Perfect partnering

When it comes to collaborations, biopharmaceutical companies can generate a lot of value by selecting the right partner and making an effort to nurture the relationship, say Alexander Moscho and Josef Leiter.

Deal making is more important than ever to both pharmaceutical and biotechnology companies. According to a recent McKinsey study¹ of the ten largest pharmaceutical companies, the percentage of gross revenue from in-licensed compounds grew from 24% in 1992 to 35% in 2000, and is expected to reach 45% by 2002, largely as a result of the increased availability of late-stage compounds from biotechnology companies. Development of the biotechnology industry is heavily reliant on this licensing revenue,

which has risen from \$5.7 billion in 1998 to more than \$6.4 billion in 2000, and could reach \$7.8 billion in 2003 (ref. 2). US company Biogen (Cambridge, MA), for example, made about \$600 million from licensing activities between 1991 and 1995—an important

prerequisite for launching its first product, Avonex, in 1996. Last year, licensing revenues still comprised about 18% of its total revenues.

Pharmaceutical companies rely heavily on the long-term revenue generated by the biotechnology compounds in their pipelines, whereas biotechnology partners depend on the short-term revenues—and longer-term royalties—provided by their pharmaceutical partners to stay in business. The difference between a mediocre deal and a great deal can be huge, both in terms of revenue and for a company's stock price. For example, news that Curagen (New Haven, CT) had entered into a drug development alliance with Bayer (Leverkusen, Germany) sent Curagen's shares up 35% to around \$36 (*Nat. Biotechnol.* **19**, 186, 2001).

However, biotechnology companies are often dependent financially on the outcome of one or two deals, and an unsuccessfully concluded partnership can threaten their very survival. Take the case of Amylin Pharmaceuticals (San Diego, CA): In early

1998, Johnson & Johnson (J&J) informed Amylin that it had decided to discontinue development of Amylin's treatment for diabetes, Symlin (pramlintide). Even though J&J had already invested around \$175 million in the programme, this unexpected termination meant that the small biotechnology partner had to slash its workforce from 300 to 36 people, and drastically reduce the spending on its development pipeline. Yet Symlin turned out to have some potential (*Nat. Biotechnol.* **17**, 940, 1999) and is expected to be approved by the FDA within the next ten months³. However, most biotechnology companies are not that fortunate in the end.

So what really makes the difference between a successful deal and a failure? Which characteristics transform licensing contracts into long-lasting, mutually beneficial partnerships? There are five crucial steps to a successful partnership, including developing a deal strategy, improving bargaining power, and negotiating the terms of the deal. Here, we focus on the two steps most frequently neglected: finding the right partner and post-deal governance.

Choose partners with care

Given the duration and complexity of deals, today's business partnerships are like marriages—there's nothing better than finding the right relationship, and nothing worse than being trapped in the wrong one. Unfortunately, because of their limited financial resources, many biotechnology companies overemphasize short-term financial gains, often forging deals too quickly without paying enough attention to non-financial aspects such as their strategic, cultural, and organizational fit with their future partner. They don't consider whether the two companies really do have the same strategic goals or whether both regard the partnership as an integral part of their corporate strategies.

Closing deals is often a protracted process that can consume as much as 18 months, and the average duration of deals between biotechnology and pharmaceutical companies is 3–4 years, offering plenty of opportu-

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nity for dissent and quarreling. Long-term negotiations put an even greater strain on relations between the companies, and finding the most suitable partner becomes even more pertinent.

Selecting the right partner involves three steps: First, defining appropriate search criteria; second, developing a database of potential partners; and third, establishing a screening process to select a partner.

Search criteria usually fall into two categories: science and business. On the science side, companies must identify the complementary skills they need from potential partners in therapeutic areas, technology platforms and experiences, and R&D competence. On the business side, criteria might include geographic proximity (to the company's own headquarters, second-tier manufacturing partners, and attractive markets, etc.) as well as strategic, cultural, and organizational fit.

The next step is to develop a large and diverse database of all the companies that might meet the criteria. In addition to company information gathered by direct and indirect contacts, other data that can be helpful and should be included are company fundamentals (company fact files can be found in *Scrip*, IMS, or in specialized reports e.g., those from the Lehman Brothers and Pharma Business), current R&D projects (e.g., from sources like Pharma Projects), the history and results of relevant alliances and deals (e.g., Windhover or Recombinant Capital), and sales and marketing data (e.g., from IMS Sales Audit). The collection of all this information may seem difficult and unnecessary at the beginning stages of business development, but it will facilitate the deal-making process as it progresses and be useful for future deals. Young companies often ignore this step, but a good, continuously updated partnering database is an invaluable asset for business development.

