

MACROGENICS INC
Form 10-Q
August 02, 2017

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended June 30, 2017

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from _____ to _____

Commission File Number: 001-36112

MACROGENICS, INC.

(Exact name of registrant as specified in its charter)

Delaware 06-1591613

(State or other jurisdiction of incorporation or organization) (I.R.S. Employer Identification No.)

9704 Medical Center Drive 20850
Rockville, Maryland

(Address of principal executive offices) (Zip code)

301-251-5172

(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See definitions of "accelerated filer," "large accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer Accelerated filer

Non-accelerated filer (Do not check if a smaller reporting company) Smaller reporting company

Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes No

As of July 31, 2017, the number of outstanding shares of the registrant's common stock, par value \$0.01 per share, was 36,798,465 shares.

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FORWARD-LOOKING STATEMENTS

This report includes forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. Forward-looking statements include statements that may relate to our plans, objectives, goals, strategies, future events, future revenues or performance, capital expenditures, financing needs and other information that is not historical information. Many of these statements appear, in particular, under the headings "Risk Factors" and "Management's Discussion and Analysis of Financial Condition and Results of Operations". Forward-looking statements can often be identified by the use of terminology such as "subject to", "believe", "anticipate", "plan", "expect", "intend", "estimate", "project", "may", "will", "should", "would", "could", "can", the negatives thereof, variations thereon and similar expressions, or by discussions of strategy.

All forward-looking statements, including, without limitation, our examination of historical operating trends, are based upon our current expectations and various assumptions. We believe there is a reasonable basis for our expectations and beliefs, but they are inherently uncertain. We may not realize our expectations, and our beliefs may not prove correct. Actual results could differ materially from those described or implied by such forward-looking statements. The following uncertainties and factors, among others (including those set forth under "Risk Factors"), could affect future performance and cause actual results to differ materially from those matters expressed in or implied by forward-looking statements:

- our plans to develop and commercialize our product candidates;
- the outcomes of our ongoing and planned clinical trials and the timing of those outcomes;
- the timing of and our ability to obtain and maintain regulatory approvals for our product candidates;
- our estimates regarding expenses, future revenue, capital requirements and needs for additional financing;
- our ability to enter into new collaborations or to identify additional products or product candidates with significant commercial potential that are consistent with our commercial objectives;
- our ability to recover the investment in our manufacturing capabilities;
- the rate and degree of market acceptance and clinical utility of our products;
- our commercialization, marketing and manufacturing capabilities and strategy;
- significant competition in our industry;
- costs of litigation and the failure to successfully defend lawsuits and other claims against us;
- economic, political and other risks associated with our international operations;
- our ability to receive research funding and achieve anticipated milestones under our collaborations;
- our ability to protect and enforce patents and other intellectual property;
- costs of compliance and our failure to comply with new and existing governmental regulations including, but not limited to, tax regulations;
- loss or retirement of key members of management;
- failure to successfully execute our growth strategy, including any delays in our planned future growth; and
- our failure to maintain effective internal controls.

Consequently, forward-looking statements speak only as of the date that they are made and should be regarded solely as our current plans, estimates and beliefs. You should not place undue reliance on forward-looking statements. We cannot guarantee future results, events, levels of activity, performance or achievements. Except as required by law, we do not undertake and specifically decline any obligation to update, republish or revise forward-looking statements to reflect future events or circumstances or to reflect the occurrences of unanticipated events.

PART I. FINANCIAL INFORMATION
ITEM 1. FINANCIAL STATEMENTS
MACROGENICS, INC.
CONSOLIDATED BALANCE SHEETS
(in thousands, except share and per share data)

| | June 30, 2017 (unaudited) | December 31, 2016 |
|---|---------------------------------|----------------------|
| Assets | | |
| Current assets: | | |
| Cash and cash equivalents | \$ 116,627 | \$ 84,098 |
| Marketable securities | 127,033 | 192,898 |
| Accounts receivable | 1,991 | 2,764 |
| Prepaid expenses | 4,008 | 3,483 |
| Other current assets | 455 | 704 |
| Total current assets | 250,114 | 283,947 |
| Property and equipment, net | 23,179 | 17,961 |
| Marketable securities, non-current | — | 7,986 |
| Other assets | 1,553 | 1,369 |
| Total assets | \$ 274,846 | \$ 311,263 |
| Liabilities and stockholders' equity | | |
| Current liabilities: | | |
| Accounts payable | \$ 2,088 | \$ 3,995 |
| Accrued expenses | 22,319 | 16,134 |
| Deferred revenue | 3,202 | 4,261 |
| Deferred rent | 1,160 | 1,319 |
| Lease exit liability | 1,120 | 1,593 |
| Total current liabilities | 29,889 | 27,302 |
| Deferred revenue, net of current portion | 9,238 | 10,045 |
| Deferred rent, net of current portion | 4,371 | 4,867 |
| Lease exit liability, net of current portion | — | 298 |
| Total liabilities | 43,498 | 42,512 |
| Stockholders' equity: | | |
| Common stock, \$0.01 par value – 125,000,000 shares authorized, 36,680,522 and 34,870,607 shares outstanding at June 30, 2017 and December 31, 2016, respectively | 367 | 349 |
| Additional paid-in capital | 602,085 | 561,198 |
| Accumulated deficit | (371,024) | (292,714) |
| Accumulated other comprehensive loss | (80) | (82) |
| Total stockholders' equity | 231,348 | 268,751 |
| Total liabilities and stockholders' equity | \$ 274,846 | \$ 311,263 |

See accompanying notes.

MACROGENICS, INC.

CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME (LOSS)

(unaudited)

(in thousands, except share and per share data)

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|--|--------------------------------|------------|------------------------------|------------|
| | 2017 | 2016 | 2017 | 2016 |
| Revenues: | | | | |
| Revenue from collaborative agreements | \$1,081 | \$ 78,497 | \$2,359 | \$ 80,390 |
| Revenue from government agreements | 585 | 2,176 | 1,361 | 3,129 |
| Total revenues | 1,666 | 80,673 | 3,720 | 83,519 |
| Costs and expenses: | | | | |
| Research and development | 34,461 | 33,340 | 67,262 | 60,686 |
| General and administrative | 8,384 | 7,239 | 15,846 | 13,372 |
| Total costs and expenses | 42,845 | 40,579 | 83,108 | 74,058 |
| Income (loss) from operations | (41,179) | 40,094 | (79,388) | 9,461 |
| Other income | 525 | 370 | 1,078 | 640 |
| Net income (loss) | (40,654) | 40,464 | (78,310) | 10,101 |
| Other comprehensive income (loss): | | | | |
| Unrealized gain (loss) on investments | 25 | 7 | (1) | 64 |
| Comprehensive income (loss) | \$(40,629) | \$ 40,471 | \$(78,311) | \$ 10,165 |
| Basic net income (loss) per common share | \$(1.14) | \$ 1.17 | \$(2.21) | \$ 0.29 |
| Diluted net income (loss) per common share | \$(1.14) | \$ 1.12 | \$(2.21) | \$ 0.28 |
| Basic weighted average common shares outstanding | 35,784,804 | 34,616,197 | 35,373,799 | 34,560,021 |
| Diluted weighted average common shares outstanding | 35,784,804 | 36,017,411 | 35,373,799 | 35,966,987 |

See accompanying notes.

