

# 2004 Outsourcing Survey

## Growing Demand for Services and Performance

Jim Miller

Pharmaceutical companies are rapidly increasing their outsourced drug development spending, but they are spending their earnings with fewer suppliers and asking more from them.



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**B**ecause the entities dominating the CMC sector (manufacturing, packaging, formulation, and analytical services) seldom report financial results, determining the state of that portion of the pharmaceutical outsourcing industry can be challenging. Polling outsourcing providers and their clients provides a comprehensive view of the CMC sector's basic health and underlying trends.

The annual PharmSource-*Pharmaceutical Technology* outsourcing survey was conducted in June to *Pharmaceutical Technology* and *Bio/Pharmaceutical Outsourcing Report* subscribers. More than 300 respondents from all segments of the pharmaceutical and contract service provider industries completed the survey (see sidebar, "Respondents profile"). This year's survey included questions about outsourcing practices such as preferred provider relationships. All responses were classified by the size and type of company.

### Strong demand for outsourcing

Pharmaceutical company respondents expect strong growth in their outsourcing expenditures. Overall, 21% expect outsourc-

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# Survey Results

## Respondents profile

In June 2004, PharmSource and *Pharmaceutical Technology* conducted a survey of outsourcing decision-makers by e-mail. The questionnaire was sent to 8937 individuals and delivered a 3.4% response rate. Survey participants received a lottery entry to win one of two \$100 gift checks.

Respondents identified themselves as being from either a pharmaceutical or a contract services company and received a different set of questions based on their response. Of the 305 respondents, 210 (69%) represented pharmaceutical companies and 95 (31%) represented contract services providers. All major pharmaceutical segments were included: Big Pharma/Biopharma (34%), Small Pharma/Biopharma (29%), specialty pharmaceutical (20%), and generics (14%) companies. If some respondents did not answer a given question, the percentages total less than 100%. Other characteristics of pharmaceutical company respondents included the following:

### Primary job function

• technical/scientific:	47%
• project management:	19%
• quality assurance:	16%
• sourcing/procurement:	6%
• other:	9%

### Contract CMC services bought/specified

• analytical chemistry and microbiology:	54%
• dose manufacturing (solids, semisolids, oral liquids):	35%
• formulation and clinical trial material manufacture:	31%

• active pharmaceutical ingredient process development and manufacture:	29%
• dose manufacturing (injectables):	26%
• commercial packaging:	24%
• clinical packaging:	22%
• drug delivery:	18%

### Annual spending on CMC services (in millions)

• <\$10:	51%
• \$10–24:	16%
• >\$24–50:	9%
• >\$50:	12%
• not applicable:	10%

The following are characteristics of contract service provider respondents:

### Annual contract services revenues (in millions)

• <\$10:	57%
• \$10–24:	12%
• >\$24–50:	9%
• \$50–100:	7%
• >\$100:	11%

### Share of contractor revenue from Big Pharma/Biopharma companies

• 50% or more:	28%
• 25–50%:	28%
• Less than 25%:	34%

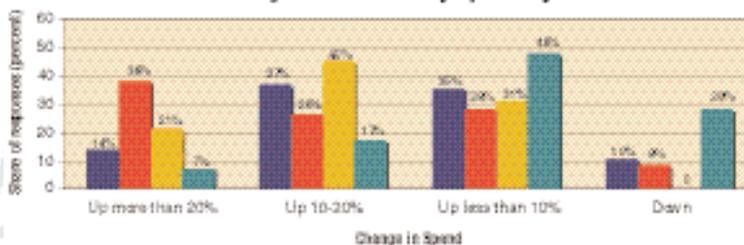
ing spending to increase by 20% or more in 2004, and 32% expect spending to increase by 10–20%. Respondents from generics companies report slower growth than those from innovator companies. Only 10% of all respondents, however, expect to reduce spending for the year.

Contractor respondents are upbeat about revenue growth. Overall, 37% expect revenues to grow more than 20% in 2004, and 39% expect a 10–20% increase in revenue.

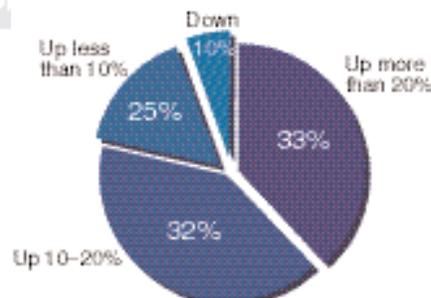
Respondents cited several reasons for the outsourcing expenditures growth that are consistent with conventional wisdom about why companies outsource. Big Pharma/Biopharma respondents most often credit the need to supplement in-house capacity, but Small Pharma/Biopharma respondents overwhelmingly identified the need for capabilities that are unavailable in-house. Among specialty pharmaceutical respondents, 25% made a strategic decision to use contractors exclusively for certain functions (e.g., clinical packaging, analytical chemistry).

