Novartis and GSK chiefs set out diverging strategies

Deal sees Swiss group focus on core business while UK rival seeks funds for growth

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It is a tale of two newly minted chief executives, each looking to send a clear signal to investors about strategy and priorities after only months at the helm.

When Novartis announced yesterday the sale to GlaxoSmithKline of its 36.5 per cent stake in their consumer health joint venture for $13bn, it marked an unexpectedly early and decisive move for Vas Narasimhan, who became CEO in February.

Emma Walmsley, meanwhile, who took over at GSK just under a year ago, has strengthened her company’s position in consumer health — but, according to people familiar with her thinking, in service of her number one priority: boosting the flagging pharma division.

When the Financial Times interviewed Mr Narasimhan in September, just after his appointment had been announced, he said he needed to “reflect on” the shape of the group, considering “what are the right adjacencies for a company like us, and where do we have the ability to really create unique value based on our Novartis capabilities?”

His term still measurable in weeks, Mr Narasimhan has not pondered long before deciding consumer health is an “adjacency” too far. He has moved to disentangle Novartis from part of the asset swap deal struck four years ago with GSK: a multi-pronged agreement that his predecessor, Joe Jimenez, had identified to the FT as “a strong part of my legacy”.

The context to the latest deal, according to two people familiar with the discussions, GSK executives repeatedly sought to gauge Novartis’s intentions, aware of the implications for its ability to fund deals on the pharma side, should it buy both Pfizer’s unit and the Swiss company’s stake in the JV.

After Mr Narasimhan signalled his openness to a sale, the negotiating teams managed to structure a deal that was all-out-agreed a week before the deadline for the Pfizer bid, according to one person familiar with the process. However, the deal was not signed until shortly before yesterday’s announcement. A separate team pressed on with negotiations aimed at acquiring the US rival’s business, but the mooted bid was abandoned after investors baulked at the prospect of GSK allocating the capital needed to clinch a purchase.

In a call with reporters, Ms Walmsley acknowledged that discussions over its prospective deal with Pfizer had paved the way for its acquisition of the Novartis stake. The “consideration and detailed review that we did around Pfizer assets opened up this opportunity and we are both very happy to conclude it”, she said. GSK also said it was launching a “strategic review” of its iconic HORlicks brand and other consumer nutrition products, which last year generated sales of £350m.

Investors appeared to believe Novartis had extracted a good price: its shares were up more than 2 per cent in Switzerland. Mr Narasimhan is expected to use the funds to expand “core” business areas — innovative prescription medicines, as well as oncology, generics and eyecare — via organic growth but also through “bolt on” acquisitions, or return cash to shareholders.

A question remains as to whether GSK can indeed turn the £7.8bn consumer healthcare division into a revenue-generating war chest as it battles to reverse underperformance in pharma R&D.

Ms Walmsley said yesterday that the business’s record spoke for itself, with operating margins up from 11.3 per cent in 2015 to 17.7 per cent last year. “We expect operating margins to approach the mid-20 per cent figure by 2022 and that is at 2017 rates,” she added.

That confidence, she suggested, was rooted in “power brands”, such as Sensodyne toothpaste and the anti-inflammatory Voltarol, and a stronger focus on over-the-counter and oral health products, as well as “a much stronger focus on supply chain cost structure”.

Ian Hilliker, analyst at Jefferies, forecast that assuming full control of consumer health should “generate at least 3 per cent to 4 per cent adjusted [earnings per share] accretion for GSK over the near to mid-term”.

Investors duly welcomed the move. Richard Marwood, senior fund manager at Royal London Asset Management, said that the companies’ decision to dissolve their JV had ticked another uncertainty off the list. “Anything you can do to get away from uncertainty overhanging your stock has to be a good thing”, he said. Shares were up almost 5 per cent by late afternoon, at £13.51p.

For Mr Narasimhan, the question is whether he will now also seek to sell Novartis’s 6 per cent stake in Swiss rival Roche, which worth about $12bn.

See Lex
In for the long haul: GSK hopes to transform its consumer healthcare division into a revenue-generating war chest as it battles to turn round pharma R&D.

Novartis has fared better since GSK moves to bulk up asset swap deal in 2014

Share prices rebased

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Source: Thomson Reuters Datastream