Zacks Small-Cap Research

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Rosetta Genomics (ROSG-NASDAQ)

ROSG: Record revenue reported for 3Q15, expect continued revenue growth for the full year 2015 and beyond; Strategic acquisition will accelerate substantial revenue growth---Buy

Current Recommendation	**Buy**
Prior Recommendation	N/A
Date of Last Change	02/26/2014
Current Price (12/01/15)	$1.36
Twelve- Month Target Price	**$7.50**

OUTLOOK

Rosetta is a molecular diagnostics company focused on microRNA-based tests for cancers and other indications. The company is currently marketing a variety of cancer tests. The company also has commercial partnerships with two companies. Recent acquisition of PersonalizeDx will greatly accelerate revenue growth.

We are optimistic with its microRNA platform technologies, which serve as the basis of continued development of molecular diagnostics. Revenue will continue to grow in the coming years due to focused marketing strategy. Long term pipeline will provide sustainable growth for the years to come.

We maintain our Buy rating.

SUMMARY DATA

52-Week High	**$4.80**
52-Week Low	**$2.19**
One-Year Return (%)	**-28.34**
Beta	**-4.10**
Average Daily Volume (sh)	**72,554**
Shares Outstanding (mil)	**15**
Market Capitalization ($mil)	**$33**
Short Interest Ratio (days)	**7.03**
Institutional Ownership (%)	**N/A**
Insider Ownership (%)	**N/A**
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 2014 Estimate	**N/A**
P/E using 2015 Estimate	**N/A**
Zacks Rank	**N/A**

Risk Level	**Above Avg.,**
Type of Stock	**Small-Value**
Industry	**Med-Biomed/Gene**
Zacks Rank in Industry	**N/A**

ZACKS ESTIMATES

Revenue
(in millions of $)

	Q1 (Mar)	Q2 (Jun)	Q3 (Sep)	Q4 (Dec)	Year (Dec)
2014		0.55 A		0.77 A	1.33 A
2015		2.30 A	2.43 A	3.50 E	8.21 E
2016					13.50 E
2017					20.00 E

Earnings per Share
(EPS is operating earnings before non recurring items)

	Q1 (Mar)	Q2 (Jun)	Q3 (Sep)	Q4 (Dec)	Year (Dec)
2014		-$0.66 A		-$0.63 A	-$1.29 A
2015		-$0.62 A	-$0.23 A	-$0.33 E	-$1.24 E
2016					-$0.75 E
2017					-$0.63 E

Zacks Projected EPS Growth Rate - Next 5 Years % **N/A**

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WHAT'S NEW

Rosetta Reports Record Revenue for Third Quarter 2015

Total revenue from continuing operations for the third quarter of 2015 was $2.4 million, as compared to $0.3 million from revenues from continuing operations for the third quarter of 2014, an increase of 790%. Third quarter revenue also represented a 17% increase from 2Q15, which was $2.1 million.

Revenue from **solid tumor testing** services in 3Q15 was $1.1 million, an increase of 319% compared to $273,000 in 3Q14 and an increase of 16% compared to $983,000 in the second quarter of 2015. Within solid tumor testing services, the Company's Cancer Origin Test posted revenue of $346,000, a 27% increase compared with $273,000 in the third quarter of 2014, and a 5% increase compared with $329,000 in the second quarter of 2015.

Revenue from **urologic cancer testing** services in 3Q15 was $1.3 million, a 17% increase compared with pro forma urologic cancer testing services revenues of $1.1 million in the second quarter of 2015. Prior to the PersonalizeDx acquisition in April 2015, Rosetta Genomics did not have revenue from urologic cancer testing services so there is no comparison with the prior-year's third quarter.

Gross billings for the third quarter of 2015 were $7.5 million compared with gross billings of $644,000 in the third quarter of 2014.

Cost of revenue for 3Q15 was $2.2 million, as compared with $377,000 for the same period in 2014.

R&D expenses for 3Q15 increased to $586,000 from $482,000 in the third quarter of 2014.

Marketing and business development expenses for 3Q15 were $1.7 million compared with $1.6 million in the year-ago period.

G&A expenses for 3Q15 were $1.9 million compared with $1.3 million for the third quarter of 2014.

The operating loss for 3Q15 was $3.9 million, compared with an operating loss of $3.4 million for the third quarter of 2014.

