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AxoGen (Nasdaq/AXGN)
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BUY 2015 finishes strong; 2016 looks positive
AxoGen develops and markets peripheral nerve repair products
Investment Highlights

1) **AxoGen reported strong financial results for their most recent Q4/2015 (December) quarter**, including revenues of \$7.81 million, up nearly 63% year-over-year, and a net loss of \$3.6 million or (\$0.12) per share, as compared with a net loss of \$6.5 million or (\$0.35) per share in the prior year period. Our estimates had been revenues of \$7.2 million (50% growth) and a net loss of \$3.0 million or (\$0.10) per share for the quarter. Revenue growth for the quarter was led by an increased number of active accounts this year, at 300, as well as an increasing number (50% more this year) of those accounts using two or more products. Gross margins increased in the quarter to 81.9% from 80.0% one year ago, due again to manufacturing efficiencies stemming from a relocation to a new facility as well as increased unit volumes. Other expenses increased this year, to \$9.0 million from \$6.5 million primarily due to higher sales and marketing costs, as the Company added to its sales force and marketing activities, such as surgeon seminars, in 2015. For the year as a whole, revenues grew 63% to \$27.3 million, with net losses of \$13.3 million, or (\$0.51) per share, as compared to losses of \$17.7 million in 2014 or \$1.00 per share. The Company used approximately \$11-\$12 million in cash for operations for 2015, down from roughly \$14-\$15 million in 2014, which was offset by proceeds from a public offering of approximately \$13.6 million and a private institutional placement of about \$17.1 million completed in 2015. At the end of the fourth quarter, AxoGen held \$25.9 million in cash and cash equivalents, up from \$8.2 million at the start of the year.

2) **For 2016, AxoGen has provided initial financial guidance, including revenues in the \$39 million area, with gross margins in the high-70% range.** Thus, we are implementing estimates for Q1/2016E and 2016E as a whole for AxoGen, including revenues of \$7.7 million in Q1/2016E, an increase of 55% year-over-year, and net losses of \$3.5 million or (\$0.12) per share. For 2016E as a whole, our estimates for AxoGen are revenues of \$39.7 million, up 45% year-over-year, and a net loss of \$9.0 million, or (\$0.30) per share, with average gross margins of

Current Price \$5.11
Price Target \$6.00

Estimates	F2014A	F2015A	F2016E
Revenues(\$000s)	\$16,817	\$27,331	\$39,650
1Q March	3,138	4,951	7,670 E
2Q June	4,214	6,417	9,310 E
3Q September	4,671	8,154	11,540 E
4Q December	4,794	7,809	11,130 E
EPS (diluted)	(\$1.00)	(\$0.51)	(\$0.30)
1Q March	(0.24)	(0.16)	(0.12) E
2Q June	(0.21)	(0.13)	(0.08) E
3Q September	(0.19)	(0.11)	(0.04) E
4Q December	(0.35)	(0.12)	(0.06) E
P/E (x)	N/A	N/A	N/A
EBITDA/Share	(\$0.42)	(\$0.29)	(\$0.11)
EV/EBITDA (x)	N/A	N/A	N/A

Stock Data	
52-Week Range	\$2.95-\$5.95
Shares Outstanding (mil.)	30.0
Market Capitalization (mil.)	\$153.4
Enterprise Value (mil.)	\$127.5
Debt to Capital (12/15)	N/A
Book Value/Share (12/15)	\$0.27
Price/Book	18.7 x
Average Trading Volume (3-month)	68,800
Insider Ownership	30.9%
Institutional Ownership	26.9%
Short Interest	169,000
Dividend / Yield	\$0.000 / 0.0%



Price target and ratings changes over the past 3 yrs:
 Initiated - May 13, 2014 - Buy - Price Target \$5.00
 Updated - September 1, 2015 - Buy - Price Target increased to \$6.00

78.6% and other costs and expenses coming in at \$36.4 million, as compared with \$31.7 million in 2015. Driving revenue growth for the Company for 2016 is expected to be increased penetration into accounts of all three product lines, Avance, AxoGuard Nerve Connector and AxoGuard Nerve Protector, as well as new product introductions such as the AcroVal neurosensory and motor testing system (slated for launch in March), as well as the expanded sales force, currently at 41 reps as compared to 29 at the start of last year. Operating cash burn for 2016E is estimated to be \$7-\$8 million before capital expenditures, well within the range of current cash balances on hand.

