

Cipher Pharmaceuticals Inc. (CPHR-NASDAQ)

CPHR: Revenue continued to grow in fiscal third quarter of 2015-----Buy

UPDATE

The Cipher story continues to become more interesting as the management executes on its plan to become a leading dermatology-focused specialty pharmaceutical company. Since the onset of 2015, Cipher has completed six transactions.

The company reported another strong quarter financial results for 3Q15 despite all the M&A activity, showing that management can execute on both the existing operations and business development.

We continue to rate Cipher shares a Buy rating.

Current Recommendation	Buy
Prior Recommendation	N/A
Date of Last Change	01/18/2015
Current Price (11/03/15)	\$4.39
Target Price	\$17.00

SUMMARY DATA

52-Week High	\$16.33
52-Week Low	\$3.61
One-Year Return (%)	N/A
Beta	N/A
Average Daily Volume (sh)	6,639

Shares Outstanding (mil)	26
Market Capitalization (\$mil)	\$114
Short Interest Ratio (days)	9.00
Institutional Ownership (%)	28
Insider Ownership (%)	6

Annual Cash Dividend	\$0.00
Dividend Yield (%)	0.00

5-Yr. Historical Growth Rates	
Sales (%)	N/A
Earnings Per Share (%)	N/A
Dividend (%)	N/A

P/E using TTM EPS	N/A
P/E using 2015 Estimate	20.8
P/E using 2016 Estimate	10.6

Risk Level	High,
Type of Stock	Small-Growth
Industry	Med-Drugs

ZACKS ESTIMATES

Revenue

(in millions of \$)

	Q1	Q2	Q3	Q4	Year
	(Mar)	(Jun)	(Sep)	(Dec)	(Dec)
2014	7.1 A	8.0 A	6.6 A	7.5 A	29.2 A
2015	9.2 A	8.8 A	8.5 A	11.0 E	35.7 E
2016					55.0 E
2017					110.3 E

Earnings per Share

(EPS is operating earnings before non recurring items)

	Q1	Q2	Q3	Q4	Year
	(Mar)	(Jun)	(Sep)	(Dec)	(Dec)
2014	\$0.14 A	\$0.16 A	\$0.31 A	\$0.13 A	\$0.74 A
2015	\$0.10 A	-\$0.01 A	-\$0.09 A	\$0.01 E	\$0.02 E
2016					\$0.33 E
2017					\$1.20 E

WHAT'S NEW

Total Revenue Grew 28% in Third Quarter of 2015

On Nov 4, 2015, Cipher Pharmaceuticals (CPHR) reported strong financial results for the fiscal second quarter of 2015 ended September 30, 2015.

Total revenue for the third quarter of 2015 was \$8.5 million, compared to \$6.6 million for the same period last year, **an increase of 28%**.

Revenue growth in third quarter of 2015 was mainly driven by strong growth in product sales, which was up 367% compared to that for third quarter of 2014. Licensing revenue grew slightly by 2% in the fiscal third quarter of 2015.

For the three months ended Sept 30, 2015 (\$'000)

	2015	2014	\$ change in 2015	% change in 2015
Licensing revenue	6,263	6,152	111	2
Product revenue	2,197	470	1,727	367
Total revenue	8,460	6,622	1,838	28

Product Revenue

Product revenue growth was primarily a result of the acquisition of **Innocutis** completed in April 2015, which added 7 commercial products marketed in the US. Innocutis products contributed \$1.6 million, composed primarily of Nuvail[®] at \$0.4 million, Bionect[®] at \$0.4 million, Sitavig[®] at \$0.3 million, Umecta at \$0.3 million and Inova at \$0.1 million. After excluding certain one-time product return reserves recorded in 3Q15, product revenue from U.S. operations would have been \$ 2.1 million with Sitavig at \$0.7 million and Nuvail at \$ 0.5 million.

Canadian product revenue from Epuris and Vaniqa sales in 3Q15 increased by 63% compared to 3Q14, with Vaniqa contributing 20% of that growth amount. Epuris was launched in June 2013 and until Q2 2015 was the only product marketed by Cipher's Canadian sales and marketing organization. In May 2015, a new product, Vaniqa was added to the Canadian portfolio.

Licensing/royalty Revenue

Total licensing revenue in 3Q15 increased 2% to \$6.3 million from \$6.2 million in 3Q14.

