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Eli Lilly and Company

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Written Assignment #4
Eli Lilly and Company

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Bus 4402W: Strategic Analysis and Decision Making

Professor Herrmann

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Abstract

Eli Lilly and Company is a pharmaceutical company that has the goal of creating new products. Eli Lilly's products are seen in hospitals and pharmacies around the US, with the hopes of growing internationally. By having a large number of drugs in their pipeline, they can be a key player in improving multiple types of illnesses as well as help aid the aging population. The healthcare sector is always one that is high-performing.

Eli Lilly and Company is positioned as a pharmaceutical company, with the goal of creating high-quality medicine for every need or to take a preexisting medicine and make it better. For the past 140 years, they have been creating medicine for various causes, but are now focusing their efforts on antibody treatments for the COVID-19 pandemic, as well as different cancers and autoimmune diseases. Everything that the company does should follow its core values: integrity, excellence, and respect for people (Eli Lilly and Company - A). Eli Lilly is found in the US, Japan, Europe, and hopes to expand to the rest of the world soon. They are broken down into Endocrinology, Oncology, Immunology, Neuroscience, & Other. The company has increased revenues from \$23,832.8 - \$25,925.3, a consistent tax rate of 15%, expenses increasing \$300k a year, accounts receivable, or a/r, decreasing as they pay less in patents and drugs go generic, consistent inventory of \$120k - \$140k, showing they do not keep a lot on hand, a weighted average cost of capital, or WACC, of 5.9% showing it does not hold a lot of debt, and a long term growth rate of 2.3%, showing a healthy but stable growth (Bloomberg LP, CapitalIQ 2021).

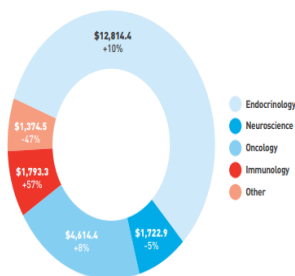
While Eli Lilly is one of the largest pharmaceutical companies, they still face a lot of competition from Big Pharma brands such as Johnson and Johnson, and smaller companies like Merck, Pfizer, and Moderna. The healthcare sector is broken down into three industries: Pharmaceuticals & Biotechnology - Where Eli Lilly is, Healthcare Facilities & Services, and Medical Equipment & Devices (Scott, 2020). Eli Lilly tends to focus on acquiring other companies to be able to expand upon the technology and name brands already created. They have had 26 acquisitions, with the most recent being Preval Therapeutics in 2020 for \$880M (*Crunchbase*). As of 2020, \$6,086 million per year goes to R&D, which will provide more value to their customers and shareholders (*Eli Lilly and Company - F*). They are one of the main insulin manufacturers in the US, producing 11% of insulin, giving them negotiating power. The top 3 pharmaceutical companies by market share include Merck at 4.44%, Johnson and Johnson at 4.27%, and Eli Lilly at 2.57% (Bloomberg L.P).

Eli Lilly does have a sustained competitive advantage. For every drug that Eli Lilly makes it costs \$2.6B. The average length of the patent is 20 years, so they need to bring drugs to the market before a company comes out with generics (Eli Lilly and Company - B). The biggest thing that they did was create a generic version of their insulin product, Humalog, at a lower price, since they believe that everyone with diabetes needs access to insulin (Keown, 2019). The

graphs below show how each therapeutic area is performing compared to the whole, and how operating expenses are rising each year. Advertising is decreasing as their products become more well known, R&D is stable and increasing ever so slightly. Eli Lilly is outperforming its

REVENUE GROWTH ACROSS THERAPEUTIC AREAS (\$ millions, percent growth)

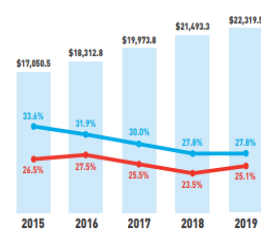
Revenue in Endocrinology increased 10 percent primarily driven by growth of Trulicity, Basaglar, and Jardiance. Taltz drove the 57 percent revenue increase in Immunology. Oncology revenue increased 8 percent due to Verzenio launch in the US. Neuroscience experienced a 5 percent decrease due to lower volume for Strattera as a result of loss of patent protection, offset in part by the launch of Emgality. Other Pharmaceutical revenue decreased 47 percent driven by lower volumes for Cialis, due to patent losses.



