Zacks Small-Cap Research

January 22, 2014
Jason Napodano, CFA
312-265-9421
jnapodano@zacks.com

scr.zacks.com
111 North Canal Street, Chicago, IL 60606

POZEN, Inc. (POZN-NASDAQ)

POZN: Insights From Meeting With Management…

Current Recommendation	**Outperform**
Prior Recommendation	Neutral
Date of Last Change	03/07/2007
Current Price (01/22/14)	$8.60
Target Price	**$12.00**

UPDATE

On Sunday, January 12, 2014, we arrived in San Francisco, CA for the annual JP Morgan Healthcare Conference, as well as the parallel Biotech showcase and OneMedForum Conferences. This was the eighth year in a row that we made the trip to San Francisco for these events, which are a must-attend for serious healthcare investors.

During my three days in San Francisco, I conducted 25 one-on-one meetings with various managements of small and mid-cap biotechnology and specialty pharmaceutical companies. Below are some "notes" from our meeting with Pozen, Inc.

SUMMARY DATA

52-Week High	**$9.77**
52-Week Low	**$4.50**
One-Year Return (%)	**59.67**
Beta	**1.39**
Average Daily Volume (sh)	**349,715**
Shares Outstanding (mil)	**31**
Market Capitalization ($mil)	**$267**
Short Interest Ratio (days)	**3.82**
Institutional Ownership (%)	**56**
Insider Ownership (%)	**4**
Annual Cash Dividend	**$0.00**
Dividend Yield (%)	**0.00**
5-Yr. Historical Growth Rates	
Sales (%)	**N/M**
Earnings Per Share (%)	**N/A**
Dividend (%)	**N/A**
P/E using TTM EPS	**N/A**
P/E using 2013 Estimate	**N/M**
P/E using 2014 Estimate	**N/A**

Risk Level	**Average**
Type of Stock	**Small-Growth**
Industry	**Med-Drugs**

ZACKS ESTIMATES

Revenue
(In millions of $)

	Q1 (Mar)	Q2 (Jun)	Q3 (Sep)	Q4 (Dec)	Year (Dec)
2012	1.3 A	1.4 A	0.9 A	1.4 A	5.3 A
2013	1.4 A	1.7 A	2.6 A	4.6 E	10.3 E
2014					32.0 E
2015					36.0 E

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

	Q1 (Mar)	Q2 (Jun)	Q3 (Sep)	Q4 (Dec)	Year (Dec)
2012	-$0.28 A	-$0.17 A	-$0.19 A	-$0.20 A	-$0.84 A
2013	-$0.19 A	-$0.13 A	-$0.16 A	-$0.05 E	-$0.53 E
2014					$0.34 E
2015					$0.58 E

© Copyright 2014, Zacks Investment Research. All Rights Reserved.

WHAT'S NEW

Pozen Inc. (POZN)
Meeting took place with Dr. John Plachetka, Chairman & CEO, and William Hodges, CFO

Pozen's stock has done very well over the past twelve months, up 51% - and that does not count the $1.75 per share special cash distribution paid on December 30, 2013. When including that payment to shareholders, Pozen returned nearly 100% in 2013.

We did our best to pry from management some information about the discussions the company had with the U.S. FDA in November 2013 around the pending PDUFA for the company's PA "safer aspirin" product. As a reminder, Pozen announced in November that the FDA requested a teleconference to discuss the new drug application for PA-325/40 and PA-81/40. Late last year, Pozen announced that the FDA had extended the PDUFA goal to April 25, 2014 to allow Pozen to conduct a comparative Phase 1 pharmacokinetic study. Although this study has yet to be listed on ClinicalTrials.gov, management was able to share some of the details with us at the meeting.

The study will compare the dissolution of the 40mg immediate release omeprazole component between PA-325/40 and PA-81/40. Pozen did the initial pharmacokinetic work for the drug on the PA-325/40 compound and the FDA wants to be sure that the characteristics of PA-81/40 are similar. Given that PA-325/40 contains 325mg of aspirin compared to only 81mg of aspirin for PA-81/40, the surface area of the 40mg omeprazole component differs between the two formulations. Management tells us that the initial pk curves between the two compounds do differ slightly, but that the overall characteristics should be similar enough (usually the FDA gives a window of ±20% on these types of things) to sail through review with no issues. Thus, we believe PA will be approved in late April 2014. We remind investors that Pozen licensed the U.S. rights of the drug to Sanofi in September 2013 in return for $15 million in upfront cash and future cash milestones and royalties on sales. Approval and launch of the product nets Pozen another $20 million combined milestone.