Revenue for Absorica was \$4.8 million in Q3 2015, compared to \$4.4 million in Q3 2014, an increase of 9%. Market share continues to hold in the 19% to 20% range consistent with the last three quarters, compared to 20.3% in Q3 2014 according to IMS Health. Overall growth for the U.S. isotretinoin market in TRxs was 10.7% compared to Q3 2014 and up 8.7% for the nine month period ended September 30, 2015.

On Oct. 5, 2015, **Cipher** announced that the Company, along with its US distribution partner, **Ranbaxy**, a Sun Pharma Company, and its in-licensing partner, **Galephar** Pharmaceutical Research, Inc., have entered into a Settlement Agreement with **Actavis** that dismisses the patent litigation suit relating to Actavis' Abbreviated New Drug Application (ANDA) for a generic version of Absorica[®] (isotretinoin capsules).

As part of the Settlement Agreement, CIPHER, Ranbaxy and Galephar have entered into a **non-exclusive** license agreement with Actavis under which Actavis may begin selling its generic version of Absorica® in the U.S. on December 27, 2020 (approximately nine months prior to the expiration of the patents in September 2021) or earlier under certain circumstances.

The Settlement Agreement is subject to review by the U.S. Federal Trade Commission and the U.S. Department of Justice.

We continue to believe Absorica will perform well and will be the largest licensing revenue contributor in the coming quarters providing strong positive cash flow to CIPHER that is allowing management to branch-out and fund all the recent acquisitions, as well as take on debt at favorable terms. Sunpharma, CIPHER's US partner, has made it clear that dermatology is a core focus for the new Sun-Ranbaxy combined company, and Absorica is the flagship brand. Sales of Absorica in 2014 were around \$240 million. We believe peak sales are around \$400 million, still leaving good room for growth in royalties to CIPHER.

Revenue for Lipofen was \$1.1 million in 3Q15, compared to \$1.0 million in 3Q14, an increase of 10%. The product continues to perform well in 2015 despite the fact the company's partner, Kowa, has decreased their commercial efforts.

Revenue from the Company's extended-release tramadol product (ConZip in the U.S. and Durela in Canada) was \$0.4 million in 3Q15, compared to \$0.7 million in 3Q14, a decrease of 43%. The reason for the sharp decline was due to an authorized generic version of the product which was launched in the U.S. market in July 2015 by CIPHER through its partner Vertical.

Licensing/Royalty (\$mm)			
	3Q15	3Q14	Change
Absorica	\$4.8	\$4.4	9.1%
Lipofen	\$1.1	\$1.0	10.0%
ConZip/Durela	\$0.4	\$0.7	-42.9%
Total	\$6.3	\$6.2	1.8%

R&D expense in 3Q15 was \$0.5 million, compared to \$0.2 million in 3Q14. R&D expenses relate to the company's drug development activities.

SG&A expenses in 3Q15 were \$7.9 million, compared to \$1.9 million in 3Q14. The increase of SG&A expenses in 3Q15 was primarily driven by the Innocutis acquisition.

GAAP net loss was \$2.2 million (\$0.09 per share) for 3Q15, compared to GAAP income of \$7.9 million (\$0.31 per share). Non-GAAP net loss for 3Q15 was \$2.2 million (\$0.09 per share), compared to non-GAAP net income of \$4.3 million (\$0.17 per share) for 3Q14.

CIPHER reported adjusted EBITDA of \$15,000 in 3Q15, compared to adjusted EBITDA of \$4.8 million in 3Q14. Adjusted EBITDA was impacted by two significant items during 3Q15. A foreign exchange loss on the conversion of Canadian denominated cash and cash equivalents of \$2.1 million and the impact of one time product return provisions recorded in 2Q15 of \$0.5 million. Excluding the impact of these two items would have resulted in an improvement in Adjusted EBITDA of approximately \$2.6 million for the three month period ended September 30, 2015.

	2015	2014	\$ change in 2015	% change in 2015
ADJUSTED EBITDA	15	4,777	(4,762)	(100)

Balance Sheet Remains Strong

As of September 30, 2015, Cipher held \$28.1 million in cash and cash equivalents. During the nine month period ended September 30, 2015 the Company generated net cash from operating activities of \$8.4 million and utilized cash of \$7.4 million to acquire new products as well as \$9.0 million for the purchase of Innocutis.

In April, 2015, Cipher closed on a private offering of \$100 million in aggregate principal amount of Senior Secured Notes due 2020, provided by investment funds managed by Athyrium Capital Management. Cipher received an initial drawdown of \$40 million, which was used to fund the majority of the upfront purchase of INNOCUTIS. The remaining balance of the Senior Secured Notes will be made available to finance future acquisitions and is subject to certain conditions. The five year fixed rate 10.25% Notes are payable on the last day of each quarter. The Notes are interest-only and are secured by assets of Cipher and its subsidiaries, subject to certain exceptions.

