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Pharma focus

MONTHLY REVIEW OF THE INDIAN PHARMA SECTOR

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The Great Healthcare ‘buyout’

Couple or so years back Nicholas Piramal Ltd, a company listed on the Indian stock exchanges, re-engineered itself into Piramal Healthcare Limited and Piramal Life Sciences Ltd. The former was to impart greater focus to the manufacture/sales of branded generics and contract manufacturing, while the latter was to create a ‘service arm’ to promote in house research as well as for others. This move appears to have paid ‘dividends’ to Piramal Healthcare, when it was able to sell its domestic formulations business to Abbott Laboratories of US for a whopping US $ 3.72 billion. This valuation has aroused wonderment and curiosity among industry peers.

Though the promoters need not do so, especially in view of their dominant shareholding, they are seeking formal approval of the sale from shareholders. While this procedural detour would delay the inflow of money, it would also be setting a precedent / benchmark of corporate governance for other Indian companies to take such a path.

Quid Pro Quo –Piramal Abbott Deal

Quid for Piramal

- Cash to be received by Piramal Healthcare Ltd – US $ 3720 million
- US $ 2120 to be paid upfront and the balance to be paid in 4 equal annual instalments.
- Retention of Piramal Healthcare Ltd / listing in stock exchanges.

Pro Quo for Abbott

- Manufacturing Facilities at Baddi, Himachal Pradesh
- Rights to 350 brands and trademarks
- Transfer of employees to Abbott
- Emerges as largest Pharma company in India in terms of sales.

Once the deal is approved, Piramal Healthcare would receive an upfront payment of US $ 2.12 billion, with four deferred annual instalments of US $ 400 million for the next 4 years. The bulk of the money thus received would come into the company coffers and would ‘technically’ be shareholder’s wealth.

The initial reaction among shareholders has been negative, reflected by the decline in the price of the company’s shares. This was largely driven by the initial mistaken perception that the promoters were the main gainers and that the average shareholder would not derive any benefit. However, this was corrected to an extent with the

Business Retained by Piramal Healthcare

- Manufacture and supply of Active Pharmaceutical Ingredients
- Over the Counter Consumer Products
- Vitamins and fine chemicals
- Critical Care Products (including inhalation anesthetics)
- Custom Manufacturing for third parties
- Diagnostic Services including pathology laboratories and radiology centres
- Clinical Research Services

Company's Chairperson, Ajay Piramal being somewhat more explicit about the deal and future plans.

As a result of the deal with Abbott the key activity of the company would be wound up, leaving the key question for shareholders as to how the company would pass on the benefit from sale to them and add value to their shareholdings in future. The Chairperson has indicated that there could be a 'special dividend' to shareholders shortly. However, he is not too clear as yet as to how the 'liquidity' coming into the company would be used for business in future. All he asks of shareholders, at this stage, is to give the company two years time after which, in case the company does not use the resources, shareholders would be returned their share.

From these 'unclear' replies it seems clear that the funds may not be utilized in the pharma or related business spheres. This perception has been further bolstered by the fact that Ajay Piramal has often stated in recent interviews that their group wants to have businesses that have high growth rates – indicating that the 20 % plus annual growth of the branded generics business was not good enough. Perhaps, Piramal Healthcare Solutions is in for further 're-engineering', perhaps, into a new sector. For the present the main contribution to the Healthcare / Pharma sector would be in the form of CRAMS – Contract Research and Manufacturing Services – which are currently growing at an annual rate of 40 – 50 % in India.

Is the 'indigenous' Pharma sector 'laying down its arms'?

In the first issue we had mentioned that the India pharma sector had 'mushroomed' since the 1970s and in the process acquired intrinsic strength. We had also averred that the 'plusses' of the industry could make Indian companies the target for acquisition. While in terms of sales the Indian companies have been the dominant ones since the turn of the century emerging, M&A's provide a different picture. Now of the top 10 companies, in terms of sales in the Indian market, as many as 4 are 'foreign' MNCs. In December 2008 only 1 foreign MNC, GlaxoSmithKline Pharmaceuticals Ltd.

