Biopharmaceuticals deal trends

Competition for innovation overcomes economic headwinds
In 2020, deal making surged in pharmaceuticals. Despite the impact of COVID-19 on the economy, major pharma companies closed 1,138 deals. A record deal count. What drove so many deals? The biggest factor: Competition to build innovative pipelines and acquire new capabilities in transformative technologies such as mRNA, cell therapies, gene therapies, and bispecifics. Underlying this highly competitive and active deal market was the combined effect of the perpetual need of the pharmaceutical industry to find assets that can provide future revenue and the maturity of technologies developed in an era of innovation unlike the industry has ever seen. Although the Biden administration’s comments about anticompetitive behavior in the pharmaceutical industry may create a headwind for mega-mergers and larger acquisitions, we expect small and mid-size deals to continue to thrive in 2021.

In this paper, we take an in-depth look at how biopharmaceutical companies are deploying their capital. We analyze what types of targets they focused on in 2020 and present our expectations for 2021. The message: For the foreseeable future, biopharma executives will continue to use a wide range of deal strategies from M&A to creative partnerships to strategic R&D collaborations to balance opportunities and risks in pursuing innovation and building their pipelines. As in the recent past, the challenge will be to select the best opportunities amid rising valuations and still-unproven targets.
Key Insights

— 2020 was a banner year—more deals than EVER!
— The total value of company acquisitions was down in 2020 compared to 2019
— The number of strategic R&D deals were up over 2X compared to prior years
— Asset licensing deals were up 233 transactions
— The number of corporate acquisitions were up in 2020 versus 2019
— Only one deal was north of $30 billion in 2020 compared to 2019 which involved two deals over $60 billion

The quest for innovation

When the COVID-19 outbreak slammed the economy, it seemed like deals in the biopharmaceutical industry and other sectors would also slow down. Many observers predicted that transaction volume would be down in 2020. However, a deeper analysis of the industry shows that the volume of deals hit an all-time high (Exhibit 1). The total number of deals in 2020 was 1,138 compared with 634 for 2019.

Exhibit 1. Volume of all biopharma deals hit a record in 2020


1See for example, Pharma Intelligence, "A Decade of Biopharma M&A and Outlook for 2020," March 2020.
The growth was particularly dramatic for transactions using creative deal structures. Strategic R&D collaborations more than doubled from 161 in 2019 to 367 in 2020. Asset licensing deals jumped from 360 to 593. In contrast, there was only one headline-grabbing mega-merger (an acquisition we define as $30 billion or more). This deal was significantly smaller than two mega-deals in 2019, both of which were for more than $60 billion.

However, there were more acquisitions under $30 billion in 2020 (121 acquisitions) versus 2019 (79 acquisitions). The total value of these was $66.8 billion (when controlling for mega-mergers), down from $70.8 billion in 2019 (Exhibit 2). This means either that deal valuations fell or the acquisitions made were on average smaller than prior years. Analyzing the deal data, we concluded that it was smaller deal size.

In the annual KPMG survey of executives across healthcare and life sciences, more than 80 percent of 31 biopharma executives surveyed said valuations had increased in 2020, and nearly a quarter estimated that values jumped by 20 percent or more (Exhibit 3).

Exhibit 2. Total deal value of full company acquisitions (excluding mega-mergers) remained in-line in 2020

Exhibit 3. Valuations increased significantly in 2020, according to biopharma executives


When we asked the executives what drove valuations in 2020, a large majority (61 percent) agreed that a primary driver was intense competition for high-value and innovative assets (Exhibit 4). This perspective from the pharmaceutical executives fits both our own advisory experience and our analysis of deal data, which shows growth in deals focused on innovation (e.g., cell and gene therapies). Across the biopharmaceutical industry, companies must sustain innovation or risk significant revenue cliffs as patent protections expire. This inherent characteristic of the industry means that this acceleration of the competition for innovative assets, particularly first-in-class or second-in-class assets, will remain a major driver of the deal market.

Exhibit 4. Intense competition for innovation had the highest impact on valuations in 2020

<table>
<thead>
<tr>
<th>Factor</th>
<th>Not a factor</th>
<th>Modest impact on valuation</th>
<th>High impact on valuation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Improved R&amp;D productivity through acquisition of external assets</td>
<td>35%</td>
<td>49%</td>
<td>16%</td>
</tr>
<tr>
<td>The financial impact of COVID-19 on acquisition targets</td>
<td>32%</td>
<td>49%</td>
<td>19%</td>
</tr>
<tr>
<td>The cost of capital</td>
<td>13%</td>
<td>35%</td>
<td>52%</td>
</tr>
<tr>
<td>Competition over a limited number of high value and/or highly innovative assets</td>
<td>3%</td>
<td>36%</td>
<td>61%</td>
</tr>
</tbody>
</table>

Source: KPMG, 2021 Healthcare and life sciences investment outlook

As noted, pharma acquirers are relying more on creative deal structures to mitigate the risk associated with the acquisition of clinical-stage assets. In 2020, biopharmaceutical companies frequently used deal structures that defer deployment of capital into the future.

