OUTSOURCING

Private equity ramps up in pharmaceutical services

A yearslong incursion has accelerated, transforming a small-company chemical sector

by ***Rick Mullin***

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Credit: Fabbrica Italiana Sintetici

Fabbrica Italiana Sintetici has expanded this plant in Termoli, Italy. The firm is now looking to Bain Capital, a private equity firm that is acquiring the company, to support its next phase of growth.

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Fabbrica Italiana Sintetici (FIS), a family-owned pharmaceutical services firm in Montecchio, Italy, recently went through a few rough years. Hobbled by debt after a series of acquisitions and investments, the company lost some key accounts. A new CEO was appointed in 2021, and a $370 million bond was issued in 2022, partially to refinance debt. Industry observers, concerned about FIS's future, questioned whether the Ferrari family, its owner, could continue to run a company that had grown to over 2,000 employees and 300 customers.

It was no surprise when FIS was **acquired earlier this year**. Nor was it particularly surprising that the purchaser, Bain Capital, is a private equity (PE) investor.

PE firms invest their own or their shareholders' money to acquire companies, improve them, and sell them for a profit. Although they have long dabbled in the pharmaceutical services sector, only in recent years have they emerged as serious players with deals for industry stalwarts such as Cambrex and Albany Molecular Research Inc. (now Curia).

Firms like FIS—which produce active pharmaceutical ingredients (APIs) and other materials for drug companies and are often called contract development and manufacturing organizations (CDMOs)—were an anomaly at first. To the extent it could be defined, the field was dominated by small players, many of them family-owned European firms. There were also large companies, notably Lonza, but they were outnumbered by the more entrepreneurial, small-scale chemistry specialists.

Although they looked to the outside world like high-tech industrial operations, these CDMOs were primarily service companies, which may have initially confused potential investors. The oddball sector flourished, however, as major drug companies exited manufacturing and ceded drug discovery to asset-poor biotechnology firms. Both trends created a huge market for research and manufacturing services, much of it focused on small-molecule chemistry.

The sector has gained definition over the past 10 years as large players—companies such as Thermo Fisher Scientific, Catalent, and WuXi AppTec—emerged. These broad-service corporations helped frame the industry as ripe for investment. Visibility heightened during **the COVID-19 pandemic**, when the world discovered the intricacies of the pharmaceutical supply chain. CDMOs also demonstrated their importance in 2020 and 2021 by **delivering billions of doses** of vaccines in record time.

Investment by PE companies ramped up in tandem with the newly prominent corporate CDMOs, and that combination has transformed both leadership and culture for the sector. Corporate management systems replaced governance based on human interaction and an atmosphere of familial inclusion, some industry watchers say.

It’s too early in the life cycle of many of the PE investments to determine if PE firms are successful operators in the segment. But already, many longtime industry participants view the investor-owned large companies as the antithesis of the service firms that invented the sector, and they lament the loss of family culture and the spirit of entrepreneurship.

“Private equity has completely redesigned the landscape,” says Guy Villax, who until recently was the CEO of Hovione, a company his parents started in Portugal in 1959 and is still family owned. “All these companies were started as independent businesses by some strong-personality entrepreneur, and these were the people running the business in the ’80s and ’90s,” he says. “Then there was a succession issue. Sometimes it worked, sometimes it didn’t. And private equity bought a lot of them out.”

INVESTMENT RAMP-UP

Jean-Jacques Mondoloni, managing partner of Wombat Capital, which provides advisory services on mergers and acquisitions, attributes a lot of the PE industry's interest in pharmaceutical services to the pandemic.

“Before, a lot of people, including investors, thought the Pfizers of the world were manufacturing their own drugs,” Mondoloni says. “Through the COVID period and the media exposure, the same investors and individuals realized there was a real industry behind the manufacturers of drugs, and I can tell you that since that period I receive, very often, calls from private equity firms that want to invest in CDMOs.”

