

QUICK NOTE



Aratana Therapeutics, Inc.

BUY

(PETX - \$19.67)

Price Target: \$30

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Aratana Stakes Its Claim To Additional Territory On The Companion Animal Therapeutics Frontier Via The Acquisition Of Okapi Sciences And Its Novel Antiviral Product Pipeline. We Reiterate Our BUY Rating And \$30 Price Target.

Yesterday morning, Aratana announced the purchase of Okapi Sciences N.V. for a total of ~\$45M in cash and stock. Okapi is Belgium-based with a proprietary pet therapeutics antiviral platform and 6 clinical/development stage new product candidates. The acquisition establishes a physical presence for Aratana in Europe, enhancing its platform for future business development, academic collaboration, and internal research activities. We believe the organizations share a common culture and focus on enhancing the lives of pets through the development of novel high science molecules specifically for the treatment of companion animal species. We also think the deal is well timed, as it comes as both entities have begun formulating more global strategies and should allow leverage of already established expertise and relationships at E.U. and U.S. regulatory agencies to effectively pursue new product filings and approvals. In the land grab that is emerging for higher-science companion animal therapeutics, Aratana appears to be executing very well on its strategies and capitalizing on its first mover advantage.

AT-011 Dog Canine Parvovirus		
AT-012 Cat Feline Calicivirus		
Lymphoma Diagnostic		
AT-013 Cat Lymphoma		
AT-010 Dog Atopic Dermatitis		Diagnostic Koi Carp KHV Infections
AT-009 Mast Cell – Dog	AT-007 Cat Feline Immunodeficiency virus	AT-006 Cat Feline Herpesvirus
Option 1 Alpha	AT-008 Dog Lymphoma	AT-002 Dog Appetite Stimulant
Option 2 Beta	AT-003 Dog Post-operative Pain	AT-004 Dog B-Cell Lymphoma
Option 3 Gamma	AT-003 Cat Post-operative pain	AT-005 Dog T-Cell Lymphoma
AT-001 Cat Osteoarthritis	AT-002 Cat Appetite Stimulant	AT-001 Dog Osteoarthritis
Proof of Concept	Pilot	Pivotal / Commercial

Source: Company Presentation

Okapi brings 6 programs in clinical development to a growing roster of new product candidates at Aratana (per the table above, now totaling over 20). Okapi's lead product is a novel small molecule antiviral focused on ocular disease caused by the feline herpes virus. The product is currently on track for EU approval in 2015 and would be commercialized under an existing development partnership with Novartis Animal Health. The Company is also currently developing products for the treatment of feline immunodeficiency virus, canine lymphoma and parvovirus, and feline calicivirus. In total, we believe the Okapi products represent a total future market opportunity of roughly \$1B on top of the roughly \$1B TAM represented by the balance of PETX's pipeline. We think we are being measured with our assessment as nearly 2M cats in the U.S. suffer from Feline Immunodeficiency Virus (FIV), as a \$1/day potential treatment for this chronic condition implies the annual domestic market could reach \$700M for just this one product. Although not formally updating our model at this time, we anticipate the addition

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of Okapi's development programs and capabilities will increase our cash burn estimate modestly (by approximately 10% or \$700K per quarter during 2014). Post the initial payment of ~\$14M in cash and the issuance of a ~\$15M promissory note at closing yesterday, the Company has agreed to make an additional payment of ~\$16M in cash or common stock (883,950 shares with a 20% collar) within the next 90 days. Given year-end 2013 cash guidance of \$45-\$50M, Management continues to believe the Company is funded to at least the end of 2014.

As highlighted in our November 2013 research notes on Aratana, we anticipate a number of positive catalysts throughout 2014 pertaining to the Company's development programs including initiation of a pivotal study for AT-002 in dogs, results from proof of concept work for AT-002 in cats, initiation of a pilot field study in client-owned dogs for AT-003, a potential full license for the B-cell Lymphoma product in dogs, a potential conditional license for the T-cell Lymphoma product in dogs, and decisions by Aratana on 3 new product candidates (yet undisclosed) that are actively being evaluated under its recently established "Option Program."

