

CareDx, Inc. (CDNA)

Overweight

1Q15 Upside; Kidney On-Track With Revised Timelines; Remain Overweight

CONCLUSION

CareDx reported 1Q15 revenue growth of 21.8% to \$7.2M, above our in-line \$6.8M estimate with upside driven by higher reimbursement per test. CareDx launched the DART 1 study beginning of May to assess clinical validity of cfDNA in kidney transplant patients and management expects interim data 1H16. cfDNA kidney is a >\$1B opportunity and favorable results from DART 1 will be key for test development. Given initial data of cfDNA in heart transplants (cfDNA detects rejection before traditional biopsies) we are expecting positive results. Beyond DART 1, management reiterated its DART 2 clinical utility study as well as revised cfDNA kidney launch timelines. Given previously adjusted timelines were reiterated, we are leaving our forward estimates largely unchanged. We remain Overweight with a \$8 PT based on 3.2x FY17 EV/Revenue discounted 25% basis.

- 1Q15 Upside:** CareDx reported 21.8% yoy revenue growth to \$7.2M, above our \$6.8M estimate (Street: \$6.8M). Upside in the quarter was driven by higher-than-expected reimbursement per test (~80% vs. PJC: 77%). Product gross margin decreased 110 bpts yoy to 62.4% (-990 bpts qoq), below our 66.5% estimate with a reduction in excess consumables inventory leading to the qoq decline. Operating expenses of \$5.9M were favorable to our \$6.3M estimate. All-in, EPS of (\$0.19) was \$0.01 below our in-line (\$0.18) estimate. CareDx entered into a new ~\$16M term loan (~5% per annum) during quarter and retired ~\$11.4M of existing debt (~10% per annum). As a result, CareDx's cash balance increased \$2.6M sequentially to \$39.0M (\$23.3M net cash).
- Business Update:** Management described continued progress penetrating the domestic Allomap opportunity, with tests delivered increasing 11% yoy to ~3,100 (PJC: 3,082). Encouragingly, 10 centers added Allomap transplant protocols during the quarter, with 58 centers out of 129 now following Allomap guidelines. Management reiterated cfDNA heart data presented at ISHLT. As a reminder, our take of the data is positive (see our note [here](#)) with cfDNA detecting rejection up to 25 days before traditional biopsies. Management reiterated revised timelines for its cfDNA kidney test development and management enrolled the first DART 1 patients in May. As a reminder, DART 1 will assess the clinical validity of cfDNA in ~200 kidney patients from 6 centers and management expects interim data 1H16. Additionally, DART 2 (clinical utility of kidney cfDNA) will begin following DART 1's interim data readout and management continues to expect no kidney revenue in 2016.
- FY15 Guidance:** Management reiterated revenue guidance of \$28M-\$30M (+2.6%-9.9%). Given the strong quarter and 10 incremental centers adhering to transplant protocols, we continue to view guidance as achievable, with room for upside.

RISKS TO ACHIEVEMENT OF PRICE TARGET

Risks: weaker-than-expected AlloMap penetration, pipeline delays and competition.

COMPANY DESCRIPTION

CareDx develops novel tests for recipient organ transplant surveillance.

YEAR	REVENUE (US\$ m)						EARNINGS PER SHARE (US\$)					
	Mar	Jun	Sep	Dec	FY	FY RM	Mar	Jun	Sep	Dec	FY	FY P/E
2014A	5.9	6.8	6.7	8.0	27.3	2.2x	(0.21)	0.02	0.12	0.00	(0.08)	NM
2015E	7.2A	7.1	7.4	7.7	29.5	2.0x	(0.19)A	(0.16)	(0.15)	(0.13)	(0.62)	NM
2016E	8.3	8.7	9.2	9.7	35.8	1.7x	(0.12)	(0.09)	(0.09)	(0.09)	(0.39)	NM

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CareDx, Inc.

PRICE: US\$4.90

TARGET: US\$8.00

3.2x FY17E EV/Revenue discounted 25% to FY16E (FY17E Rev: \$43.4M, FY16E: 12.7M shares outstanding, \$0.26 in net cash/sh).