MACROGENICS, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(unaudited)
(in thousands)

| | Six Months Ended June 30, | |
|--|------------------------------|-----------|
| | 2017 | 2016 |
| Cash flows from operating activities | | |
| Net income (loss) | \$(78,310) | \$10,101 |
| Adjustments to reconcile net income (loss) to net cash used in operating activities: | | |
| Depreciation and amortization expense | 3,981 | 3,557 |
| Share-based compensation | 7,063 | 6,124 |
| Changes in operating assets and liabilities: | | |
| Accounts receivable | 773 | (77,151) |
| Prepaid expenses | (525) | (1,976) |
| Other assets | 65 | (426) |
| Accounts payable | (2,026) | (355) |
| Accrued expenses | 6,185 | 866 |
| Lease exit liability | (771) | (2,134) |
| Deferred revenue | (1,866) | (3,179) |
| Deferred rent | (655) | (563) |
| Net cash used in operating activities | (66,086) | (65,136) |
| Cash flows from investing activities | | |
| Purchases of marketable securities | (56,937) | (202,392) |
| Proceeds from sale and maturities of marketable securities | 130,505 | 141,611 |
| Purchases of property and equipment | (8,795) | (8,339) |
| Net cash provided by (used in) investing activities | 64,773 | (69,120) |
| Cash flows from financing activities | | |
| Proceeds from issuance of common stock, net of offering costs | 33,175 | — |
| Proceeds from stock option exercises and ESPP purchases | 667 | 351 |
| Net cash provided by financing activities | 33,842 | 351 |
| Net change in cash and cash equivalents | 32,529 | (133,905) |
| Cash and cash equivalents at beginning of period | 84,098 | 196,172 |
| Cash and cash equivalents at end of period | \$116,627 | \$62,267 |

See accompanying notes.

MACROGENICS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (unaudited)

1. Basis of Presentation and Recently Issued Accounting Standards

Basis of Presentation

The accompanying unaudited interim consolidated financial statements of MacroGenics, Inc. (the Company) have been prepared in accordance with U.S. generally accepted accounting principles (GAAP) for interim financial information. The financial statements include all adjustments (consisting only of normal recurring adjustments) that the management of the Company believes are necessary for a fair presentation of the periods presented. These interim financial results are not necessarily indicative of results expected for the full fiscal year or for any subsequent interim period.

The accompanying unaudited interim consolidated financial statements include the accounts of MacroGenics, Inc. and its wholly owned subsidiary, MacroGenics UK Limited. All intercompany accounts and transactions have been eliminated in consolidation. These consolidated financial statements and related notes should be read in conjunction with the financial statements and notes thereto included in the Company's 2016 Annual Report on Form 10-K filed with the Securities and Exchange Commission (SEC) on February 28, 2017.

There have been no material changes to the significant accounting policies previously disclosed in the Company's 2016 Annual Report on Form 10-K other than the adoption of ASU No. 2015-17, Improvements to Employee Share-Based Payment Accounting, as disclosed in the Recently Issued Accounting Standards section below.

Recently Issued Accounting Standards

In May 2014, the Financial Accounting Standards Board (FASB) issued ASU No. 2014-09, Revenue from Contracts with Customers (Topic 606) (ASU 2014-09). ASU 2014-09 will eliminate transaction- and industry-specific revenue recognition guidance under current GAAP and replace it with a principle-based approach for determining revenue recognition. ASU 2014-09 will require that companies recognize revenue based on the value of transferred goods or services as they occur in the contract. The ASU also will require additional disclosure about the nature, amount, timing and uncertainty of revenue and cash flows arising from customer contracts, including significant judgments and changes in judgments and assets recognized from costs incurred to obtain or fulfill a contract. ASU 2014-09 is effective for annual reporting periods beginning after December 15, 2017 and interim periods therein, with early adoption permitted for interim and annual reporting periods beginning after December 15, 2016. ASU 2014-09 may be adopted either retrospectively or on a modified retrospective basis whereby ASU 2014-09 would be applied to new contracts and existing contracts with remaining performance obligations as of the effective date, with a cumulative catch-up adjustment recorded to beginning retained earnings at the effective date for existing contracts with remaining performance obligations. In 2016, the FASB issued ASU 2016-08, Revenue from Contracts with Customers: Principal versus Agent Considerations, ASU 2016-10, Revenue from Contracts with Customers: Identifying Performance Obligations and Licensing, and ASU 2016-12, Revenue from Contracts with Customers: Narrow-Scope Improvements and Practical Expedients to provide supplemental adoption guidance and clarification to ASU 2014-09. The effective date for these new standards is the same as the effective date and transition requirements for ASU 2014-09. Management has begun an initial review of each of the Company's collaboration and license agreements and is performing an assessment of the potential effects of the standard on the Company's consolidated financial statements, accounting policies, and internal controls over financial reporting. The Company anticipates that the adoption of the new revenue recognition standard will have primarily two impacts on its contract revenues generated by its collaborative research and license agreements:

- (i) Changes in the model for distinct licenses of functional intellectual property which may result in a timing difference of revenue recognition. Whereas revenue from these arrangements was previously recognized over a period of time pursuant to revenue recognition guidance that was in place for the arrangements at the time such arrangements commenced, revenue from these arrangements may now be recognized at point in time under the new guidance.
- (ii) Assessments of milestone payments, which are linked to events that are in the Company's control, will result in variable consideration that may be recognized at an earlier point in time under the new guidance, when it is probable that the milestone will be achieved without a significant future reversal of cumulative revenue expected.

The Company plans to adopt the new standard effective January 1, 2018 using the modified retrospective method with the cumulative effective of initially applying the new standard recognized in retained earnings at the date of initial adoption. The Company has begun to analyze its existing revenue agreements to evaluate the impact of adoption. In February 2016, FASB issued ASU No. 2016-02, Leases (ASU 2016-02) that provides principles for the recognition, measurement, presentation and disclosure of leases for both lessees and lessors. ASU 2016-02 requires a lessee to recognize

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assets and liabilities on the balance sheet for operating leases and changes many key definitions, including the definition of a lease. ASU 2016-02 includes a short-term lease exception for leases with a term of 12 months or less, in which a lessee can make an accounting policy election not to recognize lease assets and lease liabilities. Lessees will continue to differentiate between finance leases (previously referred to as capital leases) and operating leases, using classification criteria that are substantially similar to the previous guidance. ASU 2016-02 is effective for fiscal years beginning after December 15, 2018, and interim periods within those fiscal years, with earlier application permitted. The Company is currently evaluating the effect of the standard on its consolidated financial statements and related disclosures.

In March 2016, the FASB issued ASU 2016-09, Improvements to Employee Share-Based Payment Accounting (ASU 2016-09). This amendment addresses several aspects of the accounting for share-based payment transactions, including the income tax consequences, classification of awards as either equity or liabilities and classification on the statement of cash flows. ASU 2016-09 is effective for fiscal years beginning after December 15, 2016, including interim periods within that year. The Company adopted ASU 2016-09 effective January 1, 2017 and has elected to continue to estimate the number of stock-based awards expected to vest, as permitted by ASU 2016-09, rather than electing to account for forfeitures as they occur. The adoption of this standard did not have a material impact on the Company's financial statements or related disclosures.

2. Fair Value of Financial Instruments

The Company's financial instruments consist of cash and cash equivalents, marketable securities, accounts receivable, accounts payable and accrued expenses. The carrying amount of accounts receivable, accounts payable and accrued expenses are generally considered to be representative of their respective fair values because of their short-term nature. The Company accounts for recurring and non-recurring fair value measurements in accordance with FASB Accounting Standards Codification (ASC) 820, Fair Value Measurements and Disclosures (ASC 820). ASC 820 defines fair value, establishes a fair value hierarchy for assets and liabilities measured at fair value, and requires expanded disclosures about fair value measurements. The ASC 820 hierarchy ranks the quality of reliability of inputs, or assumptions, used in the determination of fair value and requires assets and liabilities carried at fair value to be classified and disclosed in one of the following three categories:

Level 1 - Fair value is determined by using unadjusted quoted prices that are available in active markets for identical assets and liabilities.

