

Big pharma

Close to the edge

A fast-approaching patent cliff prompts a flurry of deals

A PRICE TAG of \$10.8bn would look hefty for most acquisitions of smallish and newish companies. But for Merck, a drugs giant known as MSD outside America, the money it is spending to buy Prometheus Biosciences, a biotech firm based in California, is relatively small change. In the world of big pharma such deals have the potential to generate enormous returns.

Even though Prometheus makes no profits to speak of and has no approved drugs on its slate, the big prize for Merck is PRA023, a drug approaching the late-stage of clinical trials developed by Prometheus to treat ulcerative colitis, Crohn's disease and other nasty autoimmune conditions. For now, Prometheus is burning through cash at a fast-rising rate. Merck's decision to scoop it up is a bet on what comes next.

The American giant badly needs promising new treatments to replenish its drugs pipeline. Like other pharma companies, it is facing a cliff-edge as patents on money-spinning treatments come to an end. Keytruda, Merck's cancer-immunotherapy drug, accounted for over a third of its sales in 2022, but will face competition from cheaper copycats once key patents expire in 2028 in America and in Europe two years later.

The problem goes industry-wide. Patents for more than 190 drugs will expire before the end of the decade, leaving sales worth as much as \$236bn at risk of a dramatic drop-off. Few will be spared the coming onslaught. The world's ten biggest drugmakers, including Merck and Pfizer, an American rival, stand to lose around 46% of their revenues, which amounted to over \$500bn combined in 2021, according to ZS, a consultancy. For five of these companies, at least half of their annual revenues are at stake.

Pharma bosses are spending big to plug the gaps. The industry has long turned to dealmaking as a way of compensating for the potential loss of revenue from expiring patents. Despite a dearth of mergers and acquisitions in other sectors, drugmakers are driving a wave of consolidation across the sector. PwC, a consultancy, estimates that the value of takeovers in the pharma and life-sciences industries could reach \$275bn in 2023, up by almost three-quarters from last year.

So far, the prices buyers are willing to pay have come with huge premiums. Merck is forking out \$200 per share for

Prometheus, a whopping 75% above the firm's closing price just before the offer was made. Another acquisition unveiled in March will see Pfizer pay \$43bn for Seagen, a loss-making cancer biotech firm. The industry's richest deal in three years came at a 33% premium to Seagen's share price. And on April 18th GSK, another pharma giant, agreed to buy Bellus Health, a Canadian biotech firm with a promising treatment for chronic coughs, at around double the company's pre-deal value.

The benefits of paying out vast sums for drugs that are close to regulatory approval are clear. It can take more than a decade to bring a new drug to market, and many cures fail along the way. With a healthy \$1.4trn in cash piles waiting to be deployed, big pharma is choosing to buy its way out of trouble instead. ■



Fast Retailing

Faster, please

SINGAPORE

Uniqlo's success mirrors the growth of Japan's industrial giants

DRIVE THROUGH any city in South-East Asia and Japan's commercial presence is visible everywhere: vehicles made by Toyota, Honda and Nissan clog the roads, the result of decades of market dominance in the region. If Fast Retailing, the parent company behind Uniqlo, a clothing retailer, has its way, the drivers of those vehicles will soon be wearing Japanese clothes, too.

The company's latest results were a boon for shareholders, with operating profits of ¥103bn (\$760m) in the three months to the end of February, up by 48% compared with the same period last year. They already had good reason for cheer: the company's shares have risen by 53% in the

past 12 months, making it one of the best-performing large listed companies in Japan. Its shares are now just 10% shy of their all-time highs in February 2021, and, with a market capitalisation of \$76bn, it is the country's sixth-largest listed firm.

At first glance, Uniqlo is an unusual story of a Japanese retailer succeeding overseas. Fast Retailing's main international competitors—Hennes & Mauritz AB, the parent company of H&M, and Inditex, the parent of Zara—are based in Sweden and Spain respectively. But the firm's growth abroad follows as much in the footsteps of Japan's industrial and manufacturing firms as its European peers.

Japanese industrial firms, carmakers in particular, made South-East Asia a second home from the 1960s onwards. Fast Retailing is also expanding particularly rapidly in Asia, where sales (excluding its home market and greater China) are up by 71% in the six months to the end of February, compared with the same period a year ago. The region now accounts for 16% of sales, up from 11% a year ago, and it is closing in on mainland China, Hong Kong and Taiwan, which dropped from 25% to 22% over the same period. In the 1960s the focus of Japanese firms was on exploration for oil, the supply of natural resources and producing industrial goods in countries with import-substitution policies. Now the region represents a promising market for Uniqlo rather than somewhere to put factories.

The comparison extends beyond geography. Exposed to demographic constraints in fast-ageing Japan, Fast Retailing has used technology and automation to replace workers, further mimicking the country's large manufacturers. Keyence, a largely unheralded giant of industrial automation, is Japan's second-largest listed firm, worth \$11bn. Since 2017 Uniqlo has embedded all its garments with tiny identification tags, which enable automatic scanning at checkouts.

The reliance on automation goes deep into the company's business operations and supply chain, too. In 2019 it joined up with Japan's Mujin and France's Exotec Solutions, both small robotics companies, with the aim of automating the jobs in its warehouses. It had already joined forces in 2018 with Daifuku, a larger automation firm, which helped reduce the workforce at a warehouse in Tokyo by 90%.

The savings are no longer just a bonus for the firm's bottom line. Uniqlo raised salaries for some employees by up to 40% in March, in an effort to make corporate wages comparable to similar firms internationally, in order to compete for talent, and will set pay based on global standards in future. Savings from automation will be a necessity if the company wants to avoid eating into its profit margins to bump up salaries for its staff. ■