

Dermira, Inc.

DERM - BUY - The Beauty of This Company Proves to Be More Than "Skin" Deep;
Increasing PT to \$40 from \$22

August 7, 2015

Conclusion: On August 5, DERM announced the pricing of a follow-on public offering that generated \$96.75MM of gross proceeds (\$90.4MM, net). A 675,000 share shoe remains, and we estimate this could generate an additional \$14.5MM in gross proceeds (\$13.6MM, net, assuming \$21.50 per share). This news along with pipeline advancements drive us to increase our PT to \$40 from \$22. We arrive at our new 12-month PT by using a DCF analysis (increased our exit multiple from 6x to 9x). We have even greater conviction in our positive investment thesis for DERM now that the company has enough cash to fund operations through '17 and given its key data releases, which include Phase 2b data for DRM01, Cimzia Phase 3 data, and DRM04 Phase 3 data. Over the past few months, the company has initiated Phase 3 studies for DRM04 in axillary hyperhidrosis (data expected 2H16) and Phase 2b for DRM01 in acne vulgaris (data expected 1H16). We continue to think stock price appreciation will be driven by upward earnings revisions because sales from DERM's 3 late-stage assets could reach ~\$500MM by '21. Also, DERM is an attractive company in a consolidating industry, in our view.

Multiple pipeline catalysts will drive stock price appreciation in '15+, in our view. We outline these catalysts below. See page 3 for details. DERM has 2 pipeline products in Phase 3 trials (Cimzia and DRM04). FDA filings and approvals, for both products, are anticipated in '17 and '18, respectively. We also highlight the potential for additional upside from business development. We believe DERM would only acquire a high quality, differentiated drug.

DERM's pipeline addresses large unmet needs in the \$21B dermatology market. This includes psoriasis, hyperhidrosis, and acne. These areas of unmet need are growing double digits while the overall dermatology market is growing mid-single digits.

We have updated our financial model for the recent equity raise. The increase in our '15E EPS is a result of a higher share count from the recent raise. Our '16E EPS decreases because we had assumed an equity raise in '16. With the recent financing, we do not assume another raise again until '17.

Potential Catalysts. 1) DRM01 Ph2b results ~1H16; 2) DRM04 Ph3 data 2H16; 3) Cimzia Ph3 data in '17, approval in '18; and 4) Business development.

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DERM BUY

COMPANY UPDATE

Investment Thesis: Growth

SHARE PRICE	\$24.10
PRICE TARGET	\$40.00

Revenue (\$M) (FY Dec)	1Q	2Q	3Q	4Q	FY
2014	0.0	0.0	0.0	7.3	7.3
2015	0.0	0.0E	0.0E	0.0E	0.0E
2016	—	—	—	—	13.0E

Adjusted EPS (\$)	1Q	2Q	3Q	4Q	FY
2014	(0.82)	(0.80)	(0.57)	(0.29)	(2.49)
P/E					NM
2015	(0.57)	(0.73)E	(0.77)E	(0.97)E	(3.04)E
Prior	—	—	(0.88)E	(1.17)E	(3.34)E
P/E					NM
2016	—	—	—	—	(2.51)E
Prior	—	—	—	—	(2.25)E
P/E					NM

Market Data & Valuation Multiples

52-Week Range	\$12.68 - \$25.24
Shares Out (M)	24.7
Market Cap (M)	\$545
ADV (3 mo; 000)	70