Level 2 - Fair value is determined by using inputs other than Level 1 quoted prices that are directly or indirectly observable. Inputs can include quoted prices for similar assets and liabilities in active markets or quoted prices for identical assets and liabilities in inactive markets. Related inputs can also include those used in valuation or other pricing models, such as interest rates and yield curves that can be corroborated by observable market data.

Level 3 - Fair value is determined by inputs that are unobservable and not corroborated by market data. Use of these inputs involves significant and subjective judgments to be made by a reporting entity - e.g., determining an appropriate adjustment to a discount factor for illiquidity associated with a given security.

The Company evaluates financial assets and liabilities subject to fair value measurements on a recurring basis to determine the appropriate level at which to classify them each reporting period. This determination requires the Company to make subjective judgments as to the significance of inputs used in determining fair value and where such inputs lie within the ASC 820 hierarchy.

Financial assets measured at fair value on a recurring basis were as follows (in thousands):

Fair Value Measurements at June 30, 2017

| | Total | Quoted Prices in Active Markets for Identical Assets Level 1 | Significant Other Observable Inputs Level 2 | Significant Unobservable Inputs Level 3 |
|--|-----------|---|---|--|
| Assets: | | | | |
| Money market funds | \$92,815 | \$92,815 | \$ — | \$ — |
| U.S. Treasury securities | 13,782 | — | 13,782 | — |
| Government-sponsored enterprises | 26,129 | — | 26,129 | — |
| Corporate debt securities | 87,122 | — | 87,122 | — |
| Total assets measured at fair value ^(a) | \$219,848 | \$92,815 | \$ 127,033 | \$ — |

(a) Total assets measured at fair value at June 30, 2017 includes approximately \$92.8 million reported in cash and cash equivalents on the balance sheet.

Fair Value Measurements at December 31, 2016

| | Total | Quoted Prices in Active Markets for Identical Assets Level 1 | Significant Other Observable Inputs Level 2 | Significant Unobservable Inputs Level 3 |
|--|-----------|---|---|--|
| Assets: | | | | |
| Money market funds | \$46,781 | \$46,781 | \$ — | \$ — |
| U.S. Treasury securities | 8,826 | — | 8,826 | — |
| Government-sponsored enterprises | 29,759 | — | 29,759 | — |
| Corporate debt securities | 166,300 | — | 166,300 | — |
| Total assets measured at fair value ^(a) | \$251,666 | \$46,781 | \$ 204,885 | \$ — |

(a) Total assets measured at fair value at December 31, 2016 includes approximately \$50.8 million reported in cash and cash equivalents on the balance sheet.

The fair value of Level 2 securities is determined from market pricing and other observable market inputs for similar securities obtained from various third-party data providers. These inputs either represent quoted prices for similar assets in active markets or have been derived from observable market data. There were no transfers between Level 1 and Level 2 investments during the periods presented.

3. Marketable Securities

Available-for-sale marketable securities as of June 30, 2017 and December 31, 2016 were as follows (in thousands):

June 30, 2017

| | Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses | Fair Value |
|----------------------------------|-------------------|------------------------------|-------------------------------|---------------|
| U.S. Treasury securities | \$13,802 | \$ — | \$ (20) | \$13,782 |
| Government-sponsored enterprises | 26,159 | — | (30) | 26,129 |
| Corporate debt securities | 87,152 | 5 | (35) | 87,122 |
| Total | \$127,113 | \$ 5 | \$ (85) | \$127,033 |

| | December 31, 2016 | | | |
|----------------------------------|-------------------|------------------------------|-------------------------------|---------------|
| | Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses | Fair Value |
| U.S. Treasury securities | \$4,826 | \$ — | \$ (1) | \$4,825 |
| Government-sponsored enterprises | 29,764 | 5 | (10) | 29,759 |
| Corporate debt securities | 166,376 | 51 | (127) | 166,300 |
| Total | \$200,966 | \$ 56 | \$ (138) | \$200,884 |

All available-for-sale marketable securities held as of June 30, 2017 had contractual maturities of less than one year. All of the Company's available-for-sale marketable securities in an unrealized loss position as of June 30, 2017 and December 31, 2016 were in a loss position for less than twelve months. There were no unrealized losses at June 30, 2017 or December 31, 2016 that the Company determined to be other-than-temporary.

4. Lease Exit Liability

In 2008, the Company acquired Raven Biotechnologies, Inc. (Raven), a private South San Francisco-based company focused on the development of monoclonal antibody therapeutics for treating cancer. The Company undertook restructuring activities related to the acquisition of Raven. In connection with these restructuring activities, as part of the cost of acquisition, the Company established a restructuring liability attributed to an existing operating lease. During the year ended December 31, 2016, the Company entered into an agreement to sublease a portion of the space subject to this operating lease. The Company will receive approximately \$1.3 million in sublease payments over its term, which ends at the same time as the original lease in February 2018. No sublease income was contemplated when the restructuring liability was recorded in 2008; therefore, the Company adjusted the liability to reflect the future sublease income during the year ended December 31, 2016 and recorded an offset to research and development expenses of approximately \$1.3 million in the same period.

Changes in the lease exit liability are as follows (in thousands):

| | |
|--------------------------------------|---------|
| Accrual balance at December 31, 2016 | \$1,891 |
| Principal payments | (771) |
| Accrual balance at June 30, 2017 | \$1,120 |

5. Stockholders' Equity

On April 26, 2017, the Company entered into a definitive agreement with an institutional healthcare investor to purchase 1,100,000 shares of its common stock at a purchase price of \$21.50 per share in a registered direct offering. Gross proceeds to the Company, before deducting estimated offering expenses, were \$23.7 million. The shares were offered pursuant to the Company's shelf registration on Form S-3 that was filed with the SEC on November 2, 2016.

On May 3, 2017, the Company entered into a sales agreement with an agent to sell, from time to time, shares of its common stock having an aggregate sales price of up to \$75.0 million through an "at the market offering" (ATM Offering) as defined in Rule 415 under the Securities Act of 1933, as amended. The shares that may be sold under the sales agreement would be issued and sold pursuant to the Company's shelf registration statement on Form S-3 that was filed with the SEC on November 2, 2016. Through June 30, 2017, the Company sold 536,942 shares of common stock under the sales agreement, resulting in net proceeds of \$9.7 million related to the ATM Offering.

6. Collaboration and Other Agreements

Janssen Biotech, Inc.

In December 2014, the Company entered into a collaboration and license agreement with Janssen Biotech, Inc. (Janssen) for the development and commercialization of MGD011 (also known as duvortuxizumab), a product candidate that incorporates the Company's proprietary DART® technology to simultaneously target CD19 and CD3 for the potential treatment of B-cell hematological malignancies (MGD011 Agreement). The Company contemporaneously entered into an agreement with Johnson & Johnson Innovation - JJDC, Inc. (JJDC) under which JJDC agreed to purchase 1,923,077 new shares of the Company's common stock for proceeds of \$75.0 million. Upon closing the transaction in January 2015, the Company received a \$50.0 million upfront payment from Janssen as well as the \$75.0 million investment in the Company's common stock.

