

# OncoMed Pharmaceuticals

(OMED-NASDAQ)

**Stock Rating:** Outperform  
**Industry Rating:** Outperform

December 3, 2013

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## Deal Validates OMED Cancer Stem Cell Approach

### Event

OncoMed (OMED) announced today a large collaboration deal with Celgene (CELG) for global development and commercialization of anti-DLL4 antibody demcizumab, a pre-clinical DLL4/VEGF bi-specific antibody and up to 4 pre-clinical cancer stem cell (CSC) product candidates targeting the RSPO-LGR pathway or a novel, undisclosed CSC/immune pathway. Terms of the deal include \$155M upfront payment, \$22.5M equity investment, potential milestone payments on demcizumab option exercise/development/commercialization of up to \$790M, up to \$505M in milestone payments for the DLL4/VEGF program and up to \$440M in milestones for each of the other 4 CSC programs. CELG will fund 2/3 of development after opt-in, with a 50:50 profit split in the US and royalties on ex-US sales for demcizumab, the DLL4/VEGF program and 3 of 4 other programs and with royalties of global sales of the 4th other program. OMED expects to report updated phase 1b data for demcizumab + ABRAXANE/GEMZAR in pancreatic CA at ASCO GI in January 2014, to shortly initiate randomized phase 2 studies for demcizumab in pancreatic CA, NSCLC and ovarian CA, and to file an IND for DLL4/VEGF by YE14.

### Impact & Analysis

We reiterate our Outperform rating on shares of OMED and increasing our price target to \$43 following the transformational deal with CELG. We believe that the deal validates OMED's cancer stem cell (CSC) approach, increases likelihood of success for demcizumab across multiple indications and provides downside support through multiple other programs and significant milestone opportunities.

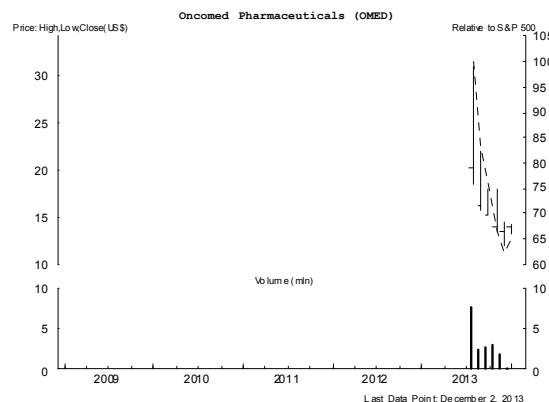
### Valuation & Recommendation

We arrive at our \$43 price target by applying a 20x multiple on 2020 EPS estimate of \$6.65 and discounting at 25%. We rate OMED shares Outperform.

### Securities Info

Price (2-Dec)	\$14.00	Target Price	\$43.00 ↑
52-Wk High/Low	\$31/\$12	Dividend	--
Mkt Cap (mm)	\$390	Yield	--
Shs O/S (mm, BASIC)	27.8	Float O/S (mm)	5.4
Options O/S (mm)	NA	ADVol (30-day, 000s)	113

### Price Performance



### Valuation/Financial Data

(FY-Dec.)	2012A	2013E	2014E	2015E
EPS GAAP	-\$1.00	-\$0.58↑	\$0.64↑	-\$1.02↑
P/E		nm	21.9x	nm
First Call Cons.		-\$0.79	-\$0.86	-\$0.77
FCF	na	na	na	na
P/FCF		na	na	na
EBITDA (\$mm)	-\$22	-\$17	\$18	-\$36
EV/EBITDA		nm	13.6x	nm
Rev. (\$mm)	\$25	\$41	\$109	\$99
EV/Rev		6.0x	2.3x	2.5x
Quarterly EPS	1Q	2Q	3Q	4Q
2012A	na	na	na	na
2013E	-\$0.16A	-\$0.43A	-\$0.15A	\$0.17↑
Balance Sheet Data (31-Mar)				
Net Debt (\$mm)	-\$144	Total Debt/EBITDA		nm
Total Debt (\$mm)	\$0	EBITDA/IntExp		na
Net Debt/Cap.	nm	Price/Book		-0.1x

Notes: Quarterly EPS may not sum due to share count. All values in US\$.

Source: BMO Capital Markets estimates, Bloomberg, Thomson Reuters, and IHS Global Insight.

