US Financial accounts reports

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ALZA Corporation (NYSE: AZA): Results for the nine months to 30th September, 2000

ALZA was part of the biotechnology industry before the term even existed. Founded in the late 1960s by one of the great names in the industry, Alejandro Zaffaroni, for many years ALZA developed its drug delivery technology and licensed it to the pharmaceutical industry. This created a healthy revenue stream but one largely based on royalties. The ALZA executives realised many years ago that a royalty-based revenue stream left the company at the whim of the licensee. In 1993 over half ALZA's revenues came from royalties and of that over 60 per cent arose from one product, Procardia, licensed to Pfizer and Bayer; far too many eggs in one basket. Consequently the decision was made to turn ALZA into a fully integrated pharmaceutical company, with its own product range and salesforce.

The results for the nine months ended 30th September, 2000, show just how far the company has come. The nine month revenue figure of US$727m (up 20 per cent on the prior year) suggests ALZA will this year achieve its target of becoming a 'billion dollar' company. More significantly, royalties now account for only around 30 per cent of total revenues with product sales contributing 60 per cent. The increasing emphasis on own product sales has brought with it the benefit of increasing margins, with the gross margin on net sales in the third quarter of 2000 increasing to an all-time high of 71 per cent. Net income for the nine month period increased by 17 per cent on the same period last year (excluding US$33m of merger-related charges in 1999).

ALZA has achieved this transformation by following a number of clear, distinct strategies, many of which were demonstrated over the past nine months. One of the most significant of these was the announcement in September that ALZA was exercising its option to acquire all the outstanding share capital of Crescendo Pharmaceuticals. Part of ALZA's approach to developing its own products has been through the establishment of special purpose entities and Crescendo was the most recent of these. Crescendo was established as a stand-alone, publicly traded company in 1997 with a licence to ALZA's E-TRANS and DUROS technology along with US$300m from ALZA. The Crescendo collaboration has resulted in the development of several products including Viadur, a treatment for advanced prostate cancer and E-TRANS fentanyl, for acute pain management.

Co-promotion agreements have also been key to the expansion of ALZA's product sales revenues, and the deal with Bayer in May is an example of this. Under the agreement ALZA will co-promote Bayer's Avelox in the US, while Bayer will promote ALZA's Ditropan XL.

In order to secure co-promotion agreements, ALZA has obviously needed to build up a strong salesforce. This it has done and the company now boasts some 400 sales and marketing staff, a substantial number of whom joined ALZA through the acquisition of SEQUUS Pharmaceuticals at the start of 1999.

A salesforce obviously needs products to sell and, as well as developing its own products and entering into co-promotion agreements, ALZA has adopted a strategy of acquiring product rights withing its core therapeutic areas of oncology, pain relief and urology. The acquisition of SEQUUS was consistent with this strategy, giving the company the cancer treatment Doxil. Doxil is ALZA's second highest earning product, although sales growth has been somewhat

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disappointing. Sales of the treatment for overactive bladder, Ditropan XL, however, are outstripping expectations and reached US$127m in the nine months to September 2000. Also looking very promising is Concerta, the company's treatment for Attention Deficit Hyperactivity Disorder which was launched in the third quarter of this year. Sales in this period amounted to US$24m. It is worth noting that ALZA's largest single source of revenues now is from its own product, Ditropan XL, accounting for 17 per cent of total revenues. This compares very favourably to the situation in 1993 when 30 per cent of revenues came from Procardia royalties and gives an indication of the strong progress made by the company over recent years.

ALZA signalled that progress has not stopped when it successfully raised approximately US$600m in July 2000 through the issue of convertible subordinated debentures. Part of the funds raised will be used to make the US$100m payment to acquire Crescendo.

This financial year started on something of a low note for ALZA. The abandonment of the merger with Abbott could have had a lasting negative impact on the company. The news flow through the year does not indicate any sign of that having happened and indeed, after a 25 per cent fall in the share price in December 1999 following the Abbott announcement, the company's share price has grown steadily and has more than doubled during 2000. The company is now valued at about US$10bn. The transformation of ALZA may not yet be complete, but it is certainly a very different and much stronger company compared with a decade ago.

