

August 22, 2019

OUTPERFORM

Danielle Antalfy
(212) 277-6044
danielle.antalfy@svbleerink.com

Rebecca Wang
(212) 277-6087
rebecca.wang@svbleerink.com



Reason for report:

PROPRIETARY INSIGHTS

TANDEM DIABETES CARE, INC.

Management Mtgs. Suggest Runway for Growth to Continue Into 2020 and Beyond

• **Bottom Line:** This week, we hosted investor meetings with TNDM CEO John Sheridan and CFO Leigh Vosseller. Based on the stock's performance over the last 3 months – basically flat despite beating sales by over \$40M (35% upside surprise YTD) through 2Q19 – it seems clear that investors are shifting focus to the 2020 outlook. This too was very much in focus at the majority of our meetings, along with potentially changing competitive dynamics as MDT (MP) expects to bring the 780G to market by the end of their FY2020 (early CY2020). **But probably the number one, very consistent takeaway throughout the meetings was that management seems confident that the same – if not stronger – growth drivers will be in place in 2020 that have driven growth in 2019.** These include: (1) First and foremost Control.IQ, which CEO Sheridan has said as recently as our Leadership Series call ([LINK](#)) should “definitely” drive another inflection once it receives approval in late 2019; (2) International, which – while the Animas tailwind seems to have largely lapsed – is only just now seeing Basal.IQ launch; and (3) Renewals, which continue to ramp, with TNDM highly focused on pushing up the rate to 70% eventually – in line with the industry standard more broadly – from what we believe are mid-40% levels today. And beyond these TNDM-specific growth drivers, these meetings also left us reinforced in our view that insulin pump market growth continues to accelerate, with TNDM management noting their rough math suggests new patients to pump are on pace to double this year vs. what has been a steady number historically. **Overall, we do think investor fears around difficult y/y comps in 2020 based on the strong YTD performance has created an opportunity. While the law of large numbers is likely to drive y/y growth deceleration, we see no signs from management – or the market – that adoption momentum is slowing. With Control.IQ likely to attract even more patients new to pump therapy – as well as accelerate competitive conversions – we think our and Street 2020 sales growth projections of 23% and 25% look not only achievable but very beatable.**

• **Reiterate OP, PT \$83.** Over the next 12 months, we believe TNDM shares can trade to \$83. Our DCF arrives at a 12-month valuation of ~\$83, while our comparable company analysis arrives at a 12-month valuation in the \$76-\$90 range. Our \$83 valuation applies a ~10x-11x EV/sales multiple to our \$447.6M FY2020 sales estimate, assuming a stable multiple from the current level at just over ~10x EV/2019E sales. This represents a premium to what we view as a comparable higher-growth small-cap MedTech group – currently trading at ~7x-8x 2019 sales estimates. We believe a top-tier growth profile and a clear pathway to profitability support a valuation in this ~10x-11x EV/sales range.

• **Continued Inside...**

Dec Yr	1Q	2Q	3Q	4Q	FY Rev	1Q	2Q	3Q	4Q	FY EPS	P/E
2018A	\$27.3	\$34.1	\$46.3	\$76.2	\$183.9	(\$1.82)	(\$1.17)	(\$0.62)	\$0.06	(\$2.64)	NM
2019E	\$66.0A	\$93.3A	\$86.2	\$118.9	\$364.4	(\$0.40)A	(\$0.03)A	(\$0.19)	\$0.04	(\$0.56)	NM
2020E	\$90.6	\$106.1	\$109.1	\$141.8	\$447.6	(\$0.08)	\$0.07	\$0.10	\$0.46	\$0.55	NM

Source: Company Information and SVB Leerink LLC Research.

Revenues are in \$M.

GAAP EPS

Key Stats:

(NASDAQ: TNDM)

Sector: Medical Supplies and Devices
S&P 500 Health Care Index: 1,054.96
Price: \$63.09
 Price Target: \$83.00
 Methodology: Discounted Cash Flow + ~10x-11x EV/2020E Sales

52 Week High: \$74.81
 52 Week Low: \$26.40
 Shares Outstanding (mil): 58.2
 Market Capitalization (mil): \$3,671.8
 Book Value/Share: \$2.50
 Cash Per Share: \$2.26
 Net Debt to Total Capital: NA
 Dividend (ann): \$0.00
 Dividend Yield: 0.0%
 Est LT EPS Growth: NA

Completion: August 22, 2019, 5:57AM EDT.
 Distribution: August 22, 2019, 5:57AM EDT.