### Changes

**Annual EPS**  
 2013E -\$1.32 to -\$0.58  
 2014E -\$1.43 to \$0.64

2015E -\$2.52 to -\$1.02

**Quarterly EPS**  
 Q4/13E -\$0.57 to \$0.17

**Target**  
 \$32.00 to \$43.00

## Exhibit 1: OMED Income Statement 2012A-2020E

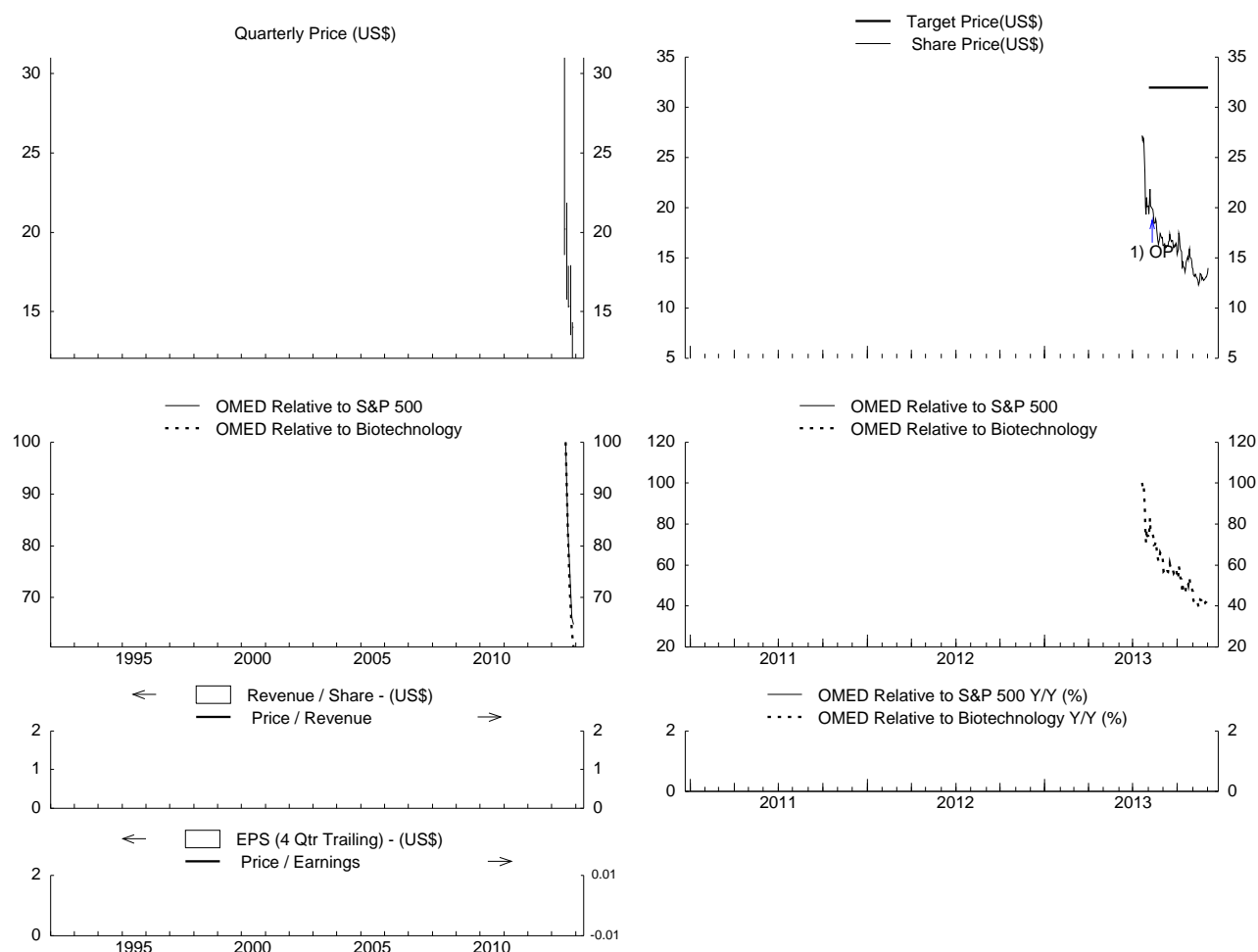
	2012A	1Q13A	2Q13A	3Q13A	4Q13E	2013E	2014E	2015E	2016E	2017E	2018E	2019E	2020E
<b>INCOMESTATEMENT (\$M)</b>													
<b>REVENUES</b>													
Product Revenues	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 112.2	\$ 364.2	\$ 520.2
Collaborative Revenues/Milestones	24.7	2.9	2.9	12.9	22.3	41.0	109.0	99.0	99.0	99.0	99.0	-	-
<b>TOTAL REVENUES</b>	<b>\$ 24.7</b>	<b>\$ 2.9</b>	<b>\$ 2.9</b>	<b>\$ 12.9</b>	<b>\$ 22.3</b>	<b>\$ 41.0</b>	<b>\$ 109.0</b>	<b>\$ 99.0</b>	<b>\$ 99.0</b>	<b>\$ 99.0</b>	<b>\$ 211.2</b>	<b>\$ 364.2</b>	<b>\$ 520.2</b>
<b>EXPENSES (GAAP)</b>													
Cost of Goods Sold (COGS)	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 0.2	\$ 0.7	\$ 1.0
R&D Expense	39.9	9.6	10.5	13.1	14.0	47.1	72.0	108.0	120.0	119.9	120.0	120.0	120.0
SG&A Expense	7.2	2.0	2.0	3.2	3.5	10.7	19.0	27.0	34.7	43.0	51.0	59.0	70.0
<b>TOTAL EXPENSES</b>	<b>47.1</b>	<b>11.6</b>	<b>12.4</b>	<b>16.4</b>	<b>17.5</b>	<b>57.8</b>	<b>91.0</b>	<b>135.0</b>	<b>154.7</b>	<b>162.9</b>	<b>171.2</b>	<b>179.7</b>	<b>190.9</b>
<b>Operating Income</b>	<b>(22.4)</b>	<b>(8.6)</b>	<b>(9.5)</b>	<b>(3.5)</b>	<b>4.8</b>	<b>(16.8)</b>	<b>18.1</b>	<b>(36.0)</b>	<b>(55.7)</b>	<b>(63.9)</b>	<b>40.0</b>	<b>184.5</b>	<b>329.3</b>
Depreciation and Amortization	-	-	-	-	-	-	-	-	-	-	-	-	-
EBIT	(22.4)	(8.6)	(9.5)	(3.5)	4.8	(16.8)	18.1	(36.0)	(55.7)	(63.9)	40.0	184.5	329.3
Interest Income	0.1	0.0	-	-	0.3	0.3	1.2	1.5	1.8	2.2	2.6	3.8	6.1
