

US Equity Research

26 January 2015

BUY

unchanged

PRICE TARGET US\$18.00↑

from US\$12.00

Price (23-Jan) US\$8.54

Ticker EGLT-NASDAQ

52-Week Range (US\$): 3.81 - 19.85
 Avg Daily Vol (M) : 53.5
 Shares Out. (M) : 17.3
 Market Cap (US\$M): 148

FYE Dec	2013A	2014E	2015E
Sales (US\$M)	0.0	1.1	21.2
EPS Adj&Dil (US\$)	(1.45)	(3.18)	(0.81)

Quarterly Sales	Q1	Q2	Q3	Q4
2013A	0.0	0.0	0.0	0.0
2014E	0.3A	0.5A	0.3A	0.0
2015E	0.0	6.8	7.0	7.4

Quarterly EPS Adj&Dil	Q1	Q2	Q3	Q4
2013A	(2.12)	(2.28)	(4.34)	(0.67)
2014E	(1.34)A	(0.73)A	(0.63)A	(0.69)
2015E	(0.50)	(0.16)	(0.07)	(0.08)



Egalet is a specialty pharma company focused on developing abuse-deterrent formulated drugs, including opioids.

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Raising Target Price

Major catalyst mid-2015 with EGLT-002; higher confidence based on positive EGLT-001 Category 3 data

Head-to-head study vs. Purdue major catalyst, expect data by mid-2015

We expect positive results for EGLT-002 (abuse-deterrent oxycodone) by mid-2015 from a Category 3 likeability study head-to-head versus Purdue's Oxycontin OP, which should move shares substantially higher. Validation of Egalet's Guardian Technology from the Category 3 study with EGLT-001 gives us higher confidence for positive results from EGLT-002. Both drugs use a polymer API-based matrix and utilize the same injection molding manufacturing process. Importantly, EGLT-002 uses a two-part abuse deterrent technology, which may be even more robust vs. EGLT-001's one-part technology. Finally, the recent withdrawal of Remoxy by Pfizer significantly reduces competitive risk for EGLT-002, which we believe puts the company in a strong competitive position.

EGLT-001 demonstrates significantly lower abuse potential vs. MS Contin, positive for EGLT-002

Top-line results from the Category 3 abuse-deterrent human abuse liability (HAL) study for EGLT-001 showed significantly lower potential for abuse vs. manipulated MS Contin, a positive in giving further validation of the company's Guardian Technology. EGLT-001 continued to retain its abuse-deterrent characteristic after severe manipulation, where there was no statistical difference between the drug liking scores (as measured by Emax) between the intact and manipulated formulation. We remind investors that FDA recently required the company to modify its Category 3 study design, based on the very high level of abuse deterrence seen with EGLT-001.

Phase 3 data for EGLT-001, EGLT-002 due 1H16

EGLT plans to initiate a Phase 3 study for EGLT-001 in 1Q15, and for EGLT-002 in 1H15, with Phase 3 data expected for both studies during early 2016. We expect both studies to be positive, given similar AUC for EGLT-001 and EGLT-002 versus MS Contin and Oxycontin OP. We remind investors that AUC is the critical factor in pain relief for long-acting opioids.

Increase price target to \$18, BUY rating

We increase our price target to \$18 and maintain our BUY rating as we have higher confidence in seeing a positive result from the Category 3 EGLT-002 study and phase 3 EGLT-001 clinical study. In our NPV valuation, we increase our probability adjustment of EGLT-001 and EGLT-002 to 65% and 50%, respectively, from 50% and 35%.

Figure 1: EGLT Catalysts

Event	Timing	Drug	Description	Effect	Importance	Notes
FDA meeting	1Q15	Egalet-001	Update from FDA meeting to discuss full Egalet-001 bioequivalence data	↑	High	EGLT will discuss 15, 60, and 100 mg bioequivalence data, possible 100 mg path forward
Data	mid-2015	Egalet-001	Tier 1 Abuse Deterrence results	↑	Moderate	Expect positive data supporting Tier 1 abuse deterrence given physiochemical performance of Egalet-001, more extensive physical manipulation
Data	1H15	Egalet-002	Tier 1 physical manipulation studies	↑	High	EGLT will discuss physical manipulation data for EGLT-002
Data	mid-2015	Egalet-002	Likeability data - oral	↑	Critical	Expect positive data given physiochemical superiority of Egalet-002 vs OxyContin
Data	YE15	Egalet-002	Likeability data - intranasal	↑	Critical	Expect positive data given physiochemical superiority of Egalet-002 vs OxyContin
Data	YE15 / early 2016	Egalet-001	Phase 3 Study Results	↑	High	Anticipate positive data supporting safety and efficacy
Data	YE15 / early 2016	Egalet-002	Phase 3 Study Results	↑	Critical	Anticipate positive data supporting safety and efficacy
FDA Decision	YE16	Egalet-002	PDUFA	↑	High	Expect approval given unmet need for abuse-deterrent formulation of oxycodone

