Merck wipes Serono off Swiss biotech map

On the average report card a test score of three out of five would usually draw the comment ‘could do better’. The admonishment to try harder was also given by some observers to Darmstadt-based Merck KGaA’s surprise €10.6- ($13.2)-billion acquisition of Serono on September 21. Although the price tag, roughly 5.1 times 2005 sales, looked reasonable—albeit in excess of the 3.2 times paid by Bayer for Schering and the 4.4 times UCB paid for the Schwarz Pharma—serious doubts remain about the rationale of lashing the two companies together.

Michael Roemer, chairman of Merck KGaA (R) and Ernesto Bertarelli, head of Serono shake hands during press conference 21 September 2006 in Darmstadt, Germany, announcing Serono’s take over.

By picking up Geneva-based Serono, Merck KGaA boasts that it has achieved three of the five objectives it set itself to foster growth and remain independent. These are: achieving competitive scale in R&D (now up to about €1.1 billion), adding new therapeutic treatments in specialist areas and expanding its geographical reach into to the US.

Michael Roemer, Merck chief executive appears to have struck the deal personally with Ernesto Bertarelli for his family’s 64.5% stake in Serono, surprising the rest of Serono’s executives. Despite the gloss put on the deal by Roemer, the two outstanding objectives on its list—the strengthening of the oncology franchise and gaining an entry into Japan—make the deal look like one struck not from a position of strength but one of weakness, says analyst Mike Booth of investment bank Canaccord Adams in London. “Most people would agree that Merck needed to do something,” he says. “They missed out on Schering and they had a lot of cash that they needed to be seen doing something with.”

Alongside needing scale to compete with the deep research pockets of big pharma and big biotech, Merck has also been looking for a way to alleviate its dependence on its highly cyclical liquid crystal display business, prompting the bid for Schering to beef up its ethical drug making business. But well-publicized problems inside Serono have also given the deal an air of two less-than-fit companies trying to prop each other up. Most recently Serono has been grappling with the fallout of its very public failure to find a buyer after it put itself up for sale last November (*Nat. Biotechnol.* **24**, 5, 2006).

Questions were also hanging over its pipeline given the slowdown in its mature reproductive health business and increasing challenges to Rebif (interferon β-1a), its top-selling multiple sclerosis drug, which, with sales of about €1 ($1.3) billion in 2005, contributed more than half of group turnover. However, the paucity of late-stage products available from the combined groups’ 28 compounds (5 in phase 3) has left Andy Smith, investment manager at venture capital firm SV Life Sciences in London questioning what the deal will ultimately deliver. “What it adds for Merck in the next five years is going to be difficult to work out,” he says.

As such the acquisition has drawn unflattering comparisons to Altana’s decision to sell its pharmaceuticals business to Danish company Nycomed in Roskilde for €4.5 ($5.7) billion. Konstanz, Germany-based Altana, which has been looking for a buyer since August 2005, also cited the need for scale. But others have pointed out the generic threat to Protonix (pantoprazole), the group’s blockbuster ulcer drug and the decision by New York-based Pfizer to hand back the rights to Altana’s next generation of ulcer treatments as more compelling reasons to cozy up to Nycomed.

One company that has managed to convince the market that its recent merger was about adding value is Brussels-based UCB. Its €4.4- ($5.6)-billion deal to acquire the family-controlled Schwarz, headquartered in Monheim, Germany, was greeted with almost universal approval, given the nine late-stage products it added to the pipeline. UCB is now expecting to launch three products over the next three years, including Cimzia (certolizumab) to treat Crohn disease. This helped the shares, which have hovered around the €42 mark this year, hit a record high of €50.

Peter Fellner, former chief executive of Celltech and present UCB director, argues that although some of the recent mergers may have been done from positions of weakness, the take-home lesson is that pharma and biotech need scale to keep driving the innovation. “To be in the game you have to be able to place some big bets, and if you don’t have the financial clout to place these bets then you will be out of the game,” he says. And although the once great white hope of European biotech, Serono, might be out of the game, many believe its disappearance will do little to alter the rest of the continent’s much smaller market cap biotech companies, still wrestling with funding, signing licensing deals and bringing products to market.

One of the consequences, however, says Booth, could be the sparking of interest in previously neglected companies. “Analysts could start to look at covering some of the less liquid companies in the sector in the hope of a deal,” he argues.

Smith is equally pragmatic about the demise of Serono, but believes that it will shift investment to the next layer of biotech companies. “Money usually finds other places to go and the bigger market cap European biotech groups like Speedel, Actelion and Genmab could take up the slack.”

Robin Campbell, biotech analyst at investment bank Jeffries, in London, however, argues that Serono, as part of Merck, could continue to drive consolidation in the industry in its attempt to score five out of five in its strategic objectives. “When Merck gets its act together and is recapitalized, that will determine how much flexibility they will have in terms of in-licensing new products, in addition to what Serono brings.”

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