Neoprobe Corporation

OTC: BB-NEOP- $0.58

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1Q01 Results

1Q01 Margins Improve Despite Temporary Component Shortage

Current Data		EPS	FY: Dec	P/E
Current Price	$ 0.58	2000	$ 0.04	14.2
52-Week Range	1.25 -.38	2001E	$ 0.03	18.9
Shares Out (Mill)	25.9	2002E	$ 0.04	15.5
Ave Volume LTM	79,300	**Valuation**	**Current**	**LTM**
Market Capitalization	$ 15.0	P/E (Next FY)	18.9	29-(4)
LTD/Total Capital (est.)	1.5%	P/B	6.7	32-4
Institutional Holdings	3.0%	Price/Sales	1.7	4-1
Insider Holdings	29%	**Operating Data**	**This Qtr**	**LTM**
Book Value (est.)	$ 0.09	Sales Growth	-35.5%	-4.4%
30Yr Bond	5.70%	EBITDA Margin	14.6%	53.4%
Oil/Barrel	$ 27.57	Net Inc. Growth	210%	113.6%

Source: Baseline, Big Charts, and researchstock.com

Source: Big Charts

Key Investment Points

- 1Q01 EPS was $0.00 versus a loss of $0.03 in 1Q00.
- Sales were lower than expected due to a temporary component shortage that delayed some sales until 2Q01.
- Recent stock rise due to announced joint venture to find a new cancer therapy.
- We raised our 12-18 month target price to $1.00, but this does not factor in any benefits from the joint venture.

Company Description

Dublin, Ohio-based Neoprobe is dedicated to improving the diagnosis and treatment of cancer by the innovative use of gamma guided surgery. Neoprobe's main product is a gamma detection device used for a surgical procedure called intraoperative lymphatic mapping ("ILM") of the sentinel node. ILM is a minimally invasive technique for evaluating the potential spread of cancer to lymph nodes. Surgeons are using lymphatic mapping as a standard of care for patients with malignant melanoma and investigating its use with breast cancer. The company is developing strategic partnerships to commercialize products worldwide that are based on its proprietary radioimmuioguided surgery technology (RIGS®).

The Bottom Line

NEOP remains a company of great potential. Despite the challenges of 1Q01, the Company remains one of the few in its peer group to have profitable operations and cash flows. The June 5, 2001 announcement of the collaboration between NEOP and Aastrom Biosciences, Inc. (NASDAQ: ASTM) to develop a new cell therapy delivery mechanism that will utilize ACT technology to treat cancer is an example of this. Subsequent to the announcement, the stock price spiked to an intra-day high of over $1.00, reflecting market expectations of what the collaboration could bring to the companies. If the price holds above $0.50, we think it would be an indication that the announcement increased investor awareness of NEOP.

We revised our 12-18 month target price to $1.00 (up $0.06) based on our forecast of NEOP's current business. Our earnings model and target price does not reflect any of the potential benefits from the Aastrom collaboration because we cannot quantify the impact on NEOP's operations.

1Q01 Results

Results for the first quarter improved over 1Q00, despite lower than expected sales. EPS for 1Q01 was $0.00 versus a loss of $0.03 in 1Q00. This was lower than our $0.01 EPS forecast due mainly to a temporary disruption of component deliveries that caused sales to fall below our expectations.

Total revenues for the quarter were $1.6 million versus $1.8 million in 1Q00. We estimate that unit sales (total revenues net of license fees) were almost $1.4 million versus $1.6 million in 1Q00, a decline of 13%. Part of this decline was expected as NEOP's original contract with Ethicon Endo-Surgery, Inc. ("EES") called for a new pricing structure in 2001. However, a delay in outsourced component deliveries caused some sales to be delayed until 2Q01 and resulted in the lower than expected unit sales.

NEOP's sales growth has slowed recently (see Figures 1 and 2, next page) for three reasons:

- The shift from retail to wholesale pricing. Prior to the EES contract, NEOP sold "direct" at a retail price. Under the EES agreement (that started in 4Q99), NEOP now sells units to EES at a "wholesale" price.

- Sales growth in 4Q00 turned negative due to a difficult comparison with 4Q99 when sales benefited from the initial shipment of units and demo units to EES.

- As noted above, a component shortage delayed sales in 1Q01.

