

Conatus Pharmaceuticals Inc. (CNAT)

Overweight

KOL Comments and Data Bode Well for Emricasan in ACLF

CONCLUSION

Conatus reported Phase I data for lead compound emricasan in healthy volunteers today at the AASLD meeting. While only Phase I, the data appear to address an important concern among investors regarding the safety of the compound. These data, and KOL comments regarding the clinical need and differentiated mechanism, bode well for Phase IIb data in acute-on-chronic liver failure (ACLF) expected 1H14, in our view. Based on the results presented at AASLD and our KOL diligence, we have enhanced conviction in the emricasan program, including the Phase IIb data and a Phase III start expected in 2H14, and we reiterate our Overweight rating and \$16 price target on Conatus.

- **What's new?** The data presented at AASLD is the first examining important biomarkers of apoptosis in healthy volunteers, to our knowledge. Recall that apoptosis is "programmed cell death" and is a mechanism the body uses to destroy unwanted cells. Conatus proposes to improve liver disease outcomes by preventing this pathway from destroying the liver cells. In prior studies of patients with HCV, emricasan reduced the apoptosis biomarker caspase cleaved CK18 (cCK18). A remaining concern was whether inhibiting the natural apoptosis pathway would have negative effects on patients (eg cancer). This latest study demonstrates that cCK18 levels in healthy volunteers treated for 10 days at 25mg OD or 25mg BID (doses shown to be maximally effective in HCV patients) were unchanged, suggesting lack of significant impact on the normal apoptotic process.
- **Supports safety database.** Combined with completed toxicology studies, this data support an emerging positive safety database for emricasan in over 500 patients. So far, we have seen nothing to warrant concerns that emricasan might have similar problems as seen with prior attempts to inhibit caspases.

RISKS TO ACHIEVEMENT OF PRICE TARGET

Principal risks to our price target include: 1) emergence of a safety signal or lack of efficacy; 2) new HCV anti-virals could reduce size of HCV-POLT market opportunity beyond our expectations 3) delay in emricasan to reach the market and 4) inability to raise capital.

COMPANY DESCRIPTION

Conatus focuses on treatments for liver disease.

PRICE: US\$9.20

TARGET: US\$16.00

DCF of projected 2015-2028 free cash flows, 15% discount rate

Charles C. Duncan, PhD

Sr. Research Analyst, Piper Jaffray & Co.
212 284-5025, charles.c.duncan@pjc.com

Roy Buchanan, Ph.D.

Research Analyst, Piper Jaffray & Co.
212 284-9458, roy.d.buchanan@pjc.com

Changes	Previous	Current
Rating	—	Overweight
Price Tgt	—	US\$16.00
FY13E Rev (mil)	—	US\$0.0
FY14E Rev (mil)	—	US\$0.0
FY13E EPS	—	US\$(0.46)
FY14E EPS	—	US\$(1.63)
52-Week High / Low	US\$11.24 / US\$8.26	
Shares Out (mil)	16.5	
Market Cap. (mil)	US\$151.8	
Avg Daily Vol (ooo)	39	
Book Value/Share	US\$0.34	
Net Cash Per Share	US\$3.80	
Debt to Total Capital	1%	
Yield	0.00%	
Fiscal Year End	Dec	

