

▶ **Warning, merge with care: Sanofi-Aventis**

A near-shotgun marriage for France's two largest pharmaceutical companies

BY KIMBERLY S. CLEAVES AND ANN M. THAYER

With the goal of building a dominant player in the pharmaceutical industry, French drugmaker Sanofi-Synthélabo launched a hostile takeover in January of a much larger rival, the French-German pharmaceutical company Aventis. Although Aventis at first scoffed at the notion, the advances got the industry's and larger company's attention. And the smaller company's persistence in the ensuing face-off eventually resulted in a "happy marriage" that will create the third-largest pharmaceutical company in the world after Pfizer and GlaxoSmithKline.

Initially fighting off the unwanted overture, Aventis launched an ad campaign in the guise of a phony drug product called "Bid - Hostile Take Over." The ads included warnings such as "This medication may be harmful to Aventis shareholders and employees" and "This medication can seriously stunt growth." Among its arguments against a deal, Aventis's management questioned in one ad whether the loss of patent protection on two main products, which represent about 43% of Sanofi's sales, would negatively impact Aventis's own anticipated sales growth.

In another ad, Aventis pointed out that the patent on the antithrombotic drug Plavix, a leading product contributing \$1.65 billion to Sanofi's 2003 sales, is being challenged in a U.S. court. "Should the decision be unfavorable to Sanofi-Synthélabo, certain analysts believe that its share price could lose up to a third of its value. Why should Aventis shareholders have to take such a risk?" the ad asked. Aventis's management and supervisory boards, along with its employee shareholder association, also warned of "brutal job losses" and "severe value destruction."

However, the Aventis campaign could not

stop the merger's momentum, particularly after intervention by the French government. And despite the initial vitriol, even more aggressive legal tactics, and the emergence of another suitor, Aventis and Sanofi did reach an agreement. What is to be called "Sanofi-Aventis" is now poised to become the European pharmaceutical leader after a rocky start getting there.

Just say no

In January, believing the Sanofi proposal offered inferior value and significant risk,



Aventis's Landau (left) and Sanofi-Synthélabo's Dehecq eventually came to terms.

Aventis's management board rejected the nearly \$60 billion acquisition attempt. Soon after, however, the Autorité des marchés financiers (AMF), France's stock market authority, cleared Sanofi's unsolicited tender offer, pursuant to French tender offer rules. Aventis subsequently filed a legal action with the Court of Appeals of Paris seeking to invalidate the AMF decision. Meanwhile, the company's supervisory board recommended that shareholders not accept the offer and directed management to look for alternatives.

By early March, Aventis submitted its official rejection to the AMF for review. "We firmly believe that this offer is not in the best interests of Aventis shareholders or employees," said management board chair-

man Igor Landau at the time of the filing. The company followed with its "Say No to Sanofi's Offer" defense brochure, sent to 69,000 employees and more than 300,000 individual shareholders. Sanofi, which is half Aventis's size, would control the merged company.

The 16-page document detailed several arguments against a merger. In addition to a valuation considered 30% too low, the risk of a largely stock-based deal, and the possibility of major job cuts, they included concerns that the proposed combination would provide little strategic benefit for Aventis. The company believed that it, not Sanofi, was best positioned to drive growth through new product launches and to contribute the most to earnings growth.

For example, if the Plavix and other patents were lost, Aventis said, Sanofi's pipeline was not expected to offset lost sales. Aventis noted that between 2004 and 2006 it expects to launch six new products, while Sanofi anticipates only three. Aventis also believes it has four more potential breakthrough products in its pipeline—including Alvesco (ciclesonide), an inhaled corticosteroid for chronic pulmonary disease—compared with Sanofi's one potential blockbuster, Acomplia (rimonabant). The drug, an endocannabinoid receptor antagonist (CB1A) under development for the treatment of obesity and smoking cessation, is expected to reach the market in 2005.

Aventis also stated that the offer would dilute its sales in the United States and increase its exposure to European markets. The company said it saw few sales or competitive synergies, and significant differences in size and organizational cultures. In the end, "we don't need Sanofi, but they need Aventis," Landau concluded.