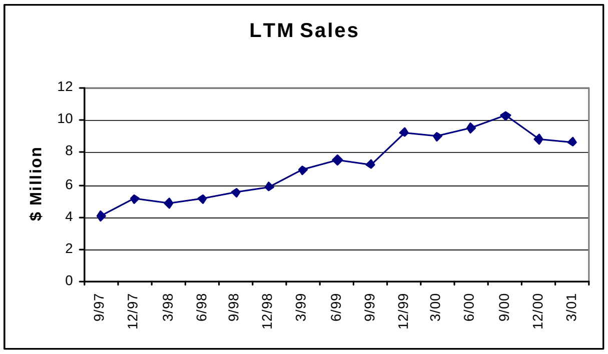

Figure 1

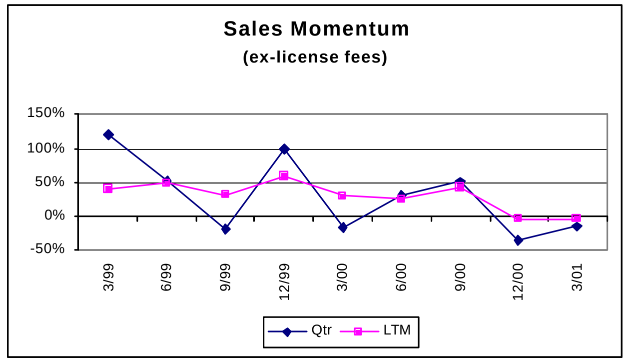

Figure 2

Despite lower sales, operating margins improved to 1.9% from a negative 3.4% as lower operating costs offset a decline in the gross margin to 48.1% from 63.4%. A lower gross margin was expected due to the re-pricing of the EES contract, but actual results beat our forecast of 29.8%. Also:

- R&D expenses fell dramatically (75%) as the result of EES reimbursement for some R&D and as 1Q00 contained non-recurring severance and un-reimbursed development costs.
- Marketing expense dropped to zero, which is consistent with the trend during the last year and is due to EES assuming the marketing responsibility. 1Q00 also had severance costs.
- General administrative expenses fell to 40.9% of sales from 41.6% in 1Q00 due to continued cost controls.

As a result, NEOP posted net income of $81,000 versus a net loss of $27,000 in 1Q00. Figures 3 and 4 illustrate the longer-term trend in net income

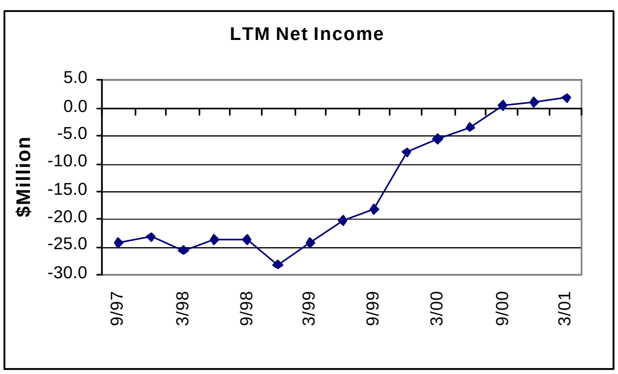

Figure 3

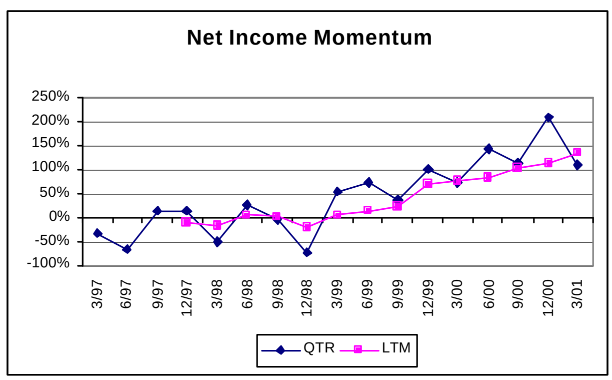

Figure 4

Table 1 compares the operating results for 1Q01 and 1Q00.

