A Second Coming

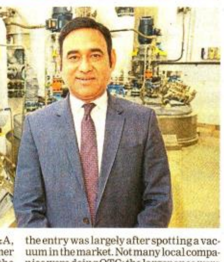
Ajay Piramal may have exited the pharma business in 2010 with a bang, but eight years on, the small segment he retained has ensured that he's back – with a bigger bang. ▶▶ 18

A SECOND COMING

Did you know Ajay Piramal's pharma empire today is more than twice the size of the business he sold 8 years ago for a jawdropping sum? Amid frenzied speculation of a comeback as the non-compete deadline draws near, here's the inside story of what's cooking in the labs

Kiran Kabtta Somvanshi in Phoenix | Detroit
& Arijit Barman in Mumbai

Photo: BHARAT CHANDA



(Clockwise from above) Ajay Piramal flanked by daughter Nandini and son-in-law Peter D'Young, with Kedar Rajadnye, PEL COO (consumer products); Piramal facilities in Riverview, Michigan and Lexington, Kentucky; Vivek Sharma, CEO, Pharma Solutions, PEL

Unlike other weekends, this one was an exceptionally busy one at Ash Stevens — Piramal Pharma's acquisition in the resurgent Detroit. The firm was going live with new enterprise software to eventually integrate with Piramal Pharma. The excitement could be heard in the voice of chief executive Vivek Sharma, who had flown in from Boston for a townhall with the team and to announce an incentive pay scheme for the employees.

More than a year after joining the ever-growing Piramal family, the 55-year-old contract manufacturing firm catering to pharma and biotech companies continues to undergo transition, starting from the very top. A new commercial officer, financial manager and HR head are on board.

"Integrating American and Indian cultures is probably one of the most engaging parts of my job," says Michael Jordan, head of HR, Piramal Pharma Solutions.

"This was not a distress sale, but after death of the company's founders, their successors wanted to cash out," says Vince Ammoscato, vice-president, operations, a veteran of 24 years.

For the Piramals, though, this sixth acquisition in North America has been a strategic add-on. "With the acquisition of Cold Stream, we got the research & development (R&D) and manufacturing capability in injectables. With Ash Stevens, we got high potent API capabilities," says Sharma. "Besides, we also got two unique sets of customers to whom we can sell our existing capabilities."

Now, in case you are wondering — yes, Ajay Piramal exited the pharma business in 2010 for a jawdropping $3.72 billion; a lion's share of it actually — the ₹1,800 crore domestic formulations business.

However, he retained the smaller segments of drug discovery, over-the-counter (OTC) consumer products and contract manufacturing. And within eight years, these have actually grown twice the size of what he sold; arguably, at the right time.

It explains the frenzied speculation of a domestic formulations re-entry, as the September no-compete deadline nears.

ANOTHER INNINGS?

Group chairman Ajay Piramal offers a sneak peek into his mind when he says the industry has undergone a sea change in these eight years. "It's become much tougher now... The spread of price control has gone up and regulators want to keep pushing down prices. There is also far more competition and restrictions on drug promotion." Yet, typical of the man, he leaves room for second guessing. "We haven't yet made up our minds. We will see how 2018 pans out."

Group watchers say sections are keen to jump right back with an acquisition, but nothing cheap is available. "They have been evaluating chronic space for cardio, diabetic centric targets but it's not in their DNA to pay prevailing rich multiples of 5-6x sales," feels an investment banker who tracks them closely. "Returns are low. I don't see them doing anything big bang. Something like a Unichem would have been a great platform."

The domestic formulations exit was timely and generated funds that were deployed in financial services, realty and information management. Piramal continued to build on fledgling pharma segments

Piramal has always been counter-intuitive. In 1990s and early 2000s, when everyone was into reverse engineering and knock-offs, he decided to partner with Big Pharma MNCs and not go against them.

Buying and selling is second nature — Piramal scooped up Indian arms of MNCs (Aventis, Rhone Poulenc, Roche etc) and subsequently Rhodia, Pfizer Morpeth and Avecia that helped build a track record and international presence in custom manufacturing as well as trust with the likes of GSK or Pfizer.

