ALANTRA

Ep.4: Building Success in Consumer Health with Chris Harley-Martin

Rusty Ray (00:05):

Hi, I'm Rusty Ray with Alantra, I head up the US Healthcare Investment banking team here in New York, and you are listening to Crossroads, our podcast that focuses on interesting products, technologies, and services in the healthcare space, all with an eye toward M&A.

(00:21):

Today, we're joined here with Chris Harley-Martin, former head of GSK's consumer health BD team. And we're going to pick up on our prior conversation where we talked about trends and observations with the consumer health space as it relates to M&A product portfolios and what's happening. We want to look at a different topic now, maybe press on the idea a little bit deeper and think about what sellers look for when they're evaluating divestitures. Are there regional differences and portfolio optimization as it relates to different geographies and categories?

(01:00):

This brings us to a conversation around differences between the US and EU markets, what the opportunities are as well as the challenges between those markets and how a new trend has emerged where private equity platforms are going with an asset-lite model using a lot of third-party providers. Everything from brand management to logistics to manufacturing to marketing and product development, and really everything in between, and how that's led to some tremendous successes in the space for those folks and some really successful exits.

(01:36):

I think as the strategies around acquiring brands, growing consumer health platforms, especially in the OTC space, it's not just cash, it's not just a good management team because there are many folks out there that meet those criteria. I think it's having a different perspective. It's trying to understand what the seller needs to achieve through divestment, how you're simplifying their lives, making their lives easier, and how it becomes a bit more of a collaborative process and hence maybe a more structured deal than a straight acquisition.

Chris Harley-Martin (02:11):

Yeah, I can see that. We can see that. And also what problem you're solving for the seller, because if there's no incentive necessarily for them to offload brands and businesses, they need to be sold on the idea that there's a problem to be solved here. Whether that's a declining asset dragging down the business, or issues that are likely to become problems in the future, regulatory, manufacturing, or just the very fact that there is a better use of the capital, but maybe over time, and actually it's a structured transaction that allows people to think about how they manage that cash flow towards some future that they might want to realize. I think the other observation I have is that regionally it can be quite different. You've got assets in Europe owned by private equity, Bain / Cinven with STADA, EQT with Karo, CVC until recently with Cooper.

(02:59):

There have been roll ups of brands, but not exits yet. I'm kind of curious to see how the thesis evolves when and if there are exits. Some of them are obviously banking on IPOs. Galderma was a good example. That was timetabled for IPO. But clearly the environment today in September 2022 is perhaps not conducive towards that. Whereas in the US, I still see some real motivation to consolidate more brands behind smaller platforms. There are more exits, there do seem to be more buyers in the market for the one, two, $300 million businesses. So I think the dynamics can be quite different by geography.

Rusty Ray (03:40):

For sure. I think people are still chasing in the US and probably will be for the foreseeable future. In many ways, it's a much more simple market to tackle than Europe. It's large, it's regulatory regimes as single, and in terms of marketing, sales, distribution, it's all on a national scale. So you're not parsing up your business to operate in New York versus Iowa versus California. The same infrastructure can be applied really across the country and even into Canada in some ways.

(04:15):

I think Europe is interesting and you raise a good point about Karo and STADA. I think those are two examples of successes, in my eyes, of folks that have been able to acquire across different countries, across different regulatory regimes within Europe and have been successful. They're the two that come to mind that are truly sort of pan-European, maybe Karo less, but still a good foothold across Europe that aren't the big pharma players. I think people are going to watch them very closely because the US is getting expensive. It's very competitive in terms of acquiring brands. Any process that leads out now is highly contested. Any brand that comes to market, there's a list of buyers a mile long. I would say that's less the case in Europe. I think what holds people back in Europe is the lack of understanding of what it takes from a regulatory perspective, be it France, Germany, et cetera.

(05:13):

There are nuances, there are some centralized systems around it, but there are nuances across countries. Language - that doesn't often get thought of, but that is a barrier for some folks to think about. And then the third, and I think the biggest is distribution. It's so very different than the US. You're dealing with very small pharmacies on the corner where people still go and talk to an expert to get recommendations. That's really not done quite as much in the US. The idea that e-comm has a place in Europe or that distribution is easy and getting your product into the consumer's hand is just a much more challenging prospect than it is in the US.

Chris Harley-Martin (05:54):

I do agree with that. I think though that over the course of the last couple of decades, the dynamic has changed a bit with third parties coming and offering those services in the US, like Emerson, and Europe and beyond, Ceuta now, with slightly different business models, admittedly, but with strong capability to provide those sales and distribution into the market. So whilst I agree with you it is more complicated in Europe, it's not as if the industry hasn't evolved to find ways to provide services for brand owners and entrepreneurs who are trying to get their products to market. Your e-commerce point is very well-made because I think there's a long way to go with e-commerce building in Europe, and there are some businesses that have focused on the direct to consumer e-commerce models, but equally, we all know that the direct to consumer business is not the most profitable. It can be very difficult to run effectively. I think everyone's beginning to turn now to more of a sort of omnichannel approach, which again creates opportunities for M&A.