Table 1: Comaprative Operating Results			
($Million)	**1Q00**	**1Q01**	
Revenues	1.856	1.619	-13%
COGS	0.838	0.948	13%
Gross Income	1.018	0.671	-34%
R&D	0.294	0.074	-75%
Marketing	0.111	0.000	-100%
Gen & Admin.	0.668	0.570	-15%
Operating Income (Loss)	-0.055	0.027	149%
Other, Net	0.028	0.054	93%
Net Income (Loss)	-0.027	0.081	400%
Loss-retirement of prefrd Stk	-0.764		
Net to shareholders	-0.791	0.081	110%
Diluted EPS	$ (0.03)	$ 0.00	110%
Diluted Shares O/S	25.395	26.086	3%
Margin Analysis			
Gross	55%	41%	
Operating	-3%	2%	
Net to Shareholders	-43%	5%	

The component delay had a minimal impact on 1Q01 asset utilization. As shown in Figure 5, days sales outstanding (DSO) increased slightly due to the decline in sales. Inventory turnover continued to improve, but we expect the ratio to decline as NEOP builds reserves to avoid a future component shortage

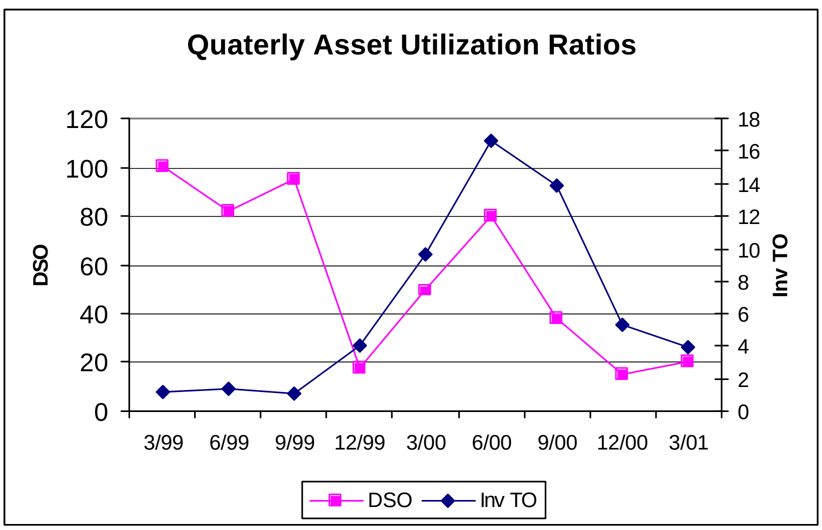

Figure 5

Operating cash flow fell to -$817,000 from -$714,000 in 1Q01 and $1.3 million in 4Q00. The main reason for the negative cash flow is the build up of inventories to meet current demand and provide a buffer supply of components.

Financial Condition

NEOP's financial condition continues to improve. As shown in Figure 6, leverage remains low. Prior to 1Q00, the debt/equity ratio ranged from 18% in 1Q98 to 42% in 2Q99. During the last half of 1999, the ratio was distorted as the result of a capital restructuring (redemption of preferred stock: see our initial report dated October 16, 2000 for more details).

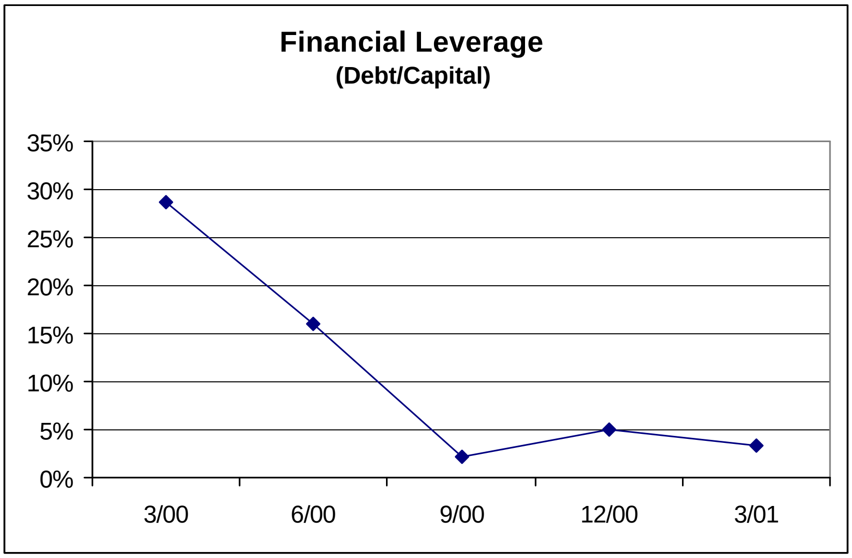

Figure 6

Peer Group Comparison

NEOP outperformed the peer group despite the challenges caused by the new pricing structure and component shortage. As shown in Table 2, NEOP's;

- Net margin lead the field for the trailing 12-month period, despite the 8% drop in sales,
- EPS was better than 75% of the peer group, and
- Leverage ratio was the lowest of the group.

