

Equity Research

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Evoke Pharma, Inc. (EVOK-\$7.88)

Rating: BUY

Target Price: \$19.00

Business On Track; Earnings Irrelevant For Now; Reiterate BUY And \$19 PT

REV	1Q	2Q	3Q	4Q
2012A	0.0A	0.0A	0.0A	0.0A
2013E	0.0A	0.0A	0.0A	0.0E
2014E	—	—	—	—
EPS	1Q	2Q	3Q	4Q
2012A	(0.38)A	(0.38)A	(0.43)A	(0.59)A
2013E	(0.32)A	(0.32)A	(0.41)A	(0.21)E
Prev	(0.09)A	(0.09)A	(0.10)E	(0.10)E
2014E	—	—	—	—
FY	2012A	2013E	2014E	
REV	0.0A	0.0E	0.0E	
EPS	(1.79)A	(1.18)E	(2.40)E	
Prev	—	(0.38)E	(1.83)E	
P/E	(4.4)x	(6.7)x	(3.3)x	

- **3Q:13 EPS results were inconsistent with our sole estimate due to share count discrepancy:** Evoke reported net loss of \$0.5M, which was in line with our loss estimate of \$0.4M. With respect to EPS, the company reported a loss of (\$0.41) using a share count of 1.2M shares, which does not compare to our calculated loss of (\$0.10). Ours was based on a weighted average share count of 3.9M shares. Had we used 1.2M shares in our calculation, we would have arrived at (\$0.34). At this time there are no other analysts being captured in FactSet consensus estimates. The miss is therefore irrelevant, in our view. We have updated our share count estimates after speaking with management, which resulted in revisions to our EPS forecasts. The stock has meaningfully traded down since its IPO price of \$12.00/share for no apparent reason, and we continue to view the opportunity as highly attractive and reiterate our BUY rating and \$19 PT, which is based on a 60% risk-adjusted, discounted 3x multiple of two potential peak revenue scenarios (\$230M weighted at 90%, and \$415M weighted at 10%). We note that recent multiples in the GI space were closer to 7x, possibly implying an even higher value for the company in the future.
- **Why we like the story:** We believe that the EVK-001 program (intranasal metoclopramide for diabetic gastroparesis) is relatively low risk following the positive data in female patients from a recent Phase II trial, coupled with the well-characterized nature of metoclopramide. We also like the large commercial opportunity since there were over 3.6M metoclopramide prescriptions written in the last 12 months and there are approximately 2 million patients already taking metoclopramide. We think peak sales for EVK-001 should most likely approach \$230M by 2023 (seven years after 2016 launch). We believe the company is adequately capitalized through its Phase III data in mid-2015 and, if results are positive, we believe that Evoke could get acquired.
- **We believe the cash should last through the Phase III data release in 2015:** Management assured us that it is using many of its previously successful sites along with high-enrolling new sites. The company is selecting a CRO with which it has a long-standing relationship and management plans to remain highly involved in overseeing patient recruitment and trial conduct such that the program does not encounter delays.

Current Statistics

Market Cap (\$Mil)	\$48.0	Float Shares (Mil):	6.100
Avg. Daily Trading Volume (3 mo.):	NA		
Shares Out (Mil):	6.097		

ADDITIONAL DETAILS FROM THE EARNINGS CALL

We summarize our 3Q:13 Earnings estimates in Exhibit 1 below.

Exhibit 1: Evoke 3Q:13 Earnings

	3Q:13E	3Q:13A	% Variance	Y/Y Growth	Q/Q Growth	Comments
Revenues	0.00	0.00	NM	NM	NM	
Total Revenues	0.00	0.00	NM	NM	NM	
COGS	0.00	0.00	NM	NM	NM	
Gross Profit	0.00	0.00	NM	NM	NM	
SG&A	0.17	0.41	141.0%	189.1%	177.1%	
R&D	0.20	0.08	-60.6%	-76.6%	-34.9%	
Other	0.00	0.00	NM	NM	NM	
EBIT	-0.37	-0.49	NM	NM	NM	
Interest and Other Income	-0.04	0.00	NM	NM	NM	
Pre-tax income	-0.41	-0.49	NM	NM	NM	
Income tax expense	0.00	0.00	NM	NM	NM	
Net Income	-0.41	-0.49	NM	NM	NM	
Diluted shares	3.88	1.19	-69.4%	5.7%	-66.7%	
Operating EPS	(\$0.10)	(\$0.41)	NM	NM	NM	

Source: Company reports, Cantor Fitzgerald estimates, and FactSet consensus

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 \$17.50. We employ a seven-year peak sales duration (assuming that peak sales are reached 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 \$31.60. 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 \$19.00 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 (59% of the stock is held by insiders).
- (4) Progression of competitive products in gastroparesis.
- (5) Manufacturing risk.

