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Reason for report:

COMPANY UPDATE

## NANOSTRING TECHNOLOGIES

### Prosigna Clearance a Meaningful Positive

• **Bottom Line:** We view NSTG's announcement that it has received 510(k) clearance from the FDA for its Prosigna breast cancer prognostic test as a meaningful positive. The clearance occurred sooner than we had expected, and the test appears to have been awarded a label which allows designation of both risk category as well as risk score (the best case scenario, in our view). We continue to rate shares of NSTG Outperform with a \$15 price target, 97% upside from today's close.

• **Prosigna receives FDA clearance earlier than expected.** NSTG announced this evening that it has received FDA clearance for its Prosigna breast cancer prognostic test. The company submitted this test to the FDA in December 2012, and we had assumed a 12-month review process due to the complexity of the submission. Thus, this clearance occurred sooner than we had expected. We believe this clearance will drive U.S. diagnostic instrument placements in 4Q:13 and that U.S. labs will begin offering the Prosigna test in 1Q:14.

• **Risk score is on the label, which is a best case outcome, in our view.** One of the investment debates on NSTG, as discussed in our [initiation piece](#), was whether or not the FDA would allow the risk score to appear on the test's label. Allowing a score was important because it would further differentiate NSTG's test from Agendia's MammaPrint, the #2 breast cancer prognostic assay, but uncertain since the predicate device (MammaPrint) doesn't report a score. It appears this debate has now been settled as NSTG's Prosigna test will report both a score and a risk category based on the score and number of affected nodes.

• **No change to numbers, but higher confidence in forecast.** The earlier-than-anticipated FDA clearance and seemingly best case label do not motivate any increase in our revenue estimates but rather give us greater confidence in our current estimates. Recall that Prosigna and related instrument revenue comprise ~5%, 28%, and 37% of our 2013, 2014, and 2015 forecasts, respectively.

• **More detail expected on call.** We expect NSTG will provide more detail on a conference call tomorrow at 8:30am ET; dial-in: 888-793-9492.

• **GHDX's stock could be impacted.** We believe the positive announcement from NSTG could negatively impact Outperform-rated GHDX's stock, as GHDX sells the market leading breast cancer prognostic test.



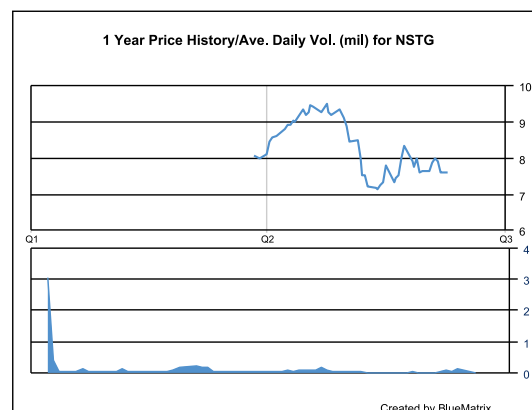
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HEALTHCARE EQUITY RESEARCH

## Key Stats:

(NASDAQ:NSTG)

<b>S&amp;P 600 Health Care Index:</b>	<b>1,119.79</b>
<b>Price:</b>	<b>\$7.62</b>
Price Target:	\$15.00
Methodology:	~3.5x EV/Jun-15 TTM revenue
52 Week High:	\$10.00
52 Week Low:	\$7.01
Shares Outstanding (mil):	14.6
Market Capitalization (mil):	\$111.5
Book Value/Share:	\$2.66
Cash Per Share:	\$3.41
Net Debt to Total Capital:	(27)%
Dividend (ann):	\$0.00
Dividend Yield:	0.0%

*Book Value/Share: estimated**Net Debt to Total Capital: estimated*

Dec Yr	1Q	2Q	3Q	4Q	FY Rev	1Q	2Q	3Q	4Q	FY EPS	P/E
2012A	\$4.5	\$5.9	\$6.0	\$6.5	\$23.0	(\$0.46)	(\$0.49)	(\$0.53)	(\$0.66)	(\$2.21)	NM
2013E	\$5.7A	\$7.2A	\$7.9	\$9.6	\$30.4	(\$0.79)A	(\$0.78)A	(\$0.66)	(\$0.90)	(\$3.13)	NM
2014E	--	--	--	--	\$52.1	--	--	--	--	(\$2.23)	NM