Table 2: Sector Comparables			**Performance Last 12 Months (LTM)**						
(Million except ratios and EPS)			**Revenues**		**Net**			**Debt/**	**Interest**
Company	**Ticker**	**Price**	**(Million)**	**% Chg**	**Margin**	**EPS**	**% Chg**	**Capital**	**Cover**
NEOPROBE CORP.	**NEOP**	**$ 0.58**	**$ 8.8**	**-4%**	**27.9%**	**$ 0.04**	**112%**	**1.5%**	**22.9**
PEER GROUP (see below)		$ 8.67	$ 16.9	67.1%	-415.8%		43%	2.5%	5.2
JOHNSON & JOHNSON	JNJ	$ 52.03	$ 30,000	6%	16.8%	$ 1.77	15%	7.3%	58.7
Peer Group									
TRIPATH IMAGING	TPTH	$ 7.75	$ 34.0	52%	-53.2%	$ (0.37)	61%	2.9%	-
CELSION	CLN	$ 0.90	$ 0.4	0%	-1425.0%	-	na	-	-
FISCHER IMAGING	FIMG	$ 6.70	$ 49.0	-18%	4.1%	$ 0.28	176%	2.8%	5.2
VISTA MEDICAL TECH	VMTI	$ 1.08	$ 6.7	3%	-55.4%	$ (0.21)	60%	-	-
MATRITECH	NMPS	$ 3.40	$ 1.8	110%	-458.8%	$ (0.29)	-16%	1.9%	-
CHROMAVISION MED SYS	CVSN	$ 5.50	$ 1.9	326%	-844.4%	$ (0.76)	-15%	-	-
VYSIS	VYSI	$ 27.30	$ 26.0	20%	7.7%	$ 0.07	108%	-	-
PHOTOELECTRON	PHX	$ 4.45	$ 1.1	59%	-781.8%	$ (0.92)	-3%	-	-
IGEN INT'L	IGEN	$ 20.97	$ 31.0	52%	-134.9%	$ (1.99)	-25%	-	-
(Source: Baseline, researchstock.com)									

Product Development
NEOP provided additional information on their efforts to widen the Company's product line:

- Patient enrollment began in clinical evaluations of NEOP's proprietary lymphatic targeting agent.

- NuRigs, Ltd. submitted applications for regulatory approval to begin clinical evaluations of the colorectal RIGScan product (that NEOP licensed to them), but the FDA requested additional information.

- NEOP received three new patents, including one for a laparoscopic probe, and received notice of allowance for three additional patents.

- New instrument products have reached the prototype stage and the Company is planning to begin the clinical evaluation.

Outlook
We are reiterating our EPS forecast of $0.03 in 2001 and raised our 2002 forecast to $0.04 (up $0.01). Our sales forecast for the remainder of 2001 is unchanged because we are not assuming that any sales lost in 1Q01 will be recouped in 2Q01. However, this is a possibility. We did reduce our assumption on quarterly marketing spending from $70,000 to the $20,000-$30,000 range in 2001, but this did not have a material impact. In 2002, the reduced marketing assumption ($40,000 from $70,000) and reduced G&A did result in the $0.01 increase in 2002. Table 3 contains our annual forecast and Table 4 shows our quarterly expectations.

Table 3: Annual Income Statement & Forecast
($Million, except per share data)