Exhibit 2: Evoke Income Statement (dollars in millions)

	2011	2012	1Q:13A	2Q:13A	3Q:13A	4Q:13E	2013E	2014E	2015E	2016E	2017E	2018E	2019E	2020E	2021E	2022E	2023E
Revenues:																	
Revenue	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	15.0	45.0	102.0	145.0	180.0	205.0	221.0	230.0
Total revenues	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	15.0	45.0	102.0	145.0	180.0	205.0	221.0	230.0
Operating expenses:																	
COGS	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.6	1.8	4.0	5.6	6.8	7.7	8.2	8.4
Gross Profit	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	14.4	43.2	98.0	139.4	173.2	197.3	212.8	221.6
R&D	1.8	1.2	0.1	0.1	0.1	0.3	0.6	10.0	5.0	4.0	4.2	4.4	4.6	4.9	5.1	5.4	5.6
SG&A	0.6	0.8	0.1	0.1	0.4	0.3	1.0	2.4	8.0	30.0	100.0	105.0	110.3	111.4	112.5	113.6	114.7
Other	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	0.0	0.0	0.0
Total operating expenses	2.4	2.0	0.3	0.3	0.5	0.6	1.6	12.4	13.0	34.0	104.2	109.4	114.9	116.2	117.6	119.0	120.4
Operating income (Loss)	(2.4)	(2.0)	(0.3)	(0.3)	(0.5)	(0.6)	(1.6)	(12.4)	(13.0)	(19.6)	(61.0)	(11.4)	24.5	56.9	79.7	93.9	101.3
Interest income	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.1	0.2	0.1	0.1	0.1	0.1	0.2	0.2	0.2	0.2
Interest expense	(0.0)	(0.0)	(0.0)	(0.0)	(0.0)	(0.0)	(0.1)	(0.1)	(0.1)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Change in fair value of warrant liability	0.0	0.0	(0.1)	(0.1)	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
Other income, net	0.01	(0.0)	(0.1)	(0.1)	(0.0)	0.0	(0.2)	(0.1)	0.1	0.1	0.1	0.1	0.1	0.2	0.2	0.2	0.2
Pretax Income	(2.4)	(2.0)	(0.4)	(0.4)	(0.5)	(0.5)	(1.7)	(12.5)	(12.9)	(19.5)	(60.9)	(11.3)	24.7	57.1	79.9	94.1	101.5
Tax Rate	NA	NA	NA	NA	NA	0.0%	0.0	0%	0%	0%	0%	0%	15%	38%	38%	38%	38%
Tax expense	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	3.7	21.7	30.4	35.7	38.6
Net income	(2.4)	(2.0)	(0.37)	(0.37)	(0.5)	(0.5)	(1.7)	(12.5)	(12.9)	(19.5)	(60.9)	(11.3)	21.0	35.4	49.6	58.3	62.9
Weighted average common shares (diluted)	1.1	1.1	1.1	1.1	1.2	2.4	1.5	5.2	10.0	12.0	12.6	13.2	13.9	14.6	15.3	16.1	16.9
Diluted EPS	(\$2.18)	(\$1.79)	(\$0.32)	(\$0.32)	(\$0.41)	(\$0.21)	(\$1.18)	(\$2.40)	(\$1.29)	(\$1.63)	(\$4.83)	(\$0.85)	\$1.51	\$2.43	\$3.24	\$3.63	\$3.73
Margin Analysis	2011	2012	1Q:13A	2Q:13A	3Q:13A	4Q:13E	2013E	2014E	2015E	2016E	2017E	2018E	2019E	2020E	2021E	2022E	2023E
Gross Margin	-	-	-	-	-	-	-	-	-	96.0%	96.1%	96.1%	96.2%	96.2%	96.3%	96.3%	96.4%
COGS	-	-	-	-	-	-	-	-	-	4.0%	4.0%	3.9%	3.9%	3.8%	3.8%	3.7%	3.7%
SG&A	-	-	-	-	-	-	-	-	-	200.0%	222.2%	102.9%	76.0%	61.9%	54.9%	51.4%	49.9%
R&D	-	-	-	-	-	-	-	-	-	26.7%	9.3%	4.3%	3.2%	2.7%	2.5%	2.4%	2.4%
Operating Margin	-	-	-	-	-	-	-	-	-	-130.7%	-135.5%	-11.2%	16.9%	31.6%	38.9%	42.5%	44.0%
Net Income Margin	-	-	-	-	-	-	-	-	-	-130.1%	-135.3%	-11.0%	14.5%	19.7%	24.2%	26.4%	27.4%
Growth (Y/Y)	2011	2012	1Q:13A	2Q:13A	3Q:13A	4Q:13E	2013E	2014E	2015E	2016E	2017E	2018E	2019E	2020E	2021E	2022E	2023E
Net Sales	-	-	-	-	-	-	-	-	-	-	200%	127%	42%	24%	14%	8%	4%
SG&A	47%	-17%	-17%	-17%	189%	-	14%	153%	233%	275%	233%	5%	5%	1%	1%	1%	1%
R&D	-37%	-53%	-53%	-77%	-	-	-47%	1511%	-50%	-20%	5%	5%	5%	5%	5%	5%	5%
EBIT	-	-	-	-	-	-	-	-	-	-	-	-	-	132%	40%	18%	8%
Interest income (expense)	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Tax	-	-	-	-	-	-	-	-	-	-	-	-	-	486%	40%	18%	8%
Net Income	-	-	-	-	-	-	-	-	-	-	-	-	-	69%	40%	18%	8%
Diluted EPS	-	-	-	-	-	-	-	-	-	-	-	-	-	61%	33%	12%	3%