The attention is welcomed by small and midsize CDMOs “looking to bring their business to another level through the support of a private equity firm,” Mondoloni says. There is also an upside for their customers in the drug industry. “A private equity firm has an objective to grow the business,” he says. “It will make investments in adding capacity, something that will benefit the customer.” And new owners may have fresh ideas. “They will put in place some processes, hire more people, transform the quality department and project management. This will also benefit the customer,” he adds.

The question is whether the level of PE activity will continue, according to Stefan Loren, managing director for health-care investment banking at Oppenheimer. Several economic and political influences will come into play, Loren says. For example, the Inflation Reduction Act allows the US government to negotiate prices directly with manufacturers of certain high-priced, single-sourced drugs, and this power may turn off investors that see dimming prospects in the pharmaceutical sector at large.

SURGE

Key private equity acquisitions of the past decade

Year: 2013

Company: Cambridge Major Laboratories

American Capital acquires the Wisconsin-based contract development and manufacturing organization (CDMO), launched by chemist Michael Major in 2000, for $212 million. The seller is Arlington Capital Partners, a private equity (PE) firm that bought Cambridge in 2007.

Year: 2017
Company: Albany Molecular Research Inc. (AMRI) (now Curia)
The Carlyle Group and GTCR acquire AMRI—founded 1991 by Thomas E. D'Ambra, a one-time research chemist at Sterling Winthrop—for $1.5 billion. The deal took the company private.

Year: 2019
Company: Cambrex
Permira acquires one of the largest CDMOs in the US, another of a handful of publicly traded firms in the sector, for $2.4 billion.

Year: 2021
Company: Seqens
A group led by SK Capital Partners acquires the French company from Eurazeo, a French investment firm. Seqens, formerly Novacap, was formed via a series of CDMO acquisitions, including Chemie Uetikon in Germany, PCAS in France, and PCI Synthesis in the US.

Year: 2022
Company: CordenPharma
Astorg, a European PE firm, acquires the German CDMO from another PE firm, International Chemical Investors Group, which also owns the fine chemical maker Weylchem.

Year: 2023
Company: Fabbrica Italiana Sintetici (FIS)
Bain Capital acquires the family-owned CDMO for an estimated $1 billion. An Italian financial journal had reported that the Italian CDMO Olon, in partnership with the PE firm Permira, was the lead contender to buy FIS.

Sources: Companies, C&EN research.

On the other hand, efforts to reshore pharmaceuticals and APIs that are now available only from China may stimulate investor interest in CDMOs in the West, Loren says.

He adds that the need for consolidation in the industry bodes well for PE firms with a strategy of extending CDMO services across the full reach of discovery, development, and commercialization via serial acquisition. Indeed, a wave of such acquisitions in India over the past 3 years has had a significant PE component, says Gagan Gujral, vice president of Sambi Sciences, a CDMO in Hyderabad.

He says that Advent International, which has closed four deals, illustrates a trend in India of PE firms intending to amass a full range of services by acquiring small specialist firms and building a network. He argues that much of the drug-related manufacturing that will exit China in the years ahead will move to India.

Mondoloni and Loren agree that as PE investors advance, familiarity with the CDMO space no longer presents a challenge for them. “Normally the PE groups don’t jump into this area without some understanding and having some expertise in it,” Loren says.

CHEMICAL FOCUS

PE firms fall roughly into two categories: large marquee firms such as Bain with assets across multiple industries, and smaller ones with a more specialized focus. Cleveland-based Edgewater Capital Partners is an example of an investment firm concentrated in the chemical industry that has also moved into pharmaceutical services.

“We started investing in the specialty chemicals sector for over 20 years but have since moved into other sectors,” says Brian Scanlan, who heads Edgewater’s life sciences unit. “We have always kept the same base criteria for what works in specialty chemicals.”

