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Bankers must bet Bayer cannot do more with less

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A 100% life sciences-focused Bayer will need all the help it can get if it is to maintain a claim to having one of the world's fastest-growing pharma businesses. So the amount it spends on R&D – currently under 16% of pharma sales – might come as a surprise.

The group's chief executive, Marijn Dekkers, admits that this is near the low end of the scale for the peer group, as *EvaluatePharma* data bear out (see table below). After the disposal of material science and plastics this year, how and where the group allocates cash will be a key focus for bankers pitching M&A transactions.

What will not be music to their ears, however, is Mr Dekkers' repeated stressing of Bayer's internal prospects at yesterday's 2014 financials conference. "Being on the low end of [the R&D scale] didn't hurt us with 11% organic growth last year," he stated. "We are one of the fastest-growing pharma companies in the world."

Sales of the group's top five prescription drugs rose 19% to €2.9bn ($3.2bn), and Bayer expects them to total €4.0bn in 2015 and €7.5bn at peak. But reported pharma R&D spending of €1.9bn in 2014 amounted to 15.6% of sales, which was broadly in line with the 15.8% of pharma revenues reinvested in R&D the previous year, and below the average of Bayer's competitors.

R&D budgets at selected pharma groups		
Company	**R&D as % of 2013 pharma sales**	**2013 pharma R&D spend (USbn)**
Eli Lilly	25.4%	5.3
Bristol-Myers Squibb	22.7%	3.7
Roche	21.2%	8.3
Johnson & Johnson	20.7%	5.8
Novartis	20.5%	9.3
Merck & Co	19.0%	7.1
AstraZeneca	16.6%	4.3
Bayer	15.8%	2.0
GlaxoSmithKline	15.1%	5.0
AbbVie	15.1%	2.8
Sanofi	14.9%	6.1
Pfizer	13.7%	6.6
NB segment calculations computed by EvaluatePharma		

A related consideration is how the group might use any proceeds from the planned spin-out or flotation of its material science division in the second half of this year.

Bankers will undoubtedly hope that M&A is on the cards, though Bayer's net debt pile, which nearly tripled last year to €19.6bn, might first need to come down. Nevertheless, "everything can be financed these days", said Bayer's recently appointed finance chief, Johannes Dietsch, no doubt referring to historically low interest rates.

"There are excellent opportunities in the capital markets for borrowing. Should there be an overwhelmingly interesting acquisition opportunity we'll find a way of financing it."

Asset prices

One problem for a historically conservative group like Bayer is the sky-high prices of biotech assets, as evidenced by Bristol-Myers Squibb's recent $800m acquisition of a preclinical project from Flexus Biosciences (*Flexus shows other immuno-oncology wannabes how it's done, February 24, 2015*).

This was a point readily acknowledged by Kemal Malik, Bayer's head of innovation. But talking to *EP Vantage* he too stressed Bayer's internal capabilities; some of these efforts are collaborative, such as a BiTE antibody deal with Amgen, while others are so early that they necessarily operate behind a cloak of secrecy.

In this context it will not pass unnoticed that there are clear crossover opportunities between healthcare and Bayer's other major remaining unit, crop science. This has large areas of "commonality" with pharma, said Mr Malik, not only in terms of scale but also in the underlying science, especially in genetics.

He revealed, for instance, that through a separate alliance Bayer's crop business is working on CRISPR/Cas, presently one of the hottest gene editing technologies (*CRISPR steps closer to centre stage as AstraZeneca piles in, January 29, 2015*).

And while Bayer's cancer immunotherapy work is still very early it presents the possibility of using existing gene editing capabilities, as the French CAR-T company Cellectis (once a crop protection player) has shown with its use of TALENs and meganucleases.

It was thus noteworthy that Mr Dekkers yesterday categorically ruled out a future spin-out of Bayer CropScience. Other rumoured areas of interest for investment bankers include a trade sale of its diabetes-monitoring systems or an acquisition of the animal health business Zoetis, though on these the group is making no comment.

Buying in growth could to some extent compensate a company's status as an R&D laggard, though Mr Dekkers said the 16% percentage would likely go up in the coming years. In any case you cannot just look at the percentage of sales spent, he noted. "You also have to be good at R&D to get your money back."

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