



VENUE® Market Spotlight

PHARMA M&A

July 2015 Edition

RR DONNELLEY



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WELCOME

Dear Valued Reader,

Welcome to the July 2015 edition of the *Venue Market Spotlight*. This month, we are putting deal-making within the pharmaceuticals sector under the microscope.

The industry for producing, researching and marketing medicine is one of the biggest markets in existence. According to the IMS Institute for Healthcare Informatics, the global market for pharmaceuticals is expected to hit US\$1.1tn in 2015, with signs that this can only increase as developing economies continue to increase their demand. Indeed, according to Business Monitor International, sales of medicine in China are expected to reach US\$175.8bn in 2020, compared with just US\$66.9bn in 2011.

On top of this, rapid developments in the biopharmaceutical sphere are creating new opportunities within the wider pharmaceutical space. According to McKinsey & Company, the market already makes up around 20% of revenues of the global pharmaceutical market, and major pharmaceutical companies are refocusing more of their research and development (R&D) into this space.

However, challenges are apparent. Increasingly tough regulations, especially in the US, are challenging drug manufacturers. Expiration of patents is also an issue - according to FiercePharma, US\$44bn-worth of patents are set to expire this year, the highest figure since 2012. Moreover, R&D is becoming increasingly costly for companies to do themselves. According to research from the Tufts Center for the Study of Drug Development, the cost of R&D for a new drug was 30% higher in 2013 than it was in 2003.

With these challenges and opportunities in mind, respondents to this month's *Spotlight* are unanimous in expecting pharma M&A to increase. Whether to grow in new markets or consolidate offerings, the case for growing deal activity in the sector seems quite clear.

Best Regards,



Tom Juhase
President, Financial Services Group
RR Donnelley

FOREWORD

Last year, pharmaceutical companies completed more deals and spent more money on M&A than in any year prior and as we enter the second half of 2015, this activity is not expected to slow down any time soon. In H1 2015, US\$211.7bn had been spent on pharma deals, compared with US\$205.4bn in H1 2014.

The pharmaceutical industry executives surveyed are unanimous that this record pace of deal-making will continue. Of those, 36% believe that the expected boost in M&A will be significant. Following a half-year period that has already yielded six deals worth over US\$10bn each – one of them worth US\$35bn alone – it is not hard to see why.

From blue-chip giants to new startups, doing a deal is becoming an increasingly attractive option. For established players, a high-profile mega-merger could consolidate costs as well as bring in new specialties, while picking up cheaper, newer companies is providing many with a clear method for gaining new research and development (R&D) capabilities. For smaller firms, an acquisition could provide a way for these companies to keep their heads above water amidst a hyper-competitive environment. As one of our respondents says, in the industry today, “it’s either buy or be bought.”

Other key findings include:

- Cardiovascular is expected to be the therapeutic area most sought after by acquisitive companies, chosen by 36% of respondents. An additional 21% chose cancer as their top choice.
- Asia-Pacific was chosen by 36% of respondents as the region that will see the largest increase in pharma M&A this year, as industry players look to tap a potentially lucrative market. By contrast, many of the 32% who chose North America as the top pharma M&A growth area saw plays there centered around consolidation and cost-saving.
- Nearly three-quarters (72%) expect an increase in the number of divestments for pharma M&A in the next 12 months, as companies look to specialize and respond to shareholder pressure regarding cost-cutting.

In many ways, pharma companies are at a crossroads as to whether they should play aggressive and expand, or improve their own operations first. However, on both sides of the fence, M&A is being seen as a key way to navigate through the landscape.

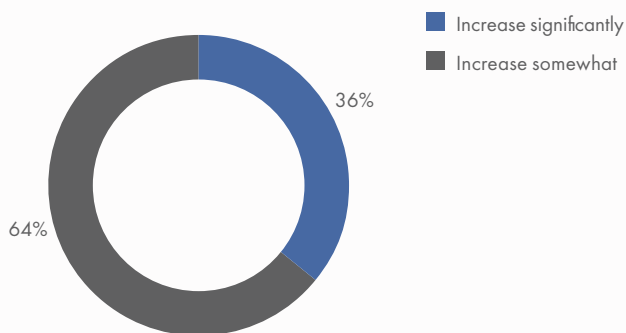
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From blue-chip giants to new startups, doing a deal is becoming an increasingly attractive option.