Gilead invests $300 million in cancer drug maker Tizona

In July 2020, Gilead Sciences acquired a 49.9 percent stake in Tizona Therapeutics for $300 million. But the deal is potentially worth $1.55 billion if Gilead exercises its exclusive option for a full acquisition (upon Tizona’s meeting certain milestones for TTX-080, it’s first-in-class cancer medicine).

The Tizona cancer immunotherapy drug is investigational, and its efficacy and safety are unproven. But Gilead will fund Tizona’s R&D to accelerate development. Tizona expects to have sufficient data for Gilead to trigger its option for a full acquisition in the next two years.
Global R&D trends

Global deal trends mirror the trends in global R&D: The global pipeline is expanding rapidly in large-molecule and nucleic-acid-based therapeutics (Exhibit 5). Opportunities across these areas continue to grow, creating a fertile ground for creative deals targeting early-stage assets and technology platforms that are still pre-proof of concept.

Exhibit 5. Large-molecule and nucleic-acid-based therapeutics are driving worldwide pre-commercial biopharma pipeline

Note: Includes registered, pre-registration, Phase III, Phase II, Phase I, and Preclinical assets.
Over the past 10 years, growth across nucleic-acid-based therapeutics—e.g. RNA, oligonucleotide, and cell and gene therapies—has outpaced even the growth in large-molecule mABs. A vast number of small biotechnology companies that are pre-revenue are powering this trend (Exhibit 6).

**Exhibit 6. Small biotechnology companies are driving the cell and gene therapy pipeline**

Cell and gene therapy pipeline by company size (2020)

![Bar chart showing the distribution of cell and gene therapy pipeline by company size (2020).](image)

Source: BioMedTracker; KPMG analysis.

Deals in nucleic-acid technologies were an area of significant focus for the pharmaceutical industry in 2020 (Exhibit 7). The overall deal volume across cell and gene therapies rose to 141 from 83 in 2019, largely driven by a significant growth in asset licensing deals.

**Exhibit 7. Cell and gene therapy deals are growing rapidly**

![Bar chart showing the growth in cell and gene therapy deals from 2016 to 2020.](image)

KPMG believes biopharmaceutical companies in 2021 will continue to vigorously compete for the most promising new technologies, especially in oncology, immunology, neurology and infectious diseases. Indeed, in our survey of biopharma executives, 52 percent indicated they would increase the number of M&A transactions by 10 percent or more in 2021. As in 2020, they cite the limited number of high-value or innovative targets as the biggest driver for their M&A plans. More than 20 percent of executives also expect valuations to increase by 10 percent or more in 2021 compared with 2020.

We believe that companies will continue to focus on creative deals for early-stage pipeline assets in 2021 and beyond, as companies seek to mitigate the risk of investing in early-stage assets. According to our survey, pharma leaders expect the top three types of investment deals will be:

1. Early-stage, pre-revenue biotech acquisitions;
2. Strategic partnerships; and
3. Creative equity or financing deals with milestones.

As Exhibit 6 shows, many of these opportunities exist in next-generation cell and gene therapies, where a significant proportion of innovation is coming from small biotech companies that have lead assets in either pre-clinical or phase 1 stages of development.

Another common theme in 2021 will be more divestments of non-core pipeline or lower-performing commercial products by large pharmaceutical companies looking to improve their capital positions. This emerging trend was seen in 2020 and early 2021 in a few transactions, such as Merck’s decision to spin off its low growth assets to Organon; AstraZeneca’s divesting European rights to Crestor to Grünenthal for $320 million, with future milestone payments of up to $30 million. Larger companies will continue to assess the effects of the global economic downturn on non-core products and the implications for their aging assets.

Implications for 2021

Will there be a Biden effect?

Early signs from the Biden administration are pointing to a tougher regulatory stance on pharmaceutical deals. On March 16, the Federal Trade Commission launched a working group with competition authorities in Canada, the United Kingdom and the European Union to “update their approach” to pharmaceutical mergers. FTC Acting Chair Rebecca Kelly Slaughter explained that “given the high volume of pharmaceutical mergers in recent years, amid skyrocketing drug prices and ongoing concerns about anticompetitive conduct in the industry, it is imperative that we rethink our approach toward pharmaceutical merger review.” Her words could lead to a pullback in large acquisitions in the coming months—although companies will await the FTC’s evidence for any anti-competitive behaviors in the industry.

