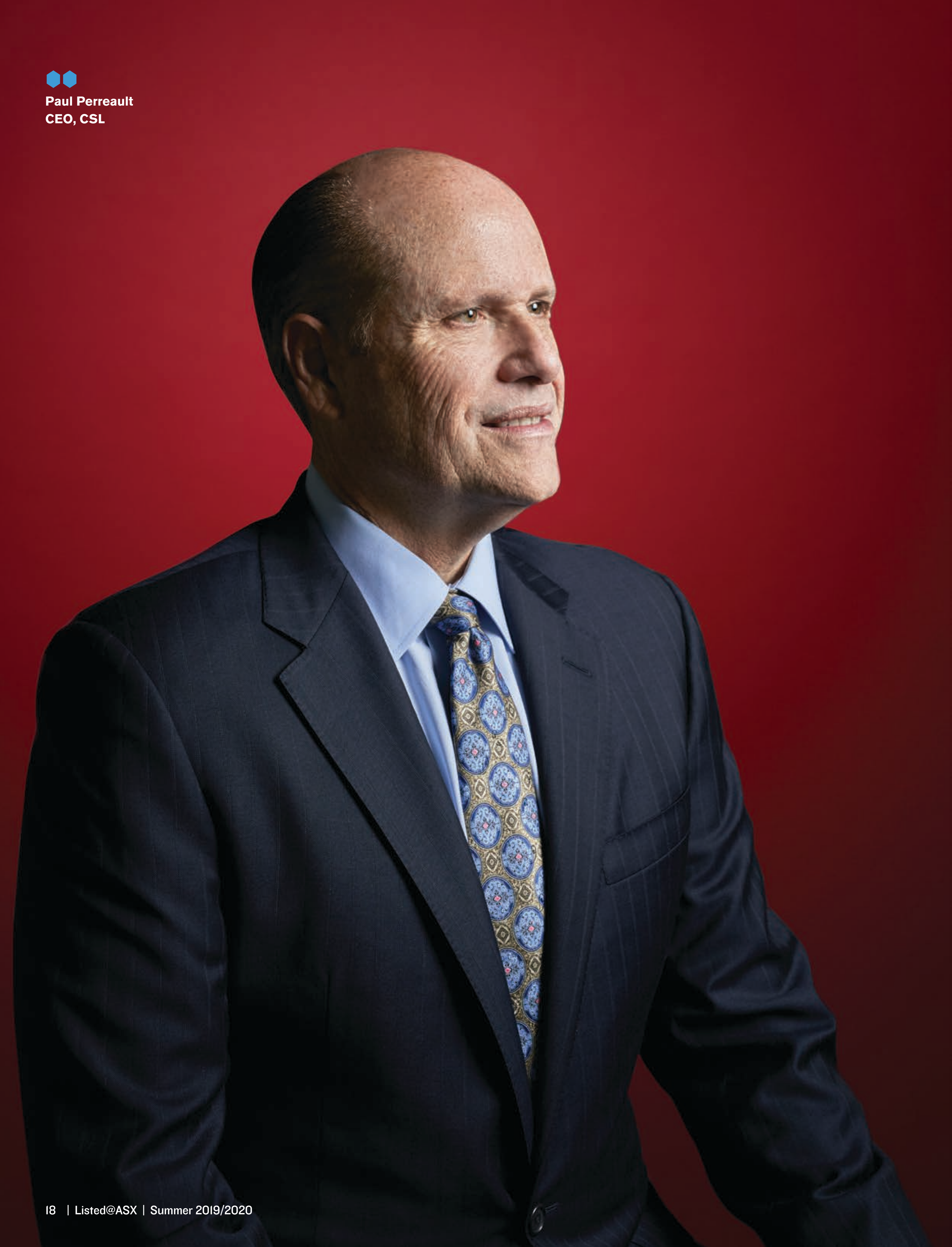

Paul Perreault
CEO, CSL

In a sign of confidence, global biotechnology manufacturer CSL plans over the next five years to double the number of scientists it can house at its global headquarter in Melbourne's Parkville biomedical precinct by constructing a third, on-site research laboratory. There will be more white coats walking the corridors than you can poke a test tube at. The company's medicine cabinet already holds lifesaving, globally-distributed plasma and vaccine treatments, which last year raked in record revenues of $12.2 billion. Its scientists are also concocting a slew of others to be trialled for public release, some in biotech products.

