



# CRAIG-HALLUM CAPITAL GROUP LLC

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Changes	Previous	Current
Rating:		Buy
Fundamental Trend:		Improving
Price Target:	-	\$30.00
FY13A Rev M:	\$0.0 E	\$0.1
FY14E Rev M:	-	\$2.0
FY15E Rev M:	-	\$10.0
FY13A EPS:	(\$1.04)E	(\$0.33)
FY14E EPS:	(\$1.15)	(\$1.50)
FY15E EPS:	(\$0.97)	(\$1.32)

Profile		
Price:		\$19.42
52 Wk Range:	\$6.56	\$29.32
Avg Daily Vol:		268,048
Shares Out M:		29.0
Market Cap M:		\$567.8
Insiders Own:		49%
Short Interest (M):		0.28
BV/Sh:		\$4.04
Est LT EPS Gr:		15%
Net Cash/Sh:		\$1.26
Debt / Capital:		9.8%
Year Ends:		Dec.

Rev (M)	2013A	2014E	2015E
Mar	\$0.0	\$0.2	-
Jun	\$0.0	\$0.3	-
Sep	\$0.0	\$0.6	-
Dec	\$0.1	\$1.0	-
FY	\$0.1	\$2.0	\$10.0

EPS*	2013A	2014E	2015E
Mar	(\$0.29)	(\$0.40)	-
Jun	(\$0.30)	(\$0.39)	-
Sep	(\$0.22)	(\$0.38)	-
Dec	\$0.33	(\$0.34)	-
FY	(\$0.33)	(\$1.50)	(\$1.32)

\*Share counts have been adjusted to reflect IPO shares, the 10/13 private placement, stock issued in the acquisition of Vet Therapeutics and the recent secondary offering.

FY P/E	NM	NM	NM
FY EV/S	NM	NM	NM

Management	
CEO	Stephen St. Peter
CFO	Craig Tooman

## ALPHA SELECT LIST

<b>Aratana Therapeutics, Inc.</b>	<b>BUY</b>
(PETX - \$19.42 intraday)	Price Target: \$30

### Strong Pipeline Remains On Track. Transfer Of Coverage. Maintaining BUY Rating & \$30 Price Target.

*Aratana Therapeutics licenses and develops innovative human pharmaceutical products for the companion animal therapeutics market.*

#### OUR CALL

We have transferred coverage of Aratana Therapeutics Inc. (PETX) and are maintaining a Buy rating and \$30 price target. Aratana reported 4Q13 results which featured the company's first revenues from its Lymphoma franchise acquired 10/13. Subsequently, PETX strengthened its position as a first mover in pet therapeutics and expanded its reach through its acquisition of Okapi Sciences in early January. We are encouraged by the progress within Aratana's pipeline and believe that with a total addressable market now approaching \$2B, PETX is ideally positioned in the lucrative companion animal therapeutics market.

#### KEY TAKEAWAYS

	4Q13		1Q14		FY'13		FY'14	
	Rev	EPS	Rev	EPS	Rev	EPS	Rev	EPS
<b>Actuals:</b>	<b>\$0.1</b>	<b>\$0.33</b>	--	--	<b>\$0.1</b>	<b>(\$0.33)</b>	--	--
C-H Previous Est.:	\$0.0	(\$0.25)	--	--	\$0.0	(\$1.04)	\$2.0	(\$1.15)
Prior Consensus Est.:	\$0.0	(\$0.21)	\$0.1	(\$0.29)	\$0.0	(\$7.48)	\$0.8	(\$1.00)
C-H Revised Est.:	--	--	\$0.2	(\$0.40)	--	--	\$2.0	(\$1.50)

Source: Aratana Therapeutics, Inc., First Call, Craig-Hallum Capital Group

- **Initial Revenue Generated in 4Q13, No Major Surprises in Guidance** – Aratana generated revenue from its Oncology franchise one quarter earlier than we had anticipated. 4Q EPS was aided by a \$15.5M income tax benefit associated with the Vet Therapeutics acquisition. Guidance of \$35M - \$40M of use of cash from operations in 2014 is consistent with what we would have expected given the company's recent acquisitions.
- **Development Programs Commentary**
  - AT-001 Canine: Positive topline results and selection of once daily dosage for field effectiveness study completed in Q4; study beginning in 2Q14; continue to anticipate U.S. approval in 2016.
  - AT-002 Canine: Initiated pivotal field effectiveness trial in client-owned dogs and enrolling patients; anticipate U.S. approval in 2016.
  - AT-003 Canine: Presented program to the CVM and plans to initiate pilot field study in 2Q14; anticipate U.S. approval in 2016.
  - AT-004 B-cell Lymphoma Canine: Received conditional license from the USDA; submitted the data to support a full license which is expected in the next 9-12 months; licensing revenue this quarter was earlier than anticipated.
  - AT-005 T-cell Lymphoma Canine: Received conditional license in January from the USDA; Aratana is conducting studies to support a full license which it expects to receive in 2015.
  - AT-006 Feline Herpes Virus: Expects to file for EU regulatory review in 2014; filed INAD application with CVM and plans on meeting with FDA to present development plan.
  - AT-007 Feline Immunodeficiency Virus: Currently undergoing a pilot trial in EU; filed an INAD with the CVM early this year.
  - Option Programs (3 original programs): Evaluation of two molecules in same therapeutic class yielded only one candidate for further evaluation; opt-in/opt-out decisions on the remaining two molecules continues to be expected in 1H14.



