

Cepheid Inc

(CPHD-NASDAQ)

CPHD: Hold Zacks Company Report

Current Recommendation	Hold
Prior Recommendation	N/A
Date of Last Change	10/11/2004
Current Price (03/13/08)	\$24.11
Six- Month Target Price	\$26.00

OUTLOOK

CPHD reported Q4 EPS that were \$0.02 lower than our estimate on revenue that exceeded our forecast. We increased our FY08 revenue estimate to within the initial management guidance but lowered our FY08 EPS estimate. For the entire 2008 year, the company expects to be profitable excluding stock compensation and amortization of acquired intangibles. We initiated FY09 estimates. The company is focused in driving growth primarily by penetrating further in the clinical market and launching new products. Our price target is based on a price-to-revenue multiple of roughly 7.9x our 2008 revenue estimate.

SUMMARY DATA

52-Week High	\$32.34
52-Week Low	\$8.50
One-Year Return (%)	178.41
Beta	1.89
Average Daily Volume (sh)	1,513,670

Shares Outstanding (mil)	55.9
Market Capitalization (\$mil)	\$1,348
Short Interest Ratio (days)	7.96
Institutional Ownership (%)	81
Insider Ownership (%)	5

Annual Cash Dividend	\$0.00
Dividend Yield (%)	0.00

5-Yr. Historical Growth Rates	
Sales (%)	57.6
Earnings Per Share (%)	N/A
Dividend (%)	N/A

P/E using TTM EPS	N/A
P/E using 2008 Estimate	N/A
P/E using 2009 Estimate	N/A

Zacks Rank	3
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Risk Level	High
Type of Stock	Mid-Growth
Industry	Med Instruments
Zacks Rank in Industry	30 of 42

ZACKS ESTIMATES

Revenue

(in millions of \$)

	Q1	Q2	Q3	Q4	Year
	(Mar)	(Jun)	(Sep)	(Dec)	(Dec)
2006	20 A	20 A	24 A	24 A	87 A
2007	26 A	27 A	36 A	40 A	129 A
2008	41 E	44 E	47 E	54 E	186 E
2009					238 E

Earnings per Share

(EPS is operating earnings before non recurring items)

	Q1	Q2	Q3	Q4	Year
	(Mar)	(Jun)	(Sep)	(Dec)	(Dec)
2006	-\$0.15 A	-\$0.13 A	-\$0.07 A	-\$0.09 A	-\$0.43 A
2007	-\$0.11 A	-\$0.10 A	-\$0.09 A	-\$0.10 A	-\$0.39 A
2008	-\$0.08 E	-\$0.07 E	-\$0.04 E	-\$0.02 E	-\$0.21 E
2009					\$0.07 E

Note: Our EPS estimates include expected stock option expense. Our historicals prior to 2006 exclude the expense.

Zacks Projected EPS Growth Rate - Next 5 Years %	15
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OVERVIEW

Cepheid is a molecular diagnostics company that develops, manufactures, and markets fully-integrated systems for genetic analysis in the clinical molecular diagnostic, industrial, and biothreat markets. These systems enable rapid, sophisticated molecular testing for organisms and genetic-based diseases by automating otherwise complex manual laboratory procedures. Molecular testing involves a number of complicated and time-intensive steps, including sample preparation, DNA amplification, and detection. Cepheid's easy-to-use systems integrate these steps and analyze complex biological samples. The company is focusing efforts on those applications where rapid molecular testing is particularly important, such as identifying infectious disease and cancer in the clinical molecular diagnostic market; food, agricultural and environmental testing in the industrial market; and identifying bio-terrorism agents in the biothreat market. In 2007, clinical molecular diagnostic, biothreat, and industrial markets contributed 52%, 35%, and 13% respectively to total revenue. The company's initial public offering of stock was on June 21, 2000.

The company derives revenues primarily from the sales of its two instrument platforms and associated reagents and disposables in the clinical molecular diagnostic, industrial, and biothreat markets, and to a lesser extent from contract and government sponsored research. The two principal instrument platforms are the SmartCycler and GeneXpert systems. The SmartCycler system, integrates DNA amplification and detection to allow rapid analysis of a sample. The GeneXpert system integrates automated sample preparation with the SmartCycler DNA amplification and detection technology. The GeneXpert system, a closed, self-contained, fully-integrated and automated system, represents a paradigm shift in the automation of molecular analysis, producing accurate results in a timely manner with minimal risk of contamination. The GeneXpert system can provide rapid results with superior test specificity and sensitivity over comparable systems on the market today that are integrated but have open architectures. In 2007, instrument sales, reagent/disposable sales, contract revenue, and grant/government sponsored research revenue contributed 37%, 53%, 7%, and 3% respectively to total revenue.

