

Antidotes for an Ailing Biotechnology Sector

Although Financing Levels Are Starting to Increase, Biotech Still Needs to Be Savvy

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For decades the biotech industry has provided lifesaving cures to the world, but now many biotech companies are in need of a lifesaving cure themselves—in the form of cash.

Analysts estimate that nearly half of public and private biotech companies have insufficient cash to subsist for even a year. Given the current economic crisis, which includes a tight credit market, an IPO drought, and investor reluctance, raising capital has become increasingly daunting, so much so that companies have been turning to other capital-raising structures that are customarily underutilized. In particular, biotech companies have been forced to engage in creative cash structures or alternative exit strategies in order to bring their products to market.

All hope should not be considered lost for biotech companies just yet, however. According to the second quarter 2009 MoneyTree Report, investments in the life sciences sector (biotech and medical devices industries combined) represented the highest percentage of total venture capital investments since 1995 and increased 47% to \$1.5 billion from the previous quarter.

The same report notes that, similar to previous quarters, the biotech industry received the largest amount of funding for all industries in the quarter, and that funding increased 54% to \$888 million from the previous quarter. Further, following positive Phase III trial results for its obesity drug, **Orexigen Therapeutics** completed a secondary stock offering that raised approximately \$71 million in late July. In early August, following optimistic results for its investigational treatment for lupus, **Human Genome Sciences** raised almost \$358 million, which is one of the largest biotech offerings so far this year.

But that doesn't mean that biotech companies should start dusting off their precedent financing documents with visions of capital funds dancing in their heads. Although financing levels are starting to increase, the levels are still considerably lower than earlier in the decade and finding investors will still be laborious. Additionally, such financings may only be short-term fixes. Fortunately, there are alternate, nondilutive options that biotech companies can implement to raise money and develop their pipelines such as strategic partnering, acquisitions, and royalty monetization that can result in long-term solutions.

Strategic partnering, either in the form of a license or through a strategic alliance, for a start-up or early-stage biotech company may be the key to its survival. Licensing allows a biotech company to grant a right in its intellectual property to another company in exchange for up-front payments, milestone payments, and/or royalties based on product sales.

The license can be tailored to be narrow in scope so that it only includes rights to certain

territories, technologies, fields of use, dosage forms, indications, etc. This could allow, for example, a biotech company patent holder to license only a portion of its technology to raise cash for development and commercialization while keeping another part of the

technology for itself. On the other hand, strategic alliances allow a biotech company to partner with another company to accomplish a mutual goal while dividing up the respective rights and obligations of the parties within that relationship.

Partnering with a seasoned pharmaceutical company or even a larger biotech company can provide a start-up or early-stage biotech company the expertise, leadership, commit-



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ment, and most importantly, the funds to allow for proper product development given

See Financing on page 19

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Financing

Continued from page 17

the pharmaceutical company's (or larger biotech company's) aptitude and operational capability in the development and commercialization of new products.

Such a collaboration is equally beneficial for the partner as its patents expire or pipeline productivity fails to meet expectations; big pharma and larger biotech companies can turn to start-up or early-stage biotech companies to bolster their pipelines and diversify market penetration while mitigating risks. In fact, partners often view biotech companies as cost-effective incubators for new product pipelines.

Strategic partnering, however, isn't just for start-up or early-stage biotech companies. At the end of July, **Amgen** and **GlaxoSmithKline** (GSK) entered into a major partnering relationship to commercialize denosumab, Amgen's product for the treatment of postmenopausal osteoporosis. GSK will pay initial and near-term commercial milestones to Amgen totaling \$120 million to share profits in Europe, Australia, New Zealand, and Mexico and to register, commercialize, and sell the drug in countries where Amgen has no presence, such as China, Brazil, India, Taiwan, and South Korea.

Perhaps one of the most widely known partnering relationships, and often touted as the most commendable, innovative, and successful, was formed in 1990 between **Genentech** and **Roche**.

The partnership was credited for uniquely solving a biotech company's need for financing while strengthening a big pharma's pipeline. During the relationship, Roche held a majority 55.9% stake in Genentech while Genentech remained independent to develop its oncology treatments. Over time, however, Roche became more and more reliant on Genentech's pipeline and made an offer in July 2008 for the remainder of Genentech's outstanding shares. Roche acquired Genentech in March 2009 for \$46.8 billion.

Strategic alliances or licensing can occasionally trigger an acquisition, as it did for Genentech/Roche. And due to the recent economic climate, pharmaceutical companies may be predisposed to shift directly to acquisitions rather than entering into strategic partnering relationships while their pipelines dissipate and many small biotech companies fight off insolvency and sinking valuations.

Acquisitions by pharmaceutical or large biotech companies represent an alternate exit option for biotech companies to IPOs. The first half of 2009 has seen a wave of acquisitions by pharmaceutical companies, although not all acquisitions have been such goliath mergers as the **Merck/Schering-Plough** and **Pfizer/Wyeth** mergers. Instead, some recent acquisitions were the result of pharmaceutical companies paying a premium for less-established biotech companies, such as big pharma **Johnson & Johnson's** (J&J) acquisition of biotech company **Cougar Biotechnology** for approximately \$894 million.

Another alternative approach to raising

capital is by royalty monetization, which is the sale of future revenue in the form of either royalties or product revenues. This is similar to partnering, as an investor has a shared goal for the success of the product underlying the revenue stream. Royalty monetization has been more popular in recent years, but is frequently limited to those biotech companies that already have

(or expect very soon to have) a commercialized product or are already receiving some type of return on their intellectual property, such as from license agreements. There are some firms that specialize in royalty monetization such as Paul Capital Healthcare, Drug Royalty, and Royalty Pharma.

Although risks are associated with any of the aforementioned capital-raising alterna-

tives, much can be mitigated by careful negotiating and drafting. Each biotech company has its own unique set of circumstances surrounding its capital-raising endeavors. Before seeking another round of financing, biotech companies should explore which options best meet their needs and can provide the lifesaving cash injection that the current economic climate especially demands. GEN



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