INVESTMENT THESIS

We rate TNDM shares Outperform with an \$83 12-month price target. We believe that we are currently in an adoption inflection for all diabetes devices – both insulin pumps and CGMs (continuous glucose monitors). We believe TNDM specifically is a major driver of this adoption inflection as the recent t:slim Basal.IQ launch has driven not only higher patient switches from MDT and Animas but is also ramping new patient adds from MDI (multiple daily injection) users. By partnering with a best-in-class CGM in DXCM and developing a differentiated pump platform with remote upgradeability and an easy-to-use touch screen, as well as the company's mid-term commitment to launch one new product per year, we believe TNDM has built an ever-widening competitive moat between itself and the other major durable pump player. This puts TNDM in a position to continue to drive patient switches. Beyond patient switches – which constitute ~50% of TNDM's patient adds – TNDM's ease-of-use and positive Basal.IQ patient experience in successfully managing their diabetes have also driven accelerating adoption among MDIs, which is a dynamic that we see as sustainable for the foreseeable future.

Longer term, we view the pump market opportunity as compelling as it targets a large, growing, and undertreated patient population in diabetics, which we estimate at \$8B worldwide in Type 1s. We believe TNDM is positioned within the Type 1 market to drive not only market share gains via patient switches but also bring new patients onto pump therapy, and there is untapped opportunity in a market we estimate at ~\$4B for insulin-dependent Type 2 with ~10% of TNDM's installed base Type 2. Because of this, we see TNDM as a sustainable, strong double-digit sales grower for the foreseeable future, with even potential for further upside from our 45% projected CAGR over the 2018-2023E timeframe, and we are meaningfully ahead of consensus in the out-years. We believe that much of our above-Street estimates in the out-years is due to what we believe is a key misperception among analysts and investors – we believe insulin pump market growth has accelerated from mid-single-digits previously to now sustainable double-digit growth. And from here, we see potential for even more upside with just modest penetration into Type 1s and only marginal penetration into insulin-dependent Type 2s, with increased adoption driven by continued product evolution, including TNDM's upcoming t:slim Control.IQ launch in 4Q19.

Beyond likely continued estimate upside, TNDM shares could move even higher driven by: 1. Control.IQ launch in 4Q19, which we believe could drive yet another adoption inflection for TNDM; and 2. Continued clinical updates/progress on the next-generation t:sport, expected to launch in 2020, which will eventually have phone control and should help TNDM accelerate further new patient adds from MDI patients and potentially even ramp adoption in insulin-dependent Type 2 patients

Management Meetings Suggest Runway for Growth to Continue Into 2020 and Beyond

This week, we hosted investor meetings with TNDM CEO John Sheridan and CFO Leigh Vosseller. Based on the stock's performance over the last 3 months – basically flat despite beating sales by over \$40M (+35% upside surprise YTD) through 2Q19 – it seems clear that investors are shifting focus to the 2020 outlook. This too was very much in focus at the majority of our meetings, along with potentially changing competitive dynamics as MDT expects to bring the 780G to market by the end of their FY2020 (early CY2020). **But probably the number one, very consistent takeaway throughout the meetings was that management seems confident that the same – if not stronger – growth drivers will be in place in 2020 that have driven growth in 2019.** These include:

1. First and foremost Control.IQ, which CEO Sheridan has said as recently as our Leadership Series call ([LINK](#)) should “definitely” drive another inflection once it receives approval in late 2019;
2. International, which – while the Animas tailwind seems to have largely lapsed – is only just now seeing Basal.IQ launch; and
3. Renewals, which continue to ramp, with TNDM highly focused on pushing up the rate to 70% eventually – in line with the industry standard more broadly – from what we believe are mid-40% levels today.

And beyond these TNDM-specific growth drivers, these meetings also left us reinforced in our view that insulin pump market growth continues to accelerate, with TNDM management noting their rough math suggests new patients to pump are on pace to double this year vs. what has been a steady number historically. **Overall, we do think investor fears around difficult y/y comps in 2020 based on the strong YTD performance has created an opportunity. While the law of large numbers is likely to drive y/y growth deceleration, we see no signs from management – or the market – that adoption momentum is slowing. With Control.IQ likely to attract even more patients new to pump therapy – as well as accelerate competitive conversions – we think our and Street 2020 sales growth projections of 23% and 25% look not only achievable but very beatable.**

Focus on 2020 Outlook Shows No Signs of Slowing Momentum

TNDM management was adamant that the 2020 outlook is just as good as what we've seen in 2019, if not “arguably better”, according to CEO Sheridan. One misconception management highlighted that seems to be a major driver of increasing investor anxiety of the 2020 growth potential is the contribution of Animas to recent outperformance, as the Animas tailwind will likely significantly mitigate in 2H19 and into 2020. But management noted that, while Animas did double over the last 12-18 months vs. historical, the percentage of total shipments for Animas did not change, implying that both patients new to pump therapy and MDT conversions also grew at a similarly proportionate rate. The former is particularly meaningful, in our view, as it to us represents the strongest leading indicator for sustainable strong double-digit growth longer-term.