Simultaneously, Sanofi's arguments for a merger centered on the combined entity's size: its market share, significant R&D investment, existing high-growth products, 9 drugs each with annual sales over \$600 million, 60 products in late-stage clinical development, and expected savings of

nearly \$2 billion per year, along with a 15% premium on Aventis's share price.

"This major strategic project will enable us to take advantage of our exceptional complementary businesses to create a market leader with strong, sustainable, profitable growth," said Sanofi chairman and CEO Jean-François Dehecq when launching the bid. Industry analysts have tended to side with Sanofi, believing it offers a stronger potential for earnings growth than Aventis.

A white knight?

Aventis's next steps were even more aggressive. It filed a communication with the U.S. Securities and Exchange Commission and posted information on its website providing an outside legal analysis of the Plavix litigation. The company proposed offering warrants to protect its shareholders in case Plavix lost market exclusivity. It also filed a legal action with the U.S. District Court in New Jersey attempting to block the tender offer. The complaint stated that Sanofi's public filings and statements contained "significant omissions and representations," related to the Plavix patent situation. Then, in early April, Aventis's supervisory board unanimously invited Novartis to enter merger talks.

Drug industry participants and analysts had already been speculating that Novartis, Switzerland's largest drugmaker and number five in the world, might emerge as a white knight, and come to Aventis's defense with a friendlier deal. If it had happened, such a deal would have created the number two pharmaceutical company in the

world behind U.S.-based Pfizer. Novartis had already begun conducting a feasibility study in March.

However, some individuals in the French government were voicing their opposition to the Swiss giant's involvement with the number one and number two French drug companies. Comments from French government officials, including Prime Minister Jean-Pierre Raffarin, expressed concern about a non-French partner for Aventis and support for an all-French alliance. Novartis indicated that it would negotiate with Aventis only if the French government took a neutral position.

On April 25, Novartis decided to stop negotiations with Aventis and said it would not submit a merger bid. Apparently, Aventis was in talks with Sanofi. "Following Aventis's decision to engage in discussions with Sanofi, at the strong intervention of the French government, Novartis decided not to proceed," the company said when removing itself from the competition.

On April 26, Sanofi and Aventis announced an agreement. "We are pleased to have reached an agreement that recognizes the value of Aventis from a financial standpoint as well as the talent and expertise of our employees," Landau said. "By being equally represented in the management of Sanofi-Aventis, this agreement provides the necessary conditions for the success and development of the new group."

The new deal is valued 14% higher, for a total of roughly \$68 billion, and offers a 31.4% premium on Aventis's share price. The transaction consists of 71% in Sanofi shares

and 29% in cash versus 81% and 19%, respectively, in the original offer. Aventis's supervisory board now believes the offer represents a valuation in line with comparable transactions, improved terms reflecting Aventis's contributions and growth potential, successful and fair integration between the two companies, and full disclosure on the Plavix situation. In return, Aventis will withdraw all outstanding litigation against Sanofi and the AMF.

In a webcast, Sanofi appealed to Aventis shareholders to accept the deal with a concluding slide: "Aventis Shareholders: Tender your shares to Sanofi-Synthelabo's friendly improved offer."

Joining forces

Interestingly, both Aventis and Sanofi-Synthelabo are the results of mergers themselves. In 1999, Aventis was formed from the combination of the French life sciences company Rhône-Poulenc and German giant Hoechst. Sanofi-Synthelabo was also created in 1999 from the merger of the French health care companies Sanofi and Synthelabo.

However, this may be where the similarities end.

According to a research report by pharmaceutical industry analysts Exane and Bionest Partners, "Corporate culture shock is the greatest risk from the merger." The analysts go on to explain that, although the two companies share many traditional values, they differ greatly in other areas. For example, Aventis, created from a string of mergers and acquisitions, eventually found unity around growth drivers and key products. Its management structure is international, and decision-making is shared by geographic operations.

In contrast, "The man behind Sanofi-Synthelabo is Jean-François Dehecq," the analysts say. "The company's key values reflect his entrepreneurial strength: bold innovation, performance, and solidarity. The management team is French, and the decision-making centers are located in France." The best combination, they conclude, would draw on Aventis's organizational structure and the smaller company's management momentum. As chairman and CEO, Dehecq will head the newly formed Sanofi-Aventis with a German vice chairman.

