

THE CHRONIC MICROCAP TRAP

HOW LAUNCH IS THE ESCAPE FOR TRUE GROWTH

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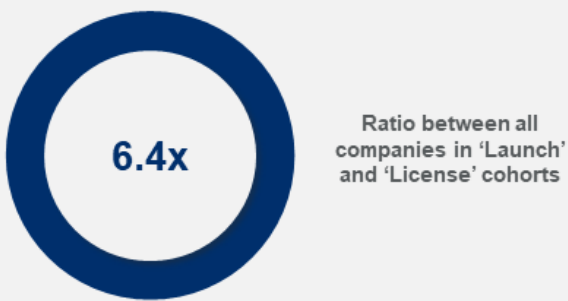
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The Chronic Microcap Trap: How Launch Is the Escape for True Growth

Pre-commercial pharma companies face a common choice: commercialize products independently or collaborate with another pharmaceutical company as a commercialization partner. As the C-suite leaders in these organizations wrestle with the pros and cons of this choice, one factor they must consider is the impact their decision will have on their current and future market valuation. The question is this: How much of a premium does the market put on a company that chooses to launch and commercialize its product independently? As Figure 1 suggests, that premium can be substantial. The average market capitalization of a cohort of public companies that developed paths to launch their own products (including successful and sub-optimal launches) was over six times greater than a cohort of public companies who consistently license with other pharma companies to launch their products.

Figure 1: Ratio of average market capitalization between a cohort¹ of 'Launch' and 'License' public companies

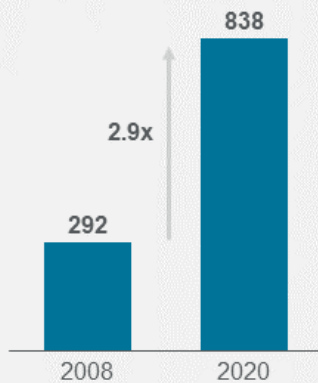


¹ The 'Launch' cohort consists of 33 companies that commercialized their own product and the 'License' cohort has 17 that partnered with larger biopharma companies

SOURCE: EVERSANA Analysis

A company that successfully launches and commercializes its product independently generates revenue and earnings that stay within the company's walls, as opposed to taking only a small percentage of royalty revenue from licensing its asset. The cash the company generates from independent commercialization can fuel further clinical development programs and acquisitions, which can set the stage for a completely different growth path. Hence, a company that is successful at commercialization commands significantly higher market capitalization estimates compared with companies that choose to license their products.

Figure 2: Number of public biotech companies with market capitalization less than \$250M



SOURCE: Nature Biotechnology Survey 2008, EVERSANA Analysis

As illustrated in Figure 2, the universe of nanocap and microcap pharma companies continues to grow, creating a growing backlog of companies trying to chart the course away from being a permanent microcap company and toward becoming a mid-cap or even large-cap company. Clearly, the primary means of reaching that goal is successfully launching and commercializing products independently.

Launch Can Be Too Expensive and Complex to Execute Independently

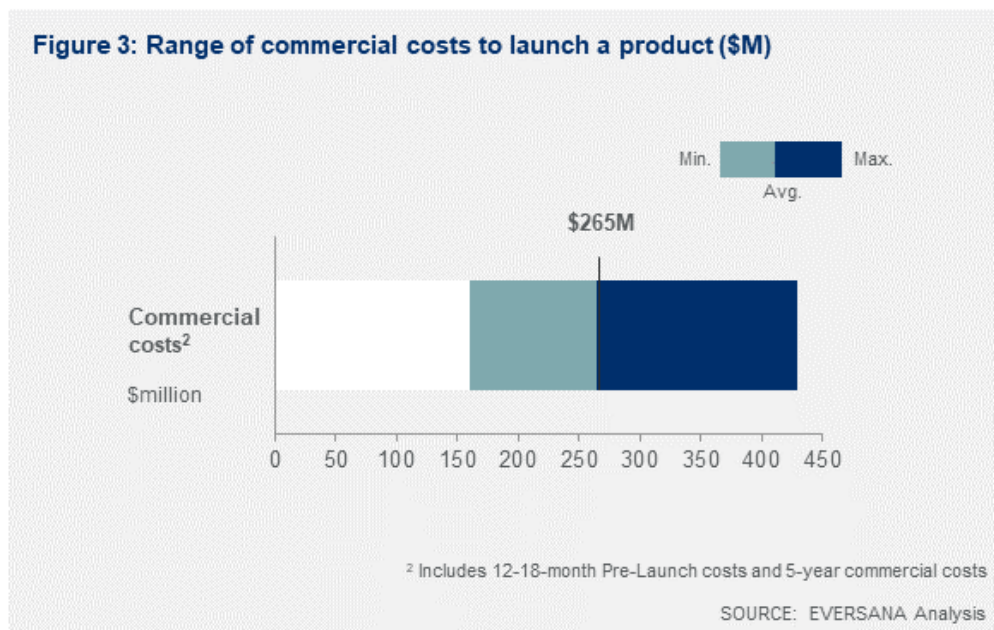
Though an independent launch may be the “obvious” choice based on market cap impact, the harsh reality is that few companies are able to execute a launch on their own. To launch an asset with even a modest market opportunity can be a costly endeavor. On average, funding the pre-launch and five-year post-launch activities for a product can range from \$200M - \$450M (Figure 3). If companies underfund their launch, they risk undermining the commercial potential of the asset. Even if companies choose to allocate conservative funds for commercialization, they still face funding requirements that could exceed their current market capitalization in the nanocap and microcap space.

