



AEGIS CAPITAL CORP

Biotechnology
Jason Wittes
 (646) 502-2482
 jwittes@aegiscap.com
Evan Wang
 EWang@aegiscap.com

Company Update / Estimates Change

November 11, 2016

Key Metrics

HRTX - NASDAQ	\$18.45
Pricing Date	Nov 10 2016
Price Target	\$41.00
52-Week Range	\$31.32 - \$13.95
Shares Outstanding (mm)	37.5
Market Capitalization (mm)	\$691.9
Institutional Ownership	94%
Book Value/Share	\$2.30
Price/Book	8.0x

EPS FY: December

	2015A	Prior 2016E	Curr. 2016E	Prior 2017E	Curr. 2017E
1Q-Mar	(0.70)	--	(0.92)A	--	--
2Q-Jun	(0.74)	--	(1.17)A	--	--
3Q-Sep	(0.63)	(1.20)E	(1.24)A	--	--
4Q-Dec	(0.87)	(1.15)E	(1.18)E	--	--
FY	(2.95)	(4.44)E	(4.53)E	(4.08)E	(4.18)E
P/E	NM		NM		NM

REVENUE

	2015A	Prior 2016E	Curr. 2016E	Prior 2017E	Curr. 2017E
1Q-Mar	0.0	--	0.0A	--	--
2Q-Jun	0.0	--	0.0A	--	--
3Q-Sep	0.0	--	0.0A	--	--
4Q-Dec	0.0	--	3.8E	--	--
FY	0.0	--	3.8E	--	50.1E

Company Description:

Heron is a biopharmaceutical company developing novel, patient-focused solutions that apply innovative science and technologies to already-approved pharmacological agents. This is the company's proprietary Biochronomer® drug delivery technology, which can deliver therapeutic levels of a wide range of otherwise short-acting pharmacological agents over a period of days to weeks with a single dose.

Heron Therapeutics

Rating: Buy

3Q16: Model Update

Investment Highlights:

We have updated our model to reflect 3Q16 results: HRTX reported an EPS of -\$1.24, higher than consensus of -\$1.17. Heron ended the quarter with \$88.9 million in cash, with cash used for operating activities this quarter of \$36.1 million driven by preparation for the launch of Sustol – we believe Heron has the cash to fund operations into 2018. R&D expense for the quarter increased to \$30.2 million from \$27.3 million the prior quarter, and SG&A expense increased to \$17.5 million from \$15.8 million. We reiterate our Buy rating and \$41 PT.

The company launched sales of Sustol in October, the first and only approved 5-HT3 receptor antagonist with an extended-release effect and 5 days of Chemotherapy Induced Vomiting (CINV) prevention for MEC and HEC regimens. 4Q16 will represent the first quarter of Sustol sales, though we expect a modest start given the reimbursement situation – Sustol will launch with a miscellaneous J code and will not get its own specific code until January, creating a quarter of reimbursement delay, though HRTX will offer extended payment terms as compensation (see initiation for more detail). Sustol has two key advantages the current market leader, Aloxi: 1) a true extended 5-day release versus Aloxi, which drops off after 3-4 days, which is too soon for most MEC and HEC regimens; 2) a higher profitability potential for oncologists. We think Sustol represents at least a \$300 million opportunity over the next five years.

Valuation: Our \$41 price target is based on a DCF analysis, using a 10% discount rate applied to all cash flows and the terminal value, which is based on a 6 multiple of our projected 2020 EBITDA. This includes a contribution from HTX-011, in 2019, which we see as the most significant opportunity.

Heron Therapeutics, Inc.**Income Statement**

Fiscal Year ends December

(in 000, except per share items)

