

Reason for report:

PROPRIETARY INSIGHTS

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DERMIRA, INC.

Preclinical DRM01 Data Along w/ Ph IIa Compelling; Increasing PT to \$39

• **Bottom Line:** We are raising PT for DERM on our increasing conviction in the DRM01 Ph2b acne trial. The company presented data at the European Society for Dermatological Research (ESDR) on DRM01 (topical sebum inhibitor). The study showed DRM01 penetrated model animal skin in a dose- and formulation-dependent manner, accumulating in the sebaceous glands. Our conversation with mgmt. and a MEDACorp KOL further confirmed our confidence in the ongoing Ph2b trial. We raise the assigned probability of success (POS) for DRM01 from 50% to 70%, and raise our DCF-based PT from \$34 to \$39.

• **Preclinical pig model bolsters conviction that DRM01's RoA is effective.** The Yorkshire pig is a well-established model in dermatology due to its close resemblance to human skin morphology and physiology. This study cannot realistically be done on human subjects because the quantitative MALDI imaging requires serial skin samples. DERM mgmt and the KOL emphasized this data demonstrated that DRM01 is capable of reaching the sebaceous gland, a critical aspect for its topical route of administration (RoA). Mgmt indicated that 1H16 timing of the DRM01 Ph2b topline result readout is still on track, and the pig skin data will be part of the pre-clinical data package when submitting for FDA review.

• **Rational dose selection consistent with Ph2b study design.** We note that the pig skin study tested 4% and 7.5% topical gel at once or twice daily dosing. This is in line with the dose finding Ph2b trial design with three treatment arms (4% Q1D, 7.5% Q1D and Q2D). The skin penetration demonstrated in the study validate that the lower 4% QD dose is sufficient to reach the sebaceous gland. In our view, this bodes well for the market opportunity for DRM01 as less frequent dosing would increase the appeal of the drug and broaden the patient base.

• **DRM01 is the biggest value driver for DERM in our view.** While each of DERM's three programs (DRM01, DRM04 for hyperhidrosis, and Cimzia for psoriasis) contribute relatively equally in our DCF valuation at present, the DRM01 program is the most critical long term valuation driver. We forecast ~\$550M peak DRM01 sales at 100% POS and it contributes ~\$30/shr to our DCF. Additionally, we assign a 75% POS to DRM04 (hyperhidrosis) pending final Ph3 results in 2H16; the 90% POS for Cimzia reflects the low-risk of failure. DRM04 and Cimzia contribute \$11/shr and \$10/shr, respectively, to our valuation.

Key Stats:

(NASDAQ :DERM)

Sector: Biotechnology
S&P 600 Health Care Index: 1,719.60
Price : \$27.46
Price Target: \$39.00 from \$34.00
Methodology: DCF with 12% discount rate & 2% terminal growth rate

52 Week High: \$27.76
52 Week Low: \$12.68
Shares Outstanding (mil): 24.7
Market Capitalization (mil): \$678.3
Book Value/Share: \$6.77
Cash Per Share: \$7.08
Net Debt to Total Capital: 0%
Dividend (ann): \$0.00
Dividend Yield: 0.0%
Est LT EPS Growth: NM

Book Value/Share: Pro Forma including proceeds from recent stock offering.

Cash Per Share: Pro Forma including proceeds from recent stock offering.



Dec Yr	1Q	2Q	3Q	4Q	FY Rev	1Q	2Q	3Q	4Q	FY EPS	P/E
2014A	0.0	0.0	0.0	\$7.3	\$7.3	(\$9.56)	(\$9.72)	(\$8.66)	(\$0.29)	(\$4.96)	NM
2015E	0.0A	0.0	0.0	0.0	0.0	(\$0.57)A	(\$0.69)A	(\$0.79)	(\$1.04)	(\$3.09)	NM
2016E	--	--	--	--	\$10.0	--	--	--	--	(\$2.78)	NM

Source: Company Information and Leerink Partners LLC Research
Revenues in \$MM.

GAAP EPS. Quarterly EPS may not sum to annual total due to change in shares outstanding.