The latest one to enter the 'top 10' is Abbott with its acquisition of a division of Piramal Healthcare solutions. This trend started with the Daiichi Sankyo acquiring the promoter's stake in Ranbaxy Laboratories in December 2008. In 2008 Shantha Biotechnics was being hailed as an Indian success story of a company that took on MNCs in the area of vaccines. However, this was acquired by Sanofi-Arentis AG in 2009 (though it did not enter the top 10 slots).

The reemergence of MNCs as top players in the Indian pharma space after the 1970s is, however not entirely due the acquisition of Indian companies. It is also related to global M&A's. For instance, Pfizer, by virtue of acquiring the multinational Wyeth has become the 8th largest player in the Indian pharma market. In a similar fashion, by acquiring Schering Plough, Merck & Co has become the 10th largest in terms of market share in India.

As a result of this restructuring in the Indian pharma sector an emerging trend seems to be the growing control of the India pharma market by fewer players. This is evident from the fact that whereas, till end of 2008 the top ten had a market share of 37%, the fresh lot commands as much as 41% of the market. The estimated market share of the 4MNCs in the top ten slot is around 20% or almost 50% of the sales in this niche of pharma majors.

While market experts feel that there may be a couple of more Indian companies that might be acquired over the next year or so, the important questions are whether 'strong' indigenous companies are trying to exit the pharma space. Alternatively, is this only a temporary 'tremor'.

Ranbaxy Laboratories Ltd announced that its European unit was recalling select batches of three products to add safety warnings under the regulations there. Ranbaxy, the country's top drug maker by sales and majority owned by Japan's Daiichi Sankyo, said there was no "product quality concerns" for the drugs, it said in a statement, but did not name the products. Ranbaxy said the drugs were being recalled from Britain, Denmark and Ireland. "The recall is being carried out as patient information leaflets need to be updated, to include safety warnings initiated by the European Medicines Agency," the company statement said. The US Food and Drug Administration had said in February 2009 Ranbaxy sold misbranded or adulterated drugs in the United States, the company's largest market, having earlier banned imports of over 30 generic drugs from the firm. Ranbaxy Chief executive Atul Sobti said a "corrective action plan" was underway to address the US regulator's charges about the quality of some of its drugs.

The top 25 pharmaceutical companies in India registered a growth of 180 per cent in bottom line during the year ended March 2010 mainly on account of a sharp drop in their foreign exchange losses as compared to the previous year. As per a Pharmabiz preliminary study, the net profit of these 25 listed companies with net sales above Rs 400 crore, has taken a quantum jump and touched Rs 5,596 crore during the year ended March 2010 from Rs1,999 crore in the previous year. The foreign exchange loss adjustment of these companies came down to Rs 75 crore during 2009-10 from Rs 4,244 crore in the previous year helping the companies to push up the profitability. Foreign exchange adjustments (gain or loss) represents exchange difference on foreign currency borrowings including FCCBs and mark-to- market loss on outstanding derivatives relating to loans. The net profits of these companies before adjustments of foreign exchange losses however showed a decline of 3.5 per cent due higher taxation which went up by over 340 percent during 2009-10. The net sales of these 25 companies increased by 11.1 per cent to Rs 56,467 crore from Rs 50,848 crore. The sales of the 25 companies accounted for over 50 per cent of total sales by Indian pharmaceutical industry during last year. in the current year.

Strengthening the collaboration announced earlier this year, Strides Arcolab recently announced the signing of two licensing and supply agreements with Pfizer to address new markets and product segments. Under the first agreement, Strides will license and supply up to 38 generic oncology products to Pfizer for markets in the European Union, Canada, Australia, New Zealand, Japan, and Korea. The second agreement covers niche sterile injectables for the US market. The finished dosage form products will be commercialised by Pfizer through its Established Products Business Unit. The financial terms of both agreements were not disclosed.

According to a recently published report by the International Policy Network (IPN), substandard medicines are still harming the reputation of the Indian pharmaceutical industry and endangering the wellbeing of patients. The report includes the results of a small sampling study conducted by the Liberty Institute in India which found that 7 per cent of drugs purchased from wholesale traders in Delhi were substandard, with half of these found to contain no active ingredients at all. Some of the spurious drugs contained chalk or talcum powder mixed with a pain reliever to trick and defraud the patient.

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