Started from scratch during World War I by a federal government that urgently needed to secure critical domestic drug supplies, CSL has grown to become a powerhouse. It zoomed ahead after being privatised 25 years ago. CEO Paul Perreault is confident a disciplined focus and a pipeline of new drugs will keep the ball rolling.

The company is capitalised at around $110 billion, meaning that it is neck and neck with BHP Billiton for the honours of being the second-largest listed entity after the Commonwealth Bank. If events run as the US-born Perreault plans, outright leadership might not be far over the horizon. It has already outpaced the other major banks and mining companies that for decades have dominated Australia's blue chip scene. One gauge of its rise is its value, which is more than 350 times the $299 million capitalisation it reached when trading ended on the day of its ASX debut. Gross profit margins top 50 per cent, critical to it returning more than half its capital by way of dividends and buybacks during the last decade. It's not always up, however. The shares can be volatile depending on currency movements, and it had to act decisively in recent years to secure the long-term viability of its flu vaccine business.

BECOMING THE BLOOD BEHEMOTH

The homegrown biotech has constantly met the market's expectations and boasts stable and respected management. New opportunities in China and treating heart attacks should keep CSL on investors' radars.

By Alan Deans

Photography by James Braund

"We never intended to be this big," Perreault concedes. "It's never been a goal to be the largest company in Australia. It's because of us investing back into the business, and understanding the need for discipline and focus, that we are where we are today.

"Going global is satisfying, but that's not the goal. The goal is to take care of patients around the globe. We have to continue to deliver, to stay focused. We can't let it go to our heads if we become the largest company on ASX. We can't confuse our values."

Explaining his commitment to build new labs and speed up the pace of product launches, Perreault says: "We are the largest private investor in biotech research and development in Australia, and it's really important that we continue to invest. We have a hub and spoke model, with the hub for research based here. We have spokes in Germany, Switzerland and the US and, through all of them, we run research and development as a truly global model. The development work – most of the clinical trials – are run out of the US because of their scale.

"But the research labs that we're building here are not just for us. We will have space to help start-up biotechs within our buildings. They will have access to our scientists and to projects that are synergistic with what we are doing. The precinct aims to be an incubator that can foster that next level of science. If you meet some of the best medical researchers around the country, you'll find most of them have worked at CSL at one time. And that's why it's extremely important to maintain a high quality of research in Australia.

"People will come from our sites in Switzerland and the US for assignments, but most of the jobs will be for Australians. We want to encourage the federal government to continue investing in education and the sciences. It's important that we maintain that part of the ecosystem, because it can be really tough on scientists here."

CSL has kindled significant investor interest in recent years with its disciplined approach to developing new medicines and for the turnaround in the Seqirus flu vaccine business. That gives Perreault breathing space to focus on the long-term challenge of how best to use its technological advantages to deliver greater global scale.

"What keeps us moving forward has a lot to do with the products that we manufacture," he explains. "Our products are really non-discretionary pharmaceuticals, compared with the ones made by our counterparts. Demand and growth for these products across the globe really contributes to the strong base of our business. Countries need a healthy workforce to be able to survive during the bad times and thrive in the good. I'm not saying that we are recession proof, but you need healthy workers to sustain our economies. And ours are lifesaving, widely-accepted medicines."