INVESTMENT THESIS

We rate DERM Outperform. DERM represents an unique investment opportunity, with a highly experienced and proven management team developing three late-stage dermatology assets, each with robust, positive Phase II data and multi-hundred million dollar commercial potential. Cimzia is an extremely high probability psoriasis biologic partnered with UCB and likely to provide profits and milestones sufficient to fund Dermira's standalone operations. DRM04 represents the first topical pharmaceutical wipe for hyperhidrosis with a high probability of success given a well-characterized mechanism, positive Phase II data, in an area of high unmet need. DRM01 is a first-in-class topical sebum inhibitor with an on-target mechanism that MEDACorp acne KOLs have called the "holy grail" of topical acne treatment.

VALUATION

We value DERM at \$39/share. Our price target is based on a DCF valuation that assumes a 12% discount rate on probability-adjusted sales and profits through 2026E and applies a 2% terminal growth rate. Our valuation assumes late-stage assets Cimzia, DRM04, and DRM01 have 90%, 75%, and 70% probabilities of success, respectively, and each contributes \$10-18 per share. This price target equates to 22x 2021E EPS of \$3.53 discounted back 6 years at 12%. Fully valued, with 100% probability for all three programs, we arrive at a DCF-based price target of \$52/share with Cimzia and DRM04 contributing \$10/share and \$11/share, respectively, and DRM01 contributing \$30/share.

RISKS TO VALUATION

An investment in DERM involves a pooling of different risks including technical, regulatory, and commercial risk for three fundamentally different pipeline products. Most significant to DERM's overall valuation, in our opinion, is clinical success of DRM01 in acne. Important for Cimzia and DRM04 is commercial execution associated with launches into the highly competitive psoriasis and the underdeveloped hyperhidrosis markets, respectively. There are also competitive risks from other pipeline therapies. Finally, DERM may face financing risk beyond mid-2017.

Dermira - Income Statement Analysis 2014-2022E

(\$ in Millions, Except EPS)													
(Year Ended December 31)	2014	1Q15	2Q15	3Q15E	4Q15E	2015E	2016E	2017E	2018E	2019E	2020E	2021E	2022E
Total Revenue Incl 1x Milestones	7	-	-	-	-	-	10	19	34	150	270	397	499
Total Revenue	-	-	-	-	-	-	-	-	34	128	260	387	499
Growth (% y/y)											104%	49%	29%
COGS	-	-	-	-	-	-	-	-	2	11	27	44	61
COGS (% of sales)							nm	nm	7%	9%	10%	11%	12%
Gross Profit	7	-	-	-	-	-	10	19	32	139	243	353	438
Gross Profit (% of sales)	nm					nm	nm	nm	nm	nm	93%	91%	88%
SG&A	8	4	4	5	7	20	22	34	74	93	93	155	175
SG&A (% of sales)	nm					nm	nm	nm	219%	72%	36%	40%	35%
R&D	31	10	13	18	23	65	69	54	40	35	50	77	100
R&D (% of sales)	nm					nm	nm	nm	118%	27%	19%	20%	20%
Operating Income	(32)	(14)	(17)	(23)	(30)	(85)	(81)	(68)	(83)	11	100	121	164
Operating Margin (% of sales)									(2)	0	0	0	0
Total Interest and Other Income/ (Expense)	(0)	0	0	-	-	-	-	-	-	-	-	-	-
Pre-tax Income	(31.844)	(14.0)	(17.2)	(23)	(30)	(85)	(81)	(68)	(83)	11	100	121	164
Change in Unrealized Gain / loss													
Taxes	0									-	-	-	0
Rate (% of pre-tax income)										-	-	-	0
Net Income	(31.9)	(14.0)	(17.16)	(23.0)	(30.4)	(85.0)	(81.4)	(68.5)	(82.7)	11.4	100.4	121.1	163.7
EPS (pro forma)	(\$4.96)	(\$0.57)	(\$0.69)	(\$0.79)	(\$1.04)	(\$3.09)	(\$2.78)	(\$1.99)	(\$2.41)	\$0.33	\$2.92	\$3.53	\$4.77
Average Shares Outstanding	6.4	24.7	24.7	29.2	29.3	27.0	29.3	34.3	34.3	34.3	34.3	34.3	34.3