We think PA is a $250 to $300 million product in the U.S. Pozen management expects Sanofi to put forth a "first class" effort with PA, piggy-backing off the success in this area by the company with mega-blockbuster Plavix. In our view, the future for Pozen remains very bright given the pending launch of PA around the middle of 2014 and the recent acquisition of Vimovo by Horizon Pharma. When we asked Dr. Plachetka, "What's next for Pozen," his response was, "Continue to return cash to shareholders!"

We've done some initial modeling on what Pozen will look like with PA on the market and a reinvigorated Vimovo selling at Horizon (see below). We think Pozen could generate as much as $60-70 million in free cash flow starting in 2017. Based on the current share count, with equates to over $2.00 in potential free cash flow per share earmarked for future cash distributions.

	Vimovo		PA		Licsening	Cash				Free Cash
	WW Sales	Royalty	WW Sales	Royalty	Payments	Revenues	Op. Exps	Taxes	Cash Adjs	Flow
2013	$89	$6.2	$0	$0	$15.0	$21.2	($26.5)	$0	$2	($3.3)
2014	$95	$9.0	$50	$10.0	$20.0	$39.0	($22.0)	$0	$2	$19.0
2015	$115	$11.5	$100	$20.0	$0	$31.5	($18.0)	$0	$2	$15.5
2016	$125	$12.5	$200	$40.0	$10.0	$62.5	($16.0)	$0	$2	$48.5
2017	$140	$14.0	$300	$60.0	$0	$74.0	($16.0)	($6)	$2	$54.1
2018	$150	$15.0	$400	$80.0	$10.0	$105.0	($16.0)	($22)	$2	$68.6
2019	$140	$14.0	$450	$90.0	$0	$104.0	($16.0)	($30)	$2	$60.1
2020	$130	$13.0	$450	$90.0	$10.0	$113.0	($16.0)	($24)	$2	$75.0
2021	$120	$12.0	$450	$90.0	$0	$102.0	($16.0)	($21)	$2	$67.2
2022	$110	$11.0	$450	$90.0	$0.0	$101.0	($16.0)	($18)	$2	$69.3
2023	$100	$10.0	$425	$85.0	$0	$95.0	($16.0)	($18)	$2	$63.5

TGR:	1%	Net Present Value of Cash Flows	$236.7
Discont Rate:	15%	Term Value	$97.4
		Cash Projection As of Year-End 2013	$31.8
Jason Napodano, CFA		**Firm Value**	$365.9
		Shares Outstanding	30.4
		Target Price	**$12.04**

At the current stock price, these dividends would equate to a 20-25% yield. You can't find that kind of "high-income yield" anywhere in the market! Pozen's stock should be trading at $12 per share based on the future projected cash flows and return of capital to shareholders. Now we understand there is a discount based on the fact that PA has yet to be approved and Horizon has yet to demonstrate it can grow Vimovo; but we think both caveats are low hurdles to overcome. We also note that our modeling above has Pozen paying taxes starting in 2017. Our assumptions could be increased by 1/3rd if Pozen decides to sell to a tax advantaged organization, similar to what the company did when it monetized the Treximet royalty to Canada's CPPIB Credit Investments in November 2011. That sales price of Treximet royalty for $75 million was around 35% higher than we factored in our DCF model due to tax implications.