In addition to significant funding requirements, launching a pharmaceutical product requires significant and highly technical subject-matter expertise from a finite pool of talent resources who are in high demand in the pharma and biotechnology industries. You cannot fake your way through product commercialization in the pharmaceutical industry. Companies require professionals who have a strong command of the given market they are trying to serve while being able to navigate strategic, operational, regulatory and scientific issues. This is a non-trivial set of skills that cannot be established quickly or easily *de novo*.

Even when companies have sufficient funding and talent, they still face significant risks and challenges related to establishing an operational backbone of technology, supply chain and services, all of which require a high degree of orchestration of various internal and external (third-party) agencies.

Faced with these challenges, many companies are unable to justify the potential investment based on the risk and limited funding channels at their disposal. Consequently, the choice between independent commercialization and licensing skews heavily toward licensing to another pharma company that already possesses the commercial infrastructure and resources to successfully launch their product.

“A launch winner yields 12 times the growth vs. a license winner yielding just double growth.”



Realizing Sub-optimal Value Creates a Microcap Trap

Once a company reaches the conclusion that the odds of successfully launching on its own are low, the company naturally turns toward licensing, partnership and co-commercialization options. The upside to these options is the ability to get the product to patients, address unmet needs, and realize the commercial value of the product. Unfortunately, the majority of the commercial value does not flow back to the company with the asset. As Figure 4 suggests, approximately 80% of the commercial value goes to the company with the commercial infrastructure.

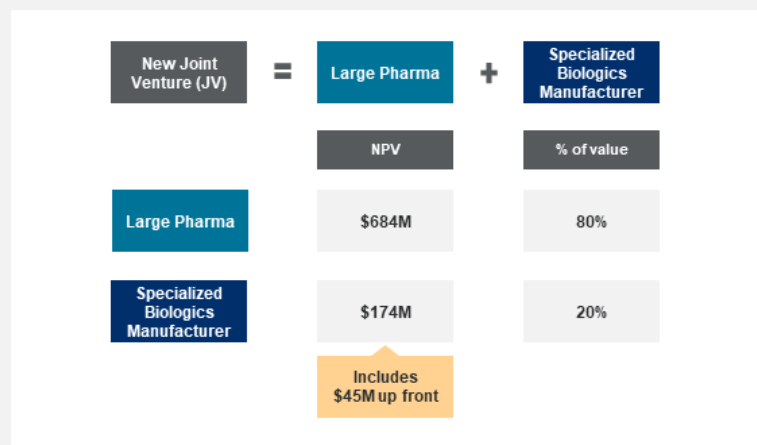
Nanocap and microcap companies and their shareholders have been conditioned to believe and accept that this result is as good as it gets in terms of a successful outcome. However, the market recognizes the limitations of these types of partnerships and reflects those limitations in the stock price. Most nanocap and microcap companies become a permanent resident in this space. The companies that end up forming partnerships may get some increase in valuation, but that value is far below the valuation of companies that have been able to commercialize their assets and retain the majority of the commercial value. We conducted a cohort analysis to substantiate this claim.