Source: Canaccord Genuity estimates

Figure 2: EGLT income statement

Income Statement (\$000's)	2013A	Mar-14A	Jun-14A	Sep-14A	Dec-14E	2014E	2015E	2016E	2017E	2018E	2019E	2020E	2021E	2022E
Total revenues	0	256	490	346	-	1,092	21,211	42,425	149,883	272,076	486,427	594,945	780,796	866,115
Cost of goods sold								6,364	20,984	35,370	63,236	71,393	93,695	103,934
Gross profit	0	256	490	346	-	1,092	19,053	36,061	128,899	236,706	423,192	523,551	687,100	762,181
Operating expenses														
Research & development														
Egalet-001	1,187	1,800	2,100	1,696	2,000	7,596	9,282	9,746	9,259	7,407	7,407	7,407	7,407	7,407
Egalet-002	371	48	3,400	3,400	3,600	10,448	12,000	1,800	900	900	900	900	900	900
Other Clinical and Preclinical Milestones	1,288	567	1,489	1,250	1,250	4,556	5,000	5,500	7,494	34,010	60,803	74,368	97,599	108,264
Personnel Related	1,431	365	372		7	1,503	1,578	1,735	2,083	2,499	2,999	3,599	4,318	5,182
R&D	6,280	2,780	7,361	6,346	6,857	24,103	27,860	18,782	19,735	44,816	72,109	86,274	110,225	121,753
						23,344			16,487	32,649	72,964	95,191	124,927	138,578
Egalet-001							5,625	16,500	17,160	17,846	18,560	19,303	20,075	20,878
Egalet-002									37,500	43,125	49,594	57,033	65,588	75,426
Sales							16,500	17,325	18,191	20,465	28,651	32,233	36,262	40,794
General & administrative	4,873	3,269	4,728	4,194	4,507	8,000	8,900	9,790	11,748	14,685	18,356	22,945	27,534	30,288
SG&A	4,873	3,269	4,728	4,194	4,507	8,000	31,025	43,615	84,599	96,122	115,161	131,513	149,459	167,386
						16,698			29,977	95,227	170,250	208,231	124,927	129,917
Total expenses	11,153	6,049	12,089	10,540	11,364	32,103	58,885	62,397	104,335	140,937	187,271	217,787	259,683	289,139
Depreciation & amortization		242	336	430	524	1,532		5,309	6,874	7,674	7,420	8,571	9,000	9,450
EBITDA	(11,153)	(5,551)	(11,263)	(9,764)	(10,840)	(37,418)	(15,207)	(21,026)	31,439	103,443	243,341	314,336	436,417	482,492
Operating income	(11,153)	(5,793)	(11,599)	(10,194)	(11,364)	(38,950)	(15,207)	(26,335)	24,565	95,769	235,921	305,764	427,417	473,042
Interest income			4	5										
Interest expense	8,842	(7,092)	-	-	-	(7,092)	(735)	(588)	(294)	(74)	-	-	-	-
Other expense / (income), net	190			46	50	96	200	200	200	200	200	200	200	200
Interest & other	9,032	(7,092)	4	51	50	(6,996)	(535)	(388)	(94)	127	200	200	200	200
Gain on foreign currency exchange		4	(40)											
Pre-tax income		(12,881)	(11,635)	(10,143)	(11,314)	(45,973)	(15,742)	(26,723)	24,471	95,896	236,121	305,964	427,617	473,242
Taxes	22	35	16	35			-	-	9,124	35,388	87,217	113,059	158,070	174,951
Tax rate							37%	37%	37%	37%	37%	37%	37%	37%
Net income - GAAP	(20,207)	(12,916)	(11,651)	(10,178)	(11,314)	(46,059)	(15,742)	(26,723)	15,347	60,508	148,904	192,905	269,547	298,290
GAAP EPS	(\$1.45)	(\$1.34)	(\$0.73)	(\$0.63)	(\$0.69)	(\$3.18)	(\$0.81)	(\$1.22)	\$0.63	\$2.25	\$5.33	\$6.63	\$8.91	\$9.48
Adjusted EPS excl. options expe	(\$1.45)	(\$1.34)	(\$0.73)	(\$0.63)	(\$0.69)	(\$3.18)	(\$0.81)	(\$1.22)	\$0.63	\$2.25	\$5.33	\$6.63	\$8.91	\$9.48
Diluted shares outstanding	13,902	9,638	15,888	16,207	16,288	14,505	19,515	21,972	24,411	26,888	27,963	29,082	30,245	31,455