Very Attractive Valuation

We continue to rate Cipher shares a Buy and reiterate our price target of \$17 per share.

Our model is consistent with management's guidance that the INNOCUTIS deal will become accretive in two years. We model product revenue will reach \$10 million in 2015, and grow to \$125 million in 2018, an impressive compound annual growth rate (CAGR) of 133%, driven by both existing products and new approvals.

With respect to the valuation, we believe Cipher shares are undervalued at current market price. Currently, Cipher shares are traded at about \$5.00 per share, which values the company at about \$132 million in terms of market cap. This is deeply discounted compared to its peers. We believe Cipher shares are fair-valued at \$17 per share. The specialty pharmaceutical industry trades at an average P/E ratio of 15x. According to our financial model, Cipher's EPS will grow from \$0.02 in 2015 to \$1.95 in 2018. Applying the 15 x P/E multiple and the \$1.95 EPS in 2018, discounted at 20% for three years, we come up with the fair value of \$17 per share.

If management continues to capitalize on selective acquisitions, continues to develop their deep and growing pipeline of dermatology products, we believe the shares continue to offer significant upside potential. With the recent acquisitions, we believe Cipher is on its way to building a leading pure play dermatology based specialty pharmaceutical company with a focus on growing its North American presence. And what is even more impressive is that execution remains excellent. As such, we continue to have faith in management's vision, growth strategies and strategic priorities, and expect another solid performance for 4Q15 and beyond.

Finally, we see the end-game for Cipher shareholders as an acquisition by a larger U.S. pharmaceutical player.

Acquisition, an Integral Part of Growth Strategy

Cipher achieves sustainable growth by both organic growth and acquisition. Management is committed to make Cipher to become a leading dermatology-focused specialty pharmaceutical company. Since the onset of 2015, Cipher has completed the following six transactions:

- Cipher began the year with the acquisition of the [Canadian licensing rights to Ozenoxacin](#), a topical antibiotic for the treatment of adult and pediatric impetigo, from privately-held Ferrer of Spain. Second Phase 3 trial was completed in July 2015. We expect Cipher to file NDA in Canada in 1Q16.
- Later in January 2015, Cipher completed the [acquisition of Melanovus Oncology Inc.](#), with access to seven pre-clinical assets for melanoma and other cancers for only \$0.5 million.
- In February 2015, Cipher completed the [acquisition of Astion Pharma](#), which provided two late-stage inflammatory products and a mid-stage candidate for lupus.
- In March 2015, Cipher licensed the [Canadian rights to Can-Fite's CF101](#) for moderate to severe plaque psoriasis.
- On April 13, 2015, Cipher completed the [acquisition of INNOCUTIS](#) with seven marketed dermatology products including a potential breakthrough treatment for herpes labialis (cold sores).
- Finally, on May 6, 2015, Cipher acquired the Canadian rights to [Vaniga and Actikerall](#) from Spanish pharmaceutical company, Almirall S.A.

We will discuss the Innocutis acquisition in more detail. We believe this is the most important one which establishes the company's US presence, the largest healthcare market in the world.

Acquisition of INNOCUTIS

On April 13, 2015, Cipher announced it had [acquired INNOCUTIS Holdings LLC](#), a privately held specialty dermatology company, for US \$45.5 million in cash. With the acquisition, Cipher enters the U.S. dermatology market, specifically with infrastructure to launch products with the current 31 full-time sales representatives covering approximately 3,500 dermatologists across 28 states in the U.S. The products consist of established revenue-generating branded prescriptions that provide physicians with alternate solutions for the management of challenges experienced in daily dermatological practice. INNOCUTIS has seven marketed products and we highlight several of these products below.

- [Sitavig®](#) (acyclovir) 50 mg employs the proprietary Lauriad® Muco-Adhesive Buccal technology where a single dose tablet is placed in the gum, delivering a high concentration of acyclovir directly to the site of the cold sore infection. INNOCUTIS claims this is the only treatment proven to reduce the occurrence of future outbreaks of herpes labialis (cold sores) and represents a breakthrough for the treatment of herpes, which is composed of over 20 million prescriptions and approximately \$4 billion in annual sales in the U.S. alone. In a recent study, over 1/3 of patients were cold sore free after 10 months of treatment with Sitavig® ([Bieber et al., 2014](#)).

