

January 30, 2015

HEALTHCARE/BIO TECHNOLOGY

Stock Rating:
OUTPERFORM

12-18 mo. Price Target \$42.00
OCUL - NASDAQ \$30.23

3-5 Yr. EPS Gr. Rate	NA
52-Wk Range	\$30.45-\$11.90
Shares Outstanding	20.6M
Float	6.5M
Market Capitalization	\$644.6M
Avg. Daily Trading Volume	80,860
Dividend/Div Yield	NA/NM
Book Value	\$0.72
Fiscal Year Ends	Dec
2014E ROE	NA
LT Debt	\$15.0M
Preferred	NA
Common Equity	\$56M
Convertible Available	No

Trading range since July 2014 IPO.

EPS Diluted	Q1	Q2	Q3	Q4	Year	Mult.
2013A	--	--	--	--	(5.11)	NM
2014E	(2.45)A	(2.10)A	(0.48)A	(0.40)	(2.78)	NM
2015E	--	--	--	--	(1.31)	NM
Revenue (\$/mil)	Q1	Q2	Q3	Q4	Year	Mult.
2013A	--	--	--	--	0.0	NM
2014E	0.0A	0.1A	0.1A	0.2	0.5	NM
2015E	--	--	--	--	1.8	NM

Ocular Therapeutix

Still More to Go, Adding Allergic Conjunctivitis Revs, PT to \$42

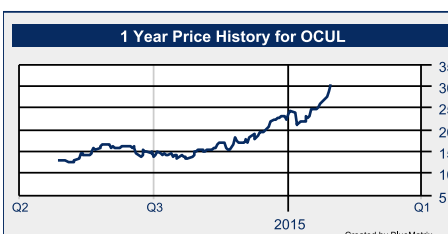
SUMMARY

After its strong run (stock is ~\$30 and our PT was \$25), investors are appropriately crediting Ocular's pipeline with implied success in glaucoma (OTX-TP) and post-cataract surgery pain/inflammation (OTX-DP). However, we see another leg of upside emerging for Ocular's sustained drug-delivery platform with the inclusion of allergic conjunctivitis (AC) OTX-DP revs in our model, driving our PT to \$42. Recall Ocular reported positive Ph.2 results in AC in 4Q14 (see our [note](#)) and recent FDA interaction (4Q14) clarified the path forward in AC (see below). We expect OTX-DP Ph.3 data in AC in late 2015. With ~8% peak share in AC, we see peak AC revs for OTX-DP of ~\$80M (we model mid-2017 launch).

KEY POINTS

- **Adding AC to model.** We estimate OTX-DP peak US share in AC of ~8%. We drive our model (Ex.3) off AC eye-drop scrips (~6.8M TRx 2014, Ex.1) and assume one TRx for OTX-DP lasts ~2 months (30-day retention rate ~97%). We assume pricing for a pair of plugs of ~\$250, in line with branded drops.
- **AC Ph.2 data recap.** Recall the six-week trial (N=68) showed statistically significant lower ocular itching and redness vs. placebo at days 14, 28, and 42. Given a single-administration sustained-release formulation, we see achieving stat. sig. vs. placebo at the distant six-week time point as particularly impressive.
- **Comp to steroid drops.** In Ph.2, OTX-DP showed a >0.5 point mean benefit vs. placebo on itching/redness (5-point scale) at all time-points. This looks in line with Alrex with an effect size of ~0.55/~0.8 on itching/redness. That said, with 4x/day dosing for Alrex, OTX-DP provides sig. compliance/convenience and safety (no IOP spike) advantages.
- **Ph.3 design.** Two replicate Ph.3 trials (N~144 total) will start 1H15 with expected design (CAC model) and endpoints per Ph.2. Thus we see the Ph.3s as low-risk trials. Imptly, we would expect Ph.3 to permit plug replacement (Ph.2 did not) to capture add'l mean benefits on itching/redness.
- **2015 catalysts:** 1) OTX-DP Phase 3a/3b readout in post-surgical inflammation/pain (1Q15); 2) initiation of OTX-DP Phase 3 in AC (1H15); 3) NDA submission for OTX-DP (2Q15); 4) feedback from Pharma partners on next steps for anti-VEGF (2Q15); and 5) OTX-TP Phase 2b readout in glaucoma (3Q15).

