

## Biocept, Inc.

*Company Description: Biocept is an early-stage cancer diagnostics company with proprietary platforms for circulating tumor cells (CTCs) and circulating tumor DNA (ctDNA) with one test currently marketed and five tests intended to launch in the next 18 months. The company also offers clinical research services to support biopharmaceutical drug development and clinical trial support at their CLIA certified and CAP accredited lab. Biocept is based in San Diego, California.*

Healthcare- Molecular Diagnostics May 20, 2014

### Biocept reports Q1 results, announces sales team, reiterate STRONG BUY (BIOC - \$4.51) STRONG BUY

#### Key Points

- Biocept reported first quarter results last week, with negligible revenue (as expected) and loss per share of \$(1.96) compared to our \$(0.91) estimate.
- Operating expenses were largely in-line with our expectations with the exception of ~\$1.5 million of stock-based comp and IPO-related personnel expenses, approximately \$0.9 million of which is non-recurring in nature.
- Interest expense was higher than our estimate due to \$1.3 million in amortization and write-offs of discounts to notes payable. Total other expenses were \$1.6 million above our estimates.
- ASPs for commercial tests increased to \$758 in the quarter from \$610 in the year ago quarter. Clinical trial test ASPs remained flat year-over-year at \$400. While we have not modeled increasing ASPs during 2014, we anticipate they will increase as Biocept broadens their test menu.
- The company announced on April 30 it had received a \$5.0 million loan, and had \$10.4 million of cash on hand at the end of the quarter.
- Yesterday, Biocept announced the recruitment of a national sales team to market OncoCEE. We believe the sales force now represents about a half dozen salespeople. Biocept noted each hire possesses more than 15 years of oncology sales experience with firms such as Genentech, Eli Lilly, GE Healthcare, Clariant, Life Technologies, and Labcorp. We believe these experienced hires serve to validate Biocept's technology as experienced sales representatives are highly sought after. Further, we think this signals Biocept will soon begin marketing their OncoCEE-BR test with ER (estrogen receptor) and PR (progesterone receptor) status added to their existing HER2 test.
- We believe the company remains on track to achieve the milestones as laid out in their corporate presentation. As a result, our model does not change appreciably due to the release of Q1 numbers.
- Reiterating STRONG BUY rating and \$14.00 (3.5x 2016 EV/sales, discounted back 25%) price target.

#### Financial Summary

Rev(mil)	2013A	2014E	2015E
Mar	\$0.0A	\$0.0A	\$1.5E
June	\$0.0A	\$0.1E	\$2.3E
Sept	\$0.0A	\$0.4E	\$3.6E
Dec	\$0.0A	\$0.8E	\$5.1E
FY	\$0.1A	\$1.2E	\$12.5E
P/Sales	201x	16.7x	1.6x

EPS	2013A	2014E	2015E
Mar	(\$10.67)A	(\$1.96)A	(\$0.55)E
June	(\$10.83)A	(\$0.67)E	(\$0.52)E
Sept	(\$15.72)A	(\$0.74)E	(\$0.44)E
Dec	(\$13.57)A	(\$0.78)E	(\$0.29)E
FY	(\$50.80)A	(\$3.05)E	(\$1.79)E
P/E	NM	NM	NM

Price:	\$4.51
52-Week Range:	\$10.02-\$4.16
Target:	\$14.00
Rating:	STRONG BUY
Shares Outstanding:	4.4 mil
Mkt. Capitalization:	\$20 mil
Ave. Volume:	21,000
Instit. Ownership:	N/A
BV / Share:	\$2.54
Debt / Tot. Cap.:	17%
Est. LT EPS Growth:	40%