Scanlan explains that Edgewater tends to invest in companies that make a product that is a low-cost but critical component for a finished good. But it avoids investing in commodity-product manufacturers, preferring firms with specialized expertise. “It’s chemist to chemist, scientist to scientist,” says Scanlan, who was previously vice president of corporate development and ultimately CEO at Cambridge Major Laboratories, a pharmaceutical services firm that was **acquired by the PE firm** Arlington Capital Partners in 2007 and then by American Capital in 2013. "It's a highly technical sell."

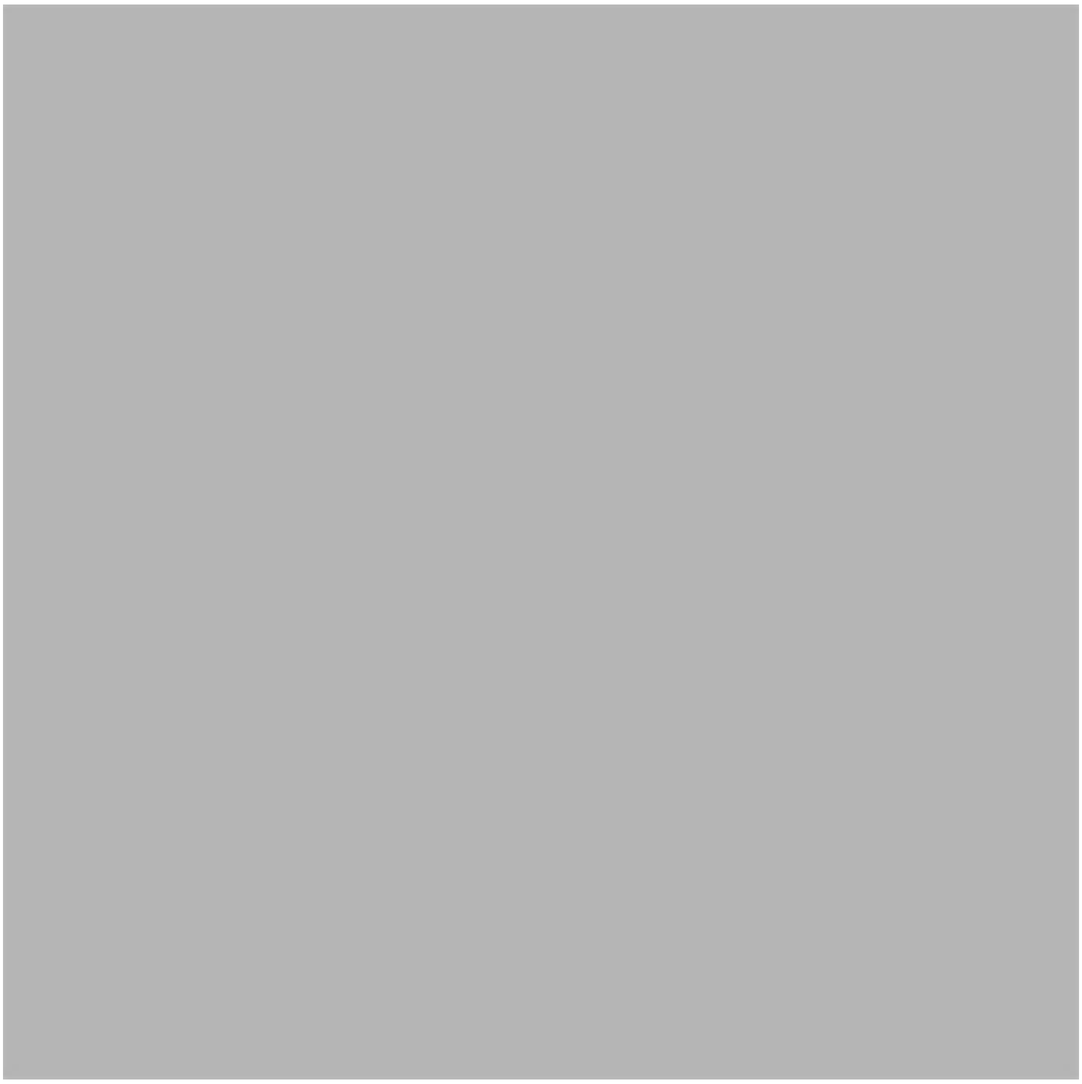
Edgewater's business model is "acquire and merge, or grow organically," Scanlan says. "Ultimately, we create value, add value, and sell." He says a cultural fit is especially important when buying a small, entrepreneur-run company such as GL Chemtec, which Edgewater purchased last year. "We need to be aligned with their sensitivities, because they built the business from scratch," Scanlan says. "They are very emotionally attached."