Interest Expense	(0.0)	5.0	(0.1)	-	-	-	-	(0.1)	-	-	(0.1)	-	(0.3)
Other Expense	-	-	-	-	-	-	-	-	-	-	-	-	-
Interest and Other (net)	\$ 0.1	\$ 5.0	\$ (0.1)	\$ -	\$ 0.3	\$ 5.2	\$ 1.2	\$ 1.4	\$ 1.8	\$ 2.2	\$ 2.5	\$ 3.8	\$ 5.8
Pre-Tax Income	(22.2)	(3.6)	(9.6)	(3.5)	5.1	(11.6)	19.2	(34.5)	(53.9)	(61.7)	42.5	188.3	335.1
Income Taxes	-	-	-	-	-	-	-	-	-	-	-	-	-
<b>Net Income (GAAP)</b>	<b>(22.2)</b>	<b>(3.6)</b>	<b>(9.6)</b>	<b>(3.5)</b>	<b>5.1</b>	<b>(11.6)</b>	<b>19.2</b>	<b>(34.5)</b>	<b>(53.9)</b>	<b>(61.7)</b>	<b>42.5</b>	<b>188.3</b>	<b>335.1</b>
EPS (GAAP) (basic)	\$ (1.00)	\$ (0.16)	\$ (0.43)	\$ (0.15)	\$ 0.18	\$ (0.57)	\$ 0.68	\$ (1.09)	\$ (1.49)	\$ (1.48)	\$ 0.87	\$ 3.94	\$ 6.95
<b>EPS (GAAP) (diluted)</b>	<b>\$ (1.00)</b>	<b>\$ (0.16)</b>	<b>\$ (0.43)</b>	<b>\$ (0.15)</b>	<b>\$ 0.17</b>	<b>\$ (0.58)</b>	<b>\$ 0.64</b>	<b>\$ (1.02)</b>	<b>\$ (1.41)</b>	<b>\$ (1.41)</b>	<b>\$ 0.83</b>	<b>\$ 3.77</b>	<b>\$ 6.65</b>
Total of Reconciliation Items	2.6	0.2	0.3	0.5	2.0	3.0	8.0	8.0	8.0	8.0	8.0	8.0	8.0
Net Income (Non-GAAP)	\$ (29.1)	\$ (3.4)	\$ (9.4)	\$ (3.0)	\$ 7.1	\$ (8.7)	\$ 27.2	\$ (26.5)	\$ (45.9)	\$ (53.7)	\$ 50.5	\$ 196.3	\$ 343.1
Impact of Adjustments to EPS	2.37	0.01	0.01	0.02	0.07	0.11	0.27	0.24	0.21	0.18	0.16	0.16	0.16
EPS (Non-GAAP) (basic)	\$ (15.82)	\$ (0.15)	\$ (0.42)	\$ (0.13)	\$ 0.25	\$ (0.45)	\$ 0.97	\$ (0.84)	\$ (1.27)	\$ (1.29)	\$ 1.04	\$ 4.11	\$ 7.12
EPS (Non-GAAP) (diluted)	\$ (15.82)	\$ (0.15)	\$ (0.42)	\$ (0.13)	\$ 0.24	\$ (0.47)	\$ 0.90	\$ (0.79)	\$ (1.20)	\$ (1.23)	\$ 1.00	\$ 3.93	\$ 6.81
Weighted average shares outstanding (basic)	22.2	22.3	22.3	22.5	27.9	23.7	28.0	32.1	36.7	42.4	46.5	47.7	48.2
Weighted average shares outstanding (diluted)	22.2	22.3	22.3	22.5	29.9	24.2	30.1	34.1	38.8	44.5	48.6	49.9	50.4

