Nick Arvanitidis

Are CEOs the biggest obstacle to consolidation?

Common sense tells us that consolidation within the biopharmaceutical industry is inevitable. Where will the money be found to support the growth of approximately 200 public and 800 private biopharmaceutical companies when it will take an estimated $250 million to $500 million per company to achieve profitability? Given the relative dearth of products commercialized by the biotech industry—approximately 20 therapeutic products since the advent of genetic engineering in 1973—vis-a-vis the billions of dollars invested, the money is unlikely to come from Wall Street, as both institutional investors and individual investors have been badly burned by an approximate 30% drop in biotech stock prices over the past year alone.

There are several reasons why biotech stocks plummeted so sharply. The 30 or so biotech drug failures in the clinic during the last three yyperhaps the main reason The onslaught of health-care co st-containment initiatives coming from both the private sector and- the public sector has also contri uted, as has an increasing suspic on that the "easy" biotech drugs ave been developed, while the mo e technologically difficult therap es have yet to be created. From a financial perspective, furthermore, it is counterintuitive to expect that each of the 1000 biopha maceutical companies will be abl to bble to uild an independent infrastructure for commercializing pharmaceutical products, since such an infrastructure includes entire divisions devoted to integral functions like regulatory, medical/clinical, and marketing and sales, in addition to research and development and, of course, manufacturing. Yet the dream of becoming an independent, fully integrated pharmaceutical company is the force driving of many, if not most, entrepreneurs involved in the biotechnology game.

Unfortunately, history shows that it is generally not until a biotech company is on its knees that merger and consolidation is considered, whereas healthy biotech companies with technical and financial synergies continue along separate paths. It appears that the notion of financial vulnerability has not taken sufficient root in the collective corporate consciousness to motivate an orderly consolidation in the biotech industry, despite the fact that—without added financial support—approximately one half of the public biotech companies will run out of money over the next 18 months. Thus, cash is king, and as a result, the cost of buying technology is decreasing, as the need for cash in biotech companies is increasing. For example, Amgen (Thousand Oaks, CA) bought Synergen (Boulder, CO) last year for $260 million, an amount that not only gave it Synergen's technology, but $110 million in cash, a discounted net-operating carryforward of $100 million, lab space worth up to $40 million, and a manufacturing plant worth up to $50 million. Indeed, as biotech companies run out of money, technology acquisition will become more and more of a bargain.

The likelihood of a burgeoning and successful biotech industry sometime in the foreseeable future—based on the industry's present configuration—becomes even more problematic when the availability of experienced and capable people is considered. If one examines the demise of individual biotech companies, it is more likely that a lack of people with the appropriate talent and experience caused the fatal misstep than a lack of money. It would, without a doubt, be interesting to validate this assumption with case studies of companies like Synergen, Centocor (Malvern, PA), and Xoma (Berkeley, CA).

It is definitely unreasonable to expect that the pharmaceutical industry can provide the emerging biotech industry with the talent and the experience needed to get the job done. Consider the enormity of the demand and the relative paucity of the supply, for instance, the need for 1000 medical directors, each backed by 35 to 40 clinical and regulatory people, all with experience in developing and implementing clinical-trial strategies oriented to the U.S. Food and Drug Administration (Rockville, MD). Contract research organizations can provide part of this supply, but no where near all of it. So the incentive to consolidate should be as much—if not more—people driven as finance driven.

I've allowed myself more candor than usual in expressing my opinions since stepping down after 14 years as chief executive officer (CEO) of Liposome Technology (Menlo Park, CA)—which was recently renamed Sequus Pharmaceuticals—or 98-dog years if one considers that 1 man-year in biotech is equivalent to approximately 7 dog-years. I believe that the single greatest impediment to consolidation lies in the character of the typical biotech CEO, who is bright, young, and accustomed to running his or her own show. The prospect of unemployment or assuming a second-in-command position as a result of a merger is not terribly appealing to this group as a whole.

Vaughn Kailian, president and CEO of COR Therapeutics (S. San Francisco, CA), captured this sentiment quite aptly during a Laguna Miguel conference for biotech CEOs when he said, "Biotech CEOs are like cats. And the question is, Has anyone tried to herd cats?" And therein lies the rub. ///

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