Most of its products fall within CSL's Behring plasma therapies arm, which accounts for 85 per cent of total sales. These medicines depend on plasma supplies from the company's extensive global blood collection centres. There are more than 220 such clinics, and more are being added at a rapid rate to ensure it can supply the fuel for its own growth. Plasma contains something like 3,500 different proteins, a small number of which form the basis of drugs used for life-saving operations. CSL currently processes only about 20 of these proteins, but it is working hard to find and develop treatments involving others. Proteins help power many bodily functions, including the immune system. They are essential for blood clotting and for moving lipids, hormones, vitamins and minerals around the body. Plasma is therefore critical in developing new treatments to improve and prolong life.

The two core plasma types the company specialises in are immunoglobulin, which aids the body's immune response to bacteria and viruses, and albumin, which regulates blood pressure and is widely used in operating theatres and at accident scenes to reduce bleeding. These are everyday products in common use, and together they make CSL the world leader in the $US30 billion plasma therapy industry.

Five new drugs have been brought to market from within these two product strands since 2016. CSL talks about them as being some of the most successful launches in the industry, and they already make significant contributions to their bottom line. Their success helps to drive forward the development of new drugs. The first, Idelvion, is a coagulant used in the treatment of haemophilia B. Afstyla serves a similar function for patients with haemophilia A and Haegarda helps reduce swelling and painful attacks for those with hereditary angioedema. Privigen and Hizentra help prevent infections. They are all in high demand.

The influenza side of the business, Seqirus, has been revamped after a period of under-performance. It is now a global leader because it is armed with a new and more effective means of producing vaccines on a global scale. Eggs traditionally have been used to grow them but, since buying drug maker Novartis's flu business in 2014, it can now be done more quickly and with improved effectiveness by cultivating the vaccine within cells. They are made on three continents, where they can be quickly dispatched to immunise masses of people. Perreault says its new vaccine, Flucelvax, shows a 34 per cent reduction in flu related symptoms and a 12.5 per cent reduction in hospitalisations.

CSL partners with many governments to ensure supplies are ready in case of a pandemic outbreak. While we haven't had such an emergency since swine flu erupted in 2009, it could strike at any time and cause millions of deaths. The impact of flu can be much higher than other infectious diseases, including HIV/aids, pneumococcal disease and tuberculosis.

One cloud to emerge globally for businesses in recent times is uncertainty about exports to China in the wake of the US trade war. Once a booming source of demand for Aussie products, from baby formula to iron ore, this disruption is having serious repercussions because of a slowing in global growth and orders being slashed. Not so for CSL, at least not yet. "We haven't seen it in our business at all," Perreault says. "We've had operations there for more than 20 years, and sell a lot of product there. We export a single product – albumin – which has become the third largest pharmaceutical product in China. We are held in fairly high regard. It would