3) Going forward, AxoGen investors can look forward to more of the same initiatives from 2015 to drive improved results and enthusiasm in 2016. Most recently, AxoGen hosted a well-attended panel discussion (over 100 surgeons) on nerve repair practice at the American Association of Hand Surgeons conference in January. After sponsoring nine professional educational programs in 2015, up from four in 2014, AxoGen is planning to sponsor twelve such seminars in 2016, focusing on the review of the latest science and best practices in surgical nerve repair. Similarly, the Company plans to continue to grow its sales force, with a target of 45-50 reps in place by the end of this year. Finally, AxoGen continues to make progress on its RANGER study, with 815 Avance nerve repair procedures now enrolled in the multi-center observational study of surgical repair of peripheral nerve discontinuities, and the Company has also started enrollment (June 2015) in the RECON study, a 150-patient, multicenter study comparing Avance Nerve Graft to nerve cuffs in peripheral nerve repair, which is expected to be the pivotal study to support the Company's Biologics License Application.

Conclusion/Stock Valuation

With a bolstered balance sheet, solid intellectual property, a diverse and growing product portfolio, and rapidly increasing revenues in a growing market in a well-placed medical area, AxoGen shares have much to offer to both value- and growth-oriented investors. AXGN shares have held steady this spring after reaching and exceeding our initial \$5 price target in 2015, due to strong revenue growth and positive reaction to a new investment from venture fund Essex Woodlands, which included the addition of one representative from the firm on AxoGen's Board of Directors. Still, continued revenue growth expected for this year and improved bottom-line results may keep AXGN shares on their recent upward trajectory, and thus we are maintaining our Buy rating on AXGN shares and our 12-18 month price target of \$6.00 per share. (For a complete description of our stock valuation analysis please see our Initiation report dated May 13, 2014 and Company Update dated September 1, 2015)

Catalysts/Investor Timeline

- 1) Q1/2016 (March) quarterly earnings announcement – early-May 2016
- 2) New product strategic alliances – Ongoing 2016-17
- 3) Upcoming Conferences – University of Florida Celebration of Innovation Startup Showcase (March 2016)
- 4) New product line extensions - Ongoing 2016-17
- 5) Continuation of clinical studies and initiation of new RECON study – Ongoing 2016-17

Risk Factors

In addition to normal economic and market risk factors that impact most equities and the common risks shared by AxoGen with other companies in the industry, we believe an investment in AXGN involves the following risks:

- **Reliance on key management** – At present, AxoGen relies on several key members of its management team who either founded the Company or have been in key executive positions for an extended period of time. Should one or more of these key executives leave the Company, AXGN could find it difficult to replace their long-standing knowledge of operations and industry expertise.
- **Reliance on government funded-programs** - Currently, AxoGen relies on various government-funded programs, including Medicare and Medicaid, to provide funding for its customer base. However, for the past several years the US Congress and Executive branch have considered several initiatives to change healthcare reimbursement rates and processes, and there can be no assurance in the future that current reimbursement rates for many types of medical products are not reduced or even eliminated.
- **Limited stock liquidity** – Trading volume in AXGN stock is comparatively light and these shares have a relatively limited history of trading compared with other healthcare stocks. As such, news regarding AXGN, its target market, partners and/or competitors could lead to significant volatility in the stock price.
- **Competitive Markets** – The Company competes in its target medical products markets with a number of companies, many of which are considerably larger than the Company. There can be no assurance that the Company will be able to successfully compete and launch new products into these competitive markets in the future.
- **FDA and regulatory risks** - AxoGen is subject to regulatory review for its ongoing research and development activities, principally the US Food and Drug Administration’s 510(k) and BLA application processes. In addition, the quality assurance and assembly of the Company’s medical products are subject to ongoing oversight and regulation, and any negative correspondence from the FDA could have an adverse effect on the ongoing operations of the Company.
- **Lack of historic profitability** - AxoGen has not achieved operating profitability on an annual basis for several years, and according to our forecasts is not expected to do so in the near future. Although the Company maintains adequate cash reserves at the present time, there can be no assurance the Company will not need to raise additional working capital in the future should these operating losses continue. In addition, the Company has a long-term liability to Three Peaks Capital related to an earlier investment, and must also forward cash royalties to Three Peaks in the near future.
- **Need to defend patents and other intellectual property** – AxoGen currently holds 6 US and 3 International patents on its products, some of which expire as soon as 2021. The Company may be required to defend its patents in the US and overseas in the future, and there can be no assurance these defenses will be successful.