Stock Price Performance



Company Description

Ocular Therapeutix, Inc. is a biopharmaceutical company focused on the development and commercialization of therapies for diseases and conditions of the eye using its hydrogel platform technology.

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Exhibit 1**TRx for Ophthalmic Solution Drugs in Allergic Conjunctivitis**

DRUG (Generic Name)	TRx			
	2014	%	2013	%
OLOPATADINE HCL	4,064,851	60.2%	4,011,492	58.3%
LOTEPREDNOL ETABONATE	734,034	10.9%	1,022,343	14.9%
AZELASTINE HCL	623,893	9.2%	547,873	8.0%
KETOTIFEN FUMARATE	587,940	8.7%	502,505	7.3%
ALCAFTADINE	259,534	3.8%	311,359	4.5%
BEPOTASTINE BESILATE	187,758	2.8%	217,048	3.2%
EPINASTINE HCL	169,538	2.5%	169,575	2.5%
DEXAMETHASONE SOD PHOSPHATE	98,061	1.5%	66,760	1.0%
NEDOCROMIL SODIUM	11,269	0.2%	12,785	0.2%
LODOXAMIDE TROMETHAMINE	7,259	0.1%	8,309	0.1%
DEXAMETHASONE	5,990	0.1%	4,756	0.1%
EMEDASTINE DIFUMARATE	1,077	0.0%	998	0.0%
TOTAL	6,751,204	100.0%	6,875,803	100.0%

Source: Symphony Health, Oppenheimer Research.

Valuation

Exhibit 2

DCF Valuation

Time of Valuation	Jan-15
WACC	10%
Intermediate CF Growth	20%
Terminal FCF Growth	0.0%
NPV FCF (2014-2030)	\$552
Terminal FCF Value \$MM	\$372
Total PV FCF \$MM	\$925
Cash \$MM	\$81
Debt \$MM	\$14
Equity Value \$MM	\$992
Diluted Shares Outstanding (MM)	23.8

DCF Value / Share	\$42
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Source: Oppenheimer Research.

Valuation Method: We value Ocular using a discounted cash flow (DCF) analysis with a weighted average cost of capital (WACC) of 10% and a 0% terminal growth rate post 2032.

Discount Rate: Our valuation framework utilizes a 10% discount rate for commercial stage companies that have achieved Phase 2 proof-of-concept and have products on the market.

Terminal Growth Rate: We explicitly model cash flows to 2024. From 2025 to 2030, we grow cash flows at 20% of the prior year's cash flow growth rate. After 2031 we assume a terminal growth rate of 0% yielding a terminal value of ~\$372.