PROJECTED INCOME STATEMENT

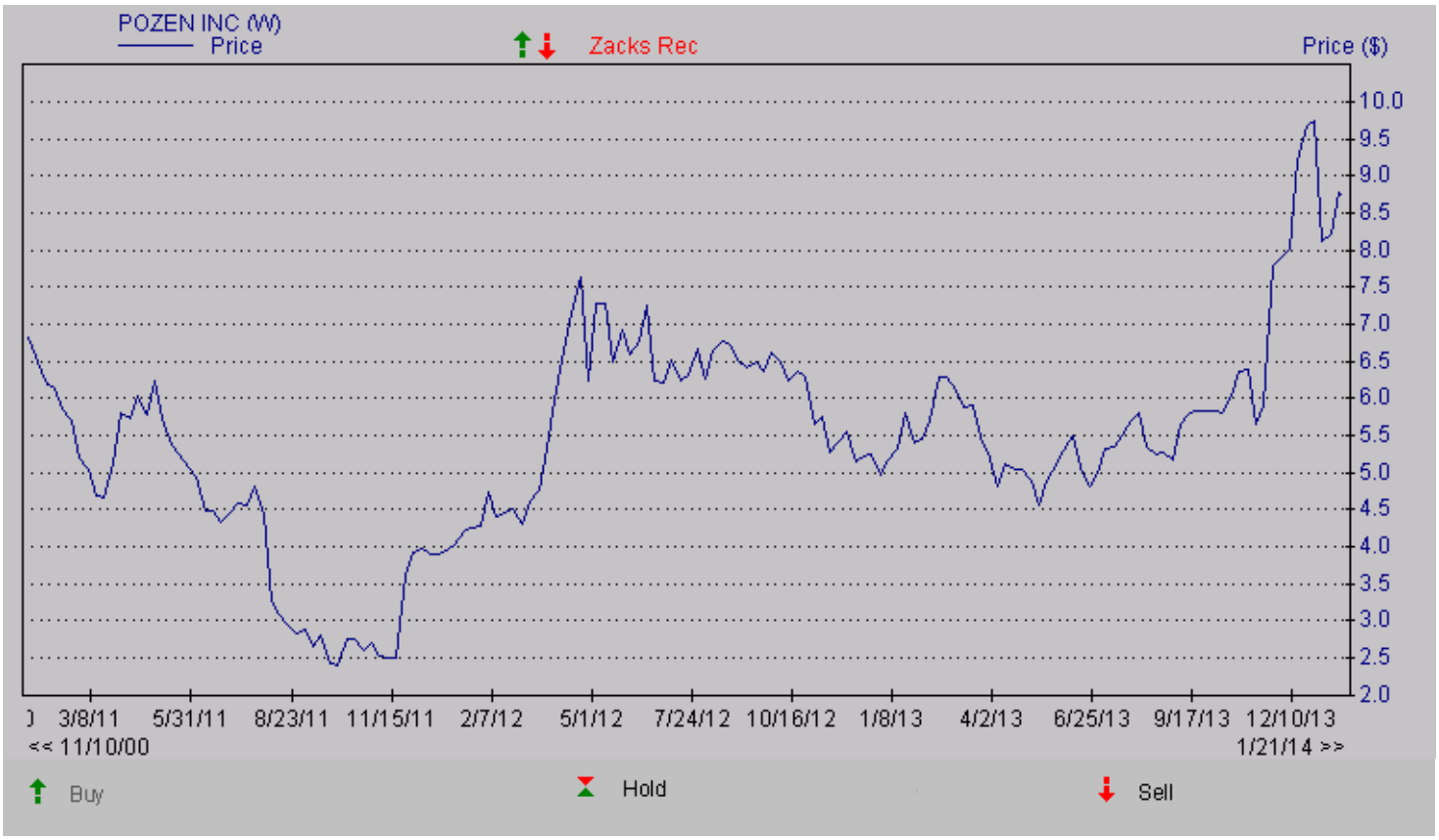
INCOME STATEMENT

Pozen, Inc.	2011 A	2012 A	Q1 A	Q2 A	Q3 A	Q4 E	2013 E	2014 E	2015 E
Vimovo (sales)	$33.8	$64.4	$19.7	$23.3	$23.0	$23.0	$89.0	$90.0	$85.0
Vimovo (royalty)	**$2.9**	**$4.8**	**$1.4**	**$1.7**	**$1.6**	**$1.6**	**$6.3**	**$8.5**	**$11.0**
YOY Growth	*533.0%*	*66.5%*	-	-	-	-	*29.1%*	*35.8%*	*29.4%*
PA-Franchise (royalty)	**$0**	**$0**	**$0**	**$0**	**$0**	**$0**	**$0**	**$12.5**	**$25.0**
YOY Growth	-	-	-	-	-	-	-	-	*100.0%*
Licensing / Development	**$71.9**	**$0.5**	**$0**	**$0**	**$1.0**	**$3.0**	**$4.0**	**$11.0**	**$0**
YOY Growth	-	-	-	-	-	-	-	-	-
Total Revenues	$87.0	$5.3	$1.4	$1.7	$2.6	$4.6	$10.3	$32.0	$36.0
YOY Growth	*26.8%*	*-93.8%*	*-71.1%*	*-97.7%*	*-97.0%*	*257.6%*	*91.8%*	*211.9%*	*12.5%*
Cost of Goods Sold	$0	$0	$0	$0	$0	$0	$0	$0	$0
Product Gross Margin	*100.0%*	*100.0%*	-	-	-	-	*100.0%*	*100.0%*	*100.0%*
SG&A	$21.8	$19.0	$3.6	$3.7	$5.2	$4.0	$16.5	$14.0	$12.0
% SG&A	*25.0%*	*355.7%*	*256.8%*	*224.9%*	*200.6%*	*86.8%*	*161.1%*	*43.8%*	*33.3%*
R&D	$23.0	$11.9	$3.6	$1.9	$2.2	$2.3	$10.0	$8.0	$6.0
% R&D	*26.5%*	*221.8%*	*253.3%*	*117.6%*	*84.5%*	*49.9%*	*97.5%*	*25.0%*	*16.7%*
Operating Income	$42.2	($25.5)	($5.8)	($4.0)	($4.8)	($1.7)	($16.3)	$10.0	$18.0
Operating Margin	*48.5%*	*-477.5%*	*-410.1%*	*-242.5%*	*-185.1%*	*-36.7%*	*-158.7%*	*31.3%*	*50.0%*
Interest Income / Net	$0.2	$0.3	$0.0	$0.0	$0.0	$0.1	$0.2	$0.4	$0.4
Pre-Tax Income	$42.3	($25.3)	($5.8)	($4.0)	($4.8)	($1.6)	($16.1)	$10.4	$18.4
Taxes	$0	$0	$0	$0	$0	$0	$0	$0	$0
Tax Rate	*0%*	*0%*	*0%*	*0%*	*0%*	*0%*	*0%*	*0%*	*0%*
Net Income	$42.3	($25.3)	($5.8)	($4.0)	($4.8)	($1.6)	($16.1)	$10.4	$18.4
YOY Growth	*83.5%*	*-159.7%*	-	-	-	-	*-36.2%*	*-164.5%*	*76.9%*
Net Margin	*48.7%*	*-472.7%*	*-408.3%*	*-241.6%*	*-184.6%*	*-34.5%*	*-157.2%*	*32.5%*	*51.1%*
Reported EPS	$1.40	($0.84)	($0.19)	($0.13)	($0.16)	($0.05)	($0.53)	$0.34	$0.58
Fully Diluted Shares	30.3	30.1	30.3	30.4	30.5	30.5	30.4	31.0	32.0

