

Novartis international ag – company profile essay



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STOCK PRICE DATA AND INVESTMENT ANALYSIS8 IX. CONCLUSIONS & RECOMMENDATIONS10 EXECUTIVE SUMMARY This company profile provides a preliminary investigation and analysis of Novartis International AG, a multinational pharmaceutical company based in Basel, Switzerland. Novartis is one of ten companies the Investment Board will consider for further in-depth research for a multimillion-dollar investment. Novartis was created in 1996 from the merger of two Swiss-based chemical/life sciences giants; Ciba-Geigy and Sandoz Laboratories. Novartis is comprised of four business divisions: pharmaceuticals, vaccines and diagnostics, Sandoz Generics, and consumer health.

Dr. Daniel Vasella is Chairman of Novartis since 1999, and is Chief Executive Officer of Novartis since the merger that created Novartis in 1996. The global pharmaceutical industry tops \$600 billion in sales annually, where Novartis' top three competitors are Johnson & Johnson, Merck, and Pfizer. Novartis' sales over the past 5 years have steadily increased from \$23. billion to \$36.7 billion.

Major factors affecting investment potential include heightened competition from generic drug makers, unprecedented pricing pressure from payers, hard-to-control inflation in research and development budgets, a new U. S. Medicare prescription drug benefit boosting sales, and an aging population.

Novartis has a strong diversified approach to healthcare in its four business divisions.

Its largest and most profitable division, pharmaceuticals, has a strong product portfolio while continuing to invest heavily in R&D to ensure a healthy drug development pipeline. Generics have become the fastest-growing sector of the pharmaceuticals industry, and Novartis is well positioned with their Sandoz division as the largest manufacturer of generic drugs in the world. Novartis stock has performed well over the past five years, and analysts are now strongly recommending buying Novartis stock during the next 6 months. In light of these conclusions, Group #4 Planning Analysts strongly recommend to the Investment Board that Novartis be chosen for further in-depth research for potential investment. I.

INTRODUCTION This report provides a preliminary investigation and analysis of Novartis International AG, a multinational pharmaceutical company based in Basel, Switzerland, for the purposes of assessing its investment potential.

This company profile was requested by Damon Chapman, Chief Executive Officer, and intended for review by the Investment Board. Novartis is one of ten companies to be studied and reported to the Investment Board, which is tasked with reviewing and selecting three investment possibilities for further in-depth research. II. COMPANY HISTORY Novartis was created in 1996 from the merger of two Swiss-based chemical/life sciences giants; Ciba-Geigy and Sandoz Laboratories, which at the time became the largest corporate merger in history at approximately \$41 billion.

Ciba-Geigy was formed in 1970 by the merger of J. R. Geigy (founded in Basel in 1758) and Ciba (founded in Basel in 1859). Sandoz was created in 1886. Since the 1996 creation of Novartis, the company has experienced multiple acquisitions and divestitures.

In 1997, Novartis acquired the crop protection business of Merck & Co. based out of New Jersey. In 2000, Novartis Pharma AG acquired the products Famvir and Vectavir/Denavir from SmithKline Beecham, and also acquired BASF Pharma's European generics business. Additionally in 2001, Novartis Seeds merged with AstraZeneca's ' agribusiness operations to form Syngenta, the first global group focusing exclusively on agribusiness. In 2001, Novartis Generics acquired generics manufacturer Lagap Pharmaceuticals.

In 2002, Novartis Consumer Health Sector divested its Health & Functional Food business. In 2003, Novartis united its generics businesses under one single global brand: Sandoz. Additionally in 2003, Novartis acquired the worldwide adult medical nutrition business of Mead Johnson & Company, a subsidiary of Bristol-Myers Squibb. In 2004, Novartis acquired two generics companies: the Danish company Durasacan A/S from AstraZeneca plc and Sabex Holdings Ltd of Canada.

In 2005, Novartis acquired Hexal AG and Eon Labs, creating the world leader in generics. Additionally in 2005, Novartis acquired North American OTC brand portfolio from Bristol-Myers Squibb, and divested its Nutrition & Sante unit. In 2006, Novartis acquired the California-based Chiron Corporation. As of April of this year, Novartis is reportedly selling off its non-healthcare

businesses to Nestle who has agreed to purchase Novartis' medical nutrition business for \$2.5 billion and its Gerber baby products business for \$5.