STOCK OPPORTUNITY

We believe PETX has the management team, opportunity and strategy to become a leading provider of innovative specialty pharmaceuticals within the emerging Pet Therapeutics market. We see success with these efforts dramatically improving companion animal veterinary care and continue confident that PETX's strategy to introduce novel pharmaceutical therapies specifically developed for companion animal species will be a winner and drive substantial returns for the Company's shareholders. We accordingly reiterate our BUY rating on Aratana Therapeutics, Inc. with a \$30, DCF driven, price target (see page 5).

RISKS

We believe an investment in Aratana Therapeutics, Inc. involves the following risks:

- **Government Regulation**
The Animal Therapeutic industry is highly regulated by the Center for Veterinary Medicine at both the state and federal level. Changes to existing regulation or new legislation could have a material adverse effect on the PETX's business and financial performance.
- **Dependence On Suppliers**
The Company's business model relies on third parties to manufacture its products. Any malfunctions in the manufacturing processes of its suppliers or other sources of interruption to the supply of products could have an adverse impact on the Company's financial results.
- **Generic Products**
Generic products may be viewed as more cost effective than branded therapeutics. While the Company's IP should protect its products from generic entry in the near term, substantially cheaper generic versions of competing products, even if they are less efficacious, may represent a challenge to the commercialization of the Company's products.
- **Intellectual Property And Trade Secrets**
The Company's financial success is in part dependent on its ability to secure and enforce its substantial intellectual property. If PETX is forced to defend its intellectual property through litigation or if it is unable to maintain propriety of its trade secrets, the Company may incur extra expenses and financial results may be adversely affected.
- **Ongoing Need To Finance Growth**
While the Company finished the third quarter with ~\$52M in cash on its balance sheet and estimates that its current capital is sufficient to fund its operations through the end of 2014, the Company may need to seek additional capital in order to continue to fund its operations in the future. Such financing could be dilutive to stockholders or impose debt covenants and obligations.
- **Future Expirations Of Lock-Up Agreements**
Roughly 13M of the Company shares are subject to a lock-up restriction connected to the Company's public offering are now scheduled to release at 5:00pm ET on February 12th 2014. The release or pending release of a large number of shares from a lock-up restriction may adversely affect the share price of the Company's stock.



CRAIG-HALLUM ALPHA SELECT LIST

The Alpha Select list is an actively researched collection of small, under-followed public companies that we believe have the potential to become much larger. An “acorn” list of sorts, The Alpha Select List will typically consist of sub-\$250M market cap companies with attractive business models, above average growth trends, favorable macro/secular themes and management teams that we believe have the ability to take the business to the next level.