Axogen, Inc.
Consolidated Statements of Income
 (In 000s, except per share data)

Calendar Year	2010	2011	2012	2013	2014	1Q15	2Q15	3Q15	4Q15	2015	1Q16E	2Q16E	3Q16E	4Q16E	2016E
Revenues	\$3,004	\$4,849	\$7,692	\$10,947	\$16,817	\$4,951	\$6,417	\$8,154	\$7,809	\$27,331	\$7,670	\$9,310	\$11,540	\$11,130	\$39,650
Cost of goods sold	1,379	2,427	1,962	2,440	3,442	983	1,040	1,410	1,415	4,848	1,610	1,960	2,540	2,390	8,500
Gross Profit	1,626	2,423	5,730	8,508	13,375	3,968	5,377	6,743	6,394	22,483	6,060	7,350	9,000	8,740	31,150
Costs and expenses															
Sales and marketing	3,007	4,379	6,884	10,259	13,194	3,933	4,812	5,513	5,832	20,089	5,500	5,700	5,900	6,100	23,200
Research and development	436	697	1,427	2,125	3,033	671	736	936	894	3,237	850	900	950	1,000	3,700
General and administrative	2,664	4,316	5,221	5,715	6,949	1,909	1,982	2,212	2,320	8,423	2,300	2,350	2,400	2,450	9,500
Total costs and expenses	6,107	9,392	13,532	18,100	23,176	6,512	7,531	8,661	9,046	31,749	8,650	8,950	9,250	9,550	36,400
Operating income (loss)	(4,482)	(6,969)	(7,802)	(9,592)	(9,801)	(2,544)	(2,153)	(1,918)	(2,652)	(9,267)	(2,590)	(1,600)	(250)	(810)	(5,250)
Other (income) expense															
Interest expense, net	(814)	(1,095)	(1,391)	(4,820)	(6,812)	(995)	(1,024)	(1,042)	(928)	(3,989)	(900)	(920)	(940)	(960)	(3,720)
Interest expense - deferred financing	(1,322)	(1,223)	(987)	(179)	(1,101)	(34)	(31)	(31)	(32)	(128)	(30)	(30)	(30)	(30)	(120)
Other income	1,196	67	24	34	3	(3)	17	13	(0)	27	10	10	10	10	40
Total other income (expense)	(941)	(2,250)	(2,354)	(4,965)	(7,910)	(1,031)	(1,038)	(1,061)	(960)	(4,090)	(920)	(940)	(960)	(980)	(3,800)
Income (loss) before tax	(5,423)	(9,219)	(10,156)	(14,557)	(17,710)	(3,575)	(3,191)	(2,979)	(3,611)	(13,356)	(3,510)	(2,540)	(1,210)	(1,790)	(9,050)
Income tax expense (benefit)	0	0	738												
Net income (loss)	(5,423)	(9,219)	(9,418)	(14,557)	(17,710)	(3,575)	(3,191)	(2,979)	(3,611)	(13,356)	(3,510)	(2,540)	(1,210)	(1,790)	(9,050)
Preferred stock dividends	(1,566)	(1,028)													
Net income (loss) available to common	(6,989)	(10,248)	(9,418)	(14,557)	(17,710)	(3,575)	(3,191)	(2,979)	(3,611)	(13,356)	(3,510)	(2,540)	(1,210)	(1,790)	(9,050)
Basic income per share	(\$8.35)	(\$2.77)	(\$0.85)	(\$1.08)	(\$1.00)	(\$0.16)	(\$0.13)	(\$0.11)	(\$0.12)	(\$0.51)	(\$0.12)	(\$0.08)	(\$0.04)	(\$0.06)	(\$0.30)
Diluted income per share	(\$8.35)	(\$2.77)	(\$0.85)	(\$1.08)	(\$1.00)	(\$0.16)	(\$0.13)	(\$0.11)	(\$0.12)	(\$0.51)	(\$0.12)	(\$0.08)	(\$0.04)	(\$0.06)	(\$0.30)
Basic shares outstanding	837	3,697	11,089	13,500	17,722	22,517	24,938	26,841	30,010	26,077	30,000	30,100	30,200	30,300	30,150
Diluted shares outstanding	837	3,697	11,089	13,500	17,722	22,517	24,938	26,841	30,010	26,077	30,000	30,100	30,200	30,300	30,150
Key ratios:															
Revenue growth		61.4%	58.6%	42.3%	53.6%	57.8%	52.3%	74.5%	62.9%	62.5%	55.0%	45.0%	41.5%	42.5%	45.1%
Gross margin	54.1%	50.0%	74.5%	77.7%	79.5%	80.1%	83.8%	82.7%	81.9%	82.3%	79.0%	79.0%	78.0%	78.5%	78.6%
Sales & marketing/revenue	100.1%	90.3%	89.5%	93.7%	78.5%	79.4%	75.0%	67.6%	74.7%	73.5%	65.0%	65.0%	65.0%	65.0%	60.0%
R&D/revenue	14.5%	14.4%	18.6%	19.4%	18.0%	13.6%	11.5%	11.5%	11.4%	11.8%	11.1%	9.7%	8.2%	9.0%	9.3%
General & admin/revenue	88.7%	89.0%	67.9%	52.2%	41.3%	38.5%	30.9%	27.1%	29.7%	30.8%	30.0%	25.2%	20.8%	22.0%	24.0%
Tax Rate	0.0%	0.0%	-7.3%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
Deprec, amort & non-cash comp.	1,970	1,850	1,322	1,050	2,316	600	400	400	300	1,700	450	450	450	450	1,800
Cash Flow/share	(\$4.13)	(\$1.99)	(\$0.80)	(\$1.00)	(\$0.87)	(\$0.13)	(\$0.11)	(\$0.10)	(\$0.11)	(\$0.45)	(\$0.10)	(\$0.07)	(\$0.03)	(\$0.04)	(\$0.24)
EBITDA/share	(\$1.57)	(\$1.37)	(\$0.52)	(\$0.63)	(\$0.42)	(\$0.09)	(\$0.07)	(\$0.06)	(\$0.08)	(\$0.29)	(\$0.07)	(\$0.04)	\$0.01	(\$0.01)	(\$0.11)

