

Patheon Places Big Bet with Mova Acquisition

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Patheon is betting the whole is worth more than the sum of the parts in its acquisition of Puerto Rico contract manufacturer Mova.

Patheon's \$350-million acquisition of Mova Pharmaceuticals caught much of the industry by surprise. It was widely known that Mova's owners were interested in selling the company, but few people thought that Patheon (Toronto, Canada, www.patheon.com) had the financial wherewithal to complete such a big transaction.

In fact, Patheon took on a lot of debt and diluted the position of its stockholders to bring the deal off. Patheon is paying Mova's shareholders 12.7 million shares of Patheon stock (worth \$81 million when the deal was announced), plus \$144 million in cash, which it raised by selling shares of its publicly-traded stock. In addition, Patheon is assuming \$125 million of Mova's debt obligations. Mova's principal shareholder, Joaquin Viso, will own 16% of Patheon's stock when the deal is complete.

The payments don't stop there, however. Under the earn-out provisions of the acquisition agreement, Patheon may pay Mova stockholders as much as \$91 million if the business reaches certain profitability targets in the first nine months of Patheon's ownership, which will bring the total purchase price to \$441 million. Patheon will probably incur additional debt or sell more shares to raise the cash for the additional payments.

The acquisition price represents a multiple of 2.6 times Mova's revenues and 9.1 times Mova's EBITDA (earnings before interest, taxes, depreciation, and amortization). To justify those numbers, Patheon is clearly counting on Mova's operations to boost its performance and stock valuation in a big way.

A big part of the benefit will come from marrying Mova's large-scale manufacturing operations with Patheon's business development capabilities. Mova's Manati site (where Roche once

manufactured Valium) has the very large-scale, solid-dose manufacturing capacity that Patheon's Canadian facilities lack, and is operating at only 20% utilization. Mova's Carolinas cephalosporin facility provides the company with a unique capability and significant capacity. Patheon's large sales force can churn up new opportunities for those facilities, while its rapidly-growing development operations can create a pipeline of new NDA products over time.

Patheon's executives made it clear, however, that financial considerations were a big motivation in their decision to do the deal. For one, the Mova acquisition will help Patheon overcome the currency mismatch that eats away at Patheon's profits. Patheon's contracts are generally denominated in US dollars, but most of its expenses are in Canadian dollars, Euros, or British pounds. The devaluation of the dollar has increased the translated dollar value of those expenses, which reduces Patheon's reported profits. By adding Mova's operations to its other US-based operation in Cincinnati (acquired from Aventis in 2003), Patheon might achieve a better match between revenues and expenses.

Patheon's profitability will also benefit from Mova's lower tax rate. Because it is a Puerto Rican company, Mova enjoys a corporate tax rate of 2-7%, while Patheon's current corporate tax rate is 40%. Patheon says the Puerto Rican authorities have assured it that its Puerto Rican operations will continue to enjoy the same tax rate after the acquisition is completed. The combined income statements will give Patheon a lower average tax rate.

Patheon also expects to see cash flow improve as a result of the acquisition. For the past several years, Patheon has suffered negative "free cash flow" (operating cash flow less capital investment) because of low margins and heavy capital investment. Mova enjoys better margins and a low tax rate and has required less capital investment, so it has a better free cash flow that will immediately benefit Patheon's finances.

Patheon's Mova acquisition changes the competitive contract manufacturing landscape, especially for standard dosage forms (solid dose, semi-solid, and liquid products). The Mova acquisition



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removes a principal competitor from the standard dose arena and may lead to higher contract manufacturing prices.

At the same time, the presence of a large, global player will enhance the industry's legitimacy. Patheon now has \$650 million in total revenues, giving it the dose manufacturing scale of a \$6 billion pharmaceutical company, and is the only standard dose manufacturer with global manufacturing

sites. If it performs well, it will raise the bar for the industry and drive competitors to improve their performance. If it performs poorly, however, it could sour Big Pharma's view of contract manufacturers.

PRA goes public

PRA International (McLean, VA, www.prainternational.com), a clinical CRO, completed its initial public offering on 17

November. PRA sold 6 million shares at \$19 each, raising \$106 million after underwriting expenses. Early investors in the company got \$42 million of the proceeds, and the company took in \$64 million for general business purposes. The stock price jumped nearly 20% in the first two weeks of trading, valuing the company at nearly \$500 million.

PRA generated \$249 million in revenues in 2003, and earned \$31 million in pretax operating revenue. For the first nine months of 2004, its revenues were up 11% and operating income was up nearly 30%.

Baxter rebrands service offerings

Baxter Healthcare Corporation (Deerfield, IL, www.baxter.com) has brought together its contract services and drug delivery capabilities into a single unit, **Baxter BioPharma Solutions** (www.baxterbiopharma.com). The reorganization creates an integrated sales and marketing effort and a single point of customer contact for a portfolio of formulation and manufacturing services, including biomanufacturing, contract manufacturing of injectable products (including cytotoxic injectables), and drug delivery technologies. Baxter acquired most of these capabilities during the past five years. **PT**

FYI

Filtration equipment demonstrations

The American Filtration and Separations Society (AFS, Minneapolis, MN, www.afssociety.org) has a new strategy to educate specifiers, buyers, and users of filters and filtration and separation equipment during the 2005 AFS Annual Conference and Exposition, which will be held 10-13 April 2005 in Atlanta, Georgia.

To maximize the opportunity for plant engineers, the AFS has created "Plant Floor" by setting aside a major portion of the exposition floor for manufacturers to demonstrate filtration products in continuous operating mode. This is an opportunity for industry to inspect a wide variety of filters, filtration equipment, and systems operating in a single location.

For information about visiting the plant floor or exhibiting at AFS, visit www.afssociety.org or contact Steve Rose at 262.547.4900 ext. 11.