Vantage point – What Brexit means for life science funding and strategy

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It would be hard to overstate the importance of EU money to the UK life science sector. Support for drug and medical device developers flows across the English Channel via many streams, including grant money, academic collaborations and the European Investment Fund, which among other activities backs commercial venture firms.

Many fear the loss of access to these huge pools of capital, as well as restrictions on the movement of highly trained labour, and rightly so. If Britain becomes a less attractive place to do business the long-term implications are clear. In the short term, many are calling on the government to signal its support with new tangible measures before Brexit negotiations begin in earnest, to help companies make crucial plans for a future as non-EU citizens.

The government has already offered some reassurance. For example the Treasury has committed to underwriting bids to the EU’s Horizon 2020 programme, an €80bn pot for science and innovation, even when projects continue beyond Brexit.

Brexit looks likely to happen in 2019, given Prime Minister Theresa May’s pledge to trigger Article 50, allowing two years of negotiations to begin, by March next year.

Still, some want the government to make much bigger gestures, such as commitments in cash terms to scientific research in the longer term, and pledges to beef up existing mechanisms to make the UK an attractive place for life science companies to locate.

Steve Bates, chief executive of the Bioindustry Association, says more money for the biomedical catalyst would be top of his hit list. This publicly funded programme backs fledgling commercial ventures arising from academia or industry, and the BIA has long called for assurance of sizeable annual top-ups.

Other areas the government could address in the near term include the range and scope of R&D tax credits, the patent box and entrepreneurs’ relief. The patent box cuts corporation taxes for income based on intellectual property, while entrepreneurs’ relief cuts capital gains taxes for the owners of small companies that are sold.

“There are lots of things available for the government to do prior to Brexit. The autumn statement in November and budget early next year will both precede anything substantial on the negotiations, and provide early opportunities to show their support,” he says.

The government could also do more to bolster the NHS, the increased funding of which was one of the key promises of the Brexit campaign. Already the largest buyer of medical technologies in the UK, the NHS could become a more important customer for UK companies if, as seems likely, Brexit makes it tougher for them to sell into the rest of the continent.

“It’s always been difficult for companies to get investment capital if their case is based largely on sales to the NHS,” says Richard Devereaux-Phillips, of medtech industry group the Association of British Healthcare Industries. “If a large part of their business plan is dependent on export and that becomes more difficult, and at the same time the local market is not particularly receptive to innovation and new technology, that’s a problem.”

Matthew Godfrey-Faussett, of the law firm Pinsent Masons, agrees: “If the NHS has less cash to spend or is forced to reorganise, that creates uncertainty in our home market and that will certainly have an impact on the medtech sector.”

Short-term pain

For some in the academic world the impact of Brexit is already being felt.
“We’re already seeing an impact on R&D at some of the universities,” says Ramesh Jassal, international head of healthcare at corporate finance house Clearwater International. “There is a lack of funding coming through – will they get any further grants and funds from the EU?”

Additionally, researchers are being asked not to be part of any framework arrangements, according to Raj Mehta, business development executive at Cancer Research Technology.

“Most EU funds come as part of consortium funding. Essentially, what UK scientists will not be able to do is be part of those big consortiums. So there’s the money itself, but also the issue of being part of large collaborations,” he says.

Collaborations between universities and the corporate world could also come under threat, as many receive EU backing. For example a £50m partnership arranged in January between Albion Ventures and UCL obtained half of its funding from the European Investment Fund.

Among its activities the EIF injects huge amounts of cash into European venture capital firms in return for a pledge to invest a certain proportion of their funds in European start-ups. In a statement issued after the Brexit vote, the EIF suggested that its activity in the UK might change, and while this is far from a definite decision to abandon UK companies, it adds to the uncertainty.

According to figures provided by the EIF, in 2015 alone it invested €656m in the UK via equity participations – which includes venture funds. Not all of this would have gone to life sciences but it is easy to imagine the crucial support this provides to corporate investors. Indeed one of the calls from the sector is for the government to set up an EIF equivalent, post Brexit.

Financial adjustment

It is easy to imagine how a drop in funding for universities and the end of EU grants could have a long term impact on start-ups – a good portion of medtech and biotech companies start as university spin-outs.

But start-ups also want to maximise their chances of obtaining qualified staff, limit the strain of regulation and ensure straightforward, robust intellectual property protection.

“We will see business looking elsewhere for potential locations, because you’ve got a larger market guaranteed if you are within the EU than if you are seeking to negotiate a trading position with the EU,” Mr Godfrey-Faussett says. “There may have been a preference for the UK – that will now need to be reconsidered.”

This is a relevant consideration for established businesses as well.

“From our side, the UK will continue being an important country, but we will have to adjust financially how we do business in the UK,” says Manuel Ortega, senior vice-president at the German cardiology device company Biotronik.

In geographic terms, one beneficiary of Brexit is likely to be Ireland. Already an attractive location thanks to its low rate of corporate tax, as of early 2019 the country will be the only EU member state whose first language is English.

“It’s becoming a bit of a medical device cluster there,” says Mr Jassal. “[The UK] could be second to that if we do go down the route of becoming completely independent.”

After the Brexit referendum in June IDA Ireland, the investment agency of the Irish Government, wasted no time in noting that the situation could present an opportunity for the country to attract foreign investment.

The UK has generally been thought of as the first entry point to Europe from the US, Mr Devereaux-Phillips says. This advantage could now be lost.

Pulling the levers

There are signs that some groups are already delaying strategic decisions until the effects of Brexit become clear. However in terms of business activity many are surprised at how little impact the vote to leave has had.

After an initial pause on a collective sharp intake of breath, deal-making has continued apace, and stock markets have largely recovered. “Commercially I haven’t seen any difference, either investment-wise or in deal-making,” CRT’s Mr Mehta says.

As details of the negotiations emerge over the next two years few expect this to remain the case.

“Particularly if the UK heads for a “hard Brexit”, the UK will be a less attractive venue for investment by pharma. It’s one of the sad side effects of all this,” says Grant Castle, a lawyer for Covington & Burling.

Although the government has levers within its reach to help maintain a favourable investment climate, having
apparently committed to leaving the single market it is hard to see how issues like freedom of movement of labour can be addressed to the sector’s satisfaction. UK life sciences is a sector heavily reliant on talented immigrants.

Whatever Brexit route is taken, Britain will still have a life science sector worth £60bn that employs 220,000, which is clearly in the government’s interest to protect and propagate. It is easy to see how the industry could form a key plank of any new industrial strategy, particularly considering the UK’s strong scientific heritage and world reputation.

To make this possible the government needs to negotiate a future where life science companies find that the drawbacks of being outside the EU are easily outweighed by the incentives on offer to locating within the UK. Given the scope that Brexit presents to shape policy and make funding pledges, this is not impossible.

But it will take bold steps and big pledges, in cash terms at the very least.

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