## FINANCIAL PERFORMANCE &amp; OUTLOOK

PETX Earnings Review  
4Q13

	Actual	Estimate	Variance	Y/Y Growth	Notes:	Last Q	Q/Q Growth	Last Y
Revenue	\$0.1	\$0.0	\$0.1	NM	Company generated initial revenue from its Lymphoma franchise	\$0.0	NM	\$0.0
R&D	\$3.1	\$3.8	(\$0.7)	59%		\$3.2	-4%	\$2.0
SG&A	\$4.7	\$1.7	\$2.9	482%	Impacted by one time costs associated with the Vet Therapeutics Acq.	\$1.4	227%	\$0.8
Operating Income	(\$8.1)	(\$5.5)	(\$2.6)	91%		(\$4.7)	75%	(\$4.3)
EPS GAAP	\$0.33	(\$0.25)	\$0.58	NM	Positively impacted by a \$15.5M tax benefit resulting from the purchase of the Vet Therapeutics Acquisition.	(\$0.22)	0%	(\$6.50)
Gross Margin	11.4%	NM	NA			NM		NM
Operating Margin	NM	NM	NA			NM		NM
Net Margin	NM	NM	NA			NM		NM

Source: Aratana Therapeutics, Inc. and Craig-Hallum Capital Group

## Estimate Changes

\$ in mils	1Q14 New	1Q14 Prev.	FY14 New	FY14 Prev.	FY15 New	FY15 Prev.
Total Revenue	\$0.2	--	\$2.0	\$2.0	\$10.0	\$10.0
Y/Y Growth*	NM	--	NM	NM	NM	NM
R&D	\$6.6	--	\$25.4	\$20.0	\$20.6	\$14.7
SG&A	\$3.0	--	\$13.3	\$8.0	\$20.2	\$14.6
Total Operating Expense	\$10.0	--	\$40.3	\$28.1	\$42.6	\$29.4
<b>Total Operating Income</b>	<b>(\$10.0)</b>	--	<b>(\$39.3)</b>	<b>(\$26.1)</b>	<b>(\$35.1)</b>	<b>(\$21.9)</b>
Y/Y growth	NM	--	NM	NM	NM	NM
<b>EPS</b>	<b>(\$0.40)</b>	--	<b>(\$1.50)</b>	<b>(\$1.15)</b>	<b>(\$1.32)</b>	<b>(\$0.97)</b>
Y/Y growth	NM	--	NM	NM	NM	NM
Gross Margin	15.0%	--	46.5%	NM	75.0%	NM
Operating Margin	NM	--	NM	NM	NM	NM
Net Margin	NM	--	NM	NM	NM	NM

Source: Craig-Hallum

## 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 remain confident that PETX's strategy to introduce novel pharmaceutical therapies specially tailored to the companion animal market will be a winner and drive substantial returns. We are reiterating our Buy rating on Aratana and our DCF driven \$30 price target (see page 5).

## RISKS

We believe an investment in Aratana 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 disruptions to manufacturing processes at its suppliers or other interruption to the supply of its 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 expects to exit 2013 with between \$45M-\$50M in cash on its balance sheet and estimates that its current capital is sufficient to fund its operations for over 2 years, 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 4M of the Company shares are subject to a lock-up restriction connected to the Company's public offering are scheduled to release at 4:00pm ET on December 9<sup>th</sup> 2013. Certain of the Company's officers, directors and other stakeholders (representing ~14M shares) have agreed to a new lock-up restriction for a period of 90 days following the closing of the Vet Therapeutics acquisition. 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.