The net loss for 3Q15 was $3.9 million ($0.27 per share), compared with a net loss for 3Q14 of $3.4 million ($0.29 per share).

Our Takeaway

This is the first time that Rosetta reported quarterly financial results. Previously the company only reported financial results semi-annually. We welcome this change as it enhances the communication between the company and the investment community.

We are very pleased to see a record quarterly revenue growth both organically and through acquisition. The 790% increase year over year and 17% increase quarter over quarter in total revenue for 3Q15 were more than impressive.

The breakdown was also encouraging. Revenue from both the solid tumor testing and urologic cancer testing increased nicely year over year and sequentially.

Based on the impressive performance for 3Q15, and new products launch in the third quarter, we are confident that revenue will continue to grow dramatically in 4Q15 and beyond. Specifically, we model revenue for 4Q15 will be $3.5 million, an increase of 45.8% compared with revenue from 3Q15.

We model total revenue of 2016 to be $13.5 million and revenue will increase to $105 million in 2020 both organically and through acquisition.

Balance Sheet Remains Strong

As of September 30, 2015, Rosetta Genomics had $10.3 million in cash and cash equivalents, restricted cash and short- and long-term bank deposits, compared with $14.5 million as of June 30, 2015. The Company used approximately $4.2 million in cash to fund operations during the third quarter 2015.

In October, Rosetta Genomics raised net proceeds of $7.4 million in a private placement of units that consisted of common shares and warrants.

Under the terms of the agreement, Rosetta sold an aggregate of 3,333,333 units at $2.40 per unit, with each unit consisting of

- one ordinary share,
- a Series A Warrant to purchase one-half of an ordinary share at an exercise price of $2.75 per ordinary share, exercisable for a period of five years from the closing date, and
- a partially pre- funded Series B Warrant. The Series B Warrants have an exercise price of NIS 0.6 (which has been prepaid) plus $0.0001 per share. The Series B Warrants are intended to reset the price of the units, and will be exercisable for an aggregate number of ordinary shares based on a reset price per unit equal to 85% of the arithmetic average of the five lowest weighted average prices calculated during the ten trading days following the effective date of the Company's resale registration statement to be filed for the private placement; provided that the maximum aggregate number of ordinary shares issuable upon exercise of the Series B Warrants will not exceed 2,666,667. The Series B Warrants are exercisable for 60 days following the effective date of the resale registration statement.

With the addition of the net proceeds from the private placement, the company's balance sheet is getting strong. We estimate the Company's current cash could last into first quarter of **2017** based on our financial model.

New Products Launched in 3Q15 Will Contribute to Top Line Growth

BRAF Mutation Assay

In October, 2015, Rosetta launched a molecular test for **BRAF mutation** analysis to help personalize therapy for melanoma and colon cancer patients.

Rosetta Genomics' BRAF mutation analysis test utilizes highly specific and sensitive Competitive Allele-Specific TaqMan® (CAST) PCR™ technology that can detect as little as 0.5% mutated DNA in a large, normal DNA sample. BRAF mutations occur in up to 50% of malignant melanomas, and several FDA-approved BRAF inhibitor therapies have been introduced to the market for use in patients with late-stage metastatic melanoma.

This newest assay will complement the company's broad offerings so that oncologists can optimize treatment decisions for their cancer patients.

Thyroid Cancer Assay

In late September, Rosetta Genomics reached an agreement-in-principle with **FNApath** of Little Rock, Arkansas, under which Rosetta Genomics will provide endocrinologists initially testing their patients for **thyroid cancer** with the option of using a pathologist or laboratory of their own choosing, or FNApath, a centralized laboratory with an expertise in diagnosing thyroid cancer. In the event of an indeterminate result, the sample would then be tested with RosettaGx Thyroid **Reveal™**, the Company's thyroid neoplasia assay for the differential diagnosis of indeterminate fine needle aspirates (FNAs).

In October, Rosetta introduced its RosettaGx Thyroid Reveal assay and reported on its clinical performance at the 15th International Thyroid Congress (ITC) and 85th Annual Meeting of the American Thyroid Association (ATA) taking place October 18-23, 2015 in Lake Buena Vista, Florida.

Performance data from the study showed that where final diagnosis was unanimously confirmed by three pathologists (n=159), the highest standard reference diagnoses, RosettaGX Reveal demonstrated a Sensitivity of 95%, Specificity of 79%, Negative Predictive Value (NPV) of 98% and Positive Predictive Value (PPV) of 63%.

