

Big pharma on biotech acquisition spree

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Pharma giants have finally come to realize that acquisition of biotech companies is their last hope with patents expiring and R&D pipelines drying up.

Multi-billion dollar deals is something pharma and biotech companies should get used to by now. The life sciences industry had in March, 2009, completed its hat trick with, Roche and Genentech ending their long drawn 'hostile war', by entering into a mutual agreement, with the former buying out the latter for \$46.8 billion at \$95 per share. What is all the more exciting is analysts predicting that a spate of similar deals will follow suit in the current year. These acquisitions has but gone much against market soothsayers advice on shutting out options of large scale investments (mainly M&As) during a period of prolonged recession. "The industry is going through a transition, and such deals were bound to happen to prevent the death of the big pharma, be it recession or no recession," confided a reliable industry analysts under the condition of anonymity. Earlier in the beginning of the year, we had seen big pharma, Pfizer, buying over Wyeth for \$68 billion, the fourth largest acquisition in the pharmaceutical industry. This was followed by another US-based giant, Merck, closing its \$41 billion dollar deal to acquire Schering Plough. A marriage between the pharmaceutical and biotech companies has suddenly become a reality and it is accelerating at a breakneck speed.

Cash is king

An acquisition was a much more attractive proposition for these bigwigs than an alliance or licensing deals. Much has been debated. Firstly, it is but a myth that banks and financial institutions are reluctant to lend money for such deals. The more appropriate answer is "Big pharma can afford to go ahead with such mighty deals. They have their own cash reserves and then we have stocks. For the Pfizer-Wyeth deal, Attribute it to the notion that this is the right time for large scale M&As. Experts unanimously point out that the ideal mantra at this time is "This is the ideal time for buyouts because valuations for biotech companies are at an all time low so this is the ripe time for pharma to acquire them." The Pfizer-Wyeth acquisition deal was financed through cash, debt and stocks with banks giving out cash amounting to \$22.5 billion.

The symbiotic relationship

With the lurking fear among big-wigs as their revenues taking a nose dive due to drying up of R&D pipelines and patent expiration of blockbuster drugs, these deals will definitely be the answer to their prayers.

While commenting on the acquisition trend Sujay Shetty, associate director, Financial Advisory Services Pharma/LifeSciences, Pricewaterhouse Coopers Pvt Ltd said, "These acquisitions will strengthen the pipeline of the pharma companies and prevent their revenues from falling. Like for Merck, it will also give them access to the emerging markets. These deals will also help in a lot of cost reductions. Tapping of emerging markets comes more in their long term strategy. It has been estimated that by 2012 when patents expire, revenue losses may amount up to \$130 billion."

The environment now is such that on one hand we have big pharma companies sitting on lots of cash, their account books showing minimal margins of cash debt, which on an average is just around six percent, but they are on the verge of collapse with drying up pipelines and patents of their blockbuster products; while on the other hand we have biotech companies, having a slew of innovative products in their pipeline, which are slated to be the next 'big thing' yet reeling under a credit crunch during the prolonged period of recession. There is a strategic similarity to all these deals. "The purpose of all the three deals is cost cutting; for each of the deal, both companies have targets which fit into each other's business models. They are complimentary to each other. Its more of the US and European companies coming together," said Supratim Majumdar, industry analyst, South Asia and Middle

East, Healthcare, Frost & Sullivan.

Take Merck-Schering Plough deal for instance, both the companies have overlapping portfolios for cardiovascular, respiratory and anti-viral drugs, and experimental drugs. Schering-Plough will add animal health products and a consumer division to Merck's profile, while bolstering its women's health area, led by Merck's cervical cancer vaccine, Gardasil. The companies already had an agreement with their cholesterol treatment, Vytorin, a combination of Schering-Plough's Zetia and Merck's generic drug Zocor. Moreover Schering-Plough has drugs in late-stage testing that may top \$6 billion in annual sales, and already has a partnership with Merck to split sales of the Zetia and Vytorin cholesterol pills, which generated \$4.6 billion last year.

A Pfizer-Wyeth conglomerate will bring about a 50 percent increase in total revenues. Nandakishore K, industry manager, Health care Practice, Frost and Sullivan had earlier told BioSpectrum when the deal was just announced, "Pfizer's dependency on one drug is huge. A merger will bring about a consolidation in their market position not just in the purely pharmaceutical space but in diversified areas like vaccines, animal health and biologicals."

"Wyeth's product portfolio includes the more non-traditional areas of pharmaceuticals which in a way compliments with that of Pfizer, which focus on niche areas like oncology and antibiotics. A nexus will give them a wider base," said Ajit Mahadevan, partner, Advisory Services, Ernst and Young. About 12 percent of Wyeth's revenues comes from consumer healthcare, five percent from animal health and 36 percent from biologics. At present, Pfizer has a product pipeline which includes clinical trials for Sutent (oncology) 10 phase-I programs whose mechanisms have not yet been designed. In the same therapeutic segment, Wyeth's products include clinical trials like Posutinib (for diseases like breast cancer) and Inotuzumab. Pfizer has two phase-II and one Phase-I trial in Alzheimer while Wyeth has five phase-I programs in this segment.

