Zacks Equity Research

www.zacks.com

June 16, 2010
Jason Napodano, CFA
312-265-9421
jnapodano@zacks.com

111 North Canal Street, Chicago, IL 60606

Neurocrine Biosciences, Inc.

(NBIX-NASDAQ)

NBIX: Homerun Partnership With Abbott Labs To Develop and Commercialize Elagolix…

Current Recommendation	**Outperform**
Prior Recommendation	Neutral
Date of Last Change	06/16/2010
Current Price (06/16/10)	$4.70
Six- Month Target Price	**$9.00**

UPGRADING RATING

This morning Neurocrine Bio announced a worldwide development and commercialization partnership with Abbott Labs for elagolix. The partnership includes elagolix for the treatment of endometriosis-pain, as well as potential development into uterine fibroids or oncology. Abbott paid Neurocrine $75 million upfront, with the potential for another $500 million plus royalties still to come. The partnership is a homerun in our view. Abbott is the ideal partner for Neurocrine with elagolix. The news comes less than a month after the phase II DAISY-901 program offered up positive data on all primary and secondary endpoints for the treatment of endometriosis. We expect Abbott to be in position to initiate the phase III program on elagolix in endometriosis by the end of the year.

SUMMARY DATA

52-Week High	**$4.84**
52-Week Low	**$2.00**
One-Year Return (%)	**44.17**
Beta	**0.49**
Average Daily Volume (sh)	**2,026,423**
Shares Outstanding (mil)	**55**
Market Capitalization ($mil)	**$258**
Short Interest Ratio (days)	**6.84**
Institutional Ownership (%)	**71**
Insider Ownership (%)	**5**
Annual Cash Dividend	**$0.00**
Dividend Yield (%)	**0.00**
5-Yr. Historical Growth Rates	
Sales (%)	**-62.7**
Earnings Per Share (%)	**N/A**
Dividend (%)	**N/A**
P/E using TTM EPS	**N/A**
P/E using 2010 Estimate	**N/A**
P/E using 2011 Estimate	**N/A**
Zacks Rank	**3**

Risk Level	**Below Avg.**
Type of Stock	**Small-Growth**
Industry	**Med-Drugs**
Zacks Rank in Industry	**18 of 77**

ZACKS ESTIMATES

Revenue
(in millions of $)

	Q1 (Mar)	Q2 (Jun)	Q3 (Sep)	Q4 (Dec)	Year (Dec)
2009	0.7 A	0.7 A	0.7 A	0.7 A	3.0 A
2010	0.8 A	0.9 E	1.8 E	1.8 E	5.2 E
2011					15.0 E
2012					25.0 E

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

	Q1 (Mar)	Q2 (Jun)	Q3 (Sep)	Q4 (Dec)	Year (Dec)
2009	-$0.51 A	-$0.39 A	-$0.21 A	-$0.20 A	-$1.30 A
2010	-$0.18 A	-$0.21 E	-$0.16 E	-$0.15 E	-$0.70 E
2011					-$0.43 E
2012					-$0.29 E

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

© Copyright 2010, Zacks Investment Research. All Rights Reserved.

WHAT'S NEW

Collaboration With Abbott Labs For Elagolix…

On June 16, 2010, Neurocrine Bio announced that they have entered into a collaboration agreement to develop and commercialize elagolix for the treatment of endometriosis-related pain with Abbott Labs. Under the terms of the agreement, Abbott will receive worldwide exclusive rights to develop and commercialize elagolix and all next-generation GnRH antagonists for women's and men's health. This includes potential indication beyond endometriosis pain, such as uterine fibroids, adenomyosis, premenstrual dysphoric disorder (PMDD), polycystic ovarian syndrome (PCOS), breast cancer, or benign prostatic hypertrophy (BPH).