BULL STORY

Revenue growth in past periods was driven by the substantial revenue contributions from the USPS BDS program in the Biothreat market. Before this program, revenue growth was driven by sales of tests and disposables for the SmartCycler System in the clinical molecular diagnostic market and industrial market. The company began shipping GeneXpert modules and anthrax test cartridges in the fourth quarter 2003 for incorporation into the Biohazard Detection System (BDS) developed by a Northrop Grumman-led consortium that includes Cepheid for use by the United States Postal Service (USPS) for the detection of anthrax. The GeneXpert module is an automated system for sample preparation, amplification, and detection from raw biological samples designed for integration into larger biodetection systems. This consortium was awarded a production contract wherein BDS installations were completed at the end of 2005. The company launched the GeneXpert system for stand-alone use in the biothreat market in the third quarter 2004. On August 16, 2007, the company announced that it completed a 5 year agreement to sell anthrax test cartridges to Northrop Grumman that begins with the USPS fiscal year of October 1, 2007 and thus ends on September 30, 2011.

Since 2006, revenue growth primarily has been driven by the launch of tests in the clinical molecular diagnostic market. The company is focused on driving this growth primarily through the GeneXpert system. Tests have been launched on the GeneXpert and SmartCycler systems. After initially launching in Europe, the company has been successfully expanding in the U.S. clinical market.

The company began this launch in the clinical market with the European introduction as CE IVD Mark products the GeneXpert system and Xpert BCR-ABL Monitor test in February 2006 and successfully launched other tests thereafter. BCR-ABL serves as an abnormal genetic marker used to detect patients with Chronic Myelogenous Leukemia (CML). The company during the second quarter 2006 launched the

Xpert GBS test as a CE IVD Mark product in Europe. Physicians use this test to rapidly detect Group B Streptococcus in antepartum and intrapartum women. In May 2006, the company launched the Smart EBV test as a CE IVD Mark product in Europe for the SmartCycler system. The EBV test is used to rapidly detect and quantify Epstein-Barr Virus viral load. Many diseases are associated with EBV infection. The EBV test serves as a first test launched to manage immunocompromised patients. During the second quarter 2006, the company launched another CE Mark certified test, the Smart VZV in vitro diagnostic test for the SmartCycler system. The Smart VZV test serves to rapidly detect the varicella-zoster virus, a member of the herpes virus subfamily. The Smart VZV test can serve as a second product in the management of immunocompromised patients. In June 2006, the company launched in Europe the Xpert EV test as a CE IVD Mark product. The EV test helps physicians detect enterovirus associated meningitis. The company subsequently launched during June 2006 the Smart CMV test as a CE IVD Mark product. Cytomegalovirus is a member of the herpes virus family. The CMV test serves to rapidly detect and quantify CMV viral load and can be used as a third product in the management of immunocompromised patients. Late in the second quarter 2006, the company launched the Smart GBS test as a CE IVD Mark product. In October 2006, the company launched the Xpert MRSA test as a CE IVD Mark product used to help in the reduction of hospital acquired infections by detecting Methicillin-resistant Staphylococcus. This release completes the initial European launch of tests for the GeneXpert system. In March 2007, the company launched the Smart HBV test as a CE IVD Mark product used to rapidly detect Hepatitis B Virus viral load. In the fourth quarter 2007, Cepheid launched in Europe combination tests that include Xpert MRSA/SA Blood Cultures (BC) and Xpert MRSA/SA Skin & Soft Tissue Infection (SSTI). Under an exclusive agreement entered into in April 2007 with CPHD, Instrumentation Laboratory began selling on March 4 the Xpert HemosIL FII & FV assay to assess genetic risk of thrombosis (thrombophilia) as a CE IVD Mark product in Europe.