Management noted that the pump market is seemingly on track to add ~50k patients this year vs. ~25k each year on average historically, and technology is only improving while awareness is only growing from here, pointing to what we believe should be continued momentum on this front.

From a competitive and pipeline standpoint, TNDM pointed to their calling card – ease of use – as a key differentiator and competitive moat as it relates to not only current technology on the market, specifically MDT's 670G, but also future technology with the upcoming 780G launch. Accuracy is also a key driver, with management noting that Control.IQ data that we saw at the ADA (American Diabetes Association) meeting earlier this year demonstrating TIR (Time in Range) of 71% was highly representative of real-world performance given that the study was run by the NIH, outside of TNDM's purview and control. Because of this, TNDM noted that anecdotal physician feedback is very positive, which jives with what we heard from MEDACorp physicians and diabetes nurse educators at ADA. Management noted several times that with Basal.IQ, they've been able to penetrate accounts this year that they'd never had access to previously because they were MDT strongholds – something that we think could point to an opportunity for TNDM to also accelerate competitive conversions from MDT with Control.IQ. And beyond the upcoming Control.IQ launch, TNDM continues to expect to launch t:sport in late 2020 with an ACE designation, which management believes will enable the company to compete more effectively vs. PODD (OP) with a much smaller, wearable footprint that retains the ease of use and accuracy of Control.IQ. Lastly on this front, TNDM noted that they will continue to innovate Control.IQ to improve performance and ease of use even further.

Other key 2020 and beyond growth drivers noted include:

1. International, with Basal.IQ only just now launching, and management pointing to the inflection this product drove in the U.S. as a potential proxy for the impact it could have in Europe. Now with the Animas backlog largely worked through internationally, TNDM noted they are now developing distributor relationships outside of Animas to start really building an organic business.
2. Renewals, which came up much less frequently in these meetings, but which to us represent one of the most compelling aspects of the story longer-term given their ability to de-risk future revenue streams ([LINK](#)).

Margin Expansion Also in Focus, Cash Flow Positive Starting in 2H19

Management reiterated their goal of 25% operating margins longer-term, i.e., over the next 5 years. Gross margin expansion – to 55% exiting 2019E – represents a key component of this, with CFO Vosseller pointing to the following near-to-medium term drivers:

1. **Capacity utilization. TNDM tripled output last year so the company was very much focused on expanding manufacturing and the labor force. Now the company is shifting focus to accelerating cycle times and improving yields, which is the first piece of the gross margin expansion story;**

2. T:sport, which has a cartridge designed to reduce COGS. TNDM plans to freeze the design by year-end, with regulatory and clinical testing to begin early next year, and submission as an ACE pump designation that should accelerate the timeline to approval by ~9 months, meaning t:sport could hit the market by late 2020; and
3. Ongoing shift to direct, with management expecting to reach 50%/50% direct/distributor eventually within the U.S. business vs. 25%/75% today. Not only does the shift to direct drive a modest increase in revenue, more importantly CFO Vosseller noted it will drive natural efficiencies in terms of service and support, including TNDM having more direct access to the patient over the pump's 4-year lifespan, potentially leading to higher renewal rates. Once direct with a payer, TNDM can also negotiate with each payer on possible outcomes-based payments, with the goal of the benefits accruing to TNDM.
4. At a higher level, TNDM is also looking to reduce costs across all customer-facing functions, as evidenced by the recent announcement of a Boise facility opening to expand these teams at a lower cost of labor, on average, as well as looking at things like creative, lower-cost ways for training, to name a few.

VALUATION

Over the next 12 months, we believe TNDM shares can trade to \$83. We arrive at this valuation using both a discounted cash flow (DCF) and comparable company EV/sales analysis. Our DCF arrives at a 12-month valuation of ~\$83, while our comparable company analysis arrives at a 12-month valuation in the \$76-\$90 range. Our \$83 valuation applies a ~10x-11x EV/sales multiple to our \$447.6M FY2020 sales estimate, assuming a stable multiple from the current level at just over ~10x EV/2019E sales. This represents a premium to what we view as a comparable higher growth small-cap MedTech group – currently trading at ~7x-8x 2019 sales estimates (ATRC, AXGN, AVDR, DXCM, INGN, PODD). We believe a top-tier growth profile and a clear pathway to profitability support a valuation in this ~10x-11x EV/sales range, especially given that the financial overhang is now removed, as a result of 2018 equity raises and an improved free cash flow picture.