Under the MGD011 Agreement, the Company granted an exclusive license to Janssen to develop and commercialize duvortuxizumab. Following the Company's submission of the Investigational New Drug (IND) application, Janssen became fully responsible for the development and commercialization of duvortuxizumab. Assuming successful development and commercialization, the agreement entitles the Company to receive up to \$205.0 million in development milestone payments, \$220.0 million in regulatory milestone payments and \$150.0 million in sales milestone payments. The Company determined that each potential future clinical and regulatory milestone is substantive. Although the sales milestones are not considered substantive, they will be recognized upon achievement of the milestone (assuming all other revenue recognition criteria have been met) because there are no undelivered elements that would preclude revenue recognition at that time. The Company may elect to fund a portion of late-stage clinical development in exchange for a profit share with Janssen in the U.S. and Canada. If commercialized, the Company would be eligible to receive low double-digit royalties on any global net sales and has the option to co-promote the molecule with Janssen in the United States.

The Company evaluated the MGD011 Agreement and determined that it is a revenue arrangement with multiple deliverables, or performance obligations. The Company's substantive performance obligations under the collaboration and license agreement include the delivery of an exclusive license and research and development services during the preclinical research period (through the filing of the IND application for duvortuxizumab). The Company evaluated the MGD011 Agreement and determined that the license and preclinical research and development activities each represented separate deliverables and were accounted for as separate units of accounting. The Company concluded that the license had standalone value to Janssen and was separable from the research and development services because the license was sublicensable, there were no restrictions as to Janssen's use of the license and Janssen or other third parties have significant research capabilities in this field. Thus, the total arrangement consideration for these two deliverables was allocated using the relative best estimate of selling price method to each deliverable. The best estimate of selling price for the exclusive license was determined using a discounted cash flow model that includes Level 3 fair value measurements. The best estimate of selling price for the research and development services was determined using other similar research and development arrangements, which are Level 2 fair value measurements. The Company evaluated the stock purchase agreement and the collaboration and license agreement as one arrangement and determined that the stock purchase price of \$39.00 per share exceeded the fair value of the common stock by \$12.3 million. This excess was recognized in the same manner as the upfront payment allocated to the license and preclinical research and development activities. Of the total arrangement consideration of \$125.0 million, the Company allocated \$62.7 million to equity (representing the fair value of common stock purchased), \$62.3 million to the license and preclinical research and development activities, and a de minimis amount to the ongoing research and development activities. The Company submitted the IND application and therefore met its performance obligation during the year ended December 31, 2015.

There was no revenue recognized under the MGD011 Agreement during any of the three or six-month periods ended June 30, 2017 or 2016.

In May 2016, the Company entered into a separate collaboration and license agreement with Janssen, a related party through ownership of the Company's common stock, for the development and commercialization of MGD015 (also known as JNJ-9383), a product candidate that incorporates the Company's proprietary DART technology to simultaneously target CD3 and an undisclosed tumor target for the potential treatment of various hematological

malignancies and solid tumors (MGD015 Agreement). The transaction closed in June 2016, and the Company received the \$75.0 million upfront payment from Janssen in July 2016.

Under the MGD015 Agreement, the Company granted an exclusive license to Janssen to develop and commercialize MGD015. Janssen will complete the IND-enabling activities and will be fully responsible for the future clinical development and commercialization of MGD015. Assuming successful development and commercialization, the agreement entitles the Company to receive up to \$100.0 million in development milestone payments, \$265.0 million in regulatory milestone payments and \$300.0 million in sales milestone payments. The Company determined that each potential future clinical and regulatory

milestone is substantive. Although the sales milestones are not considered substantive, they will be recognized upon achievement of the milestone (assuming all other revenue recognition criteria have been met) because there are no undelivered elements that would preclude revenue recognition at that time. The Company may elect to fund a portion of late-stage clinical development in exchange for a profit share with Janssen in the U.S. and Canada. If commercialized, the Company would be eligible to receive low double-digit royalties on any global net sales and has the option to co-promote the molecule with Janssen in the United States.

The Company evaluated the MGD015 Agreement and determined that it is a revenue arrangement with multiple deliverables, or performance obligations. The Company's substantive performance obligations under the MGD015 Agreement include the delivery of an exclusive license and research and development services during the preclinical research period. The Company evaluated the MGD015 Agreement and determined that the license and preclinical research and development activities each represented separate deliverables and were accounted for as two separate units of accounting. The Company concluded that the license had standalone value to Janssen and was separable from the research and development services because the license was sublicensable, there were no restrictions as to Janssen's use of the license and Janssen or other third parties have significant research capabilities in this field. Thus, the total arrangement consideration for these two deliverables was allocated using the best estimate of relative selling price method to each deliverable. The best estimate of selling price for the exclusive license was determined using information from the previous collaboration and license agreement with Janssen as well as other third party collaboration and license agreements, which are Level 2 fair value measurements. The best estimate of selling price for the research and development services was determined using other similar research and development arrangements, which are also Level 2 fair value measurements.

The company recognized \$0.2 million and \$0.3 million of revenue under the MGD015 Agreement during the three and six months ended June 30, 2017, respectively. No revenue was recognized under the MGD015 Agreement during the three and six months ended June 30, 2016.

Les Laboratoires Servier

In September 2012, the Company entered into a right-to-develop collaboration agreement with Les Laboratoires Servier and Institut de Recherches Servier (collectively, Servier) and granted it options to obtain three separate exclusive licenses to develop and commercialize DART molecules, consisting of those designated by the Company as flotetuzumab (also known as MGD006 or S80880) and MGD007, as well as a third DART molecule, in all countries other than the United States, Canada, Mexico, Japan, South Korea and India. During 2014, Servier exercised its exclusive option to develop and commercialize flotetuzumab, and during 2016 Servier notified the Company that it did not intend to exercise the option for the third DART molecule. Servier retains the option to obtain a license for MGD007.

Upon execution of the agreement, Servier made a nonrefundable payment of \$20.0 million to the Company. In addition, the Company will be eligible to receive up to \$40.0 million in license fees, \$63.0 million in clinical milestone payments, \$188.0 million in regulatory milestone payments and \$420.0 million in sales milestone payments if Servier exercises the remaining available options and successfully develops, obtains regulatory approval for, and commercializes a product under each license. In addition to these milestones, the Company and Servier will share Phase 2 and Phase 3 development costs. The Company has determined that each potential future clinical and regulatory milestone is substantive. Although sales milestones are not considered substantive, they are still recognized upon achievement of the milestone (assuming all other revenue recognition criteria have been met) because there are no undelivered elements that would preclude revenue recognition at that time. Under this agreement, Servier would be obligated to pay the Company from low double-digit to mid-teen royalties on net product sales in its territories. The Company evaluated the research collaboration agreement with Servier and determined that it is a revenue arrangement with multiple deliverables, or performance obligations. The Company concluded that each option is substantive and that the license fees for each option are not deliverables at the inception of the arrangement and were not issued with a substantial discount. The Company's substantive performance obligations under this research collaboration include an exclusivity clause to its technology, technical, scientific and intellectual property support to the research plan and participation on an executive committee and a research and development committee. The Company determined that the performance obligations with respect to the preclinical development represent a single

unit of accounting, since the license does not have stand-alone value to Servier without the Company's technical expertise and committee participation. As such, the initial upfront license payment was deferred and initially recognized ratably over a 29-month period, which represented the expected development period. During 2014, the Company and Servier further refined the research plan related to the three DART molecules and as such, the development period was extended. Based on this revised development period, the Company prospectively adjusted its period of recognition of the upfront payment to a 75-month period. The impact of this change in accounting estimate reduced revenue that would have been recognized in 2014 by \$3.7 million.

