Evaluate Vantage

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For Gilead Kite is no Pharmasset

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Comparisons are odious, and among the many things that can be said about Kite Pharma, bought by Gilead for $11.9bn yesterday, one thing is certain: it's no Pharmasset.

Notwithstanding superficial similarities between these two Gilead acquisitions, investors desperate for the company to put its cash to use must bear in mind that buying Kite will not be plain sailing. But, despite the many caveats, if only some of Kite's assets pan out the deal will be a resounding success, and its price tag could be seen as a bargain.

In this sense the takeover is a gutsy move to seize a dominant position in a new and untested market – cell therapy. In the best tradition of biotech it has a strong binary outcome nature: it will either be a masterstroke or it will crash and burn.

Not so similar

Gilead had bought Pharmasset for an amount similar to what it has paid for Kite, after a period in which the target's stock price had surged. It will not go unnoticed that Kite's shares had climbed 90% in the past three months leading up to Gilead's takeout, which factored in an additional 29% premium.

But Pharmasset was a bet on a single product – Sovaldi – in a field with which Gilead was familiar. For an HIV-focused company to get into hepatitis C was a no-brainer, and Sovaldi could be plugged straight into existing operations. Kite is an entirely different animal: not only is Gilead's oncology presence superficial, its cell therapy expertise is non-existent.

Moreover, Pharmasset was a success largely because the planned cost of Sovaldi had been deemed too cheap; Gilead launching it at a much higher price transformed the deal's economics. Conversely, it is hard to see much of an advance on the dizzyingly high assumed price of CAR-T therapy, which might cost over $500,000 per patient.

The non-profit non-government organisation Knowledge Ecology International has already released a statement urging Kite's CAR-T therapies to be made available "on reasonable terms", though if anyone can weather a drug price controversy it is probably Gilead.

And investors will take heart that among Gilead's decidedly patchy M&A record it is the biggest deal that has been a resounding success (*Buying growth is a tricky choice for Gilead, February 8, 2017*).

Still, the risks are obvious. Since CAR-T is anything but a plug-and-play addition to Gilead's pipeline the acquirer will have to count on retaining key Kite employees. No one knows how CAR-T will play out in the market, whether unexpected toxicity issues pop up, and whether manufacturing can be scaled and made more reliable.

Efficacy is clearly excellent in haematological cancers, but Gilead is making a big bet on cell therapy's applicability further afield, particularly in solid tumours. Adverse events in areas where efficacy is lower could be problematic.

There was caution from the sellside yesterday. Stifel said few companies could buy a business as complex as Kite and not ruin it, and called Gilead a small-molecule company that does not currently commercialise antibody therapeutics.

Evercore ISI opined that four key points would determine the quality of the takeover: whether Kite's T-cell receptor projects work in solid tumours, whether side-effect management prevents deaths, whether Kite's allogeneic approach could leapfrog more advanced rivals, and whether Juno's '190 patent, upheld at interpartes review, could constrain Kite.

Rising tide

Either way yesterday's Gilead tide lifted all cell therapy boats. The struggling Juno and Bellicum climbed 19% and 14% respectively, the allogeneic player Cellectis was up 17%, and even the T-cell receptor-focused group

Adaptimmune rose 15%.

The inference is not only that Gilead has given all cell therapies a major endorsement, but also that some of these rival groups could attract buyers. Who could now be pressured to act? Most obviously Celgene, which already has CAR-T licensing deals in place with Juno and Bluebird.

And while Gilead's move clearly is not cheap – Kite has run up an accumulated deficit of under $500m since inception – cell therapy has simply become too important an area for the group not to be in.

"Our oncology efforts have been fairly nascent, and we have had few real successes," Gilead's chief executive, John Milligan, admitted on a call yesterday. "[Kite] is a pivot to cellular therapy as our main strategy."

For a company that had recently become better known for share buybacks than deal-making this is a bold move. Perhaps the biggest risk would have been for Gilead not to have a piece of the action.

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