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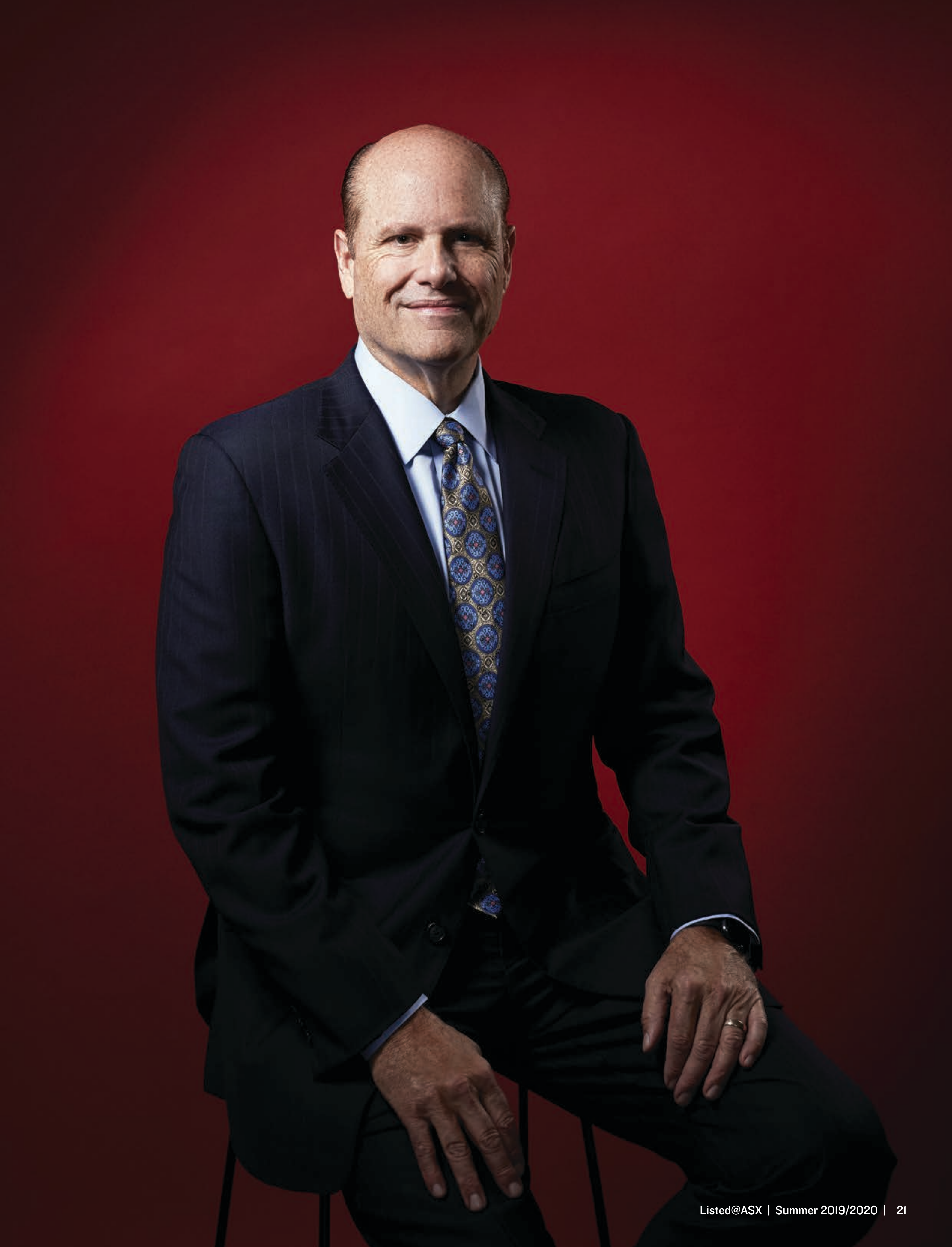

