



GETTY/ALEXIS RENDEL/GARETH J. BURGESS

# A fine question

Fine chemical players must consider pharmaceutical and biotech customer concerns before doing a deal

## INVESTMENT BANKER PERSPECTIVE

CHRIS CERIMELE  
LINCOLN INTERNATIONAL

WHAT ARE some of the common concerns among outsourcers of fine chemicals, and how does merger and acquisition (M&A) activity relate to those issues?

To address this question, it's helpful to understand the key concerns that a pharmaceutical or biotech firm – as a customer – would have concerning M&A activity among the fine chemical players as outsourcing partners. A review of transaction dynamics will then help shed light on some of the trends.

According to *Contract Pharma's* 2006 Annual Outsourcing Survey, the top five factors that contribute to the outsourcing decision among pharmaceutical and biotech firms,

together, known as pharma-tech, include quality, timeliness, confidentiality, good manufacturing practice capability and relationship.

These five factors all ranked ahead of cost. More importantly, each of these factors, including cost, can change dramatically following a change in ownership.

Adding to the risk for pharma-tech companies is the fact that, in many cases, there are few alternative supply sources. Many try to maintain at least two separate suppliers.

However, if there are unique technologies involved, there may be only one or two firms globally that can manufacture a particular intermediate or active pharmaceutical ingredient (API). Even when alternatives exist, switching can be difficult because of the requirements of technology transfer, validation, and regulatory approval.

In light of these concerns, it is no wonder that pharma-tech firms have a keen interest in the impact M&A could have on the stabil-

ity of its critical fine chemical supplier base.

We have often found that the largest concerns revolve around successor ownership. The key question is: "Who will buy the business and what will a new owner do that could alter or disrupt my source of supply?"

### M&A TRENDS

If ownership changes are of significant concern, then who are the buyers of fine chemical businesses and how are they different?

Since early 2005, the M&A market has been dominated by three types of buyers: Western fine chemical companies, midmarket private equity firms and increasingly, Indian fine chemical producers. Each has its own unique dynamics:

- In the past five years, Western firms have been under increasing price pressure from lower-cost Asian manufacturers, and many have chosen consolidation as a way to remain competitive. Acquisitions have been highly strategic, focused on adding specific technologies or establishing a new geographic presence. Fewer players could mean fewer alternatives for pharma-tech customers, and there are inherent risks if manufacturing is moved or consolidated.

- Since 2005, private equity firms have been increasingly active buyers. But their ability to compete effectively may be hampered, given the recent pressure in the US credit markets.

- Indian firms have emerged as a competitive force in the past several years. These companies are offering increasingly higher quality, sophisticated fine chemicals at a lower cost, and are continuously seeking acquisitions as a way to fuel growth.

Any fine chemical company considering M&A should be sensitive to customer concerns before starting a process. Likewise, having a grasp of current trends can help a pharma-tech company effectively evaluate the risk of their supply base. ■



» Chris Cerimele is a senior vice president in the global chemicals M&A practice of Lincoln International, where he advises clients on midmarket mergers, acquisitions and corporate divestitures



Listen to Chris Cerimele present his views on M&A at this event on October 24–25 at the Hyatt Regency in New Brunswick, New Jersey, US. For more information and to register online, go to [www.dcat.org](http://www.dcat.org)