As a result of Servier exercising its option in 2014, the Company received a \$15.0 million payment from Servier for its license to develop and commercialize flotetuzumab in its territories. Upon exercise of the option, the Company evaluated its performance obligations with respect to the license for flotetuzumab. The Company's substantive performance obligations under this research collaboration include an exclusive license to its technology, technical, scientific and intellectual property support to the research plan and participation on an executive committee and a research and development committee. The Company determined that the performance obligations with respect to the clinical development represent a single unit of accounting, since the license does not have stand-alone value to Servier without the Company's technical expertise and committee participation. As such, the \$15.0 million license fee was deferred and was being recognized ratably over a period of 82 months, which represented the expected development period for flotetuzumab. During the three months ended June 30, 2017, the Company and Servier determined that the expected development period should be extended to 124 months. The impact of this change in accounting estimate reduced revenue that would have been recognized in 2017 by \$0.8 million. In accordance with the agreement, the Company and Servier will share costs incurred to develop flotetuzumab. Reimbursement of research and development expenses received in connection with this collaborative cost-sharing agreement is recorded as a reduction to research and development expense. During the three months ended June 30, 2017 and 2016, the Company recorded approximately \$0.4 million and \$0.7 million as an offset to research and development costs under this collaboration agreement, respectively. During the six months ended June 30, 2017 and 2016, the Company recorded approximately \$0.9 million and \$1.1 million as an offset to research and development costs under this collaboration agreement, respectively.

The Company recognized revenue under this agreement of \$0.6 million and \$0.8 million during the three months ended June 30, 2017 and 2016, respectively. The Company recognized revenue under this agreement of \$1.4 million and \$1.7 million during the six months ended June 30, 2017 and 2016, respectively. At June 30, 2017, \$9.7 million of revenue was deferred under this agreement, \$2.3 million of which was current and \$7.4 million of which was non-current. At December 31, 2016, \$11.1 million of revenue was deferred under this agreement, \$3.3 million of which was current and \$7.8 million of which was non-current.

NIAID Contract

The Company entered into a contract with the National Institute of Allergy and Infectious Diseases (NIAID), effective as of September 15, 2015, to perform product development and to advance up to two DART molecules, including MGD014. Under this contract, the Company will develop these product candidates for Phase 1/2 clinical trials as therapeutic agents, in combination with latency reversing treatments, to deplete cells infected with human immunodeficiency virus (HIV) infection. This contract includes a base period of \$7.5 million to support development of MGD014 through IND application submission with the FDA, as well as up to \$17.0 million in additional development funding via NIAID options. Should NIAID fully exercise such options, the Company could receive total payments of up to \$24.5 million. The total potential period of performance under the award is from September 15, 2015 through September 14, 2022. The Company recognized \$0.4 million and \$2.1 million in revenue under this contract during the three months ended June 30, 2017 and 2016, respectively. The Company recognized \$1.0 million and \$3.1 million in revenue under this contract during the six months ended June 30, 2017 and 2016, respectively.

7. Stock-Based Compensation

Employee Stock Purchase Plan

In May 2017, the Company's stockholders approved the 2016 Employee Stock Purchase Plan (the 2016 ESPP). The 2016 ESPP is structured as a qualified employee stock purchase plan under Section 423 of the Internal Revenue Code of 1986, as amended, and is not subject to the provisions of the Employee Retirement Income Security Act of 1974. The Company reserved 800,000 shares of common stock for issuance under the 2016 ESPP. The 2016 ESPP allows eligible employees to purchase shares of the Company's common stock at a discount through payroll deductions of up to 10% of their eligible compensation, subject to any plan limitations. The 2016 ESPP provides for six-month offering periods ending on May 31 and November 30 of each year. At the end of each offering period, employees are able to purchase shares at 85% of the fair market value of the Company's common stock on the last day of the offering period. During the three and six months ended June 30, 2017, employees purchased 19,351 shares of common stock under the

ESPP plan for net proceeds to the Company of approximately \$0.3 million.

Employee Stock Option Plans

Effective February 2003, the Company implemented the 2003 Equity Incentive Plan (2003 Plan), and it was amended and approved by the Company's stockholders in 2005. The 2003 Plan originally allowed for the grant of awards in respect of an aggregate of 2,051,644 shares of the Company's common stock. Between 2006 and 2012, the maximum number of shares of

common stock authorized to be issued by the Company under the 2003 Plan was increased to 4,336,730. Stock options granted under the 2003 Plan may be either incentive stock options as defined by the Internal Revenue Code (IRC), or non-qualified stock options.

In 2013, the 2003 Plan was terminated, and no further awards may be issued under the plan. Any shares of common stock subject to awards under the 2003 Plan that expire, terminate, or are otherwise surrendered, canceled, forfeited or repurchased without having been fully exercised, or resulting in any common stock being issued, will become available for issuance under the Company's 2013 Stock Incentive Plan (2013 Plan), up to a specified number of shares. As of June 30, 2017, under the 2003 Plan, there were options to purchase an aggregate of 1,053,487 shares of common stock outstanding at a weighted average exercise price of \$1.85 per share.

Under the provisions of the 2013 Plan, the number of shares of common stock reserved for issuance will automatically increase on January 1 of each year from January 1, 2014 through and including January 1, 2023, by the lesser of (a) 1,960,168 shares, (b) 4.0% of the total number of shares of common stock outstanding on December 31 of the preceding calendar year, or (c) the number of shares of common stock determined by the Board of Directors. During the six months ended June 30, 2017, the maximum number of shares of common stock authorized to be issued by the Company under the 2013 Plan was increased to 6,769,888. As of June 30, 2017, there were options to purchase an aggregate of 3,567,521 shares of common stock outstanding at a weighted average exercise price of \$24.88 per share under the 2013 Plan.

The following table shows stock-based compensation expense for stock options, RSUs and ESPP (in thousands):

| | Three Months | | Six Months | |
|--|----------------|---------|----------------|---------|
| | Ended June 30, | | Ended June 30, | |
| | 2017 | 2016 | 2017 | 2016 |
| Research and development | \$1,833 | \$1,445 | \$3,506 | \$2,841 |
| General and administrative | 1,769 | 1,678 | 3,557 | 3,283 |
| Total stock-based compensation expense | \$3,602 | \$3,123 | \$7,063 | \$6,124 |

The fair value of each option award is estimated on the date of grant using the Black-Scholes option-pricing model using the assumptions in the following table for options issued during the period indicated:

| | Six Months Ended June 30, | |
|-------------------------|---------------------------|---------------|
| | 2017 | 2016 |
| Expected dividend yield | 0% | 0% |
| Expected volatility | 66.7% - 67.7% | 63.7% - 65.4% |
| Risk-free interest rate | 2.0% - 2.3% | 1.3% - 2.1% |
| Expected term | 6.25 years | 6.25 years |

The following table summarizes stock option and restricted stock unit (RSU) activity during the six months ended June 30, 2017:

| | Shares | Weighted-Average Exercise Price | Weighted-Average Remaining Contractual Term (Years) | Aggregate Intrinsic Value (in thousands) |
|--------------------------------|------------|---------------------------------|---|--|
| Outstanding, December 31, 2016 | 3,838,060 | \$ 18.93 | 7.0 | |
| Granted | 1,120,950 | 20.38 | | |
| Exercised | (155,484) | 2.36 | | |
| Forfeited or expired | (182,518) | 24.13 | | |
| Outstanding, June 30, 2017 | 4,621,008 | 19.63 | 7.2 | \$ 17,581 |
| As of June 30, 2017: | | | | |
| Exercisable | 2,534,628 | 15.86 | 5.8 | 16,784 |
| Vested and expected to vest | 4,407,535 | 19.37 | 7.1 | 17,489 |

The weighted-average grant-date fair value of options granted for the six months ended June 30, 2017 was \$12.73. The total intrinsic value of options exercised during the six months ended June 30, 2017 was approximately \$2.6 million, and the total cash received for options exercised was approximately \$0.3 million. The total fair value of shares vested in the six months ended June 30, 2017 was approximately \$6.1 million. As of June 30, 2017, the total unrecognized compensation expense related to non-vested stock options, net of related forfeiture estimates, was approximately \$26.5 million, which the Company expects to recognize over a weighted-average period of approximately 2.6 years.