Market Model for Allergic Conjunctivitis

Exhibit 3

US Allergic Conjunctivitis Model	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024
TRx for Allergic Conjunctivitis	6,875,803	6,751,204	6,784,960	6,818,885	6,852,979	6,887,244	6,921,680	6,956,289	6,991,070	7,026,026	7,061,156	7,096,461
Growth rate		-2%	1%	1%	1%	1%	1%	1%	1%	1%	1%	1%
Number of TRx/Year	2.0	2.0	2.0	2.0	2.0	2.0	2.0	2.0	2.0	2.0	2.0	2.0
Patients with Allergic Conjunctivitis	3,437,902	3,375,602	3,392,480	3,409,442	3,426,490	3,443,622	3,460,840	3,478,144	3,495,535	3,513,013	3,530,578	3,548,231
Market Penetration Rate	0%	0%	0%	0%	3%	5%	8%	8%	8%	8%	8%	8%
OTX-DP Patients	0	0	0	0	85,662	172,181	276,867	278,252	279,643	281,041	282,446	283,858
Cost per 2 plugs	\$250	\$253	\$255	\$258	\$260	\$263	\$265	\$268	\$271	\$273	\$276	\$279
Cost Growth %	0%	1%	1%	1%	1%	1%	1%	1%	1%	1%	1%	1%
OTX-DP TRx (2-month plug)	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0
Revenue (\$MM)	\$0	\$0	\$0	\$0	\$22	\$45	\$73	\$75	\$76	\$77	\$78	\$79
EU Allergic Conjunctivitis Model	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024
% US	0%	0%	0%	0%	0%	60%	60%	60%	60%	60%	60%	60%
Revenue (\$MM)	\$0	\$0	\$0	\$0	\$0	\$27	\$44	\$45	\$45	\$46	\$47	\$48
20% Royalty from Future Partner	\$0	\$0	\$0	\$0	\$0	\$5	\$9	\$9	\$9	\$9	\$9	\$10
JP Allergic Conjunctivitis Model	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024
%US	0%	0%	0%	0%	0%	40%	40%	40%	40%	40%	40%	40%
Revenue (\$MM)	\$0	\$0	\$0	\$0	\$0	\$18	\$29	\$30	\$30	\$31	\$31	\$32
20% Royalty from Future Partner	\$0	\$0	\$0	\$0	\$0	\$4	\$6	\$6	\$6	\$6	\$6	\$6
Total Revenue (\$MM)	\$0	\$0	\$0	\$0	\$22	\$54	\$88	\$89	\$91	\$92	\$94	\$95

Sources: Oppenheimer Research.

Exhibit 4

Ocular Therapeutix Income Statement

(\$MMs except per share data)