In a joint statement given by both the parties it was specified, "This combination means a broad portfolio of health care solutions and treatments for every stage of life: leadership positions in key therapeutic areas such as cardiovascular, oncology, women's health, CNS and infectious disease; in vaccines, biologics and small molecules; and in animal health, with products for companion animals, biologics and anti-infectives. A robust pipeline of biopharmaceutical development projects include programs in inflammation/immunology, oncology and pain, as well as a significant opportunity to find a cure for Alzheimer's disease."

The Roche-Genentech deal, is more a synergy of capabilities and expertise. The combined company will be the seventh largest pharmaceuticals company in the US in terms of market share. It will generate approximately \$17 billion in annual revenues and will employ around 17,500 employees in the US pharmaceuticals business alone, including a combined sales force of approximately 3,000 people.

Genentech's anti-cancer drug as well as best selling product, Avastin, will be something both parties will be pinning their hopes on. The study data expected to be released in April, 2009, on the effectiveness of Genentech's Avastin in treating early-stage colon cancer. The drug is already approved for various types of breast, lung and colon cancers.

Research and early development will operate as an independent center within Roche from its existing campus in South San Francisco, retaining its talent and approach to discovering and progressing new molecules. Roche's Pharma commercial operations in the US will be moved from Nutley, New Jersey to Genentech's site in South San Francisco. The combined

company's US commercial operations in pharmaceuticals will operate under the Genentech name, leveraging the strong brand value of Genentech in the US market. Roche has already begun to wind down operations at its Palo Alto facility and will relocate the site's virology research and development activities to South San Francisco. Roche's Palo Alto Inflammation group is in the process of becoming part of Roche's Nutley research and development organization. Genentech's late stage development and manufacturing operations will be combined with the global operations of Roche, achieving substantial scale benefits, operational synergies and cost avoidance. Roche's manufacturing operations in Nutley will be closed and support functions, such as informatics and finance, will be consolidated with those of Genentech.

The darker side

The bad news is that the mergers and acquisitions might blunt the incentive for innovation for biotech companies which have been swallowed by their pharma partners. There have been fears that these pharma giants may bring a stopgap to research of some innovative products which biotech companies have been working upon.

The much feared about change which might come about is layoffs which was already initiated and declared during the Pfizer-Wyeth deal. When the Pfizer-Wyeth deal was announced there were rumors doing the rounds of a possible 20,000 cuts in jobs globally, out of which 8,000 would be researchers. Merck has already declared that it would cut jobs by 16,000 along with operating costs to improve their bottom lines. After the deal was closed Roche-Genentech came up with a press release which stated, "Synergies will be largely driven by reducing complexity and eliminating duplicative functions and processes in areas like late stage development, manufacturing, corporate administration and support functions. Savings resulting from this combination will enable the new company to increase and better focus its investment in innovation."

The Roche-Genentech deal will see job cuts amounting to almost 1,500 most of which will be from commercial operations, largely sales and marketing personnel. Skeptics also foresee that such mergers might slow down R&D activities. Their contention being that big R&D teams do not necessarily mean bright future prospects of blockbuster drugs. They opine that scientists operate better in comparatively small teams. In the past, we have also seen big pharma going into numerous other acquisitions with the same purpose of portfolio strengthening, spending billions of dollars on R&D alone, however it failed to lead to an upsurge of products. "The R&D structure is different for pharma and biotech. So to mathematically assume that innovative products will double with a merger of two R&D teams is incorrect. A lot depends on integration," asserted Majumdar.

However, Shetty gives a justification for his disagreement. "Pharma companies were looking incremental innovation, higher productivity and strengthening of R&D. For this a much deeper impact was required. These acquisitions will help them achieve such targets. Plus this is the right time for such deals with valuations reaching historic lows and cost reduction pressures".

Who is next in the pipeline ?

The three 'blockbuster' mergers will offset and probably build on the pressure for many other pharma companies to follow suit. There are talks doing the rounds of Bristol Myers Squibb (BMS) going the same route. "Yes in fact before the Merck-Schering Plough deal, we had anticipated either Merck or BMS going in for a mega deal. So now with Merck having already acquired Schering Plough, we are expecting BMS going into a similar deal," said Shetty.

"I do not think we will see more than two mega deals coming through this year or even towards early 2010. Out of which BMS is a likely candidate for the next deal," confirmed Majumdar. From the biotech side Amgen and Genezyme are some of the likely candidates to be acquired. Both these companies have their focus on niche areas, have products which are most likely to become blockbusters. Genezyme for instance, has its focus on rare diseases, giving its products less prone to competition. Other attractive biotech companies include Biogene, Vertex and Amylin.

The year 2009, is definitely a landmark in the history of the life sciences industry. But the message now is loud and clear- Biotech is the place to be!

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