8. Commitments and Contingencies

Operating Leases

The Company leases manufacturing, office and laboratory space in Rockville, Maryland under five leases that have terms that expire between 2018 and 2023 unless renewed. During the three months ended June 30, 2017, one of these leases was renewed for an additional five years. The Rockville leases include a seven-year lease executed in July 2015 for additional space that the Company intends to use as mixed-use office, laboratory and manufacturing space. Under the terms of the lease, which commenced on January 1, 2016, the Company received an assignment fee from the former tenant and a tenant improvement allowance from the landlord totaling \$5.1 million, which has been recorded as deferred rent and will be recognized over the lease term. The Company also leases office and laboratory space in South San Francisco under a lease that expires on February 28, 2018. During the year ended December 31, 2016, the Company entered into a sublease agreement for a portion of the South San Francisco space (see Note 4). As of June 30, 2017, future payments to be received by the Company under this sublease total approximately \$0.5 million. In April 2017, the Company entered into a 72-month lease commencing December 1, 2017 for office and laboratory space which will be occupied upon the termination of the current South San Francisco lease.

All of the leases contain rent escalation clauses and certain leases contain rent abatements. For financial reporting purposes, rent expense is charged to operations on a straight-line basis over the term of the lease.

Future minimum lease payments under noncancelable operating leases as of June 30, 2017 are as follows (in thousands):

| Year Ended December 31, | |
|-------------------------|----------|
| 2017 | \$6,391 |
| 2018 | 5,346 |
| 2019 | 5,077 |
| 2020 | 3,454 |
| 2021 | 3,926 |
| Thereafter | 5,129 |
| | \$29,323 |

Contingencies

From time to time, the Company may be subject to various litigation and related matters arising in the ordinary course of business. The Company does not believe it is currently subject to any material matters where there is at least a reasonable possibility that a material loss may be incurred.

9. Net Income (Loss) Per Share

Basic income (loss) per common share is determined by dividing income (loss) attributable to common stockholders by the weighted-average number of common shares outstanding during the period, without consideration of common stock equivalents. Diluted income (loss) per share is computed by dividing the income (loss) attributable to common stockholders by the weighted-average number of common stock equivalents outstanding for the period. The treasury stock method is used to determine the dilutive effect of the Company's stock option grants. 4,621,008 stock options (common stock equivalents) were excluded from the calculation of diluted loss per share for the three and six months ended June 30, 2017, respectively, because their inclusion would have been anti-dilutive. 257,678 and 114,148 stock options were excluded from the calculation of diluted loss per share for the three and six months ended June 30, 2016, respectively, because their inclusion would have been anti-dilutive.

Basic and diluted income (loss) per common share is computed as follows (in thousands except share and per share data):

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|---|--------------------------------|------------|------------------------------|------------|
| | 2017 | 2016 | 2017 | 2016 |
| Numerator: | | | | |
| Net income (loss) used for calculation of basic and diluted EPS | \$(40,654) | \$ 40,464 | \$(78,310) | \$ 10,101 |
| Denominator: | | | | |
| Weighted average shares outstanding, basic | 35,784,804 | 34,616,197 | 35,373,799 | 34,560,021 |
| Effect of dilutive securities: | | | | |
| Stock options and restricted stock units | — | 1,401,214 | — | 1,406,966 |
| Weighted average shares outstanding, diluted | 35,784,804 | 36,017,411 | 35,373,799 | 35,966,987 |
| Net income (loss) per share, basic | \$(1.14) | \$ 1.17 | \$(2.21) | \$ 0.29 |
| Net income (loss) per share, diluted | \$(1.14) | \$ 1.12 | \$(2.21) | \$ 0.28 |

10. Subsequent Events

On July 6, 2017, the Company entered into an agreement to sublease a portion of the space it leases in Rockville, MD. Under the terms of the sublease, which commences August 1, 2017, the Company will receive a total of \$2.4 million over the 30 month term.

On July 21, 2017, the Company executed a lease amendment for its headquarters building in Rockville, MD. This amendment extends the term of the lease to August 2027, restructures the rent due under the lease, and provides for an additional tenant improvement allowance from the landlord of \$7.5 million. Future rent payments under the amended lease will increase by \$23.5 million, which is not reflected in the future minimum lease payments table in Note 8.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion of our financial condition and results of operations is based upon our unaudited consolidated financial statements included in this Quarterly Report on Form 10-Q, which have been prepared by us in accordance with GAAP, for interim periods and with Regulation S-X promulgated under the Securities Exchange Act of 1934, as amended. This discussion and analysis should be read in conjunction with these unaudited consolidated financial statements and the notes thereto as well as in conjunction with our audited consolidated financial statements and related notes thereto included in our Annual Report on Form 10-K for the year ended December 31, 2016.

Overview

We are a biopharmaceutical company focused on discovering and developing innovative antibody-based therapeutics for the treatment of cancer as well as various autoimmune disorders and infectious diseases. We currently have a pipeline of product candidates in human clinical testing, primarily against different types of cancers, which have been created using our proprietary technology platforms. We believe our programs have the potential to have a meaningful effect on treating patients' unmet medical needs as monotherapy or, in some cases, in combination with other therapeutic agents.

We commenced active operations in 2000, and have since devoted substantially all of our resources to staffing our company, developing our technology platforms, identifying potential product candidates, undertaking preclinical studies, conducting clinical trials, developing collaborations, business planning and raising capital. We have not generated any revenues from the sale of any products to date. We have financed our operations primarily through the public and private offerings of our securities, collaborations with other biopharmaceutical companies, and government grants and contracts. Although it is difficult to predict our funding requirements, based upon our current operating plan, we anticipate that our cash, cash equivalents and marketable securities as of June 30, 2017, combined with collaboration payments we anticipate receiving, will enable us to fund our operations into 2019.

We have incurred significant losses since our inception and we have an accumulated deficit of approximately \$371.0 million as of June 30, 2017. Our net losses were \$78.3 million for the six months ended June 30, 2017 and \$58.5 million for the fiscal year ended December 31, 2016. These losses have resulted principally from costs incurred in connection with research and development activities and general and administrative costs associated with our operations. We expect to continue to incur losses for the foreseeable future, and we expect these losses to increase as we continue our research and development of, and seek regulatory approvals for, our product candidates, prepare for and begin to commercialize any approved products, and add infrastructure and personnel to support our product development efforts and operations. The net losses and negative cash flows incurred to date, together with expected future losses, have had, and likely will continue to have, an adverse effect on our stockholders' deficit and working capital. The amount of future net losses will depend, in part, on the rate of future growth of our expenses and our ability to generate revenue.

Strategic Collaborations

We pursue a balanced approach between product candidates that we develop ourselves and those that we develop with our collaborators. Under our current strategic collaborations to date, we have received significant non-dilutive funding and continue to have rights to additional funding upon completion of certain research, achievement of key product development milestones, or royalties and other payments upon the commercial sale of products. Currently, our most significant strategic collaborations include the following:

Janssen. In December 2014, we entered into a collaboration and license agreement with Janssen for the development and commercialization of duvortuxizumab, a product candidate that incorporates our proprietary DART technology to simultaneously target CD19 and CD3 for the potential treatment of B-cell hematological malignancies. We contemporaneously entered into an agreement with JJDC, an affiliate of Janssen, under which JJDC agreed to purchase 1,923,077 new shares of our common stock for proceeds of \$75.0 million. Upon closing, we received a \$50.0 million upfront payment from Janssen as well as the \$75.0 million investment in our common stock. Janssen is leading the development of this product candidate, subject to our options to co-promote the product in the United States and Canada and to invest in later-stage development in exchange for a United States and Canada profit-share.

