



cutting through complexity

Pharmaceuticals & Life Sciences Industry Outlook Survey:

Executives Focus on
Growth Despite
Regulatory Challenges

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KPMG's Industry Outlook Survey

KPMG LLP, (KPMG) the audit, tax and advisory firm, surveyed C-suite and other top-level executives in the pharmaceutical & life sciences industry during the second quarter of 2012, before the Supreme Court decision on the healthcare reform legislation.

Taking the past year into account, participants were asked about business conditions in their sector, their expectations for revenue growth, merger and acquisition activity, specific industry challenges, and capital spending plans in the year ahead. They were also asked to discuss the impact of regulation and healthcare reform legislation on their businesses.

These responses were compared to the findings of a similar survey conducted among pharmaceutical executives in the second quarter of 2011.

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Foreword

In an effort to gauge industry momentum and better understand current challenges, we have once again reached out to senior pharmaceutical & life sciences executives across the United States for their insights and perspectives. This report includes both a snapshot of current conditions and impressions of what may lie ahead for an industry in pursuit of growth amid persistent political and regulatory uncertainties.

Pharmaceutical executives acknowledge an extremely difficult business environment with no clear single path forward. They are struggling to grow revenue in the face of pricing and regulatory pressures, including fines, taxation, fees, and reporting requirements. Therefore, it is not surprising to see an unusual combination of tentativeness combined with pockets of creative experimentation.

Clearly, access to new technologies and products remain critical in today's market. However, while mergers and acquisition and expansion into new markets are still critical drivers of growth, fewer executives indicate that they are lining up to make major acquisitions. In the meantime, they are continuing to work on their research portfolios, including alliance and contractual arrangements.

Despite challenges, this year's survey results reveal slow but steady sector progress as evidenced by reports of moderate revenue increases and hiring activity over the last 12 months. Executives believe that these trends will continue, with modest gains expected about these areas for the year ahead. However, respondents are less enthusiastic over their longer-term outlook, with many pushing back their predictions for a complete U.S. economic recovery until 2014 or beyond.

On behalf of KPMG, I would like to thank those who participated in this survey. I hope the findings are useful to you in addressing market challenges and opportunities. I also welcome the chance to discuss this study and its implications for your business in the year ahead.

David Blumberg

Advisory Sector Leader, Pharmaceuticals & Life Sciences
KPMG LLP



Key Findings from KPMG's 2012 Industry Outlook Survey

KPMG's survey reflects the responses of 107 pharmaceutical & life sciences sector executives from U.S.-based companies with \$100 million or more in annual revenue. Forty-five percent of respondents work for companies with annual revenue exceeding \$10 billion, while 36 percent represent companies with annual revenue from \$1 billion to \$10 billion, and 20 percent represent companies with annual revenue from \$100 million to \$1 billion. Respondents indicate that 79 percent of these companies are publicly held, while 21 percent are privately held.

- Navigating the regulatory environment and investing in organic growth will be the key focus of management over the next two years.
- Sixty percent of executives cite regulatory and legislative pressures as the most significant barrier to their company's growth over the next year. Additionally, half of the respondents consider the growing regulatory burden to be the top concern for their company's future.
- Executives expect the biggest drivers of revenue growth will come from new therapies from their own research (52 percent), followed by therapies from a current/potential alliance partner (36 percent), and growth from non-U.S. markets (34 percent).
- The top three areas in which executives plan to increase spending over the next year include organic growth (47 percent), business acquisition (41 percent), and research and development (40 percent).
- Almost two thirds (65 percent) of survey respondents believe that healthcare reform in the United States does not address the real challenges of U.S. healthcare. In addition, 46 percent say that it adds complexity to their business operations.
- Executives plan to use digital marketing technologies in a variety of ways. More than one-third (36 percent) of respondents say they will use social media to gain customer insight, and 31 percent expect to deploy customer-facing mobile applications over the next year.
- When asked about their expectations for the U.S. economy a year from now, 54 percent of sector executives expect mostly modest improvements while 38 percent believe it will essentially remain the same. In addition, 70 percent believe a substantial economic recovery will not occur until 2014–2015 or later.

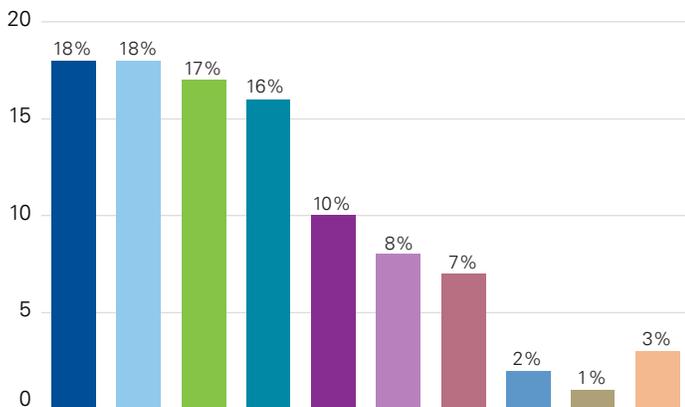
The Many Impacts of the Regulatory Environment

Despite the growing concerns over regulation, executives say they will concentrate efforts on pursuing growth opportunities, relying on new therapies to help boost revenues over the next three years. Overall, executives expect modest sector gains in revenues and hiring over the next year but are less optimistic over the long term, predicting a substantial economic recovery will not occur until 2014 or later.

Key initiatives in focus

In their quest for growth, executives plan to focus their time and energy most on navigating the regulatory environment and investing in organic growth.