## INVESTMENT THESIS

Biocept has developed an intriguing platform for the capture of circulating tumor cells (CTCs) and circulating tumor DNA (ctDNA) from whole blood, in essence a "liquid biopsy". Their solution enables analysis of CTCs and ctDNA through traditional methods of cancer diagnostic analysis such as fluorescence in situ hybridization (FISH) as well as newer methods, such as next-generation sequencing (NGS). The "liquid biopsy" aspect presents a huge opportunity to improve care, in our view, as many cancer patients are too unwell to undergo tissue biopsies to monitor their cancers, or the cancer tissues may be inaccessible; in any case, tissue biopsies can be quite expensive. By enabling cancer diagnosis and monitoring through blood draws, we believe Biocept's technology can improve care and reduce costs. That said, the company only has a breast cancer test commercialized to date, and while their pipeline is strong and projected to come to market in the near future, competition exists in the CTC market. We think Biocept's platform has a strong chance of succeeding, given the smart design choices made in the development of their platform. The company, however, has not generated significant revenue to date, and would, as a result, be considered a more speculative investment. Based upon our outlook for the company, we have assigned BIOC share a \$14.00 price target (3.5x 2016 EV/sales, discounted back 25%), and we have assigned the company a STRONG BUY rating.

### Biocept Q1 2014 Variance Analysis

	Estimate	Actual	Variance
<b>Revenue</b>	<b>0.0</b>	<b>0.0</b>	<b>-5.8%</b>
Cost of revenues	0.7	0.7	0.5%
Gross profit	(0.6)	(0.6)	-0.8%
<i>Gross margin</i>	-2083.3%	-2228.3%	
Research and development expenses	0.8	1.0	26.1%
General and administrative expenses	0.9	1.9	105.7%
Sales and marketing expenses	0.3	0.0	-96.6%
Total operating expenses	2.0	2.9	42.2%
<b>Operating income (loss)</b>	<b>(2.7)</b>	<b>(3.5)</b>	<b>-32.5%</b>
<i>Operating margin</i>	-8875.0%	#####	
Interest income (expense)	-	(1.4)	
Change in fair value of warrant liability	-	(0.2)	
Other income (expense)	-	(1.6)	
Income (loss) before income taxes	(2.7)	(5.1)	-92.6%
Income tax expense	-	-	
<i>Tax rate</i>	0.0%	0.0%	
<b>Net income (loss)</b>	<b>(2.7)</b>	<b>(5.1)</b>	<b>-92.6%</b>
<b>EPS</b>			
<b>Basic</b>	<b>\$ (0.91)</b>	<b>\$ (1.96)</b>	<b>-116.3%</b>
<b>Diluted</b>	<b>\$ (0.91)</b>	<b>\$ (1.96)</b>	<b>-116.3%</b>
Weighted average shares outstanding			
Basic	2.9	2.6	-11.0%
Diluted	2.9	2.6	-11.0%

May 20, 2014

Biocept, Inc. (BIOC)