5 billion. Currently, Novartis is comprised of four business divisions: pharmaceuticals, vaccines and diagnostics, Sandoz Generics, and consumer health. The company's mission is to discover, develop and successfully market innovative products to prevent and cure diseases, to ease suffering and to enhance the quality of life. III. CHIEF EXECUTIVE OFFICER Dr. Daniel Vasella is Chairman and Chief Executive Officer of Novartis.

He was appointed Chairman in 1999 and has served as CEO and executive member of the Board of Directors since the merger that created Novartis in 1996. Dr. Vasella is also a member of the Board of Directors of Pepsico, Inc., and a member of the Board of Dean's Advisors at the Harvard Business School.

In addition, he is a member of the Chairman's Council of DaimlerChrysler AG (Germany). He is President of the International Federation of Pharmaceutical Manufacturers Associations, a member of the International Board of Governors of the Peres Center for Peace in Israel, and a member of the International Business Leaders Advisory Council for the Mayor of Shanghai. Dr. Vasella graduated with an M.

D. from the University of Bern in 1979. He joined Sandoz Pharmaceuticals in the United States in 1988. He completed the Program for Management Development at Harvard Business School in 1989.

Later, he was a recipient of the Harvard Business School's Alumni Achievement Award. After holding a number of medical positions in Switzerland, he was awarded an honorary doctorate by the University of Basel in 2002. A readership survey of the Financial Times selected Dr. Vasella as the most influential European businessman of the past quarter century.

In addition, Time magazine included him as one of the one hundred most influential people of 2004. He is married and has three children. He was born in Switzerland and speaks three languages fluently. For the fiscal year ending December 2006, his salary was 3, 000, 000 CHF (Swiss franc), or approximately the equivalent of \$2. million USD. He is currently 52 years old.

IV. MAJOR PRODUCTS Novartis is a world leader in providing medicines to improve people's well being and cure them from diseases. Novartis's many products target different people and animals' needs. Novartis is comprised of four business divisions: pharmaceuticals, vaccines and diagnostics, Sandoz Generics, and consumer health. **Pharmaceuticals Division** The Novartis Pharmaceuticals Division is a world leader in the discovery, development, manufacture, and marketing of prescription medicine.

Prescription drugs account for 60% of Novartis' revenues. Their current product portfolio includes more than 40 key marketed products, and their development portfolio involves over 130 projects in various stages of clinical development. Product categories and descriptions are as follows:

Cardiovascular & Metabolism: Products to treat cardiovascular disease, particularly high blood pressure (hypertension), elevated cholesterol

(hyperlipidemia), chest pain (angina pectoris) and heart failure.

Neuroscience: Treatments for disorders that include Alzheimer's disease, Parkinson's disease, attention deficit / hyperactivity disorder, epilepsy, depression, migraine and schizophrenia.

Respiratory & Dermatology: Medicines for important respiratory and dermatological conditions. ABGHI (Arthritis, bone, gastrointestinal, hormone replacement therapies, urinary incontinence): Treatments for patients with a variety of internal diseases that have significant unmet medical needs, particularly in the areas of gastrointestinal disorders, urinary incontinence, arthritis, osteoporosis and the treatment of pain. Infectious Diseases: Products including anti-virals, anti-bacterials and tropical medicine. Oncology & Hematology: Products for the treatment of a number of different cancers and for cancer complications, Transplantation & Immunology: Products include immunosuppressants and therapeutic products for the prophylaxis of organ rejection. Ophthalmics: Products for the treatment of a number of different ophthalmic diseases.

Vaccines and Diagnostics Division Novartis Vaccines and Diagnostics, created in 2006 following the acquisition of Chiron, comprises two businesses: Novartis Vaccines and a diagnostics business that retains the Chiron name. Novartis offers products that prevent over 20 viral and bacterial diseases. Sandoz Generics Division Sandoz is a leading global supplier of generic pharmaceuticals that develops, produces and markets these drugs along with pharmaceutical and biotechnological active substances. Generic pharmaceuticals account for 15% of Novartis' revenues.

The following figure illustrates sales percentages of types generic products sold. Figure 1.