Top initiatives on the mind of management

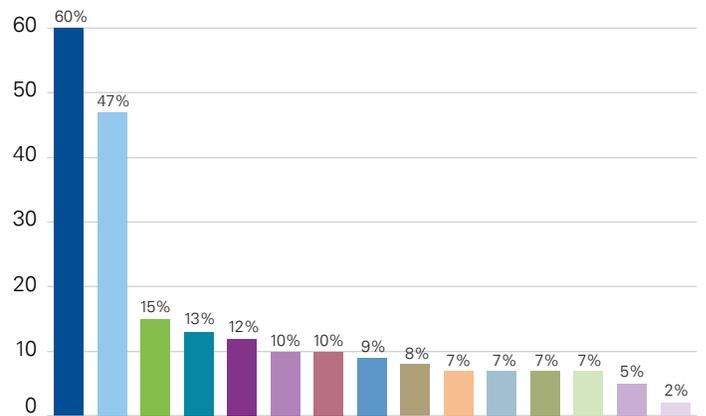


Key

- Navigating significant changes in the regulatory environment
- Significant investment in organic growth¹
- Significant improvement of operation processes and related technology
- Significant changes in business model
- Significant cost reduction initiatives
- Strategic divestiture of current assets
- Merger/acquisition
- Improve enterprise risk management programs/processes
- Significant changes to financial processes and related technology
- Other

While setting their sights on growth, executives also acknowledge they are grappling with the constraints and complexity of an evolving regulatory environment. In fact, 60 percent of survey respondents view regulatory and legislative pressures as the top growth barrier for their company in the year ahead, followed by pricing pressures (47 percent).

Barriers to growth

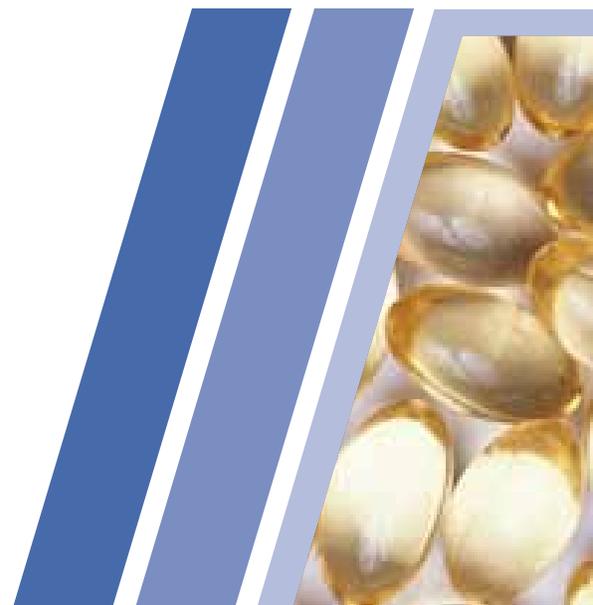


Key

- Regulatory and legislative pressures
- Pricing pressures
- Increased taxation
- U.S. dollar strength
- Staying on top of emerging technologies
- Lack of qualified workforce
- Lack of customer demand
- Risk management issues
- Energy price
- Foreign competition
- Access to and managing capital
- Labor costs
- Exchange rate fluctuations
- Volatile commodity/input prices
- Inflation

Multiple responses allowed

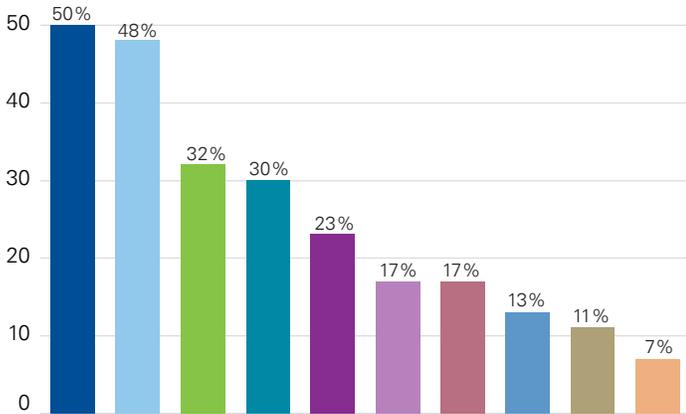
¹ New product development, pricing strategies, geographic expansion



Potential future hurdles

Half of the executives surveyed cite regulation as the biggest issue of concern for their company's future. Other key concerns include patent expirations of key therapies and generic competition (48 percent), price controls (32 percent), and a lack of new products in the pipeline (30 percent).

Key issues of concern



Key

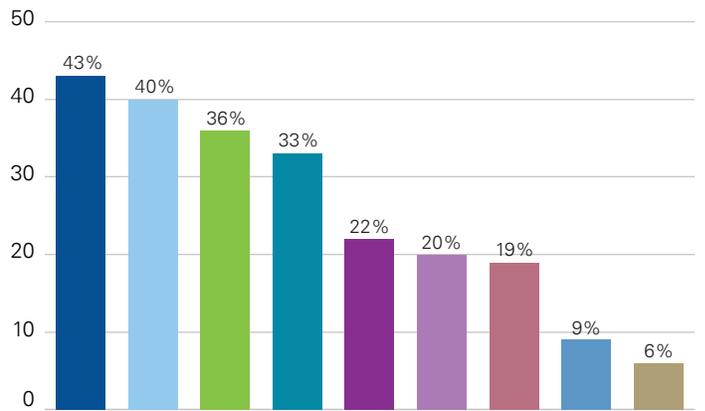
- Increasing regulation and enforcement
- Patent expirations of key therapies and generic competition
- Price controls
- Lack of new products in the pipeline
- Challenge of new markets in other countries
- Ability to retain and develop future leaders
- Redefining your brand(s) for the future
- Potential adverse effects of one or more of your products
- Stock price
- Corporate reputation

Multiple responses allowed

Greatest regulatory concerns

In particular, 43 percent say government pricing and reporting is the greatest regulatory or legal concern, followed by U.S. reform taxes and industry fees (40 percent) and price controls (36 percent).