Source: Company Information and Leerink Swann LLC Research  
Revenues in \$millions

EPS ex-extraordinary 1x items, FAS 123 option expense included



## INVESTMENT THESIS

We rate Seattle, Washington-based NanoString Technologies (NanoString) with an Outperform rating and apply a \$15 price target to it. The company's proprietary technology fills an important role in the research market by enabling mid-density gene analysis in formalin-fixed, paraffin embedded (FFPE) samples. This capability translates readily to oncology diagnostics, in which NanoString's nCounter Analysis System promises to enable complex molecular testing in a decentralized setting. Our Outperform rating reflects a view that NanoString's revenue growth opportunities, in both life science research and clinical diagnostics, are underappreciated at current levels.

## VALUATION

Our 12-month price target for NSTG reflects an enterprise value (using projected levels of debt and cash) that is ~3.5x our revenue forecast for the twelve months ended June 2015. We prefer revenue multiples for companies not yet meaningfully profitable. This multiple is consistent with the life science tools and diagnostics peer group median EV/FTM revenue, which we believe appropriately balances NSTG's greater revenue growth prospects with commercialization risks in diagnostics.

## RISKS TO VALUATION

Risks to our price target for NSTG include, but are not limited to: Prosigna commercialization uncertainty in both the U.S. and Europe, competition, and tightening research budgets. While we model the company raising equity in 2014 to help fund operations, its ability to tap the equity markets or obtain additional funding may be a potential uncertainty.