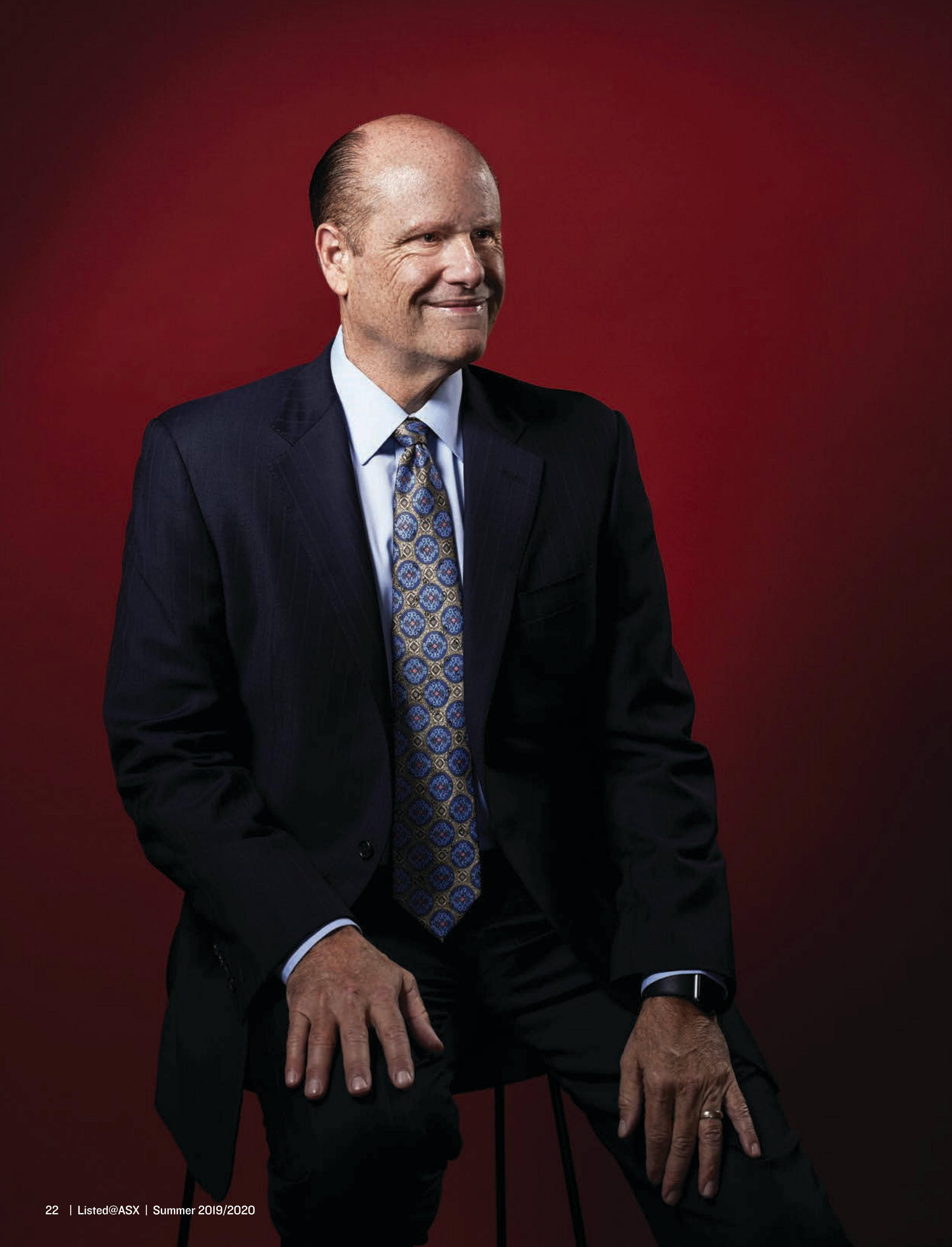

be difficult for the Chinese to meet the growing demand for this product without a top-up from imports. There are local manufacturers, but this is a complex business and they share the same difficulties in terms of scale and raw material supply. Of course, we keep a close eye on geopolitical developments around the world but, I would say, where we stand today, we think it will be OK."

Investors have been nervous, however, because China accounts for about 40 per cent of global demand for albumin. Working in CSL's favour is that it is adopting a new model for collecting blood in that country. It will become a so-called tier one distributor, removing its reliance on third parties and improving access to clinicians. That means obtaining a new type of operating licence and making changes to its blood collection system, which will take six to 12 months to complete. There will be higher costs, but CSL seems confident it will maintain strong growth in albumin sales. Stockbroking analysts who cover the company have recently made cuts to their estimates of albumin revenues in China, at least for the next year or so. For its part, the company says revenues would return to normal within two years.

Whatever the short-term distractions may be, Perreault says he is focusing attention on the long game.

"My main message has been around consistent delivery. It's about understanding what the market drivers are so we know we're going to continue to grow. Is this the end of our growth? Are our margins growing? What do the results look like in the different divisions? We're continuing to focus on the core of the business."

His core motivation is that, where growth is identified, funds need to be committed to boost capacity to ensure that opportunities are maximised. While that may sound simple, a key to success is having a detailed understanding of what the competitive environment is like. When a gap emerges that others don't see, Perreault aims to fill the opportunity. This is not a short-term pre-occupation. Rather, it is front-of-mind when he is looking at market dynamics 10 or more years into the future. While he may no longer be at CSL by then, he believes that the real measure of success depends on being able to identify industry dynamics that can be developed well before others.