November 2000

Millennium Pharmaceuticals, Inc. (Nasdaq: MLNM): Results for the nine months to 30th September, 2000

Millennium is widely regarded as one of the stars of the biotechnology industry. Founded only seven years ago, it has grown to a market capitalisation that approached US$20bn early in 2000, although it has fallen back in recent months with the general technology decline.

The company is the 'boy-band' of the biotechnology industry in that, to some extent, it was manufactured. In 1993, CEO Mark Levin and colleagues at the Mayfield Fund tracked down four of the leading experts in the genomics field at the time and brought them together at Millennium. Levin then set about raising funds to build an 'industrial genomics' company. The company began by identifying genes and trying to determine related targets using bioinformatics and high-throughput screening techniques. The key to Millennium's success is that it managed to establish some significant alliances early in its development. The company's list of partners now looks like a who's who within the biopharmaceutical sector.

The team at Millennium realised at an early stage that the provision of genetic data and target identification would very quickly become commoditised and so have adopted a policy of continually moving downstream to the higher value end of the drug development process. Key to that strategy was the acquisition of Leukosite around the turn of 1999. This gave the company six products in the clinic, including Campath, an antibody treatment for chronic lymphocytic leukaemia currently being reviewed by the US Food and Drug Administration (FDA). Campath is being developed through a joint venture with ILEX Products, Inc.

Further evidence of Millennium's intent on building its drug discovery and development capabilities was demonstrated in September 2000 with the acquisition of Cambridge Discovery Chemistry (CDC), based in Cambridge, England, for US$53m cash. The acquisition will significantly enhance the company's medicinal and computational chemistry abilities.

The cornerstone of Millennium's success, its alliance network, continued to develop during the first nine months of 2000 with new or expanded agreements with Caliper Technologies, Biacore, Abgenix and Eli Lilly.

Probably the most significant agreement during the year was the alliance with Aventis Pharma, announced in June 2000. This has been billed as a truly collaborative effort between the two organisations as opposed to the common biotech–pharma relationship of licensor–licensee. Under the agreement, Aventis will make payments to Millennium of up to US$200m over five years in exchange for rights to Millennium's drug discovery technologies. In addition, Aventis made a US$150m equity investment in the company and will make two further US$50m investments in 2001. An agreement such as this reflects both Millennium's increased negotiating power and the ever-increasing dependency of the large pharmaceutical companies on the biotechnology industry to fill their pipeline.

The increase in research and development activity through the acquisition of Leukosite and CDC, as well as a general expansion in activity, was reflected in the increased loss for the nine month period of US$204m, as compared to US$1m for the same period in the prior year. R&D expenses increased by around US$78m to US$191m, and general and administrative expenses increased by approximately US$10m. In addition the company recorded a US$39m charge for amortisation in connection with the Leukosite acquisition. The loss also includes one-off charges of US$46m, relating to the acquisition of the remaining outstanding shares of Millennium Predictive Medicine from the company's erstwhile partner in the venture, Becton Dickinson, and a US$49m charge relating to the conversion of debt issued earlier in the year.

In common with many of its US peers, Millennium has had a bumper year for fundraising, with about US$1.4bn sitting in the bank at the end of October. In January the company raised US$400m through the issue of convertible debt. In the third quarter US$275m of the debt was converted into equity. Millennium paid debt-holders a US$49m sweetener to induce conversion. In October, the company successfully raised a further US$767m through a common stock offering, despite the fact that the market for technology stocks had turned by this stage.

The past twelve months have seen Millennium take a number of significant steps towards its transformation from a toolbox company to a platform-based drug development operation. Having established a European bridgehead with the acquisition of CDC, it is likely we will see the company making further forays into Europe on the acquisition trail. The strong cash position leaves the company well placed to continue to pursue its strategy of moving downstream in the drug development process, and with a good drug development pipeline Millennium is likely to remain a significant player in the biotechnology industry for some time.

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