Abbott will make an upfront payment of $75 million and will fund all ongoing development activities. Neurocrine is eligible to receive additional milestone payments of approximately $500 million from Abbott for the achievement of certain development, regulatory and commercial milestones. Neurocrine will also receive funding for certain internal collaboration expenses, plus royalty payments (we model 20%) on any future product sales. On the conference call highlighting the deal, CEO Kevin Gorman noted that the "vast majority" of the $500 million milestones are for development. This gives us confidence that Neurocrine will recognize a significant portion of these milestones prior to potential FDA approval in 2013 or 2014. Finally, Neurocrine will handle the CMC and commercial scale-up for elagolix, which will be funding by Abbott Labs.

…Is Homerun For Neurocrine Bio…

The collaboration is a homerun for Neurocrine Bio. Abbott is the pioneer and market leader in GnRH antagonists with Lupron (leuprolide) for the treatment of hormone-responsive cancers such as prostate cancer or breast cancer. The drug is also by Ob/Gyns for the treatment of endometriosis and uterine fibroids, as well as to treat precocious puberty, and to control ovarian stimulation in In-Vitro Fertilization (IVF). Abbott has a strong appreciation for the GnRH mechanism and the company is clearly committed to see elagolix a success with Lupron expected to lose patent protection in 2015. Abbott's Lupron sales in 2009 were $800 million ($540 million U.S.). We believe that Abbott will look to replace Lupron in the Ob/Gyn market with elagolix thanks to superior efficacy and tolerability, as well as patent protection.

The $75 million upfront from Abbott, as well as the potential to receive several hundred million more over the next few years, dramatically improved the strategic position at Neurocrine Bio. We expect Neurocrine to report roughly $135 million in cash on the books at the end of the second quarter 2010. Management can now push forward the development of internal pipeline candidates, including CRF receptor antagonists and VMAT-2, as well as in-license new pre-phase II molecules within the company's core CNS focus. We view this as a game-changer for Neurocrine. Accordingly, we are raising our rating to 'Outperform', and increasing our price target to $9 per share.

INVESTMENT THESIS

DAISY Program Offers Positive Results…

On May 24, 2010, Neurocrine Bio announced that the DAISY PETAL (Study-901) program provided statistically significant results in all top-line primary and secondary endpoints testing the company's proprietary, orally-active nonpeptide Gonadotropin-Releasing Hormone (GnRH) receptor antagonist, elagolix, in patients with endometriosis. In addition, the company confirmed that the daily scales for menstrual and non-menstrual pelvic pain, developed with extensive input from the U.S. FDA and patients, functioned well in a clinical trial setting. Daisy PETAL (901) study enrolled 137 endometriosis subjects into one of two treatment groups; elagolix 150 mg (n=66) or placebo (n=66) once daily for two months of treatment, in a double-blind design.

Top-line results confirm that elagolix is associated with statistically significant reduction in the two co-primary endpoints, Dysmenorrhea and Non-Menstrual Pelvic Pain, and the exploratory endpoint, Dyspareunia, when compared to placebo based on the ITT population.

Data at Week 8	Baseline	Elagolix	Placebo
Change in Baseline (ITT population) of…			
Dysmenorrhea (mean, 0-3)	2.1 / 2.1	-1.13	-0.37
Non-Menstrual Pelvic Pain (mean, 0-3)	1.4 / 1.3	-0.47	-0.19
Dyspareunia (pain, 0-3)	1.6 / 1.3	-0.61	-0.23
All p<0.01			

Management also conducted a responder analysis that demonstrated clinically meaningful improvement of 30% or greater from baseline on all three endpoints (ITT population).

Data at Week 8	Elagolix	Placebo
Responder Analysis (>30%)…		
Dysmenorrhea	63% [1]	33%
Non-Menstrual Pelvic Pain	63% [1]	33%
Dyspareunia	58% [2]	34%
1 = p<0.01 2 = p<0.05		

Secondary endpoints also demonstrated statistically significant improvement from elagolix subjects versus the placebo on validated efficacy outcome assessments.