SCENARIO	VALUATION	INVESTMENT THESIS
Bull Case	2021E EPS: \$6.00 12-Month Bull-Case Scenario: \$60 Probability: 13% Upside/Downside Potential: 155%	<ul style="list-style-type: none"> • Cimzia launch in 2018, 2021 sales of \$140.7 million • DRM04 launch in 2018, 2021 sales of \$145.3 million • DRM01 launch in 2019, 2021 sales of \$330.1 million • Accretive business development and/or M&A
Base Case	2021E EPS: \$5.01 12-Month Bull-Case Scenario: \$40 Probability: 74% Upside/Downside Potential: 70%	<ul style="list-style-type: none"> • Cimzia launch in 2018, 2021 sales of \$113.5 million • DRM04 launch in 2018, 2021 sales of \$127.7 million • DRM01 launch in 2019, 2021 sales of \$241.7 million • No business development and/or M&A
Bear Case	2021E EPS: \$4.25 12-Month Bull-Case Scenario: \$18 Probability: 13% Upside/Downside Potential: -24%	<ul style="list-style-type: none"> • Cimzia launch in 2018, 2021 sales of \$95.2 million • DRM04 launch in 2019, 2021 sales of \$110.3 million • DRM01 launch in 2020, 2021 sales of \$180.7 million • No business development and/or M&A

Source: Guggenheim Securities, LLC

VALUATION METHODOLOGY AND RISKS

We use Discounted Cash Flow (DCF) to get to our new 12-month price target of \$40. We use a WACC of 20% and an exit multiple of 9 times (up from 6 times before) forward EBIT. Risks to our valuation include: 1) Larger companies with more resources developing dermatology products that compete with DERM; 2) Pipeline setbacks; 3) Actions taken by development partners on collaborations; and 4) Competition to Cimzia, DRM 01 and DRM04 coming to market before DERM's products.

CATALYST CALENDAR

Date	Driver	Upcoming Event
2015		
2015	DRM02	Assess preclinical data and determine next steps
2015	DRM05	Assess preclinical data and determine next steps
2016+		
1H16	DRM01	Report Phase 2b data
Mid-16	Cimzia	Complete enrollment of Phase 3 trials
2H16	DRM04	Complete enrollment of Phase 3 trials and Phase 3 data
1H17	DRM01	Initiate Phase 3 trials
2017	DRM04	Complete carcinogenicity study
2017	Cimzia	Phase 3 topline data
2017	DRM04	FDA Submission
2H17	Cimzia	FDA Submission
2018	Cimzia	FDA Approval (our assumption)
2018	DRM04	FDA Approval (our assumption)
1H18	DRM01	Complete enrollment of P3 trials
2018	DRM01	Report Phase 3 data
2018	DRM01	FDA Submission
2019	DRM01	FDA Approval (our assumption)

Source: Guggenheim Securities, LLC and Company reports

FINANCIAL MODEL

(\$ in MM, except per share amounts)	Dermira 2015		Guggenheim 2015
	Guidance	Midpoint	Estimate
Operating Expense	\$80 to \$85	\$83	\$85
R&D as a % of Total Operating Expenses	75%		75%

Source: Guggenheim Securities, LLC and Company Reports

(1) Of the total expected operating expenses for 2015, DERM expects R&D expenses to comprise approximately 75% and G&A to comprise the remaining 25%.

(2) DERM also expects that research and development and total operating expenses in the second half of 2015 will be significantly higher than in the first half of the year.