Balance Sheets

	(S000s)	
Assets:	12/31/14	12/31/15
Cash and equivalents	\$8,216	\$25,910
Accounts receivable, net	2,872	4,783
Inventory	3,214	3,934
Prepaid expenses & other	109	425
Total current	14,411	35,051
Property, plant & equip., net	619	971
Intangible assets, net	577	678
Deferred financing costs & other	793	846
TOTAL ASSETS	\$16,401	\$37,546
Liabilities:		
Accounts payable and accrued expenses	\$2,431	\$3,695
Current portion of deferred revenue	14	14
Total current	2,445	3,709
Note Payable	25,086	25,547
Long-term portion of deferred revenue	115	94
Total liabilities	27,646	29,350
Stockholders' equity	(11,246)	8,196
TOTAL LIAB & EQ	\$16,401	\$37,546

Quarterly Earnings Comparisons

	March	June	Septem	Decem	Total
Revenues (in \$Mill)					
2010					3,004
2011	1,121	1,225	1,140	1,361	4,849
2012	1,653	2,013	1,981	2,044	7,692
2013	2,143	2,862	2,957	2,985	10,947
2014	3,138	4,214	4,671	4,794	16,817
2015	4,951	6,417	8,154	7,809	27,331
2016E	7,670	9,310	11,540	11,130	39,650
Earnings per Share (diluted)					
2010	(\$0.06)	(\$0.05)	(\$5.32)	(\$5.32)	(\$8.35)
2011	(2.21)	(1.65)	(2.63)	(2.63)	(2.77)
2012	(0.19)	(0.09)	(0.21)	(0.36)	(0.85)
2013	(0.31)	(0.31)	(0.25)	(0.24)	(1.08)
2014	(0.24)	(0.21)	(0.19)	(0.35)	(1.00)
2015	(0.16)	(0.13)	(0.11)	(0.12)	(0.51)
2016E	(0.12)	(0.08)	(0.04)	(0.06)	(0.30)

Source: Dawson James Securities, Inc. estimates; Company documents

Important Disclosures:

Price Chart:



Price target and ratings changes over the past 3 years:

Initiated – May 13, 2014 – Price Target \$5.00

Updated – September 1, 2015 – Price Target increased to \$6.00

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Ratings Distribution	Company Coverage		Investment Banking	
	# of Companies	% of Total	# of Companies	% of Totals
Market Outperform (Buy)	16	67%	10	63%
Market Perform (Neutral)	8	33%	6	75%
Market Underperform (Sell)	0	0%	0	0%
Total	24	100%	16	67%

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