	1996	1997	1998	1999	2000	2001	2002
Unit Sales	1.17	5.13	5.83	9.25	8.84	**8.39**	**9.90**
Lic Fees	0.00	0.00	0.00	0.20	0.88	**0.88**	**0.80**
Total Revs	1.17	5.13	5.83	9.45	9.71	**9.27**	**10.70**
COGS	0.68	1.58	1.40	4.51	4.99	**5.85**	**6.93**
Gross Margin	0.49	3.55	4.43	4.94	4.72	**3.42**	**3.77**
Market/Sell	1.53	4.31	5.27	4.47	0.28	**0.08**	**0.16**
G&A	6.22	6.85	6.09	3.74	2.68	**2.34**	**2.42**
R&D	16.08	19.66	14.37	1.31	0.47	**0.45**	**0.46**
Discont. Ops	0.00	0.00	7.18	0.48	0.00	**0.00**	**0.00**
Operating Income	-23.34	-27.27	-28.47	-5.06	1.29	**0.56**	**0.72**
Interest Inc	0.00	0.00	0.60	0.10	0.21	**0.13**	**0.10**
Interest Expense	0.00	0.00	-0.19	-0.08	-0.03	**-0.01**	**-0.01**
Other Income/(Exp.)	2.37	4.02	0.03	0.16	0.37	**0.13**	**0.16**
PreTax Income	-20.97	-23.25	-28.03	-4.17	1.84	**0.80**	**0.97**
Inc Taxes	0.00	0.00	0.00	0.00	0.00	**0.00**	**0.00**
Net Inc	-20.97	-23.25	-28.03	-4.17	1.84	**0.80**	**0.97**
Stock Conversion	0.00	0.00	0.00	-3.72	-0.76	**0.00**	**0.00**
Net to Comm SH	-20.97	-23.25	-28.03	-7.90	1.08	**0.80**	**0.97**
EPS-Dil	**$ (1.06)**	**$ (1.02)**	**$ (1.23)**	**$ (0.34)**	**$ 0.04**	**$ 0.03**	**$ 0.04**
Shares	19.743	22.735	22.842	23.003	26.319	**26.087**	**26.087**
Growth Rates							
Unit Sales	22.0%	337.9%	13.7%	58.5%	-4.4%	**-5.0%**	**17.9%**
Operating Income	-102.6%	-16.8%	-4.4%	82.2%	125.5%	**-56.6%**	**29.8%**
Net Income	94.9%	10.9%	20.6%	-71.8%	-113.6%	**-25.8%**	**21.9%**
EPS		3.7%	-20.0%	72.0%	111.9%	**-25.1%**	**21.9%**
Margin Analysis							
Gross (ex-Lic Fees)	42.2%	69.3%	75.9%	51.2%	43.5%	**30.3%**	**30.0%**
Operating	-1993.4%	-531.7%	-488.1%	-54.7%	14.6%	**6.6%**	**7.3%**
Net	-1790.8%	-453.3%	-480.6%	-45.1%	20.8%	**9.5%**	**9.8%**

Boldface data are estimates

Table 4: Quarterly Forecast

	1Q	2Q	3Q	4Q	FY
1998	$ (0.31)	$ (0.23)	$ (0.24)	$ (0.44)	$ (1.23)
1999	$ (0.14)	$ (0.06)	$ (0.15)	$ 0.01	$ (0.34)
2000	$ (0.03)	$ 0.02	$ 0.02	$ 0.03	$ 0.04
2001	$ 0.00	**$ 0.01**	**$ 0.01**	**$ 0.01**	**$ 0.03**

Boldfaced data are forecasts

Valuation

The recent announcement of the joint venture with Aastrom Bioscience (ASTM-$1.91) increased investor expectations for NEOP's earnings potential and caused the shares to rise to a level that approximates our current 12-18 month target price of $1.00. While we think there is a potential for increased earnings from the partnership, our earnings model does not incorporate any impact at this point. However, the increased awareness that NEOP has received as the result of the announcement could be a catalyst for valuation multiples that exceed our expectations.

Since the announcement of the Aastrom joint venture (on June 5th), the shares have risen 150%, from $0.40 at the start of the month to $1.00 on June 8th. As a result, NEOP's valuation metrics have improved, but remain below peer group averages. The key points to note in Table 5 are:

- NEOP remains relatively undervalued on a price/sales and price/book basis,
- NEOP is the only one with expectations of positive earnings, and
- For stocks with similar market caps (under $50 million), NEOP is undervalued on a price/sales basis and the only one with positive EPS in 2000 and expectations of positive EPS in 2001.