RISKS TO VALUATION

Risks to TNDM shares include: (1) Increasing competition in pump market; (2) failure to drive further operating leverage; and (3) failure to execute in driving insulin pump penetration.

Disclosures Appendix

Analyst Certification

I, Danielle Antalffy, certify that the views expressed in this report accurately reflect my views and that no part of my compensation was, is, or will be directly related to the specific recommendation or views contained in this report.

Rating	Count	Percent	Distribution of Ratings/Investment Banking Services (IB) as of 06/30/19	
			IB Serv./Past 12 Mos.	
			Count	Percent
BUY [OP]	161	70.9	55	34.2
HOLD [MP]	62	27.3	2	3.2
SELL [UP]	4	1.8	0	0.0

Explanation of Ratings

Outperform (Buy): We expect this stock to outperform its benchmark over the next 12 months.

Market Perform (Hold/Neutral): We expect this stock to perform in line with its benchmark over the next 12 months.

Underperform (Sell): We expect this stock to underperform its benchmark over the next 12 months.

The degree of outperformance or underperformance required to warrant an Outperform or an Underperform rating should be commensurate with the risk profile of the company.

For the purposes of these definitions the relevant benchmark will be the S&P 600[®] Health Care Index for issuers with a market capitalization of less than \$2 billion and the S&P 500[®] Health Care Index for issuers with a market capitalization over \$2 billion.

Important Disclosures

This information (including, but not limited to, prices, quotes and statistics) has been obtained from sources that we believe reliable, but we do not represent that it is accurate or complete and it should not be relied upon as such. All information is subject to change without notice. The information is intended for Institutional Use Only and is not an offer to sell or a solicitation to buy any product to which this information relates. SVB Leerink LLC (“Firm”), its officers, directors, employees, proprietary accounts and affiliates may have a position, long or short, in the securities referred to in this report, and/or other related securities, and from time to time may increase or decrease the position or express a view that is contrary to that contained in this report. The Firm’s research analysts, salespeople, traders and other professionals may provide oral or written market commentary or trading strategies that are contrary to opinions expressed in this report. The Firm’s asset management group and proprietary accounts may make investment decisions that are inconsistent with the opinions expressed in this document. The past performance of securities does not guarantee or predict future performance. Transaction strategies described herein may not be suitable for all investors. This document may not be reproduced or circulated without SVB Leerink’s written authority. Additional information is available upon request by contacting the Editorial Department, SVB Leerink LLC, One Federal Street, 37th Floor, Boston, MA 02110.

Like all Firm employees, research analysts receive compensation that is impacted by, among other factors, overall firm profitability, which includes revenues from, among other business units, Institutional Equities, Research, and Investment Banking. Research analysts, however, are not compensated for a specific investment banking services transaction. To the extent SVB Leerink research reports are referenced in this material, they are either attached hereto or information about these companies, including prices, rating, market making status, price charts, compensation disclosures, Analyst Certifications, etc. is available on <https://svbleerink.bluematrix.com/bluematrix/Disclosure2>.

MEDACorp is a network of healthcare professionals, attorneys, physicians, key opinion leaders, and other specialists accessed by SVB Leerink LLC and its clients.

For price charts, statements of valuation and risk, as well as the specific disclosures for covered companies, client should refer to <https://leerink2.bluematrix.com/bluematrix/Disclosure2> or send a request to SVB Leerink LLC Editorial Department, One Federal Street, 37th Floor, Boston, MA 02110.

© 2019 SVB Leerink LLC. All Rights Reserved. Member FINRA/SIPC. SVB Leerink LLC is a member of SVB Financial Group.

