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17 Aug 2020 |

Stockwatch: Takeaways And Ironies From Pandemic Lockdowns

After Big Pharmaceutical Second-Quarter Earnings Announcements, The Impacts Of The Pandemic On The Sector Are Now Clear

by Andy Smith

Lilly's diabetes and oncology franchises epitomize the effects of the pandemic on pharmaceutical sales. For much smaller companies, these effects were magnified.

Eli Lilly and Company*, among the last of the big pharmaceutical companies to announce second-quarter earnings, encapsulated a neat summary of the general effects of the pandemic on specific sectors and franchises. It was a cathartic period, but let's not do it again.

Lilly Provides A few Final Clues

Unusually in earnings season, Lilly's second-quarter revenues of $5.5bn missed analysts' consensus estimates of $5.8bn. The company's revenues were only 2.4% lower than those of the same quarter of 2019 but fell by 6.2% between the ends of the first and second quarters of 2020. The 2.4% quarterly drop over last year was a far cry from the first quarter's 15% rise over the same quarter of 2019. Most companies reported strong first quarters and weak second quarters as the pandemic prompted channel inventory builds ahead of impending lockdowns, and then the working down of that inventory as lockdowns eased. In addition, lockdowns themselves threatened the defensive characteristic of pharmaceutical stocks as fewer patients visited hospitals and clinics. Lilly estimated that decreased customer buying in the second quarter of 2020 resulted in a negative $250m impact while the pandemic-related delay in new patient prescriptions had an additional $250m revenue impact.

At the start of the pandemic, I was concerned by the drastic reduction in US ophthalmology and oncology clinic visits and their knock-on effects on the revenues of companies with significant therapeutic franchises in these areas. Roche Holding AG, for example, had a miserable second quarter with US sales of its drug Lucentis (ranibizumab) for age-related macular degeneration falling by 27.6% over the same quarter in 2019 and by 11.9% between the ends of the first and second quarters of 2020. Roche's pandemic-related misery was deepened by a 4.3% fall in revenues from its top five oncology products that were not subject to biosimilar competition between the ends of the first and second quarters, and a 17.4% revenue decline in its three biggest products that were. While Lilly's oncology franchise comprised 23.1% of its second-quarter sales, I was more worried by its diabetes franchise, which could be subject to the ravages of not just diabetologist and primary care clinic closures, but also the inventory work down of diabetes drugs from the first quarter of 2020.

Oncology To Diabetes's Rescue

In the event, Lilly's second-quarter diabetes revenues fell by 13.4% over the same period in 2019, but only by 6.4% – similar to its total revenues – between the end of the first and second quarters of 2020. Unlike Roche's, Lilly's oncology franchise was a bright spot with second-quarter revenues growing by 6.0% over the same period in 2019 and by 5.6% between the ends of the first and second quarters of 2020. But the growth in this, its second largest franchise, was not enough to offset the weakness in diabetes, its largest. If Roche is considered a biosimilar-impacted outlier, a key takeaway from the pandemic based on the performance of the oncology franchises of *Pfizer Inc.**, *Merck & Co., Inc.**, Lilly and *AstraZeneca PLC* between the ends of the first and second quarters of 2020 was that the oncology therapeutic area was much more robust than the clinic closures towards the end of the first quarter would have suggested. Perhaps oncology clinics were just quicker at reopening than ophthalmology clinics.

While larger companies like Lilly hedged the different risks through therapeutic diversification, smaller companies like *MannKind Corporation* – which has only one product – could not. MannKind's second-quarter Afrezza (inhaled human insulin powder) revenues fell 12.7% between the ends of the first and second quarters of 2020. Similarly, an oncology franchise alone is not enough to weather the pandemic if it consists of only one product. Despite growing 21% in the second quarter compared with the same period in 2019, revenues of *Clovis Oncology, Inc.*'s only product – Rubraca (rucaparib) – fell by 6.3% between the end of the first and second quarters of 2020.

Vaccines And Pandemics

An irony to emerge from the pandemic was its effect on vaccines – which are expected to be the saviors of the world from coronavirus – as their revenues were hit the hardest. This was presumably because of the fall in travel, preventative and scheduled vaccinations resulting from few in-person visits to primary care clinics. There is a nightmare Catch-22 scenario in there somewhere.

Pfizer was the first to highlight this dynamic with a 22.6% fall in vaccine revenues between the ends of the first and second quarters of 2020. But Pfizer's vaccine division contributed only

10.6% of its total second-quarter revenues. GlaxoSmithKline plc's vaccine division however, made up 14.9% of its second-quarter turnover. GSK reported second-quarter 2020 vaccine revenues that fell by 28.5% over the same period in 2019 and by 37.2% between the end of the first and second quarters 2020. So, while GSK's second-quarter total turnover fell by 2.4% over the same period in 2019 – as did Lilly's – GSK's larger vaccine division resulted in total turnover falling by 16.1% between the ends of the first and second quarters of 2020 whereas Lilly's fell by 6.2% in those three months. Merck reinforced the effect of the pandemic on vaccine businesses when it reported the second-quarter revenues of its five key vaccines. These grew by 0.7% over the same period in 2019, but fell by 8.3% between the ends of the first and second quarters of 2020.

Small Commercial Companies Are Not Beautiful in Pandemics

In the same way as revenues of small oncology or diabetes franchises were much more susceptible to pandemic pressures than those of larger and more diverse franchises at big pharmaceutical companies, small commercial vaccine companies might be particularly exposed in a pandemic. Despite its early-stage pandemic research collaborations, the second-quarter sales of Dynavax Technologies Corporation's Heplisav-B (recombinant adjuvanted hepatitis B vaccine) fell by 71% over the same period in 2019 and by 77.1% between the end of the first and second quarters of 2020, leaving Dynavax with the wrong product at the wrong time.

Andy Smith gives an analyst and former investor's view on life science companies. He joined the independent research house Equity Development in October 2019 having previously been an analyst at Edison group and a Senior Principal in ICON PLC's Commercialization, Pricing and Market Access consulting practice. Smith has been the lead fund manager for four life science–specific funds, including 3i Bioscience, International Biotechnology and the AXA Framlington Biotech Fund, and was chief investment officer at Mannbio Invest. He was awarded the techMark Technology Fund Manager of the year for 2007 and was a global product manager at SmithKline Beecham Pharmaceuticals until 2000.

*Andy's pension funds hold Lilly, Merck & Co. and Pfizer.