**NanoString (NSTG)**  
Income Statement

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	2010	2011	Mar-12	Jun-12	Sep-12	Dec-12	2012	Mar-13	Jun-13	Sep-13e	Dec-13e	2013e	2014e	2015e
Revenue														
<b>Product</b>	<b>\$11,506</b>	<b>\$17,109</b>	<b>\$3,833</b>	<b>\$5,335</b>	<b>\$5,456</b>	<b>\$6,235</b>	<b>\$20,859</b>	<b>\$5,338</b>	<b>\$6,828</b>	<b>\$7,493</b>	<b>\$9,217</b>	<b>\$28,876</b>	<b>\$50,519</b>	<b>\$81,061</b>
Service	224	691	669	608	579	258	2,114	338	390	405	400	1,533	1,610	1,771
Total revenue	11,730	17,800	4,502	5,943	6,035	6,493	22,973	5,676	7,218	7,898	9,617	30,409	52,129	82,832
COGS	9,128	9,777	2,655	3,334	3,086	3,286	12,361	2,882	3,522	4,107	5,001	15,512	21,476	30,132
Gross profit	2,602	8,023	1,847	2,609	2,949	3,207	10,612	2,794	3,696	3,791	4,616	14,897	30,652	52,699
SG&A	8,027	9,529	3,165	3,249	4,382	4,690	15,486	6,126	6,708	8,372	12,118	33,324	44,309	50,527
R&D	7,547	8,990	1,998	3,126	2,650	3,860	11,635	3,059	3,626	4,502	5,193	16,380	21,894	23,066
<b>Operating income (loss)</b>	<b>(12,972)</b>	<b>(10,496)</b>	<b>(3,317)</b>	<b>(3,766)</b>	<b>(4,083)</b>	<b>(5,343)</b>	<b>(16,509)</b>	<b>(6,391)</b>	<b>(6,638)</b>	<b>(9,083)</b>	<b>(12,695)</b>	<b>(34,806)</b>	<b>(35,551)</b>	<b>(20,894)</b>
Interest expense (income)	65	589	307	202	107	167	783	382	486	602	592	2,062	2,352	2,318
Other expense, net	(269)	(153)	61	(9)	75	289	416	486	9	0	0	495	0	0
Pretax income	(12,768)	(10,932)	(3,685)	(3,959)	(4,265)	(5,799)	(17,708)	(7,259)	(7,133)	(9,684)	(13,287)	(37,363)	(37,903)	(23,212)
Taxes	0	0	0	0	0	0	0	0	0	0	0	0	0	0
Net income	(\$12,768)	(\$10,932)	(\$3,685)	(\$3,959)	(\$4,265)	(\$5,799)	(\$17,708)	(\$7,259)	(\$7,133)	(\$9,684)	(\$13,287)	(\$37,363)	(\$37,903)	(\$23,212)
Basic shares outstanding			8,018	8,018	8,018	8,018	8,018	9,195	9,201	14,651	14,701	11,937	16,826	19,026
Diluted shares outstanding			8,018	8,018	8,018	8,018	8,018	9,195	9,201	14,651	14,701	11,937	16,826	19,026
<b>EPS diluted</b>			<b>(\$0.46)</b>	<b>(\$0.49)</b>	<b>(\$0.53)</b>	<b>(\$0.72)</b>	<b>(\$2.21)</b>	<b>(\$0.79)</b>	<b>(\$0.78) (1)</b>	<b>(\$0.66)</b>	<b>(\$0.90)</b>	<b>(\$3.13)</b>	<b>(\$2.23)</b>	<b>(\$1.22)</b>
<i>EPS growth</i>														
Sales growth		51.7%					29.1%	26.1%	21.5%	30.9%	48.1%	32.4%	71.4%	58.9%
Gross margin	22.2%	45.1%	41.0%	43.9%	48.9%	49.4%	46.2%	49.2%	51.2%	48.0%	48.0%	49.0%	58.8%	63.6%
SG&A % of revenue	68.4%	53.5%	70.3%	54.7%	72.6%	72.2%	67.4%	107.9%	92.9%	106.0%	126.0%	109.6%	85.0%	61.0%
R&D % of revenue	64.3%	50.5%	44.4%	52.6%	43.9%	59.5%	50.6%	53.9%	50.2%	57.0%	54.0%	53.9%	42.0%	27.8%
<b>Operating margin</b>	<b>(110.6%)</b>	<b>(59.0%)</b>	<b>(73.7%)</b>	<b>(63.4%)</b>	<b>(67.7%)</b>	<b>(82.3%)</b>	<b>(71.9%)</b>	<b>(112.6%)</b>	<b>(92.0%)</b>	<b>(115.0%)</b>	<b>(132.0%)</b>	<b>(114.5%)</b>	<b>(68.2%)</b>	<b>(25.2%)</b>
Tax rate	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
D&A	\$972	\$1,454	\$815	\$573	\$579	(\$20)	\$1,947	\$464	\$437	\$371	\$456	\$1,728	\$1,659	\$2,211
<b>EBITDA</b>	<b>(\$12,000)</b>	<b>(\$9,042)</b>	<b>(\$2,502)</b>	<b>(\$3,193)</b>	<b>(\$3,504)</b>	<b>(\$5,363)</b>	<b>(\$14,562)</b>	<b>(\$5,927)</b>	<b>(\$6,201)</b>	<b>(\$8,712)</b>	<b>(\$12,238)</b>	<b>(\$33,078)</b>	<b>(\$33,892)</b>	<b>(\$18,683)</b>
<b>Free cash flow</b>														
Operarating cash flow	(\$10,965)	(\$10,692)	(\$2,630)	(\$4,113)	(\$3,859)	(\$4,206)	(\$14,808)	(\$9,009)	(\$5,233)			(\$37,283)	(\$37,584)	(\$20,773)
CapX	(1,932)	(2,688)	(133)	(91)	(87)	(117)	(428)	(136)	(118)			(1,704)	(5,105)	(5,833)
Free cash flow	(\$12,897)	(\$13,380)	(\$2,763)	(\$4,204)	(\$3,946)	(\$4,323)	(\$15,236)	(\$9,145)	(\$5,351)			(\$38,987)	(\$42,689)	(\$26,606)
<b>Guidance</b>														
Total revenue												\$29.5M - \$31.5M		
<b>Segment revenue</b>														
Life Science Tools	\$11,730	\$17,800					\$22,973	\$5,676	\$7,018	\$7,498	\$8,817	\$29,009	\$37,329	\$52,492
Diagnostics	0	0					0	0	200	400	800	1,400	14,800	30,340
Total revenue	\$11,730	\$17,800					\$22,973	\$5,676	\$7,218	\$7,898	\$9,617	\$30,409	\$52,129	\$82,832