Greatest regulatory concern



Key

- Government pricing and reporting
- U.S. reform taxes/fees on the industry
- Price controls
- Good manufacturing/clinical practices
- U.S. Sunshine Act - reporting aggregate spend with U.S. physicians
- U.S. class-action suits
- Sales force and marketing compliance
- Foreign Corrupt Practices Act and other anti-bribery/corruption laws
- U.S. support for whistleblowers

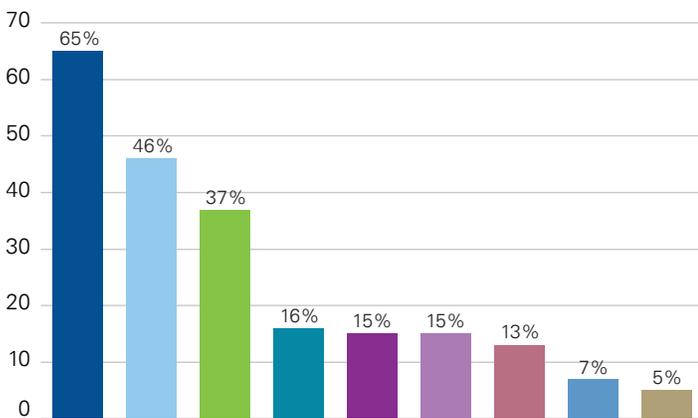
Multiple responses allowed



Perception of healthcare reform

Interestingly, almost two-thirds (65 percent) of survey respondents have a skeptical view of healthcare reform in the United States, believing it does not address the real challenges of U.S. healthcare. In addition, 46 percent say that it adds complexity to their business operations.

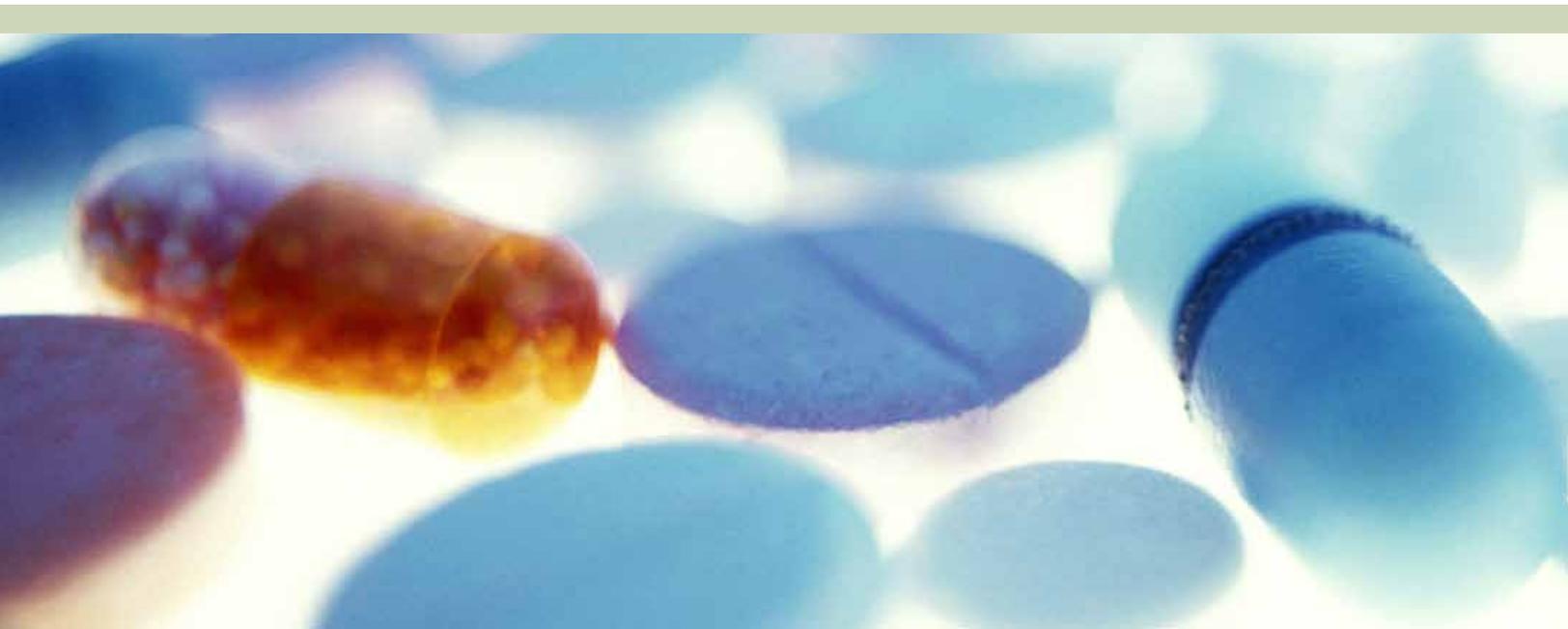
Opinions on healthcare reform



Key

- Not addressing the real challenges for U.S. healthcare
- Adds complexity/cost to your own business operations
- Adds to the cost of healthcare
- Beneficial to your business in increasing coverage
- Helps reduce the overall cost of healthcare
- Helps improve the quality of care
- Adds risk management burdens
- Promising investment in new therapies
- Not very important to your business