But Edgewater does set to work making changes, he says, implementing management and finance systems and developing growth strategies—"maybe with more of an outside perspective than the owners had going into it." The firm generally holds assets like GL Chemtec for 5–7 years.

FAMILY HOLDOUTS

Several European CDMOs remain committed to family ownership, despite receiving several overtures a month from PE companies offering a lot of money.

Hovione was **established by Ivan and Diane Villax**, who got their start developing fermentation processes for antibiotics in their basement. Their son, Guy, took over as CEO in 1997. The company has since grown to employ about 2,300 people at facilities in the US, Ireland, and China. It's a prime target for a corporate owner with experience managing a large company.



Credit: Rick Mullin/C&EN

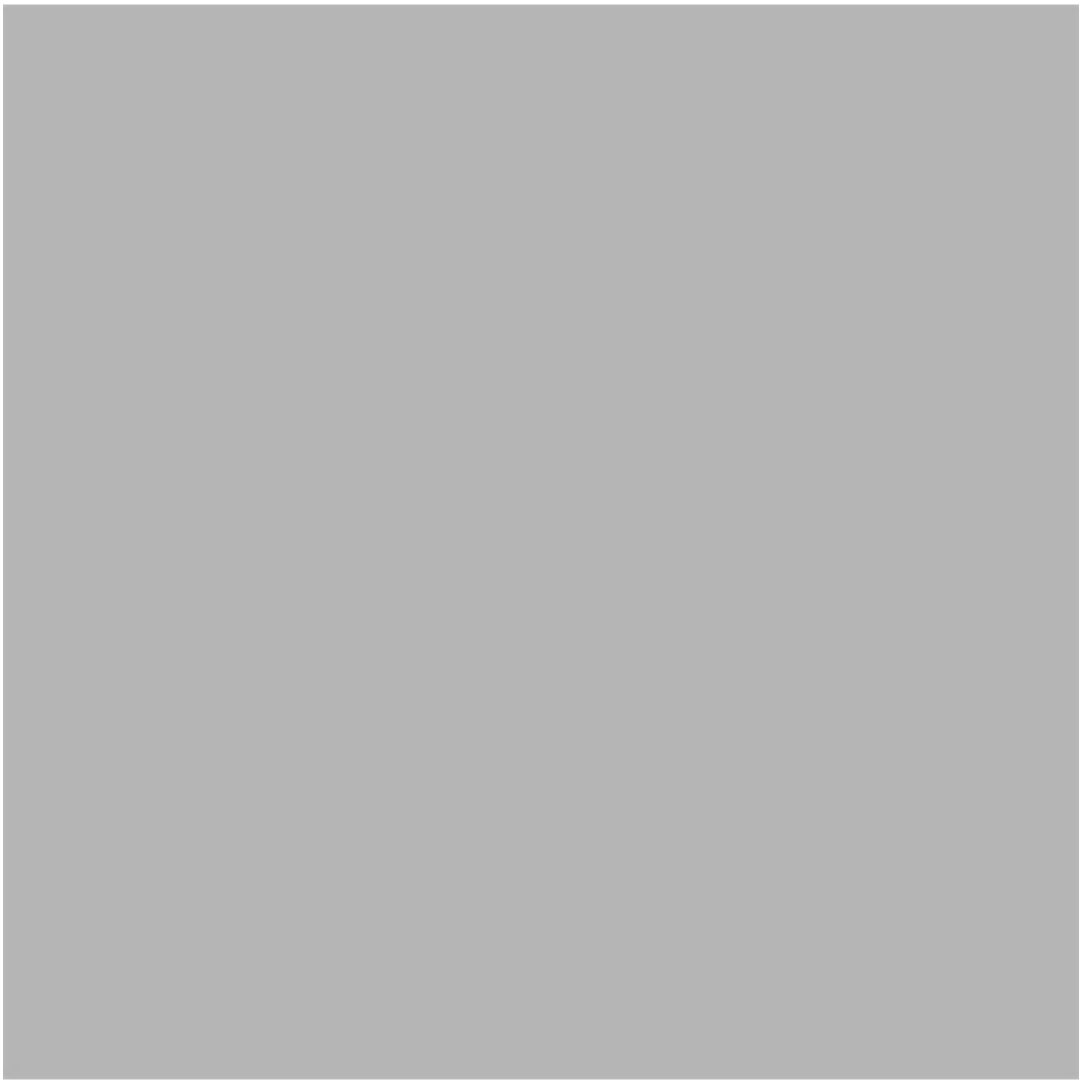
Gianpaolo Negrisoli (left) and Guy Villax took charge of the companies their fathers launched, Flamma and Hovione, respectively. They are committed to family ownership going forward.