Sandoz Generic Division Sales Percentages Consumer Health Division

Novartis Consumer Health focuses on creating, developing and manufacturing a wide range of competitively differentiated products that restore, maintain or improve the health and well-being of customers.

Consumer Health is comprises the following business units: Over the Counter: Product categories include cough, cold, allergy, gastrointestinal, dermatological and smoking cessation treatments, as well as mineral supplements. Animal Health: Treatments for the most common pet ailments, such as internal and external parasites, arthritic pain control, renal, heart and allergic diseases as well as insecticides for farm fly and pest control. Medical Nutrition: Products for the medical nutrition market including tube and oral nutrition brands and devices. Gerber: Baby food and baby care products. CIBA Vision: Contact lenses and lens care products.

V. MAJOR COMPETITORS The global pharmaceutical industry tops \$600 billion in sales annually (Hoover's Industry Information, 2007). The top three competitors to Novartis are Johnson & Johnson, Merck, and Pfizer. The following table presents a comparison of sales and relative market share for Novartis and their top competitors. Table 1. Novartis and Top Competitors Sales and Market Share

	Novartis	Johnson & Johnson	Merck	Pfizer
Annual Sales (\$ mil.	36,749.00	53,324.00	22,636.04	8,371.00

36, 749. 0053, 324. 0022, 636. 048, 371.

00 Relative Market Share (based on \$600 bil. industry)6%9%4%8% VI. SALES HISTORY Novartis' sales over the past 5 years have steadily increased from \$23. 1 billion to \$36. 7 billion. Novartis achieved a sales growth of 3% this past year.

Novartis's pharmaceuticals division accounted for \$22. 6 billion in sales while the Sandoz division accounted for \$6 billion of sales revenues. The consumer health division produced \$6. 5 billion in sales and the vaccines and diagnostics division produced \$956 million of sales revenues. Net income has increased from \$4. billion in 2002 to \$5.

3 billion in 2006. Figure 1 presents the relationship between sales and net income over the past five years. Figure 2. Novartis Sales vs. Net Income Novartis distributes a portion of its net income to their stockholders in the form of dividends.

Last fiscal year Novartis distributed over \$2 billion in dividends to their stockholders which equated to \$0. 75 for every share their investors owned. For fiscal year 2006 Novartis's earnings per share (EPS, net income dividend by the weighted average of the common shares of stock) was \$2. 3.

Table 1 presents a comparison of dividends per share and earnings per share over the last five years. Table 2. Dividends and Earnings per Share, years 2002 – 2006. 20022003200420052006 Dividends\$0. 46 \$0. 60 \$0.

66 \$0. 75 \$0. 75 EPS\$1. 71 \$2. 00 \$2. 34 \$2.

62 \$2. 23 VII. MAJOR FACTORS AFFECTING INVESTMENT POTENTIAL In the past few years, the pharmaceuticals industry has been subjected to

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heightened competition from generic drugmakers, unprecedented pricing pressure from payers, and hard-to-control inflation in research and development (R&D) budgets. In addition, the new Medicare prescription drug benefit in the United States is helping to bolster sales. Longer term, new products and an aging population are likely to drive growth in this industry (S&P Industry Information, 2007).

The following paragraphs describe some of these major industry trends. Long-term growth for the pharmaceutical industry depends ultimately on its ability to innovate. R&D spending by large pharmaceutical companies has been rising steadily, but the investment has not led to proportionally greater productivity. New products are emerging more slowly, and at the same time, the growing complexity of drug development is increasing the time needed to bring new drugs to market.

The entire drug development process may take many years (while patent protection is running down), with only a small percentage of candidate drugs surviving the testing and approval process. On average, the industry claims, discovering and developing a new drug takes ten to 15 years and costs \$500 million. Biotechnology is the fastest growing subsector of the pharmaceutical industry. Market researchers estimate that biotechnology accounted for \$58. billion (or 10%) of total global pharmaceutical sales in 2006. Biotechnology products typically command higher prices than traditional medicines because they are perceived to be more efficacious, face limited competition, and because many of them address life-threatening or seriously disabling diseases. Manufacturers' ability to command high prices for patent-protected

biotechnology products guarantees high margins, even if the customer base is smaller than it is for traditional medicines. Payers are voicing concerns about the high prices of some biotechnology drugs, but they have yet to demonstrate strong resistance. As prices escalate, however, tensions are growing.