Data at Week 8	Elagolix	Placebo
Secondary Efficacy Endpoints (ITT population) on…		
Patient Global Impression of Change (PGIC) "much" or "very much improved"	60%	30%
Endometriosis Health Profile 5 (EHP-5) Related-Pain Assessment, 0-100	-28 pts	-13 pts
Composite Pelvic Signs & Symptoms Scale (CPSSS) Reduction from Baseline (9.5), 0-15)	-4.45 pts	-2.19 pts
All p<0.001		

During the phase II program, the elagolix demonstrated encouraging safety and tolerability. Discontinuation due to adverse events (AEs) was low at 4.4% for elagolix vs. 1.4% for the placebo. The most common adverse event reported more often with elagolix than with placebo was nausea (7.4% elagolix; 2.9% placebo). This was consistent with what we saw in previous clinical studies. Importantly, there were no elagolix treatment-related serious adverse events (SAEs). We note that subjects are continuing for an additional four months of open-label elagolix treatment and assessments program. This 24-week open-label data should be available in late August 2010.

…Next Step – Meet With The FDA…

The top-line data from Daisy PETAL was been reported in late May 2010. Management will request an end of phase II (Type-B) meeting with the Division of Reproductive Products at the FDA. We expect this request (filing) will take place in late June 2010. The FDA usually responds within 60 days, and our best guess is that the meeting will take place in late August / early September 2010. We expect that Abbott Labs will participate in the meeting.

In total, Neurocrine should be able to sit down with the FDA and offer up data from 6 phase II programs (2 phase IIa and 4 phase IIb) on roughly 1,000 patients. Concurrent to the end of phase II meeting request, management will file a draft proposal for a special protocol assessment (SPA) for the phase III design. The company believes that the first round of discussions on the proposed SPA will take place with the agency at the end of phase II meeting. The final SPA agreement should be in hand by late in the Q3-2010. This should allow Abbott to begin a phase III program before the end of the year.

We expect that the pivotal phase III program will include two large-scale (n~500) patient programs with co-primary Dysmenorrhea and Non-Menstrual Pelvic Pain endpoints. The exploratory Dyspareunia endpoint may also be tested in the phase III program. There will also be a long-term (n~400) safety program. Depending on Abbott's European strategy, one of the two phase III programs may include a head-to-head non-inferiority program vs. Lupron for the European submission.

Peak sales for elagolix in the U.S. are $500 million. We believe a specialty Ob/Gyn sales force of 200 to 250 representatives can effectively target greater than 90% of the market.

…Background Info on Endometriosis…

Endometriosis is a medical condition characterized by growth of the endometrium (uterine tissue) outside of the uterus, most usually on the pelvis, that affects an estimated 100 million women of reproductive age worldwide, or about 5-10% of the female population according to the World Endometriosis Foundation. There are an estimated 8 million women affected by endometriosis in the U.S. Endometriosis also occurs in a small percentage (2-4%) of postmenopausal women. Symptoms of endometriosis are severe recurring pain that can include dysmenorrhea (menstrual pain), dyspareunia (painful sex), dyschezia (painful bowel movements) and dysuria (painful urination). Endometriosis is caused by an excess of the hormone estrogen, and thus can manifest during peak reproductive years. Hereditary and environmental factors, as well as associated infections (such as HPV), can increase incidence and severity.

The disease is often treated, ineffectively, by a number of medications. NSAIDs are used to treat mild-to-moderate pain associated with endometriosis. Progesterone or progestin and hormonal contraceptives are used to regulate estrogen levels when appropriate. In fact, industry data shows that almost 20% of all oral contraceptives prescribed are written specifically for the treatment of endometriosis. Steroids and aromatase inhibitors are used to block estrogen levels and endometrium growth. However, these have significant negative side-effects. Lupron, a gonadotropin depo shot, is used to lower estrogen levels and slow endometrium growth. However, Lupron shuts down estradiol production and puts the body into “medicated menopause”, resulting in significant side effects such as hot flashes and a reduction in bone mineral density. In the most severe cases, a hysterectomy is performed.

Elagolix, a gonadotropin-releasing hormone (GnRH) antagonist has efficacy characteristics similar to Lupron for the treatment of endometriosis, but with less potential for bone mineral density loss. The drug works by blocking the action of GnRH and suppressing luteinizing hormone and follicle-stimulating hormone. There are a few other GnRH molecules on the market, but none that are oral in dosing or have amassed the clinical data of elagolix. Therefore, we believe that Neurocrine can achieve significant market share gains with elagolix upon commercialization. Most women shy away from Abbott’s Lupron due to side-effects. Nevertheless, Abbott is still the market leader in this category. As such, we believe that Neurocrine has the ideal pharmaceutical partner to further develop and commercialize elagolix in Abbott Labs.