Instead of selling to a PE firm, though, Hovione revamped management. Villax retired as CEO in 2022, and the company promoted Jean-Luc Herbeaux, a former Evonik Industries executive who joined Hovione as chief operating officer in 2020, to CEO. Villax is frank about his need to bring in a leader with corporate management experience. “I grew the company until I was unable to manage it,” he says. He remains on the board, and Hovione remains family owned.

“We get frequent calls to see if we’re interested in selling the company,” Villax says. “The answer is no, because the family thinks the company has a great future and that it has strong management and a good board. We think our capital is very well employed in the CDMO business.”

Villax admits that PE investors are generally up to the challenge of taking over a CDMO. “I don’t think we can fault private equity on their choice of top management. They are usually very good at it.” But so are the leaders of the family-owned firms that remain. “You have people at the helm with great understanding of the market, great understanding of the opportunities,” he says.

Dottikon, a family-held Swiss CDMO, was founded as an explosives manufacturer in 1913 “by two brothers and a German beer brewer,” says CEO Markus Blocher, the son of Christoph Wolfram Blocher, an entrepreneur who bought the company in 1986. Markus and his sisters took over Dottikon and EMS Group, a specialty polymer company also owned by the family, when Christoph embarked on a political career—he eventually became Switzerland’s minister of justice—in 2003. By then, Dottikon was involved in pharmaceutical chemicals.



Credit: Dottikon

“You cannot run a business of such complexity if you are not yourself a chemist or an engineer,” says Markus Blocher, CEO of Dottikon, advocating for the experience of family-owned pharmaceutical services companies.

In 2005, the siblings split the family's holdings, EMS-Dottikon, into separate polymer and pharmaceutical chemical firms. Markus Blocher became head of Dottikon and currently owns 65% of the company, which is also listed on the Swiss stock exchange.

And **it is growing** rapidly. "Over the last 5 years we have grown by 20% every year in net sales," he says. "And we've invested $700 million, more than twice our annual revenue, in additional plants and infrastructure in order to cope with the growth." All the new capacity will be built in Switzerland.

Markus Blocher does not foresee Dottikon growing out of reach of its current management. "Yeah, there is critical size, but this is a long-term business, and it's a service business. You really need to understand the needs of the customer and react to their needs," he says. "When somebody comes to you with a new API, they want to make sure you don't change your strategy in 10 years and that it's reliable. That works best if you have an entrepreneur running the company."

What's more, he says, top management needs to be intimately familiar with the technical details of pharmaceutical services. "You cannot run a business of such complexity if you are not yourself a chemist or an engineer."

