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Bayer exits chemicals and goes for growth

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In spinning off its chemicals business, Bayer has taken a step away from its long-cherished strategy of diversification. A glance at *EvaluatePharma*'s data on the top 10 big pharma companies instantly explains the decision: the company's drug sales are forecast to grow faster than those of all but one of its peer group (see table below).

The MaterialScience unit is not going to grow at anything like the 5% annual rate Bayer's prescription and over-the-counter drugs are set to enjoy. It is clear that the unit has been dragging the company's share price down, and investors responded to news of the spinout by sending the stock up 6% to €112.20 ($144.93) today.

Sluggish

After the planned flotation of MaterialScience in the next 12 to 18 months Bayer will be left with drug, consumer health and agribusiness units, which in 2013 made up roughly 36%, 19% and 25% of its total group sales. It also has a tiny medtech segment, accounting for around 4% of sales.

The chemicals unit currently accounts for 28% of the Leverkusen group's revenue with 2013 sales of €11.2bn, but its growth is projected to be relatively sluggish, at just 3% annually from 2013 to 2020.

It has been apparent for some time that the drugs unit is where the action is. Driven in large part by blockbusters such as Xarelto and Eylea, the group's growth rate from 2013 to 2020 outstrips all of the top 10 companies except Novo Nordisk.

Interestingly from a strategic point of view, the other top 10 pharma company whose prescription and over-the-counter sales have a growth rate close to Bayer's is also a conglomerate: Johnson & Johnson. That said, having a diversified offering is not a golden ticket: the drugs arm of Merck KGaA, which gets most of its profits from liquid crystals, is forecast to shrink at -0.4% annually to 2020, *EvaluatePharma* data show.

Top 10 companies by 2020 prescription and OTC sales

	Sales ($bn)			Market Rank	
Company	**2013**	**2020**	**CAGR**	**2013**	**2020**
Novartis	49.1	62.0	+3%	1	1
Sanofi	41.7	55.6	+4%	3	2
Roche	39.1	49.4	+3%	4	3
Pfizer	47.1	49.0	+1%	2	4
GlaxoSmithKline	36.1	42.6	+2%	6	5
Johnson & Johnson	29.1	41.0	+5%	7	6
Merck & Co	38.0	40.9	+1%	5	7
Bayer	*19.4*	*27.4*	*+5%*	*10*	*8*
AstraZeneca	24.5	27.2	+2%	8	9
Novo Nordisk	14.9	25.4	+8%	15	10

An IPO of MaterialScience could raise around $10bn, UBS analysts say, which the company could use to retire debt – Bayer currently has $18bn of debt on the books – or to make an acquisition in animal health. Pfizer's former unit Zoetis could be a target, for instance.

The company itself says it can no longer find sufficient development capital for MaterialScience “due to the substantial investment needs of the Life Science businesses”. After it is spun out, the polymer specialist will be Europe's fourth-largest chemicals company, Bayer said. MaterialScience was what was left after Bayer sloughed off some of its chemicals via the 2004 spin-out of its Lanxess subsidiary.

The group had telegraphed the growing importance of its drug businesses with the acquisition of Merck & Co’s over-the-counter products in May. This deal is expected to close by the year end.

The recent trend towards streamlining and purification among large diverse companies is unmistakable. Bayer celebrated its 150th anniversary last year, and J&J has been around for nearly 130 years. J&J's other units are also growing more slowly than its drugs – the overall company has a projected annual growth rate of just 3%. The age of the healthcare conglomerate has not passed yet, but this is starting to look like the beginning of its end.

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