Dermira - Quarterly Income Statement Analysis 2013-2021E

(\$ in Millions)													
(Year Ended December 31)	2013	2014	1Q15A	2Q15A	3Q15E	4Q15E	2015E	2016E	2017E	2018E	2019E	2020E	2021E
Total Revenue	0.0	7.3	0.0	0.0	0.0	0.0	0.0	13.0	15.7	23.1	138.7	281.8	496.2
COGS	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	2.9	14.7	31.3	56.1
Gross Profit	0.0	7.3	0.0	0.0	0.0	0.0	0.0	13.0	15.7	20.3	124.0	250.5	440.2
SG&A	4.4	8.3	4.1	5.1	5.2	6.7	21.1	23.0	33.0	86.0	95.0	100.0	103.5
R&D	17.9	30.7	10.1	13.3	17.0	23.0	63.4	68.0	52.2	38.0	45.0	47.0	49.0
Other (Income)/Expense	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
Total Operating Expense	22.3	39.0	14.2	18.4	22.2	29.7	84.5	91.0	85.2	124.0	140.0	147.0	152.5
Operating Income	(22.3)	(31.7)	(14.2)	(18.4)	(22.2)	(29.7)	(84.5)	(78.0)	(69.5)	(103.7)	(16.0)	103.5	287.7
Interest and Other Income (Expense)	(0.0)	0.0	0.2	0.4	0.4	0.6	1.6	1.8	1.0	1.9	0.8	0.5	1.0
Interest Expense	(0.0)	(0.2)	(0.0)	(0.0)	(0.0)	(0.0)	(0.1)	(0.1)	(0.1)	(0.1)	(0.1)	(0.1)	(0.1)
Non-Operating Items	(0.0)	(0.1)	0.2	0.4	0.4	0.6	1.5	1.7	0.9	1.7	0.7	0.4	0.9
Pre-tax Income	(22.4)	(31.8)	(14.0)	(18.0)	(21.8)	(29.1)	(83.0)	(76.2)	(68.6)	(102.0)	(15.3)	103.9	288.5
Tax Rate	0.0%	NM	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	40.0%	40.0%
Taxes	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	41.5	115.4
Net Income	(22.4)	(31.9)	(\$14.0)	(\$18.0)	(\$21.8)	(\$29.1)	(\$83.0)	(\$76.2)	(\$68.6)	(\$102.0)	(\$15.3)	\$62.3	\$173.1
Average Shares Diluted	9.7	12.8	24.7	24.8	28.2	29.9	27.3	30.3	33.3	33.6	33.9	34.2	34.5
Adjusted Diluted EPS	(\$2.31)	(\$2.49)	(\$0.57)	(\$0.73)	(\$0.77)	(\$0.97)	(\$3.04)	(\$2.51)	(\$2.06)	(\$3.03)	(\$0.45)	\$1.82	\$5.01
%Change YOY													
Total Revenue	NM	NM	NM	NM	NM	-100.0%	-100.0%	NM	20.8%	47.4%	499.2%	103.2%	76.1%
COGS	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	410.9%	113.3%	79.2%
Gross Profit	NM	NM	NM	NM	NM	-100.0%	-100.0%	NM	20.8%	29.1%	511.6%	102.0%	75.7%
SG&A	89.8%	128.8%	191.4%	207.9%	120.2%	154.9%	8.9%	43.5%	160.6%	10.5%	5.3%	3.5%	3.5%
R&D	71.2%	50.9%	91.1%	181.8%	108.4%	106.4%	7.2%	-23.2%	-27.2%	18.4%	4.4%	4.3%	4.3%
Operating Income	NM	NM	NM	NM	NM	NM	NM	-7.8%	-10.8%	49.2%	-84.6%	-747.3%	178.0%
Non-Operating Items	NM	NM	NM	NM	NM	550.5%	NM	12.9%	-45.7%	86.3%	-59.4%	-45.7%	130.4%
Pre-tax Income	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	177.8%
Tax Rate	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	0.0%
Taxes	NM	NM	NM	NM	NM	-100.0%	-100.0%	NM	NM	NM	NM	NM	177.8%
Net Income	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	177.8%
Adjusted Diluted EPS	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	175.4%

Source: Guggenheim Securities, LLC and Company Reports

(1) To be conservative, we assume a 40% tax rate upon profitability.

(2) Assume share dilution in 2016 from additional equity raise.

Dermira - Quarterly Margin Analysis 2013-2021E

	2013	2014	1Q15A	2Q15A	3Q15E	4Q15E	2015E	2016E	2017E	2018E	2019E	2020E	2021E
Total Revenue	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%
COGS	NM	0.0%	NM	NM	NM	NM	NI	0.0%	0.0%	12.4%	10.6%	11.1%	11.3%
Gross Margin	NM	100.0%	NM	NM	NM	NM	NI	100.0%	100.0%	87.6%	89.4%	88.9%	88.7%
SG&A	NM	113.5%	NM	NM	NM	NM	NI	176.9%	210.2%	371.5%	68.5%	35.5%	20.9%
R&D	NM	420.7%	NM	NM	NM	NM	NI	522.7%	332.5%	164.2%	32.4%	16.7%	9.9%
Operating Income	NM	-434.2%	NM	NM	NM	NM	NI	-599.6%	-442.7%	-448.1%	-11.5%	36.7%	58.0%
Pretax Income	NM	-436.2%	NM	NM	NM	NM	NI	-586.3%	-436.7%	-440.6%	-11.0%	36.9%	58.1%
Net Income	NM	-436.6%	NM	NM	NM	NM	NI	-586.3%	-436.7%	-440.6%	-11.0%	22.1%	34.9%