Sanofi-Aventis will be major drug industry player

Headquarters	Paris
Chairman and CEO	Jean-François Dehecq
Pro forma sales	\$30.5 billion ^a
Pro forma net income	\$5.53 billion
R&D spending	\$5.13 billion ^a
Number of employees	102,000 ^a
Product areas	Cardiovascular, oncology, diabetes, central nervous system diseases, internal medicine, and human vaccines

^a Roughly two-thirds from Aventis. Source: Company results for 2003.

In general, the Exane–Bionest analysts and others are positive about the combination, seeing complementary strengths. Pharmaprojects, which tracks pharmaceutical development, reports a good, and not very overlapping, pipeline fit between the two companies. Aventis, it says, appears to have drugs in development in a wider selection of therapeutic areas than Sanofi. Aventis is stronger in anti-infectives than Sanofi, which itself is strong in neurology, but the two firms match up well in the number of metabolic, anticancer, and cardiovascular drugs under development, Pharmaprojects adds.

The two companies also differ in their approach to R&D: Aventis has a complex and expensive program spread across various worldwide sites, whereas Sanofi's more focused efforts are built around a small decision-making group. "Sanofi-Synthelabo is usually viewed as having a strong pipeline of products under development, while Aventis is generally described as one of the last in the class," the Exane–Bionest analysts say. However, Sanofi's approach is very risky, they add, with many products in the Phase II clinical

stage from a multitude of innovative approaches. Aventis, meanwhile, has overhauled its R&D operation and has purchased a large number of products to build up its pipeline.

Still, the Exane–Bionest analysts believe

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the merger makes economic sense, resulting in a world leader with a more attractive risk profile. With a combined 12 new chemical entities being launched between 2005 and 2007, the product profile would be broad enough to reduce dependency on any one project and help counter the effects of patent expirations.

Although Sanofi's sales are only half of Aventis's, the two companies have more-equal market valuations. The deal has been supported by Total and L'Oréal, two French companies that own a combined 44% of Sanofi's shares. Total has expressed its desire to exit the investment, and a pact between the two major shareholders ends in December. According to IMS Health, this possible shift is thought to have been "a major spur to Dehecq's bold move, as Sanofi could have become a vulnerable takeover target itself."

Meanwhile, Novartis, the potential white knight, is still involved in speculation about the next big drug industry merger. It owns 33.3% of Roche, which is just 500 shares short of its being required to launch a takeover bid, but seems willing to wait until Roche is less resistant to the idea, IMS Health suggests.

"The likes of GlaxoSmithKline and AstraZeneca could well be tempted to move in on one of the struggling U.S. firms to keep their place in the rankings," the research firm also points out. "It seems likely that a fresh wave of consolidation could sweep through the industry." ■

► Decommissioning knowledge silos

To succeed, R&D, clinical, and marketing departments must see each other as assets.

BY RANDALL C. WILLIS

The pharmaceutical industry has reached a critical stage in its history. At the same time it is facing greater government scrutiny and more costly regulatory processes, the industry is also being inundated by ever-shorter periods of exclusivity and accelerated genericization. As governments and insurers threaten to cut back on reimbursement schedules, the public continues to see the industry as outrageously profitable. And, even as R&D spending has continued to increase, the number of new molecular entities has not.



Bayney

Drug discovery traditionally has started with pushing a screening hit unidirectionally from the R&D phase into clinical trials and, if successful, into the market, with little or no feedback from the downstream end as to whether the product is relevant or marketable. At each stage, relevant information about the potential drug product has been compartmentalized into silos. According to several industry insiders, however, as the price tag of each new drug soars, it will become ever more critical for these silos to be broken down and for the multiple departments involved in the process to become active partners, feeding information forward and back.

Changing business

According to pharmaceutical industry analysts Françoise Simon and Philip Kotler, the advent of postgenomic research and information technology not only will change drug development timelines but will also precipitate new marketing approaches. Thus, they argue, "Addressing this fundamental change requires a rethinking of the concepts of health and disease, but also of drugs (shift from pills to integrated solutions, including diagnostics) and marketing models."