Source: Leerink Partners and Company Reports

Dermira - Income Statement Analysis 2014-2026E

(\$ in Millions, Except EPS)														CAGR
(Year Ended December 31)	2014	2015E	2016E	2017E	2018E	2019E	2020E	2021E	2022E	2023E	2024E	2025E	2026E	'18-22
Product Revenue (POS adj.)	-	-	-	-	9	76	181	285	387	449	518	557	611	
DRM04	-	-	-	-	9	23	61	102	148	180	200	209	231	100%
DRM01	-	-	-	-	-	53	120	183	240	269	318	348	381	NM
Other DRM Pipeline	-	-	-	-	-	-	-	-	-	-	-	-	-	NM
Royalty Revenue (POS adj.)	-	-	-	-	25	52	79	102	112	117	120	112	109	
Cimzia End User Sales	-	-	-	-	42	85	133	185	206	217	225	207	200	
Cimzia Royalty (from UCB)	-	-	-	-	25	52	79	102	112	117	120	112	109	
Other Revenue (POS adj.)	7	-	10	19	-	22	10	10	-	-	-	-	-	
Cimzia Development Milestones	7	-	10	19	-	-	-	-	-	-	-	-	-	
Cimzia Regulatory Milestones	-	-	-	-	-	12	-	-	-	-	-	-	-	
Cimzia Commercialization Milestones	-	-	-	-	-	10	10	10	-	-	-	-	-	
Total Revenue Incl 1x Milestones	7	-	10	19	34	150	270	397	499	565	638	669	721	
Total Revenue	-	-	-	-	34	128	260	387	499	565	638	669	721	96%
Growth (% y/y)							104%	49%	29%	13%	13%	5%	8%	
COGS	-	-	-	-	2	11	27	44	61	72	82	87	96	126%
<i>COGS (% of sales)</i>			nm	nm	7%	9%	10%	11%	12%	13%	13%	13%	13%	
Gross Profit	7	-	10	19	32	139	243	353	438	493	556	582	625	93%
<i>Gross Profit (% of sales)</i>	nm	nm	nm	nm	nm	nm	93%	91%	88%	87%	87%	87%	87%	
SG&A	8	20	22	34	74	93	93	155	175	187	198	201	202	24%
<i>SG&A (% of sales)</i>	nm	nm	nm	nm	219%	72%	36%	40%	35%	0	0	0	0	
R&D	31	65	69	54	40	35	50	77	100	113	128	134	144	26%
<i>R&D (% of sales)</i>	nm	nm	nm	nm	118%	27%	19%	20%	20%	20%	20%	20%	20%	
Operating Income	(32)	(85)	(81)	(68)	(83)	11	100	121	164	194	231	248	279	NM
Operating Margin (% of sales)					(2)	0	0	0	0	0	0	0	0	
Total Interest and Other Income/ (Expense)	(0)	-	-	-	-	-	-	-	-	-	-	-	-	
Pre-tax Income	(31.844)	(85)	(81)	(68)	(83)	11	100	121	164	194	231	248	279	
Change in Unrealized Gain / loss														
Taxes	0					-	-	-	0	11	24	29	40	NM
<i>Rate (% of pre-tax income)</i>						-	-	-	0	0	0	0	0	
Net Income	(31.9)	(85.0)	(81.4)	(68.5)	(82.7)	11.4	100.4	121.1	163.7	183	207	218	239	
EPS (pro forma)	(\$4.96)	(\$3.09)	(\$2.78)	(\$1.99)	(\$2.41)	\$0.33	\$2.92	\$3.53	\$4.77	\$5.33	\$6.04	\$6.35	\$6.95	
Average Shares Outstanding	6.4	27.0	29.3	34.3	34.3	34.3	34.3	34.3	34.3	34.3	34.3	34.3	34.3	

