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## Lure of Products Leads Drug Firms to Biotechs

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Faced with patent expirations on highly profitable drugs, big pharmaceutical firms are turning to small biotechs to re-stock their medicine chests.

The latest example came last week, when Pfizer Inc. agreed to buy Vicuron Pharmaceuticals Inc. for \$1.9 billion. Vicuron, based in King of Prussia, Pa., worked on antibiotics and drugs for fungal infections, key areas for Pfizer.

The acquisition followed one in April by GlaxoSmithKline, which agreed to buy Corixa Corp., a Seattle company fo-

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cused on vaccines. Other recent deals include the purchase of Angiosyn Inc. by Pfizer, Idun Pharmaceuticals by Pfizer, TransForm Pharmaceuticals Inc. by Johnson & Johnson and Peninsula Pharmaceuticals Inc. by Johnson & Johnson.

Of course, Pfizer, Glaxo, Johnson & Johnson, Merck & Co. and some other big pharmaceutical companies have always looked to the biotechnology in-

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dustry as a source of new products. In fact, drugs licensed from biotech firms account for 30% of their revenues, according to consulting firm Deloitte & Touche.

What's changed is that big drug makers aren't just negotiating product deals but are snapping up biotech companies themselves. There have been 16 acquisitions of biotech companies by drug companies this year, compared with three during the first six months of 2004, according to data provided by investment bank Barrington Associates.

Big drug companies were responsible for a small fraction of the total merger deals in the biotech sector, which jumped from 59 in 2003 to 99 the next year, according to merger information company FactSet Mergerstat.

But they clearly were the biggest spenders. Pfizer, Johnson & Johnson and others together have spent \$5.5 billion to acquire biotech companies this year, half the total value of all mergers in the sector.

There's no mystery to the trend, said Paul Kacik, head of healthcare practice at Barrington. The big drug companies need to fill their product development pipelines because they stand to lose billions in revenue when some popular drugs lose patent protection and face competition.

In addition, the American Jobs Creation Act has allowed U.S. companies to repatriate earnings from foreign subsidiaries at a reduced tax rate, leaving big drug companies with massive cash hordes available for investment. The 2004 law was promoted as a way to galvanize job growth by encouraging companies to invest overseas profits do-

mestically.

Pfizer, for example, already has repatriated foreign income of \$28.3 billion and says the total may climb to \$40 billion before the year is over, creating a vast pool for acquisitions. By 2007, Pfizer drugs with annual sales totaling \$14 billion — one-quarter of total company sales — will lose patent protection. Among them are Zoloft, an antidepressant, and Zithromax, an antibiotic.

So the world's largest drug company has been on a highly visible shopping spree. Pfizer agreed to pay an 84% premium for Vicuron — a price that fund managers said prevented a bidding war from breaking out for the firm.

"I suspect some people think we're crazy and buying everything that moves," said John LaMattina, Pfizer's research and development chief. "But all our acquisitions have been strategic."

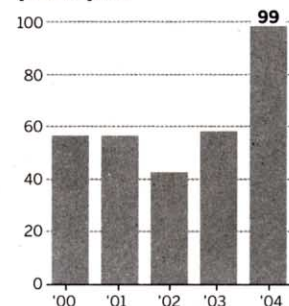
Angiosyn, a San Diego company, added to Pfizer's depth in eye diseases, he said, an area in which the drug giant co-markets Macugen for macular degeneration. Drugs in development at Vicuron could help replace revenue lost when Zithromax loses patent protection in November.

Right now, big pharmaceutical companies are finding willing sellers among smaller biotech firms. According to Ernst & Young, 40% of publicly traded biotechnology companies have less than two years of cash remaining, up from 31% a year earlier. At the same time, private companies hoping to go public face investors who have become hostile to new stock offerings.

"We're seeing sort of a confluence of factors" driving merger deals, said Rich Kollender, a

### Merger fever

With 75 deals already struck this year, the number of biotechnology mergers and acquisitions is likely to surpass last year's by far.



Source: FactSet Mergerstat

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principal with Quaker BioVentures in Philadelphia.

Because drug firms are looking for deals, biotechs with promising technology or drugs close to market can command premiums, as in the case of Vicuron. "These companies are very hungry for assets," said Kollender, adding that a four-way bidding war had broken out over a biotech that Quaker invested in.

Not every deal may be as good as it looks. Kurt von Emster, a partner with MPM Capital, said that Corixa was worth more than Glaxo offered for the company. Glaxo offered \$300 million for Corixa in April, a 48% premium over the company's share price at the time. But Von Emster said Corixa's stock was depressed by the overall swoon in biotech stocks after the withdrawal of Tysabri, a multiple sclerosis drug associated with life-threatening infections.

Although Corixa said the offer was fair, Von Emster, whose fund owns 2% of the biotech, said he believed that the company was worth more. "It is probably one of the most undervalued companies I have seen," he said.