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Pharma-biotech partnership balance shifts

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Impact: Under the cover of credit crunch, big pharma is likely to swoop repeatedly to acquire substantial biotech targets

The impact of the credit crunch on the corporate world is "the abrupt loss of cheap debt". However, the big pharmaceutical companies have stayed out of the cheap debt game and as a result, the credit crunch will actually play out as a net positive for an industry much in need of good news.

According to Dr Chris Phelps, head of company analysis at Datamonitor, pharma companies are not only expected to weather the financial storm successfully but to also use this period to exploit their unique cash strength by embarking on an acquisition spree.

The average net debt as a proportion of capital employed for the top 20 pharmaceutical companies is just six percent, while the average net debt carried by financial institutions is 95 percent. This fact alone suggests that the fallout from the credit crisis will not be as significant in the pharmaceutical industry as in other more highly leveraged sectors.

According to Datamonitor, when this is combined with the fact that the average top 20 pharma company has access to $7.5 billion in cash, equivalents and short-term investments, the ability of large pharma companies to weather the credit storm is very clear.

Impact on Asian market

Although the credit crunch has no direct impact on the Asian pharmaceutical industry like the global pharmaceutical industry but it will have some impact on the niche and upcoming biotechnology sector which is heavily dependent on financing and venture capital or government support.

Sharing his concerns on the crisis and impact on Chinese pharma market, Dr T J Deng, Senior Director, Bioanalytical DMPK & Analytical Chemistry at BioDuro Beijing, China said, "The pharmaceutical industry is relatively recession-proof unlike other industries which are already facing the pinch. However, the biotechnology industry will have a hard time ahead as these companies will likely face a problem in raising capital. Also, the valuation of these companies might drop when they look for being acquired by big pharma companies.

But for CROs, it is a good time as outsourcing might increase in the coming months. Though there is a possibility that mid-size companies in the US and Europe might withdraw their orders. This might put small-sized CROs in a fix. Coming to the manufacturing front, the Chinese API companies will end up with marginal profit due to volatility in currency and rising costs. The only companies that can sustain the pressure are the big pharmaceutical companies that have huge capital.

Sharing similar views Dr Prasad Kanneganti, Quality Operations Director, Pfizer-Asia Pacific, Singapore, states that the pharma industry is recession-proof. "During recession people become too stressed. They need to take care of their health and need rather more medicine. I think this is a correction phase for the industry. The companies that do diligent homework will survive. India and China have better chance of receiving outsourcing business. On the other hand, the biotech companies, I guess, might face some problems," he says.

Meanwhile, Singapore assured the scientific community that government funding for scientific research and development, that helped push it to a record 2.6 percent of gross domestic product last year, will not be cut in the current economic downturn. "The government is fully committed to its investment in R&D as a vital driver of the economy for the future," promised Mr Lee Hsien Loong, Prime Minister of Singapore while speaking at the opening of science and technology research and development center Fusionopolis in mid-October, this year.

"The current economic crisis in the US and Europe will be a boon for the CROs in India and China particularly the Indian firms," believes Dr B S Patravale, President of Aarti Industries, a custom synthesis and contract research company from India.

"The growth rate of our sales for the current fiscal year will be affected as compared to the previous years. The volatility in the currency will hit hard the end users, as India is very price sensitive market. The companies might tighten their budget on R&D,"
-Mr S Thyagarajan, Chairman, Spinco Biotech, Chennai

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Reacting to the crisis, Dr Sureerat Prachartum, Vice President, Thai Pharmaceutical Manufacturers Association, Thailand, says: "At present we don't see any impact on our pharmaceutical industry. The companies that are involved in export might get affected. But in Thailand there are hardly any companies that are involved in pharma exports."

While making comments on research activities, Dr Uthai Suvanakoot, Associate Professor, Chulalongkorn University, Bangkok, Thailand said, "We don't feel the heat of credit crunch on our research initiatives in Thailand."

Smaller countries are also not unsettled by this. Talking about the impact on the Sri Lankan pharma industry, Mr Thusitha Wilegoda, Managing Director, Labmasters, Sri Lanka, said, "For next three-four months, I think, the crisis will not have any impact on the industry. The small local pharmaceutical manufacturing industry in Sri Lanka like the one in Bangladesh, Nepal might face problem if the problem lasts for long. On the other hand the R&D institutes that are receiving foreign grants are likely to face problem in near future."

On the contrary, the bio suppliers sector in the region might face some problem. Mr S Thyagarajan, Chairman, Spinco Biotech, a leading bio supplier from India notes that the crisis will affect the revenue in the coming months. "The growth rate of our sales for the current fiscal year will be affected as compared to the previous years. The volatility in the currency will hit hard the end users, as India is very price sensitive market. The companies might tighten their budget on R&D," he adds.

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While the credit crunch promises to strengthen large pharma, the outlook is far from positive for small biotech players. The biotechnology companies and research organizations that are dependent on finance from venture capital and financial institutions are likely to face problems in raising capital for their further research and clinical research/trial activities. Either they have to look out for partnerships with the big pharma companies which are already headhunting for acquisition of smaller biotechs with good number of molecules in product pipeline or to be acquired by these giants.

Over the last decade, the pharma industry has increasingly looked at the biotechnology sector to help replenish its dwindling product pipelines. A symbiotic relationship has been established whereby biotechs provided innovative therapies and in return, pharma firms pumped-in funding and development know-how. A natural balance was established in the pharma-biotech relationship: risk and reward were shared.

However, in recent years biotech's access to funding from other sources of capital has become easier. Financing became cheaper and the balance of power in the pharma-biotech relationship shifted: pharma's need for access to biotech products increased significantly, while biotech's need for pharma funding diminished.

Consequently, biotechnology companies could afford to either carry more risk themselves by taking their projects deeper into clinical development or by demanding more favorable terms from the increasingly desperate pharma industry. This shift in power towards biotech companies is reflected in the declining number of licensing deals between pharma and biotech companies," Dr Phelps elaborates.

The current credit crisis it appears is set to change again the balance of power in the pharma-biotech relationship. Biotechnology companies' ready access to capital and funding has dried up almost overnight, and while there are few that will struggle immediately, the funding of their operations in the long term looks more difficult. In terms of licensing deals biotech companies will be forced to accept less favorable terms. According to Dr Phelps, under the cover of the credit crunch, big pharma will swoop repeatedly to acquire substantial biotech targets.

Narayan Kulkarni in Singapore