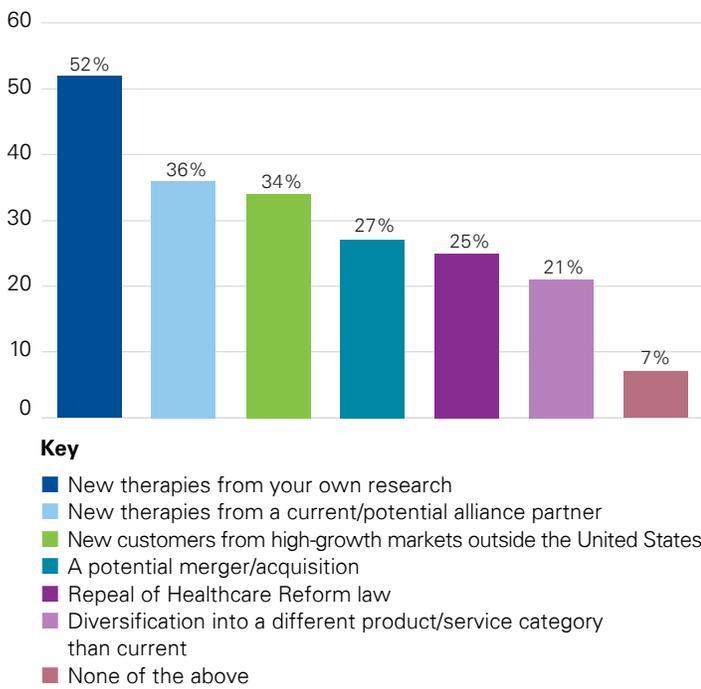
Multiple responses allowed



Pursuing Growth and Opportunity

New therapies will be the key to driving revenues over the next three years. Survey respondents cite new therapies from company research (52 percent) and new therapies from alliance partners (36 percent) as their company's top revenue growth drivers during the next three years.

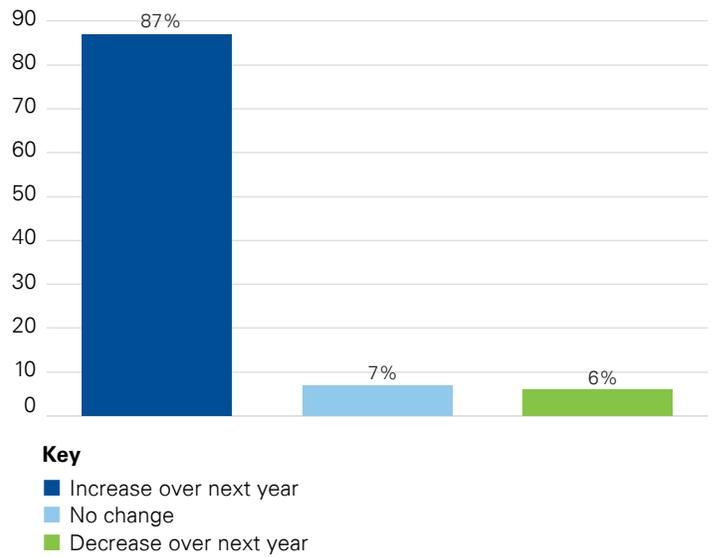
Biggest drivers of company's revenue growth: Next 1-3 years



Multiple responses allowed

Despite the challenging market environment, 87 percent of survey respondents expect the pharmaceutical and life sciences industry to continue to experience growth over the next year.

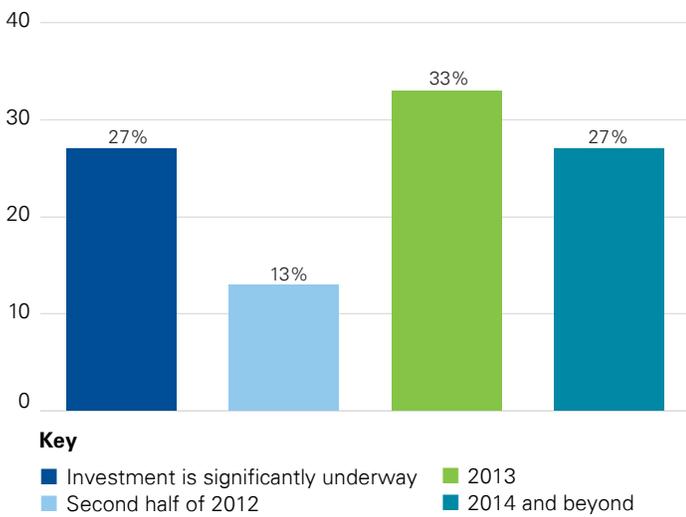
Pharmaceutical and life sciences industry growth rate