Notes:  
Source: Company reports and Leerink Swann estimates  
(1) Excludes accretion of mandatorily redeemable convertible preferred stock and change in fair value of preferred stock warrant liability

**NanoString (NSTG)**

<b>Balance Sheet (\$ thousands)</b>	Mar-12	Jun-12	Sep-12	Dec-12	Mar-13	Jun-13	Sep-13e	Dec-13e
<b>Assets</b>								
Cash, equivalents, and short-term investments	\$13,783	\$9,412	\$5,361	\$21,692	\$11,794	\$10,755	\$49,928	\$36,552
Accounts receivable	2,613	3,702	4,111	3,322	4,356	4,779	4,927	6,061
Inventory	3,742	4,098	3,905	5,380	5,337	5,627	5,851	6,577
Other	<u>2,201</u>	<u>1,531</u>	<u>2,984</u>	<u>1,320</u>	<u>2,162</u>	<u>2,533</u>	<u>2,997</u>	<u>3,318</u>
Total current assets	22,339	18,743	16,361	31,714	23,649	23,694	63,703	52,507
Property and equipment, net	4,843	4,445	4,040	3,674	3,346	3,028	2,967	3,650
Goodwill	0	0	0	0	0	0	0	0
Other intangibles	0	0	0	0	0	0	0	0
Other	<u>331</u>	<u>383</u>	<u>378</u>	<u>2,018</u>	<u>2,580</u>	<u>3,768</u>	<u>3,768</u>	<u>3,768</u>
Total assets	\$27,513	\$23,571	\$20,779	\$37,406	\$29,575	\$30,490	\$70,438	\$59,926
<b>Liabilities and shareholders' equity</b>								
Notes payable and current maturities of long-term debt	\$0	\$0	\$0	\$2,789	\$4,021	\$2,675	\$2,642	\$2,627
Accounts payable	2,174	1,571	2,259	2,865	1,839	2,727	2,611	3,452
Accruals and other	<u>3,709</u>	<u>4,066</u>	<u>5,306</u>	<u>6,123</u>	<u>5,539</u>	<u>7,385</u>	<u>6,594</u>	<u>8,111</u>
Total current liabilities	5,883	5,637	7,565	11,777	11,399	12,787	11,846	14,189
Long-term debt	7,478	7,447	7,413	9,970	8,814	15,047	14,971	14,884
Other	<u>3,230</u>	<u>3,052</u>	<u>2,866</u>	<u>2,265</u>	<u>6,206</u>	<u>4,686</u>	<u>4,686</u>	<u>4,686</u>
Total liabilities	\$16,591	\$16,136	\$17,844	\$24,012	\$26,419	\$32,520	\$31,503	\$33,759
Shareholders' equity	\$10,922	\$7,435	\$2,935	\$13,394	\$3,156	(\$2,030)	\$38,935	\$26,167
Total liabilities, shareholders' equity, and minority interest	\$27,513	\$23,571	\$20,779	\$37,406	\$29,575	\$30,490	\$70,438	\$59,926

Notes:

