

Neothetics Inc.

NEOT - BUY - More Reasons Why NEOT is Our Top Small Cap Pick in '15

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FLASH NOTE

SECTOR: Specialty Pharmaceuticals

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Conclusions: We hosted a day of meetings with CEO George Mahaffey and CFO Susan Knudson of NEOT (BUY, \$6.75) on 1/22/14. Post our meetings with NEOT, we continue to think LIPO-202 could be the next Botox (which has sales of \$1B+) for fat reduction, with peak sales potential of over \$1B (we expect a launch in '18), but Neothetics' market cap of only \$90MM (and ~\$75MM of cash at the end of '14) suggests to us that the Street is underestimating this opportunity. Also companies similar to NEOT, like KYTH (NC, \$35.57) and RVNC (NC, \$16.81), have much larger market caps (~\$800MM and \$400MM, respectively). We believe investing in Neothetics could provide a good entry point into the body contouring market early in its growth and development. Also, in our view, there is a free call option on LIPO-102, which has orphan designation for the treatment of exophthalmos. Neothetics' valuation ascribes no value for this pipeline product. We highlight the key takeaways that support our positive investment thesis below.

- AGN (NEUTRAL, \$222.79) and ZLTQ (NC, \$30.32) have begun a pilot program to co-promote AGN's injectable products (Botox and Juvederm) along with ZLTQ's CoolSculpting treatment (device to reduce fat). Patients who participate in the AGN and ZLTQ program will get a \$100 rebate on AGN injectables if they are also receiving CoolSculpting. This underscores why we think patients already using cosmetic injectables such as Botox and Juvederm would add a product like LIPO-202 to their aesthetic regimen. Having an established company like AGN interested in non-surgical fat reduction validates the market opportunity in our view. We think additional partnerships similar to the AGN and ZLTQ program could drive further adoption and awareness of non-surgical fat reduction.
- A related company, KYTH, has a drug, ATX-101 (deoxycholic acid), for improvement in the appearance of moderate to severe submental fullness (elimination of chin fat). KYTH's AdCom is scheduled for 3/9/15 and a good outcome could provide positive read throughs for NEOT. KYTH has a PDUFA date of 5/13/15. Interestingly, KYTH noted at a recent conference on 1/12/15 that it will not be pursuing an indication for ATX-101 to reduce belly fat. This is positive for NEOT because it takes away one potential competitor for its drug. Interestingly, we think NEOT's drug could be used in other areas of the body in addition to the belly, such as the chin.
- There are an increasing number of doctors looking to add cosmetic procedures to their practice to increase revenue. For example, OB-GYNs are a growing class of doctors that are adding aesthetic procedures to their treatment regimens.
- Although the efficacy rate of NEOT's Phase 2 results for LIPO-202 were not high, we still think that uptake will be robust as long as the drug gets approved because this is a cash pay aesthetic product so if patients feel better using the drug then they will get the treatment done.
- NEOT will be presenting data to physicians at two upcoming meetings. We think this should increase awareness and appreciation of LIPO-202.

Potential Catalysts: 1) LIPO-202 Phase III results, '15 and '16; 2) LIPO-202 – we estimate submission in 2H16; 3) LIPO-202 – we estimate approval and launch in 2H17.

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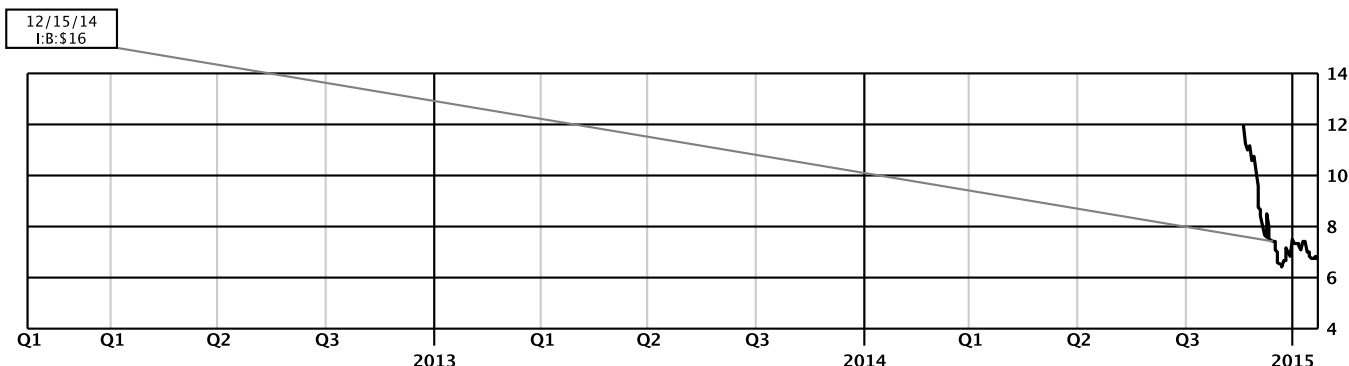
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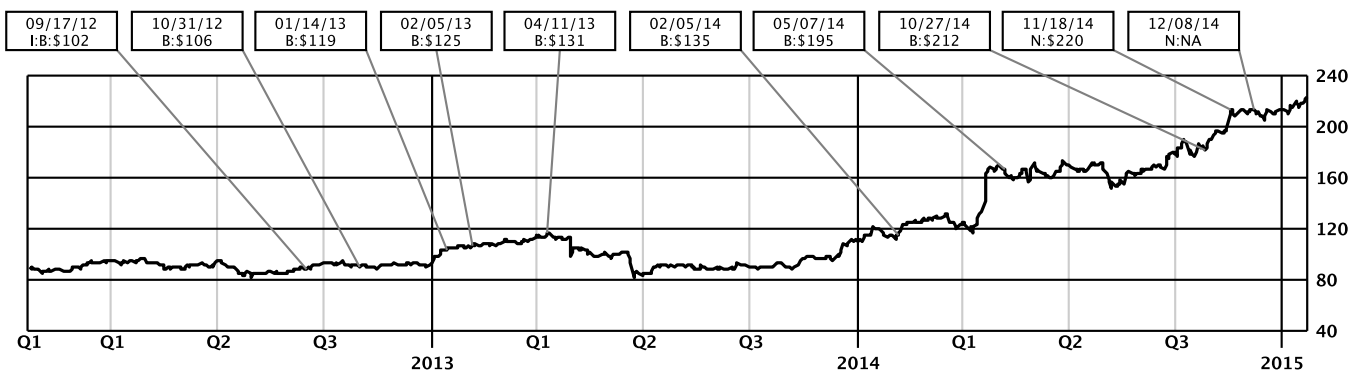
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Rating and Price Target History for: Neothetics Inc. (NEOT) as of 01-22-2015



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