

## Johnson & Johnson to Split into Two Companies; Shares Rise



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Health-care giant Johnson & Johnson is splitting off its consumer division, following in the footsteps of other big drugmakers that have moved to focus on the more-profitable pharmaceutical market.

The consumer division will be separated in 18 to 24 months, the company said in a statement. The unit has been beset by lawsuits involving products such as baby-powder, which has been linked to ovarian cancers in some users. J&J shares gained 1.4 per cent as of 10:31 a.m. in New York.

“This is a historic day for Johnson & Johnson, but this is something we’ve been looking at for years,” Chief Executive Officer Alex Gorsky said in an interview on Bloomberg Television. “COVID-19 we think also brought about a fundamental change about how people thinking about personal care.”

J&J said the legal challenges it’s facing had nothing to do with the decision to split. The pharmaceutical arm has long been the strongest performer at the more than 130-year-old company, featuring top sellers such as immune drug Stelara and Imbruvica for cancer. Prescription drugs generated 55 per cent of the company’s sales in 2020, with another 28 per cent coming from the medical device unit, and 17 per cent from the consumer arm. Altogether in 2020, J&J made US\$83 billion in revenue, and analysts estimate US\$94 billion in 2021 sales.

The stock gained just 3.6 per cent this year through Thursday’s close. Meanwhile, rival Pfizer Inc. rose 36 per cent, while Eli Lilly & Co. surged 55 per cent and Merck & Co. 7.7 per cent.

The decision comes just days after General Electric Co. said it would break itself into three pieces. While conglomerates made up of many disparate businesses were once numerous, many of the old giants that once dominated the global business landscape have broken up into smaller entities that executives say can be nimbler in responding to rapidly shifting economic trends and consumer preferences.

Other major pharma companies are sharpening focus on profitable drug-development efforts. GlaxoSmithKline Plc plans to spin off its consumer business, a joint venture in which Pfizer holds a minority stake. Novartis AG is unwinding its shareholding in Swiss rival Roche Holding AG, a move that could yield cash for deals, and has announced a strategic review of the Sandoz generic-drug unit. Novartis also previously sold a stake in Glaxo’s consumer-health business, which owns brands like Sensodyne toothpaste and Advil painkillers.

J&J didn’t outline financial terms of the proposed move in detail, though it said the transaction would be tax-free and that it expected to continue to pay dividends at least at current levels.

“We’re still I’d say in the early stages,” Chief Financial Officer Joseph Wolk said in an interview.

“We’re looking at either a spin option or an IPO split option, and we’re going to take a little more time to see what the market indicates to us is the best path forward.”

Investors could potentially receive new shares of the consumer health company, or might trade J&J shares for those of the new health company, Wolk said.

For decades J&J's board has perennially considered a breakup, Wolk said. Even as competitors have spun out various units to focus on high-growth drugs, J&J decided it was better together, he said.

## CONSUMER CONNECTION

COVID-19 changed the equation, as J&J identified a shift in how people were connecting to consumer products. The pandemic showed how the market for consumer products has evolved, Wolk said.

"If you think about how folks purchase consumer-health products today, it's often dictated by a celebrity influencer who has a social media campaign that used a product that worked really well for them," he said. The new consumer health company will lean into that strategy, Wolk said.

As its units' business models diverged, the consumer division was finally hitting its stride as a stand-alone entity, Wolk said

"Let's say four years ago, we had trouble hitting market growth. Our operating margins lagged significantly against the competitive peer set," Wolk said. Now, "there's a little bit of room to run."

Though J&J's consumer unit brings in the smallest piece of the revenue pie, it's got immense brand recognition. The division boasts over-the-counter medications such as Tylenol, Motrin and Zyrtec, as well as household name brands like Band-Aid, Listerine, Neutrogena, Neosporin, Aveeno, Clean & Clear and Rogaine.

"Personal health and wellness is center-stage, and there is a growing need for consumer product innovation," Gorsky said in a conference call with investors. The new entity will personalize the consumer experience via ecommerce platforms, he said.

The consumer unit has untapped potential, with four billion-dollar brands and other bestsellers in the pipeline. There's more opportunity in the "high-growth, highly attractive markets" for self-care and wellness, he said.

While the company said the decision wasn't spurred by potential liabilities from numerous lawsuits alleging its baby powder caused ovarian cancer, the transaction could help it get out from under that dark cloud, especially if it's unsuccessful at hiving off the liabilities in a bankruptcy court maneuver. J&J faces as much as US\$7.5 billion in potential settlement losses from the suits, according to Bloomberg Intelligence analyst Holly Froum.

Wolk said the claims had "absolutely zero" impact on the decision to split.

## LEADERSHIP OVERHAUL

J&J isn't interested in detaching the pharmaceutical powerhouse from its medical-device unit, which benefits from the scale and customer connections of a larger-sized company, Wolk said.

The planned move won't interfere with potential deal-making, Wolk said.

"I don't see this disrupting the M&A process," Wolk said. "If anything, it could accelerate it."

J&J, a behemoth that employs more than 136,000 people globally, will soon undergo a leadership overhaul. The company recently announced that Chief Executive Officer Alex Gorsky will be replaced by longtime veteran Joaquin Duato.

On Friday, the companies announced that Duato will serve as chief executive officer of the unit that will be focused on pharmaceuticals and medical devices. J&J has not yet named a replacement for Chief Scientific Officer Paul Stoffels, who also recently announced he would step down.

The new consumer health company, which has yet to be named, does not yet have leadership in place.

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