Source: Canaccord Genuity estimates

Figure 3: EGLT Valuation

Product	Peak Sales (\$MM)	Peak Year	Current Value (\$MM)	Probability Adjustment	Value / Share	Scenario probability	Adjusted Value
Non-Partnered							
Egalet-001 (morphine)	112	2025	34	65%	\$2	20%	\$0
Egalet-002 (oxy codone)	886	2027	341	50%	\$25	20%	\$5
Equity Value					\$27	20%	\$5
Partnered							
Egalet-001 (morphine)	112	2025	34	65%	\$2	55%	\$1
Egalet-002 (oxy codone)	1112	2027	198	50%	\$14	55%	\$8
Equity Value					\$17	55%	\$9
Royalty							
Egalet-001 (morphine)	112	2025	34	65%	\$2	25%	\$1
Egalet-002 (oxy codone)	200	2027	147	50%	\$11	25%	\$3
Equity Value					\$13	25%	\$3
Total Equity Value							\$18
Net Cash (50% adj)							\$0
Value per share							\$18
Shares Outstanding (MM)							13.9
Risk-Free Rate	2.00%						
Beta	1.3						
Risk Premium	8%						
Discount Rate	12%						

Source: Canaccord Genuity estimates

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Target Price / Valuation Methodology:

Egalet Corp. - EGLT

Our \$18 price target is based on a probability-adjusted NPV valuation.

Risks to achieving Target Price / Valuation:

Egalet Corp. - EGLT

Risks to our rating and price target include the following: Approval for Egalet-001 and Egalet-002 may be delayed or may never occur at all: If the FDA does not allow Egalet to pursue approval for Egalet-001 through the Section 505(b)(2) pathway via bioequivalence to MS-Contin, the company may be forced to conduct Phase III studies resulting in increased costs, delayed revenue generation, and more competition. Total revenues, even with timely approvals, may be lower than our estimates: Egalet-001 and Egalet-002 face competition from currently marketed non-abuse-deterrent products, while the planned reintroduction of Embeda, another abuse-deterrent long-acting morphine drug (Pfizer) may have a negative impact on the market opportunity for Egalet-001. Also, legislation to remove non-abuse-deterrent opioid drugs from the market may never materialize, resulting in investor concern. Future litigation may delay or reduce total revenues. Several competitors currently in the space may undertake legal strategies to delay the launch of Egalet-001 and Egalet-002. These competitors have significantly greater resources at their disposal than Egalet and have more experience maneuvering the legal field. From a financial standpoint, although Egalet currently has adequate cash on hand ~\$65, the company may require additional capital before the anticipated launch of Egalet-001 in the second half of 2015. An additional capital raise could pressure shares.

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	#	%	%
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Hold	349	32.31%	13.75%
Sell	51	4.72%	1.96%
Speculative Buy	48	4.44%	60.42%
	1080*	100.0%	

*Total includes stocks that are Under Review

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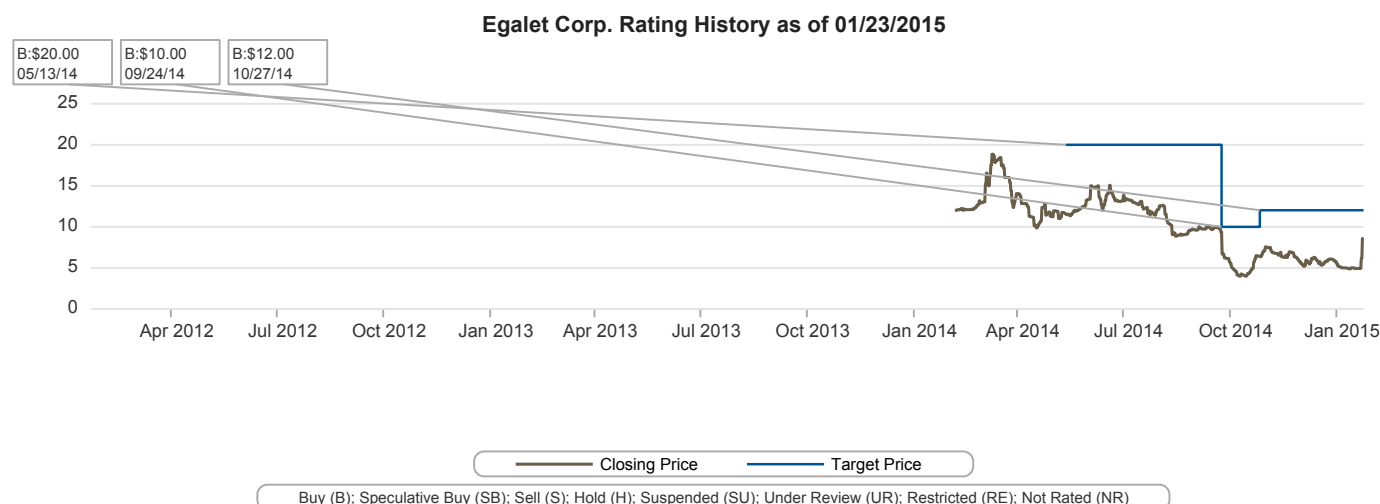
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