Finally, the screening process, which takes on average one to three months depending on the amount and availability of information, as well as on the difficulty of finding companies that meet the criteria. It is important to note that, ultimately, the most important criteria for selecting a deal partner should be the experiences and results gained during the negotiation of the terms of the deal.

The human factor

Maintaining a good relationship is not a question of contractual or structural deterrents, signed as part of any elaborated legal deal framework, but on the quality of

human relations. In 1997, David Deeds and Charles Hill⁴ conducted a study of 109 alliances through interviews with 57 biotechnology executives (CEOs, vice presidents of business development or research). They found evidence that a strong relationship between the parties had a significantly greater influence on deterring "opportunistic behavior"⁵ than any contingent penalty clauses. The study highlighted the importance of top management's understanding and involvement in the management of the alliance.

For a long-term partnership that is to be mutually beneficial, companies must trust each others' strengths and exchange know-how openly. It is important for both partners to develop excellent network-management skills, to modify or even extend collaborations, and to create the right incentives to share learning and measure performance. Deal makers should not underestimate the importance of monitoring the partnership on an ongoing basis, and installing procedures to defuse troubles as they arise, before they can damage the relationship.

Two very different deals illustrate how the state of a relationship can affect the ultimate outcome of a deal. The first is the historic marketing deal between Johnson & Johnson (Whitehouse Station, NJ) and Amgen (Thousand Oaks, CA) for erythropoietin (EPO), a treatment for anaemia in patients. In 1985, the companies entered a marketing agreement under which Amgen would supply EPO to meet the dialysis demands in the United States, and J&J would supply EPO for the non-dialysis market in the United States and generally for Europe through its daughter company, Janssen-Cilag. Just one year after the launch of EPO in 1988, the two companies started a legal battle over the distribution of the revenue from dialysis and non-dialysis sales. The ongoing lawsuits just recently found their culmination in a jury decision ruling that Amgen would get the rights for the EPO successor, NESP (novel erythropoiesis stimulating protein)⁶.

Although the companies had separated the dialysis- and non-dialysis-sales in their contract, it turned out that, in reality, US hospitals (the primary buyer of EPO) prefer single-provider-relationships for the same compounds, no matter what the purpose. Most probably, this problem had not been anticipated by J&J or Amgen while negotiating the terms of their deal. But instead of solving it together, it seems that both companies saw the opportunity for individual gain⁵. As a result of the subsequent wran-

gling, J&J could lose a significant part of its current annual sales (EPO accounts for approximately US\$ 1.9 billion, currently), and Amgen will lose parts of its licensing revenues. The ongoing lawsuit has also taken up a lot of management attention.

The long-lasting, productive relationship between Pfizer (New York) and Neurogen (Branford, CT) provides a sharp contrast. The "marriage" began with licensing of the CNS drug compound NGD 91-1, a potential treatment for Alzheimer's disease and anxiety, to Pfizer in 1992. Today, after contributing another four compounds (for Alzheimer's disease, anxiety, and insomnia) to Pfizer's pipeline, Neurogen is often viewed by industry experts as an integral part of Pfizer's CNS drug-development program. Even when phase I trials for the NDG 91-1 needed to be repeated 11 times, Pfizer remained committed to the biotechnology company. As a result, the partnership currently has several products in preclinical trials and two in late clinical development (NGD-91-3 against anxiety disorder, and NGD-97-1 as an Alzheimer's therapy).

Several things have kept the partnership thriving. First of all, both partners invested heavily in building trust and partnership. For example, Neurogen officials participate in internal Pfizer committees, and both companies share all relevant data. In addition, geographical proximity makes it easy for scientists and management to establish face-to-face meetings as part of their deal-monitoring procedure. Moreover, their research programs are complementary, enhancing the "one-company" feeling, and at the same time avoiding the "not-invented-here" syndrome.

In summary, finding the right deal partner and pampering the relationship are two of the key ingredients in successful deal making. Only when these two pieces of the puzzle are firmly in place can companies realize the advantages that, in today's competitive environment, are crucial to their well-being and survival.

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