

## Aratana Therapeutics, Inc.

### First Look at Second-Quarter Results; Portfolio Timelines Updated

- Aratana Therapeutics reported second-quarter operating results on Monday afternoon, August 12, providing the first update since its initial public offering in late June. Results included a loss of \$4.248 million, which compared with our estimate for a loss of \$3.6 million and the consensus expectation for a loss of \$4.7 million. Total expenses were slightly higher than our \$3.6 million estimate and accounted for the difference relative to our model. Given that the company's product portfolio is in its early stages, we believe investor focus on Tuesday's 7 a.m. CT conference call will be on progress developing the current compounds as well as the three new products mentioned briefly in Monday's release. While we view Aratana as higher risk than other vet industry peers, we believe the \$210 million enterprise valuation (\$189 million market cap) and unique business model offer a compelling opportunity for small-cap investors.

#### Key Points

- We believe Aratana has sufficient cash to fund operations through the middle of 2015.** Aratana ended the quarter with cash, cash equivalents, and marketable securities of \$20.2 million, which was pre-IPO, and \$57.1 million of cash following the IPO's closing in early July. Management noted an expectation to burn \$7 million-\$12 million in the second half of 2013, and confirmed its current cash balance should last through the end of 2015 (we have forecast an additional equity raise during 2015).
- Several clinical catalysts are expected beginning late in 2013 or 2014.** There are several key events expected before the end of 2013 that are potential catalysts for the stock, mostly notably the initiation of a pivotal efficacy study of AT-002 (for appetite stimulation) for dogs in late 2013 or early 2014. In addition, a dose-ranging field study result in AT-001 (for the treatment of osteoarthritis) for dogs is expected in November 2013. AT-003 in dogs (for the treatment of post-operative pain) initiated dose-ranging studies in the second quarter and management is anticipating initial discussions with the FDA's CVM on a development program later this year. AT-003 also completed a safety study in lab cats and the company expects to start dose-ranging studies later this year. We continue to expect regulatory filings for all these compounds in 2015, with potential approvals in 2016.
- Valuation.** Aratana is trading at \$189 million in market capitalization and an enterprise value of \$210 million. This compares with human therapeutics-oriented specialty pharmaceutical peers with similar clinical progress with a market cap in the \$100 million to \$500 million range. We believe fair value per share with the current portfolio is in the midteens, with upside driven by additional potential compound deals. We look for additional information on Tuesday's call regarding the therapeutic area and clinical timelines associated with the three new products announced in Monday's press release.

*Aratana is a specialty biopharmaceutical company focused solely on the companion-animal market. The company was founded in Kansas City, Kansas, in 2010 to pursue in-licensing, development, and commercialization of novel therapeutics for cats and dogs. The company has three molecules focused on osteoarthritic pain, lack of appetite, and post-surgical pain in both dogs and cats, which, if effective, could reach the market by 2016.*

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Please consult the last page of this report for all disclosures.

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August 13, 2013

Stock Rating: **Outperform**  
Company Profile: **Aggressive Growth**

Symbol: PETX (NASDAQ)  
Price: \$9.53 (52-Wk.: \$7-\$11)  
Market Value (mil.): \$189  
Fiscal Year End: December  
Long-Term EPS Growth Rate:  
Dividend/Yield: None

	2012A	2013E	2014E
<b>Estimates</b>			
EPS Q1	NA	A\$-0.27	NA
Q2	NA	\$-0.19	NA
Q3	NA	\$-0.18	NA
Q4	NA	\$-0.19	NA
FY	\$-0.91	\$-0.84	\$-0.94
CY		\$-0.84	\$-0.94

<b>Valuation</b>			
FY P/E	NM	NM	NM
CY P/E		NM	NM

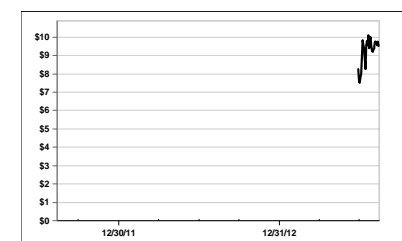
#### Trading Data (FactSet)

Shares Outstanding (mil.)	1
Float (mil.)	1
Average Daily Volume	46,827

#### Financial Data (FactSet)

Long-Term Debt/Total Capital (MRQ)	-0.2
Book Value Per Share (MRQ)	-16.6
Enterprise Value (mil.)	8,732.4
EBITDA (TTM)	-11.4
Enterprise Value/EBITDA (TTM)	-769.0x
Return on Equity (TTM)	-40.6