Janssen initiated a human clinical trial in 2015 for a variety of B-cell hematological malignancies, including diffuse-large B cell lymphoma, follicular lymphoma, mantle-cell lymphoma, chronic lymphocytic leukemia and acute lymphoblastic leukemia. The initiation of this trial triggered a \$10.0 million milestone payment to us. Assuming successful development and commercialization, we could receive up to an additional \$565.0 million in clinical, regulatory and commercialization milestone payments. If commercialized, we would be eligible to receive low double-digit royalties on any global net sales.

In May 2016, we entered into a separate collaboration and license agreement with Janssen for the development and commercialization of MGD015, a product candidate that incorporates our proprietary DART technology to simultaneously target CD3 and an undisclosed tumor target for the potential treatment of various hematological malignancies and solid tumors. The transaction closed in June 2016, and we received the \$75.0 million upfront payment from Janssen in July 2016. Under the collaboration and license agreement, we granted an exclusive license to Janssen to develop and commercialize MGD015. Janssen will complete the IND-enabling activities and will be fully responsible for the future clinical development and commercialization of MGD015. Assuming successful development and commercialization, the agreement entitles us to receive up to \$665.0 million in development, regulatory and sales milestone payments. If commercialized, we would be eligible to receive low double-digit royalties on any global net sales and have the option to co-promote the molecule with Janssen in the United States. Servier. In September 2012, we entered into an agreement with Servier to develop and commercialize three DART molecules in all countries other than the United States, Canada, Mexico, Japan, South Korea and India. We received a \$20.0 million upfront option fee. In addition, we became eligible to receive up to approximately \$1.0 billion in additional license fees and clinical, development, regulatory and sales milestone payments for each product Servier successfully develops, obtains regulatory approval for, and commercializes. Additionally, assuming exercise of its options, Servier may share Phase 2 and Phase 3 development costs and would be obligated to pay us low double-digit to mid-teen royalties on product sales in its territories.

In February 2014, Servier exercised its option to develop and commercialize flotetuzumab, for which we received a \$15.0 million license option fee. We also received two \$5.0 million milestone payments from Servier in 2014 in connection with the IND applications for flotetuzumab and MGD007 clearing the 30-day review period by the U.S. Food and Drug Administration (FDA). As of June 30, 2017, Servier still retains an option to obtain a license for MGD007, but has notified us that they have terminated their rights to license the third DART molecule.

Critical Accounting Policies and Significant Judgments and Estimates

Our critical accounting policies are those policies which require the most significant judgments and estimates in the preparation of our consolidated financial statements. A summary of our critical accounting policies is presented in Part II, Item 7, of our Annual Report on Form 10-K for the year ended December 31, 2016. There have been no material changes to our critical accounting policies during the three months ended June 30, 2017.

Results of Operations

Revenue

The following represents a comparison of our revenue for the three months ended June 30, 2017 and 2016:

| | Three Months Ended June 30, | | Increase/(Decrease) | |
|---------------------------------------|--------------------------------|---------|---------------------|--------|
| | 2017 | 2016 | | |
| | (dollars in millions) | | | |
| Revenue from collaborative agreements | \$1.1 | \$ 78.5 | \$ (77.4) | (99)% |
| Revenue from government agreements | 0.6 | 2.2 | (1.6) | (73)% |
| Total revenue | \$1.7 | \$ 80.7 | \$ (79.0) | (98)% |

| | Six Months Ended June | | Increase/(Decrease) | |
|---------------------------------------|--------------------------|--------|---------------------|--------|
| | 30, | 2016 | | |
| | (dollars in millions) | | | |
| Revenue from collaborative agreements | \$2.4 | \$80.4 | \$ (78.0) | (97)% |
| Revenue from government agreements | 1.4 | 3.1 | (1.7) | (55)% |
| Total revenue | \$3.8 | \$83.5 | \$ (79.7) | (95)% |

Collaboration revenue decreased by \$77.4 million for the three months ended June 30, 2017 compared to the three months ended June 30, 2016 and \$78.0 million for the six months ended June 30, 2017 compared to the six months ended June 30, 2016 primarily due to the \$75.0 million upfront payment under the Janssen MGD015 agreement and a \$2.0 million milestone payment from Pfizer, Inc., both of which were recognized in the second quarter of 2016. Revenue from government agreements decreased by \$1.6 million and \$1.7 million for the three and six months ended June 30, 2017 compared to the three and six months ended June 30, 2016, respectively, primarily due to less costs incurred under the NIAID cost plus fixed fee contract.

Research and Development Expense

The following represents a comparison of our research and development expense for the three and six months ended June 30, 2017 and 2016:

| | Three Months Ended June 30, | | Increase/(Decrease) | | |
|---|-----------------------------|--------|---------------------|--------|---|
| | 2017 | 2016 | | | |
| | (dollars in millions) | | | | |
| Margetuximab | \$10.4 | \$12.4 | \$ (2.0) | (16) | % |
| Enoblituzumab | 5.1 | 4.4 | 0.7 | 16 | % |
| Flotetuzumab | 0.9 | 0.1 | 0.8 | 800 | % |
| MGD007 | 1.7 | 0.6 | 1.1 | 183 | % |
| MGD009 | 0.8 | 0.6 | 0.2 | 33 | % |
| MGD010 | 0.5 | 1.4 | (0.9) | (64) | % |
| Duvortuxizumab | — | 0.7 | (0.7) | (100) | % |
| MGA012* | 3.1 | — | 3.1 | N/A | |
| Preclinical immune checkpoint programs | 5.1 | 5.3 | (0.2) | (4) | % |
| Other preclinical and clinical programs, collectively | 6.9 | 7.8 | (0.9) | (12) | % |
| Total research and development expense | \$34.5 | \$33.3 | \$ 1.2 | 4 | % |

| | Six Months Ended June 30, | | Increase/(Decrease) | | |
|---|---------------------------|--------|---------------------|-------|---|
| | 2017 | 2016 | | | |
| | (dollars in millions) | | | | |
| Margetuximab | \$21.1 | \$19.8 | \$ 1.3 | 7 | % |
| Enoblituzumab | 9.0 | 8.6 | 0.4 | 5 | % |
| Flotetuzumab | 1.9 | 1.9 | — | — | % |
| MGD007 | 2.9 | 1.6 | 1.3 | 81 | % |
| MGD009 | 1.9 | 1.5 | 0.4 | 27 | % |
| MGD010 | 2.1 | 3.2 | (1.1) | (34) | % |
| Duvortuxizumab | 0.1 | 2.1 | (2.0) | (95) | % |
| MGA012* | 5.5 | — | 5.5 | N/A | |
| Preclinical immune checkpoint programs | 10.0 | 10.8 | (0.8) | (7) | % |
| Other preclinical and clinical programs, collectively | 12.8 | 11.2 | 1.6 | 14 | % |
| Total research and development expense | \$67.3 | \$60.7 | \$ 6.6 | 11 | % |

*MGA012 was included in Preclinical immune checkpoint programs for the three and six months ended June 30, 2016.