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Income Statement (000s)	2012	Q1	Q2	Q3	Q4	2013	Q1	Q2	Q3	Q4	2014	Q1	Q2E	Q3E	Q4E	2015E	2016E	2017E
<b>Revenue</b>	<b>0.1</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.1</b>	<b>0.0</b>	<b>0.1</b>	<b>0.4</b>	<b>0.8</b>	<b>1.2</b>	<b>1.5</b>	<b>2.3</b>	<b>3.6</b>	<b>5.1</b>	<b>12.5</b>	<b>28.2</b>	<b>46.4</b>
Cost of revenues	1.2	-	-	-	-	2.3	0.7	0.7	1.0	1.3	3.7	1.9	2.3	2.7	3.1	10.0	11.1	15.4
Gross profit	(1.1)	(0.5)	(0.5)	(0.6)	(0.6)	(2.2)	(0.6)	(0.7)	(0.7)	(0.6)	(2.5)	(0.3)	0.1	0.8	2.0	2.6	17.1	30.9
Gross margin	-999.6%	-1456.7%	-1126.5%	-1839.4%	-2933.7%	-1635.6%	-2228.3%	-1083.3%	-182.5%	-78.3%	-210.7%	-23.0%	2.9%	23.3%	39.4%	20.5%	60.7%	66.7%
Research and development expenses	6.6	0.7	0.7	1.0	0.7	3.1	1.0	0.8	0.9	0.9	3.6	1.0	1.0	1.1	1.2	4.3	4.8	4.8
General and administrative expenses	2.1	0.5	0.5	0.8	0.8	2.5	1.9	0.9	1.0	1.0	4.8	1.0	1.0	1.0	1.0	3.9	4.4	5.0
Sales and marketing expenses	0.0	0.1	0.0	0.0	0.0	0.1	0.0	0.6	0.8	1.0	2.3	1.2	1.4	1.6	1.7	5.9	8.9	12.2
Total operating expenses	8.6	1.3	1.2	1.8	1.5	5.7	2.9	2.3	2.6	2.8	10.7	3.1	3.4	3.6	3.9	14.0	18.1	22.0
<b>Operating income (loss)</b>	<b>(10.5)</b>	<b>(1.8)</b>	<b>(1.7)</b>	<b>(2.4)</b>	<b>(2.1)</b>	<b>(7.9)</b>	<b>(3.5)</b>	<b>(3.0)</b>	<b>(3.3)</b>	<b>(3.4)</b>	<b>(13.2)</b>	<b>(3.5)</b>	<b>(3.3)</b>	<b>(2.8)</b>	<b>(1.9)</b>	<b>(11.5)</b>	<b>(1.0)</b>	<b>9.0</b>
Operating margin	-9610.4%	-5034.6%	-3600.5%	-7438.4%	-10949.7%	-5917.9%	-12474.0%	-4937.5%	-905.1%	-458.2%	-1100.3%	-231.2%	-141.0%	-78.7%	-36.4%	-91.4%	-3.4%	19.3%
Other income (expense)	(0.0)	(0.2)	(0.2)	(0.5)	(0.4)	-	(1.6)	-	-	-	(1.6)	-	-	-	-	-	-	-
Income (loss) before income taxes	(12.3)	(1.9)	(2.0)	(2.9)	(2.5)	(9.2)	(5.1)	(3.0)	(3.3)	(3.4)	(14.8)	(3.5)	(3.3)	(2.8)	(1.9)	(11.5)	(1.0)	9.0
Income tax expense	0.0	-	-	-	-	0.0	-	-	-	-	-	-	-	-	-	-	-	3.6
Tax rate	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%	40.0%
<b>Net income (loss)</b>	<b>(12.3)</b>	<b>(1.9)</b>	<b>(2.0)</b>	<b>(2.9)</b>	<b>(2.5)</b>	<b>(9.2)</b>	<b>(5.1)</b>	<b>(3.0)</b>	<b>(3.3)</b>	<b>(3.4)</b>	<b>(14.8)</b>	<b>(3.5)</b>	<b>(3.3)</b>	<b>(2.8)</b>	<b>(1.9)</b>	<b>(11.5)</b>	<b>(1.0)</b>	<b>5.4</b>
<b>EPS</b>																		
Basic	\$ (76.43)	\$ (10.67)	\$ (10.83)	\$ (15.72)	\$ (13.57)	\$ (50.80)	\$ (1.96)	\$ (0.67)	\$ (0.73)	\$ (0.77)	\$ (3.70)	\$ (0.55)	\$ (0.52)	\$ (0.44)	\$ (0.29)	\$ (1.79)	\$ (0.15)	\$ 0.84
Diluted	\$ (76.43)	\$ (10.67)	\$ (10.83)	\$ (15.72)	\$ (13.57)	\$ (50.80)	\$ (1.96)	\$ (0.67)	\$ (0.73)	\$ (0.77)	\$ (3.70)	\$ (0.55)	\$ (0.52)	\$ (0.44)	\$ (0.29)	\$ (1.79)	\$ (0.13)	\$ 0.62
Weighted average shares outstanding																		
Basic	0.2	0.2	0.2	0.2	0.2	0.2	2.6	4.4	4.4	4.4	4.0	6.4	6.4	6.4	6.4	6.4	6.4	6.4
Diluted	0.2	0.2	0.2	0.2	0.2	0.2	2.6	4.4	4.4	4.4	4.0	6.4	6.4	6.4	6.4	6.4	7.5	8.7

## Analyst Certification

I, **Ben Haynor, CFA**, certify that the views expressed in this research report accurately reflect my personal views about the subject company and its securities. I also certify that I have not been, am not, and will not be receiving direct or indirect compensation related to the specific recommendations expressed in this report.