Since the second half of 2006, the company has been successfully expanding in the U.S. clinical market. After filing the 510(k) late in the first quarter 2006, the company received FDA approval and launched the Xpert GBS test in the third quarter 2006. Shortly after the approval in July 2006, the FDA categorized this test for GBS as moderate complexity. This categorization allows in addition to specially trained lab personnel non-laboratory personnel to run the tests. The number of laboratories certified as moderate complexity significantly outnumbers the ones certified as high complexity. Late in the fourth quarter 2006, the company received FDA clearance and launched the Smart GBS test. After filing the 510(k) early in the second quarter 2006, the company received FDA approval and launched the Xpert EV test late in the first quarter 2007. After receiving FDA approval in April 2007, the company launched the Xpert MRSA test in the second quarter 2007. The launch of the Xpert MRSA test completes the initial offering of tests in the U.S. for the GeneXpert system. In May 2007, the FDA categorized the Xpert MRSA test as moderate complexity. MRSA testing volumes have been benefiting from the initiation of MRSA surveillance programs in hospital acquired infection (HAI) initiatives. The most notable HAI is the Veterans Administration (VA) initiative. Legislative action has been supporting the adoption of these initiatives.

Sales growth is also expected to be driven by the acquisition of Sangtec Molecular Diagnostics AB in Bromma, Sweden in February 2007. The acquisition brought a relatively complete line of products for potential use in managing infections of immunocompromised patients. The company estimates the market for the management of infections in the immunocompromised patient population to be approximately \$212 million in the U.S. and \$149 million in Europe. The company has integrated the Sangtec affigene family of Real-time PCR molecular diagnostic products targeted at the immunocompromised market into its existing European and U.S. portfolio of in vitro diagnostic products. The expanded line includes affigene assay kits for CMV, EBV, Herpes Simplex Virus 1 and 2 (HSV), Hepatitis B Virus (HBV), Varicella Zoster Virus (VZV), BK Virus (BKV), and Aspergillus. Plans have been under development for application of these tests to the GeneXpert system. This acquisition also brings to the table an experienced R&D operation to develop and expand the company's clinic test products and a reagent manufacturing base in Europe. Subsequent to the acquisition, Sangtec's name was changed to Cepheid AB.

BEAR STORY

Expansion efforts may prove more expensive than the company currently anticipates, and the company may not succeed in increasing revenue to offset higher expenses. Although clinical product sales are accelerating, industrial product sales may be at risk from decreases in government research funding. The growth in SG&A is expected to be driven from efforts at expanding the sales force and marketing programs. The growth in R&D is expected to be driven from efforts at internally developing and through collaborative programs new tests for the GeneXpert and SmartCycler systems. The acquisition of Actigenics in August 2006 expanded the company's R&D development ability. A leader in the new field of micro RNA technology located in Toulouse, France, Actigenics provides the company new potential test markers. As a result of the acquisition, the company has over 140 validated micro RNA markers that are being evaluated as potential diagnostic markers for use in developing molecular diagnostic tests for cancer and infectious disease applications.

In addition to test development, the company's R&D programs also include systems development. The company developed a GeneXpert 16-Site System that began shipment in the fourth quarter 2006. The GeneXpert family of instruments was recently upgraded to six color multiplex capabilities from four. On January 7, 2008, Cepheid announced the initiation of shipments of this next generation of systems including a portable GX-I single module system. This upgrade allows these instruments to test simultaneously up to 60 targets in a single test cartridge. System development also includes a high volume Infinity Series of GeneXpert Systems with robotic cartridge handling. In the Infinity Series, 48 and 72 module systems were previously expected to be available in mid 2009. The company now expects to ship the 48 system in 2008.

In the U.S., the company has a small but growing sales force that sells products to both the clinical and industrial markets. As a result of the strong growth in the clinical market, the company has been relying on distributors to drive lower margin sales growth in the industrial markets. The company also relies on distributors in selling products in the U.S. biothreat market. In European markets and markets in the rest of the world, the company sells through distributors.

Biothreat sales can fluctuate year to year during the five year agreement Northrop Grumman signed with the company. During the third quarter 2007, Northrop Grumman signed a five-year agreement with Cepheid to purchase up to \$200 million in *Bacillus anthracis* (anthrax) test cartridges and associated materials for use in Biohazard Detection Systems installed at USPS mail processing centers nationwide. Under the agreement, the annual purchase quantity of anthrax tests will be determined prior to initiation of the USPS fiscal year, October 1 through September 30. The company has received a purchase order for approximately two million anthrax test cartridges for the USPS fiscal 2008.

