Corporate Strategy: Katherine Smith

How European MidPharmas have grown profits

Europe is home to 85 mid-sized pharmaceutical companies (MidPharmas) that invest in developing and commercialising pharmaceutical products. Many of these companies have achieved impressive, upward-trending earnings before interest and tax (EBIT) margins in the last five years. The median EBIT margin of MidPharma is now comparable to that of the largest pharma companies and many MidPharmas now outperform their larger rivals on measures of both profitability and revenue growth. The reason is straightforward: the mid-sized companies have a strong strategic focus.

The top-performing companies in this group choose to focus on product innovation, the examples being Genmab A/S of Denmark, PharmaMar SA of Spain, and Pharming Group NV of the Netherlands. Or they focus on commercial innovation such as Recordati SpA of Italy, Swedish Orphan Biovitrum AB (Sobi) of Sweden and Orion Corp of Finland. The product innovators take risks on promising, but unproven technologies, while the commercial innovators operate further along the value chain.

Genmab and Pharming both have their roots in cutting-edge technology platforms. In each case, the lead asset led to a therapeutic identity for the company that laid the foundation for a portfolio, investors, and pharmaceutical partners. In the case of Genmab, the platform generated daratumumab, one of the earliest monoclonal antibody therapies. The drug paved the way for a significant group of antibody therapeutics for oncology indications and in 2020 contributed to the company's EBIT margin of 62%. Similarly, Pharming's recombinant protein platform, accompanied by expertise in a specific biological pathway, the complement cascade, helped the company focus on a subset of rare diseases, resulting in an EBIT margin of 36% in 2020.

Original technology, coupled with a strong focus, helped these biotechs attract partners and investors and generated substantial cash flow in their formative years. US backers now account for 40% of Genmab's investors and large pharma companies such as Janssen Biotech Inc, AbbVie Inc and Roche have contributed significant revenue in the form of royalties and milestone payments.

Similarly, PharmaMar has a strong focus, but in this case on drug discovery. The Spanish company is exploring the anti-cancer mechanisms of marine invertebrates. The company maintained an impressive EBIT margin of 61% in 2020 despite spending 21% of revenue on research and development. This was partly due to keeping a lean commercial footprint. PharmaMar commercialises its three approved medicines in eight European countries with a 100-person team. It has also out-licensed the medicines to 17 local champions with specific market knowledge and resources to maximize their impact in 50 other countries, including the US. In addition, PharmaMar is continually looking to in-license late-stage assets that complement its existing commercial and R&D infrastructure. Partnerships are a lower risk and lower cost alternative to full vertical integration and give biotechs a foundation for future growth.

Pharming's strategy is to grow and stay profitable by increasing sales of its lead product Ruconest, use its technology platform to develop new recombinant proteins, and in-license or acquire new assets. Ruconest accounts for 96% of the company's revenue and is now commercialised in-house in the US, UK, and the EU. In 2021, the company renewed a manufacturing partnership with Sanofi SA instead of spending money on a new production facility.

Commercial innovators Recordati, Sobi and Orion achieve profitability by a different route. Investment in R&D is kept relatively low – typically around 10% of revenue – and marketed or late-stage assets are acquired or in-licensed. Investment instead is directed towards growing a commercial presence and infrastructure. In 2019, Sobi acquired Dova Pharmaceuticals Inc for €814 million to flesh out its haematology portfolio and breathe new life into Doptelet, a product for severe thrombocytopenia. Sales of this product subsequently grew by 104% in 2021. Following the acquisition, Sobi doubled the size of its haematology sales force. This franchise accounted for 77% of operating profit in 2020 and 82% in 2021.

Recordati's cash flow is mostly reinvested in international expansion through mergers and acquisitions. To date, most acquisitions have been less than €100 million to ensure successful integration. By product area, it has invested in rare diseases to complement its strength in specialty medicines and primary care. Since CVC Capital Partners acquired a controlling stake in the company in 2018, Recordati has made more substantial acquisitions to support its rare disease portfolio. Hedging its risk in this way between its existing primary and specialty care segment and its new rare disease medicines helped the company sustain strong EBIT margins at 32% in 2020.

Orion maintained a 26% EBIT margin in 2020 despite the impact on sales of generic competition and spending on Nubeqa, a treatment for prostate cancer. Orion avoided heavy development costs for Nubeqa by signing an agreement with Bayer AG which fronted most of the development expense in return for access to Orion's manufacturing capacity and co-promotion rights in Europe. Orion plans to focus on in-licensing and M&A to reinforce its proprietary and generics portfolios, while continuing to expand geographically.

The profitability of these six MidPharma companies shows that scale is far from a disadvantage. Their clear focus enables them to evolve effective operating models. For the product innovators, this means embracing risk and investing in R&D. For the commercial innovators, it means securing a return from diverse portfolios across many geographies.

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