The domestic formulations exit was timely and generated funds that were deployed in a host of other businesses such as financial services, realty and information management. Simultaneously, Piramal continued to build on fledgling pharma segments. He has now built a ₹4,000-crore pharma empire that has withstood regulatory scrutiny and headwinds at home and abroad, which most of his local peers are grappling with today; even if 85% of pharma revenues are global.

"His legacy is to create value for shareholders and build a reputation as a value generator, rather than dedicating himself to just one industry," says Ajit Mahadevan, former strategy and M&A head, Piramal Enterprises (PEL).

In the past year alone, PEL stock has appreciated 80%, hitting a record high in June. "There was always the belief that we are good at building and creating businesses and we can do this again," quips Nandini Piramal, executive director, PEL, who oversees OTC. She recalls a dinner conversation with her parents and sibling Anand the night before the Abbott transaction was announced. "We retained contract manufacturing because we believed we have lot of expertise in it. (We) deliberately kept OTC."

PEL's growth trajectory is a classic example of opportunism meeting expertise. From the ₹15,000 crore it received from Abbott, ₹6,000 crore was invested in the pharma segment. The business has now grown to earn revenues of ₹4,000 crore — ₹3,500 crore from global pharma generics and ₹500 crore from OTC products sold in India.

Revenues from global pharma business have doubled in the past six years with FY17 Ebitda margin at 20%. The company has six OTC brands in India's top 100 and is among the top five category players. In eight years, net sales have grown at a CAGR of around 20%.

Growth has mostly come inorganically, spending approximately $500 million on seven acquisitions — two US plants for contract manufacturing, two hospital products and three portfolios of OTC products in India — in the last two years.

An eye on profitability and market potential has also influenced exits. From spinning out the R&D division into a separate listed company to closing it down in 2014, PEL has been quick at course correction.

"He (Piramal) tried to make a real play in the R&D new drug development space with investments over 10-15 years. It didn't work out as it perhaps needs a different mindset. So he exited," says a company official who did not wish to be quoted.

With the group's foray into areas such as financial services, pharma's slice in the overall PEL revenue pie has shrunk to around 42% in FY17. In the medium term, it is likely to be hived off and listed separately to unlock value and visibility.

"Our long-term plan is to get to Ebitda margins of 18-20%. Within global pharma, we expect to be 20-25% over the next three years," says Nandini. "Our businesses seem disparate but all three verticals are bound by a common vision. We have just delegated responsibilities to independent teams for more accountability. The synergies benefit all," adds her father.

GLOBAL PLAY

The international contract manufacturing blueprint prepared by McKinsey in 2003, for example, was based on the premise of patent non-infringement and collaboration in drug development and manufacturing. It proposed using India for cost arbitrage but leveraging a global footprint to stay closer to the customer.

With innovators lacking infrastructure to outsource too far, Piramal acquired manufacturing capabilities in the US.

It has paid off in unique ways. A global contract research and manufacturing services (CRAMS) business means PEL's pharma facilities getting audited by 78-plus regulators.

"We have someone coming into one of our 13 plants twice a week," explains Nandini. "The cost of non-compliance is higher. We have seen plants that have been in remediation for 3-4 years. I'd rather comply than deal with loss of business. The cost of reputation is also very high."

No Piramal facility has faced US Food and Drug Administration (USFDA) issues – unlike their Indian peers, which have been severely hamstrung by global audits. As Piramal puts it, "The desire to grow fast and profitably is what made the difference," and ultimately Indian players are paying for it. "In some cases which have been well documented, there were blatant efforts to put things incorrectly."

RIGHT DOSAGE

Pharma business includes...
Global pharma and the India consumer products business (OTC)

Pharma contributed **42%** of total PEL revenues for first 9 months of FY18

Global pharma business grew at a 6-year CAGR of **16%** and Ebitda margins improved from 4% in 9 months of FY11 to 21% for 9 months of FY18

13 manufacturing facilities in 3 continents of North America, Europe, Asia

It is among top 5 OTC players; 6 brands are within the top 100 brands in the country

8 acquisitions in last 3 years — 4 in global pharma and 4 in India consumer products

FY17 pharma revenues
₹3,892 crore

Since 2011, PEL has successfully cleared 29 USFDA inspections, 91 other regulatory inspections and 698 customer audits

Contract manufacturing is riding on growth and cost pressures plaguing pharma majors, says CEO Sharma. "They are looking to get more effective drugs out faster and cheaper."