	2013	2014E	2015E	2016E	2017E	2018E	2019E	2020E	2021E	2022E	2023E	2024E
OTX-TP Glaucoma		0.0	0.0	0.0	0.0	25.2	63.2	107.0	153.8	203.1	254.8	309.2
OTX-DP Allergy		0.0	0.0	0.0	22.3	54.3	88.2	89.5	90.8	92.2	93.6	95.0
OTX-DP Inflammation		0.0	0.0	4.8	15.7	27.9	35.6	37.4	38.1	38.9	39.7	40.5
ReSure		0.5	1.8	3.1	6.5	8.0	10.3	12.8	15.0	15.6	16.4	17.1
Total Revenue	0.0	0.5	1.8	7.9	44.4	115.5	197.3	246.7	297.9	349.8	404.4	461.8
COGS		0.1	0.1	0.8	7.2	18.6	31.5	37.2	43.2	49.3	55.8	62.5
OTX-TP Glaucoma		0.0	0.0	0.0	0.0	2.5	6.3	10.7	15.4	20.3	25.5	30.9
OTX-DP Allergy		0.0	0.0	0.0	2.2	5.4	8.8	8.9	9.1	9.2	9.4	9.5
OTX-DP Inflammation		0.0	0.0	0.5	1.6	2.8	3.6	3.7	3.8	3.9	4.0	4.0
ReSure		0.0	0.1	0.2	0.3	0.4	0.5	0.6	0.8	0.8	0.8	0.9
Royalties to Incept		0.0	0.0	0.2	0.9	2.1	3.4	4.2	5.1	5.9	6.8	7.7
R&D	10.5	19.2	20.2	21.2	23.3	25.7	28.2	31.0	34.1	37.6	41.3	45.5
SG&A	2.4	9.0	9.9	17.4	26.0	48.2	53.0	55.7	56.2	56.8	57.3	57.9
Operating Income	(12.9)	(27.9)	(28.4)	(31.4)	(12.2)	23.0	84.5	122.7	164.3	206.1	250.0	295.9
Interest Income	0.0	0.4	0.4	0.2	0.3	0.4	0.7	1.0	1.3	1.8	2.4	3.1
Interest Expense	(0.4)	(1.0)	1.0	0.7	0.3	0.5	0.0	0.0	0.0	0.0	0.0	0.0
Other income (expense), net	0.0	(0.4)										
Pre-Tax Income	(13.3)	(28.9)	(27.0)	(30.5)	(11.6)	23.9	85.2	123.7	165.7	207.9	252.4	299.0
Tax Expense (Benefit)	0	0.0	0.0	0.0	0.0	0.0	0.0	38.9	58	72.8	88.3	104.7
Tax Rate	35.0%	35.0%	35.0%	35.0%	35.0%	35.0%	35.0%	35.0%	35.0%	35.0%	35.0%	35.0%
Net Income to Common	(13.3)	(28.9)	(27.0)	(30.5)	(11.6)	23.9	85.2	84.8	107.7	135.2	164.1	194.4
Net Income per Share	(5.11)	(2.78)	(1.31)	(1.35)	(0.47)	0.80	2.85	2.83	3.60	4.51	5.47	6.47
Weighted average shares, basic	2.6	10.4	20.6	22.6	24.6	26.7	26.7	26.7	26.7	26.8	26.8	26.8
Weighted average shares, diluted	2.6	11.2	23.8	25.8	27.8	29.9	29.9	29.9	29.9	30.0	30.0	30.0