Looking at the data on recent pharmaceutical deals, the initial view of KPMG is that the vast majority of them are focused on acquiring new capabilities and enabling innovation rather than impacting drug pricing. But this trend could be a factor in driving drug prices higher, because the industry is moving away from medicine for large populations in favor of smaller-population, specialty areas like cancer and other rare diseases. For pharmaceutical companies to pursue the development of these lifesaving, small-population therapies, they have to price drugs at high prices given the massive investment required in innovative R&D, new manufacturing capacity and supply-chain requirements. So policy makers will need to balance the goal of checking drug price rises for consumers with their interest in encouraging the pharmaceutical industry to keep developing innovative drugs.

Conclusion: Position to win

The competition for innovation pushes biopharmaceutical companies to pursue earlier-stage pipeline assets in order to tap into innovative options. The risks they face are compounded by the fact that these early-stage assets have lower probabilities of success, and many of the different emerging technologies are competing with each other for the same future commercial opportunities.

Predicting which technology will succeed or displace other emerging innovations is a gamble—the range of disruptive technologies in the global pharmaceutical pipeline is too diverse and it’s too early to know which will succeed. This is driving many savvy pharmaceutical and biotech companies to spread their bets and invest across multiple modalities.

We also expect more deals using creative structures focused on milestone-based investments in clinical-stage assets and increasingly, on pre-clinical-stage ones. The fight for innovation is now a battle for rights to own a wider range of platforms and individual assets that are early in development.

Against this backdrop, here are the key takeaways for biopharmaceutical companies for deal making in 2021:

- **Adopt a diversified strategy focused on a wide range of technology types:** There is too much uncertainty about which modalities will be most successful, even as competition is driving the deal market to earlier-stage investments. To improve the likelihood of building a robust late-stage pipeline and future revenues, focus on deal strategies that de-risk investments with lower upfront payments and allow the company to make more, smaller bets.

- **Consider the possibility that another earlier-stage technology will win:** For a given disease, only one or two highly effective therapies under development in the global pharmaceutical pipeline may be commercially successful. Buyer beware.

- **Align the integration strategy with your growth strategy:** Integration has proven to be one of greatest challenges, especially for acquisitions of nucleic-acid technology assets. The wrong integration strategy can undo an expensive acquisition by losing the core technical talent necessary to realize the full value of the deal.

- **Be on the lookout for increased divestitures in 2021:** Larger pharmaceutical and biotech companies will seek to optimize their portfolios and may jettison non-core pipeline assets and aging products in non-core markets. In 2021, these divestitures may provide opportunities for creative private-equity firms and mid-market pharmaceutical companies.
How KPMG can help

The KPMG Healthcare and Life Sciences Strategy practice specializes in advising corporate, private-equity, and public organizations across all phases of the M&A lifecycle from deal strategy to diligence to post-close value creation. Our integrated, multidisciplinary approach provides clients with critical insights into value opportunities—and obstacles to value—at deal speed. Further, KPMG has a proprietary set of tools and methodologies to deliver data-driven insights. We understand the regulatory, commercial, operational, and accounting complexities unique to the industry and provide a client-centric, integrated suite of services across the deal lifecycle to assist our clients in achieving business results.

Above all, we are former scientists and business professionals trained as strategy consultants, with deep expertise in clinical and therapeutic areas and extensive experience translating strategy into actionable plans.

Our healthcare and life sciences M&A teams have a long history of enabling mergers, acquisitions, affiliations, JVs, and partnerships for pharmaceutical clients

Where is the growth opportunity and who to target?
— KPMG has a dedicated life science team for assessing the landscape of emerging technologies and companies in order to prioritize a short list of company and/or asset targets for business development.

What’s the investment thesis and target valuation?
— KPMG has specialized teams who can build the forecast models, valuations and the overall strategic point of view to justify future transactions.

To what degree are the financial, commercial and operational assumptions supporting the investment rationale?
— KPMG has life sciences specialists highly experienced in providing the full range of due diligence services: Financial Due Diligence, Commercial Due Diligence, Operational Due Diligence, Tax Due Diligence and HR Due Diligence.

How to integrate?
— KPMG has specialized teams dedicated to helping pharmaceutical companies develop their integration strategies and then operationalize the integration across all back-office and front-office functions.

How to optimize value creation opportunities for the portfolio?
— KPMG has strategists to help clients run sophisticated analyses to identify the optimal capital creation options to ensure that the financial and strategic goals of the core portfolio are set for growth and sustainability.
— Once the divestment options are identified, KPMG has specialized teams to support the operational separation of the entities across all major functions.
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