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Biotech

Biotechs look to sell royalties to raise cash in a tough market

Companies look for alternative sources of funds after share sell-off

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Biotechs are turning to specialist royalty companies to generate cash from future sales of their products, as they try to survive a dramatic sell-off in the sector.

Companies such as Royalty Pharma, Healthcare Royalty Partners and Blackstone Life Sciences are among those looking to acquire royalties for approved drugs or those in late-stage development.

Others are opening up newer areas of the market, such as Xoma pushing into earlier stage royalties, and Zai Lab buying rights to sell drugs in China.

Clarke Futch, chief executive of Healthcare Royalty Partners, said inquiries from biotechs about royalty sales had risen 50 per cent since the second quarter and that he expects to do more deals than usual this year.

"There has really been a pretty dramatic acceleration in the level of interest. Companies that maybe last year had a $5bn market cap, and today, that's $2bn, are much more interested in royalty options than they were 12 or 24 months ago."

The S&P XBI index of smaller biotech companies has fallen 41 per cent since November, after valuations shot up during the coronavirus pandemic.

But the private debt market — including venture debt and royalty streams — is up 23 per cent year on year, according to life sciences investment bank Torreya.

Pablo Legorreta, chief executive of Royalty Pharma, said interest in royalty deals rose more than 50 per cent between 2019 and 2021.

"Pressure on biotech equity prices could expand the universe of partners and royalty opportunities, increase the attractiveness of royalties versus financing alternatives and result in consolidation," he told the Financial Times.

In May, Royalty raised its capital deployment target to $10bn-12bn over the next five years, up from a previous target of $7bn set in February 2021.

Nick Galakatos, head of Blackstone Life Sciences, said there is more interest in selling royalties because the supply of capital from the public market has fallen dramatically. Blackstone has done large deals that combine equity, debt and royalties to push specific drugs through clinical trials.

"The demand for capital continues to grow unabated because innovation continues. It doesn't matter if the markets are being rocked by global economic uncertainty, invention at academic centres at Oxford, Cambridge, MIT or Harvard continues."

In a royalty deal, a biotech company sells rights to the revenue from a product made in partnership with a large pharmaceutical company, while a "synthetic" royalty deal involves rights to future sales of a product it is aiming to bring to market on its own.

Royalty Pharma has done synthetic royalty deals with companies including Biohaven, acquired this year by Pfizer, and Immunomedics, which was bought in 2020 by Gilead. It says synthetic royalties are a growth opportunity for the company. In the past five years, they made up only 2 per cent of capital raised by biotech companies, but Legoretta said there is a "strong case" they should be a core part of capital structures.

Antoine Papiernik, chair of venture capital firm Sofinnova Partners, said the strategy was "very good" for companies that did not have partnership opportunities with big pharmaceutical companies and wanted to bring their products to market.

"You are cutting some of the upside by doing a royalty deal but you are getting cash upfront."

But one healthcare banker said that royalty companies wanted big returns, especially if they funded their deals with debt. "As the cost of debt increases the required returns to do those deals higher and higher," he said.