RECENT NEWS

On February 28, 2008, Cepheid announced fourth quarter and year-end results. Total revenue in the quarter increased 71% year-over-year to \$40.4 million from \$23.6 million and grew 48% in 2007 to \$129.5 million from \$87.4 million in 2006. Gross margin on product sales in the quarter was flat year-over-year at 42% and flat in 2007 at 41% compared to 2006. Operating expenses as a percentage of revenue in the quarter fell year-over-year to 53.0% from 59.1% on lower R&D and fell to 56.0% in 2007 from 57.6% in 2006 on lower R&D. Net loss per share in the quarter increased year-over-year to \$0.10 on 55.53 million basic/diluted weighted average shares outstanding from a net loss per share of \$0.09 on 54.93 million basic/diluted weighted average shares outstanding. Net loss per share in 2007 declined to \$0.39 on 55.26 million basic/diluted weighted average shares outstanding from a net loss per share of \$0.43 on 52.33 million basic/diluted weighted average shares outstanding in 2006.

Revenue results by category are as follows. Total product sales in the quarter grew year-over-year to \$36.9 million from \$21.6 million and grew to \$116.5 million in 2007 from \$82.4 million in 2006. Within product sales, instrument sales in the quarter increased year-over-year to \$15.6 million from \$6.9 million

and grew to \$47.7 million in 2007 from \$22.7 million in 2006 while reagent & disposable sales in the quarter grew year-over-year to \$21.3 million from \$14.7 million and increased to \$68.8 million in 2007 from \$59.7 million in 2006. Contract revenue in the quarter grew year-over-year to \$2.7 million from \$1.6 million and grew to \$8.6 million in 2007 from \$3.9 million in 2006. Grant and government sponsored research revenue in the quarter grew year-over-year to \$816,000 from \$341,000 and increased to \$4.4 million in 2007 from \$1.0 million in 2006.

The increase in product sales in the quarter was driven by clinical product sales that grew 260% year-over-year to \$22.2 million from \$6.2 million, which more than offset biothreat sales that fell 2% year-over-year to \$11.4 million from \$11.6 million and industrial sales that decreased 15% year-over-year to \$3.3 million from \$3.8 million. The increase in product sales in 2007 was driven by clinical product sales that grew 211% to \$61.0 million from \$19.6 million in 2006, which more than offset biothreat sales that fell 15% to \$40.8 million from \$48.0 million in 2006 and industrial sales that were roughly flat compared to 2006. The increase in clinical sales was driven by market adoption of both the GeneXpert System and the company's menu of available tests, specifically the Xpert MRSA product. The industrial market segment is now primarily supported by distributors, which results in a lower average selling price for products realized by the company, as compared to prices realized through direct sales. This was the primary driver for the decrease in product sales for the industrial market. The decrease in biothreat sales was the result of a planned decrease in the purchase price of Anthrax test cartridges to the United States Postal Service (USPS) in conjunction with a five-year contract.

Management revealed its initial 2008 guidance. Product sales are expected to be in a \$175-\$180 million range. The MRSA market within the Healthcare-Associated Infections (HAI) market is developing into three segments: surveillance, diagnosis, and pre-surgical testing. The company has expanded its corporate accounts sales program in order to develop other relationships with group purchasing organizations and integrated delivery networks. In the fourth quarter, the company signed a group purchasing contract with Broadlane. In the current or first quarter, Tenet Healthcare selected Cepheid as its vendor of choice for molecular HAI surveillance testing. The company is continuing to accelerate expansion of its U.S. sales and field service support organization based on the rapidly developing HAI market and expects to go direct in the U.K. by the end of the year. Other revenue (contract revenue/grant & government sponsored research revenue) is expected to be in a \$7-\$9 million range. Total revenue is expected to be in a \$182-\$189 million range. Net income excluding the effect of stock compensation expense and the amortization of acquired intangibles is expected to be in the range of \$3-\$5 million.

On February 25, 2008, Cepheid and Instrumentation Laboratory (IL) announced the release of the Xpert HemosIL FII & FV assay as a European CE IVD Mark product under the European Directive on In Vitro Diagnostic Medical Devices. Delivering results in just over thirty minutes with a single GeneXpert cartridge, the Xpert HemosIL FII & FV assay detects Factor II (FII) and Factor V Leiden (FV) genetic variations associated with thrombophilia, an increased risk of blood clots (thrombosis). Developed and manufactured by Cepheid, the test is expected to be available for sale beginning March 4th through IL, the exclusive worldwide distributor for the Xpert HemosIL FII & FV assay. Xpert HemosIL FII & FV is the first test to be commercialized under the exclusive development and distribution agreement for hemostasis molecular diagnostic tests, entered into by IL and Cepheid in April 2007.