"The strategy involves thinking long-term, because in our business the transition from research to commercialisation takes anywhere from eight to 12 years. For R&D, thinking now about the things that are coming in 2030 would be too late. That groundwork has already been laid, so it's also about long-term preparation. And it's understanding what you have in research, what you have in Phase I trials, what you have in Phase 2, and when that product will be approved and launched, so that we're successful. It's also making sure the pipeline is delivering over that time, and that we're continuing to invest in the base business."

This poses the question of what CSL will look like in 10 years.

"I see a company that really takes care of patients with unmet medical needs. A company that has a culture of employee engagement that's high. That has a culture of integrity that is unsurpassed, in terms of the industry. There are people who give lip service to these things, who don't really deliver every day. But it must be more than a poster on the wall.

"Overall, I'd say we will increase our portfolio, be operating in more countries and will bring more products to patients who are currently underserved. By 2030, we will also have very differentiated products for patients who have had no other options prior to CSL bringing them to market."

Another question is the future approach to acquisitions.

"I've probably looked at 100 opportunities in the last year. You have to look hard and look broadly. That's what is good about having a long-term strategy. We build in optionality, as not everything will work. Clinical trials are great, but there's risk there. Some may or may not work. It depends on the patient outcomes. But, if you have to grow by acquisition alone, it means your strategy isn't working too well. That is why we have a long-term growth perspective based just on the core business.

"Having said that, what we look for in acquisitions is different. I've seen people acquire things when they don't have another strategy to grow. That helps them for a couple of years, but then they struggle. Sometimes they struggle so much that they say what they bought is no longer core. That can be a code for 'we couldn't make it work'.

"[That makes us] very cautious about acquisitions and also about making sure they stay within our core competencies. We're a very focused organisation. We know what we do well. We do complex, hard biologics very well. About 50 per cent of the world's research and development money is spent today in oncology. I probably won't be going there. We are not going to compete with the Bristol-Myers Squibbs, and the Pfizers and Johnson & Johnson's of the world in oncology. I've got plenty of other things to invest in that I think are beneficial for the company, and that fall within our capabilities and know how.

"But it's one of those things that you do take a look at. If it's in haematology or coagulation, I'm interested. If it's in immunology, I'm interested. If it's in transplantation, I'm interested. If it's in cardiovascular and metabolic, I'm interested. If it's in neurology, I'm interested. If it's in implants, I'm probably not interested. If it's in diabetes, probably not. You really have to have discipline, because there's only so much research and development money to spend."

Perreault is only CSL's second CEO since the company listed. Before him, Brian McNamee had been in the hot seat for 23 years and retired in 2013. He led the privatisation and also the global growth strategy. After leaving, he stayed closely connected to the industry, by advising private equity business Kohlberg Kravis Roberts on its global pharmaceutical and healthcare investments and other private start-ups. He returned to CSL as chairman nearly two years ago.

Perreault says he is very happy to have him back. "To see us where we are today, after 25 years of McNamee's leadership and then my good fortune to step in and lead has just been fantastic.

"TO SEE US WHERE WE ARE TODAY, AFTER 25 YEARS OF MCNAMEE'S LEADERSHIP AND THEN MY GOOD FORTUNE TO STEP IN AND LEAD HAS JUST BEEN FANTASTIC."

"THE STRATEGY INVOLVES THINKING LONG TERM, BECAUSE IN OUR BUSINESS THE TRANSITION FROM RESEARCH TO COMMERCIALISATION TAKES ANYWHERE FROM EIGHT TO 12 YEARS."

"We worked together for a number of years and he advocated for me when the board was looking for a successor. Brian and I speak weekly. We keep up-to-date. He's a great person to bounce ideas off from a strategic point of view. He brings a different perspective now, as chair, to the table, and keeps me focused on governance.

"We work very well together. He's a good agent as well as a good boss, and he cares deeply about CSL. He's probably been approached to be on many, many boards in Australia. But, because of his affinity for the science, with his medical background and his belief in CSL, he took on the chair's role. We're alike in some ways and different in others, but that's what makes the world go around."