Source: Leerink Partners and Company Reports

Disclosures Appendix

Analyst Certification

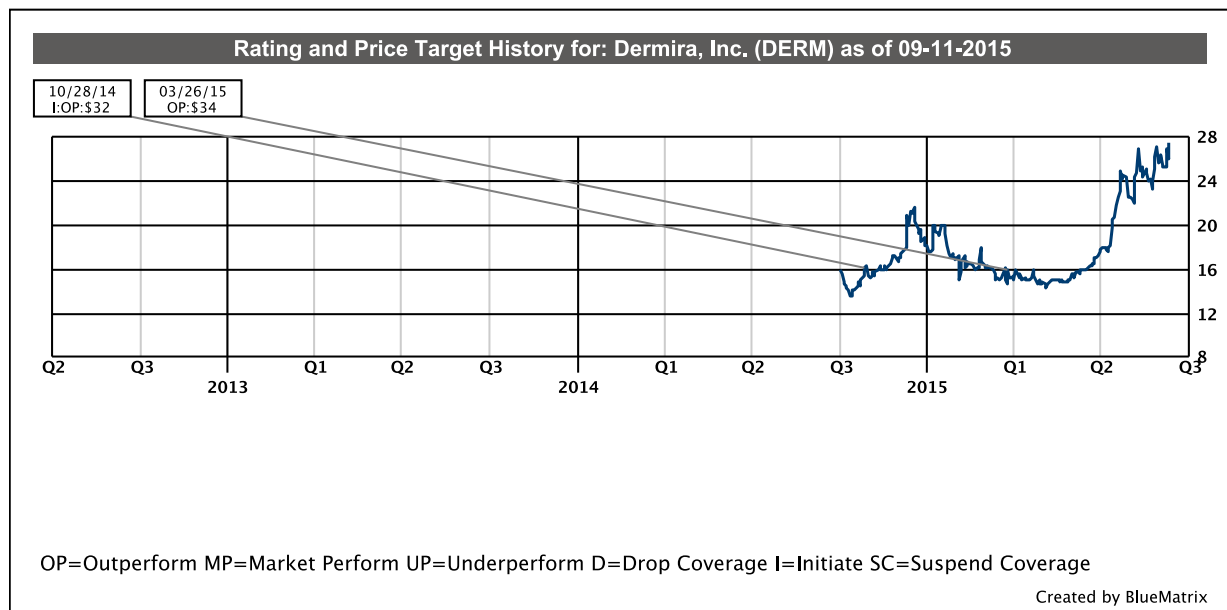
I, Seamus Fernandez, certify that the views expressed in this report accurately reflect my views and that no part of my compensation was, is, or will be directly related to the specific recommendation or views contained in this report.

Valuation

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Distribution of Ratings/Investment Banking Services (IB) as of 06/30/15				
Rating	Count	Percent	IB Serv./Past 12 Mos.	
			Count	Percent
BUY [OP]	165	73.66	66	40.00
HOLD [MP]	59	26.34	1	1.69
SELL [UP]	0	0.00	0	0.00

Explanation of Ratings

Outperform (Buy): We expect this stock to outperform its benchmark over the next 12 months.

Market Perform (Hold/Neutral): We expect this stock to perform in line with its benchmark over the next 12 months.

Underperform (Sell): We expect this stock to underperform its benchmark over the next 12 months. The degree of outperformance or underperformance required to warrant an Outperform or an Underperform rating should be commensurate with the risk profile of the company.

For the purposes of these definitions the relevant benchmark will be the S&P 600® Health Care Index for issuers with a market capitalization of less than \$2 billion and the S&P 500® Health Care Index for issuers with a market capitalization over \$2 billion.

Important Disclosures

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MEDACorp is a network of healthcare professionals, attorneys, physicians, key opinion leaders and other specialists accessed by Leerink and it provides information used by its analysts in preparing research.

In the past 12 months, the Firm has received compensation for providing investment banking services to Dermira, Inc. .

Leerink Partners LLC makes a market in Dermira, Inc.

Leerink Partners LLC has acted as the manager for a public offering of Dermira, Inc. in the past 12 months.

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