FII and FV are the most common hereditary risk factors for venous thrombosis and are key in the determination of genetic predisposition to the condition and the need for prophylactic treatment in high risk patients. The investigation of genetic and acquired defects leading to thrombosis is performed with the aid of both classic coagulation assays and molecular tests. In the past, many of these molecular tests could not be performed in a traditional hospital laboratory. Now, Cepheid's GeneXpert System enables FII and FV molecular tests to be easily performed in the hospital or independent clinical laboratory without the need for batch processing.

On February 11, 2008, Cepheid announced that Andrew D. Miller will be joining Cepheid as Senior Vice President, Chief Financial Officer on April 14, 2008, and will assume responsibility for worldwide financial operations and investor relations. Mr. Miller will report to John L. Bishop, Chief Executive Officer, and replaces John Sluis, who retired from Cepheid effective December 31, 2007.

On January 29, 2008, Cepheid announced that Health Canada has issued a medical device license for the Xpert MRSA test for the rapid detection of Methicillin Resistant Staphylococcus aureus (MRSA) on nasal swabs and the GeneXpert System. Xpert MRSA test results are available in approximately 70 minutes thereby enabling rapid identification of carriers of the potential pathogen in less than two hours, from the acquisition of the patient sample to returning the result to the floor. The availability of the Xpert MRSA test and the GeneXpert System is expected to help enable Canadian healthcare organizations to implement more efficient infection control measures, leading to lower hospital acquired infection rates and improved patient care. Xpert MRSA is Cepheid's second test to receive Health Canada license, following Smart GBS in October of 2007.

As is the situation in the United States, MRSA is a growing public health concern in Canada. According to a study published in the Canadian Journal of Infectious Diseases and Medical Microbiology the rate of MRSA in Canadian hospitals has increased steadily between 1995 and 2004. Patients with MRSA require prolonged hospitalization extending 26 days on average, special control measures, expensive treatments, and extensive surveillance. Canadian infection control officers have recommended that hospitals make prevention of healthcare acquired infections a patient safety priority, and should commit adequate resources to screening and implementation of other preventative measures. According to the March 2007 Ontario Provincial Infectious Disease Advisory Committee (PIDAC) recommendations, high-risk patients, as well as other patients as defined by local epidemiology and risk factors, should be actively screened for MRSA.

Source: Cepheid

VALUATION

At its current price of \$24.11 per share, CPHD is trading at 7.3x our 2008 revenue estimate of \$186 million, which is roughly in-line to the group multiple. At this stage, we believe most of the growth driven by the clinical market has been factored in the stock price. The share price could experience some volatility over the near term due to CPHD's belief that a new study regarding MRSA surveillance published in the Journal of the American Medical Association made unfair conclusions based on suspect testing conditions. We believe CPHD is appropriately valued at roughly a group premium of 7.9x 2008 revenue estimate. Our price target moves to \$26.00.