Capital Spending and Investment

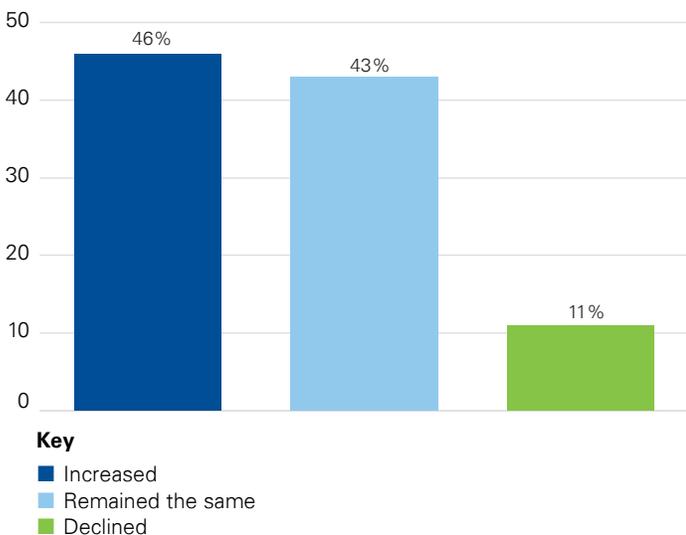
More than two-thirds (69 percent) of survey respondents acknowledge having significant cash on their balance sheets. Of those that acknowledged having cash on their balance sheet, 27 percent of executives noted that investment was already underway, but 46 percent said they expect to invest it in the second half of 2012 or in 2013.

Investment time frame



Forty-six percent of executives note that their company's cash position on its balance sheet has increased since last year, while nearly as many (43 percent) say it has stayed the same.

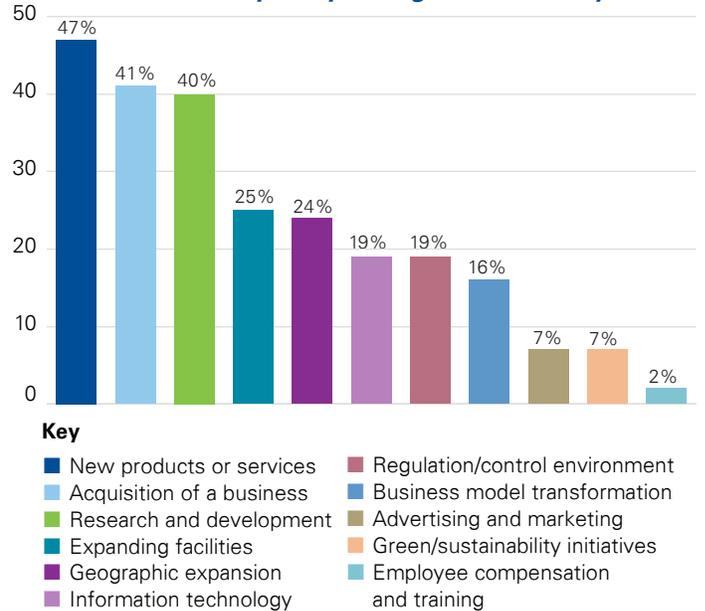
Cash position



Capital spending

Forty-four percent of survey respondents predict their institution's capital spending will increase, while 32 percent expect it to stay the same over the next year. Much of this spending will be in the areas of new products and services (47 percent), business acquisition (41 percent), and research and development (40 percent).

Increased areas of capital spending over the next year

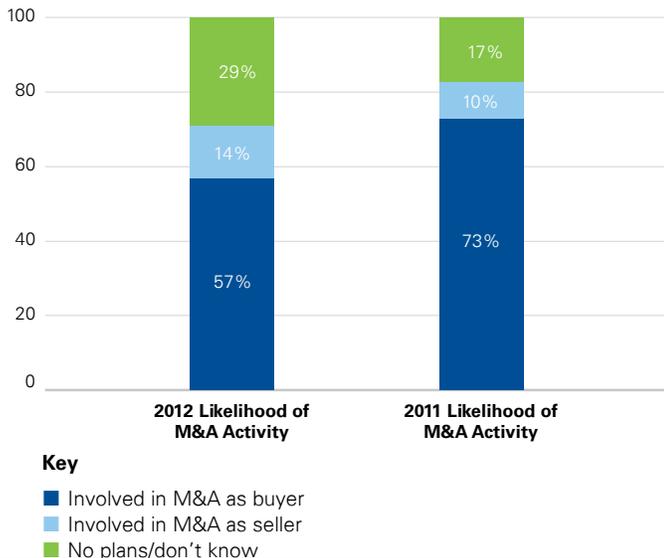


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A Closer Look at M&A Activity

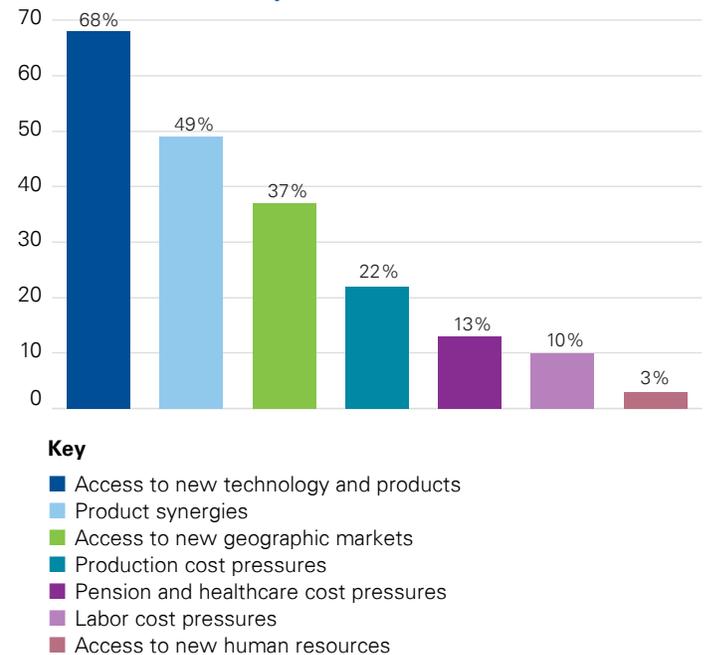
Survey results signaled a shift in expectations around mergers and acquisitions. A year ago, 37 percent of executives said a potential merger or acquisition would be one of the biggest drivers of revenue growth, but today, only 27 percent feel this way (see *revenue drivers chart, page 9*). Similarly, when asked about the likelihood of their company being involved in a merger or acquisition during the next two years, 57 percent in 2012 say they will be involved in a M&A transaction as a buyer, down from 73 percent a year ago. Meanwhile, almost 30 percent said their company has no plans or they are unsure if they will be involved in M&A activity, as compared to just 17 percent in 2011.