Source: Company reports and Leerink Swann estimates



## Disclosures Appendix

### Analyst Certification

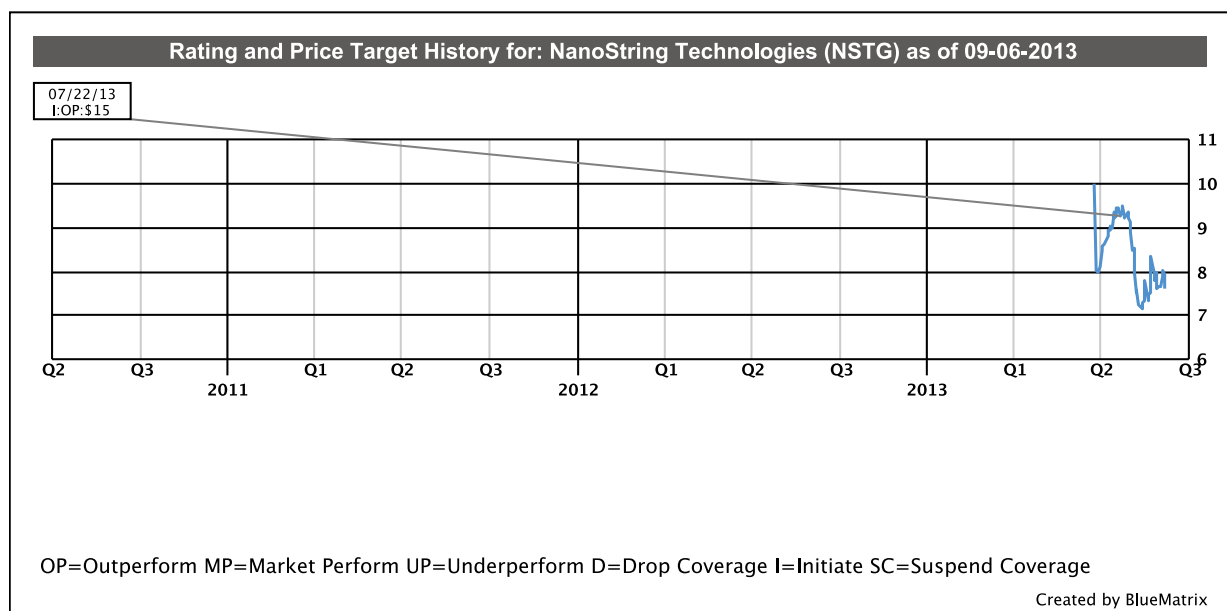
I, Dan Leonard, certify that the views expressed in this report accurately reflect my views and that no part of my compensation was, is, or will be directly related to the specific recommendation or views contained in this report.

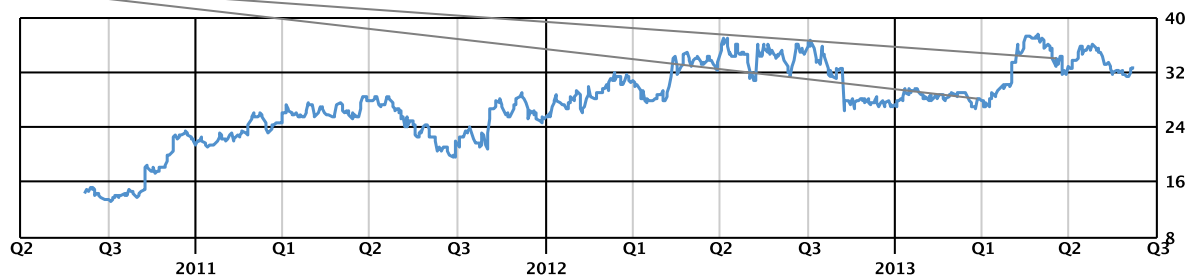
### Valuation

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### Risks to Valuation

Risks to our price target for NSTG include, but are not limited to: Prosigna commercialization uncertainty in both the U.S. and Europe, competition, and tightening research budgets. While we model the company raising equity in 2014 to help fund operations, its ability to tap the equity markets or obtain additional funding may be a potential uncertainty.



**Rating and Price Target History for: Genomic Health, Inc. (GHDX) as of 09-06-2013**03/27/13  
OP06/18/13  
OP:\$41

Leerink Swann placed a Market Perform rating on GHDX on January 17, 2008. 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				
Rating	Count	Percent	IB Serv./Past 12 Mos.	
			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.

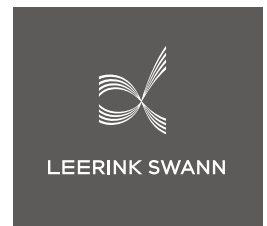
## Important Disclosures

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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 NanoString Technologies.



**Leerink Swann LLC makes a market in NanoString Technologies and Genomic Health, Inc.**

**Leerink Swann LLC has acted as a co-manager for a public offering of NanoString Technologies in the past 12 months.**

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