Source: Guggenheim Securities, LLC and Company Reports

Dermira - Quarterly Revenue Model 2013-2021E

(\$ in Millions)													
(Year Ended December 31)	2013	2014	1Q15A	2Q15A	3Q15E	4Q15E	2015E	2016E	2017E	2018E	2019E	2020E	2021E
Cimzia	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	11.7	34.1	74.5	113.5
DRM04	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	11.5	37.0	79.4	127.7
DRM01	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	54.3	114.5	241.7
DRM02	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
DRM05	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
Other	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
Milestones	0.0	7.3	0.0	0.0	0.0	0.0	0.0	13.0	15.7	0.0	13.4	13.4	13.4
TOTAL REVENUES	0.0	7.3	0.0	0.0	0.0	0.0	0.0	13.0	15.7	23.1	138.7	281.8	496.2
% Change YOY													
Cimzia		NM	NM	NM	NM	NM	NM	NM	NM	NM	192.2%	118.7%	52.4%
DRM04		NM	NM	NM	NM	NM	NM	NM	NM	NM	222.0%	114.6%	60.9%
DRM01		NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	111.1%	111.1%
DRM02		NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM
DRM05		NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM
Other		NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM
TOTAL REVENUES		NM	NM	NM	NM	-100.0%	-100.0%	NM	20.8%	47.4%	499.2%	103.2%	76.1%

Source: Guggenheim Securities, LLC and Company Reports

Dermira - Annual Revenue Model 2013-2021E

(\$ in Millions)		Year Ended December 31st,									2014/	2015E/	2016E/	2017E/	2018E/	2019E/	2020E/	2021E/	CAGR
		2013	2014	2015E	2016E	2017E	2018E	2019E	2020E	2021E	2013	2014	2015E	2016E	2017E	2018E	2019E	2020E	16E-21E
Late Stage Pipeline Drug Sales																			
Cimzia	0.0	0.0	0.0	0.0	0.0	11.7	34.1	74.5	113.5		NM	NM	NM	NM	NM	192.2%	118.7%	52.4%	NM
DRM04	0.0	0.0	0.0	0.0	0.0	11.5	37.0	79.4	127.7		NM	NM	NM	NM	NM	222.0%	114.6%	60.9%	NM
DRM01	0.0	0.0	0.0	0.0	0.0	0.0	54.3	114.5	241.7		NM	NM	NM	NM	NM	NM	111.1%	111.1%	NM
Total Late Stage Pipeline Drug Sales	0.0	0.0	0.0	0.0	0.0	23.1	125.3	268.4	482.9		NM	NM	NM	NM	NM	441.4%	114.2%	79.9%	NM
Early Stage Pipeline Drug Sales																			
DRM02	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		NM	NM	NM	NM	NM	NM	NM	NM	NM
DRM05	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		NM	NM	NM	NM	NM	NM	NM	NM	NM
Total Early Stage Pipeline Drug Sales	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		NM	NM	NM	NM	NM	NM	NM	NM	NM
Other Drug Sales	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		NM	NM	NM	NM	NM	NM	NM	NM	NM
Milestones	0.0	7.3	0.0	13.0	15.7	0.0	13.4	13.4	13.4		NM	-100.0%	NM	20.8%	-100.0%	NM	0.0%	0.0%	0.6%
TOTAL REVENUES	0.0	7.3	0.0	13.0	15.7	23.1	138.7	281.8	496.2		NM	-100.0%	NM	20.8%	47.4%	499.2%	103.2%	76.1%	107.2%