M&A drivers

According to survey respondents, the primary drivers of M&A activity will be access to new technology and products (68 percent), product synergies (49 percent), and access to new geographic markets (37 percent).

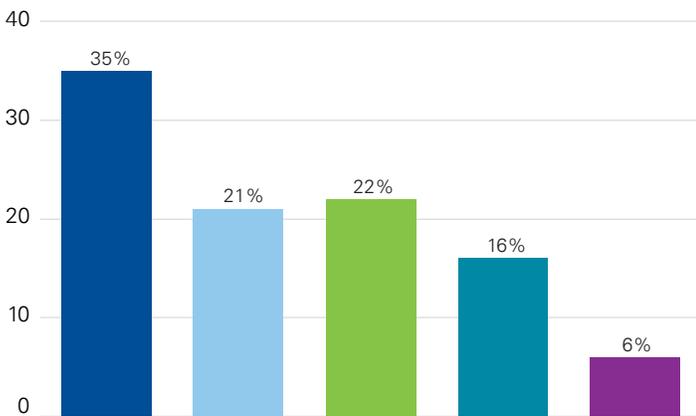
Drivers of M&A activity



Data Analytics and Digital Marketing Channels

When asked to describe the organizational maturity regarding usage of data analytics, more than one-third (35 percent) of executives rate the data analytics literacy of their company as average, while 21 percent rate their data analytics literacy as high.

Data analytics maturity of company

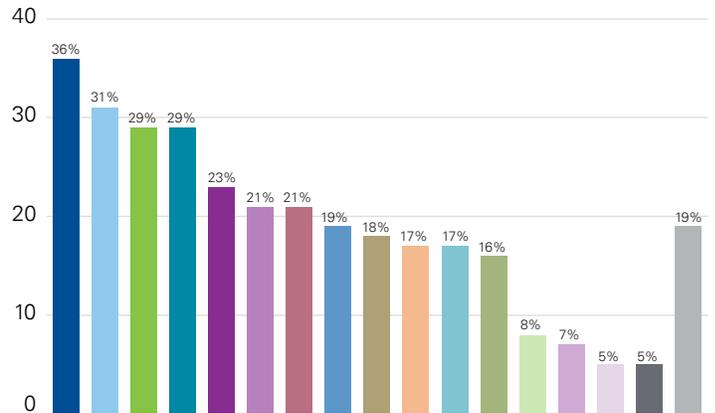


Key

- Average when it comes to utilizing analytics
- High data analytics literacy
- Rapidly moving toward high analytical literacy
- Average to low analytical literacy
- Don't know

Pharmaceutical & Life Sciences executives plan to use digital, social, and mobile technologies in a variety of ways over the next 12 months. In fact, more than one-third (36 percent) have plans to use social media to gain customer insight, and 31 percent expect to deploy customer-facing mobile applications over the next year.

Digital marketing strategies planned for year ahead



Key

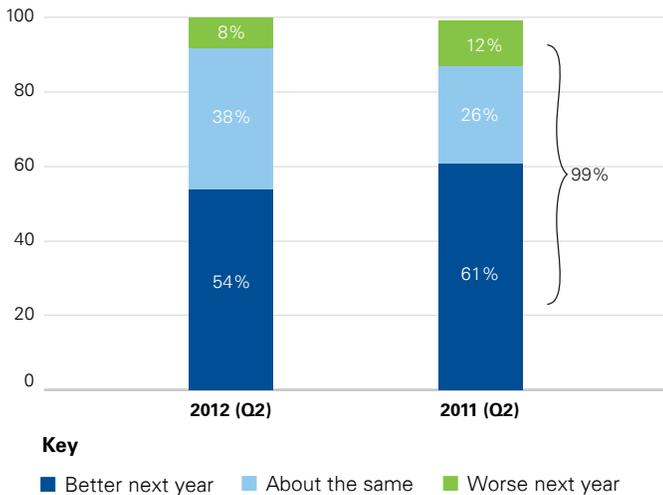
- Social media for customer insight
- Customer-facing mobile applications
- Social media for external brand promotion
- Social media for recruiting
- Social media for enterprise collaboration/knowledge sharing
- Enterprise mobile applications
- Mobile-specific customer-facing Web sites
- Social media for two-way customer engagement
- Mobile-specific enterprise Web sites (i.e., mobile intranets)
- Creation and distribution of digital media marketing messages using video²
- Location-based marketing using mobile technology
- Creation and distribution of digital media internal messages using video
- Social media for customer crowdsourcing
- Mobile-commerce technologies including near field communication-enabled payments and mobile wallets
- Social media for enterprise crowd sourcing
- Social media for enterprise risk management
- Don't know