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**Strong Buy:** The stock is expected to have total return potential of at least 20%. Catalysts exist to generate higher valuations, and positions should be initiated at current levels.

**Buy:** The stock is expected to have total return potential of at least 10%. Near term catalysts may not exist and the common stock needs further time to develop. Investors requiring time to build positions may consider current levels attractive.

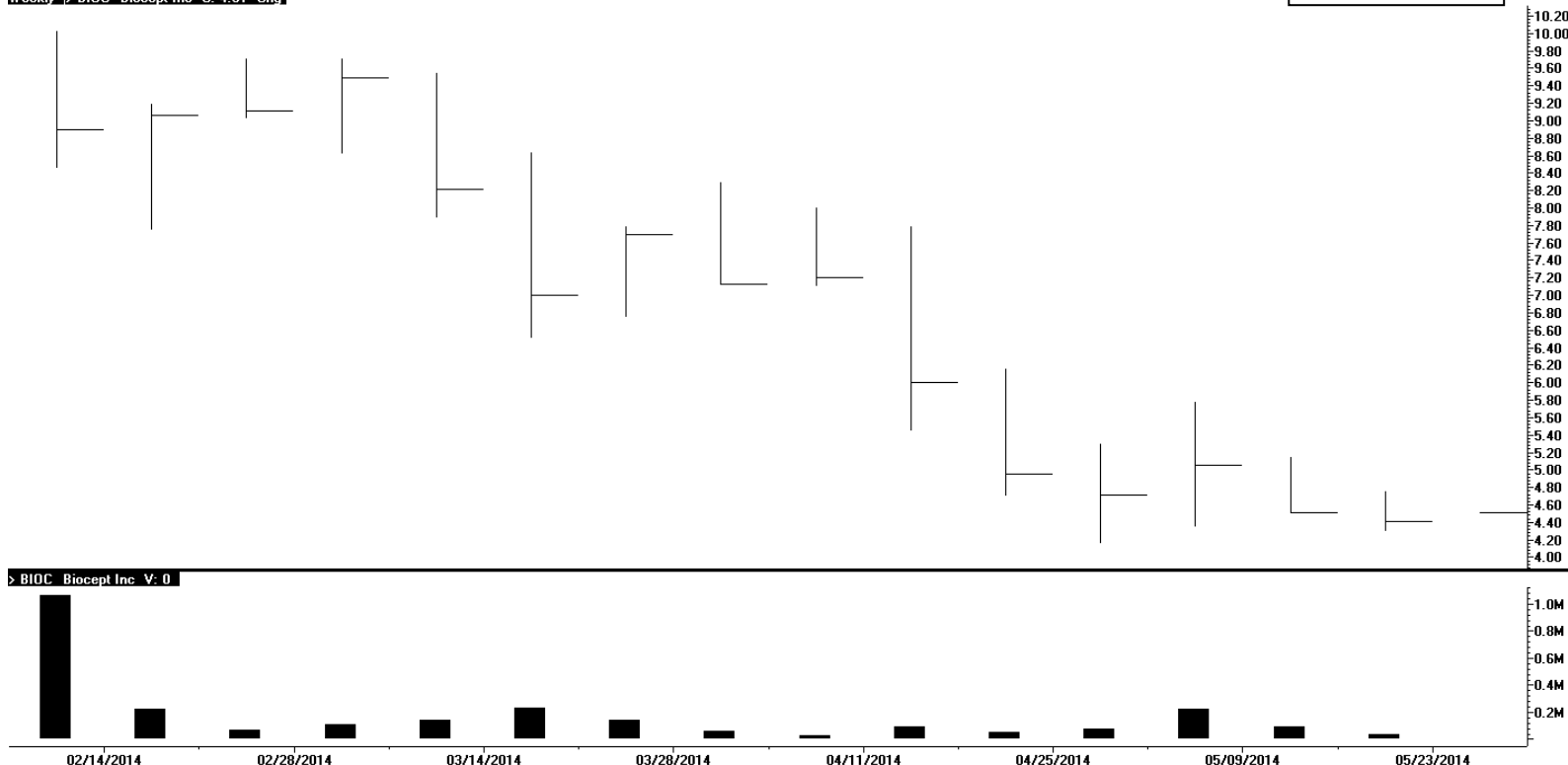
**Hold:** The stock is expected to have total return potential between positive 10% and negative 10%. Fundamental events are not present to make it either a Buy or a Sell. The stock is an acceptable longer-term holding.