We assembled and examined two representative sample cohorts of companies to understand the relationship between independent commercialization and partnering for commercialization.

- **Cohort 1: "Launch"** comprised companies who successfully launched and commercialized their assets independently.
- **Cohort 2: "License"** comprised companies who utilized partnering with other biopharma companies as their primary means to generate value for their assets.

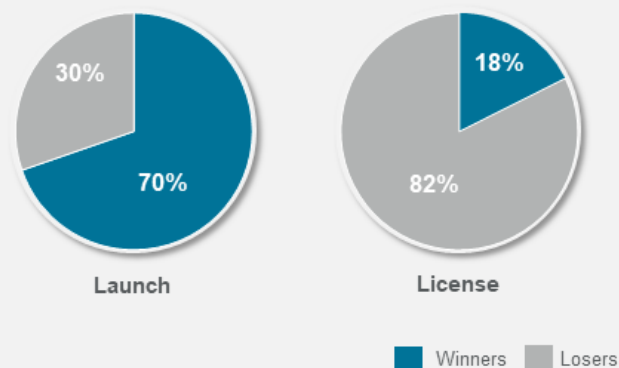
We then tracked the change of market cap for each company, identifying "winners" (market cap increased) and "losers" (market cap decreased) within

Figure 4: Large pharma company forms alliance with a biologics manufacturer to develop and commercialize product



SOURCE: EVERSANA Analysis

Figure 5: Proportion of 'winners' in the Launch and License cohorts



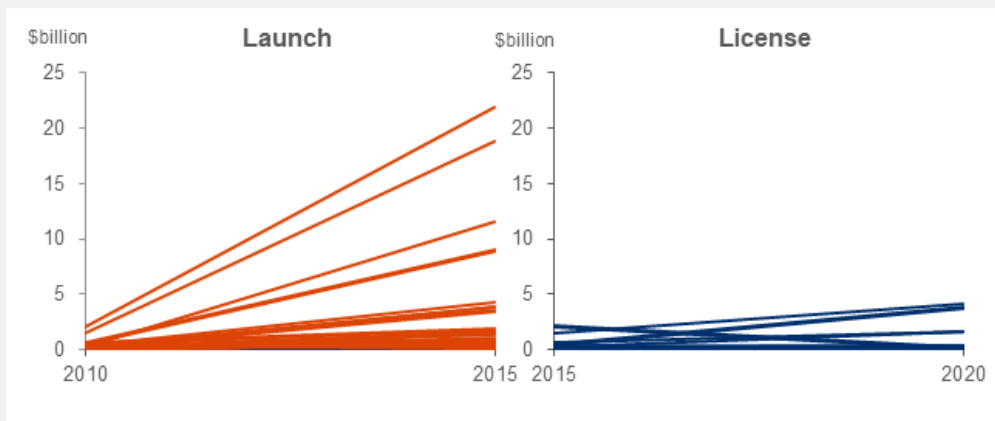
SOURCE: EVERSANA Analysis

each cohort. We also measured the change in market cap over time to understand how much of an impact/advantage independent commercialization had on the long-term market capitalization of a company.

The results were astonishing. As shown in Figure 1 of this paper, the average market cap of Cohort 1 vs. Cohort 2 had almost six times the advantage. Exploring the data further uncovered additional insights (see Figure 5); we noticed that there were far more winners in Cohort 1 than in Cohort 2. Essentially, companies who were able to launch their own products have a 70% chance of dramatically increasing the market capitalization of their company and escaping the chronic microcap trap. However, companies who license their products have only an 18% chance of escaping the trap.

In addition to more winners, the impact size of winning was far greater in Cohort 1 than in Cohort 2. Figures 6, 7 and 8 indicate how the winners in Cohort 1 saw an average 12-fold increase in their market cap. While the winners in Cohort 2 realized only double an average increase in their market cap.