The product was launched in the U.S. during the third quarter of 2014, and we expect that Cipher will file **for Canadian approval at some point in 2016**. We also think there may be an opportunity down the road for Cipher to sell (partner or sublicense) Sitavig® to other specialty markets including primary care, geriatric medicine and women's health, as studies have shown that a greater percentage of women suffer from herpes labialis than men, with increased susceptibility in the elderly population. Sitavig® currently has three active patents with expiration dates in 2027 and 2030.

Cold sores or fever blisters are small, contagious blisters that can appear on the face, lips and inside of the mouth and are caused by the herpes simplex virus, commonly referred to as HSV-1 or HSV-2 (*below*). Cold sores are contagious during an outbreak but also during a process known as "viral shedding" which can occur even when no blister is physically present. The virus is most commonly spread through kissing or sharing food and/or drink with an infected person. The blisters can itch and burn, and can be extremely painful when they break open.

Herpes labialis is a widespread condition and according to the [World Health Organization \(WHO\)](#), an estimated 400 million people worldwide are currently infected with HSV-2. By the age of 50, [up to 80% of Americans](#) will have been exposed to HSV with approximately 25-35% of adults suffering from recurrent cold sores. With approximately 100 million cold sore outbreaks occurring in the U.S. alone, this

represents a significant market potential of hundreds of millions of dollars. It is [speculated](#) that by 2017, the herpes simplex treatment market could reach \$4.8 billion. We believe that this represents a great market opportunity for Cipher's newly acquired Sitavig® as it could change the treatment care for cold sores. We think that the drug will gain more popularity with prescribers as Cipher expands on its potential and we look forward to seeing how Cipher does with this drug in North America pending Canadian approval. Sales of Sitavig in the U.S., launched only in the middle of 2014, totaled \$2.1 million. Based on our analysis of the data and the market opportunity, we believe Sitavig as peak U.S. sales of \$200 million, with another \$10-15 million potential in Canada.

- [Nuvail™](#) (poly-urethane 16%) nail solution is a patented biocompatible polymer that is FDA approved for managing the signs and symptoms of nail dystrophy, such as nail splitting and nail fragility. The product helps prevent nail brittleness and dries quickly, with an invisible matte finish and can be used in both men and women. Nuvail™ improves overall nail appearance by penetrating the intracellular spaces and nail surface ridges, creating a stable, yet flexible molecular structure and providing mechanical support (*below*). It does not wash off because it is comprised of hydrophobic (non-water soluble) molecules and continues to work following first application with continual protection of nails to environmental factors. We believe that the ease of application will appeal to both men and women who suffer from nail dystrophy.

U.S. Nuvail sales in 2014 totaled \$3.5 million. We see peak U.S. sales in the \$25-30 million range, with another \$2-3 million potential in Canada.

- [Bionect®](#) (hyaluronic acid sodium salt, 0.2%) is a non-sensitizing, water based, non-steroidal, topical low molecular weight hyaluronic acid (LMW-HA) formulation that can be used for the dressing and management of partial to full thickness dermal ulcers (pressure sores, venous stasis ulcers, arterial ulcers, diabetic ulcers), wounds including cuts, abrasions, donor sites, and post-operative incisions, irritations of the skin, and first and second degree burns. LMW-HA, which is found in Bionect® is a substance that is naturally found in the skin and other parts of the body and attracts and holds up to 1,000 times its weight in water. This key feature allows for the transport of oxygen, protein and nutrients through the skin and also helps to maintain an intact dermal matrix structure (*below*). According to studies, LMW-HA also plays a crucial role in the processes of tissue repair and inflammation ([Weindl et al., 2004](#)).

Bionect® is available in cream, gel and aqueous-based spray formulations and also promotes skin healing and is intended to cover a wound or burn and in turn, protects against abrasion, friction and desiccation. U.S. sales of Bionect in 2014 totaled only \$2.1 million. We believe peak U.S. sales are around \$5 million.