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Ratings Distribution for Feltl and Company					5/20/2014
Rating	Number of Stocks	Percent of Total	----- Investment Banking -----		
			Number of Stocks	Percent of Rating category	
SB/Buy	46	67%	9	20%	
Hold	20	29%	0	0%	
Sell	3	4%	0	0%	
	69	100%	9	13%	
The above represents our ratings distribution on the stocks in the Feltl and Company research universe, together with the number in (and percentage of) each category for which Feltl and Company provided investment-banking services in the previous twelve months.					

05/01/14 SB  
Target: \$14.00

Weekly > BIOC Biocept Inc C: 4.51 Chg



Date	Nature of Report	Rating	Price Target
05/01/14	Initiation@4.74	StrongBuy	\$14.00

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#### Valuation and Price Target Methodology:

Our valuation is based upon an EV/sales methodology. We have chosen 3.5x 2016 EV/sales as the multiple on which to value Biocept based upon comparable companies at this point in the company's development. Based on our 2016 estimates, discounted back to 2015 at a rate of 25%, this results in a market value of ~\$14.00 per share based upon 6.4 million shares expected to be outstanding at this point next year.

#### Risks to Achievement of Estimates and Price Target:

Additional funding likely needed. Biocept raised net proceeds of \$16.7 million in their recent IPO. The company will likely need to raise additional capital to execute on its plan and fulfill other obligations. We believe the company is most likely to raise additional equity funding, although we cannot rule out non-dilutive funding in the form of a partnership or license agreement. They may also be able to raise capital via a line of credit or debt financing, although we view this as unlikely. If the company chooses to raise funds via an equity offering, which we would consider the most likely option, the raise has the potential to put pressure on the share price.

Biocept has not achieved significant revenue to date. In both 2012 and 2013, Biocept generated just \$0.1 million in revenue. That said, they have not previously had a field sales force. At present, the company has begun building out its sales force, but time-to-productivity for salespeople in the oncology area is usually at least six months.

Requires a behavior change amongst practitioners. The oncology market has long sent off tissue samples to diagnostic laboratories, and behaviors in the medical community can be highly reluctant to change. As such, adoption can be slower than expected for new technologies in medicine; in fact, studies have shown it takes nearly a decade and a half for half of practitioners to adopt a new way of treatment after a major landmark study. In many cancers, it is still in the early innings of the adoption of genomic characterization, although recent FDA approvals of molecularly targeted oncology therapies is likely to increase adoption of molecular diagnostics overall. Despite this, oncologists would need to change their tissue biopsy habits to move to a liquid biopsy, something that may not occur quickly or easily.

Pipeline does not come to fruition. While Biocept believes they have made solid progress towards validation of their pipeline, unforeseen developments can always occur. Based upon other approaches available and validated for capturing CTCs and our belief Biocept's approach has advantages over competing approaches, we believe the company's pipeline will be validated, but there can be no guarantee.

Competitive CTC capture approaches in development or launched, uncertainty on which will capture mind-share. A number of other approaches are being attempted, but it is unclear which ones will ultimately be the winners. Certainly, we have seen cases where better diagnostic technology failed to gain traction in situations where inferior competitors reached market sooner, or similar technological approaches developed by firms with deeper pockets and larger sales forces won out. Please see the "Competition" section that follows for further discussion of competing approaches.

Please review the company's SEC filing for a comprehensive discussion of potential risks.

#### Other Disclosures:

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