During the three months ended June 30, 2017 our research and development expense increased by \$1.2 million compared to the three months ended June 30, 2016. This increase was primarily due to the initiation of a Phase 1 clinical trial of MGA012 in late 2016 and continued enrollment in our various clinical trials. These increases were

partially offset by a

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decrease in duvortuxizumab manufacturing costs, which are reimbursed by our collaborator. Our research and development expense increased by \$6.6 million for the six months ended June 30, 2017 compared to the six months ended June 30, 2016 primarily due to the initiation of a Phase 1 clinical trial of MGA012 in late 2016, continued enrollment in our various clinical trials and increased activity in our other preclinical and clinical programs. These increases were partially offset by a decrease in duvortuxizumab manufacturing costs, which are reimbursed by our collaborator.

General and Administrative Expense

The following represents a comparison of our general and administrative expense for the three months ended June 30, 2017 and 2016:

| | Three Months Ended June 30, | | Increase | |
|------------------------------------|--------------------------------|--------|----------|-----|
| | 2017 | 2016 | | |
| | (dollars in millions) | | | |
| General and administrative expense | \$8.4 | \$ 7.2 | \$1.2 | 17% |

| | Six Months Ended June 30, | | Increase | |
|------------------------------------|------------------------------|---------|----------|-----|
| | 2017 | 2016 | | |
| | (dollars in millions) | | | |
| General and administrative expense | \$15.8 | \$ 13.4 | \$2.4 | 18% |

General and administrative expense increased for the three and six months ended June 30, 2017 compared to the three and six months ended June 30, 2016 primarily due to increased professional fees, including consulting expenses, and increased employee compensation and benefit expense to support our overall growth.

Other Income

The increase in other income for the three and six months ended June 30, 2017 compared to the three and six months ended June 30, 2016 is due to an increase in interest income earned on investments.

Liquidity and Capital Resources

We have historically financed our operations primarily through public and private offerings of equity, upfront fees, milestone payments and license option fees from collaborators and reimbursement through government grants and contracts. As of June 30, 2017, we had \$243.7 million in cash, cash equivalents and marketable securities. In addition to our existing cash, cash equivalents and marketable securities, we are eligible to receive additional reimbursement from our collaborators, including under various government grants or contracts, for certain research and development services rendered, additional milestone payments and opt-in payments. However, our ability to receive these milestone payments is dependent upon our ability to successfully complete specified research and development activities and is therefore uncertain at this time.

Funding Requirements

We have not generated any revenue from product sales to date and do not expect to do so until such time as we obtain regulatory approval of and commercialize one or more of our product candidates. As we are currently in the clinical trial stage of development, it will be some time before we expect to achieve this and it is uncertain that we ever will. We expect that we will continue to increase our operating expenses in connection with ongoing as well as additional clinical trials and preclinical development of product candidates in our pipeline. We expect to continue our collaboration arrangements and will look for additional collaboration opportunities. We also expect to continue our efforts to pursue additional grants and contracts from the U.S. government in order to further our research and development. Although it is difficult to predict our funding requirements, based upon our current operating plan, we anticipate that our existing cash, cash equivalents and marketable securities as of June 30, 2017, as well as other

collaboration payments we anticipate receiving, will enable us to fund our operations into 2019.

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Cash Flows

The following table represents a summary of our cash flows for the six months ended June 30, 2017 and 2016:

| | Six Months Ended June 30, | |
|--|------------------------------|-----------|
| | 2017 | 2016 |
| | (dollars in millions) | |
| Net cash provided by (used in): | | |
| Operating activities | \$(66.1) | \$(65.1) |
| Investing activities | 64.8 | (69.1) |
| Financing activities | 33.8 | 0.4 |
| Net increase (decrease) in cash and cash equivalents | \$32.5 | \$(133.9) |

Operating Activities

Net cash used in operating activities reflects, among other things, the amounts used to run our clinical trials and preclinical activities. The increase in net cash used in operating activities during the six months ended June 30, 2017 compared to the six months ended June 30, 2016 was primarily due to higher research and development expenses.

Investing Activities

Net cash provided by investing activities during the six months ended June 30, 2017 is primarily due to maturities of marketable securities partially offset by purchases of marketable securities and making leasehold improvements to our facilities, including the build-out of our manufacturing suite at our headquarters location. Net cash used in investing activities during the six months ended June 30, 2016 was primarily due to investing our cash in marketable securities.

Financing Activities

Net cash provided by financing activities for the six months ended June 30, 2017 reflects cash proceeds from our securities offerings of approximately \$33.4 million, cash from stock option exercises and proceeds from the purchase of shares under our employee stock purchase plan. Net cash provided by financing activities for the six months ended June 30, 2016 reflects cash from stock option exercises.

Off-Balance Sheet Arrangements

We do not have any off-balance sheet arrangements, as defined under the rules and regulations of the Securities and Exchange Commission.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Our primary objective when considering our investment activities is to preserve capital in order to fund our operations. We also seek to maximize income from our investments without assuming significant risk. Our current investment policy is to invest principally in deposits and securities issued by the U.S. government and its agencies, Government Sponsored Enterprise agency debt obligations, corporate debt obligations and money market instruments. As of June 30, 2017, we had cash, cash equivalents and marketable securities of \$243.7 million. Our primary exposure to market risk is related to changes in interest rates. Due to the short-term maturities of our cash equivalents and marketable securities and the low risk profile of our marketable securities, an immediate 100 basis point change in interest rates would not have a material effect on the fair market value of our cash equivalents and marketable securities. We have the ability to hold our marketable securities until maturity, and we therefore do not expect a change in market interest rates to affect our operating results or cash flows to any significant degree.

ITEM 4. CONTROLS AND PROCEDURES

Disclosure Controls and Procedures

Our management, including our principal executive officer and principal financial officer, has evaluated the effectiveness of our disclosure controls and procedures as of June 30, 2017. Our disclosure controls and procedures are designed to provide reasonable assurance that the information required to be disclosed in our periodic reports filed with the SEC (such as this Form 10-Q) has been appropriately recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms, and that such information is accumulated and communicated to our management, including our principal executive officer and principal financial officer, to allow timely decisions regarding required disclosure. Based on their evaluation of our disclosure controls and procedures as of June 30, 2017, our principal executive officer and principal financial officer have concluded that our disclosure controls and procedures are effective at the reasonable assurance level.

Changes in Internal Control

No change in our internal control over financial reporting has occurred during the three months ended June 30, 2017, that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II. OTHER INFORMATION

Item 1A. Risk Factors

Our material risk factors are disclosed in Item 1A of our Annual Report on Form 10-K for the year ended December 31, 2016. There have been no material changes from the risk factors previously disclosed in our Annual Report.

Item 6. Exhibits

10.1* 2016 Employee Stock Purchase Plan (incorporated by reference to Exhibit 4.1 to the Registration Statement on Form S-8 (File No. 333-214386) filed by the Company on November 2, 2016)

31.1 Rule 13a-14(a) Certification of Principal Executive Officer

31.2 Rule 13a-14(a) Certification of Principal Financial Officer

32.1 Section 1350 Certification of Principal Executive Officer

32.2 Section 1350 Certification of Principal Financial Officer

101.INS XBRL Instance Document

101.SCHXBRL Schema Document

101.CALXBRL Calculation Linkbase Document

101.DEF XBRL Definition Linkbase Document

101.LABXBRL Labels Linkbase Document

101.PRE XBRL Presentation Linkbase Document

* Indicates management contract or compensatory plan

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

MACROGENICS, INC.

BY: /s/ Scott Koenig

Scott Koenig, M.D., Ph.D.

President and Chief Executive Officer

(Principal Executive Officer)

BY: /s/ James Karrels

James Karrels

Senior Vice President and Chief Financial Officer

(Principal Financial Officer)

Dated: August 2, 2017

EXHIBIT INDEX

Exhibit Page Number

| | |
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