The overall sample set (n=203 before QA; 192 following QA), where the final diagnoses were agreed to by at least two pathologists, demonstrated a Sensitivity of 84%, Specificity of 72%, NPV of 90% and PPV of 60%.

In November, Rosetta announced additional performance data from the recently-completed, blinded validation study of RosettaGX Reveal™. The "gold standard" for diagnosis is agreement among the three pathologists involved in the study. When compared to this "gold standard," new data demonstrate particularly strong performance in Bethesda classes III and IV of the Bethesda System for Reporting Thyroid Cytopathology (TBSRTC), where the risk of malignancy is low, yet many of these patients are still sent to surgery. The Company expects these data to be published in a peer-reviewed journal in the coming months.

The RosettaGX Reveal offers a valuable tool for the classification of pre-operative thyroid samples, including those that are presently indeterminate according to cytological evaluation, and is the only assay that can utilize cytology smears. This assay is the first commercial test that interrogates the same thyroid cells that the cytopathologist viewed for the initial indeterminate diagnosis.

Rosetta Shares Are Undervalued

We maintain our Buy rating on Rosetta Genomics (ROSG) shares and our 12-month price target is $7.50 per share.

Rosetta is a revenue generating, emerging molecular diagnostics biotech company focused on molecular testing of cancers and other life threatening diseases. The company develops its diagnostic products based on the unique and proprietary microRNA platform technology.

Currently Rosetta is marketing multiple cancer testing offerings. In addition to currently marketed tests, Rosetta is also developing other tissue or body fluid based molecular diagnostics using its microRNA technologies. Furthermore, Rosetta is developing microRNA based therapeutics. These long term pipeline will provide sustainable growth for the company in the years to come.

Rosetta is also collaborating with pharmaceutical/biotech companies to assist these companies to develop microRNA based therapeutics. This collaboration creates the third avenue for revenue growth.

The acquisition of PersonalizeDx will greatly accelerate revenue growth in the coming quarters. Specifically, we model 2015 revenue to be $8.21 million, and 2016 revenue to be $13.50 million. Revenue will grow to $105 million in 2020, a tremendous compound annual growth rate (CAGR) of 107%. With accelerated revenue growth, Rosetta will become profitable in fiscal 2019 with earnings per share (EPS) of $0.03 based on total revenue of $55 million. EPS will grow to $0.76 per share in fiscal 2020 based on total revenue of $105 million. Recent partnerships will also accelerate revenue growth in 2015 and beyond.

Rosetta has a relatively strong balance sheet. Current cash is sufficient to fund operations into 2017 according to our model.

With all these in mind, we think Rosetta's shares are undervalued at current market price. Currently, Rosetta shares are trading at about $1.25 per share, which values the company at about $23 million in market cap based on 18 million outstanding shares. This is apparently a huge discount compared to its peers. As we said, Rosetta is a revenue generating diagnostics company targeting the high growth market of molecular diagnostics. The company's microRNA platform technology has broad applications targeting both diagnostics and therapeutics. The acquisition of PersonalizeDx also de-risks Rosetta in terms of revenue growth in the coming years. We don't think the Street has recognized the potential of high revenue growth in the coming years for Rosetta.

Based on the reduced risks and our financial model, we think a P/E multiple of 30x is appropriate for Rosetta. If we apply this P/E coupled with EPS of $0.76 in 2020, discounted at 25% for 5 years, we come up with our price target of $7.5 per share. Our price target values Rosetta at $135 million in market cap, which we think is still conservative.

Execution is the key to achieve expected growth and will have a significant impact on the share price. The fluctuation of the broader market in the US will also have impact on the company's share price in the next 6 to 12 months. In general, we think the company has a **favorable risk/award profile** at this time with downside risk relatively low and high upside potential.