Table 5: Comparative Valuation Data

		Price			Market			Calendar P/E		
Company	**Symbol**			**LTM %**	**Cap.(MM)**	**P/B**	**P/S**	**2000**	**2001**	**2002**
NEOPROBE CORP.	**NEOP**	**$**	**0.58**	**28%**	**15**	**6.7**	**1.7**	**14.2**	**18.9**	**15.5**
PEER GROUP AVERAGE		$	8.67	32%	144	17.1	22.5	-25.9	-14.8	-7.8
JOHNSON & JOHNSON	JNJ	$	52.03	16%	145,369	7.3	4.9	29.4	30.5	27.0
Peer Group Detail										
IGEN INT'L	IGEN	$	20.97	23%	362	-	11.6	-10.6	-8.6	-16.5
TRIPATH IMAGING	TPTH	$	7.75	24%	265	3.4	7.7	-20.4	-27.7	19.4
VYSIS	VYSI	$	27.30	221%	278	19.5	10.8	-170.6	na	na
CHROMAVISION MED	CVSN	$	5.50	-50%	111	11.5	57.1	-7.4	-8.1	-26.2
MATRITECH	NMPS	$	3.40	-46%	88	22.8	48.8	-12.6	na	na
CELSION	CLN	$	0.90	-76%	69	56.2	-	na	na	na
FISCHER IMAGING	FIMG	$	6.70	198%	58	2.0	1.2	23.9	na	na
PHOTOELECTRON	PHX	$	4.45	-6%	43	-	39.5	-5.2	na	na
VISTA MEDICAL TECH	VMTI	$	1.08	2%	21	4.0	3.2	-4.7	na	na

Source: Baseline, Company data, and researchstock.com.

Our 12-18 month target price of $1.00 is the mid point of our target range ($1.45 - $0.56) and is based upon our expectations of NEOP's current operations and does not include any upside from the Aastrom collaboration. Our target price also uses valuation multiples that are more reflective of the recent past rather than what could occur from an overall rise in investor interest (see Table 6, next page). One could argue that, based upon this new interest, the target price should be closer to the high end of the range. But we will leave that to the reader to decide.

Table 6: Target Price Calculations

Price to:	LTM Range Absolute	LTM Range Average	Current	Forecast Multiple	2001 Estimate	Range
Sales	4.0	2.8	2.9	3.0	$ 0.36	$ 1.07
	1.1	1.5		1.5		$ 0.53
Book	32.4	16.5	11.6	14.0	$ 0.18	$ 2.54
	4.4	8.7		5.0		$ 0.91
EPS	33.8	9.4	32.7	20.0	$ 0.04	$ 0.75
	-4.0	6.3		6.0		$ 0.22

Average	High	$ 1.45
	Low	$ 0.56
	Average	$ 1.00

Risk Consideration

Investors need to consider the following risks before investing:

The stock is currently susceptible to more downside risk as the result of its recent and sudden rise. Selling pressure could come from day-traders and shareholders who are looking for an exit.

The Company currently sells just one product (the ILM technology) with a growing number of attachments and supplies.

It is difficult to forecast future sales because detailed information is not disclosed. Our forecasts assume a modest steady growth, but actual sales levels could be more erratic and cause EPS to vary from our forecast.

While other uses are under development, the units are only widely used in the diagnosis and treatment of two primary types of cancer: melanoma and breast cancer. While the Company believes that its technology has significant advantages over other methods, broad-based acceptance will not occur until physicians outside major cancer centers and teaching hospitals adopt the ILM approach.

NEOP is highly dependent on EES, the company's exclusive distributor. EES is a subsidiary of Johnson & Johnson. EES has agreed to purchase a minimum quantity of NEOP products during the first three years (until late 2002) of the first five-year term of the agreement. However, there can be no assurances that EES will purchase product from NEOP in excess of the minimum or that such purchases will generate sufficient cash flow to finance NEOP's operations over the long term.

The Company has outsourced its manufacturing needs and is dependent on one supplier. While we think it was a good decision to outsource manufacturing, this does result in the risk that the supplier may devote resources to other clients and not meet the needs of NEOP.

The Company's balance sheet does not reflect any obligations of Neoprobe Israel. However, it is possible, in the event that proceeds from the liquidation of Neoprobe Israel do not fully satisfy its outstanding obligations, that creditors could seek to pursue claims against NEOP (referred to as "piercing the corporate veil"). If such claims were successful, NEOP would be required to pay creditors some or all of the amounts owed by Neoprobe Israel. Such payments would severely deplete NEOP's cash and the Company may not be able to continue operations without seeking relief from creditors. However, management believes that the prospect that creditors would prevail if claims were brought against NEOP is remote. As such, NEOP has made no provision for such a contingent liability.

The shares are not very liquid and thus subject to volatility. Average daily volume for the last 50 days has been about 72,400 shares and 97,900 during the last 12 months.

The Company is not widely followed by Wall Street analysts. Consequently, it is possible that the stock could remain undervalued due to a lack of analyst support.

Investors should read the Company's SEC filings and consider their risk tolerance, cash needs, and investment time horizons before investing in this, and any small cap stock.

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