Rusty Ray (06:53):

Yeah, I think it's interesting you mentioned Ceuta and Emerson because I think they're two leaders, and Advantage as well I would put in there, that have really enabled private equity to participate in this space much more effectively. Whereas when you think of a team that can run a brand or multiple brands across different categories, you're talking about a C-level organization, you're talking about regulatory, you're talking about commercial folks, whether it's sales, marketing, advertising, promotion, product development, et cetera. You're talking about a very large team that's necessary to support a brand. And that doesn't even get you to distribution, logistics, manufacturing. So the idea that Ceuta or Emerson can step in and take a lot of that back office process off the table, you're really from order to cash and manage the relationships with the CDMOs, contract development manufacturers. It's really enabled private equity to handpick teams, very seasoned industry executives that know how to select brands, grow them and grow them successfully, put a lot of resources behind them and allow them to focus on growing the business, outsourcing a lot of the day to day activity to third parties. It's an asset-lite model. It's very profitable and allows folks to enter the space without having to build that infrastructure day one because you can't sort of absorb a brand and then say, “Oh, well now let's go find a team.” That time is costly. It's really been interesting what Emerson and Ceuta have been able to do. Quite frankly, I think they've led to the success of a lot of folks that have invested in the space.

Chris Harley-Martin (08:38):

Yeah, the more I think about it, the more the disaggregation of all the different parts of the P&L, the ability to get high quality contract manufacturing done, the third-party selling and marketing organizations, even third-party regulatory. It is possible to put businesses together now virtually.

I want to turn to future prospects. I have been thinking a little bit about this as I left corporate life and started to think about how I wanted to contribute to the industry - because I'm staying in the industry. I'm consulting across a number of different platforms. Two things occur to me. The first is that unlike other industries with very well-defined boundaries, consumer healthcare's a very broad collection of categories and brands. I talked earlier about defining it more as self-care, which encompasses in my mind at least all the things that consumers do to manage their own well-being, which makes it a very large market evolving the whole time and with plenty of M&A opportunities and M&A playing its part in driving growth.

(09:37):

The reason I keep mentioning growth is because the more we see the industry develop, the more we realize that growth and valuation are connected. The faster you grow, the better your prospects for growth, the higher your valuation in the public markets. The most recent explosion of transactions in vitamins, minerals and supplements, particularly in the US, is a good example for me of how the industry has evolved over the last couple of decades. I don't see that changing. I see the evolution continuing, possibly even accelerating if we can get to unlocking more Rx-to-OTC switches, particularly in the US, investing behind underserved segments. There's a lot of businesses coming to market now in women's health, which I think is a massive opportunity and other novel categories.

(10:21):

Again, picking on the US. Most recently hearing aids became available as OTC products. So I see that evolution, the permeable boundaries, meaning that there's plenty of opportunity and will continue to be lots of opportunities just because the industry will absorb different categories. The second thing that occurred to me is that although there are short-term headwinds for M&A, and we won't spend time on this today, and funding transactions is a little harder than it was, and maybe some people are a bit more wary than they have been. The very fact is we are investors, not traders, we're investors who look over the long term. I'm taken by the distinction between investors and traders because it's something that Howard Marks talks about all the time in his memos and speeches and for long-term prospects, beyond the next couple of years, perhaps, whether there is a bit of difficulty and headwinds, are really good in self-care, whether it's because governments need to shift the burden of healthcare costs to the consumer or consumers are more actively engaged in their health.

(11:24):

I genuinely think there's both growth opportunity and opportunity for innovation and M&A. The tailwinds are strong. If we just take the current year, which is a difficult year, IQVIA, I think I read recently are forecasting a 9% growth for consumer healthcare, which is incredible really, and further forecasts of similar levels of growth into the future. I'm very optimistic about not just growth, but the opportunities and for M&A to drive that growth. What's your point of view as a banker, maybe looking at it through the lens of geographies or categories?

Rusty Ray (11:56):

I think I would come at the question first on categories. You're spot on VMS. I don't see that slowing down anytime soon. I think that hearkens back to even pre-COVID when people started to seriously get online and think about their health, take a lot more control of how they thought about their health and what they needed or wanted out of products for themselves. That's obviously led to self-care. So vitamins, minerals, sublets, VMS really fills that gap in a big way. Obviously OTC continues to fill that gap in a big way. I think it's going to be just an accelerating trend that people turn more and more to their independent research, if you can call internet research that, in finding products and solutions for themselves. That did probably accelerate the VMS category in my opinion, because 10, 15 years ago it was in some niche health food stores, et cetera.

(12:58):

It's really coming to its own. It's now a massive space in its own right. It's probably led to a lot of products that don't do what they say they do or not as advertised. I've seen over the last sort of five, seven years, a focus on quality in that space. I think we're starting to see that come through, whether it's just multivitamins, clean label, good ingredients, et cetera, and that's just becoming more and more important to the consumer. I think the other categories, and you kind of mentioned this, the idea of new categories that are evolving. They're not new, it's just that we never talked about them before. Women's health, there are a tremendous number of new women's health platforms, albeit small. Most of them started digitally. Most of them started DTC or still are and are trying to turn that corner into brick and mortar.

(13:50):

We're just seeing a really interesting explosion for opportunities in women's health, whether it's a focus on certain age populations, menopause or prenatal, or just more a holistic approach to women's health that wasn't there before. The other is sexual wellness. These are areas that no one talked about. We didn't talk about it. It was behind the counter at the pharmacy, if you will. But now there's whole companies set up either DTC or digital or more in the family planning aisle within the traditional brick and mortar stores. So I think those are areas to watch.

Chris Harley-Martin (14:29):

Great. Good tips for investment. Thanks, Rusty.

Rusty Ray (14:32):

Well, that wraps up our second discussion with Chris Harley-Martin. It's always instructive having him on and learning a little bit more about the consumer health space. Having participated in M&A within the sector for 15 plus years, I still always have something to learn in talking to Chris, especially as it relates to some of the things we talked today about the differences between the US and EU markets and the challenges they're in, and some of the observations we're all seeing around the emergence of third parties as support for those newer participants in the consumer health space and really how they have transformed investment opportunities. Of course, if you want to hear any more about our experiences with US or European branded products or some of the opportunities and trends we're seeing around outsourcing in the space, please contact us at Alantra.