROA)	(67.2%)	(75.8%)	(131.8%)	-
Return on equity (ROE)	131.2%	(1637.7%)	375.6%	-
Enterprise value / sales	-	-	-	-
Enterprise value / EBITDA	-	-	-	-
Free cash flow yield	(17.6%)	(8.4%)	(10.1%)	-

Source: Company reports and J.P. Morgan estimates.
Note: $ in millions (except per-share data).Fiscal year ends Dec

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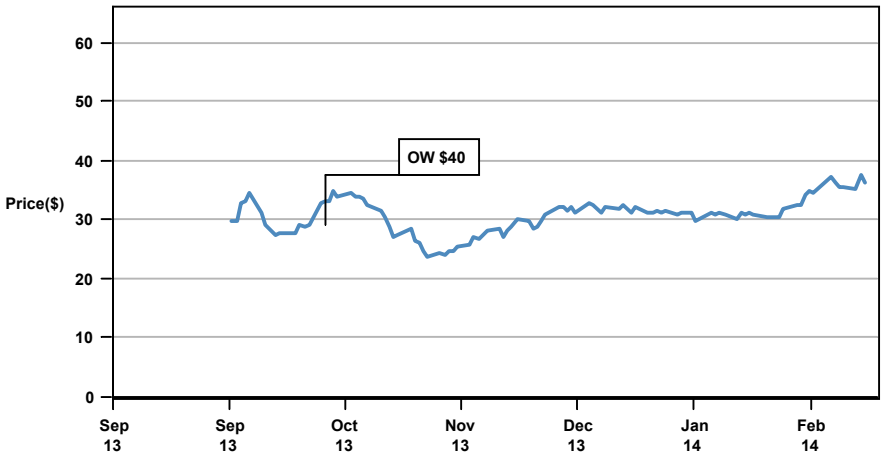
Ophthotech (OPHT, OPHT US) Price Chart



Date	Rating	Share Price ($)	Price Target ($)
21-Oct-13	OW	29.25	40.00

Source: Bloomberg and J.P. Morgan; price data adjusted for stock splits and dividends.
Initiated coverage Oct 21, 2013.

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