William R. Quirk, CFA

Sr Research Analyst, Piper Jaffray & Co.
612 303-6858, william.r.quirk@pjc.com

Alexander D. Nowak

Research Analyst, Piper Jaffray & Co.
612 303-5679, alexander.d.nowak@pjc.com

Changes	Previous	Current
Rating	—	Overweight
Price Tgt	—	US\$8.00
FY15E Rev (mil)	US\$29.0	US\$29.5
FY16E Rev (mil)	—	US\$35.8
FY15E EPS	US\$(0.72)	US\$(0.62)
FY16E EPS	US\$(0.51)	US\$(0.39)
52-Week High / Low	US\$10.89 / US\$4.88	
Shares Out (mil)		12.1
Market Cap. (mil)		US\$59.3
Avg Daily Vol (ooo)		32
Book Value/Share		US\$3.34
Net Cash Per Share		US\$1.97
Debt to Total Capital		28.0%
Yield		0.00%
Fiscal Year End		Dec

Price Performance - 1 Year

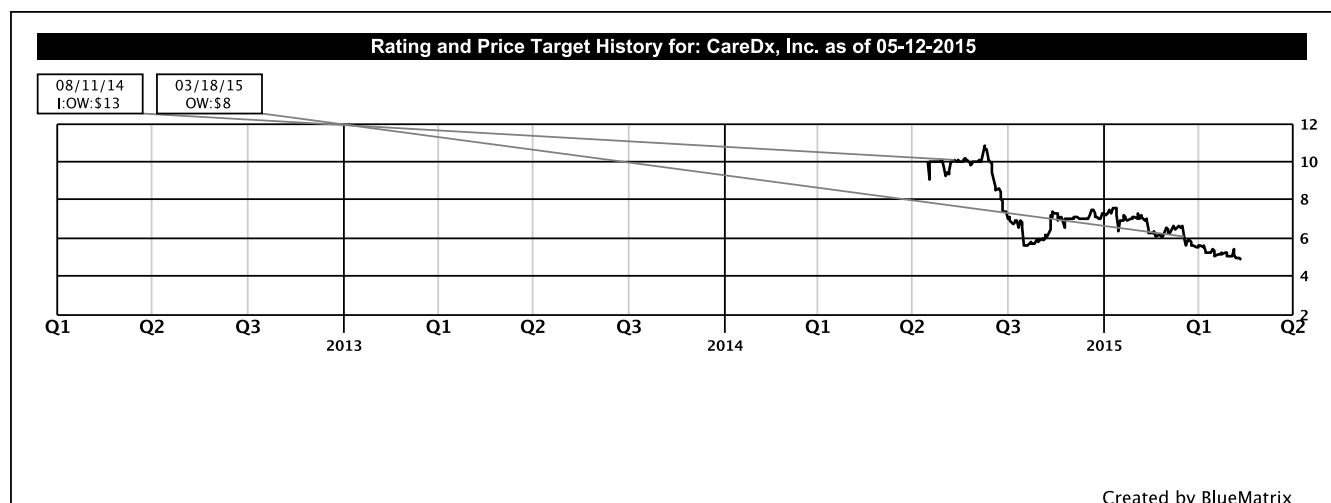


Source: Bloomberg

	2014A				2015E				2016E				Annual				
	Mar	Jun	Sep	Dec	Mar	Jun	Sep	Dec	Mar	Jun	Sep	Dec	2013A	2014A	2015E	2016E	2017E
	Qtr 1 A	Qtr 2 A	Qtr 3 A	Qtr 4 A	Qtr 1 A	Qtr 2 E	Qtr 3 E	Qtr 4 E	Qtr 1 E	Qtr 2 E	Qtr 3 E	Qtr 4 E					
Total Revenue	5,924	6,776	6,654	7,952	7,216	7,145	7,393	7,743	8,267	8,697	9,178	9,672	22,098	27,306	29,497	35,814	43,414
Cost of Product Revenue	2,162	2,403	1,772	2,204	2,711	2,343	2,356	2,406	2,518	2,612	3,055	3,409	9,078	8,541	9,817	11,594	15,416
Gross Profit	3,762	4,373	4,882	5,748	4,505	4,801	5,036	5,338	5,748	6,085	6,123	6,263	13,020	18,765	19,680	24,220	27,999
Operating Expenses:																	
Research & Development - Total	720	792	1,036	1,298	1,421	2,268	2,355	2,396	2,560	2,610	2,666	2,715	0	3,846	8,440	10,550	10,791
Research & Development - Core	720	792	961	1,198	1,308	2,143	2,218	2,246	2,397	2,435	2,478	2,515	3,176	3,671	7,915	9,825	9,741
RUO Heart	-	-	75	100	113	125	138	150	163	175	188	200	0	175	525	725	1,050
Sales & Marketing	1,474	1,610	1,753	1,635	2,023	2,198	2,223	2,248	2,378	2,428	2,333	2,383	5,891	6,472	8,692	9,522	10,307
General & Administrative	1,795	1,566	1,976	2,349	2,705	2,036	2,063	2,091	2,067	2,087	2,111	2,128	4,808	7,686	8,894	8,393	8,672
Other		750	(1,276)	37	(253)				110	110	110	110					
Total Operating Expense	3,989	4,718	3,489	5,319	5,896	6,503	6,641	6,734	7,115	7,235	7,219	7,336	13,875	17,515	25,774	28,905	30,210
Operating Income (Loss)	(227)	(345)	1,393	429	(1,391)	(1,701)	(1,605)	(1,397)	(1,366)	(1,151)	(1,096)	(1,073)	(855)	1,250	(6,093)	(4,686)	(2,211)
Interest & other income (expense), net	(1,077)	(278)	(69)	(434)	(881)	(147)	(142)	(147)	(196)	(150)	(149)	(156)	(2,686)	(1,858)	(1,317)	(650)	(715)
Pretax Income (Loss)	(1,304)	(623)	1,324	(5)	(2,272)	(1,848)	(1,747)	(1,543)	(1,562)	(1,300)	(1,245)	(1,228)	(3,540)	(608)	(7,410)	(5,335)	(2,927)
Provision for Income Taxes	0	(1,500)	0	0	0	0	0	0	0	0	0	0	0	(1,500)	0	0	0
Net Income (Loss) - Reported	(1,304)	877	1,324	(5)	(2,272)	(1,848)	(1,747)	(1,543)	(1,562)	(1,300)	(1,245)	(1,228)	(3,540)	892	(7,410)	(5,335)	(2,927)
SBC	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
Non-Recurring	0	(750)	0	0	0	0	0	0	110	110	110	110	0	(750)	0	440	440
Net Income (Loss) - Ongoing (w/ SBC)	(1,304)	127	1,324	(5)	(2,272)	(1,848)	(1,747)	(1,543)	(1,452)	(1,190)	(1,135)	(1,118)	(3,540)	142	(7,410)	(4,895)	(2,487)
Net Income (Loss) - Non-GAAP	(1,304)	127	1,324	(5)	(2,272)	(1,848)	(1,747)	(1,543)	(1,452)	(1,190)	(1,135)	(1,118)	(3,540)	142	(7,410)	(4,895)	(2,487)
Net Income (assuming 40% Tax)																	
Diluted EPS (Reported)	(0.21)	0.13	0.12	(0.00)	(0.19)	(0.16)	(0.15)	(0.13)	(0.13)	(0.10)	(0.10)	(0.10)	(0.35)	0.03	(0.62)	(0.42)	(0.23)
Diluted EPS (Ongoing, w/ SBC)	(0.21)	0.02	0.12	(0.00)	(0.19)	(0.16)	(0.15)	(0.13)	(0.12)	(0.09)	(0.09)	(0.09)	(0.57)	(0.08)	(0.62)	(0.39)	(0.19)