It should be a tremendous advantage to have such a depth of experience at the top. A core measure of the company's ongoing success will be its ability to continue bringing signficant new drugs to market. Ultimately, that's primarily how pharmaceutical companies are judged.

The biggest single rainbow on the horizon is C112, a plasma-derived product aimed at halting ongoing heart attacks by unclogging cholesterol in patients' arteries. It has passed its Phase I and 2 trials, and Phase 3 trials are underway to assess its efficacy and safety on 17,400 patients recruited from 1,000 medical centres around the world. It is by far the largest drug trial undertaken by the company, and its hopes for a successful outcome are high. In the US alone, around 800,000 acute cases occur each year that could benefit from C112. Each one now confronts the possibility of subsequent attacks within weeks and months without such treatment.

Further out on the horizon are stem cell-derived products about which CSL has said little. They focus on rare immune disorders. It gained access to this technology a couple of years ago when it bought the US company Calimmune. Perreault says the first target they are working on is sickle cell disease, a group of hereditary blood disorders, the most common being anaemia. "If it works in sickle cell, there's a good chance it will have applications elsewhere," he says.

When talking about the factors that have lifted CSL to its current position, Perreault first mentions research and development along with innovation. R&D is the life blood of the business, he says, but innovation has to stretch beyond that to extend through the whole company. It needs to find better ways to do things.

"It's never been a goal to be the largest company in Australia. But it's because of the investments we make back into the business, and the understanding, discipline and focus that we have that has got us to where we are."

On the road

Paul Perreault has been road showing CSL's latest results in recent weeks after what investors broadly concluded was another strong operating and financial performance. Earnings climbed by 17 per cent, with the help of lower than expected tax provisions. Investors seem to have taken that in their stride. Perhaps one reason is guidance given on 2020's bottom line earnings growth of seven to ten per cent, fuelled by a six per cent gain in revenues. Another one might be the poor comparative returns being posted by other listed majors.

Perreault says his main messages to investors and analysts were based around consistency of delivery by the business. He focused on helping them to understand the main business drivers. They wanted to know whether the business's growth was sustainable, whether margins were rising and how the different divisions were performing.

"My main messages are the same as they've been for the last six or seven years. They are that we're continuing to focus on the core of the business. We're continuing to invest back into infrastructure, plant and equipment and raw materials, because we do that when we see demand coming. We have to be ready.

"It's about understanding what the competitive situation is, and it's about really making sure that we're investing ahead of the demand so that we don't get caught short. Where my competitors struggle is in that area. So, I've been telling investors about our game plan and strategy. My focus today is beyond 2030. If I was only focused about next year, I probably shouldn't be CEO of the company. That strategy should have been set years ago."

Perreault's comments, supported by another strong set of earnings numbers, appear to have hit the mark. Goldman Sachs told clients that it had lifted target price guidance from $223 to $249-a-share. It noted that organic earnings growth of 11 per cent was a rare proposition in a mature health care industry. It also said that CSL was cheap compared with its five-year average, and also was priced well compared with other leading Australian drug and medical device companies. "Despite directly incorporating a number of competitive threats [in our model], we still forecast a 12 per cent earnings per share capitalised annual growth rate through to 2021-22. Longer term there are a number of questions that the plasma industry must collectively answer, but we believe risk-reward is skewed in CSL's favour given its current positioning and track record, not to mention balance sheet optionality."

Perreault: "When I talk to the investors, that's really what we talk about. The workings of the business, what levers we're pulling, where do we see demand going, our investments. And then you always get the question about line items, sending me to page 140 of the accounts, digging into the minutiae. They're good questions.

"It was satisfying to hear one of the investors on the roadshow thank us for being good stewards of their clients' money. The money aspect is not my primary focus, but it's important to have investors that are there long term for you. I want to see investors who have helped CSL for a long time continue to help us. They are now a very stable, loyal investor base."