#### Two-Year Price Performance Chart



Sources: FactSet, William Blair & Company estimates

- **Risks.** We view the following as key risks for Aratana in the next three to five years: 1) the three molecules under clinical development might not be successful and might thus fail to reach the market; 2) larger competitors with greater financial resources, like Zoetis (ZTS \$30.33), might start pursuing a similar in-licensing strategy, causing deal terms to deteriorate; and 3) the company will probably need to raise additional capital within the next two to three years since no product revenues are expected before 2016.
- **Model Adjustments.** Exhibit 1 summarizes how Aratana's second quarter compares with our model (losses were roughly \$700,000 above our model, driven by higher R&D spending). We currently estimate losses and thus cash burn of roughly \$8 million in the second half of 2013, compared with the \$7 million-\$12 million burn expected by management. We will update our estimates and our cash use assumptions following Tuesday's conference call.

### Exhibit 1. Second Quarter 2013 Earnings Variance Analysis

August 12, 2013	2Q FY13 (Actual)	2Q FY12 (Actual)	Year/Year % Change	2Q FY13 (Estimate)	Year/Year % Change	Act.-Est. Difference
Total Net Revenue		\$0	NA	\$0	NA	\$0.000
Direct Costs		0	NA	0	NA	\$0.000
Research & Development	2.469	1.929	28.0%	2.187	13.4%	\$0.282
Selling, General & Administrative	1.258	0.623	101.9%	1.426	128.9%	(\$0.168)
Total operating expenses	3.727	2.552	46.0%	3.613	41.6%	\$0.114
Operating income	(3.727)	(2.552)	46.0%	(3.613)	41.6%	(\$0.114)
Interest and other income (net)	0.287	0.003	9466.7%	0.020	566.7%	\$0.267
Earnings before tax	(3.440)	(2.549)	35.0%	(3.593)	41.0%	\$0.153
Income taxes	0	0	NM	0	NM	\$0.000
<b>Net income (excl. extraord, incl. options)</b>	<b>(3.440)</b>	<b>(2.549)</b>	<b>35.0%</b>	<b>(3.593)</b>	<b>41.0%</b>	<b>\$0.153</b>
Extraordinary item	0	0	NC	0	NC	\$0.000
Unaccreted dividends on convertible pref. stock	(0.808)	(0.522)		0		
Net income, after extra. item	(4.248)	(3.071)	38.3%	(3.593)	17.0%	(\$0.655)

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Additional information is available upon request.

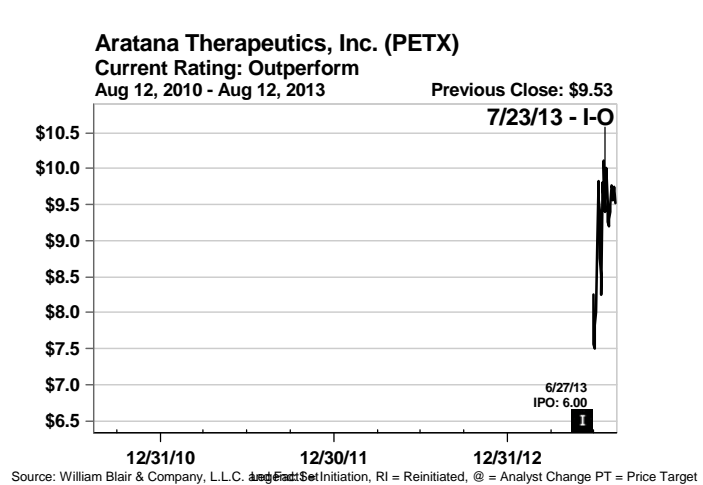
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DOW JONES: 15,419.68

S&P 500: 1,689.47

NASDAQ: 3,669.95



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Coverage Universe	Percent	Inv. Banking Relationships*	Percent
Outperform (Buy)	63	Outperform (Buy)	10
Market Perform (Hold)	33	Market Perform (Hold)	1
Underperform (Sell)	1	Underperform (Sell)	0

\*Percentage of companies in each rating category that are investment banking clients, defined as companies for which William Blair has received compensation for investment banking services within the past 12 months.

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