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## 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

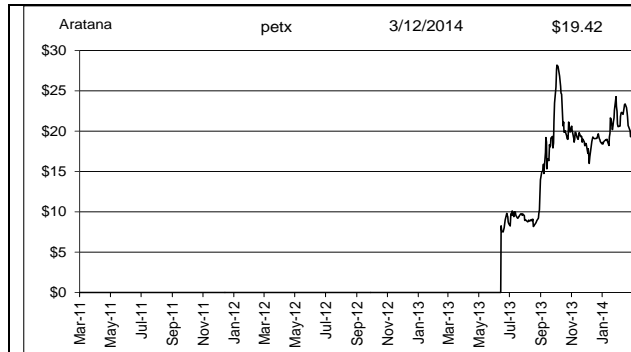
(\$ thousands)	Fiscal 2011A	Mar Q1-12A	Jun Q2-12A	Sep Q3-12A	Dec Q4-12A	Fiscal 2012A	Mar Q1-13A	Jun Q2-13A	Sep Q3-13A	Dec Q4-13A	Fiscal 2013A	Mar Q1-14E	Jun Q2-14E	Sep Q3-14E	Dec Q4-14E	Fiscal 2014E	Fiscal 2015E	Fiscal 2016E	Fiscal 2017E
<b>Total Revenue</b>	-	-	-	-	-	-	-	-	-	123	123	150	250	600	1,000	2,000	10,000	43,250	99,000
Cost of Sales	-	-	-	-	-	-	-	-	-	109	109	128	213	330	400	1,070	2,500	16,435	38,622
<b>Total Gross Margin</b>	-	-	-	-	-	-	-	-	-	14	14	23	38	270	600	930	7,500	26,815	60,377
<b>Operating Expenses</b>																			
Research and Development	2,196	1,751	1,929	1,658	1,953	7,291	2,114	2,469	3,234	3,108	10,925	6,648	6,778	6,443	5,543	25,412	20,638	21,229	23,928
Selling, General and Administrative	1,274	498	623	1,065	801	2,987	1,226	1,258	1,427	4,661	8,572	2,961	3,311	3,436	3,586	13,294	20,169	24,344	33,752
Amortization	0	0	0	0	0	0	0	0	0	380	380	380	380	400	400	1,560	1,800	1,800	1,800
In-Process R&D	0	0	0	0	1,500	1,500	0	0	0	0	0	0	0	0	0	0	0	0	0
<b>Total GAAP Operating Expenses</b>	3,470	2,249	2,552	2,723	4,254	11,778	3,340	3,727	4,661	8,149	19,877	9,989	10,469	10,279	9,529	40,266	42,607	47,373	59,480
<b>GAAP Income (Loss) from Operations</b>	(3,470)	(2,249)	(2,552)	(2,723)	(4,254)	(11,778)	(3,340)	(3,727)	(4,661)	(8,135)	(19,863)	(9,967)	(10,432)	(10,009)	(8,929)	(39,336)	(35,107)	(20,558)	897
Interest income	6	4	3	5	9	21	3	22	26	25	76	23	21	19	17	80	48	16	11
Interest Expense	0	0	0	0	0	0	(24)	(78)	(80)	(250)	(432)	(100)	(100)	(100)	(100)	(400)	(420)	(458)	(548)
Other Income	0	0	0	81	40	121	68	343	44	23	478	100	0	0	0	100	0	0	0
<b>Pre-tax GAAP Income</b>	(3,464)	(2,245)	(2,549)	(2,637)	(4,205)	(11,636)	(3,293)	(3,440)	(4,671)	(8,337)	(19,741)	(9,944)	(10,511)	(10,090)	(9,012)	(39,556)	(35,479)	(21,000)	360
Income Tax (benefit)	0	-	-	-	-	0	-	-	-	(15,455)	(15,455)	-	-	-	-	0	0	0	0
<b>GAAP Net Income</b>	(3,464)	(2,245)	(2,549)	(2,637)	(4,205)	(11,636)	(3,293)	(3,440)	(4,671)	7,118	(4,286)	(9,944)	(10,511)	(10,090)	(9,012)	(39,556)	(35,479)	(21,000)	360
<b>EPS Attributable to Common Stockholders</b>	(\$6.93)	(\$4.49)	(\$10.21)	(\$9.64)	(\$6.50)	(\$17.68)	(\$0.29)	(\$0.30)	(\$0.22)	\$0.33	(\$0.33)	(\$0.40)	(\$0.39)	(\$0.38)	(\$0.34)	(\$1.50)	(\$1.32)	(\$0.78)	\$0.01
Weighted Avg. Shares Outstanding DILUTED	500	500	301	328	730	658	13,936	14,120	20,806	21,321	17,546	25,055	26,787	26,802	26,817	26,365	26,854	26,914	26,974
<b>Margin Analysis % of Sales</b>																			
Total Gross Margin	NM	NM	NM	NM	NM	NM	NM	NM	NM	11.4%	NM	15.0%	15.0%	45.0%	60.0%	46.5%	75.0%	62.0%	61.0%
Research and Development	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	49.1%	24.2%
Selling, General and Administrative	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	56.3%	34.1%
In-Process R&D	NM	NM	NM	NM	NM	NM	NM	NM	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	NM	NM	NM	NM	NM	NM	NM	NM	109.5%	60.1%
<b>GAAP Operating Margin</b>	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	-47.5%	0.9%
Adj. EBITDA Margin	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	-47.5%	0.9%
GAAP Pre-tax Income	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	-48.6%	0.4%
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%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
<b>GAAP Net Margin</b>	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	-48.6%	0.4%
<b>Percent Change (Yr/Yr)</b>																			
Total Revenue	NM					NM	NM	NM	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%	481.9%	187.0%	141.5%	163.2%	140.8%	-23.1%	55.1%	51.7%	20.7%	38.6%
Research and Development	NM					232.0%	20.7%	28.0%	95.1%	59.1%	49.8%	214.5%	174.5%	99.2%	78.3%	132.6%	-18.8%	2.9%	12.7%
Total GAAP Operating Expense	NM					239.4%	48.5%	46.0%	71.2%	91.6%	68.8%	199.1%	180.9%	120.5%	16.9%	102.6%	5.8%	11.2%	25.6%
<b>GAAP Operating Income</b>	NM					NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM
Adj. EBITDA	NM					239.4%	48.5%	NM	NM	NM	68.5%	198.4%	179.9%	114.7%	9.8%	98.2%	-10.8%	-41.4%	-104.4%
GAAP Pre-tax Income	NM					NM	NM	NM	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	NM	NM	NM	NM
<b>GAAP Earnings Per Share</b>	NM					NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM

