

Equity Research

Concert Pharmaceuticals, Inc.

CNCE: Q1--'354 MAD Data Soon--Promising '499 Fibrosis Data

• **Summary:** On May 14, CNCE reported Q1 2014 earnings. Overall, we are encouraged by the continued progress with '354 and '499, as well as the partnered programs--for which the expedited paths remain on the table. We continue to believe Concert's valuation does not fully reflect the potential of its many proprietary and partnered programs. Adjusting 2014E/2015E EPS to -\$1.88/-\$.074 from -\$1.71/-\$.066.

• **Financials:** Concert reported a net loss of \$7.0MM, or EPS of -\$0.76, and ended Q1 with cash and equivalents of \$108.0MM. A slight uptick in quarterly R&D expense to \$5.6MM from \$5.0MM in Q1 2013 reflected increased spending on clinical development of '354. The company indicated that its current cash should be sufficient to fund operations into 2016.

• **Phase II MAD study for '354 progressing rapidly, with tox study completing.** The phase II MAD study for '354 appears to be progressing well, and initial receptor occupancy data--key for helping to determine whether the drug's therapeutic window could be broader than a standard benzo--is expected midyear, if anything, slightly sooner than expected. The company also noted it completed enrollment in the tox study, which could be important in enabling regulatory sign-off for higher doses potentially necessary in other indications such as anxiety. Though early, we continue to believe '354 has a promising profile that could address the significant limitations of benzos.

• **'499 mechanism becoming clearer--could help in near-term regulatory discussions.** The company remains encouraged by recently-reported effects of '499 in CKD, showing improvements in fibrotic biomarkers, which CNCE believes indicates an underlying mechanism of preventing the collagen deposition that causes disease progression; we agree that this could explain the apparent longer time course of action and increase the likelihood the drug is conferring true benefits, despite mixed data from the study. An end-of-phase II should come around mid-year, and we believe should set it up for a potential collaboration.

Valuation Range: \$21.00 to \$23.00

Our valuation range is based on applying a 30x multiple to our 2022 estimated EPS and discounting at 15%, blended with 6x multiple of 2022 estimated sales, and discounting 12%. Key risks, in our view, are failure of '354 and/or '499 to show efficacy in subsequent studies and regulatory hurdles in spasticity or CKD.

Investment Thesis:

We believe Concert's proprietary and partnered candidates, and drug deuteration platform, will generate long-term value.

Outperform / V

Sector: Biotechnology

Market Weight

Earnings Estimate Revised Down

EPS	2013A	2014E		2015E	
		Curr.	Prior	Curr.	Prior
Q1 (Mar.)	NE	(\$0.76) A	(0.52)	NE	
Q2 (June)	NE	(0.32)	(0.30)	NE	
Q3 (Sep.)	NE	(0.45)	(0.44)	NE	
Q4 (Dec.)	(4.66)	(0.49)	(0.47)	NE	
FY	(\$4.99)	(\$1.88)	(1.71)	(\$0.74)	(0.66)
CY	(\$4.99)	(\$1.88)		(\$0.74)	
FY P/E	NM	NM		NM	
Rev.(MM)	\$25,408	\$6,253		\$22,520	

Source: Company Data, Wells Fargo Securities, LLC estimates, and Reuters
NA = Not Available, NC = No Change, NE = No Estimate, NM = Not Meaningful
V = Volatile, * = Company is on the Priority Stock List

Ticker	CNCE
Price (05/14/2014)	\$9.85
52-Week Range:	\$7-17
Shares Outstanding: (MM)	17.9
Market Cap.: (MM)	\$176.2
S&P 500:	1,894.38
Avg. Daily Vol.:	113,641
Dividend/Yield:	\$0.00/0.0%
LT Debt: (MM)	\$0.0
LT Debt/Total Cap.:	0.0%
ROE:	NM
3-5 Yr. Est. Growth Rate:	NM
CY 2014 Est. P/E-to-Growth:	NM
Last Reporting Date:	05/14/2014
	Before Open

Source: Company Data, Wells Fargo Securities, LLC estimates, and Reuters

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All estimates/forecasts are as of 05/14/14 unless otherwise stated.

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Together we'll go far



Biotechnology

Company Description:

Concert Pharmaceuticals (CNCE), Inc., headquartered in Lexington, Massachusetts, is a biotechnology company focused on improving therapies in a variety of areas such as neurology and kidney disease, using its platform technology around deuterium substitution. The company's lead development candidate is CTP-354, a GABA-A partial agonist in development for muscle spasticity. Another development candidate is CTP-499, a phosphodiesterase enzyme inhibitor in development for diabetic kidney disease. Alongside '354 and '499, its partnered pipeline includes CTP-730, a deuterated anti-inflammatory drug partnered with Celgene, AVP-786 for major depressive disorder partnered with Avanir, and JZP-386, a deuterated version of Xyrem for narcolepsy, partnered with Jazz.

