

## Bayer's diagnostic purchase helps Chiron focus

On September 17, Chiron (Emeryville, CA) announced the sale of its in vitro diagnostics business, Chiron Diagnostics (Walpole, MA), to the Bayer Group (Leverkusen, Germany) for \$1.1 billion, confirming a redefinition of Chiron's business strategy.

Chiron Diagnostics includes immuno- and nucleic acid diagnostics, as well as critical care and chemistry businesses. For Bayer, the acquisition strengthens its diagnostic business "especially in nucleic acid diagnostics," says Bayer business planning and administration VP Christopher Seaton.

"We saw that there was a consolidation going on in that whole diagnostic area and we knew we couldn't possibly compete by ourselves," says Jim Knighton, vice president of Chiron investor relations.

Charles Engelberg, analyst at AmeriCal Securities (San Francisco, CA), says "Chiron has historically suffered from a lack of focus." He thinks the May appointment of Sean Lance as Chiron president and CEO may change all that. Prior to Lance, Chiron "was run by scientists rather than business men," he says. He is critical, for instance, of Chiron cofounder and chairman William Rutter's enthusiasm for IGF-1 myotrophin, which has not been approved by the FDA and has been withdrawn in Europe. "A company can't be run by what is scientifically appealing." He adds that, in his opinion, Chiron's only real therapeutic products—beta-interferon and interleukin-2—were obtained through the "gift" purchase of Cetus in 1991 rather than through astute business dealings.

Although Chiron's lack of focus has confused investors, says Engelberg, "Wall Street has been pretty loyal to them." Novartis (Basel) already owns 45% of Chiron and has options to acquire up to 55% of the company in 2000, and to fully acquire the company in 2001. Using conventional measures such as company earnings or cash flow, "[Chiron] is really a very mediocre company with a very high price earnings ratio," he says, explaining that creative accounting—Novartis payments as artificial revenues—has partly sustained it.

Suggestions that Novartis has been leaning on Chiron to divest its noncore activities have been denied by both Novartis director of investor relations Joe Shephard and Chiron's Knighton. But Engelberg disagrees: "Obviously [Chiron] was under tremendous pressure from Novartis," he says, explaining that it came in most part from the Sandoz side of the management, who "were even less happy with the less-than-businesslike attributes of Chiron" when it was purchased by Ciba in 1995. But Chiron is still its own entity, he says. "Frankly, I think it's going to be opposite what

many people think—[Novartis] will acquire [Chiron] if it's floundering, but if it's successful I think they'll leave well enough alone."

Knighton agrees that Chiron lacked direction in the past but does not think it is fair criticism now. "The sale of the vision business last year (*Nat. Biotechnol.* 15:1327) and the recent sale of the in-vitro diagnostic business are certainly major components of a focusing of our efforts on the commercial side. On the research side, we used to be into any number of disease areas but now we're down to three [cancer, cardiovascular, and infectious diseases]."

There is speculation that Chiron's vaccine business will be sold next. "It would certainly make sense," says Engelberg, "[Chiron] isn't even a player in the US—it's not a real business, it doesn't really compete with SmithKline, Merieux Connaught or AHP." Knighton denies that the vaccines unit is up for sale—"we have never made a statement to that effect"—but does concede that "we have to find a way to more effectively compete within the vaccines area." He says a partnering option may be one way of beefing up the vaccines division. "One of the options is to take some of the proceeds from the diagnostics business and direct it in any number of ways toward vaccines," says Knighton.

Lehman Brothers (New York) analyst, Robert Rouse, says even with the arrival of Lance, it will likely take Chiron at least another year to redefine and begin executing its business model. "Although we are more optimistic than we have been, our investment rating [Outperform] has not changed in the last 12 months." But Chiron's fairly tight trading range [\$18–25], he says, will have a more limited downside now that the company has started taking steps in the right direction.

The proceeds of the diagnostics deal could be spent on internal R&D activities, a stock buy back, or on in-licensing products, even a company purchase, says Knighton. "Its a very high probability that [product acquisition] will be in one of [our three core] areas," he says.

"[An acquisition] would make sense obviously," says Engleburg, who explains there are several companies in the Bay area that Chiron should acquire, including COR Therapeutics (S. San Francisco, CA), which he thinks would be a good cardiovascular fit. He also suggests Chiron buy products that it can sell and make some money from. "If they don't do that they're not going to be any better off than they have been."

Emma Dorey

### Bayer's Millennium deal signals shift in R&D

In addition to the Chiron Diagnostics purchase, Bayer entered into a 5-year, \$465 million agreement on September 23 with Millennium Pharmaceuticals to discover 225 new drug targets in 7 disease areas including osteoporosis and cancer. Industry analysts think the deal signals Bayer's realization that the future lies with genomics.

Bayer will make an initial payment of \$130 million consisting of a \$96.6 equity investment for 14% of Millennium, plus a \$33.4 million license fee. The remaining \$335 million will be paid out in research funding and target-delivery payments. The Millennium deal "gives us a pipeline of new drug targets," says Bayer's Seaton. "Coupled with our expertise in discovery and development, we expect to generate marketable products out of it." Any targets that Bayer does not choose to further develop will be returned to Millennium to fuel its own drug pipeline. Millennium retains rights to resulting diagnostic products.

So what has prompted the two deals? "Life sciences are the future markets," says Bayer spokesperson Christina Sehnert. Seaton supports this: The two deals "show the continuing if not an increasing focus by Bayer on life sciences."

Michael King, analyst at BancBoston Robertson Stephens (New York), puts it another way. "If you talked to people in the industry and asked who are the companies that need to shake up their R&D, I think Bayer would be one of the ones that comes up," he says. "This is a company that's lagged behind the industry in terms of life-science R&D."

"Bayer recognized that access to a genomics capability was becoming increasingly important," says Sally McCraven, Millennium corporate communications director.

"Any big pharmaceutical company that hasn't made a significant investment in genomics, either internal or external, will be functionally extinct in the next couple of years," agrees Richard van den Broek, analyst at Hambrecht & Quist (New York).

So will this deal spark a trend? "It's a wake-up call for other pharmaceutical companies that need to access targets," says Nick Woolfe, analyst at BancBoston Robertson Stephens (London). But van den Broek says it's hard to speculate about who will be next because of the many potential partners but lack of potential providers. "The universe of companies focused on genomics will be the beneficiaries of broader pharmaceutical interests for the next couple of years," he says. E.D.