Source: Company reports and BMO Capital Markets

**Other companies mentioned (priced as of the close on December 2, 2013):**

Celgene (CELG, \$163.11, Outperform)

## Oncomed Pharmaceuticals (OMED)



FYE (Dec.)	EPS US\$	P/E Hi - Lo	DPS US\$	Yield% Hi - Lo	Payout %	BV US\$	P/B Hi - Lo	ROE %	OMED - Rating as of 17-Jul-13 = NR		
Range*:		na na		NC			>15 >15		Date	Rating Change	Share Price
Current*	ND	na	0.00	0.0	na	-141.7	-0.1	na	1 8-Aug-13	NR to OP	\$19.88

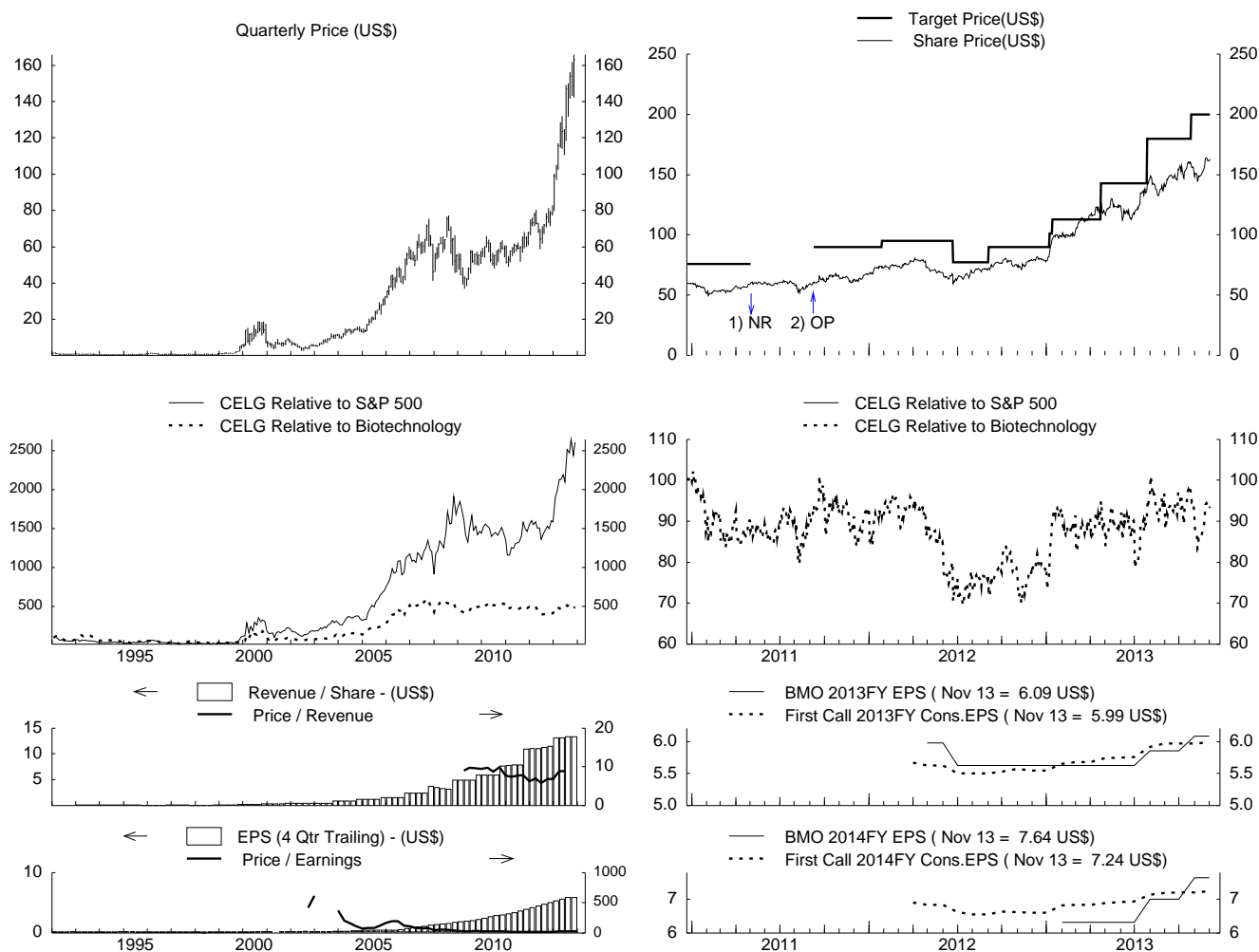
\* Current EPS is the 4 Quarter Trailing to Q3/2013.

\* Valuation metrics are based on high and low for the fiscal year.

\* Range indicates the valuation range for the period presented above.

Last Price ( December 2, 2013): \$14.00  
Sources: IHS Global Insight, Thomson Reuters, BMO Capital Markets.

## Celgene Corporation (CELG)



FYE (Dec.)	EPS US\$	P/E Hi - Lo	DPS US\$	Yield% Hi - Lo	Payout %	BV US\$	P/B Hi - Lo	ROE %
1992	-0.08	na na	0.00	0.0 0.0	0	0.3	5.1 1.9	na
1993	-0.11	na na	0.00	0.0 0.0	0	0.2	5.5 2.6	na
1994	-0.08	na na	0.00	0.0 0.0	0	0.1	6.9 4.0	na