- [Inova®](#) 4% & 8% and [Inova® ACT](#) 4/1 & 8/2 include benzoyl peroxide preparations for mild to moderate symptoms associated with acne vulgaris. Although the exact mechanism of action of benzoyl peroxide is not known, it is an oxidizing agent that has antibacterial properties against Propionibacterium acnes and patients that have been treated with benzoyl peroxide show a reduction in free fatty acids, lipids and mild desquamation (drying and peeling activity) with concurrent reduction in comedones and acne lesions. Inova® 4% & 8% have either 4% or 8% benzoyl peroxide while Inova® Acne Control Therapy (ACT) 4/1 & 8/2 incorporates benzoyl peroxide 4% and salicylic acid 1% and benzoyl peroxide 8% and salicylic acid 2%, respectively. Both are individually wrapped pads and employ the Easy Pad® Delivery System. These pads also have Tocopherol 5% Topical Antioxidant, which is a pure formulation from natural sources, and include sunflower oil as well as a silicone delivery vehicle.

We believe these products will be popular with the adolescent and teenage populations due to their convenience and ease of application and use. We believe Cipher can plug both Inova® products (as well as Dermadexin) into the company's existing product portfolio in Canada with Epuris for acne and eventually Ozenoxacin for impetigo. Inova U.S. sales in 2014 were \$1.5 million. We believe peak sales are roughly \$3-4 million.

- [CNL8™](#) (ciclopirox topical solution, 8%) nail kit provides up to six months of nail therapy and includes 15ml (3-5ml bottles) of ciclopirox 8%, 25 SwabPlus® nail lacquer remover swabs, and 1 emery board for treatment of mild to moderate onychomycosis (nail fungus) due to *Trichophyton rubrum*. The management program also includes removal of the unattached, infected nails by a physician as frequent as once a month. Ciclopirox is a synthetic antifungal and [one in vitro study](#) suggests that it works via chelation of polyvalent cations (Fe+3 or Al+3) resulting in the inhibition of the metal-dependent enzymes that are responsible for the degradation of peroxides within the fungal cell.

INNOCUTIS recorded approximately \$9.6 million in net product revenue for all of 2014, driven largely by Nuvail at \$3.5 million, Sitavig at \$2.1 million, and Bionect at \$2.1 million. We see Sitavig as having the largest upside potential, with peak North American sales approaching \$250 million. We also believe that Nuvail has peak North American sales at around \$30 million. Cipher expects that within two years, the INNOCUTIS acquisition to be accretive to earnings per share. The acquisition of INNOCUTIS will bring in 31 sales representatives to Cipher to target some 3,500 U.S. dermatologists and high-prescribing primary-care physicians for things like psoriasis, pruritis, and cold sores. We expect that Cipher will expand to approximately 60 representatives, similar to the size of the sales force that Sunpharma is using to promote Absorica, in the U.S. in 2016. This should allow the company to double its target prescriber base.

The agreement consists of \$45.5 million in cash to be paid by Cipher on closing of the deal and additional INNOCUTIS management incentive payments of up to \$3.0 million in cash over a three-year period based on the achievement of certain financial milestones. So all-in-all, at a price-to-trialing-twelve-month sales ratio of less than 5x seems very reasonable to us, especially considering we believe Cipher can get Sitavig and Nuvail to over \$250 million sales at peak.

Acquisitions Fit Nicely In With Existing Derm Products

All of the deal-making at Cipher over the past several months has been orchestrated to build a premier independent special pharmaceutical company with a laser-focus on the North American **dermatology market**. As a reminder, Cipher has two existing dermatology products, an improved formulation of isotretinoin, sold in the U.S. as Absorica® by Ranbaxy US and Epuris® in Canada by Cipher, and Beteflam Patch, currently under regulatory review by Health Canada.

- *Beteflam Patch*

On February 12, 2015, Cipher announced that Health Canada has [accepted for review](#) the new drug submission (NDS) for Beteflam Patch (previously referred to as Betesil Patch). The actual application was filed on December 15, 2014. As a reminder, [Cipher licensed](#) the Canadian rights to the Beteflam Patch in 2012 from Swiss-based Institut Biochimique SA ("IBSA"). IBSA owns the U.S. rights to the product. Acceptance for review by Health Canada resulted in a CDN\$150,000 milestone payment from Cipher to IBSA.

Beteflam Patch is a novel, patent-protected, self-adhesive medicated plaster containing 0.1% betamethasone valerate, for the treatment of inflammatory skin conditions such as chronic plaque psoriasis (CPP). The efficacy and safety of the product has been established in two successful Phase 3 trials and one successful Phase 4 trial conducted by IBSA. IBSA recently published positive results from a large non-inferiority study, which compared the product to Dovobet (betamethasone plus calcipotriol), a commonly prescribed combination product containing a corticosteroid and a vitamin D analogue.