Rick Bayney, vice president of decision analysis and portfolio management for Johnson & Johnson Pharmaceutical R&D, goes one step further, arguing that to be successful, companies will have to link their strategies and objectives across the value chain. Problems arise, Bayney believes, when the R&D investment strategy is not well connected to the portfolio strategy, which, in turn, is intended to be driven by the overarching business strategy. He recommends that, wherever possible, a

company should synchronously integrate its strategy, budget, and portfolio plans so any changes occurring in one section can be handled in the other two. To accomplish this feat, however, companies must look beyond simple milestones and instead focus on longer-term goals.

“The industry is intensely focused on fulfilling top-line goals, making it inevitable that we have to concentrate on blockbusters,” Bayney complains. “But if we manage our resources well across a larger number of products, we can increase the likelihood of reaching our launch and revenue targets.”

Similarly, he believes it is critical for the drug discovery, development, and marketing streams to be seamlessly well coordinated. “If you have a great R&D idea and an unmet market need, but the two can’t be converted in the clinic into a product that will alter a physician’s prescribing habits, the project may either not materialize or deliver suboptimal results,” he explains.

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Corporate détente

Perhaps not surprisingly, Bayney’s attitude about research, clinical development, and marketing synergies has met with some resistance, but as he explains it, focus does not have to come at the expense of creativity. “It’s not just about meeting targets,” Bayney argues. “As an industry, we need to become better at improving the quality of what comes from discovery and goes into the clinic.”

And a significant part of this improvement, adds Ramana Sonty, senior director and team leader of worldwide development at Pfizer Global Pharmaceuticals, will come from a closer working relation-

ship between the R&D and commercial groups. To get everyone pulling in the same direction, however, companies will have to overcome three main challenges.

First, there are significant differences between the life cycles of R&D projects (10–15 years) and marketing projects (1–3 years). For this reason, each group has different priorities and reward systems. Ultimately, these mechanisms result in unique cultures, and it can be very difficult to bridge the gap between the two.

Leadership is the key to executing this unification process, Sonty argues, and when he worked at Pharmacia as director of the R&D strategy group, he says this leadership came in the form of a customer-centered focus. To ensure customer satisfaction, he relates, Pharmacia made sure everyone felt some degree of ownership over the product. This meant that information had to be shared transparently from discovery through sales to optimize the product, while, at the same time, everyone was expected to understand evolving or changing customer needs.

Thus, management had to assure the marketing people that, although they would not be monetarily compensated for their long-term thinking, they would be recognized for their efforts. Likewise, senior officials had to convince R&D of the benefits of involving marketing early in the discovery and development phases. With time and patience, however, both sides came to appreciate the opinions and thoughts of their counterparts, Sonty notes.

Committed to committees

To accomplish these or similar goals, several pharmaceutical companies have introduced internal R&D review committees.

At Pharmacia, management established R&D Therapeutic Area Reviews, which have consisted of annual scientific meetings, using both internal and external experts from various fields as well as commercial people. For example, a review committee might comprise external consultants (often academics), the CSO, the president of R&D, and various vice pres-

idents of departments ranging from discovery and preclinical development to technology acquisition, primary care marketing, and commercial development.

According to Sonty, these committees have tended to focus on projects from the lead identification to Phase II stages and were set up to identify key issues and



Schirlin

provide a basis for project prioritization and resource allocation. “This was not an opportunity for show-and-tell,” he relates, “but rather to highlight and refine strategic decisions. We also had to assure people that this was not just another administrative hoop through which they had to jump.”

Likewise, according to Daniel Schirlin, global head of lead generation and senior vice president of drug innovation and approval at Aventis, his company has established Hit Evaluation Committees composed of internal and external medicinal chemists, therapeutic specialists, and others who can draw on their expertise to review and critique projects and thereby facilitate decision-making and, possibly, open doors to new avenues of exploration.

Aventis also has established a group it calls the Permanent Library Team (PLT), which looks to improve the company’s library of compounds by analyzing in-house failures and looking at external projects being pursued by other companies and academics. The group then makes recommendations to all departments and oversees cross-functional implementation in terms of compounds and required technologies. PLT members include people involved in informatics, chemical biology, lead development, medicinal chemistry, business development, and compound libraries and synthesis.

Because most of these committees are relatively recent incarnations, there are few numbers to back up how successful these methods will be.

“The real difference between success and failure comes in the skills of your people and the processes you put in place,” Schirlin explains, “not only to achieve deliverables, but also in how you use your assets.” ■