Contractors report that all industry segments are contributing to their strong performance this year. The largest share of contractors credit Big Pharma/Biopharma companies with fueling the growth. This result is consistent with Big Pharma's dominance of the industry's development and manufacturing

Change in outsourcing spending 2004

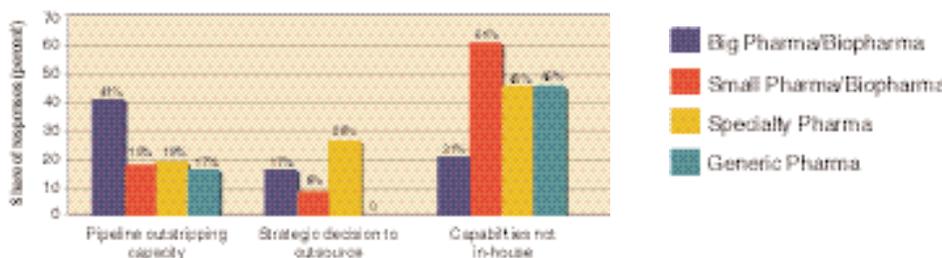


Contractor revenue growth for 2004



# Survey Results

**Why has outsourcing grown in 2004?**



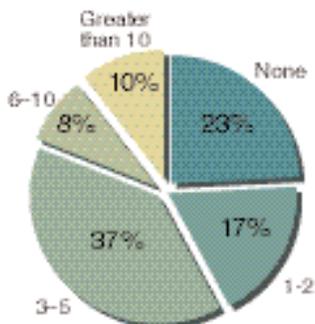
spending. Still, many contractors rely heavily on smaller companies for the bulk of their revenues (see sidebar, “Respondents profile”) and have benefited from the industry’s overall increase in development spending.

## Preferred providers

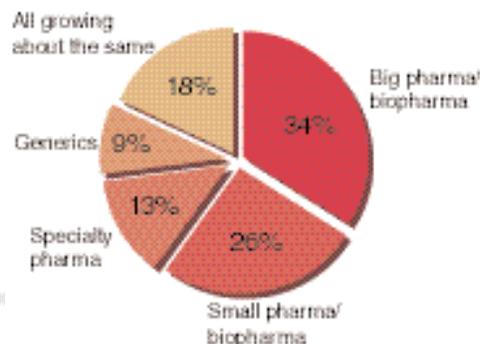
The survey confirmed the continued trend toward using fewer preferred providers. Among all pharmaceutical company respondents, 44% report that more than half of their expenditures go to preferred providers. Big Pharma/Biopharma companies are leading this trend: 49% of Big Pharma/Biopharma respondents indicate that preferred providers account for more than half of their spending, and 62% expect that more than half of their expenditures will go to preferred providers by 2006.

Not surprisingly, preferred provider relationships account for a growing share of contractor revenues. Among contractor respondents, 40% report that preferred provider clients make up a quarter or more of their revenues, and more than 50% report that at least a quarter of their revenues will come from preferred provider relationships by 2006. Of all contractor respondents, 77% have at least one preferred-provider relationship and 18% have more than 5.

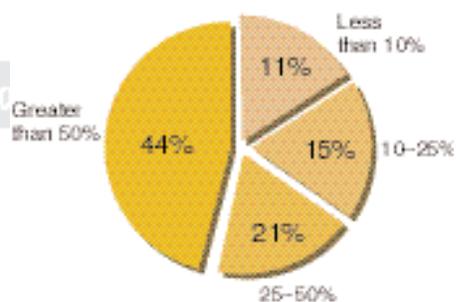
**Number of contractor preferred provider relationships**



**Which of your clients have been the biggest contributors to your growth in 2003?**



**Share of outsourcing spend going to preferred providers**

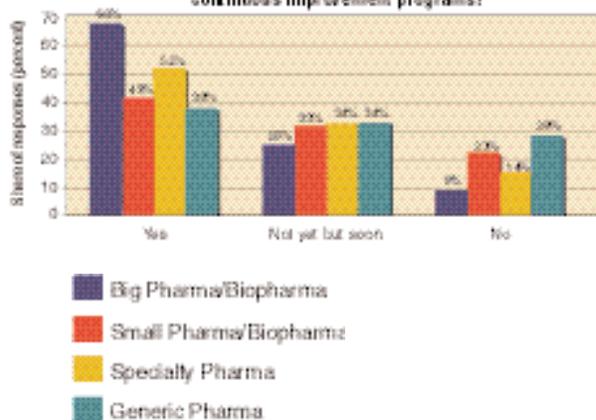


## Continuous improvement

An increasingly important element of outsourcing relationships is the expectation that contractors show steady improvement in the cost, quality, and timeliness of their services. Of all pharmaceutical/biopharmaceutical respondents, 52% at least require their preferred providers to have continuous improvement (CI) programs. Twenty-nine percent will require CI programs soon. Nearly two-thirds of Big Pharma/Biopharma clients require CI efforts, while small companies still lag behind.