The Beteflam Patch is applied once-daily to the affected region and may be cut to fit the particular size and shape of the psoriatic lesion thereby reducing potential contact of the steroid with healthy areas of skin. The occlusive format of the Beteflam Patch is designed to provide a consistent distribution, delivery and absorption of the active ingredient and enhances the potency of the corticosteroid. The patch also helps to moisturize the skin, which accelerates healing and provides a protective barrier that reduces

local trauma to the lesion due to scratching and prevents transfer of fluids from the lesion onto clothing. Beteflam patch will be the first topical betamethasone patch on the market in Canada once approved.

If approved in late 2015, we think the Beteflam Patch is an excellent complement dermatology product for Cipher's contract sales force to co-promote along with Epuris and newly acquired products like Dermadexin and Pruridexin, or even CF101. We expect a decision from Health Canada in the fourth quarter 2015.

We think Cipher can achieve breakeven Canadian operations based on the launch of Epuris alone by the end of 2015. This would be sales in the area of \$3 million. Adding several more dermatology products to the portfolio, like Beteflam Patch, Dermadexin, Pruridexin, Sitavig, and CF101 will help improve the overall efficiency and profitability of Cipher's Canadian operations. We think the Canadian operations can generate sales in the \$50 million range in time. The prescriber overlap for these newly acquired products and Epuris looks fantastic, likely over 70%.

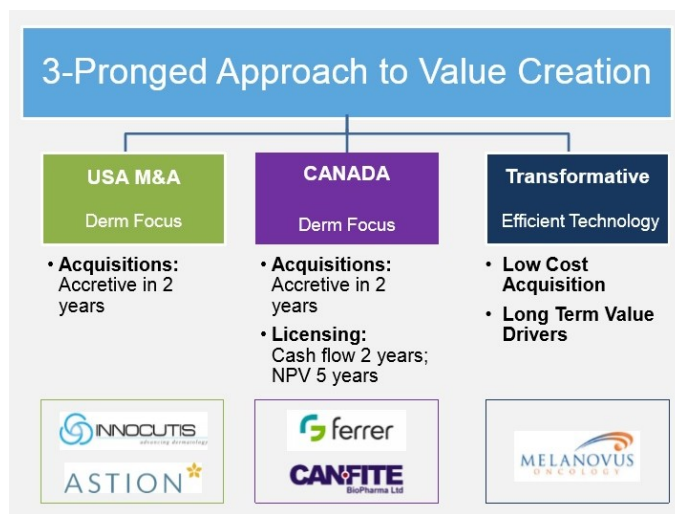
Executing on its Growth Strategy

As a summary, Cipher has completed five transactions since the start of 2015 that execute on its 3-point growth strategy:

- I. *Acquire dermatology companies and/or products in the U.S. and establish commercial infrastructure*
 - ✓ Acquired INNOCUTIS, establishing Cipher's commercial presence in the U.S. dermatology market.
 - ✓ Acquired worldwide rights to three products focused on inflammatory dermatological diseases (Dermadexin, Pruridexin, and ASF-1096) from Astion Pharma. Cipher's commercialization efforts will focus on the U.S. initially.

- II. *Expand Canadian dermatology franchise*
 - ✓ Licensed the Canadian rights to Ozenoxacin, a topical treatment for adult and pediatric impetigo.
 - ✓ Announced that Beteflam Patch has been accepted for review by Health Canada.
 - ✓ Licensed the Canadian distribution rights to CF-101, a novel chemical entity being developed by Can-Fite Biopharma for moderate to severe plaque psoriasis and rheumatoid arthritis.
 - ✓ Acquired Canadian rights to Vaniqa and Actikerall, two approved dermatology products each with \$1 to \$2 million sales potential.

- III. *Acquire potentially transformative technology that can be commercialized efficiently*
 - ✓ Acquired seven pre-clinical compounds for the treatment of melanoma, skin cancer and other cancers from Melanovus Oncology Inc.



Source: Cipher Pharmaceuticals Inc.

Conclusion

Cipher has kept itself extremely busy over the past 10 months, expanding its pipeline through several key advancements, including six acquisitions and licensing deals all designed to turn Cipher into a fully-integrated dermatology-focused specialty pharmaceutical company by 2020. Cipher's newly expanded product portfolio includes products focused on acne, psoriasis, dermatitis, pruritis, lupus, impetigo, melanoma, hyperkeratotic actinic keratosis, ulcers, nail dystrophy, herpes, onychomycosis, hyperpigmentation, un-wanted facial hair, and rheumatoid arthritis. Through these acquisitions, Cipher is on its way to building an integrated North American sales force comprised of 31 U.S. (serving over 3,500 dermatologists in 28 states in the U.S alone) and 7 Canadian sales reps. We expect that both numbers are going higher in the next several quarters.