PROJECTED INCOME STATEMENT

	2014A (Dec)			2015E (Dec)				2016E (Dec)	2017E (Dec)	2018E (Dec)	2019E (Dec)	2020E (Dec)
$ in million except per share data	1H14	2H14	FYA	1H15	3Q	4Q	FYE	FYE	FYE	FYE	FYE	FYE
Total Revenues	**$0.55**	**$0.77**	**$1.33**	**$2.28**	**$2.43**	**$3.50**	**$8.21**	**$13.50**	**$20.00**	**$35.00**	**$55.00**	**$105.00**
YOY Growth	187.0%	264.6%	227.7%	311.2%	194.0%	352.8%	518.6%	64.5%	48.1%	75.0%	57.1%	90.9%
CoGS	0.77	0.54	1.31	2.27	2.17	2.45	6.89	1.69	2.50	4.38	6.88	13.13
Gross Income	**($0.22)**	**$0.23**	**$0.02**	**$0.01**	**$0.26**	**$1.05**	**$1.32**	**$11.81**	**$17.50**	**$30.63**	**$48.13**	**$91.88**
Gross Margin	-39.0%	30.1%	1.3%	0.4%	10.8%	30.0%	16.1%	87.5%	87.5%	87.5%	87.5%	87.5%
R&D	$1.01	$0.92	$1.93	$1.36	$0.59	$0.75	$2.70	$4.50	$7.00	$9.50	$12.50	$14.50
% R&SD	182.5%	118.5%	145.2%	59.7%	24.1%	21.4%	32.9%	33.3%	35.0%	27.1%	22.7%	13.8%
SG&A	$6.01	$6.33	$12.34	$7.72	$3.56	$4.94	$16.22	$20.00	$22.50	$25.00	$30.00	$45.00
% SG&A	1085.4%	818.8%	930.1%	338.8%	146.4%	141.1%	197.6%	148.1%	112.5%	71.4%	54.5%	42.9%
Other Expense	$0.00	$0.00	$0.00	($2.35)	$0.00	$0.00	($2.35)	$0.00	$0.00	$0.00	$0.00	$0.00
Operating Income	**($7.2)**	**($7.0)**	**($14.3)**	**($6.7)**	**($3.9)**	**($4.6)**	**($15.2)**	**($12.7)**	**($12.0)**	**($3.9)**	**$5.6**	**$32.4**
Operating Margin	-1306.9%	-907.1%	-1074.0%	-294.9%	-159.7%	-132.6%	-185.7%	-94.0%	-60.0%	-11.1%	10.2%	30.8%
Other Net	$0.1	($0.3)	($0.3)	$0.0	($0.0)	($0.3)	($0.3)	($0.5)	($0.5)	($0.5)	($0.5)	($0.5)
Pre-Tax Income	**($7.2)**	**($7.3)**	**($14.5)**	**($6.7)**	**($3.9)**	**($4.9)**	**($15.5)**	**($13.2)**	**($12.5)**	**($4.4)**	**$5.1**	**$31.9**
Income taxes(benefit)	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$1.0	$4.5	$9.0
Tax Rate	0.0%	0.0%	-0.1%	-0.1%	-0.1%	0.0%	-0.1%	0.0%	0.0%	-22.9%	87.8%	28.2%
Reported Net Income	**($7.2)**	**($7.4)**	**($14.5)**	**($6.7)**	**($3.9)**	**($4.9)**	**($15.5)**	**($13.2)**	**($12.5)**	**($5.4)**	**$0.6**	**$22.9**
YOY Growth	-	-	-	-	-	-	-	-	-	-57.0%	-111.6%	3560.0%
Net Margin	-	-	-	-	-	-	-	-	-62.5%	-15.4%	1.1%	21.8%
Diluted Shares Out	10.8	11.7	11.2	13.6	14.8	15.0	14.5	17.5	20.0	22.5	25.0	30.0
Reported EPS	**($0.66)**	**($0.63)**	**($1.29)**	**($0.49)**	**($0.27)**	**($0.33)**	**($1.07)**	**($0.75)**	**($0.63)**	**($0.24)**	**$0.03**	**$0.76**
One- time charge	*$0.00*	*$0.00*	*$0.00*	($2.35)	$0.00	*$0.00*	*-$2.35*	*$0.00*	*$0.00*	*$0.00*	*$0.00*	*$0.00*
Non GAAP Net Income	**($7.2)**	**($7.4)**	**($14.5)**	**($9.0)**	**($3.9)**	**($4.9)**	**($17.9)**	**($13.2)**	**($12.5)**	**($5.4)**	**$0.6**	**$22.9**
Non GAAP EPS	**($0.66)**	**($0.63)**	**($1.29)**	**($0.62)**	**($0.23)**	**($0.33)**	**($1.24)**	**($0.75)**	**($0.63)**	**($0.24)**	**$0.03**	**$0.76**