OPERATING EXPENSES (\$ millions, percent of revenue)

Revenue R&D
Marketing, Selling & Administrative

Over the past five years, Lilly has maintained relatively flat operating expenses while growing revenue, resulting in steady improvement in operating expense as a percent of revenue.

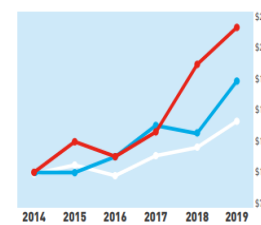


TOTAL SHAREHOLDER RETURN

Value of \$100 invested in Lilly, S&P 500 and Peer Group*

Lilly S&P 500 Peer Group

Over the past five years, Lilly's annualized total shareholder return has averaged 16.7 percent, compared to 11.7 percent for the S&P benchmark, due to the increase in the stock price and increasing dividend stream.



* The graph measures total shareholder return, which takes into account both stock price and dividends. It assumes that dividends paid by a company are reinvested in that company's stock. See "Performance Graph" for those companies included in our peer group.

competitors and benchmark in their return on investment.

The pharmaceutical industry is mature with slight growth due to mergers and acquisitions (M&A) and consolidations happening. Even with the pandemic, they have seen \$1.25T in revenue (Mikulic, 2020).

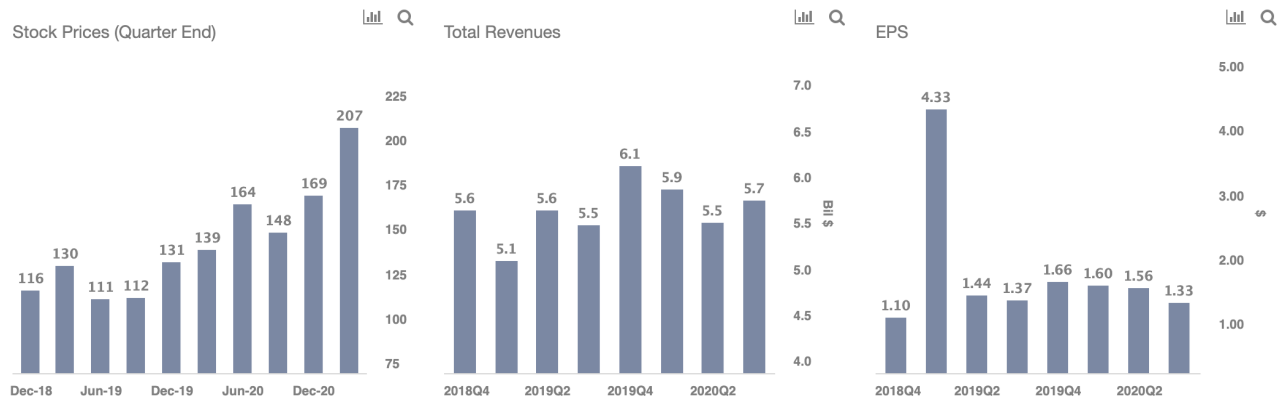
According to the National Institute of Health, healthcare competition is high, with each company trying to be the first to patent their products and secure patents before generics come out. During the generic phase, companies try to deliver on price, quality, and brand name, or even technology to reduce their costs (Rivers & Glover, 2008). Challenges in the industry life cycle include increasing threats from competitors, not using technological advances properly, not taking risks, and not having appealing advertising, compared to its competitors (Patil, 2018).

An opportunity that Eli Lilly has is political factors. After the riot at the capital, Eli Lilly had to suspend some of its political donations (Hansard & Lee, 2021). With Biden's new stimulus package, people will have additional money to buy drugs, increasing Eli Lilly's customers and market share. The Lilly foundation improves global living standards (Eli Lilly & Company - A). More people are currently being diagnosed as Covid long haulers (Hinton, 2021). According to a Harvard Medical study, "50% to 80% of patients continue to have bothersome symptoms three months after the onset of COVID-19," and this number will continue to grow as we find out more about the virus. Creating a drug that will help long haulers will have more of an impact than just people who have Covid because it can be used at any time, and you do not have

to have tested positive (Komaroff, 2020). While vaccines can help these symptoms, they do not always do.

