
Pharmaceutical Outlook 2021

Credit outlook remains stable. Favourable long-term trends and the boost from pandemic-related spending give the outlook a positive bias amid robust sales growth and healthy profit margins.

Pharmaceutical, Scope Ratings GmbH, 7 January 2021



Executive summary

The credit outlook for the global pharmaceutical sector in 2021 remains stable if not slightly more positive than a year ago.

The industry will continue to benefit from favourable demographic and lifestyle factors, innovations and a diminishing threat from expiring patents in addition to the shot in the arm for the whole sector from the Covid-19 pandemic whose impact goes beyond the vaccines segment.

The main trends we expect for 2021 are:

- Healthcare awareness among large parts of the global population has significantly increased in the course of 2020, triggered by the coronavirus pandemic.
- Demographic and lifestyle factors – such as ageing populations, diet-related illnesses in developed countries, growing prosperity in emerging markets - continue to underpin the sector's robust sales growth, set to run ahead of economic growth in many countries.
- Vaccine manufacturers are the main pharmaceutical-sector beneficiaries from the Covid-19 crisis, though other sub-sectors – such as diagnostics, over-the-counter (OTC) drug and medical-product manufacturers - are also beneficiaries of efforts to combat the pandemic and the consequences of full and partial lockdowns to reduce its spread.
- Pharmaceutical companies continue to focus on faster growing treatment areas which are less vulnerable to fierce competition such as (immune-) oncology and rare diseases.
- Pricing pressure further intensifies in mass-market, less innovative segments such as cardiovascular or diabetes.
- Governments are increasing their activity in the sector, most recently as stakeholders in vaccine businesses, but we don't see this as disruptive to business models.
- Ratings have held up in the present crisis and will continue do so through 2021.

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Key trends for 2021

Healthcare awareness among large parts of the global population has significantly increased in the course of 2020, triggered by the coronavirus pandemic, which will underpin the sector's robust sales growth, set to run ahead of economic growth in many countries.

Demographic and lifestyle factors – such as ageing populations, diet-related illnesses in developed countries, growing prosperity in emerging markets – are also crucial factors supporting sales growth.

Vaccine manufacturers are the main pharmaceutical-sector beneficiaries from the Covid-19 crisis, though other sub-sectors – such as diagnostics, over-the-counter (OTC) drug and medical-product manufacturers - are also beneficiaries of efforts to combat the pandemic and the consequences of full and partial lockdowns to reduce its spread.

Pharmaceutical companies continue to focus on faster growing treatment areas which are less vulnerable to fierce competition such as (immune-) oncology and rare diseases. Pricing pressure further intensifies in mass-market, less innovative segments such as cardiovascular or diabetes.

Governments are increasing their activity in the sector, most recently as stakeholders in vaccine businesses, but we don't see this as disruptive to business models.

Ratings have held up in the present crisis and will continue do so through 2021.

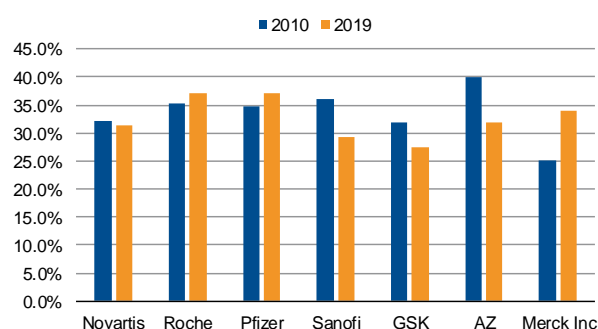
Covid-19 crisis puts sector in the spotlight

While the pharmaceutical industry, in particular, has grappled with a negative public image in the recent past – think of high drug prices, limited innovation rates - the present crisis provides a welcome catalyst to change popular perceptions profoundly. The industry has understood this. Several companies have developed or are close to developing and distributing partly innovative exploratory new vaccines in record time. Governments have been ready to help, given the importance of the vaccines for public health. They have poured large sums of money into the vaccine sector, in various forms. The German government took a EUR 300m stake in vaccine maker Curevac AG through state development bank KfW. Other vaccine developers in Europe and the US benefited from investment incentives and grants - as well as massive government pre-orders for which they received customer deposits - as governments increased spending on healthcare in general, amounting to 5% of all extra pandemic-related expenditure in OECD countries¹. While there appears to have been no maximum price condition set for receiving government support to develop a coronavirus

vaccine and accept large delivery contracts, some vaccine producers such as AstraZeneca have voluntarily committed to a “no profit” policy in marketing of Covid-19 vaccines.