Market research so far has been encouraging. Management noted that they are beginning to receive requests from physicians to prescribe elagolix on a compassionate basis. It is possible the FDA will allow elagolix compassionate use once phase III trials begin in 2010.

…Uterine Fibroids…

Beyond endometriosis-pain, uterine fibroids represent an attractive second indication for elagolix. Uterine fibroids or adenomyosis are benign tumors that form on the wall of the uterus. They are the most common type of growth found in a woman's pelvis and are most common in women aged 30-40 years. While many women do not have symptoms, depending on the size, location and number, uterine fibroids can cause heavy menstrual bleeding, can put pressure on the bladder and rectum, and can cause pain and nausea. Symptoms can also include miscarriages and infertility. Depending on the symptoms, treatment sometimes requires surgery. This is a potential billion-dollar market in the U.S. given the significant number of women affected and the lack of pharmaceutical options available.

…Benign Prostatic Hypertrophy…

In men’s health, elagolix has potential in benign prostatic hypertrophy (BPH). BPH is defined by enlargement of the prostate gland. As the prostate grows larger and presses against the urethra, normal flow of urine is hindered. A competitor is developing an injectable peptide GnRH antagonist currently in phase III trials. However, Neurocrine Bio believes that a significant advantage may be provided by oral non-peptide GnRH antagonist, such as elagolix. Moderate to severe BPH affects an estimated 21 million men in the U.S. Additionally, more than 40% of all men over the age of 60 suffer from the symptoms of BPH. Worldwide sales of current treatments for BPH exceeded $3 billion in 2006.

PROJECTED FINANCIALS

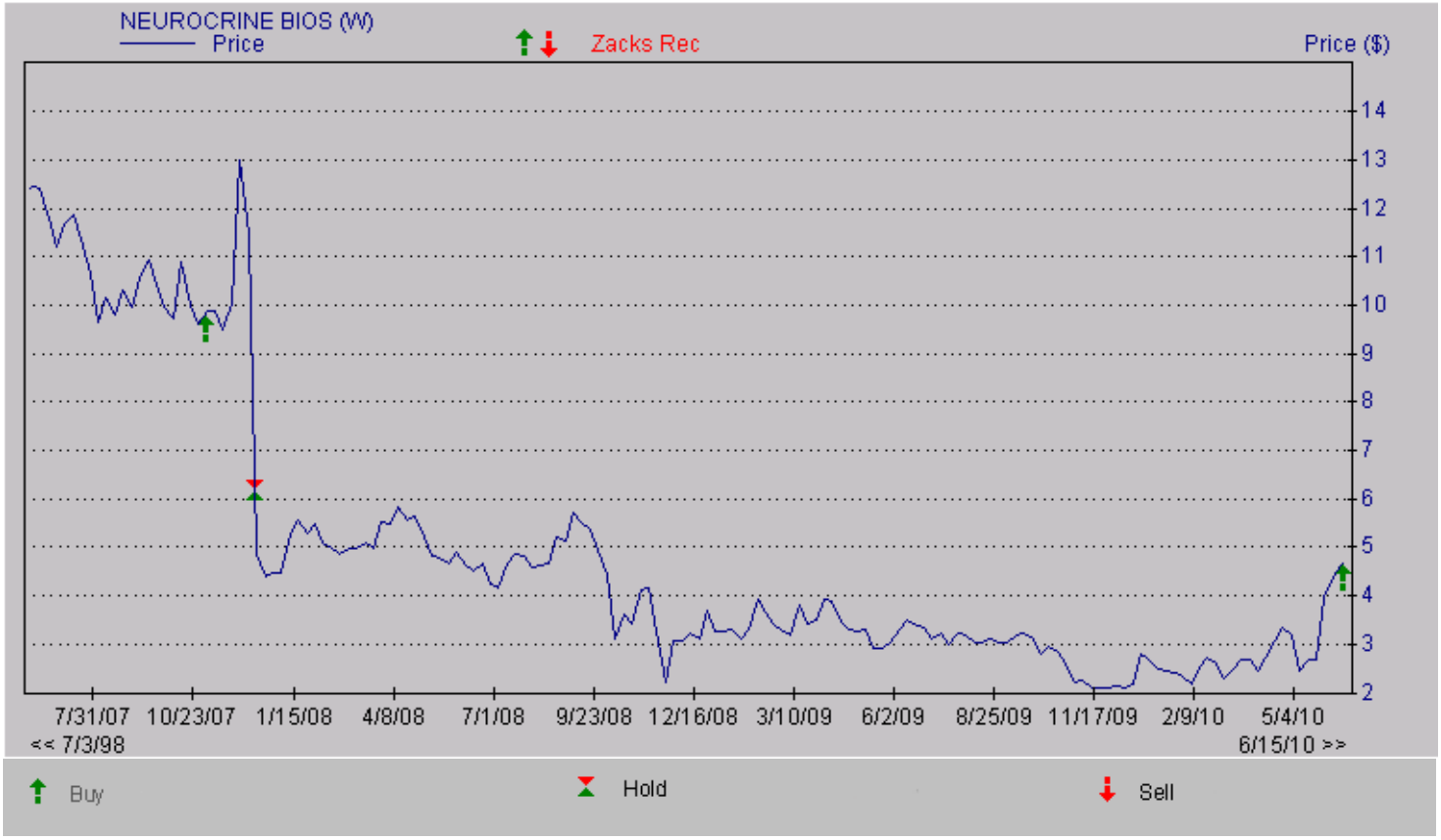
Neurocrine Biosciences Inc.
Income Statement