Multiple responses allowed

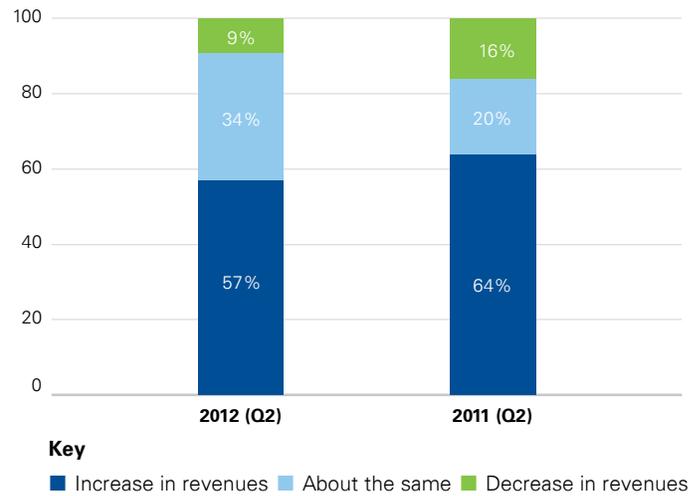
² Including company-specific external video channels

Business Conditions

Despite a lackluster economy, more than half (54 percent) of executives surveyed believe that business conditions will improve in a year's time. Still, this represents a less optimistic view than in 2011, when 61 percent answered the same question the same way.

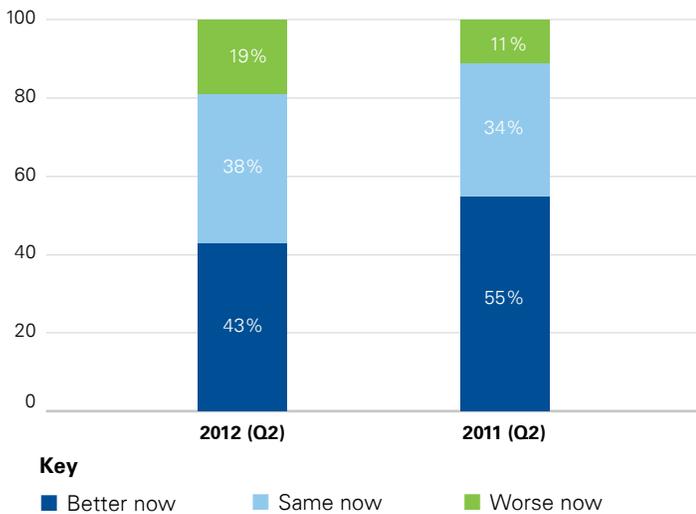


When asked to describe their expectations for revenue a year from now, more than half (57 percent) of executives predict that revenues will increase, while 34 percent believe revenues will stay flat. These results reveal lower expectations than last year, when 64 percent and 20 percent, respectively, answered the same way.



Revenues

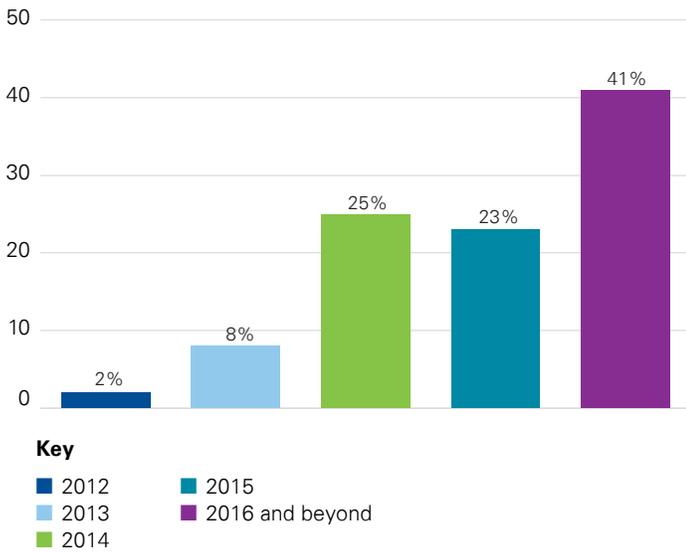
Forty-three percent of respondents reported an increase in revenues over the last year, down from 55 percent the previous year.



Profitability

When asked when they expect their company's profitability to be at its greatest, 41 percent of executives said they do not expect it to be until 2016 or later.

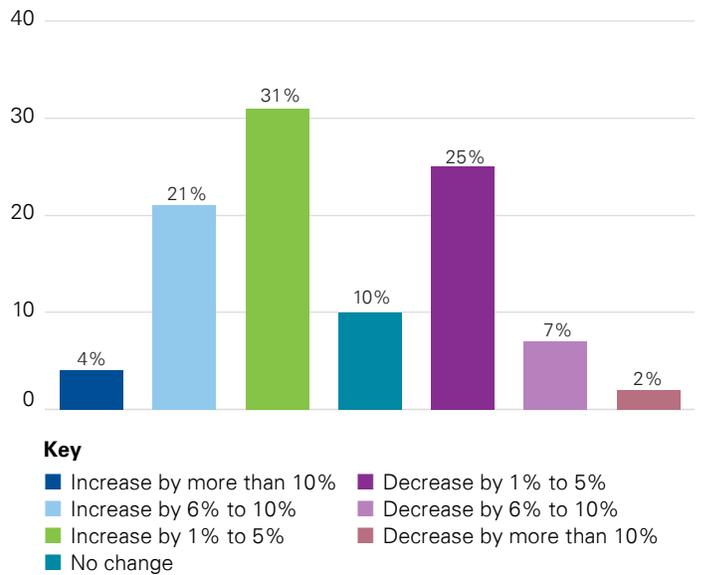
Expectations of greatest company profitability