Note: price is as of the close November 4, 2013

Price Performance - 1 Year



Source: Bloomberg

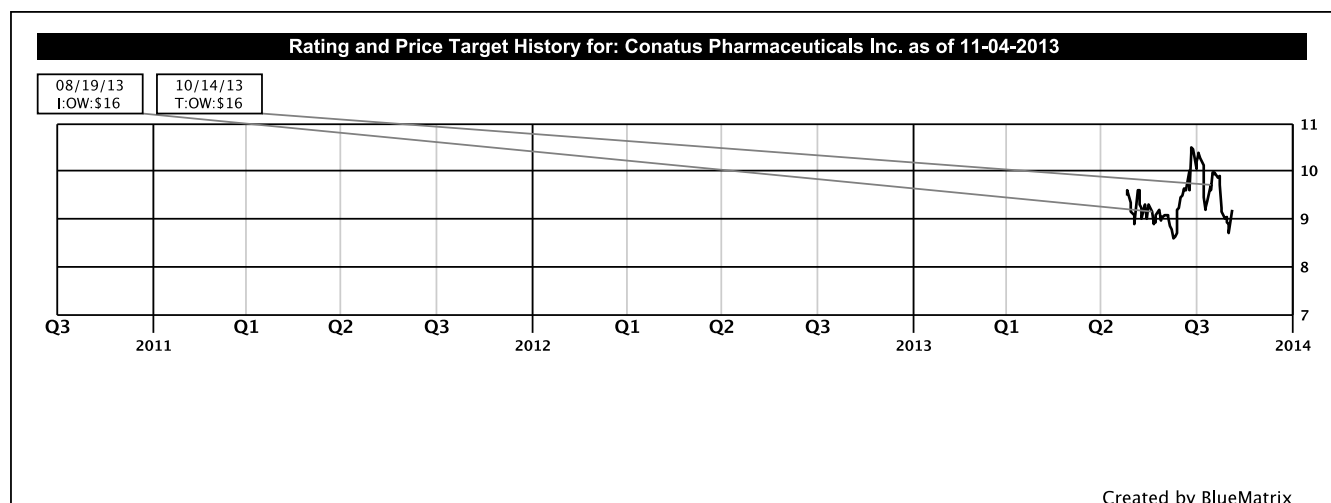
YEAR	REVENUE (US\$ m)						EARNINGS PER SHARE (US\$)					
	Mar	Jun	Sep	Dec	FY	FY	Mar	Jun	Sep	Dec	FY	FY P/E
2012A	—	—	—	—	0.0	NA	—	—	—	—	(0.91)	NM
2013E	0.0A	0.0A	0.0	0.0	0.0	NA	(1.10)A	0.16A	(0.15)	(0.22)	(0.46)	NM
2014E	0.0	0.0	0.0	0.0	0.0	NA	(0.27)	(0.35)	(0.44)	(0.57)	(1.63)	NM