If the industry can use this opportunity to position itself as a partner of governments and efficient “rescuer of society,” we believe this might unlock further significant growth potential – and possibly less price regulation in the future. While the latter is commonly cited as a risk factor for the industry, in reality, it is decades since it has left any trace on average industry profitability (see Figure 1).

Figure 1: Top pharma companies' EBITDA margins 2010 and 2019



Source: Scope Ratings

Crisis – what crisis?

As every crisis has its opportunities, we think the pharmaceutical sector will definitely benefit in the midterm from the opportunities provided. We see two main elements here.

First, there are the direct effects for any company involved in the manufacturing and distribution of the new vaccines. Secondly, in a wider sector context, we see generally positive demand stemming from increased health awareness in the general population and renewed trust in pharmaceutical products as a result of the crisis. This has also affected demand for OTC products and health-related nutrition. In addition, laboratory-equipment and services providers such as Merck KGaA – via its life sciences division (Sigma-Aldrich) - have already benefitted from increased demand significantly.

Healthcare providers are taking advantage of newly emerged trends like digitalisation and “e-health” innovations enabling easier out-of-hospital drug administration. The crisis is still a burden for the healthcare sector at a large – from the pressures on hospitals to the constraints of lockdowns and an reduced patient-doctor interaction – but we believe the likely full-year effects for 2020 will not be as dramatic as for most other industries.

¹ See: [How COVID-19 has reversed longer-term trends in the social contract in OECD countries, at least for now | The OECD Forum Network \(oecd-forum.org\)](https://www.oecd.org/forum/2020/04/how-covid-19-has-reversed-longer-term-trends-in-the-social-contract-in-oecd-countries-at-least-for-now/)

On the contrary, many companies have a good chance to lock in additional growth provided not just by increased health care awareness but also the likelihood that the present crisis will not be the last virus-related one the world experiences. These pharmaceutically favourable effects for the mid-term will add to the already high growth potential for the sector as countries grapple with ageing societies and people's less healthy lifestyles.

Lessons learned – the supply chain factor

The initial stage of the Covid-19 crisis early in 2020 abruptly highlighted the danger of being dependent on only one or very few suppliers. To be sure, the risk of individual companies' over-dependence on suppliers in China or India did not materialise, but, in the grander scheme of things, it was one of the factors identified in the crisis which could have resulted in much more disruption to the global healthcare sector. France's Sanofi SA has committed to keep its sizable raw materials production for drug development in Europe, whereas some competitors remain exposed to supply-chain disruption by relying only on emerging markets for sourcing.

A second lesson learned related to the industry's reliance on face-to-face visits between doctors and, from the commercial standpoint, the sales staff of drug makers marketing newly approved treatments, or, from the healthcare perspective, with patients from the point of view of hospital-based drug administration. The Covid-19 crisis has shown the need for greater adaptability, flexibility and reforms in this crucial interface in the sector. New trends of digitisation and e-healthcare services to support patient monitoring at home will be a welcome change to less flexible pre-Covid practices.

A separate lesson for the sector is the example of the pharma companies which have successfully concentrated on a few treatment areas like oncology, immunology and rare diseases, partly through targeted acquisitions. Take AstraZeneca PLC's recently announced US\$39 bn takeover bid for Alexion Pharmaceuticals Inc. which has focused on rare diseases and had recorded yearly growth rates of about

20% for the past five years. This strategy of focusing on high-growth medical areas, now complemented by vaccines, makes sense in our view from multiple angles. The approach allows companies to avoid more crowded treatment areas with strong pricing pressure like diabetes or cardiovascular drugs. The approach also enables them to realise significant growth and higher prices in a generally more protected commercial environment given the narrow range of competitors. The rare disease or orphan drug market is projected by EvaluatePharma to grow by a compound annual growth rate of 10.8% until 2026, about twice as much as the underlying pharma market.

Annex I: Related research

European corporates: creditors, taxpayers bear Covid-19 financial burden; will shareholders in 2021?
published Dec 2020 available [here](#)

Pharmaceutical sector: Covid-19 vaccine breakthroughs promise politically sensitive windfall profits
published Nov 2020 available [here](#)

Global Healthcare Quarterly: Covid-19 tests industry's resilience; might it enhance its reputation?
published Oct 2018 available [here](#)

Scope affirms A-/Stable issuer rating on Merck KGaA, published Oct 2020, available [here](#)

Scope affirms Sanofi at AA, Stable Outlook, published Sep 2019, available [here](#)

Global Healthcare Quarterly: Covid-19 tests sector but creates opportunities, published Jun 2020, available [here](#)



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