Sources: Ocular Therapeutix Filings, Oppenheimer Research.

Exhibit 5**Ocular Therapeutix Balance Sheet**

(\$MMs except per share data)

	2013	2014E	2015E	2016E	2017E	2018E	2019E	2020E	2021E	2022E	2023E	2024E
Assets												
Cash and Equivalents	17.5	71.1	49.6	65.1	87.6	138.4	196.6	266.1	357.9	477.6	625.9	803.7
Prepaid Expenses and Other Current Assets	0.2	0.3	1.2	1.6	2.3	3.7	4.5	5.0	5.3	5.7	6.2	6.6
Inventory	-	0.0	0.1	0.7	6.0	15.5	26.2	31.0	36.0	41.1	46.5	52.1
Accounts receivable from related party	0.0	0.0	-	-	-	-	-	-	-	-	-	-
Deferred Offering Costs	-	-	-	-	-	-	-	-	-	-	-	-
Receivables	0.3	0.1	0.2	1.0	5.5	14.4	24.7	30.8	37.2	43.7	50.6	57.7
Other Current Assets	-	0.0	0.0	0.2	1.1	2.9	4.9	6.2	7.4	8.7	10.1	11.5
Current Assets	18.0	71.6	51.2	68.6	102.6	175.0	256.9	339.0	443.9	576.9	739.2	931.7
Property, Plant, & Equipment	0.9	1.7	1.5	1.5	2.9	6.8	13.0	19.2	25.1	30.5	35.8	41.3
Restricted Cash	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2
Deposits	-	-	-	-	-	-	-	-	-	-	-	-
Other Long-Term Assets	-	-	-	-	-	-	-	-	-	-	-	-
Total Assets	19.1	73.6	53.0	70.3	105.7	182.0	270.1	358.5	469.2	607.6	775.2	973.2
Liabilities												
Accounts Payables	0.5	0.9	3.0	3.9	5.7	9.2	11.3	12.4	13.4	14.4	15.4	16.6
Accrued Liabilities	0.7	1.0	3.6	4.7	6.8	11.1	13.5	14.9	16.0	17.2	18.5	19.9
Deferred Revenue	0.3	0.3	0.3	0.3	0.3	0.3	0.3	0.3	0.3	0.3	0.3	0.3
Notes Payable, net of discount, current	1.8	-	-	-	-	-	-	-	-	-	-	-
Taxes Payable	-	0.0	0.0	0.1	0.4	1.2	2.0	2.5	3.0	3.5	4.0	4.6
Loans Payable, Current Portion	-	1.1	4.5	4.5	3.4	-	-	-	-	-	-	-
Other	-	0.4	1.5	2.0	2.8	4.6	5.6	6.2	6.7	7.2	7.7	8.3
Current Liabilities	3.3	3.7	13.0	15.5	19.4	26.4	32.7	36.2	39.3	42.5	46.0	49.7
Preferred Stock Warrants	0.3	-	-	-	-	-	-	-	-	-	-	-
Deferred rent, long-term	0.0	-	-	-	-	-	-	-	-	-	-	-
Loans Payable, Less Current Portion	-	12.5	9.1	7.9	4.5	3.4	-	-	-	-	-	-
Other Liabilities	-	-	-	-	-	-	-	-	-	-	-	-
Notes Payable, net of discount, long-term	0.7	-	-	-	-	-	-	-	-	-	-	-
Total Liabilities	4.3	16.1	22.0	23.4	23.9	29.8	32.7	36.2	39.3	42.5	46.0	49.7
Redeemable convertible preferred stock	74.3	-	-	-	-	-	-	-	-	-	-	-
Common stock	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Additional paid-in capital	1.3	147.1	147.1	193.6	240.1	286.5	286.5	286.5	286.5	286.5	286.5	286.5
Accumulated surplus/(deficit)	(60.8)	(89.7)	(116.1)	(146.7)	(158.2)	(134.3)	(49.1)	35.7	143.4	278.6	442.6	637.0
Shareholders' Equity	14.9	57.4	30.9	46.9	81.8	152.2	237.5	322.3	430.0	565.1	729.2	923.5
Total Liabilities & Equity	19.1	73.6	53.0	70.3	105.7	182.0	270.1	358.5	469.2	607.6	775.2	973.2