The Italian firm Flamma has similarly expanded in recent years, establishing **a plant in China** and a research and manufacturing facility in the US. The company recently announced a $200 million investment campaign. Founded in 1950 by Marco Maria Negrisoli, a urologist, to produce amino acids and derivatives, Flamma has been run for nearly 40 years by his son, Gianpaolo, who says he has no interest in selling.

"Our values are the roots of the company," says Gianpaolo Negrisoli, who helped grow his father's small venture into a world-scale pharmaceutical services firm after taking the reins in 1985. "If we sell the company, those values will necessarily disappear. It's like family. Do you sell your family?"

Gianpaolo's son, Gianmarco Negrisoli, is Flamma's corporate development director. He emphasizes the importance of family ownership to the firm's employees. "I can see how people who join the company look for what makes Flamma Flamma," he says. "The moment you belong to private equity, I think that part is going to go away because people don't know who is going to be commanding the boat."

The commitment to employees is reflected in commitment to customers, says Kenneth Drew, vice president of Flamma USA. "People will tell you there is a different vibe, a different feeling when you are working with someone like Flamma versus somebody like a PE-backed company," he says. "It's more transactional with a private equity CDMO. For us, it's more relationship building and long-term commitment to the customer."

TRANSITION

In a $2.4 billion deal in 2019, the PE firm Permira acquired Cambrex—a large, US-based CDMO with annual sales of over $500 million—and took it private. According to Frank Ferrante, Cambrex's chief strategy officer for mergers and acquisitions (M&A), PE ownership has increased financial support for investment. He points to a recent expansion at the company's High Point, North Carolina, facility and the purchase of Snapdragon Chemistry, a flow chemistry specialist in Massachusetts.

Ferrante, a former M&A consultant at Bain who joined Cambrex in 2022, is among several new managers at the company. So is CEO Thomas Loewald, who was appointed in 2020. Both previously held management positions at Thermo Fisher Scientific.

“In my time here I’ve appreciated an excellent partnership” with Permira, Ferrante says. “I don’t feel that there have been . . . tremendous and dramatic changes, given that Permira has great appreciation for allowing management to run the company and being an excellent stakeholder and partner in the process with us.”

Michele Gavino, CEO of FIS, foresees similar benefits from PE ownership. A strategic plan for growing the company—put into place shortly after he arrived—requires the kind of capital that a firm like Bain can provide, he says. The third CEO at FIS who is not a member of the Ferrari family, Gavino is optimistic that the family culture will be preserved, as Bain has invested in other family-owned firms and has shown respect for culture and heritage.

“And if you look at their other investments around the world, they have not been so hot for ‘get in and get out,’” Gavino says, referring to a quick sale of an acquired firm.

More important is Bain’s track record of support for existing management.

FIS is the first pharmaceutical CDMO that Bain has acquired, but Gavino says a broad-based PE firm has a lot to offer. He is an aeronautical engineer who came to FIS from the luxury shipbuilding industry; he also has management experience in aerospace, automotive, chemicals, and other sectors. “As I did, Bain can bring in experience from different industrial worlds,” Gavino says.

He is enthusiastic about the transition. “For sure, we have come a long way as a family-owned business,” he says. “But to scale at a pace that we want . . . we need an investment partner that has a flexible pool of capital to invest, the expertise to navigate the industry with all its nuances, and an understanding of the long-term vision that myself and my team, as well the family, has for the business.”

Industry watchers by and large agree that a company such as FIS will benefit from the financial and managerial support of a PE buyer. But those close to the industry express a sense of loss.

“Behind every story, there is a kind of personal history,” says Roger Laforce, an industry consultant who worked at FIS as general manager of marketing, sales, and R&D from 2004 to 2011. As family-owned companies grow, they become harder for the family to control, Laforce says. By the time a PE firm acquires a company like FIS, “everything is close to just an anonymous financial group,” he says.

“Usually, when the family moves, the culture of the company will change,” Laforce says. “I find it very sad.”

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