

A Twisted Deal Structure: Johnson & Johnson to Acquire Actelion for \$30bn in Cash

Johnson & Johnson (NYSE: JNJ) — market cap as of 10/02/2017: \$310.36bn

Actelion (VTX: ATLN) – market cap as of 10/02/2017: CHF 28.13bn

Introduction

On the January 26, 2017, the US healthcare behemoth Johnson & Johnson announced the acquisition of the Swiss biotech company Actelion for \$30bn in cash. The final arrangement came after months of negotiations, which had even halted in December 2016 because of lack of agreement over the purchase price (which J&J raised from \$20bn to \$30bn over the past three months).

About Johnson & Johnson

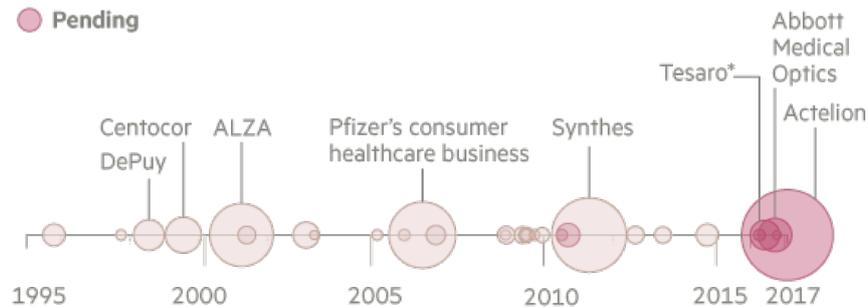
Johnson & Johnson is a leading provider of consumer health, pharmaceutical and medical products. Incorporated as a holding in 1887, it operates through 250 subsidiaries in 60 countries.

Johnson & Johnson has been active in the M&A market, pursuing an external growth strategy directed to both small and large firms. Some of its most important deals include the acquisition of Novira Therapeutics, a company focused on treatments for Hepatitis B infections, and the purchase of two medical devices producers, NeuWave Medical and Coherex Medical. Furthermore, in September 2016 J&J acquired Abbott Medical Optics for \$4.3bn, in a move to increase its scope in the eye care industry.

J&J's largest acquisitions

Deals value (\$bn)

- Completed deals
- Pending



*Commercial rights for Tesaro's Niraparib drug, which is used to treat prostate cancer

Source: Dealogic

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About Actelion

Actelion is a Switzerland-based biotech company specialized in the treatment of rare diseases and it holds a strong leading position in the European market for drugs to treat such diseases. The company was founded in 1997, when a small group of researchers and managers walked away from Roche and decided to pursue the discovery of innovative drugs to cure hypertension. In 2000, Actelion went public with its shares listed on the SIX Swiss Exchange.

In 2001, after an unsuccessful study on a drug acting on vascular resistance and cardiac functions, the shares and the company's future growth prospects went south. However, by the end of the year Actelion was able to recover

thanks to the licensing of its first marketed product, Bosentan, used in the treatment of pulmonary artery hypertension. Since then, Actelion has shown a sound base of growth: last year, it delivered a strong performance with sales rising to CHF 1.7bn, an increase of 14% on a year-on-year basis.

Moreover, growth was reflected in the rise of diluted EPS measure, which rose 32% with respect to the previous year.

Deal Structure

Johnson & Johnson will acquire all Actelion outstanding shares by means of a public tender offer to be launched on February 16, 2017. The Swiss company's shareholders will be offered \$280 per share for a total value of \$30bn, a 23.2% premium on the company's closing share price on the day prior to the announcement.

The deal will also see Actelion's R&D unit spun off, thus leading to the creation of an "R&D NewCo" whose ownership will be structured as follows: the company will be listed on the SIX Swiss Exchange with a market cap of \$1bn and Actelion's current shareholders will receive in the form of stock dividend one of the new company's shares for each Actelion share they own. Furthermore, Johnson and Johnson will be able to share in the upside of R&D NewCo by retaining a significant 16% minority interest, with the option to double it to 32% in the future. The tender offer structure of the transaction suggests the willingness of the parties to close the deal quickly, in order to avoid additional costs coming from delays or threats posed by rivals: as opposed to traditional one-step mergers, tender offers usually lead to a faster conclusion of the deal by avoiding lengthy processes like additional filings and regulatory approvals.

Deal Rationale

J&J's strategy of acquiring only the mature, well-established branch of Actelion aims at expanding its main consumer, medical device and pharmaceuticals segments by adding to its portfolio of drugs the Swiss company's ones. In this way, the US company will be able not only to take advantage of new markets and growth opportunities, but also to effectively face significant threats to its profitability. For instance, revenues generated by the Remicade – a J&J's lucrative drug to treat arthritis – fell 24% in 2016 with respect to 2015 levels, as it a cheaper Pfizer's product has been driving down prices.

Partially excluding early-stage experimental drugs through the spin-off of Actelion's R&D unit comes as a way to satisfy a twofold need of the parties. First of all, spinning-off the division will allow the current Actelion top management to maintain control over it, a condition which kept several potential bidders away from finalizing previous agreements. In the words of Actelion chairman Jean-Pierre Garnier, "a complete takeover of the company would not allow us to grow those fragile flowers (early stage drugs)", since most of the times pharma megadeals lead to the elimination of undergoing experimental projects for cost-cutting needs. In a second instance, the spin-off will let Johnson & Johnson focus on established high-price, high-margin drugs for rare diseases brought in by Actelion's mature business.

Furthermore, the transaction will also bring immediate tangible value to the US company's shareholders: the deal is indeed expected to be accretive to J&J's adjusted EPS in the first full year, by an amount ranging from \$0.35 to \$0.40. On a long-term basis, revenue and earnings growth rates are expected to go up by at least 1.0% and 1.5% - 2.0% respectively. The fact that Johnson & Johnson will retain a significant minority stake into the new standalone company expands the financial benefits of the transaction to the potential upside of the former Actelion R&D unit.

Analysts, on the other hand, have argued that the transaction is clearly overpriced with respect to comparable transactions. The high premium can be actually explained as a way to defeat competitive bidders, but most

importantly as an efficient use of the significant amount of cash that Johnson & Johnson held offshore: being held outside the US, the cash used to finance the acquisition will indeed incur no tax.

Market Reaction

On the day of the announcement, Actelion's shares climbed to CHF 271.60, a 22% increase with respect to the previous day signaling strong investor confidence in the value of the deal.

On the other hand, Johnson & Johnson's share price decreased by 0.8% to \$111.84 on the same day.

Advisors

Lazard acted as leading financial advisor to Johnson & Johnson, assisted by Citibank too. Actelion is being advised by Bank of America Merrill Lynch and Credit Suisse.

Tags: Johnson & Johnson, Actelion, M&A, USA, Switzerland, tender offer, spin-off, R&D, pharma, drugs, lazard, citi, baml, bank of america merrill lynch, credit suisse