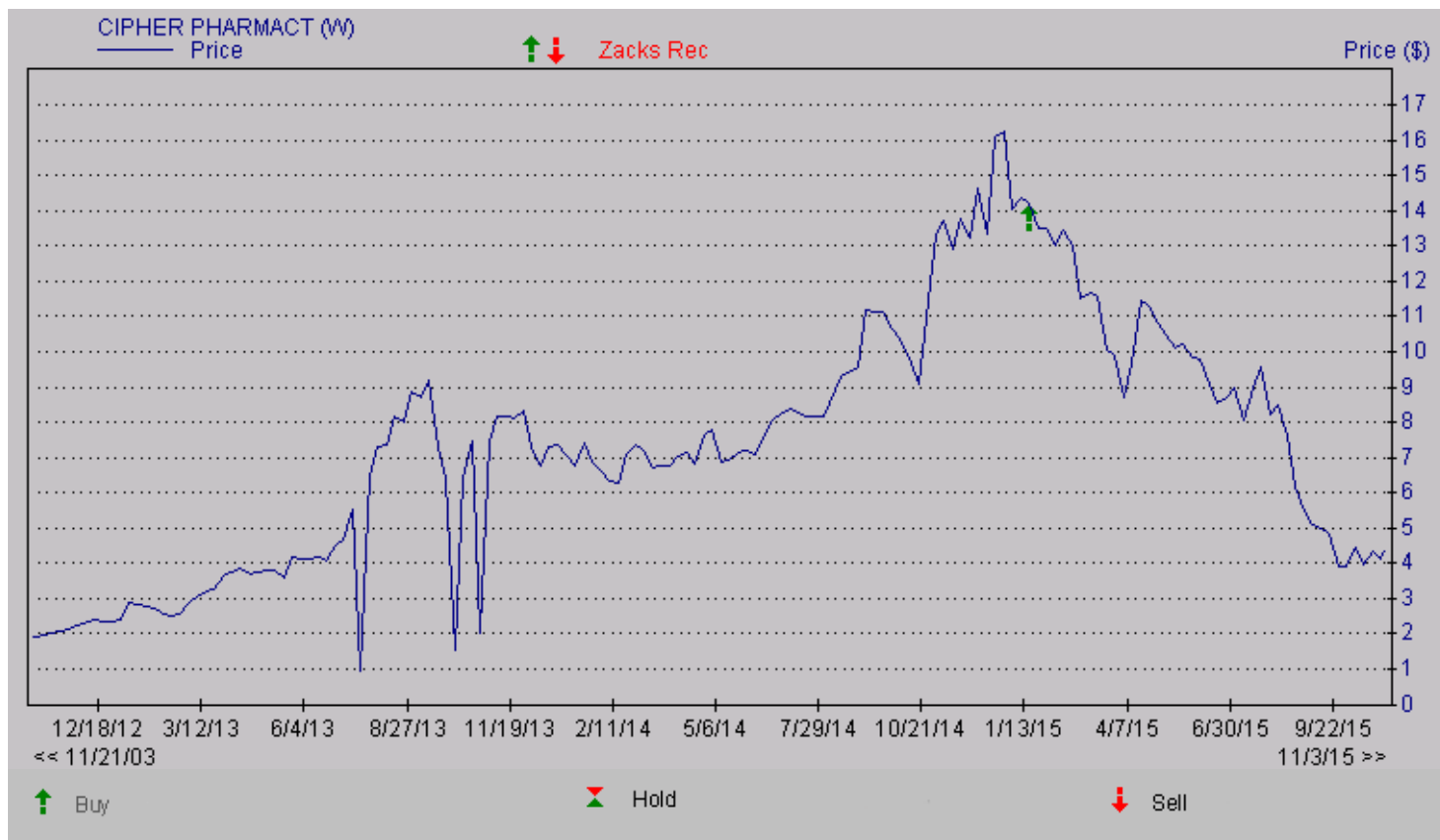
We believe the opportunity to leverage the existing sales force to cover multiple products. If approved later this year, we believe that the Beteflam Patch will be an excellent complement dermatology product for Cipher's contract sales force to co-promote with Epuris, Dermadexin, Pruridexin, and potentially CF101. Similarly, we also see considerable overlap between the acne products, Inova and Epuris, with Dermadexin and possibly Ozenoxacin. We believe that Cipher's new combined sales force and combined customer base, will offer considerable cross selling opportunities as they continue to expand their offerings in dermatology in the U.S. and Canada and will keep profit margins well above industry average.