	2009 A	Q1A	Q2E	Q3E	Q4E	2010 E	2011 E	2012 E	2013 E	2014 E
R&D / Milestones & Fees	**$3.0**	**$0.8**	**$0.7**	**$1.8**	**$1.8**	**$5.1**	**$15.0**	**$25.0**	**$25.0**	**$35.0**
YOY Growth	*-25.7%*	*0.8%*	*1.0%*	*143.1%*	*140.8%*	*71.2%*	*196.7%*	*66.7%*	*0.0%*	*40.0%*
elagolix Royalties	**$0**	**$0**	**$0**	**$0**	**$0**	**$0**	**$0**	**$0**	**$0**	**$25.0**
YOY Growth	-	-	-	-	-	-	-	-	-	-
CRF Receptor Antagonists	**$0**	**$0**	**$0**	**$0**	**$0**	**$0**	**$0**	**$0**	**$0**	**$0**
YOY Growth	-	-	-	-	-	-	-	-	-	-
Urocortin 2	**$0**	**$0**	**$0**	**$0**	**$0**	**$0**	**$0**	**$0**	**$0**	**$0**
YOY Growth	-	-	-	-	-	-	-	-	-	-
VMAT-2	**$0**	**$0**	**$0**	**$0**	**$0**	**$0**	**$0**	**$0**	**$0**	**$0**
YOY Growth	-	-	-	-	-	-	-	-	-	-
Total Revenues	**$3.0**	**$0.8**	**$0.7**	**$1.8**	**$1.8**	**$5.1**	**$15.0**	**$25.0**	**$25.0**	**$60.0**
YOY Growth	*-25.7%*	*0.8%*	*1.0%*	*143.1%*	*140.8%*	*71.2%*	*196.7%*	*66.7%*	*0.0%*	*140.0%*
CoGS / Royalties	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
Gross Margin	*100.0%*	*100.0%*	*100.0%*	*100.0%*	*100.0%*	*100.0%*	*100.0%*	*100.0%*	*100.0%*	*100.0%*
SG&A	$14.9	$3.2	$3.2	$3.2	$3.3	$12.9	$14.0	$15.0	$16.0	$17.0
% SG&A	*505.2%*	*424.8%*	*432.4%*	*179.6%*	*185.2%*	*255.1%*	*93.3%*	*60.0%*	*64.0%*	*28.3%*
R&D	$35.8	$7.6	$7.8	$6.2	$5.5	$27.1	$22.0	$24.0	$26.0	$30.0
% R&D	*1212.7%*	*1006.1%*	*1054.1%*	*348.0%*	*308.7%*	*535.5%*	*146.7%*	*96.0%*	*104.0%*	*50.0%*
Operating Income	($47.8)	($10.0)	($10.3)	($7.6)	($7.0)	($34.9)	($21.0)	($14.0)	($17.0)	$13.0
Operating Margin	-	-	-	-	-	-	-	-	-	-
Interest / Other Income	($3.3)	$1.5	($0.3)	($0.3)	($0.4)	$0.5	($1.4)	($1.8)	($2.1)	($2.1)
Pre-Tax Income	($51.0)	($8.5)	($10.6)	($7.9)	($7.4)	($34.4)	($22.4)	($15.8)	($19.1)	$10.9
Taxes	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
Tax Rate	*0%*	*0%*	*0%*	*0%*	*0%*	*0%*	*0%*	*0%*	*0%*	*0%*
Net Income	($51.0)	($8.5)	($10.6)	($7.9)	($7.4)	($34.4)	($22.4)	($15.8)	($19.1)	$10.9
YOY Growth	-	-	-	-	-	-	-	-	-	-
Net Margin	-	-	-	-	-	-	-	-	-	-
Reported EPS	**($1.30)**	**($0.18)**	**($0.21)**	**($0.16)**	**($0.15)**	**($0.70)**	**($0.43)**	**($0.29)**	**($0.33)**	**$0.18**
YOY Growth	-	-	-	-	-	-	-	-	-	-
Stock Options	*$6.1*	*$0.6*	*$0.8*	*$1.0*	*$1.5*	*$3.9*	*$4.5*	*$5.0*	*$5.5*	*$6.0*
EPS Impact of FAS-123R	*$0.16*	*$0.01*	*$0.02*	*$0.02*	*$0.03*	*$0.08*	*$0.09*	*$0.09*	*$0.10*	*$0.10*
Shares Outstanding	39.1	46.6	49.5	50.0	50.5	49.2	52.5	55.0	57.5	60.0