Reflects Diluted Non-GAAP EPS

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Conatus Pharmaceuticals Earnings Model	2012A	1Q 13A	2Q 13A	3Q 13E	4Q 13E	2013E	1Q 14E	2Q 14E	3Q 14E	4Q 14E	2014E	2015E	2016E	2017E	2018E
(\$ in 000s, except per share amounts)															
US Emricasan Sales	0	0	0	0	0	0	0	0	0	0	0	0	0	13,566	47,192
Ex-US Emricasan Sales	0	0	0	0	0	0	0	0	0	0	0	0	0	4,607	16,643
Total Product Sales	0	0	0	0	0	0	0	0	0	0	0	0	0	18,174	63,835
Other Revenue	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
Total Revenues	0	0	0	0	0	0	0	0	0	0	0	0	0	18,174	63,835
Costs & Expenses:															
Cost of Goods Sold	0	0	0	0	0	0	0	0	0	0	0	0	0	3,907	13,405
R&D	5,528	968	1,117	1,676	2,932	6,693	3,460	4,325	5,623	7,591	20,999	24,149	28,979	39,121	50,858
SG&A	3,086	749	670	838	1,048	3,305	1,309	1,571	1,854	2,132	6,867	10,301	19,572	27,400	32,880
Total Operating Expenses	8,615	1,717	1,788	2,514	3,980	9,998	4,770	5,897	7,477	9,723	27,866	34,450	48,550	70,429	97,143
Operating Income	(8,614.6)	(1,717)	(1,788)	(2,514)	(3,980)	(9,998)	(4,770)	(5,897)	(7,477)	(9,723)	(27,866)	(34,450)	(48,550)	(52,255)	(33,308)
Interest Income	26	0	0	16	313	330	298	24	3	(28)	298	(273)	1,930	1,070	96
Interest Expense	(70)	(18)	(196)	0	0	(214)	0	0	0	0	0	0	0	0	0
Other income (expense), net	(90)	(563)	(2,890)	0	0	(3,452)	0	0	0	0	0	0	0	0	0
Pretax Income (Loss)	(8,749)	(2,297)	(4,873)	(2,497)	(3,667)	(13,334)	(4,471)	(5,872)	(7,474)	(9,751)	(27,568)	(34,723)	(46,620)	(51,185)	(33,212)
Provision for (benefit from) income taxes	0	0	0	0	0	0	0	0	0	0	0	0	0	0	(1,661)
Tax Rate	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0.0%	0.0%	0.0%	5.0%
Other	92	547	5,097	0	0	5,644	0	0	0	0	0	0	0	0	0
Net Income (Loss) GAAP	(8,658)	(1,750)	224	(2,497)	(3,667)	(7,690)	(4,471)	(5,872)	(7,474)	(9,751)	(27,568)	(34,723)	(46,620)	(51,185)	(31,552)
Stock option expense, tax adjusted	144	21	0	25	25	71	21	25	25	25	96	99	101	104	109
Other	90	563	0	0	0	3,452	0	0	0	0	0	0	0	0	0
Net Income (Loss) Non-GAAP	(8,423)	(1,165)	224	(2,472)	(3,642)	(4,166)	(4,450)	(5,847)	(7,449)	(9,726)	(27,472)	(34,624)	(46,519)	(51,081)	(31,443)
Diluted Earnings Per Share Non-GAAP	(\$0.91)	(\$1.10)	\$0.16	(\$0.15)	(\$0.22)	(\$0.46)	(\$0.27)	(\$0.35)	(\$0.44)	(\$0.57)	(\$1.63)	(\$1.27)	(\$1.66)	(\$1.78)	(\$1.07)
Earnings Per Share, Diluted Fully Taxed						nm					nm	nm	nm	nm	nm
Basic Earnings Per Share Non-GAAP	(\$0.91)	(\$1.10)	\$0.20	(\$0.15)	(\$0.22)	(\$0.47)	(\$0.27)	(\$0.35)	(\$0.44)	(\$0.57)	(\$1.63)	(\$1.27)	(\$1.68)	(\$1.82)	(\$1.10)
Diluted Earnings Per Share GAAP	(\$0.94)	(\$1.29)	\$0.16	(\$0.15)	(\$0.22)	(\$0.86)	(\$0.27)	(\$0.35)	(\$0.44)	(\$0.57)	(\$1.64)	(\$1.27)	(\$1.67)	(\$1.78)	(\$1.08)
Basic Earnings Per Share GAAP	(\$0.94)	(\$1.65)	\$0.20	(\$0.15)	(\$0.22)	(\$0.87)	(\$0.27)	(\$0.35)	(\$0.44)	(\$0.57)	(\$1.64)	(\$1.28)	(\$1.69)	(\$1.82)	(\$1.11)
Diluted Shares Outstanding (000s)	9,255	1,361	1,439	16,475	16,574	8,962	16,673	16,772	16,873	16,973	16,823	27,313	27,996	28,696	29,270
Basic Shares Outstanding (000s)	9,255	1,061	1,139	16,475	16,574	8,812	16,673	16,772	16,873	16,973	16,823	27,228	27,636	28,051	28,472

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I: Initiating Coverage
R: Resuming Coverage
T: Transferring Coverage
D: Discontinuing Coverage
S: Suspending Coverage
OW: Overweight
N: Neutral
UW: Underweight
NA: Not Available
UR: Under Review

Distribution of Ratings/IB Services Piper Jaffray				
Rating	Count	Percent	IB Serv./Past 12 Mos.	
			Count	Percent
BUY [OW]	337	56.83	74	21.96
HOLD [N]	230	38.79	15	6.52
SELL [UW]	26	4.38	0	0.00

Note: Distribution of Ratings/IB Services shows the number of companies currently in each rating category from which Piper Jaffray and its affiliates received compensation for investment banking services within the past 12 months. FINRA rules require disclosure of which ratings most closely correspond with "buy," "hold," and "sell" recommendations. Piper Jaffray ratings are not the equivalent of buy, hold or sell, but instead represent recommended relative weightings. Nevertheless, Overweight corresponds most closely with buy, Neutral with hold and Underweight with sell. See Stock Rating definitions below.

Analyst Certification — Charles C. Duncan, PhD, Sr. Research Analyst — Roy Buchanan, Ph.D., Research Analyst

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