

Breaking News : Biotech/Pharmaceuticals

Pfizer, Warner-Lambert Ink Merger Deal

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After three months of wrangling, **Pfizer** ([PFE:NYSE - news](#)) announced Monday that it will acquire **Warner-Lambert** ([WLA:NYSE - news](#)) in an all-stock deal the companies have valued at \$90 billion.

The union creates the largest drug company in the U.S. and the second largest worldwide behind Switzerland's **Novartis** ([NVTSY:Nasdaq - news](#)) when ranked by sales.



American Home Products ([AHP:NYSE - news](#)), a [loser in the merger game](#) for the third time, will get \$1.8 billion to walk away.

Pfizer has agreed to exchange 2.75 of its shares for each Warner-Lambert share, valuing the deal at \$90 billion using Pfizer's closing price Friday of 35 3/4. The new exchange ratio is 10% higher than the 2.5 shares Pfizer originally offered last November and considerably higher than the 1.49 shares American Home offered. The deal is expected to close in the second half of this year.

Pfizer's shareholders will own about 61% of the new company on a fully diluted basis and Warner-Lambert shareholders will own 39%.

The chairman and chief executive of the new company will be William Steere, Pfizer's chairman and chief executive, while Warner-Lambert's chairman, Lodewijk J.R. de Vink, "has made a personal decision not to be an executive in the company after the closing." The 54-year-old de Vink took over the reins of Warner-Lambert only last May.

The new company's management team will be composed largely of Pfizer staff, with Warner-Lambert's F. Morgan Morton, president of the consumer health care unit; Peter Corr, head of research and development; and Anthony Wild, president of Warner-Lambert's pharmaceutical division, staying on. "I'm heartened to see that Pfizer's management will be most heavily represented," said analyst Richard Evans of **Sanford C. Bernstein**. "Henry McKinnell [president and chief operating officer] is the best COO in the industry."

Evans rates Pfizer an outperform and has no rating for Warner-Lambert. His firm has not done underwriting for either company.

The new company will keep the Pfizer name and be based in New York City, where Pfizer is headquartered. The new company's consumer products division will be based in

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Morris Plains, N.J., where Warner-Lambert is based.

The combined company will have annual revenues of about \$28 billion, including \$21 billion in prescription pharmaceutical sales, and a market capitalization of over \$230 billion. The research and development budget will total \$4.7 billion and profit should amount to about \$4.9 billion.

Compounded annual revenue is expected to be 13% through 2002 and earnings growth is expected to be 25% for the same period. The transaction will be accretive in the first full year of operations and will use pooling-of-interests accounting. The company was able to use the more favorable method of accounting because American Home relinquished its option to purchase Warner-Lambert shares.

"We understand the decision of the Warner-Lambert board to support the alternative transaction and we saw no benefit to impeding their ability to use pooling-of-interests accounting," said John Stafford, chairman, president and chief executive of American Home, in a statement. "The termination of our agreement brings to an immediate close the distracting and acrimonious litigation among the companies."

A major reason for Pfizer's pursuit of Warner-Lambert was the prospect of snaring all of **Lipitor's** profits for itself. Previously, the blockbuster cholesterol-lowering drug had been co-marketed by the two companies, with profits divided between them. The company said that Lipitor's sales are expected to exceed \$5 billion worldwide and the drug will be introduced in Japan this spring.

Pfizer also said anticipated cost savings and efficiencies should total \$1.6 billion, 33% greater than originally thought. Savings of \$200 million will be achieved by the end of this year, \$1 billion by the end of 2001 and \$1.6 billion by the end of 2002.

The cost savings could be even larger than projected by the company. Analyst Richard Evans of Sanford C. Bernstein thinks there could be \$2.5 billion in available synergies by 2003, with \$1.6 billion coming from savings in manufacturing costs and the rest from overlaps in administrative and support service in research and development and selling, general and administrative expenses.

Merrill Lynch analyst Steven Tighe sees additional top-line synergies from the combination of product portfolios in key therapeutic categories, such as cardiovascular, central nervous system, infectious disease and diabetes. He rates Pfizer a long-term buy, and his firm advised the company on its merger.

There have been questions about whether paying the breakup fee would eat into the cost savings of a deal, but analyst Jeffrey Kraws of **Gruntal & Co.** said, "Obviously Pfizer knew about the \$1.8 billion and factored it in." He rates both companies an outperform, his firm's highest rating. Gruntal has not participated in underwriting for either company.

The cost savings will accelerate projected compounded annual net income growth through 2002 to 25%, excluding one-time transaction and restructuring charges. Diluted earnings per share for Pfizer alone are projected to be \$1.04 for 2000, \$1.25 for 2001 and \$1.50 for 2002, while pro forma earnings per share in 1999 for the combined entity would be 80 cents.

From that base, the company projects that diluted earnings per share for the combined entity will be 98 cents in 2000, \$1.27 in 2001 and \$1.56 in 2002. The numbers include the \$1.6 billion in cost savings but do not include any increased sales from collaborative activities.

Added Kraws, "That makes this the fastest-growing large-cap pharmaceutical company in the industry."

The figure is higher than both Warner-Lambert's and Pfizer's standalone growth rates of 20%. It's also higher than Pfizer's initial projection of 24%. "That shows the synergies as well as the cost savings of the deal," said analyst Leonard Yaffe of **Banc of America Securities**. Yaffe rates Warner-Lambert a strong buy and Pfizer a buy and his firm has not participated in underwriting for either company.

Kraws also calculated that the combined company now has seven drugs with over \$1 billion in sales and after the launch of Neurontin there will be eight. "That shows the rate of growth is accelerating, not decelerating," he said.

The company will also have a strong new product pipeline, with three launches this year -- of **Tikosyn**, **Relpax** and **FemHRT** -- and six next year -- **Pregabalin**, **AG-1549**, **Valdecoxib**, **Voriconazole**, **Zeldox** and **Vfend**.

Also, the new company will have a "formidable sales capability that is well-distributed throughout the world and does not have any weak spots," wrote Tighe. "We believe Pfizer's (with Warner's) combination of products and sales power dramatically steps up the standard of being a top-tier company in this industry."

This transaction marks the third in the pharmaceutical industry in the past two months, after **Glaxo Wellcome's** ([GLX:NYSE - news](#)) \$76 billion [deal](#) to acquire **SmithKline Beecham** and **Pharmacia & Upjohn's** ([PNU:NYSE - news](#)) \$27 billion deal to [acquire Monsanto](#) ([MTC:NYSE - news](#)).

"Mergers of equals in this industry have been a recipe for disaster with the quality of execution quite bad," said Evans. "This purchase is clearly being settled on Pfizer's terms. Accordingly we expect none of the political distractions inherent in trying to realize synergies in a merger of equals."

"We view this transaction very favorably, as we believe it is rare to see two extremely well positioned companies in the sector combine," wrote Tighe. "Previous mergers have consistently been defensive consolidations between two decelerating companies," added Evans, "and this combination represents a combination of two healthy, growing companies."

In Monday trading, Pfizer shares closed up 15/16, or 3%, to 36 11/16. Warner-Lambert shares finished up 2 9/16, or 3%, to 97 1/8. American Home ended the day up 2 1/2, or 5%, to 48.

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