Sources: Ocular Therapeutix Filings, Oppenheimer Research.

Exhibit 6

Ocular Therapeutix Statement of Cash Flows

(\$MMs except per share data)

	2013	2014E	2015E	2016E	2017E	2018E	2019E	2020E	2021E	2022E	2023E	2024E
Operating Cash Flows												
Net Income	(13.3)	(28.9)	(27.0)	(30.5)	(11.6)	23.9	85.2	84.8	107.7	135.2	164.1	194.4
Adjustments:												
Non-cash Interest expense	0.0	0.1										
Licensing and consulting fees paid in common stock		2.4										
Depreciation	0.4	0.5	0.3	0.4	0.8	1.9	3.7	6.1	9.0	12.1	15.0	17.6
Amortization	0.9	-	-	-	-	-	-	-	-	-	-	-
Loss on Extinguishment of Debt	-	0.1	-	-	-	-	-	-	-	-	-	-
Share-Based Compensation	0.5	1.7	0.6	-	-	-	-	-	-	-	-	-
Revaluation of preferred stock warrants	(0.0)	0.4										
Other	-	0.0	-	-	-	-	-	-	-	-	-	-
Total Operating Sources	(11.5)	(23.9)	(26.2)	(30.1)	(10.8)	25.8	88.9	90.9	116.7	147.2	179.0	212.0
Prepaid Expenses and other current assets	0.1	0.5	(0.9)	(0.4)	(0.7)	(1.4)	(0.8)	(0.4)	(0.4)	(0.4)	(0.4)	(0.5)
Inventory	-	(0.0)	(0.1)	(0.6)	(5.3)	(9.5)	(10.7)	(4.8)	(5.0)	(5.1)	(5.4)	(5.6)
Accounts Receivable from third party	0.0	0.0	0.0	-	-	-	-	-	-	-	-	-
Accounts Receivables	(0.3)	0.2	(0.1)	(0.8)	(4.6)	(8.9)	(10.2)	(6.2)	(6.4)	(6.5)	(6.8)	(7.2)
Other Current Assets	-	(0.0)	(0.0)	(0.2)	(0.9)	(1.8)	(2.0)	(1.2)	(1.3)	(1.3)	(1.4)	(1.4)
Accounts Payable	(0.2)	0.3	2.2	0.9	1.7	3.6	2.0	1.1	1.0	1.0	1.1	1.1
Accrued Liabilities	(0.2)	(0.4)	2.6	1.1	2.1	4.3	2.4	1.3	1.2	1.2	1.3	1.4
Taxes Payable	-	0.0	0.0	0.1	0.4	0.7	0.8	0.5	0.5	0.5	0.5	0.6
Deferred Revenue	0.3	-	-	-	-	-	-	-	-	-	-	-
Other	-	0.4	1.1	0.5	0.9	1.8	1.0	0.6	0.5	0.5	0.5	0.6
Changes in Operating Assets/Liabilities	(0.2)	1.0	4.8	0.7	(6.5)	(11.2)	(17.5)	(9.1)	(9.9)	(10.1)	(10.5)	(11.0)
Operating Cash Flow	(11.7)	(22.9)	(21.4)	(29.4)	(17.2)	14.6	71.4	81.8	106.8	137.2	168.5	200.9
Capital Expenditures	(0.4)	(1.2)	(0.1)	(0.4)	(2.2)	(5.8)	(9.9)	(12.3)	(14.9)	(17.5)	(20.2)	(23.1)
Purchase/Maturities of Securities	-	-	-	-	-	-	-	-	-	-	-	-
Other	-	-	-	-	-	-	-	-	-	-	-	-
Investing Cash Flow	(0.4)	(1.2)	(0.1)	(0.4)	(2.2)	(5.8)	(9.9)	(12.3)	(14.9)	(17.5)	(20.2)	(23.1)
Proceeds from issuance of redeemable convertible preferred stock	8.5	-	-	-	-	-	-	-	-	-	-	-
Issuance/Purchase of Stock	-	69.5	-	46.5	46.5	46.5	-	-	-	-	-	-
Issuance/Payment Debt	-	13.6	-	(1.1)	(4.5)	(4.5)	(3.4)	-	-	-	-	-
Proceeds from exercise of stock options	0.0	0.0										
Repayment of notes payable	(1.8)	(5.3)	-	-	-	-	-	-	-	-	-	-
Financing Cash Flow	6.7	77.8	-	45.4	42.0	42.0	(3.4)	-	-	-	-	-
Effect of Exchange Rates	-	-	-	-	-	-	-	-	-	-	-	-
Beginning Cash	23.9	17.5	71.1	49.6	65.1	87.6	138.4	196.6	266.1	357.9	477.6	625.9
Net Increase (Decrease) in Cash	(5.4)	53.6	(21.5)	15.5	22.5	50.8	58.2	69.5	91.9	119.7	148.3	177.8
Ending Cash	17.5	71.1	49.6	65.1	87.6	138.4	196.6	266.1	357.9	477.6	625.9	803.7

Sources: Ocular Therapeutix Filings, Oppenheimer Research.

Investment Thesis

Ocular is an appealing platform play in the ophthalmology space, in our view, driven by several technological advances that permit steady delivery of drugs to the eye using punctal plugs. The company's pipeline is substantially de-risked as Ocular's plugs deliver medications already approved for glaucoma (travoprost) and post-surgical inflammation (dexamethasone). Both the inflammation (OTX-DP) and glaucoma (OTX-TP) plugs have achieved clinical proof-of-concept, and we expect FDA approvals in 2016/2018, respectively. Longer term, we see the interplay between compliance advantages of plugs vs. generic/soon-to-be generic eye-drop markets as a key debate for the stock. However, at current levels even a conservative view of peak share suggests significant upside.

Price Target Calculation

We value Ocular Therapeutix using a discounted cash flow (DCF) analysis with a weighted average cost of capital (WACC) of 10% and a 0% terminal growth rate post-2030, generating a terminal value of \$372M. Our DCF valuation indicates an equity value of ~\$992M, or \$42 per diluted share.