FINANCIALS

Aratana Therapeutics, Inc. Financial Model FISCAL YEAR ENDS DECEMBER

(\$ thousands)	Fiscal 2011A	Fiscal 2012A	Mar Q1-13A	Jun Q2-13A	Sep Q3-13A	Dec Q4-13E	Fiscal 2013E	Fiscal 2014E	Fiscal 2015E	Fiscal 2016E	Fiscal 2017E
Total Revenue	-	-	-	-	-	-	-	2,000	10,000	43,250	99,000
Cost of Sales	-	-	-	-	-	-	-	-	2,500	16,435	38,622
Total Gross Margin	-	-	-	-	-	-	-	2,000	7,500	26,815	60,377
Operating Expenses											
Research and Development	2,196	7,291	2,114	2,469	3,234	3,810	11,627	20,036	14,732	15,473	18,172
Selling, General and Administrative	1,274	2,987	1,226	1,258	1,427	1,738	5,649	8,023	14,633	18,808	28,216
In-Process R&D	0	1,500	0	0	0	0	0	0	0	0	0
Total GAAP Operating Expenses	3,470	11,778	3,340	3,727	4,661	5,548	17,276	28,059	29,365	34,281	46,388
GAAP Income (Loss) from Operations	(3,470)	(11,778)	(3,340)	(3,727)	(4,661)	(5,548)	(17,276)	(26,059)	(21,865)	(7,466)	13,989
Interest income	6	21	3	22	26	26	77	84	52	20	12
Interest Expense	0	0	(24)	(78)	(80)	(80)	(262)	(320)	(340)	(378)	(468)
Other Income	0	121	68	343	44	50	505	100	0	0	0
Pre-tax GAAP Income	(3,464)	(11,636)	(3,293)	(3,440)	(4,671)	(5,552)	(16,956)	(26,195)	(22,153)	(7,824)	13,533
Income Tax (benefit)	0	0	-	-	-	-	0	0	0	0	0
GAAP Net Income	(3,464)	(11,636)	(3,293)	(3,440)	(4,671)	(5,552)	(16,956)	(26,195)	(22,153)	(7,824)	13,533
Modification of Series A Convertible Preferred Stock	(276)	0	0	0	0	0	0	0	0	0	0
Unaccreted Dividends on Convertible Preferred Stock	(902)	(2,035)	(773)	(808)	0	0	(1,581)	0	0	0	0
Net Loss Attributable to Common Stockholders	(4,642)	(13,671)	(4,066)	(4,248)	(4,671)	(5,552)	(18,537)	(26,195)	(22,153)	(7,824)	13,533
EPS Attributable to Common Stockholders	(\$6.93)	(\$17.68)	(\$0.29)	(\$0.30)	(\$0.22)	(\$0.25)	(\$1.04)	(\$1.15)	(\$0.97)	(\$0.34)	\$0.59
Weighted Avg. Shares Outstanding DILUTED	500	658	13,936	14,120	20,806	22,395	17,814	22,718	22,778	22,838	22,898
Margin Analysis % of Sales											
Total Gross Margin	NM	NM	NM	NM	NM	NM	NM	NM	NM	62.0%	61.0%
Research and Development	NM	NM	NM	NM	NM	NM	NM	NM	NM	35.8%	18.4%
Selling, General and Administrative	NM	NM	NM	NM	NM	NM	NM	NM	NM	43.5%	28.5%
In-Process R&D	NM	NM	NM	NM	NM	NM	NM	NM	NM	0.0%	0.0%
Total GAAP Operating Expense	NM	NM	NM	NM	NM	NM	NM	NM	NM	79.3%	46.9%
GAAP Operating Margin	NM	NM	NM	NM	NM	NM	NM	NM	NM	-17.3%	14.1%
Adj. EBITDA Margin	NM	NM	NM	NM	NM	NM	NM	NM	NM	-17.3%	14.1%
GAAP Pre-tax Income	NM	NM	NM	NM	NM	NM	NM	NM	NM	-18.1%	13.7%
Tax Rate (Effective)	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
GAAP Net Margin	NM	NM	NM	NM	NM	NM	NM	NM	NM	-18.1%	13.7%
Percent Change (Yr/Yr)											
Total Revenue	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	128.9%
Selling, General and Administrative	NM	134.5%	146.2%	101.9%	34.0%	NM	89.1%	42.0%	82.4%	28.5%	50.0%
Research and Development	NM	232.0%	20.7%	28.0%	95.1%	NM	59.5%	72.3%	-26.5%	5.0%	17.4%
Total GAAP Operating Expense	NM	239.4%	48.5%	46.0%	71.2%	NM	46.7%	62.4%	4.7%	16.7%	35.3%
GAAP Operating Income	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM
Adj. EBITDA	NM	239.4%	48.5%	NM	NM	NM	46.5%	51.0%	-16.1%	-65.9%	-287.4%
GAAP Pre-tax Income	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM
GAAP Net Income	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM
GAAP Earnings Per Share	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM

Discounted Cash Flow Model

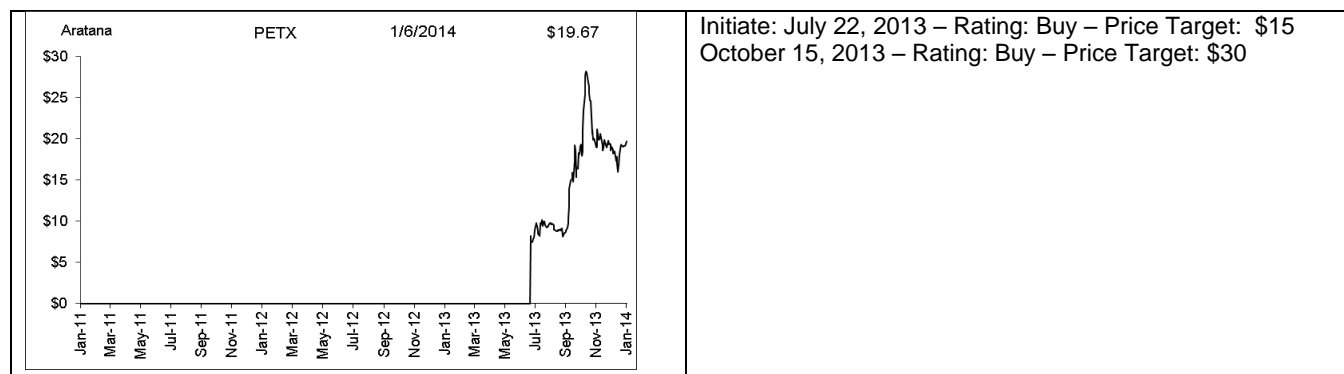
Aratana Therapeutics, Inc. Discounted Cash Flow Model