INCOME STATEMENT

CPHR (\$mm)	2013 A	2014 A	Q1 A	Q2 A	Q3 A	Q4 E	2015 E	2016 E	2017 E	2018 E
Royalties & Licensing	\$25.6	\$27.4	\$6.7	\$6.3	\$6.3	\$6.5	\$25.8	\$30.0	\$35.3	\$40.0
YOY Growth	-	6.9%	-1.3%	-16.4%	1.8%	-4.7%	-5.6%	344.8%	458.7%	538.7%
Product Sales	\$0.4	\$1.9	\$0.7	\$2.5	\$2.2	\$4.5	\$9.9	\$25.0	\$75.0	\$125.0
YOY Growth	-	369.3%	112.7%	450.8%	367.4%	610.9%	428.3%	153.3%	200.0%	66.7%
Total Revenues	\$26.0	\$29.2	\$7.4	\$8.8	\$8.5	\$11.0	\$35.7	\$55.0	\$110.3	\$165.0
YOY Growth	-	12.4%	3.6%	10.3%	27.8%	47.6%	22.1%	54.1%	100.5%	49.6%
Cost of Goods Sold	\$0.1	\$0.5	\$0.2	\$0.9	\$0.8	\$1.6	\$3.5	\$8.8	\$26.3	\$43.8
Gross Profit	\$25.9	\$28.7	\$7.2	\$7.9	\$7.6	\$9.4	\$32.2	\$46.3	\$84.1	\$121.3
Product Gross Margin	65.8%	72.7%	71.3%	62.9%	61.4%	65.0%	65.0%	65.0%	65.0%	65.0%
Selling, Marketing, General & Admin	\$6.0	\$9.0	\$3.3	\$5.9	\$7.9	\$8.0	\$25.1	\$28.0	\$32.0	\$35.0
Research & Development	\$1.3	\$1.1	\$0.4	\$0.5	\$0.5	\$0.6	\$2.0	\$3.0	\$4.5	\$5.5
Amortization Expense	\$1.1	\$0.7	\$0.1	\$1.2	\$1.3	\$1.2	\$3.9	\$4.8	\$4.0	\$4.0
Operating Income	\$17.4	\$17.9	\$3.4	\$0.3	(\$2.2)	(\$0.4)	\$1.3	\$10.5	\$43.6	\$76.8
other net	0.25	0.49	0.14	(0.48)	0.66	0.50	0.81	1.00	1.00	1.00
Net Income before tax	\$17.6	\$18.4	\$3.6	(\$0.2)	(\$1.5)	\$0.1	\$2.1	\$11.5	\$44.6	\$77.8
Taxes / Other	(\$6.2)	(\$0.4)	\$1.1	\$0.4	\$0.7	(\$0.1)	\$2.0	\$2.6	\$10.9	\$19.2
Tax Rate	-35.9%	-2.0%	31.2%	127.9%	-31.9%	26.0%	161.2%	25.0%	25.0%	25.0%
GAAP Net Income	\$23.9	\$18.8	\$2.5	(\$0.6)	(\$2.2)	\$0.2	\$0.0	\$8.8	\$33.7	\$58.6
YOY Growth	-	-21.4%	-28.6%	-113.5%	-127.9%	-93.0%	-99.8%	-52.9%	280.9%	74.0%
Reported EPS	\$0.97	\$0.74	\$0.10	(\$0.02)	(\$0.09)	\$0.01	\$0.00	\$0.33	\$1.20	\$1.95
YOY Growth	-	-23.8%	-29.6%	-113.1%	-127.5%	-93.2%	-99.8%	20879.8%	267.3%	62.4%
One time charge	0.0	(3.7)	0.0	0.4	0.0	0.0	0.4	0.0	0.0	0.0
Non-GAAP net income	23.9	15.1	2.5	(0.2)	(2.2)	0.2	0.4	8.8	33.7	58.6
Non-GAAP EPS	\$0.97	\$0.60	\$0.10	(\$0.01)	(\$0.09)	\$0.01	\$0.02	\$0.33	\$1.20	\$1.95
Shares Outstanding	24.6	25.3	25.5	25.9	26.0	26.0	25.9	27.0	28.0	30.0

Source: Company filings and Zacks estimates

HISTORICAL ZACKS RECOMMENDATIONS



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