	2014A	2015A	1Q16A	2Q16A	3Q16A	4Q16E	2016E	2017E	2018E	2019E
Sustol revenue		-	-	-	0	3,829	3,829	50,067	81,126	140,729
HTX-019 revenue								0	20,696	37,252
HTX-011B revenue		-	-	-	-	-	-	-	-	109,143
Contract revenue		-								
Total revenues	-	-	-	-	-	3,829	3,829	50,067	101,822	287,124
COGS	-	-		-	-	766	766	10,013	16,225	25,331
R&D	55,124	61,183	16,092	27,286	30,242	31,754	105,374	121,180	122,392	110,153
G&A	19,437	35,742	17,220	15,780	17,492	17,842	68,334	82,001	90,201	97,417
Total Operating Expenses	74,561	96,925	33,312	43,066	47,734	50,362	174,474	213,194	228,818	232,901
Operating Income	(74,561)	(96,925)	(33,312)	(43,066)	(47,734)	(46,533)	(170,645)	(163,128)	(126,996)	54,223
Gain on sale of royalty interest										
Other income (loss), net										
Interest income (expense), net	(1,806)	(666)	(133)	(160)	(775)	(180)	(1,248)	(500)	(500)	(500)
Pretax income	(76,367)	(97,591)	(33,445)	(43,226)	(48,509)	(46,713)	(171,893)	(163,628)	(127,496)	53,723
Provision for income tax (benefit)	-	-					-	-	-	2,686
Gain (loss) from discontinued operations										
Net Income	(76,367)	(97,591)	(33,445)	(43,226)	(48,509)	(46,713)	(171,893)	(163,628)	(127,496)	51,037
EPS	(2.87)	(2.95)	(0.92)	(1.17)	(1.24)	(1.18)	(4.53)	(4.18)	(3.16)	1.23
EPS diluted, GAAP	(2.87)	(2.95)	(0.92)	(1.17)	(1.24)	(1.18)	(4.53)	(4.18)	(2.35)	0.92
Basic shares outstanding	26,569	33,056	36,229	37,048	39,113	39,504	37,974	39,113	40,286	41,495
Diluted shares outstanding	26,569	33,056	36,229	37,048	39,113	39,504	37,974	39,113	54,286	55,495

Source: Company reports, Aegis Capital Corp. estimates

Required Disclosures

Price Target

41

Valuation Methodology

Our \$41 price target is based on a DCF analysis, using a 10% discount rate applied to all cash flows and the terminal value, which is based on a 6 multiple of our projected 2020 EBITDA. This represents a speculative investment only for those willing to take on risk.

Risk Factors

Risks to the achievement of our target price include clinical, regulatory, financing, competitive risks, as well as stock price volatility.

For important disclosures go to www.aegiscap.com.

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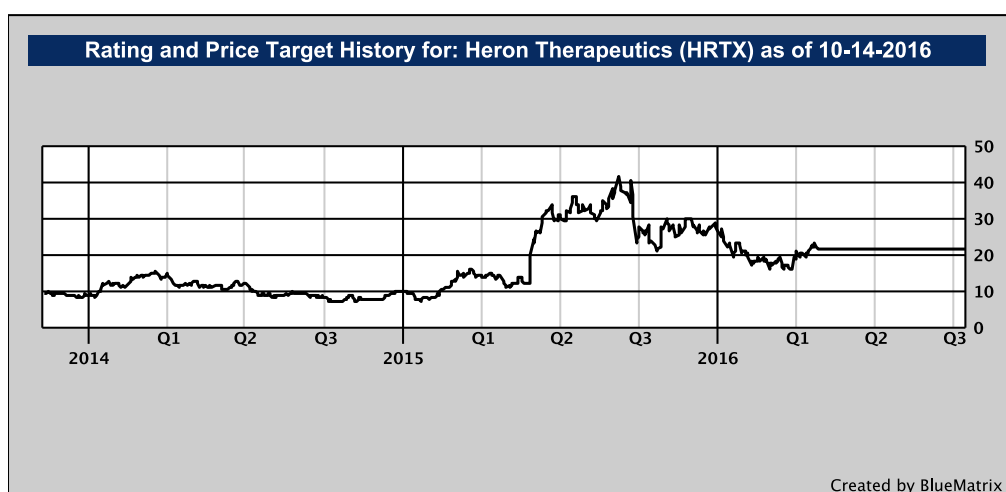
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Rating	Investment Banking Services/Past 12 Mos.	
	Percent	Percent
BUY [BUY]	87.64	42.31
HOLD [HOLD]	12.36	36.36
SELL [SELL]	0.00	0.00

Meaning of Ratings

- A) A Buy rating is assigned when we do not believe the stock price adequately reflects a company's prospects over 12-18 months.
- B) A Hold rating is assigned when we believe the stock price adequately reflects a company's prospects over 12-18 months.
- C) A Sell rating is assigned when we believe the stock price more than adequately reflects a company's prospects over 12-18 months.

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Aegis Capital Corp.
(212) 813-1010
810 Seventh Avenue, 18th Floor
New York, New York 10019