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SURVEY

What do you think will happen to pharma M&A in the next 12 months?

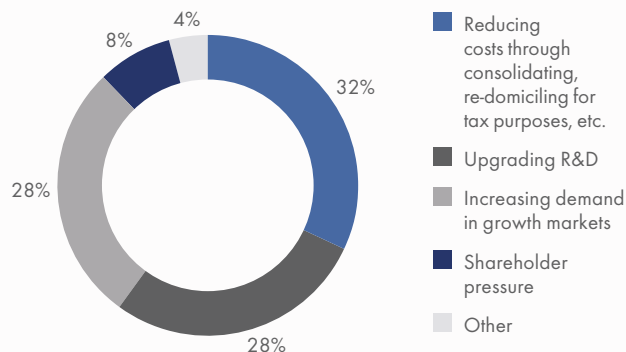


Pharma executives are unanimous in believing that M&A will increase over the next year, according to our survey. Indeed, more than two-thirds (36%) even see deal-making in the sector increasing significantly, compared with 64% who predict it will increase somewhat.

The common goals of pharma players will lead to this significant increase in deal-making, according to one director of finance. "The interest of development is mutual within pharma companies and to achieve the desired goal of innovation in their business, they will seek strategic partnerships with businesses that share the same understanding and this will contribute to an increase in M&A activity," he says.

For one corporate strategy director, consolidation in pharma will also drive activity. "Currently, the pharma industry exhibits a 'buy or be bought' mentality," he says. "The sector is moving at a rapid pace and the FDA is offering approvals to drugs, yet only after stringent checks. This leaves small players with no other option than divesting or forming a partnership with another pharma business. Consolidation will happen at the mid-level and small level as these firms will be most affected and are a majority." Figures also back this assessment up, with pharma deal-making at US\$211.7bn for the first half of 2015, compared with US\$205.4bn for H1 2014.

What is/will be the main driver of pharma M&A deals in 2015?



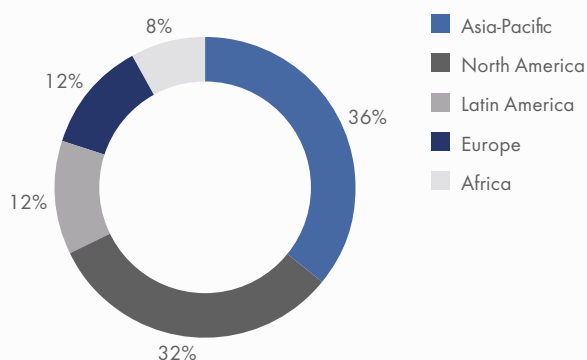
Reducing costs (32%), upgrading R&D and increasing demand in growth markets (both 28%) are the leading deal drivers for pharma in 2015, according to respondents, while shareholder pressure was chosen as the leading driver by just 8%.

Consolidation is a key motivator for M&A as companies look to rationalize their offerings. "Businesses are looking at consolidating their product offerings with other businesses and are considering the idea of capturing a larger patient base that suffer from common diseases which can be treated," says one VP of strategy. "This can help to control and reduce costs which continue to impact the balance sheets of businesses."

Improving R&D through M&A is also seen as common a way of improving companies' in-house capabilities. "R&D is an important process in the pharma industry and helps businesses gain recognition and growth at the same time based on product offerings," says one finance director. "However, the initial investment, time and most importantly the regulatory affairs are very stringent, which seems to be very challenging and not within every business's reach, so companies chose the M&A route to acquire and update R&D facilities." Demographic changes around the world are also reshaping pharma's acquisition strategies.

SURVEY (CONTINUED)

Which geography will see the biggest increase in pharma M&A in the coming year?