The image below shows that after they started testing their antibody drugs around May 2020, their stock price skyrocketed, revenues increased at a steady pace, and Earnings Per Share has also increased. By using partnerships, they address global health challenges (FSG, 2018).

KEY TRENDS IN Eli Lilly and Company STOCK OVER RECENT QUARTERS

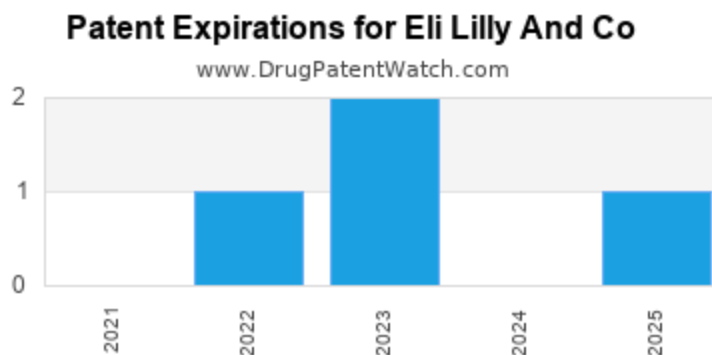


They also explore opportunities where an increasing number of patients are being diagnosed with an illness with no cure. The increase of hybrid and electric cars can decrease shipping costs, which they can reinvest into their company. They can increase their customer service by using value strategies, getting to know their customers better, and improving their data analytics (Kruse, 2019). As people are living longer, Eli Lilly can keep customers longer, while working on diseases that affect the elder population like Alzheimer's.

A threat that Eli Lilly has is lawsuits; a majority of their large drugs have been sued with huge settlements (*Eli Lilly & Co. - History and Product Lawsuits*, 2020). Some settlements have even made it to the supreme court (Blankenship, 2019). If Eli Lilly keeps getting sued, people will shop elsewhere. On March 16th, 2021, Eli Lilly sued the Department of Health and Human Services (HHS) government agency over "restricted sales of drugs discounted under the 340B program to contract pharmacies, which are third parties that dispense the products on behalf of the covered entities," which the U.S. district court ruled in favor of Eli Lilly (King, 2021). Counterfeits and low-quality products might appear in low-income markets. New technology could hinder all of their progress. Since Eli Lilly is starting to appear internationally, they will have to deal with political risk affecting the local currency and their spot rates.

A strength that Eli Lilly has is partnering with companies to produce new products. They have their medication in 125 countries, with 8,000 employees in 14 manufacturing sites (Eli Lilly & Company - A). Their research team made sure all products were being produced at a rapid pace - from zero to millions, “all while maintaining high quality standards” (Eli Lilly and Company - J). They have high customer satisfaction, reliable suppliers, and customers to overcome any shutdowns (Bloomberg L.P. 2021). They have a training program to make sure that all their workers have access to the same information (Overman, 2011). So far, Eli Lilly has performed well when entering new markets. Their new marketing manager has split their advertising into television and digital channels (Bulik, 2019).

A weakness that Eli Lilly has is merging with firms that have a different culture than they do. Their day’s inventory with a high of 329, is ahead of its peers at 224, meaning that they need to raise more capital to invest in their products (Bloomberg L.P. 2021). They need to put more money into technology and integrate their processes among all of their segments. For their marketing, they are not unique compared to competitors. In 2009, they lost over 40% of their revenue due to patent losses, forcing Eli Lilly to transform their business so they do not lose customers to competitors or generics (Younglai, 2011). Eli Lilly needs to find a way to keep their patents long term so their competitors do not copy their ideas, since the more long term a company holds a patent for, the more monopolized their drugs will be, and with the high costs, people will not want to buy from them anymore. Patents should “enable collaboration and investment to bring forward tomorrow’s cures and allow us to move quickly and effectively” (O’Neil & Eli Lilly & Company, 2021). Since Eli Lilly has some market share in each of their segments, they can not be a leader in just one segment like some companies are. The chart below shows the patents that will be expiring in the near future.