Key Risks to Price Target

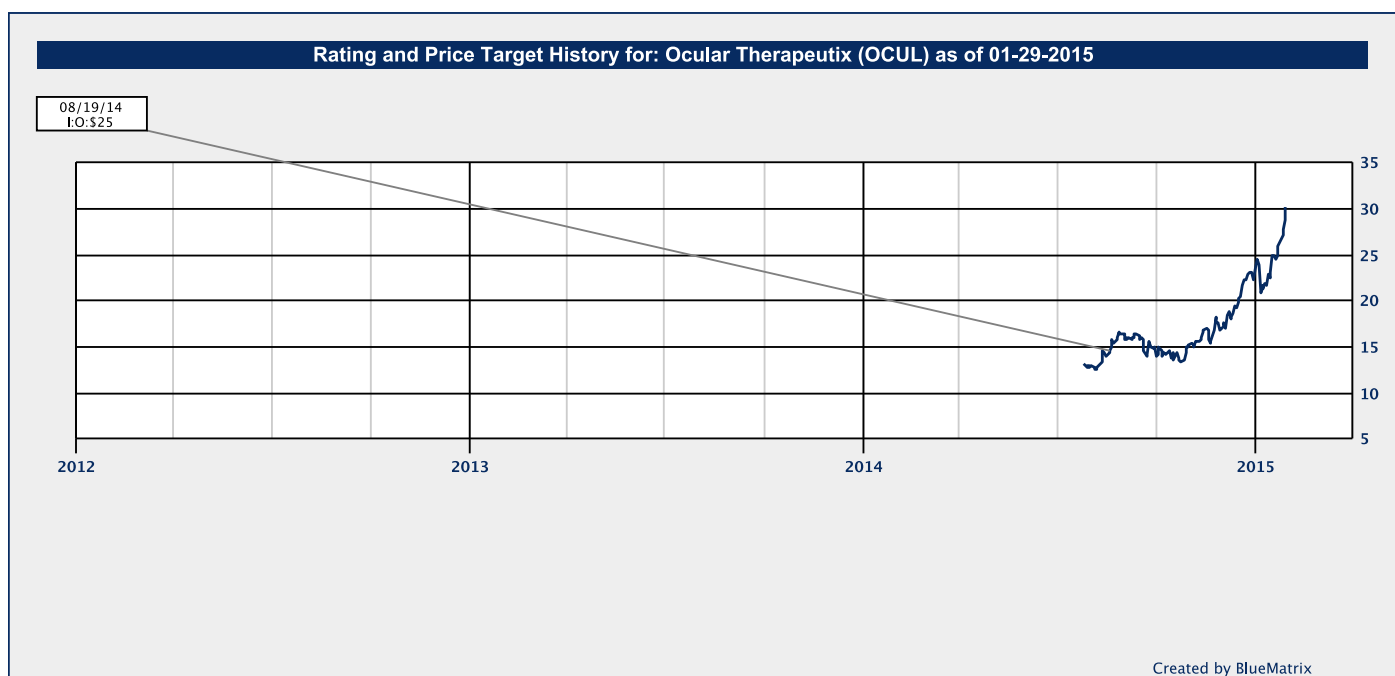
Key risks include the following: **1)** Future retention rates and/or the degree of IOP reductions in Phase 2b and/or Phase 3 for OTX-TP in glaucoma may prove insufficient for widespread treatment adoption. **2)** The Phase 3 post-surgical inflammation and pain trial may fail to meet clinical endpoints. **3)** Ocular may not be successful in commercializing OTX-TP and OTX-DP and/or share capture may be weaker than our current projections. **4)** Ocular will likely need additional dilutive capital to develop its products, and we assume additional financings of \$150M over 2016-18.

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All price targets displayed in the chart above are for a 12- to- 18-month period. Prior to March 30, 2004, Oppenheimer & Co. Inc. used 6-, 12-, 12- to 18-, and 12- to 24-month price targets and ranges. For more information about target price histories, please write to Oppenheimer & Co. Inc., 85 Broad Street, New York, NY 10004, Attention: Equity Research Department, Business Manager.

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	Count	Percent	Count	Percent
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