RESEARCH MANAGEMENT

John L. Sullivan, CFA
Director of Equity Research
(617) 918-4875
john.sullivan@svbleerink.com

Jim Kelly
Associate Director of Research
(212) 277-6096
jim.kelly@svbleerink.com

Geoffrey C. Porges, MBBS
Director of Therapeutics Research
(212) 277-6092
geoffrey.porges@svbleerink.com

Christian Clark
Vice President
(212) 277-6117
christian.clark@svbleerink.com

DIVERSIFIED BIOTECHNOLOGY

Geoffrey C. Porges, MBBS
(212) 277-6092
geoffrey.porges@svbleerink.com

Bradley Canino, CPA
(212) 277-6158
bradley.canino@svbleerink.com

Neil Puri, M.D., MBA
(212) 277-6139
neil.puri@svbleerink.com

Ke (Andrew) Yuan, CFA, CPA
(212) 277-6147
ke.yuan@svbleerink.com

TARGETED ONCOLOGY

Andrew Berens, M.D.
(212) 277-6108
andrew.berens@svbleerink.com

Thomas J. Smith
(212) 277-6069
thomas.smith@svbleerink.com

Gang Li, Ph.D.
(212) 277-6185
gang.li@svbleerink.com

IMMUNO-ONCOLOGY

Daina M. Graybosch, Ph.D.
(212) 277-6128
daina.graybosch@svbleerink.com

Dilip Joseph
(212) 277-6148
dilip.joseph@svbleerink.com

David B. Iaea, Ph.D.
(212) 277-6155
david.iaea@svbleerink.com

EMERGING ONCOLOGY

Jonathan Chang, Ph.D., CFA
(617) 918-4015
jonathan.chang@svbleerink.com

John C. Barrett, Ph.D.
(617) 918-4039
john.barrett@svbleerink.com

David Ruch
(617) 918-4817
david.ruch@svbleerink.com

GENETIC MEDICINE

Mani Foroohar, M.D.
(212) 277-6089
mani.foroohar@svbleerink.com

Rick Bienkowski, Ph.D.
(212) 277-6109
rick.bienkowski@svbleerink.com

Aravinda Kuntimaddi, Ph.D.
(212) 277-6148
aravinda.kuntimaddi@svbleerink.com

IMMUNOLOGY & METABOLISM

Pasha Sarraf, M.D., Ph.D.
(212) 277-6013
pasha.sarraf@svbleerink.com

Mike Kratky, CFA
(212) 277-6192
mike.kratky@svbleerink.com

Dylan Dupuis, Ph.D.
(212) 277-6151
dylan.dupuis@svbleerink.com

NEUROSCIENCE

Marc Goodman
(212) 277-6137
marc.goodman@svbleerink.com

Roanna Ruiz, Ph.D.
(212) 277-6144
roanna.ruiz@svbleerink.com

Rudy Li, Ph.D.
(212) 277-6127
rudy.li@svbleerink.com

RARE DISEASE

Joseph P. Schwartz
(617) 918-4575
joseph.schwartz@svbleerink.com

Dae Gon Ha, Ph.D.
(617) 918-4093
daegon.ha@svbleerink.com

Joori Park, Ph.D.
(617) 918-4098
joori.park@svbleerink.com

GENERICS, INFECTIOUS DISEASE, PAIN, WOMEN'S HEALTH, OTHER THERAPEUTICS

Ami Fadia
(212) 277-6047
ami.fadia@svbleerink.com

Eason Lee
(212) 277-6070
eason.lee@svbleerink.com

Sheldon Fan, Ph.D.
(212) 277-6074
sheldon.fan@svbleerink.com

LIFE SCIENCE TOOLS & DIAGNOSTICS

Puneet Souda
(212) 277-6091
puneet.souda@svbleerink.com

Westley Dupray
(617) 918-4549
westley.dupray@svbleerink.com

Scott Mafale
(212) 277-6107
scott.mafale@svbleerink.com

MEDICAL DEVICES, CARDIOLOGY

Danielle Antalffy
(212) 277-6044
danielle.antalffy@svbleerink.com

Rebecca Wang
(212) 277-6087
rebecca.wang@svbleerink.com

MEDICAL DEVICES, ORTHOPEDICS

Richard Newitter
(212) 277-6088
richard.newitter@svbleerink.com

Jaime L. Morgan
(212) 277-6073
jaime.morgan@svbleerink.com

EMERGING HEALTHCARE TECHNOLOGIES

Daniel Grosslight
(212) 277-6140
daniel.grosslight@svbleerink.com

EDITORIAL

SR. EDITOR/SUPERVISORY ANALYST

Mary Ellen Eagan, CFA
(617) 918-4837
maryellen.eagan@svbleerink.com

SUPERVISORY ANALYSTS

Randy Brougher
randy.brougher@svbleerink.com

Robert Egan
bob.egan@svbleerink.com

Amy N. Sonne
amy.sonne@svbleerink.com

EDITORIAL ASSOCIATE

Emily Singletary
(212) 277-6115
emily.singletary@svbleerink.com