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Private Equity Interest Points to Future Increase in Both Outsourcing and CRO Revenues

It's clear that outsourcing in the drug development industry is here to stay, and is growing. But the fact that private equity firms have been getting into the space is an even clearer and more definite sign. It's also a harbinger of revenue growth among CROs.

That's according to Rohit Waghadhare, an analyst who closely watches the pharmaceutical space and author of a recently published GBI Research report on drug development outsourcing.

"The interest of private equity players in acquiring the CROs indicates that, in the future, outsourcing by pharmaceutical companies is going to increase, which can lead us to expect that the CRO industry will perform better in generating revenue," said Waghadhare.

He pointed to the 2011 acquisition of PharmaNet and i3 by InVentiv Health, which is owned primarily by Thomas H. Lee Partners and Liberty Lane Partners, and Kendle being acquired by INC Research, owned by Avista Capital. The most recent such deal: Carlyle and Hellman & Friedman last October acquired PPD in a deal valued at $3.9 billion.

GBI's report showed the global R&D outsourcing market in 2011 was 26.5% of total pharmaceutical research and development expenditure, which is estimated to increase at a compound annual growth rate of 5%. That means by 2018 it will account for 37.1% of total R&D expenditure.

"It won't be a surprise to see the CRO industry growing in the range of 12%-15% until 2020," said Waghadhare, with much of the outsourcing now moving to a strategic partnership model and away from the traditional transactional model.

According to the report, in 2009, the CRO industry recorded revenue of $19.1 billion, showing an estimated increase of only 6% from 2008 due to the global economic crisis, which caused many pharmaceutical companies to reduce their R&D expenditure. However, more recently, funds have begun flowing back into R&D, and the expected expiry of several patents may force financially struggling pharmaceutical companies to outsource clinical trials. GBI Research estimates the CRO industry will grow at a compound annual growth rate of 12.8% to $56 billion by 2018.

Particularly poised for growth, Waghadhare said, are CROs involved in analytical testing and analytics. "And if the company is developing technologies related to biologics it will benefit the most," he said. "Bioinformatics data analysis, gene expression analysis, and multiplex protein profiling are some of the service platforms that are in demand, and the companies with experience in providing these services will continue to grow."

And that growth could be huge, he added. "Currently, both healthcare IT and analytical testing are in the nascent stage but have the potential to be a separate R&D pharma market."

India and China continue to be the major beneficiaries of outsourcing, but other countries are gaining ground, he said. "Argentina, Poland, Brazil and Russia are the new emerging economies being considered by the large pharmaceutical companies to outsource projects to.

Patient population, tax incentives by governments for attracting investments, and reducing regulatory timelines are some of the parameters that make these markets conducive for pharmaceutical companies expanding their business operations," said Waghadhare.

The report said, according to clinicaltrials.gov, by November 2011, 43.9% of clinical trials had been conducted in the U.S., while 22.9% had been carried out in Europe, and 11.6% had been conducted in Asia. The rest had been conducted in Canada, Mexico, Australia, the Middle East, and Africa, for a total of 21.4%.

—Suz Redfern

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