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

© Copyright 2014, Zacks Investment Research. All Rights Reserved.

HISTORICAL ZACKS RECOMMENDATIONS



© Copyright 2014, Zacks Investment Research. All Rights Reserved.

DISCLOSURES

The following disclosures relate to relationships between Zacks Small-Cap Research ("Zacks SCR"), a division of Zacks Investment Research ("ZIR"), and the issuers covered by the Zacks SCR Analysts in the Small-Cap Universe.

ANALYST DISCLOSURES

I, Jason Napodano, CFA, hereby certify that the view expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the recommendations or views expressed in this research report. I believe the information used for the creation of this report has been obtained from sources I considered to be reliable, but I can neither guarantee nor represent the completeness or accuracy of the information herewith. Such information and the opinions expressed are subject to change without notice.

INVESMENT BANKING, REFERRALS, AND FEES FOR SERVICE

Zacks SCR does not provide nor has received compensation for investment banking services on the securities covered in this report. Zacks SCR does not expect to receive compensation for investment banking services on the Small-Cap Universe. Zacks SCR may seek to provide referrals for a fee to investment banks. Zacks & Co., a separate legal entity from ZIR, is, among others, one of these investment banks. Referrals may include securities and issuers noted in this report. Zacks & Co. may have paid referral fees to Zacks SCR related to some of the securities and issuers noted in this report. From time to time, Zacks SCR pays investment banks, including Zacks & Co., a referral fee for research coverage.

Zacks SCR has received compensation for non-investment banking services on the Small-Cap Universe, and expects to receive additional compensation for non-investment banking services on the Small-Cap Universe, paid by issuers of securities covered by Zacks SCR Analysts. Non-investment banking services include investor relations services and software, financial database analysis, advertising services, brokerage services, advisory services, investment research, investment management, non-deal road shows, and attendance fees for conferences sponsored or co-sponsored by Zacks SCR. The fees for these services vary on a per client basis and are subject to the number of services contracted. Fees typically range between ten thousand and fifty thousand per annum.

POLICY DISCLOSURES

Zacks SCR Analysts are restricted from holding or trading securities in the issuers which they cover. ZIR and Zacks SCR do not make a market in any security nor do they act as dealers in securities. Each Zacks SCR Analyst has full discretion on the rating and price target based on his or her own due diligence. Analysts are paid in part based on the overall profitability of Zacks SCR. Such profitability is derived from a variety of sources and includes payments received from issuers of securities covered by Zacks SCR for services described above. No part of analyst compensation was, is or will be, directly or indirectly, related to the specific recommendations or views expressed in any report or article.

ADDITIONAL INFORMATION

Additional information is available upon request. Zacks SCR reports are based on data obtained from sources we believe to be reliable, but are not guaranteed as to be accurate nor do we purport to be complete. Because of individual objectives, this report should not be construed as advice designed to meet the particular investment needs of any investor. Any opinions expressed by Zacks SCR Analysts are subject to change without notice. Reports are not to be construed as an offer or solicitation of an offer to buy or sell the securities herein mentioned.

ZACKS RATING & RECOMMENDATION

ZIR uses the following rating system for the 1047 companies whose securities it covers, including securities covered by Zacks SCR:
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- 16.5%, Hold/Neutral- 77.7%, Sell/Underperform – 5.1%. Data is as of midnight on the business day immediately prior to this publication.