Source: Company filing and Zacks estimates

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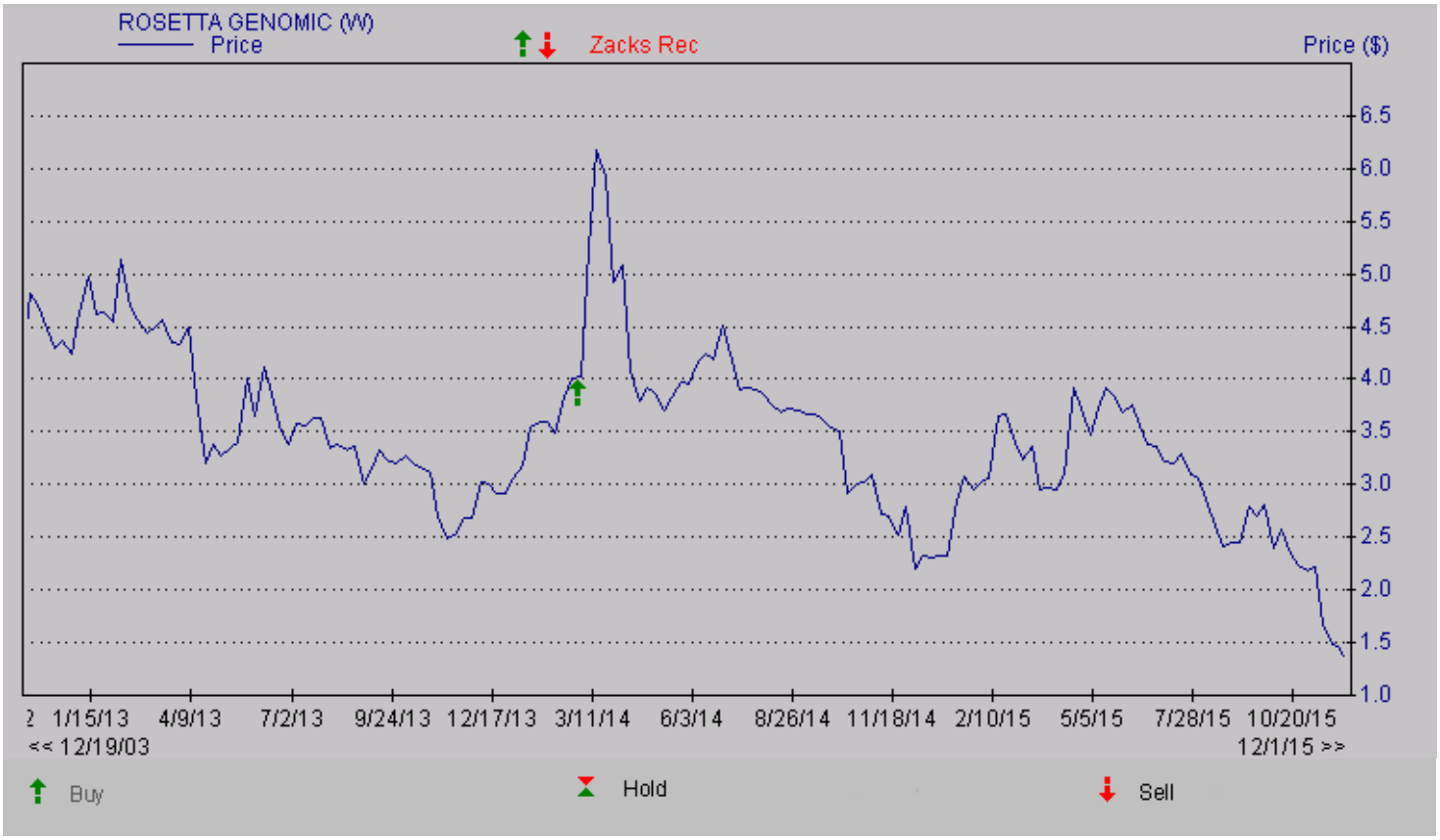

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Buy/Outperform: The analyst expects that the subject company will outperform the broader U.S. equity market over the next one to two quarters.
Hold/Neutral: The analyst expects that the company will perform in line with the broader U.S. equity market over the next one to two quarters.
Sell/Underperform: The analyst expects the company will underperform the broader U.S. Equity market over the next one to two quarters.

The current distribution is as follows: Buy/Outperform- 16.7%, Hold/Neutral- 77.5%, Sell/Underperform – 5.2%. Data is as of midnight on the business day immediately prior to this publication.