Source: Guggenheim Securities, LLC and Company Reports

Dermira - Cash Flow Analysis 2013-2021E

(\$ in Millions)									
(Year ended December 31)	2013	2014	2015E	2016E	2017E	2018E	2019E	2020E	2021E
Cash flows provided by Operating Activities:									
Net Income	(22.4)	(31.9)	(83.0)	(76.2)	(68.6)	(102.0)	(15.3)	62.3	173.1
Depreciation and Amortization	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other	0.3	1.9	-	-	-	-	-	-	-
Net Changes in Working Capital	9.9	(1.5)	1.7	(2.6)	(0.5)	(1.5)	(17.0)	(12.1)	(9.8)
Net cash provided by Operating Activities	(12.2)	(31.4)	(81.2)	(78.8)	(69.1)	(103.4)	(32.2)	50.3	163.3
Cash flows from Investing Activities									
Purchases of PP&E	(0.1)	(0.2)	(0.2)	(0.2)	(0.2)	(0.2)	(0.2)	(0.2)	(0.2)
Net proceeds from sale of assets	-	-	-	-	-	-	-	-	-
Acquisitions, net of cash acquired	-	-	-	-	-	-	-	-	-
Other	-	-	-	-	-	-	-	-	-
Net cash used in Investing Activities	(0.1)	(0.2)	(0.2)	(0.2)	(0.2)	(0.2)	(0.2)	(0.2)	(0.2)
Cash flows from Financing Activities									
(Repayment) or Issuance of long term debt	2.0	53.8	0.0	-	-	-	-	-	-
Cash dividends paid	-	-	-	-	-	-	-	-	-
Other	24.5	120.3	100.0	-	150.0	-	-	-	-
Net cash (used in) provided by Financing Activities	26.5	174.1	100.0	-	150.0	-	-	-	-
Net (decrease) increase in cash and equivalents	14.3	142.5	18.7	(78.9)	80.8	(103.6)	(32.4)	50.1	163.2
Cash and equivalents at beginning of year	7.9	22.1	164.7	183.3	104.4	185.2	81.6	49.2	99.4
Cash and equivalents at end of year	22.1	164.7	183.3	104.4	185.2	81.6	49.2	99.4	262.6

Source: Guggenheim Securities, LLC and Company Reports

Dermira - Balance Sheet Analysis 2013-2021E

(\$ in Millions)

(Year ended December 31)	2013	2014	2015E	2016E	2017E	2018E	2019E	2020E	2021E
Assets									
Cash and Cash Equivalent	22.1	164.7	183.3	104.4	185.2	81.6	49.2	99.4	262.6
Accounts Receivable, less allowance for doubtful accounts	-	7.3	-	2.6	3.1	4.6	24.3	44.0	69.9
Inventories	-	-	-	-	-	1.4	5.4	9.2	13.7
Other current assets	0.3	-	-	-	-	-	-	-	-
Total Current Assets	22.5	172.0	183.3	107.0	188.3	87.7	79.0	152.6	346.1
Plant, Property & Equipment	0.1	0.2	0.3	0.4	0.5	0.6	0.7	0.8	1.0
Identifiable intangibles	3.5	3.5	3.5	3.5	3.5	3.5	3.5	3.5	3.5
Goodwill	0.8	0.8	0.8	0.8	0.8	0.8	0.8	0.8	0.8
Other assets	0.0	1.8	1.8	1.8	1.8	1.8	1.8	1.8	1.8
Total Other Assets	4.4	6.2	6.3	6.5	6.6	6.7	6.8	6.9	7.0
TOTAL ASSETS	26.9	178.2	189.7	113.5	194.9	94.4	85.8	159.5	353.1
Liabilities & Shareholder's Equity									
Accounts Payable and Accrued Expenses	4.3	5.6	-	-	-	1.4	8.2	19.6	40.1
Other	0.2	6.3	6.3	6.3	6.3	6.3	6.3	6.3	6.3
Total Current Liabilities	4.5	11.9	6.3	6.3	6.3	7.8	14.5	25.9	46.4
Long term debt	1.8	1.9	1.9	1.9	1.9	1.9	1.9	1.9	1.9
Other liabilities	10.8	10.8	10.8	10.8	10.8	10.8	10.8	10.8	10.8
Total Liabilities	17.1	24.6	19.1	19.1	19.1	20.5	27.2	38.6	59.1
Shareholders Equity	9.8	153.6	170.6	94.4	175.8	73.8	58.6	120.9	294.0
Total Stockholder's Equity	9.8	153.6	170.6	94.4	175.8	73.8	58.6	120.9	294.0
Noncontrolling Interest	-	-	-	-	-	-	-	-	-
TOTAL LIABILITIES & STOCKHOLDERS' EQUITY	26.9	178.2	189.7	113.5	194.9	94.4	85.8	159.5	353.1