Source: Zacks Investment Research, Inc. *Jason Napodano, CFA*

© Copyright 2010, Zacks Investment Research. All Rights Reserved.

HISTORICAL ZACKS RECOMMENDATIONS



DISCLOSURES

The analysts contributing to this report do not hold any shares of NBIX. Zacks does have or seeks to have a business relationship with the companies in which it covers. Additionally, the analysts contributing to this report certify that the views expressed herein accurately reflect the analysts' personal views as to the subject securities and issuers. Zacks certifies that no part of the analysts' compensation was, is, or will be, directly or indirectly, related to the specific recommendation or views expressed by the analyst in the report. Additional information on the securities mentioned in this report is available upon request. This report is based on data obtained from sources we believe to be reliable, but is not guaranteed as to accuracy and does not purport to be complete. Because of individual objectives, the report should not be construed as advice designed to meet the particular investment needs of any investor. Any opinions expressed herein are subject to change. This report is not to be construed as an offer or the solicitation of an offer to buy or sell the securities herein mentioned. Zacks or its officers, employees or customers may have a position long or short in the securities mentioned and buy or sell the securities from time to time. Zacks uses the following rating system for the securities it covers. **Outperform**- Zacks expects that the subject company will outperform the broader U.S. equity market over the next one to two quarters. **Neutral**- Zacks expects that the company will perform in line with the broader U.S. equity market over the next one to two quarters. **Underperform**- Zacks expects the company will underperform the broader U.S. Equity market over the next one to two quarters. The current distribution of Zacks Ratings is as follows on the 992 companies covered: Outperform- 13.7%, Neutral- 80.2%, Underperform – 5.6%. Data is as of midnight on the business day immediately prior to this publication.

© Copyright 2010, Zacks Investment Research. All Rights Reserved.