## Discounted Cash Flow Model

### Aratana Therapeutics, Inc. Discounted Cash Flow Model

Estimates		2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
(\$ in Thousands)											
Total Sales		2,000	10,000	43,250	99,000	178,000	290,399	438,680	581,887	706,887	728,094
Operating Profit		(39,336)	(7,382)	(1,931)	2,587	11,923	87,120	142,571	203,660	265,083	254,833
Less: Cash Taxes Paid		0	0	0	0	0	8,712	52,751	75,354	98,081	94,288
Operating Profit After Tax		(39,336)	(7,382)	(1,931)	2,587	11,923	78,408	89,820	128,306	167,002	160,545
Depreciation & Amortization		23	176	548	616	693	780	878	987	1,111	1,250
Fixed Cap Expenditures		107	2,114	1,163	1,244	1,331	1,424	1,524	1,630	1,745	1,867
Working Cap Increase		250	1,250	4,156	6,969	9,875	14,050	18,535	17,901	15,625	2,651
FCF		(39,670)	(10,571)	(6,701)	(5,010)	1,410	63,714	70,638	109,762	150,743	157,277
PV FCF		(35,420)	(8,427)	(4,770)	(3,184)	800	32,279	31,953	44,331	54,359	50,639
<b>Perpetual FCF</b>											
Base FCF		157,277									
Weighted Avg. Cost of Capital (k)		12.0%									
Perpetual Growth Rate (g)		3.0%									
Base Year		2013									
Perpetual Start Year		2023									
Perpetual Value		1,799,943									
PV of Perpetual Growth Period		579,534									
<b>Total FCF</b>											
Value of FCF		742,095									
<b>Intrinsic Value</b>											
Cash		136,254									
Debt		9,310									
After Tax ESO Liability		8,338									
Value of Equity		860,702									
Shares Outstanding		28,954									
<b>Intrinsic Value per Share</b>		<b>\$29.73</b>									

Sensitivity Analysis					
Terminal Period Variables		FCF Growth			
Cost of Capital	2.5%	3.0%	3.5%	4.0%	
	9.5%	\$43.27	\$45.90	\$48.98	\$52.62
	10.0%	\$39.47	\$41.67	\$44.20	\$47.15
	11.5%	\$30.81	\$32.14	\$33.64	\$35.34
	12.0%	\$28.58	<b>\$29.73</b>	\$31.01	\$32.45
	12.5%	\$26.60	\$27.59	\$28.69	\$29.92
	13.0%	\$24.83	\$25.69	\$26.64	\$27.70

**REQUIRED DISCLOSURES**

Initiate: July 22, 2013 – Rating: Buy – Price Target: \$15  
 October 15, 2013 – Rating: Buy – Price Target: \$30  
 Analyst Change:  
 March 13, 2014 – Rating: Buy – Price Target: \$30

Source: Thomson

**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.

Analysts receive no direct compensation in connection with the firm's investment banking business. Analysts may be eligible for bonus compensation based on the overall profitability of the firm, which takes into account revenues from all of the firm's business, including investment banking.

**OTHER DISCLOSURES**

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