Eli Lilly has human and financial resources. Their human resources department has the employees try to reach their potential, try new things, and grow as a person (Eli Lilly & Company - A). They hire people who will be an asset to their mission of creating the best drugs. Their financial resources created the Eli Care Patient Assistant Program, providing free medicine to those who need them (American Cancer Fund®, 2015). They are more concerned with working with others across the world and accepting constructive criticism. In the past, they have made some human resource adjustments that have positively impacted leadership and have brought in more customers due to overcoming market skepticism. They have internal capabilities, such as connected care, innovation, sales, and marketing. Their resource capabilities are working more on their research and development, spending \$6.086M last year, discouraging new competitors (Statista, 2021).

In Porter's five forces, the first is the threat of new entrants. In the pharmaceutical sector, there are always companies trying to do something bigger and better than their competitors. They can do it with lower costs, and need to build economies of scale. Eli Lilly has opened up an innovation center, to create new products and services, and to make old products better to bring new customers in and make existing customers want to stay (Eli Lilly and Company - D). By spending \$6,086M per year on R&D, this will keep less experienced competitors out and discourages new competitors (Eli Lilly and Company - A). Even with the pandemic, they do not see any issues affecting their supply chain and make sure they stay in close talk with their suppliers (Manufacturing Chemist). They currently have 110 suppliers and 43 major customers (Bloomberg LP). Eli Lilly uses multiple suppliers, as a safety net in case something happens with their current suppliers. They currently distribute their products via wholesalers. The buyers have the most say in the pharmaceutical industry since they want to buy their drugs at the cheapest

cost. This forces Eli Lilly to try to build a large base of customers, so there will always be someone to buy at their price. They can reinvest that money back into their company, creating new products to discontinue current ones. The threat of substitutes forces Eli Lilly to not just focus on their products, but to focus on their key values. They need to dig down deep to find out why customers choose them, and if they leave, find out why they are leaving. All of the major pharmaceutical companies are trying to be the best, despite rivalry among competitors. Eli Lilly needs to be able to differentiate themselves, which they do with their generics, owning 11% of the insulin market, and are constantly creating products for those illnesses with no cures (Eli Lilly and Company - A). They have also successfully created the first approved antibody treatment for COVID-19, which has other uses as well (Office of the Commissioner, 2020). Instead of acquiring new companies, Eli Lilly should look at collaborating with other companies, since that would be a mutually beneficial relationship.

Political factors that impact Eli Lilly include the Biden administration. According to a recent article from PriceWaterhouse Coopers, Biden is focused on bringing prices down, allowing for drug price negotiations, partnering with groups like the World Health Organization for the development and production of new drugs, and bringing back the Affordable Care Act (PricewaterhouseCoopers). Economical factors that affect Eli Lilly include working on their supply chain to have a fewer number of higher quality suppliers, exposure to foreign currencies with the hopes to go abroad, and market regulations (*Eli Lilly and Company*, 2020). For environmental factors, they have become energy efficient by reducing their greenhouse gases (Russell, 2020) Social factors that impact Eli Lilly include focusing on diversity inclusion, including gender, race, or religion (Sprouls, 2018). They will work on increasing their diversity in clinical trials since certain groups are currently underrepresented (Eli Lilly and Company - E). The biggest technological factor that Eli Lilly needs to focus on is technology developments. They invested \$400M in their tech center for current production, but need to make sure their future medicines are following these same advancements (Area Development News Desk, 2019). For legal forces, they need to deal with potential lawsuits. Some of their well-known products have led to an increased risk of issues, so they need to have money on hand just in case they are sued. (*Eli Lilly & Co. - History and Product Lawsuits*, 2020).

Eli Lilly has had “over 135 years and a strong commitment to developing and discovering new drugs in the areas of diabetes, neuroscience, cardiovascular diseases and oncology.”After

researching and developing new products, they have a “vision to make a significant contribution to humanity by improving global health in the 21st century” (Blake, 2016). They are a top-performing pharmaceutical company while reinvesting the most money into R&D compared to their competitors. They currently own 11% of the diabetes market, and with the aging demographic, we expect more people to need diabetes care and are introducing a range of generic drugs cheaper than competitors (Eli Lilly and Company - A). Eli Lilly hopes to grow even more in the long term by producing more products that are more beneficial for their customers. Eli Lilly is delivering drugs worldwide with solid financial results. Their drug pipeline is constantly increasing, and they are expanding into new technologies like gene therapy (Eli Lilly & Company - J). With the lessons learned from the COVID-19 pandemic, they can apply those to any of their drugs.

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