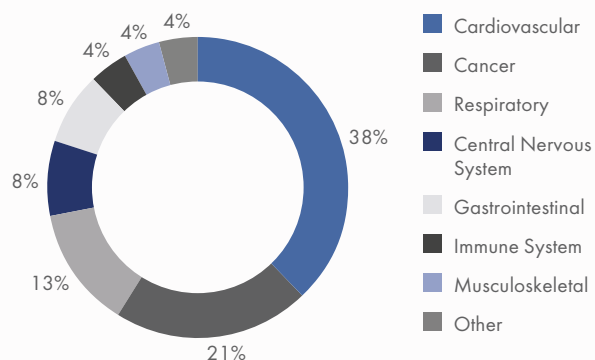


Respondents' answers regarding which region will see the biggest increase in pharma M&A in the coming year are a bit scattered with 36% saying that the Asia-Pacific (APAC) region will be the most popular followed closely by North America (32%).

Alongside the opportunity to target a growing demographic, changes to the business environment are attracting pharma companies to APAC. "First, the demand in APAC is significant because of the vast population and people in APAC countries who are earning big now, and who are able to afford high cost treatments," says a corporate director of strategy. "Second, the change in regulatory affairs in APAC which has become investment friendly and foreign firms are given many relaxations for their investments. Third there is significant capital available in APAC for M&A."

By contrast, deal-making in North America is growing in terms of pharma M&A as companies look to ease the burdens they are under. "North American businesses are under pressure because of high R&D costs, regulatory issues and expirations," says a director of corporate development. "For them, M&A is being seen as the best alternative to develop business capabilities that are essential to compete and be profitable."

Which therapeutic area will be most sought after by acquisitive companies?

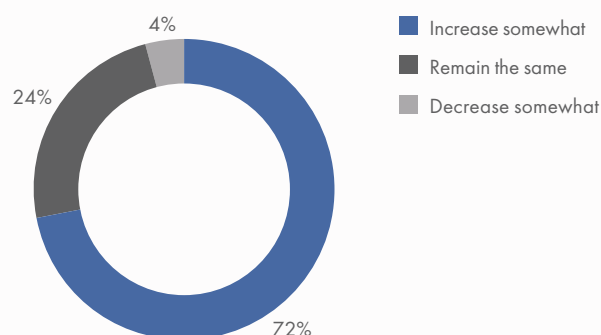


Cardiovascular was pinpointed by 38% of respondents as the therapeutic area that will be most sought after by pharma companies, the highest percentage returned. The second most popular choice was cancer, seen by 21% as the area that will see the most activity.

The increasing number of people as well as the commonness of heart conditions makes cardiovascular a key area for investment, says one corporate strategy director. "Cardiovascular treatments are expensive and with the growing population, the amount of patients suffering from heart conditions has increased which makes investment productive as more patients would result to more revenue. The cardiovascular section goes through innovation and creates new products which help in monitoring and assessment of the health condition and buying such a business, even small, can fetch a better value as the need is universal."

Investing in cancer therapies can also provide pharma companies with a long-term and diverse acquisition. "Cancer has a long lifespan, and requires a range of therapies which involve costs that can benefit the acquisitive company based on the revenue generated," says one VP of global strategy and development. "In addition, there are different types of cancer on which constant innovation is required to meet the demand which makes this healthcare division a good catch."

What do you think will happen with regard to pharma divestments in the next 12 months?

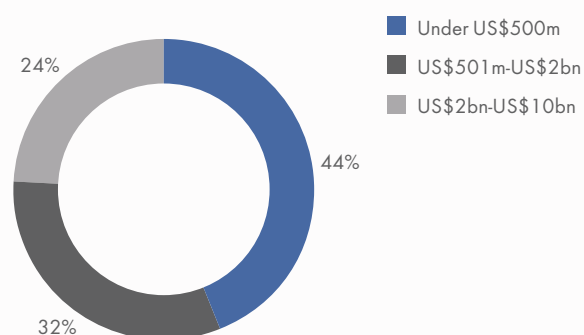


The overwhelming majority of respondents believe that divestments will increase over the next year, with 72% saying they will increase by a certain degree. Just under a quarter (24%) think the level of selling will stay the same, while just 4% think they will decrease.