1995	-0.11	na na	0.00	0.0 0.0	0	0.1	8.0 2.6	na
1996	-0.17	na na	0.00	0.0 0.0	0	0.1	12.2 3.8	na
1997	-0.18	na na	0.00	0.0 0.0	0	0.1	>15 6.8	na
1998	-0.17	na na	0.00	0.0 0.0	0	-0.0	-71.9 -17.2	na
1999	-0.15	na na	0.00	0.0 0.0	0	-0.1	-86.5 -9.5	>50
2000	-0.04	na na	0.00	0.0 0.0	0	1.0	>15 4.1	na
2001	-0.01	na na	0.00	0.0 0.0	0	1.0	>15 3.5	na
2002	-0.04	na na	0.00	0.0 0.0	0	0.9	10.8 3.3	na
2003	0.04	>100 >100	0.00	0.0 0.0	0	1.0	12.9 5.3	4
2004	0.17	95.8 55.1	0.00	0.0 0.0	0	1.5	11.2 6.5	14
2005	0.19	>100 65.0	0.00	0.0 0.0	0	1.9	>15 6.6	11
2006	0.53	>100 52.8	0.00	0.0 0.0	0	5.3	11.4 5.3	15
2007	1.06	71.2 38.9	0.00	0.0 0.0	0	7.1	10.7 5.8	17
2008	1.56	49.6 26.4	0.00	0.0 0.0	0	7.6	10.2 5.4	21
2009	2.08	28.0 17.7	0.00	0.0 0.0	0	9.6	6.1 3.9	24
2010	2.80	23.5 17.2	0.00	0.0 0.0	0	12.7	5.2 3.8	25
2011	3.79	18.0 12.9	0.00	0.0 0.0	0	12.6	5.4 3.9	30
2012	4.91	16.9 11.9	0.00	0.0 0.0	0	13.6	6.1 4.3	38
Range*		>100 11.9		0.0 0.0			>15 -17.2	
Current*	5.77	25.7	0.00	0.0	0	13.6	10.9	43
Growth(%):								
5 Year:	32.0		nm			14.0		
10 Year:	nm		nm			31.8		
20 Year:	nm		nm			20.6		