Figure 6: Market capitalization trend for companies in the Launch and License cohorts over a period of 5 years



SOURCE: EVERSANA Analysis

Figure 7: Companies in the License cohort

License cohort	Market Capitalization: Initial (\$M)	Market Capitalization: Current (\$M)	Time period	Increase in Market Capitalization	Winner/Loser
License company 1	400	3870	8	10x	Winner
License company 2	514	1590	7	3x	Winner
License company 3	798	1370	5	2x	Winner
License company 4	142	382	7	3x	No change
License company 5	205	384	11	2x	No change
License company 6	380	550	4	2x	No change
License company 7	31	33	7	1.1x	Loser
License company 8	212	205	1	1.0x	Loser
License company 9	251	223	5	0.9x	Loser
License company 10	390	280	4	0.7x	Loser
License company 11	2950	1670	1	0.6x	Loser
License company 12	449	238	8	0.5x	Loser
License company 13	480	192	8	0.4x	Loser
License company 14	580	203	4	0.4x	Loser
License company 15	107	32	11	0.3x	Loser
License company 16	17000	4100	3	0.2x	Loser
License company 17	255	21	8	0.1x	Loser

SOURCE: EVERSANA Analysis

“Companies that launched were 70% more likely to become a winner vs. companies that licensed, which had only an 18% likelihood of becoming a winner (i.e., escape).”

A vicious cycle can occur with nanocap and microcap companies that initiate licensing deals. The proceeds they receive from these deals may be just enough to generate a handsome return for shareholders but are insufficient for funding meaningful growth. This lack of funding for growth keeps these companies highly dependent on larger pharma companies for further partnerships rather than being able to grow on their own. Thus, these companies become trapped in the nanocap and microcap space for much longer than they would be if a successful and viable commercialization option were available to them without surrendering so much of the commercial value.

Launch Is the Way Out of the Trap, But It's Not So Easy

Several attempts have been made to help nanocap and microcap companies commercialize their products independently and avoid the trap of being a chronic tiny-cap company. Unfortunately, these attempts have failed or faltered for reasons that include lack of comprehensive breadth of strategic and operational capabilities, limited technology and supply chain infrastructure, poor financial wherewithal to handle funding requirements, and the risk profile of the biopharma asset.

Sometimes these attempts failed or missed expectations because they emphasized only certain aspects of commercializing a biopharma product or they focused on building capabilities that were "just good enough" rather than being forward looking and able to adapt to various launch markets and indications. Most importantly, attempts failed due to misaligned internal incentives, resulting in challenging coordination and collaboration across various disciplines and subject-matter experts. Seamless coordination and future cross-functional collaboration must be the standard rather than the exception.

These launch challenges should be acknowledged head-on and early in order to develop a successful commercialization capability. EVERSANA was founded to help companies address these challenges and realize the full value of their products.

Figure 8: Companies in the Launch cohort

Launch cohort	Market Capitalization: Initial (\$M)	Market Capitalization: Current (\$M)	Time period	Increase in Market Capitalization	Winner/Loser
Launch company 1	40	8600	16	213x	Winner
Launch company 2	9	940	11	106x	Winner
Launch company 3	25	1600	11	63x	Winner
Launch company 4	207	12800	11	62x	Winner
Launch company 5	88	4100	11	46x	Winner
Launch company 6	487	22300	22	46x	Winner
Launch company 7	299	12430	11	42x	Winner
Launch company 8	240	9900	11	42x	Winner
Launch company 9	222	8600	11	39x	Winner
Launch company 10	430	13100	11	30x	Winner
Launch company 11	640	18300	11	29x	Winner
Launch company 12	91	2600	11	29x	Winner
Launch company 13	601	13300	11	22x	Winner
Launch company 14	348	7600	11	22x	Winner
Launch company 15	274	5960	11	22x	Winner
Launch company 16	180	3930	11	20x	Winner
Launch company 17	167	3090	6	18x	Winner
Launch company 18	276	4400	6	16x	Winner
Launch company 19	508	7600	6	15x	Winner
Launch company 20	117	1400	8	12x	Winner
Launch company 21	2301	21600	9	9x	Winner
Launch company 22	154	764	11	5x	Winner
Launch company 23	540	2400	4	4x	Winner
Launch company 24	1316	1469	7	1.3x	No change
Launch company 25	434	427	11	1.0x	Loser
Launch company 26	574	562	14	1.0x	Loser
Launch company 27	611	509	6	0.8x	Loser
Launch company 28	910	553	4	0.6x	Loser
Launch company 29	419	244	7	0.6x	Loser
Launch company 30	259	115	11	0.4x	Loser
Launch company 31	696	234	4	0.3x	Loser
Launch company 32	3350	594	6	0.2x	Loser
Launch company 33	430	6	11	0.0x	Loser

SOURCE: EVERSANA Analysis

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