Source: Company reports, Cantor Fitzgerald estimates, and FactSet Consensus

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 both enhance efficacy and tolerability, and therefore represents a meaningful improvement to current metoclopramide formulations, in our view.

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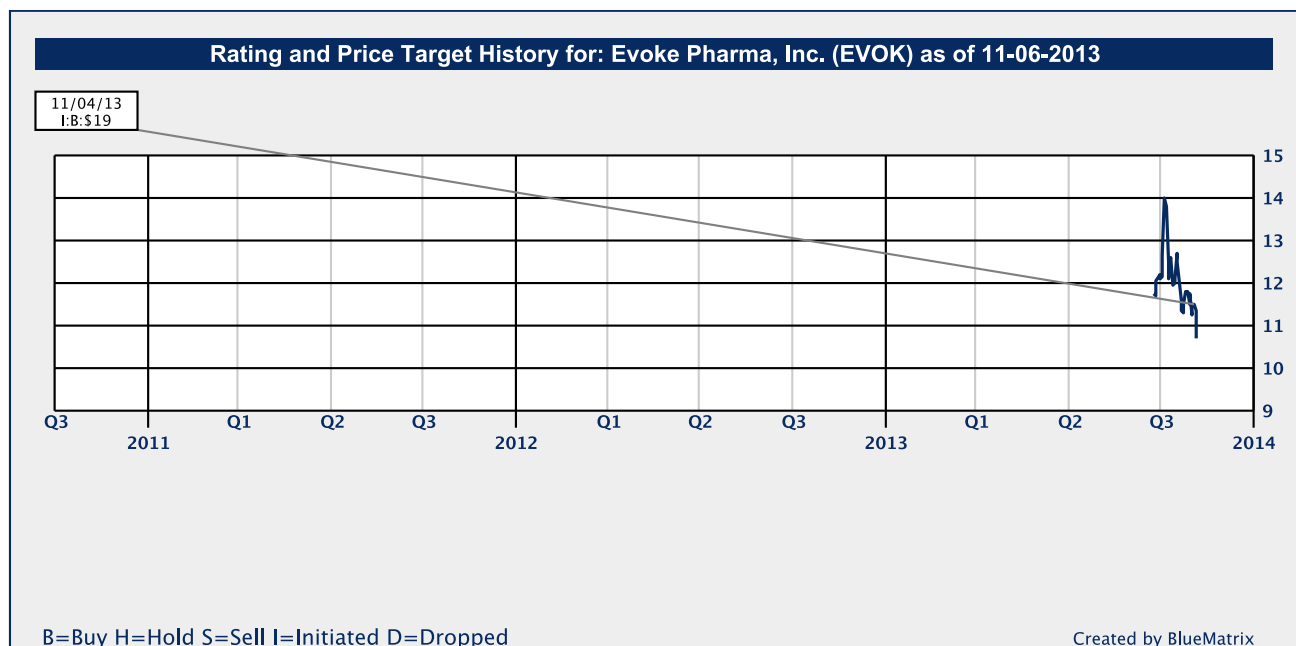
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Rating	Cantor		IB Serv./Past 12 Mos.	
	Count	Percent	Count	Percent
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