Industry Comparables

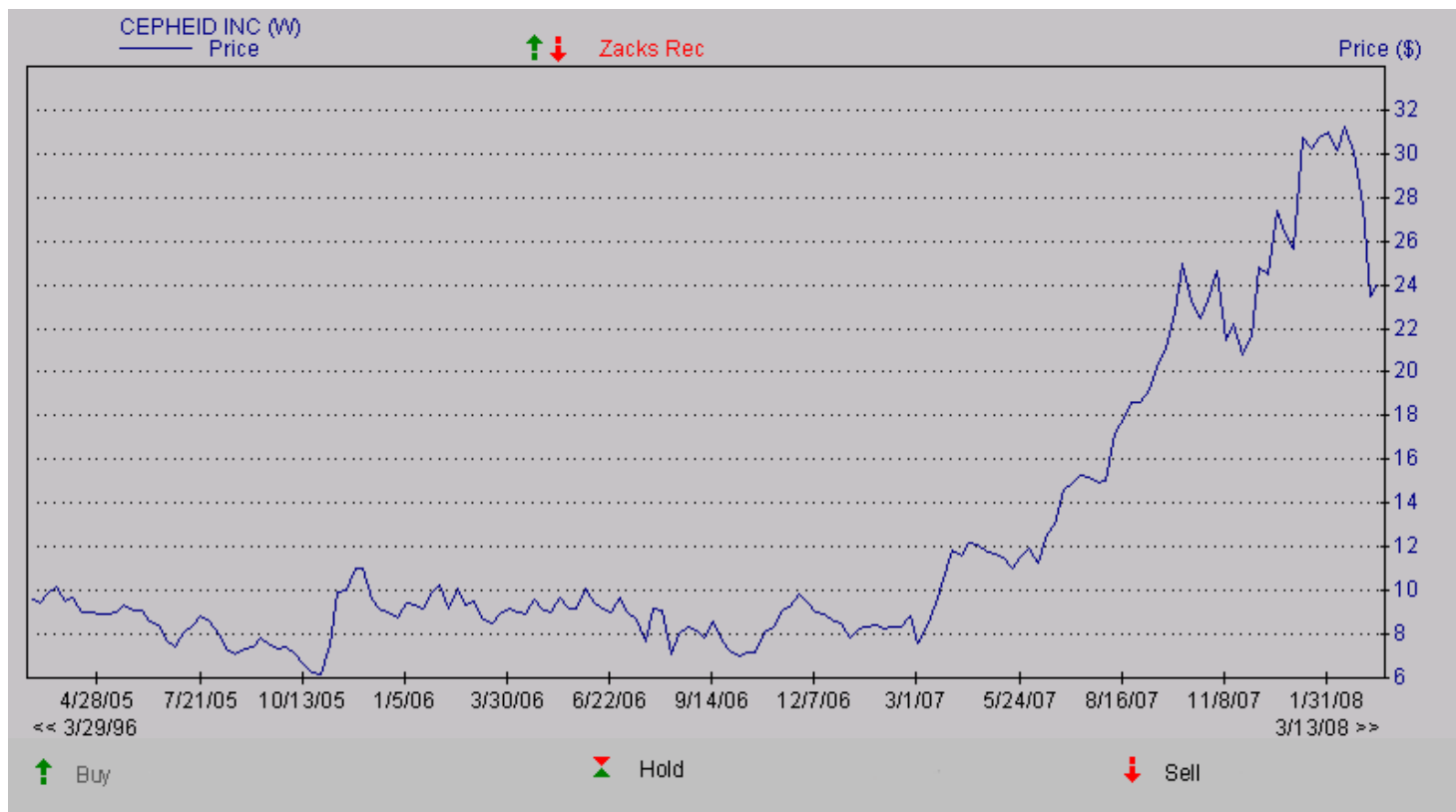
	P/Rev CFY	P/Rev NFY	EPS Gr 5Yr Est	Price/ Book	Price/ TTM Rev
CEPHEID INC	7.3	5.8	22.0	10.5	10.6
Industry Mean	3.9	3.1	22.5	3.6	5.2
Industry Median	2.6	2.5	19.8	2.7	3.1
S&P 500	1.3	1.2	12.4	4.1	2.4
Immucor	6.2	5.4	26.0	6.0	6.5
Gen-Probe Inc	5.8	5.4	22.0	3.4	6.3
Third Wave Tech	10.4	6.9	N/A	12.9	12.3
Meridian Biosci	9.2	8.1	24.0	10.9	10.0
Luminex Corp	6.0	4.9	17.0	6.4	7.8

PROJECTED INCOME STATEMENT

Cepheid Inc Income Statement (Dollars in millions, except EPS data)

	12/06	12/07	12/08E	12/09E
Revenue	87	129	186	238
Cost of Products Sold	49	69	97	121
Collaboration Profit Sharing	15	12	13	14
SG&A	26	41	52	60
R&D	24	31	38	41
Interest and other	-4	-3	-2	-2
Adjusted Net Income inclu FAS 123R	-23	-21	-12	4
Diluted EPS inclu FAS 123R	-0.43	-0.39	-0.21	0.07
Reported EPS	-0.50	-0.39	-0.21	0.07
Diluted Shares in millions	52.3	55.3	56.2	57.3

HISTORICAL ZACKS RECOMMENDATIONS



DISCLOSURES

The analysts contributing to this report do not hold any shares of CPHD. Zacks EPS and revenue forecasts are not consensus forecasts. 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. **Buy**- Zacks expects that the subject company will outperform the broader U.S. equity market over the next one to two quarters. **Hold**- Zacks expects that the company will perform in line with the broader U.S. equity market over the next one to two quarters. **Sell**- Zacks expects the company will under perform the broader U.S. Equity market over the next one to two quarters. The current distribution of Zacks Ratings is as follows on the 1130 companies covered: Buy- 25.3%, Hold- 68.4%, Sell – 5.1%. Data is as of midnight on the business day immediately prior to this publication.