Upcoming Milestones

Product	Event	Timeline
CTP-354	Data from Ph.I MAD study, GABA _A receptor occupancy study	mid-2014
	Preclinical toxicology study of higher doses, to enable dosing >6mg/day in clinical trials	mid-2014
	Initiate ph.II trials in MS/SCI spasticity patients	year-end 2014
	Report ph.II spasticity results	1H16
CPT-499	End-of-ph.II meeting with FDA	mid-2014
	Sign partnership agreement	2H14+
AVP-786	Ph.II for treatment-resistant MDD initiation	2H14
CTP-730	Ph.I study initiation	2H14
JZP-386	Ph.I study initiation	2014

Source: Company reports and Wells Fargo Securities, LLC estimates

Product Pipeline

Product (partner)	Indication/mechanism	Status
CTP-354	Spasticity, anxiety, pain; subtype selective GABA _A receptor modulator	Phase I
CTP-499	Diabetic nephropathy; multi-subtype selective inhibitor of phosphodiesterases	Phase II
AVP-786 (AVNR)	Neurologic and psychiatric disorders, depression; deuterium-substituted dextromethorphan analog plus low-dose quinidine	Entering phase II
CTP-730 (CELG)	Inflammatory diseases	Entering phase I
JZP-386 (JZP)	Narcolepsy; deuterium-substituted Xyrem analog	Entering phase I
C-10068	Pain and seizures; deuterium-substituted dextromethorphan/ analog	Preclinical
d-ivacaftor	CF, COPD	Preclinical
d-praziquantel (NIH)	Parasitic diseases	Preclinical

Source: Company reports and Wells Fargo Securities, LLC

Concert Pharma (CNCE)
Statement of Operations (Income Statement)

	2012A	1Q A	2013A	1Q E	2Q E	3Q E	4Q E	2014E	2015E	2016E	2017E	2018E	2019E	2020E	2021E	2022E	2023E
Revenues (1)																	
Revenues from CTP-354																	
Royalties from sales of CTP-499																	
Royalties from sales of AYP-786																	
Royalties from sales of JZP-386																	
Millstones	\$1,500	\$2,000	\$2,000	\$0	\$2,000	\$0	\$0	\$2,000	\$14,000	\$30,000	\$15,000	\$34,000	\$45,000	\$0	\$48,000	\$72,000	\$15,000
License and research and development revenue	\$11,349	\$3,873	\$23,408	\$1,613	\$980	\$980	\$980	\$4,253	\$8,520	\$12,520	\$12,520	\$12,520	\$9,000	\$9,000	\$9,000	\$9,000	\$9,000
Total revenues, net	\$12,849	\$5,873	\$25,408	\$1,613	\$2,980	\$980	\$980	\$6,253	\$22,520	\$42,520	\$27,520	\$61,722	\$87,127	\$112,843	\$248,483	\$487,493	\$698,624
Expenses																	
Cost of goods sold																	
Research and development	\$24,193	\$5,039	\$21,790	\$5,594	\$5,700	\$6,100	\$6,700	\$24,094	\$24,817	\$25,561	\$26,328	\$27,118	\$27,932	\$4,892	\$9,669	\$15,536	\$22,622
Selling, general and administrative	\$7,266	\$1,964	\$8,028	\$2,538	\$2,600	\$2,700	\$2,900	\$10,738	\$11,275	\$11,726	\$12,195	\$14,634	\$32,195	\$54,731	\$82,096	\$102,620	\$102,620
Total operating expenses	\$31,459	\$7,003	\$29,818	\$8,132	\$8,300	\$8,800	\$9,600	\$34,832	\$36,092	\$37,287	\$38,523	\$41,752	\$60,126	\$58,392	\$121,397	\$148,678	\$156,680
Operating income	(\$18,610)	(\$1,130)	(\$4,410)	(\$6,519)	(\$5,320)	(\$7,920)	(\$8,720)	(\$28,579)	(\$13,572)	\$5,233	(\$11,003)	\$19,970	\$27,001	\$24,450	\$127,086	\$338,815	\$542,144
Investment income	\$22	\$0	\$21	\$0	\$26	\$24	\$22	\$72	\$97	\$127	\$132	\$122	\$133	\$175	\$262	\$469	\$858
Interest and other expense	(\$1,856)	(\$649)	(\$1,667)	(\$431)	(\$265)	(\$207)	(\$148)	(\$1,051)	(\$294)	\$0	\$0	\$0	\$0	\$0	\$0	\$0	\$0
CTP-499 commercialization payment to GSK																	
(Loss) income before benefit from income taxes	(\$20,444)	(\$1,779)	(\$6,056)	(\$6,950)	(\$5,658)	(\$8,103)	(\$8,846)	(\$29,558)	(\$13,769)	\$5,360	(\$10,871)	\$17,342	\$27,134	\$24,625	\$127,348	\$339,284	\$543,002
Benefit (expense) from income taxes	\$0	\$0	\$0	\$0	\$0	\$0	\$0	\$0	\$0	\$0	\$0	(\$347)	(\$543)	(\$492)	(\$7,641)	(\$27,143)	(\$59,730)
Net (loss) income	(\$20,444)	(\$1,779)	(\$6,056)	(\$6,950)	(\$5,658)	(\$8,103)	(\$8,846)	(\$29,558)	(\$13,769)	\$5,360	(\$10,871)	\$16,995	\$26,591	\$24,132	\$119,708	\$312,142	\$483,272
Accretion on redeemable convertible preferred stock	(\$388)	(\$98)	(\$396)	(\$55)	(\$100)	(\$100)	(\$100)	(\$355)	(\$300)	\$0	\$0	\$0	\$0	\$0	\$0	\$0	\$0
Net loss applicable to common shareholders	(\$20,832)	(\$1,877)	(\$6,452)	(\$7,005)	(\$5,758)	(\$8,203)	(\$8,946)	(\$29,913)	(\$14,069)	\$5,360	(\$10,871)	\$16,995	\$26,591	\$24,132	\$119,708	\$312,142	\$483,272
Earnings per share (EPS)	(\$16.15)	(\$1.46)	(\$4.99)	(\$0.76)	(\$0.32)	(\$0.45)	(\$0.49)	(\$1.86)	(\$0.74)	\$0.25	(\$0.94)	\$0.75	\$1.14	\$0.94	\$4.56	\$11.62	\$17.59
Shares Outstanding (Basic)	1,290	1,290	1,292	9,188	17,900	18,100	18,300	15,872	18,900	19,500	20,100	20,700	21,300	23,566	24,166	24,766	25,366
Shares Outstanding (Diluted)	1,290	13,237	13,237	11,296	20,008	20,208	20,408	17,980	21,008	21,608	22,208	22,808	23,408	25,674	26,274	26,874	27,474

