



Outsourcing Outlook

Jim Miller

The chemistry, manufacturing, and controls (CMC) outsourcing industry continues to be reshaped by acquisitions and divestitures. The activity reflects the maturing of the industry and the changing strategies of key participants.

The big news is the acquisition of **Magellan Laboratories, Inc.** (Research Triangle Park, NC) by **Cardinal Health** (Columbus, OH). Magellan is a leading provider of CMC development services, including analytical and structural chemistry, pharmaceuticals, chemical synthesis, and bioanalytical testing. The company had revenues of \$60 million in 2001 and has been averaging 30% revenue growth in recent years. The purchase price had not been announced at press time.

Cardinal is recognizing the strength of Magellan's reputation and management by making it the flagship of its development services effort. Cardinal's new unit will do business as Magellan Pharmaceutical Development Services (MPDS), reversing a trend to rebrand acquired businesses under the Cardinal Health name. Magellan founders Lowry Caudill and Al Childers will manage the operation, reporting directly to George Fotiades, president of the Cardinal Health Pharmaceutical Technologies and Services group. Caudill and Childers will take over Cardinal's new \$80-million, 265,000-ft² development center in Somerset, New Jersey, and the parenteral products development operation in Albuquerque, New

Mexico, which had been part of SP Pharmaceuticals (bought by Cardinal Health in 2001).

Cardinal and Magellan view the mission of MPDS as driving new business into Cardinal's commercial manufacturing and drug delivery businesses by capturing clients at an earlier stage in the development process. At the same time, they know that the business must stand on its own. "We're going to work on anything the customer wants us to work on, including conventional dosage forms," Fotiades said.

Other deals

According to industry buzz, another big deal in the works is the sale of clinical packager **Clinical Trial Services** (CTS, Philadelphia, PA, and Craigavon, UK) by parent **Galen Health, Inc.** (Craigavon, UK). No official word has come from Galen, but the sale has been expected ever since Galen expanded its proprietary products business by buying Warner-Chilcott in 2000 and then sold its Syngal and Quchem chemical synthesis services businesses in February 2002.

In addition, the CMC industry is losing a participant as **Omnicare Pharmaceuticals** (Fort Washington, PA) closes its development operations. The company had achieved sales of almost \$20 million and was profitable, but a flood decimated its facilities in June 2001, and its parent company decided not to rebuild the business. Omnicare will reestablish a clinical packaging business at its Toledo, Ohio, repackaging facility.

CROs feed on biotech

Large CROs have been actively courting smaller biopharmaceutical and pharmaceutical companies, and the results are beginning to show. According to Wall Street analysts David Windley of Jefferies & Co. and Eric Caldwell of Prudential Securities, smaller sponsors now account for 25% of the revenue of the public CROs,

up from 10 to 15% historically. Caldwell estimates that small pharma and biotech companies represent as much as 33% of the CROs' order backlog.

Smaller companies have become more attractive clients because of their maturing pipelines and their success in raising money through the past several years. The year 2000 was unprecedented for the biotech sector in the capital markets. According to industry watcher Burrill and Company (San Francisco, CA), biotech firms pulled in an estimated \$39 billion, more than three times the amount raised in 1999.

The pace slowed significantly in 2001, however, as total capital raised fell to \$13 billion. Market conditions were considerably more difficult in 2001: Seven companies that filed for IPOs withdrew their deals, and the companies that were successful had relatively stronger and more-advanced pipelines than companies that floated IPOs in prior years.

Even though 2002 may be a disappointing year for fund-raising, the biotech and small-pharma segment should continue to spend aggressively in development services. Analysts estimate that many companies raised as much as five years' worth of capital during 2000–2001 and are only now beginning to spend those funds.

It is unlikely that biotech will ever supersede Big Pharma as CROs' principal business source. Big Pharma's already massive R&D budgets are forecast to expand 8–10% this year, and 20–30% of those funds will flow to CROs. Still, recent events have demonstrated that big CROs must diversify their client base because they cannot rely on the stability of their Big Pharma relationships. The stock of PPD Inc. (Wilmington, NC) recently took a sharp drop because of investor concern that problems at Bristol-Myers Squibb, which analysts estimate provided PPD with 10% or more of PPD's revenue, would hurt its profitability. **PT**

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