
EU Financial accounts reports

David Citron

Galen Holdings plc: Results to December 2000

Galen, the specialty pharmaceuticals group, added to its London and Irish Stock Exchange listings with a listing on the US Nasdaq exchange in September 2000 as a result of the acquisition of a US rival, Warner Chilcott.

Even for the year to September 2000, prior to the inclusion of Warner Chilcott, Galen's results indicated growth and continued profitability. At £86m, sales were up 28 per cent. These were more or less equally divided between the group's two main business segments – pharmaceutical products and the provision of pharmaceutical research services. In the former the company markets a range of brands, including therapeutic areas such as analgesics, gastrointestinal, respiratory, cardiovascular and antibiotics. Gross margins approximated 50 per cent in both segments and, with a continued low tax charge of only 25 per cent, earnings per share exhibited a strong 23 per cent increase for the year.

The £308m Warner Chilcott acquisition has transformed the group, however. This was reflected for the first time in the December 2000 quarter's results which showed a virtual doubling of sales revenues to £42m and a sharp increase in gross margin to 65 per cent. This improvement did not filter down to the pre-tax profit level which saw a deterioration from £5.2m to £2.8m. This was primarily due to the quarter's amortisation charge relating to the £272m goodwill that arose on the acquisition. Ignoring this new expense item, earnings per share in fact grew by 34 per cent in the December 2000 quarter.

Much of the value of the Warner Chilcott acquisition no doubt lies in future growth prospects. In January 2001 Galen obtained

indicative UK approval for a key new product, the intravaginal ring (IVR), a means of delivering hormone replacement therapy. With the worldwide value of this market estimated at \$4b, Galen was hoping for a European launch by mid-2002, with US approval hopefully following not too long thereafter. This important new product development dovetails well with the Warner Chilcott acquisition which will provide Galen with ready access to the large US market.

While the company's R&D services operation is no longer an equal partner in the new structure, it did spend £10m on acquisitions in that area in the year to September 2000 and has not yet indicated an intention to exit the business.

Galen's recent share price performance has reflected these positive developments with its strong out-performance of the FTSE All Share index since mid-2000. The conditional IVR approval gave the share price a strong boost and the announcement of the good December quarter results produced a 3.3 per cent increase to 860p. Between then and the time of writing (22 February 2001) the price has increased a further 9.6 per cent to 942½p, reflecting the growth potential inherent in existing products, in the new IVR drug delivery platform and in potential new acquisitions.

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Smith & Nephew plc: Preliminary results announcement for 2000

Embarking on a major new strategy since 1998, Smith & Nephew had virtually completed its restructuring by the end of 2000. While its shares had hovered around the 180p mark for about four years up until the spring of 2000, they have since then shown remarkably strong and consistent

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growth. By the end of February 2001 they were up 80 per cent at 326p.

The new Smith & Nephew is a more focused group that develops and markets advanced medical devices. It has restructured both its business and its finances.

Following the expected disposal of its ear, nose and throat business around the middle of 2001, the group will comprise four business segments: orthopaedics, endoscopy, advanced wound management and rehabilitation. A key move towards this structure was the June 2000 disposal of consumer business to Beiersdorf AG for £210m. In addition at the end of 2000 it combined its traditional wound-care casting and bandaging business with that of Beiersdorf into a 50/50 joint venture with that company.

The cash from the consumer business disposal enabled payment to shareholders of a one-off special dividend of £416m in August 2000. This resulted in a reduction in capital and reserves as well as increased net debt to £236m at the end of 2000. This produced a high net debt/equity ratio of over 70 per cent at the end of 2000 compared with the company's traditional 10 per cent over the last five years. Interest cover remains very strong, however, and the company says it could raise substantial additional borrowings to fund major acquisitions.

Total sales for 2000 came to £1.1bn, although £0.3bn of these came from discontinued businesses or those that will become part of the Beiersdorf joint venture. Operating profit from ongoing operations grew 24 per cent to £143m. With so many changes under way, a valid year-on-year comparison is fraught with difficulties. The company itself puts its pre-exceptional underlying earnings per share growth for 2000 at 15 per cent. However the dividend payout (ignoring the special dividend mentioned above) was down 43 per cent, reflecting the company's objective of retaining cash for growth.

In its February 2001 preliminary statement Smith & Nephew reiterated its new target of achieving 'an annual

percentage increase in underlying earnings per share in the mid-teens for the three years from 2002.' Recent share price performance shows that the market believes this objective to be attainable.

February 2001

Weston Medical Group plc: Results for six months to 30th June, 2000

Weston Medical floated on the London Stock Exchange during the tempestuous times of 2000 which witnessed such volatility in equity prices. Nevertheless its share offer was oversubscribed. The company raised £47.8m net, enabling it to repay £9.4m of loans. The flotation was a success not only for the company itself but also for its venture capital backers (3i, Phildrew Ventures and Nomura) as well as some employees who between them realised over £20m through share sales (see *The Times*, 4th May 2000).

The company has one key product, a prefilled, disposable needle-free syringe. This is currently licensed to five leading pharmaceutical companies including Roche, Glaxo SmithKline, Pharmacia and Celltech Medeva.

Weston's market value has witnessed its own share of volatility since that May 2000 float at a price of 170p per share. By the time of the release of its June 2000 interims in September 2000 its price had risen by one-third to 226p. While these interim results showed a modest 7 per cent increase in turnover to £0.9m, the £8.4m operating loss for the six months had increased four-fold over that of the corresponding period the year before. It is worth pointing out, however, that fully £5m of that operating loss was a charge relating to employee share options and related National Insurance levied on these. This is in accordance with UK accounting practice which requires the excess of market value at the date of an award of share options over the exercise price to be charged against profits over the period to which the employees' performance relates. This £5m charge was

seven times greater than the corresponding amount for the first half of 1999.

Since much of the operating loss related to this share options charge, which is a non-cash item, the operating cash outflow for the period was significantly lower at £2.4m. Weston Medical's June 2000 balance of cash at bank stood at a healthy £41m.

Weston's share price peaked at 272½p in January 2001, but by early February it had lost one-third of this value, much of the drop being due to the discontinuation of its licensing agreement with Johnson & Johnson. This was entirely the result of a strategic product decision taken by the large

pharmaceutical partner and not because of any problems with Weston's own product technology. Nevertheless the loss of potential revenues and the narrowing of Weston's list of partners was sufficient to cause a sharp mark down in share price.

In September 2000 Weston was projecting its first significant sales by 2003. The group's cash position looks good. However, much will depend on its ability to manage the process of gaining regulatory compliance, develop partner relationships and expand its manufacturing capability to commercially required levels.

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