Competition and shareholder determination could drive this increase, according to one VP of corporate development. "Divestments could increase as pharma businesses will be forced to focus on core business improvements due to the growing competition in the sector across the globe and increasing demand in few regions," she says. "Shareholder pressures for return are likely to drive divestment decisions as businesses will try to keep away from activism activities that display negativity about their firm."

PHARMA DIVESTMENTS SET TO INCREASE

What will be the average deal size for pharma M&A?



In terms of deal size, the pharma industry should have a wide range of values according to respondents. Forty-four percent see most deals being less than US\$500m, while 32% and 24% expect deals to be between US\$501m-US\$2bn and US\$2bn-US\$10bn respectively.

Industry uncertainty means pharma players won't commit excessive levels of capital, so they will focus on smaller investments, says one strategy director. "Businesses will focus on minor investments as healthcare trends and regulations continue to change without notice, putting big investments at risk and a cautious approach will be used by majority participants," he says. "Also it is the small and medium sized companies that are actively pursuing M&A to overcome the R&D challenges and capital issues."

By contrast, some respondents feel that the favorable funding environment may mean that bigger deals become more popular. "Deals are likely to be in the range of US\$2bn-US\$10bn as interest rates are low and the credit supply for leveraged buyouts has gotten better over the last few months," says an M&A director. "This will be a good opportunity for dealmakers and investors who are looking for big market consolidation by taking targets with high value."



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Pharma deals in the room

Venue® data room: A special report

CVS Pharmacy, Inc. acquires
Target Corporation's pharmacy
and clinic businesses
June 15, 2015

Target: Target Corporation (pharmacy and clinic business)
Financial Advisor for Buyer: Barclays
Counsel for Buyer: Dechert LLP; Fried Frank Harris Shriver & Jacobson LLP; Simpson Thacher & Bartlett LLP
Financial Advisor for Seller: Goldman Sachs
Counsel for Target: Dorsey & Whitney LLP; Faegre Baker Daniels LLP; Wachtell, Lipton, Rosen & Katz
Industry: Consumer: Retail; Chemists/health

Zeta Acquisition Corp.
III (Zeta), acquires Kura
Oncology, Inc.
March 6, 2015

Target: Kura Oncology, Inc.
Counsel for Target: Cooley LLP
Counsel for Buyer: Richardson Patel LLP
Private Equity Firm for Seller: ARCH Venture Partners; Ecor1 Capital, LLC; Tavistock Life Sciences; Nextech Invest Ltd.
Industry: Medical: Pharmaceuticals; Drug development

Cigna Corporation
acquires QualCare
Alliance Networks, Inc.
January 26, 2015

Industry: Financial Services; Medical; Services (other); Business support services; Health institutions; Insurance related

Actavis plc acquires
Allergan, Inc.
November 17, 2014

Financial Advisor for Target: Bank of America Merrill Lynch; Goldman Sachs
Counsel for Target: Latham & Watkins LLP; Matheson; Richards Layton & Finger, P.A.; Wachtell, Lipton, Rosen & Katz
Financial Advisor for Buyer: JP Morgan
Counsel for Buyer: Cleary Gottlieb Steen & Hamilton LLP; Cravath, Swaine & Moore LLP; Weil Gotshal & Manges LLP
Industry: Medical: Pharmaceuticals; Drug development; Drug manufacture; Drug supply

Acadia Healthcare Company
acquires CRC Health Group
October 29, 2014

Target: CRC Health Group, Inc.
Financial Advisor for Target: Citi
Counsel for Target: Ropes & Gray LLP
Financial Advisor for Buyer: Jefferies LLC; UBS Investment Bank
Counsel for Buyer: Cleary Gottlieb Steen & Hamilton LLP
Private Equity Firm for Seller: Bain Capital, LLC
Industry: Medical; Health institutions