Avg. Share Outstanding, Diluted	6,172	6,940	11,219	12,129	11,814	11,914	12,014	12,342	12,442	12,542	12,642	12,742	6,172	9,115	12,021	12,592	12,992
Expense Variables:																	
Cost of Revenue	36.5%	35.5%	26.6%	27.7%	37.6%	32.8%	31.9%	31.1%	30.5%	30.0%	33.3%	35.2%	41.1%	31.3%	33.3%	32.4%	35.5%
Research & Development - Total	12.2%	11.7%	15.6%	16.3%	19.7%	31.7%	31.9%	30.9%	31.0%	30.0%	29.0%	28.1%					
Research & Development - Core	12.2%	11.7%	14.4%	15.1%	18.1%	30.0%	30.0%	29.0%	29.0%	28.0%	27.0%	26.0%	14.4%	13.4%	26.8%	27.4%	22.4%
RUO Heart	0.0%	0.0%	1.1%	1.3%	1.6%	1.7%	1.9%	1.9%	2.0%	2.0%	2.0%	2.1%					
Sales & Marketing	24.9%	23.8%	26.3%	20.6%	28.0%	30.8%	30.1%	29.0%	28.8%	27.9%	25.4%	24.6%	26.7%	23.7%	29.5%	26.6%	23.7%
General & Administrative	30.3%	23.1%	29.7%	29.5%	37.5%	28.5%	27.9%	27.0%	25.0%	24.0%	23.0%	22.0%	21.8%	28.1%	30.2%	23.4%	20.0%
Total Operating Expenses	67.3%	69.6%	52.4%	66.9%	81.7%	91.0%	89.8%	87.0%	86.1%	83.2%	78.7%	75.8%	62.8%	64.1%	87.4%	80.7%	69.6%
Effective Interest Rate, cash	0.4%	0.4%	0.4%	0.4%	0.4%	0.5%	0.6%	0.6%	0.7%	0.7%	0.8%	0.8%	-52.4%	-5.1%	-4.5%	-3.4%	-4.4%
Effective Tax Rate	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM
Margin Analysis:																	
Gross Margin	63.5%	64.5%	73.4%	72.3%	62.4%	67.2%	68.1%	68.9%	69.5%	70.0%	66.7%	64.8%	58.9%	68.7%	66.7%	67.6%	64.5%
Incremental Gross Margin	96.0%	78.5%	186.0%	106.2%	57.5%	116.2%	20.9%	196.9%	118.3%	82.7%	60.9%	48.0%	77.6%	110.3%	41.8%	71.9%	49.7%
Operating Margin	NM	NM	20.9%	5.4%	NM	NM	NM	NM	NM	NM	NM	NM	NM	4.6%	NM	NM	NM
Incremental Operating Margin	58.4%	50.1%	52.8%	-2.1%	-109.6%	-368.0%	-405.8%	876.6%	12.8%	42.6%	34.6%	22.5%	126.7%	40.4%	-335.1%	22.3%	32.6%
Pretax Margin	NM	NM	19.9%	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM
Net Income Margin	NM	12.9%	19.9%	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	3.3%	NM	NM	NM
YoY Growth Rates:																	
Total Revenues	18.9%	24.2%	14.6%	35.8%	21.8%	5.4%	11.1%	-2.6%	14.6%	21.7%	24.1%	24.9%	792.9%	23.6%	8.0%	21.4%	21.2%
Cost of Goods Sold (Product Sales)	1.8%	13.4%	-29.2%	-5.5%	25.4%	-2.5%	33.0%	9.2%	-7.1%	11.5%	29.6%	41.7%	94.0%	-5.9%	14.9%	18.1%	33.0%
Research & Development	-6.1%	4.0%	20.7%	23.7%	37.2%	36.5%	26.8%	37.5%	17.5%	10.5%	4.9%	6.0%	-61.8%	15.6%	115.6%	24.1%	-0.9%
S, G & A	-28.1%	-6.4%	44.1%	81.2%	81.7%	170.6%	130.8%	87.4%	83.2%	13.6%	11.7%	12.0%	-26.3%	9.9%	34.3%	9.5%	8.2%
Operating Expenses	9.7%	31.3%	-4.0%	76.5%	47.8%	37.8%	90.3%	26.6%	20.7%	11.3%	8.7%	8.9%	-41.0%	26.2%	47.2%	12.1%	4.5%
Operating Income	NM	NM	NM	-16.0%	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM
Pretax Income	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM
Net Income (Reported)	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM
Net Income (Ongoing)	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM
EPS	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM
Other Data:																	
Days Sales Outstanding	33.6	25.7	23.8	25.5	28.3	23.5	23.4	23.1	22.5	22.8	22.8	22.8	37.5	35.9	25.0	25.9	27.1
Inventory Turns	13.9	14.4	12.8	14.9	14.8	12.0	12.0	12.0	12.0	12.0	12.0	12.0	35.1	14.2	13.0	12.0	12.1
EBITDA Per Share	(0.02)	(0.14)	0.14	0.06	(0.09)	(0.11)	(0.10)	(0.09)	(0.07)	(0.06)	(0.05)	(0.05)	(0.03)	0.13	(0.39)	(0.23)	(0.03)
Free Cash Flow Per Share	0.20	(0.08)	(0.39)	(0.07)	(0.05)	(0.12)	(0.11)	(0.12)	(0.10)	(0.09)	(0.07)	(0.08)	0.33	(0.54)	(0.40)	(0.34)	(0.18)
Net Debt (Cash) Per Share	1.66	1.57	(2.35)	(2.06)	(1.97)	(1.69)	(1.42)	(1.12)	(0.86)	(0.62)	(0.35)	(0.26)	(0.83)	(4.00)	(2.45)	(1.50)	(1.24)