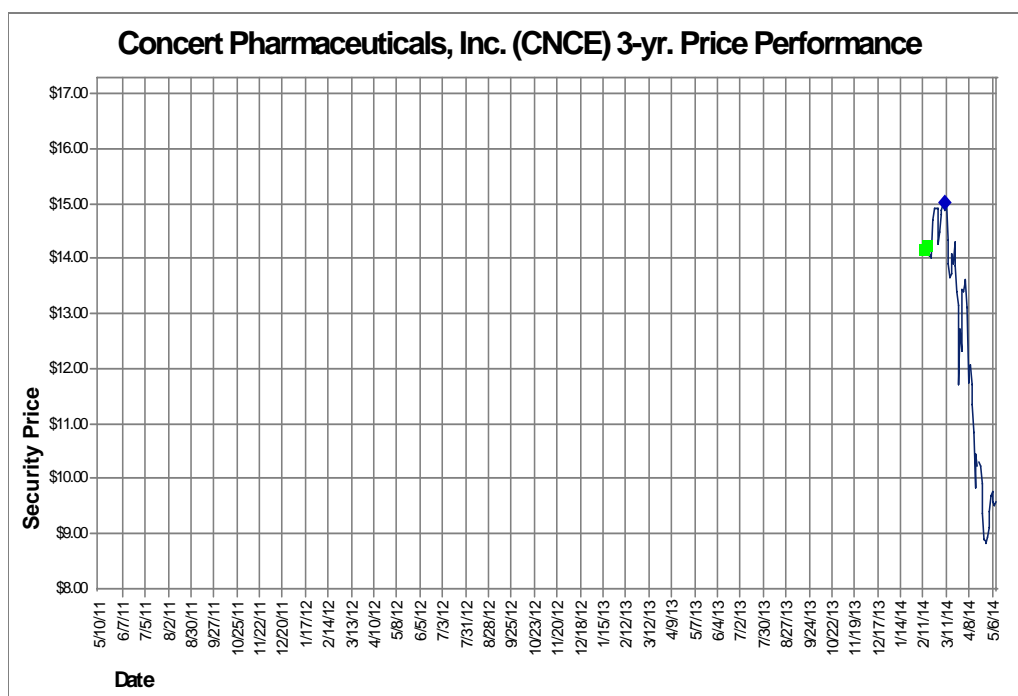
Source: Company; Wells Fargo Securities, LLC estimates

Note: We do not provide estimates of 2015 quarterly EPS at this point.

Note: In 000's \$, except per share amounts; FY ends 12/31

(1) Not probability weighted

Required Disclosures



	Date	Publication Price (\$)	Rating Code	Val. Rng. Low	Val. Rng. High	Close Price (\$)
■	2/13/2014		IPO at \$14.00			
	3/10/2014		Abrahams, M.D.			
◆	3/10/2014	14.88	1	21.00	23.00	15.03

Source: Wells Fargo Securities, LLC estimates and Reuters data

Symbol Key

- ▼ Rating Downgrade
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- Valuation Range Change
- ◆ Initiation, Resumption, Drop or Suspend
- Analyst Change
- Split Adjustment

Rating Code Key

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CNCE: Key risks, in our view, are failure of '354 and/or '499 to show efficacy in subsequent studies and regulatory hurdles in spasticity or CKD.

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