Estimates										
(\$ in Thousands)	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Total Sales	0	2,000	10,000	43,250	99,000	178,000	290,399	438,680	631,887	650,844
Operating Profit	(17,276)	(26,059)	(21,865)	(7,466)	13,989	46,071	95,832	162,312	252,755	244,066
Less: Cash Taxes Paid	0	0	0	0	0	0	9,583	60,055	93,519	90,305
Operating Profit After Tax	(17,276)	(26,059)	(21,865)	(7,466)	13,989	46,071	86,249	102,256	159,236	153,762
Depreciation & Amortization	20	23	175	547	616	693	779	877	986	1,109
Fixed Cap Expenditures	100	107	2,114	1,163	1,244	1,331	1,424	1,524	1,630	1,745
Working Cap Increase	0	250	1,000	4,156	6,969	9,875	14,050	18,535	24,151	2,370
FCF	(17,356)	(26,394)	(24,804)	(12,238)	6,392	35,558	71,554	83,074	134,440	150,757
PV FCF	(15,496)	(21,041)	(17,655)	(7,777)	3,627	18,015	32,367	33,552	48,481	48,540
Perpetual FCF										
Base FCF	150,757									
Weighted Avg. Cost of Capital (k)	12.0%									
Perpetual Growth Rate (g)	3.0%									
Base Year	2012									
Perpetual Start Year	2022									
Perpetual Value	1,725,330									
PV of Perpetual Growth Period	555,510									
Total FCF										
Value of FCF	678,122									
Intrinsic Value										
Cash	52,306									
Debt	13,691									
After Tax ESO Liability	9,072									
Value of Equity	707,666									
Shares Outstanding	23,804									
Intrinsic Value per Share										
	\$29.73									

Sensitivity Analysis					
Terminal Period Variables			FCF Growth		
Cost of Capital	2.5%	3.0%	3.5%	4.0%	
	9.5%	\$45.29	\$48.36	\$51.95	\$56.19
	10.0%	\$40.92	\$43.47	\$46.43	\$49.87
	11.5%	\$30.95	\$32.50	\$34.25	\$36.23
	12.0%	\$28.39	\$29.73	\$31.22	\$32.90
	12.5%	\$26.13	\$27.28	\$28.56	\$30.00
	13.0%	\$24.10	\$25.11	\$26.22	\$27.45



REQUIRED DISCLOSURES



Source: Baseline

Ratings definitions:

Buy rated stocks generally have twelve month price targets that are more than 20% above the current price. **Hold** rated stocks generally have twelve month price targets near the current price. **Sell** rated stocks generally have no price target and we would sell the stock.

Fundamental trend definitions:

Improving means growth rates of key business metrics are generally accelerating. **Stable** means growth rates of key business metrics are generally steady. **Mixed** means growth rates of some key business metrics are positive but others are negative. **Declining** means growth rates of key business metrics are generally decelerating.

Ratings Distribution (12/31/2013)

Rating	% Of Companies Covered	% With Investment Banking Relationships
Buy	73%	26%
Hold	24%	4%
Sell	3%	0%
Total	100%	20%

Information about valuation methods and risks can be found in the “STOCK OPPORTUNITY” and “RISKS” sections, respectively, of this report.

CHLM makes a market in this security.

CHLM has managed or co-managed an offering of securities for the subject company in the last 12 months. CHLM has received investment banking revenue from the subject company in the last 12 months. CHLM expects to receive or intends to seek compensation for investment banking services from the subject company in the next three months.

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OTHER DISCLOSURES

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