CELG - Rating as of 22-Dec-10 = OP

Date	Rating Change	Share Price
1 3-May-11	OP to NR	\$60.11
2 7-Sep-11	NR to OP	\$60.26

\* Current EPS is the 4 Quarter Trailing to Q3/2013.  
 \* Valuation metrics are based on high and low for the fiscal year.  
 \* Range indicates the valuation range for the period presented above.

Last Price (December 2, 2013): \$163.11  
 Sources: IHS Global Insight, Thomson Reuters, BMO Capital Markets.

## Important Disclosures

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### Methodology and Risks to Our Price Target/Valuation

**Methodology:** We arrive at our price target by applying a 20x multiple to our 2020 GAAP EPS estimate of \$6.65 and discounting at 25%.

**Risks:** There are a number of risks associated with investment in biotechnology companies. These risks include, but are not limited to, risk of clinical trial delay or failure, adverse regulatory decisions including product non-approval, unanticipated adverse effects of drugs which may result in removal from market, risk of manufacturing difficulties, capital market risk which may impair the ability to fund product discovery, research, regulatory filing, manufacture and/or commercialization, risk in attaining and retaining appropriate development or commercial partners, lower-than-expected product adoption, difficulties in gaining appropriate reimbursement for products from payors, unforeseen generic and branded competition, risk to patents being invalidated, and failure to meet earnings and revenue expectations.

### Company Specific Disclosures for CELG

9 - BMO Capital Markets makes a market in this security.

### Methodology and Risks to Our Price Target/Valuation

**Methodology:** Our \$200 price target is based on 25x our 2016 non-GAAP EPS estimate of \$11.91, discounted 20%.

**Risks:** There are a number of risks associated with investment in biotechnology companies. These risks include, but are not limited to, risk of clinical trial delay or failure, adverse regulatory decisions including product non-approval, unanticipated adverse effects of drugs which may result in removal from market, risk of manufacturing difficulties, capital market risk which may impair the ability to fund product discovery, research, regulatory filing, manufacture and/or commercialization, risk in attaining and retaining appropriate development or commercial partners, lower-than-expected product adoption, difficulties in gaining appropriate reimbursement for products from payers, unforeseen generic and branded competition, risk to patents being invalidated, and failure to meet earnings and revenue expectations.

Specific risks to CELG include, but are not limited to, worsening profile for Revlimid in terms of secondary primary malignancies, inability to gain favorable Article 120 review for Revlimid maintenance therapy in Europe, inability to gain Revlimid frontline maintenance approval in Europe, inability to continue to gain market share and extended dosing duration for Revlimid, earlier than expected generic entrants against Revlimid or Thalomid, new safety issues for CELG iMIDS, pipeline failure including failure to gain approval for Abraxane in lung cancer and apremilast for psoriatic arthritis.

### Distribution of Ratings (September 30, 2013)

Rating Category	BMO Rating	BMOCM US Universe*	BMOCM US IB Clients**	BMOCM US IB Clients***	BMOCM Universe****	BMOCM IB Clients*****	Starmine Universe
Buy	Outperform	35.8%	20.3%	47.8%	36.7%	48.3%	52.6%
Hold	Market Perform	59.4%	13.1%	51.1%	56.9%	50.2%	41.7%
Sell	Underperform	4.9%	3.4%	1.1%	6.4%	1.5%	5.6%

\* Reflects rating distribution of all companies covered by BMO Capital Markets Corp. equity research analysts.

\*\* Reflects rating distribution of all companies from which BMO Capital Markets Corp. has received compensation for Investment Banking services as percentage within ratings category.

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Und = Underperform - Forecast to underperform the analyst's coverage universe on a total return basis;

(S) = Speculative investment;

NR = No rating at this time; and

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