Vaccines are attracting greater interest amid increased global concern about the spread of infectious diseases. The world leaders in vaccine development seeing significant growth in vaccine sales. Advances in technology are greatly enhancing interest in vaccines, but the vaccines now in the R&D pipeline will likely take a decade to reach the market. The increasingly elderly population presents an opportunity for companies with new treatments for arthritis, heart disease, cancer, and other common conditions in the elderly. The percentage of people over sixty is expected to rise from 10% of the world's population in 2000 to more than 20% by 2050, and drug spending by 55-74 year olds will triple between 2005 and 2015. Another factor affecting the industry is the new U.

S. Democratic Congress that came into power in early 2007. The new Congress is considering changes to Medicare Part D (the prescription drug benefit that took effect in 2006) that would allow Medicare to negotiate drug prices with pharmaceutical companies. VIII. STOCK PRICE DATA AND INVESTMENT ANALYSIS Novartis's stock price moved between \$40 and \$61 between years 2004 and 2006.

The highest price of 2004 was \$50. 77 and the lowest price was \$41. 30. In 2005, the highest price and the lowest price were \$54. 71 and \$45.

63. In 2006, the highest price was \$61. 60 and the lowest price was \$51. 72.

Thus, the price increased approximately 10% each year. The gap between highest price and lowest price in each year was approximately \$10 (Hoover's historical financials, 2007). Figure 3 presents a stock price performance chart, which illustrates that the stock price was steadily increasing between years 2004 and 2006, but had not reached the target price. Between the years 2004 and 2005, analysts gave Novartis three stars meaning investors should hold this stock because total expected return was estimated to be close to the total return of the S Index. After 2006, the sale volumes increased and analysts gave Novartis five stars meaning investors were strongly encouraged to buy this stock (S Stock Report, 2007). Figure 3.

Novartis Stock Price Performance History Analysts expect revenues to increase 5%-6% after June 2007 because the company will gain in Diovan antihypertensive, and in Gleevec. Sales of generic and vaccines show growth because of inclusion of Chiron. In addition, sales of consumer health products should rise in view of analysts. However, sales of Zelnorm treatment for irritable bowel syndrome will be dropped because it will be removed from the U. S. Market.

The gross margins for 2007 are expected to increase to 76. 4% from 75. 2% in 2006 because of higher volume and productivity enhancements such as new molecular entities (NMEs). If Novartis can control R spending, analysts predict Novartis should earn a large profit this year (S Stock Report, 2007). The S Pharmaceuticals Index is positive for Novartis.

Analysts believe that investors will continue to support this sector. Their new products such as new molecular entities (NMEs) are key positive market drivers. Additionally, analysts believe that many drug stocks offer attractive P/E ratios and dividend yields (S Industry Information, 2007). The target price during the next 12 months is expected to be \$68, which was derived by applying a peer level P/E of 17.4 times earning per share. The investment risks and returns estimated by S are in the medium level; however, Novartis can reduce the risk by diversifying its product base and large drug portfolio.

Currently, analysts strongly recommend buying Novartis stock during the next 6 months (S Stock Report, 2007).

IX. CONCLUSIONS &

RECOMMENDATIONS Novartis has a strong diversified approach to healthcare in its four business divisions – pharmaceuticals, vaccines and diagnostics, generics, and consumer health. Its largest and most profitable division, pharmaceuticals, has a strong product portfolio while continuing to invest heavily in R to ensure a healthy drug development pipeline. With pressure on health care budgets around the world, generics have become the fastest-growing sector of the pharmaceuticals industry, taking an ever greater share of the total market.

Novartis has recognized this trend, and through multiple acquisitions, their Sandoz division has become the largest manufacturer of generic drugs in the world. Novartis stock has performed well over the past five years, and analysts are now strongly recommending buying Novartis stock during the next 6 months. In light of these conclusions, Group #4 Planning Analysts strongly recommend to the Investment Board that Novartis be chosen for

further in-depth research for potential investment. REFERENCES S Stock report (2007), Retrieved June 1, 2007, from <http://proxy>.

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