Source: Company reports and Piper Jaffray & Co. Current disclosure information for this company is located at <http://www.piperjaffray.com/researchdisclosures>.

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R: Resuming Coverage
T: Transferring Coverage
D: Discontinuing Coverage
S: Suspending Coverage
OW: Overweight
N: Neutral
UW: Underweight
NA: Not Available
UR: Under Review

Distribution of Ratings/IB Services Piper Jaffray				
Rating	Count	Percent	IB Serv./Past 12 Mos.	
			Count	Percent
BUY [OW]	380	61.49	102	26.84
HOLD [N]	223	36.08	14	6.28
SELL [UW]	15	2.43	0	0.00

Note: Distribution of Ratings/IB Services shows the number of companies currently in each rating category from which Piper Jaffray and its affiliates received compensation for investment banking services within the past 12 months. FINRA rules require disclosure of which ratings most closely correspond with "buy," "hold," and "sell" recommendations. Piper Jaffray ratings are not the equivalent of buy, hold or sell, but instead represent recommended relative weightings. Nevertheless, Overweight corresponds most closely with buy, Neutral with hold and Underweight with sell. See Stock Rating definitions below.

Analyst Certification — William R. Quirk, CFA, Sr Research Analyst — Alexander D. Nowak, Research Analyst

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- **Neutral (N):** Anticipated to perform in line relative to the median of the group of stocks covered by the analyst.
- **Underweight (UW):** Anticipated to underperform relative to the median of the group of stocks covered by the analyst.

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