Evaluate Vantage

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Big caps provide a safe haven

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As the curtain came down on a quarter many in biotech would rather forget, big pharma groups stood out by being the least bad investment option.

In September biotech was heading for a safe, albeit unspectacular, 2018. But then the fourth quarter happened.

As broader indices fell it was high-risk stocks like biotech that took a disproportionate hit, which amounted to some 17% of lost value over the three-month period. This has clearly made some companies affordable, as yesterday’s move by Bristol-Myers Squibb on Celgene showed, but it will not go unnoticed that this tie-up involved two of 2018’s worst performing stocks.

Across the sector a 15% nine-month climb for the Nasdaq biotech index turned into a 9% year-end decline, and Japan also had a horrific fourth quarter. Big pharma thus resumed its traditional role as provider of a safe haven of sorts.

Of course, everything is relative. The anaemic 5% full-year increase in the S&P Pharmaceuticals index, for instance, only looks impressive because all the other key biopharma indices ended 2018 either flat or in the red.

Stock index	12-mth % change
Nasdaq Biotechnology (US)	-9%
S&P Pharmaceuticals (US)	5%
Dow Jones Pharma and Biotech (US)	0%
S&P 500 (US)	-6%
DJIA (US)	-6%
Dow Jones Stoxx 600 Healthcare (EU)	-3%
Thomson Reuters Europe Healthcare (EU)	-5%
Euro Stoxx 50 (EU)	-15%
FTSE-100 (UK)	-13%
Topix Pharmaceutical Index (Japan)	-7%

And, while investors clearly fled from risk, macroeconomic issues were also behind the FTSE-100 and Euro Stoxx 50's double-digit falls. The Japan index had stood up 17% at the end of September, but this proved to be the peak that launched an 18% crash in the fourth quarter.

If any single company was to blame for this it was Takeda, one of that index's biggest constituents. Takeda's disastrous $64bn takeover of Shire resulted in the Japanese group being crowned the biggest value destroyer of the big caps outside big pharma, sitting on a 42% year-end share price fall.

The other end of the $20bn of value that Takeda lost is a gain of just $6bn for Shire, so clearly the Japanese group is suffering a broader crisis of confidence. Its poor performance was only marginally worse than that of Bayer, which is also being punished heavily for an unpopular acquisition, that of Monsanto.

Celgene, once seen as one of the smartest big biotech deal-makers, stood as a sorry laggard, a fact that goes a long way to explaining why it was yesterday bought by Bristol for $74bn, a price reflecting a 35% decline from its peak (*Bristol-Myers Squelgene makes its pre-JP Morgan splash, January 3, 2019*).

Big drugmakers ($25bn+) excluding big pharma: top risers and fallers in 2018			
		Market capitalisation ($bn)	
	12-mth change	**31 Dec**	**12-mth change**
Top 3 risers			
CSL (AUD)	31%	59.6	9.9
Shire ($)	12%	122.2	5.8
Amgen ($)	12%	53.3	(1.5)
Top 3 fallers			
Takeda (¥)	(42%)	41.3	(19.8)
Bayer (€)	(42%)	65.1	(42.3)
Celgene ($)	(39%)	53.3	5.8

The weighty fallers shielded the poor performances of Celgene peers like Gilead, off 13% for the year, and Novo Nordisk, down 11%. Amgen found itself in the top gainers club only thanks to a $10bn share buyback; its market cap actually shrank 1% over 2018.

So what about those big pharma safe havens? Once deeply unexciting companies like Lilly and Pfizer now stand as shining beacons among the sector's most rewarding investments. Even Glaxosmithkline ended the year up 13% as its recent corporate rejig showed that the group really did want to be a pharma company, and helped counteract its unpopular acquisition of Tesaro.

Big pharma: top risers and fallers in 2018			
		Market capitalisation ($bn)	
	12-mth change	31 Dec	12-mth change
Top 3 risers			
Lilly ($)	37%	122.6	29.7
Merck & Co ($)	36%	198.7	47.0
Pfizer ($)	21%	252.3	35.8
Top 3 fallers			
Bristol-Myers Squibb ($)	(15%)	84.8	(14.1)
Johnson & Johnson ($)	(8%)	346.1	(28.7)
Roche (SFr)	(1%)	210.6	(4.7)

The share price of Merck & Co, meanwhile, continues to reflect that company's growing domination of lung cancer treatment with immuno-oncology – at the expense of Bristol-Myers Squibb and Roche. The former has now been forced into a megamerger, but the latter's fall is surprising given its huge new growth drivers Ocrevus and Hemlibra.

Johnson & Johnson's 8% fall was due to a disastrous final quarter, in which a Reuters report accused the group's consumer division of concealing the presence of asbestos in baby powder.

With more winners than losers in J&J's cohort the key question going into 2019 – apart from who will be the next Bristol and Celgene – is how much longer drug price increases can be relied on to boost the performance of the biggest pharma players.