Operating costs

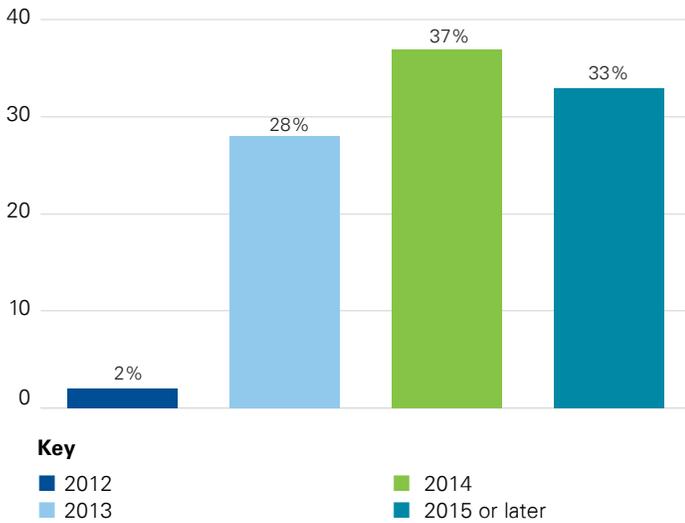
Moreover, more than half (56 percent) of respondents expect their companies' operating costs to increase over the next year. On the other hand, 34 percent anticipate that operating costs will decrease and 10 percent believe they will remain the same.

Operating costs expected in year ahead



Hope for Recovery Remains on the Horizon

The U.S. economic recovery continues to be just beyond reach, according to the executives who participated in this year's survey. Seventy percent have pushed back their expectations for a complete U.S. economic recovery until 2014 or beyond.



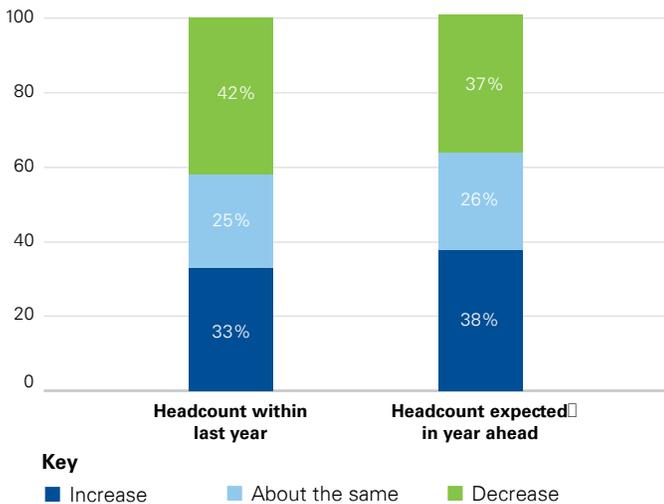
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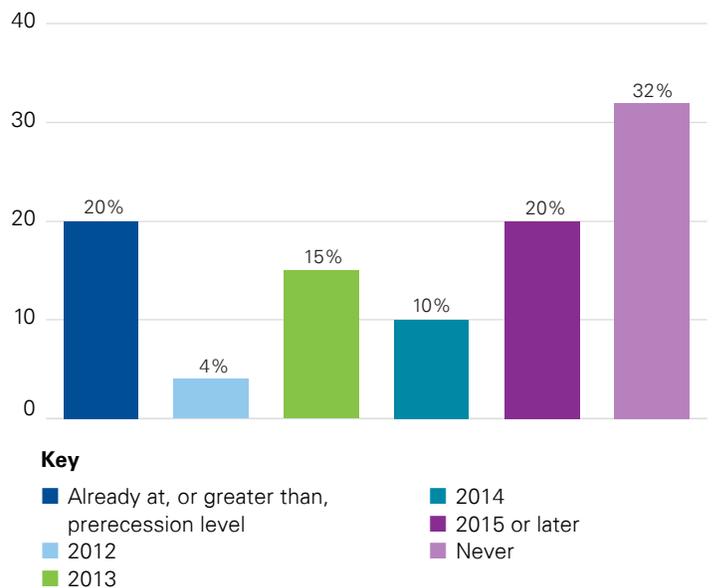
Headcount

While 33 percent of survey respondents noted they added personnel over the last year, 42 percent report a decrease in headcount. Executives have similar expectations for the year ahead, with 38 percent predicting an increase in hiring as opposed to 37 percent who anticipate a drop in headcount.



Notably, almost one-third (32 percent) of survey respondents do not expect their U.S. headcount to ever return to prerecession levels.

Headcount: Return to prerecession levels



Conclusion

Facing a lackluster economy compounded by changing market dynamics, pharmaceutical & life sciences executives plan to focus much of their time and energy investing in organic growth and navigating the evolving regulatory environment. While survey respondents expect modest improvements in revenue and hiring, they also expect to continue to face significant industry and regulatory challenges over the next year. With a decreased emphasis on M&A as a growth strategy, many executives will look to new therapies to drive revenue growth over the next one to three years. Overall, executives show a lingering concern over the economy, predicting a substantial economic recovery will not occur until 2014 or beyond.

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