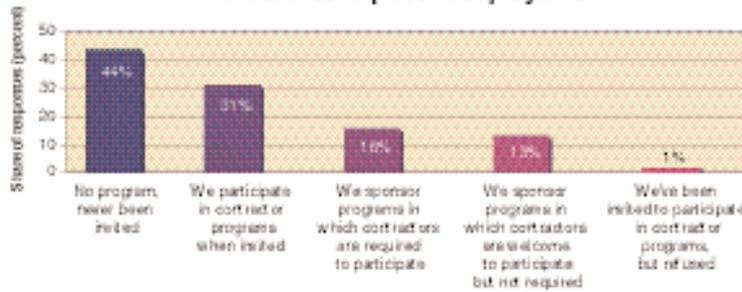
Service providers are responding to the call for better performance. Of contractor respondents, 48% have a continuous improvement program in place, and 16% plan to implement a program this year.

**Are you demanding that contractors implement continuous improvement programs?**

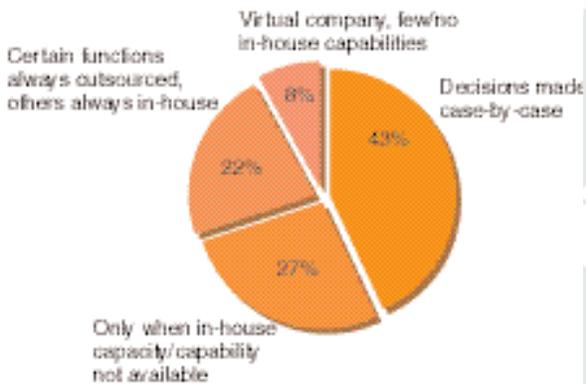


## Survey Results

### What is your involvement in your contractor's continuous improvement programs?



### What is your policy on outsourcing?



Pharmaceutical companies encourage CI efforts in different ways. Nearly 30% of respondents encourage or require contractors to participate in their sponsored CI programs. Approximately 30% of respondents have been involved in contractor-initiated CI programs. Yet, 44% have never been involved in a CI program with their contractors.

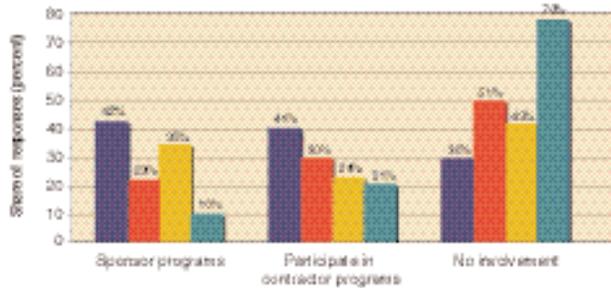
The level of involvement differs radically by the type of pharmaceutical company. More than 80% of respondents from Big Pharma/Biopharma companies are involved in a CI program that is either sponsored by their companies or the contractors. At the other end of the spectrum, 76% of respondents from generics companies have no involvement in CI programs.

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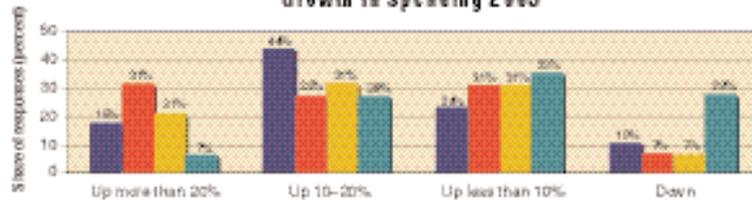
# Survey Results

**Nature involvement in continuous improvement programs by pharmaceutical companies**



- Big Pharma/Biopharma
- Small Pharma/Biopharma
- Specialty Pharma
- Generic Pharma

**Growth in spending 2005**



## Still tactical

Data from the survey indicate that pharmaceutical companies rely heavily on contract service providers and manage outsourcing relationships in a sophisticated manner. Nevertheless, most pharmaceutical companies still make a tactical decision to use outsourcing services. Fully 43% of respondents indicate that outsourcing decisions are made on a case-by-case basis without a broader strategic context. Twenty-seven percent of respondents report that projects are outsourced only when in-house capacity is unavailable. Only 30% of companies have decided to outsource certain functions exclusively.

Regardless of the motivation, the volume of outsourcing activity will continue to grow. Of all pharmaceutical respondents, 62% expect their contract services spending to increase by 10% or more in 2005, with three of the four pharmaceutical/biopharmaceutical segments expecting growth. Only generics companies expect to outsource less.

Because previous surveys have been good predictors of growth in contract services spending, the industry can look forward to continued success and banner years for 2004 and 2005. **PT**



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