He adds, "The world's top 10 companies are our customers. We also deal with niche biotech players high on innovation and drug discovery, but lacking a team."

The company remains focused on small molecules and is diversifying across a variety of dosage forms and geographies, feels V Krishna Kumar, partner, M&A, pharma & healthcare, EY — also a former Piramal Pharma executive. "Given the sheer multitude of private equity-owned assets worldwide in this sector, it would be interesting to see if Piramal makes any global moves towards becoming a capacity consolidator or a vertical integrator."

Interestingly enough, even the nucleus for the global critical care business was laid with acquisition — that of two inhalation anaesthetic products from Rhodia Fine Chemicals in 2004. Throughout, the play has been for such high-margin, niche products, which also includes injectibles and antibiotics that are used in operation theatres and critical care units.

The competition is among a handful of players ensuring better pricing power. "We (have) a differentiated strategy compared to other generic players in that all our products are focused on hospital channels," says Peter D'Young, chief executive, Piramal Critical Care.

However, niche is by no means small. When Piramal went in for anaesthetic products, it was a $1-billion market. "But wherever there are surgeries, you need anaesthesia. So we've expanded the market to look at all hospital products in the critical care space. And today, that's probably a $40-billion market with just three to four players," highlights Piramal.

The group also has plans to globally list the digital analytics business that contributes 11% to total revenues. "In the mid-term, we will list globally as the understanding of all analytics, data and insights we provide is global," says Piramal. "It's really a global business, its appreciation is global."

Yet, headwinds remain, especially in segments like CRAMS. "It's getting hyper-competitive with smaller players — some even from India — chipping on the margins. It will be a difficult business to grow," says the CEO of a rival firm who did not wish to be quoted. Another industry veteran who deals with the Piramal Group feels, "Outsourcing opportunities are drying up. Many countries are putting in trade barriers and there is increasingly a shift towards local production in the US and EU. Keeping the order pipeline robust is becoming a challenge."

OTC, though, has huge potential, having grown 21% since its start in 2008. Here too, the entry was largely after spotting a vacuum in the market. Not many local companies were doing OTC; the larger ones were all outsiders or non-pharmaceuticals. "We decided to give it a twist by pitching health and lifestyle benefits," explains Nandini. The company has invested significantly in building sales force, distribution and product innovation.

BRAND POWER

OTC actually started once joint venture Boots was dissolved and some of the brand rights for India got transferred. But it received a boost only after the Abbott sale.

"The fact that MNCs like Allegran sold their brands to him displayed the trust Piramal has built over the years. MNCs have struggled in the Indian intellectual property regime. But he has given a new lease of life to many," argues Mahadevan.

Nandini feels many of these legacies — Lacto Calamine, Waterbury's Compound — were devalued under their original MNC ownership but resuscitated once Piramal took over for their strong brand connect. "We remember many since childhood. We bought them cheap and invested in marketing and advertising spend to remind people. In some, we have added quirky innovations as well ramping up the fun quotient," she adds.

The segment has a ₹1,000-crore revenue target for FY20. "We had an early mover advantage, realising its potential in 2009," says Kedar Rajadnye, chief operating officer, OTC. "It's only in the last few years that everyone — Alkem to Cipla, Mankind and Glenmark — are making an attempt."

Piramal clung on to this small portfolio of ₹40 crore when Abbott was in negotiations and today, it is a top 5 player, up from 40th in 2010. It is also the fastest-growing despite price controls and fixed-dose combinations. "We reach out to 7 crore consumers a month with 17-18 brands," says Rajadnye, his pride unmistakable.

Even then, the pharma business remains low key, with rivals calling it too unconventional. "OTC is not exactly pharma but an FMCG play for deep pocket contenders like Piramals. Companies are just looking to outspend each other, unlike prescription pharma," feels the CEO quoted above.

Nonetheless, with his differentiated strategy, Ajay Piramal remains the last man standing.