Source: Guggenheim Securities, LLC and Company Reports

ANALYST CERTIFICATION

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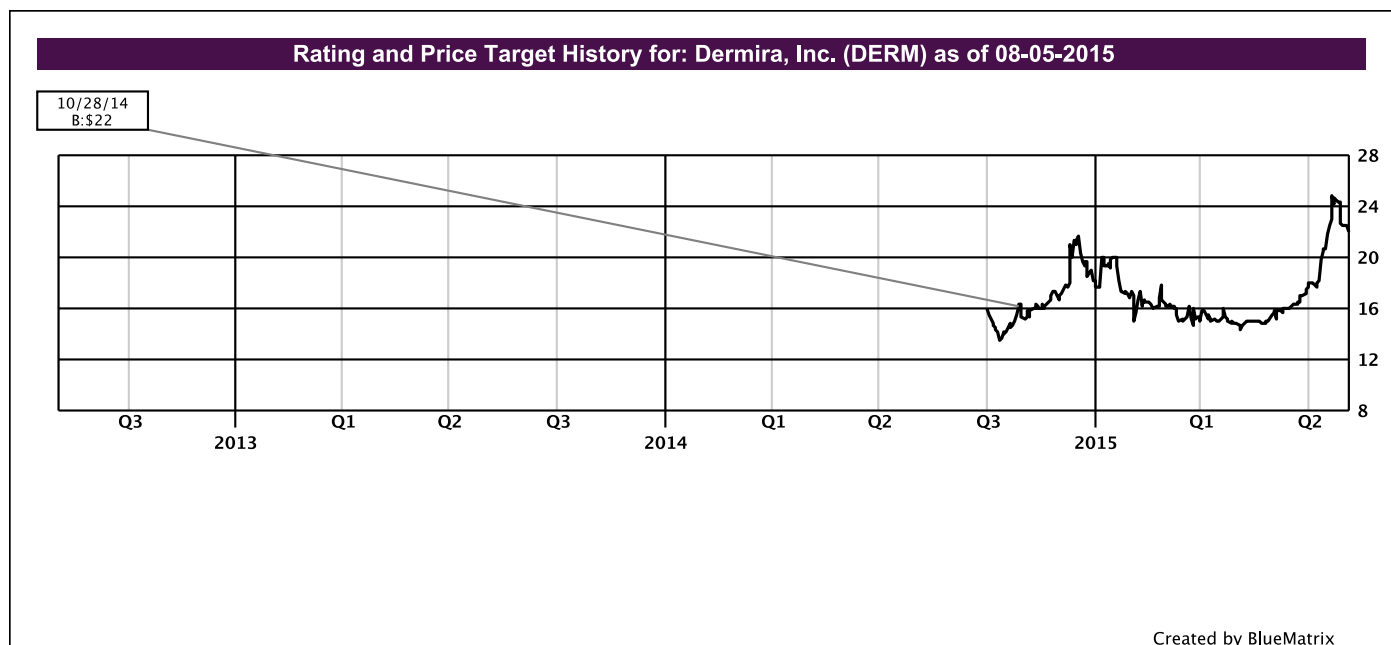
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SECTOR: SPECIALTY PHARMACEUTICALS

August 7, 2015

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			Count	Percent
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