Actavis acquires
Durata Therapeutics
October 6, 2014

Financial Advisor for Target: Bank of America Merrill Lynch
Counsel for Target: WilmerHale
Counsel for Buyer: Debevoise & Plimpton LLP
Industry: Medical: Pharmaceuticals; Drug development; Drug manufacture; Drug supply

Kroger acquires
Vitacost.com
July 2, 2014

Financial Advisor for Target: Jefferies LLC
Counsel for Target: Skadden Arps Slate Meagher & Flom LLP; White & Case LLP; Wilson Sonsini Goodrich & Rosati P.C.
Counsel for Buyer: Weil Gotshal & Manges LLP
Industry: Medical: Pharmaceuticals; Drug Supply

Prestige Brands acquires
Insight Pharmaceuticals
April 25, 2014

Target: Insight Pharmaceuticals Corporation
Financial Advisor for Buyer: Sawaya Segalas & Co., LLC
Private Equity for Seller: Teachers Private Capital; Swander Pace Capital LLC
Counsel for Seller: Kirkland & Ellis LLP
Industry: Medical: Pharmaceuticals; Drug manufacture; Drug supply

KKR acquires National Vision
February 7, 2014

Target: National Vision
Counsel for Seller: Weil Gotshal & Manges LLP
Financial Advisor for Seller: Barclays; Wells Fargo Securities LLC
Counsel for Buyer: Simpson Thacher & Bartlett LLP
Private Equity Buyer: Kohlberg Kravis Roberts & Co. L.P.
Private Equity Seller: Berkshire Partners LLC
Industry: Consumer: Retail; Chemists/health; Other retailing of consumer products and services

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Venue demo (audio enabled):
<http://www.rrdonnelley.com/venue/Resources/ProductDemo.asp>

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Venue data rooms are backed by RR Donnelley, a \$11.6 billion corporation with more than 500 locations and over 65,000 employees worldwide. RR Donnelley's total revenues are larger than all other virtual data room providers combined. We bring extensive experience to providing integrated communications services.

For more information regarding Venue, RR Donnelley, or this report, please contact us directly.

RR DONNELLEY AT A GLANCE

\$11.6 billion	2014 net sales
65,000+	Employees
500+	Global locations
Nearly 125	Manufacturing locations
750+	Issued and pending patents
Nearly \$2 billion	Capital investments over the past six years

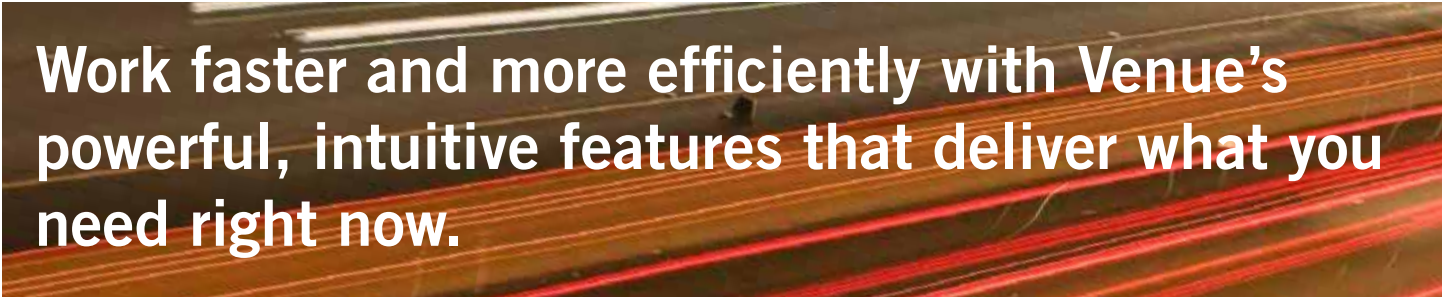
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We serve hundreds of thousands of Venue users, who are accessing content related to the highest profile deals in the market. With a Venue data room you have access to the RR Donnelley global footprint, where you can leverage our suite of financial services—everything you need from pre-negotiation to post-transaction filing and archiving—anytime, anywhere.



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