

Equity Research

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Evoke Pharma, Inc. (EVOK-\$5.71)

Rating: BUY

Target Price: \$20.00

Undervalued Phase III Gastroenterology Asset; Reiterate BUY and \$20 PT

<u>REV</u>	<u>1Q</u>	<u>2Q</u>	<u>3Q</u>	<u>4Q</u>
2013A	0.0A	0.0A	0.0A	0.0A
2014E	0.0A	0.0A	0.0E	0.0E
2015E	—	—	—	—
<u>EPS</u>	<u>1Q</u>	<u>2Q</u>	<u>3Q</u>	<u>4Q</u>
2013A	(0.32)A	(0.32)A	(0.41)A	(0.27)A
2014E	(0.49)A	(0.59)A	(0.77)E	(0.77)E
2015E	—	—	—	—
<u>FY</u>	<u>2013A</u>	<u>2014E</u>	<u>2015E</u>	
REV	0.0A	0.0E	0.0E	
EPS	(1.20)A	(2.62)E	(1.59)E	

- **We reiterate our BUY rating since EVOK has deteriorated significantly from its \$12 IPO debut:** To us, the stock now looks even more undervalued. Fundamentals have not changed for the company, so we think the decline in the stock does not make sense. Management notes that it remains on track to complete its Phase III trial of intranasal metoclopramide for the treatment of diabetic gastroparesis in women in mid-2015. Additionally, Evoke is ahead of schedule in wrapping up its QT interval cardiac safety trial by the end of 2014, which should be the next catalyst for the stock. We continue to view Evoke as an attractive M&A target in the GI space and reiterate our BUY rating and \$20 PT, which is based on takeout scenarios.
- **Cash should suffice through the 2015 data release:** We estimate that the company has approximately \$12M in cash on its balance sheet at the end of 3Q:14 and also has access to an untapped \$4.5M debt facility, which should fund operations through Phase III data. We don't see financing risk ahead of the Phase III data disclosure.
- **More reasons to like the stock:** (1) Other GI companies such as Ironwood are also interested in developing gastroparesis therapeutics, and we believe that noise about the category and large market opportunity (2M metoclopramide treated patients) could be favorable to Evoke. Any M&A in the GI universe could also highlight the attractiveness of Evoke's specialty focus. (2) The clinical program is low-risk, in our view, since intranasal metoclopramide already demonstrated efficacy on an *a priori* pre-specified efficacy endpoint (looking at the composite gastroparesis symptom score by gender) in Phase II. (3) Evoke's drug has patent protection to 2030, which supports its attractiveness to a potential acquirer. (4) Given its large retail ownership, we expect the stock to appreciate as we head into the data, as is common in biotech names.

Current Statistics

Market Cap (\$Mil)	\$34.8	Free Float (%):	6.100
Avg. Daily Trading Volume (3 mo.):	10,451		
Shares Out (Mil):	6.100		

Valuation

We value Evoke using a weighted blend of the following two scenarios:

(1) 90% probability: We apply a 3x multiple to discounted, risk-adjusted peak sales of \$230 million (our most conservative peak sales estimate, which assumes only 20% penetration of today's generic, oral, 10 mg metoclopramide market; with 6% annual price increases), which yields a hypothetical price target of \$19. We employ a seven-year peak sales duration (assuming that peak sales are reached in 2023 after launch in 2H:16). We utilize a 13% discount rate, which is at the higher end of the risk rates we utilize in our space. We also risk adjust the sales estimate by 60% to incorporate clinical risk associated with a Phase III asset.

(2) 10% probability: We apply a 3x multiple to discounted risk-adjusted peak sales of \$415 million (a more generous scenario, which assumes 16.6% penetration of prescriptions utilized by 2.2 million patients in 2023; with 6% annual price increases), which yields a hypothetical price target of \$34. We utilize a 13% discount rate, and risk-adjust the sales estimate by 60%. We include this scenario also since there could be potential upside to Evoke from capturing a small percentage of antiemetic prescriptions given the new concerns about serotonin syndrome in that drug class.

We therefore arrive at a blended price target of \$20 using these two calculations.

Risks

- (1) Clinical risk associated with intranasal metoclopramide. More specifically, we are concerned about the possibility of a strong placebo response in the pending Phase III trial of female patients.
- (2) Financing needs may pressure the stock if the company needs to raise cash ahead of the Phase III data release.
- (3) Potential volatility in the stock associated with a high percentage of insider shareholders (56% of the stock is held by insiders).
- (4) Progression of competitive products in gastroparesis.
- (5) Manufacturing risk.

Company Description

Evoke Pharma is a small, development-stage specialty pharmaceutical company. Its key pipeline product is an intranasal formulation of metoclopramide, a well-known and widely used drug for the treatment of gastroparesis. The novel drug delivery approach developed by Evoke is expected to enhance both efficacy and tolerability, and therefore represents a meaningful improvement to current metoclopramide formulations, in our view.

Companies Mentioned:

Evoke Pharma, Inc. (EVOK - NASDAQ): BUY

Ironwood Pharmaceuticals, Inc. (IRWD - NASDAQ): HOLD

Disclosures Appendix

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SELL - denotes stocks that we expect to provide a total negative return of more than 15% over a 12 month period. A SELL rated stock is expected to underperform the total average return of the analyst's industry coverage universe on a risk adjusted basis.

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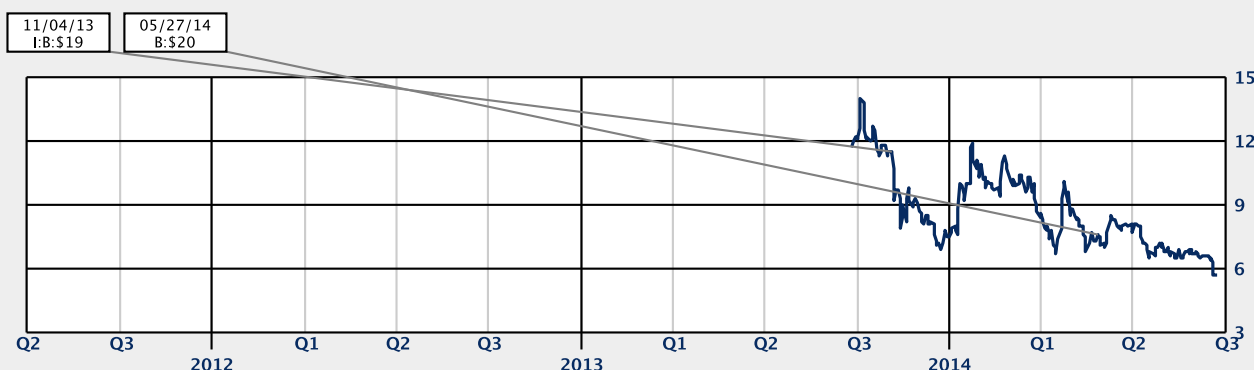
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Rating and Price Target History for: Evoke Pharma, Inc. (EVOK) as of 09-22-2014



B=Buy H=Hold S=Sell I=Initiated D=Dropped

Created by BlueMatrix

Rating and Price Target History for: Ironwood Pharmaceuticals, Inc. (IRWD) as of 09-22-2014



B=Buy H=Hold S=Sell I=Initiated D=Dropped

Created by BlueMatrix

Distribution of Ratings/Investment Banking Services (IB) as of 09/23/14

Rating	Cantor		IB Serv./Past 12 Mos.	
	Count	Percent	Count	Percent
BUY [B]	89	62.24	22	24.72
HOLD [H]	44	30.77	7	15.91
SELL [S]	10	6.99	1	10.00