

Meet the man whose company just sold for \$2.58 billion

By Kristen Schorsch November 21, 2015

David Jonas doesn't like to sit idle. He plays tennis, not golf. He's an early riser, often starting his day with a run of 4 to 5 miles on an empty stomach. When he retired from **Baxter International** after 25 years, he started a new company. It just sold for \$2.58 billion.

"Some people have hobbies," says Jonas, 72, sitting in the suburban office of the investment firm that he and his son Jonathan run. "I like the challenge."

In 2003, his challenge was to turn around a money-losing business that Baxter no longer wanted. That business, **PharMEDium Healthcare**, is now a leader in the **niche industry** of compounding, or mixing drugs that hospitals can't get from the traditional pharmaceutical market. Health systems generally used to make these medications themselves. But the work can be expensive, time-consuming, wasteful and even dangerous. As a result, hospitals have begun outsourcing the task.

Specialist suppliers face the same challenges. A bad batch of steroid injections distributed by a competitor, New England Compounding Center, caused meningitis and other infections in 2012 that killed more than 60 people and sickened more than 750, according to the **Centers for Disease Control and Prevention**. The suburban Boston business closed and its executives face criminal charges.

Today, Lake Forest-based PharMEDium has about 70 percent of the market, with much of the rest shared by a few thousand mom-and-pop outfits and regional players, according to analyst and research reports. It's a hard industry to break into. The compounding business requires a heavy investment in equipment and facilities, an obsession with sterile procedures and a reputation for getting it right, all while under tougher review by the **U.S. Food and Drug Administration**.

"I just don't think that there's really a meaningful competitor in the space today," Gordon Pan says of PharMEDium. The Chicago-based **Baird Capital** managing partner invested in PharMEDium in 2003.

Jonas, a director, owned 9.1 percent of the company, according to a filing with the **Securities and Exchange Commission**. That would put his proceeds from the sale to **AmerisourceBergen** at \$234 million. (New York private-equity firm **Clayton Dubilier & Rice** owned 89 percent of the company.)

PharMEDium produces more than 2,000 compounds and focuses on drugs for pain management, surgeries and epidurals for women in labor; they're available in a range of concentrations and containers, including syringes and IV bags. The company, which started with \$22 million in hospital contracts, is on track to generate \$465 million in revenue in 2015.

In an Aug. 31 filing for an initial public offering, PharMEDium touts its financial picture (sales increased 35 percent a year from 2012 to 2014, while gross margins averaged 36.4 percent) and stability (a more than 90 percent customer retention rate). It had about 3,000 hospital customers and 1,100 employees as of June 30, with four compounding facilities nationwide.

RISKS, UPSIDES

PharMEDium also discloses that it's a risky bet. Patients can be harmed or killed. The business has an open

warning letter and other notices stemming from FDA inspections at its compounding facilities since 2013. As hospitals consolidate and become bigger, they could demand lower prices. “We could become significantly less profitable,” the company says in the IPO filing.

The upsides clearly outweighed the risks to AmerisourceBergen, however. The Chesterbrook, Pa.-based pharmaceutical distributor, whose customers include Walgreens Boots Alliance and Express Scripts, swooped in after PharMEDium laid out its financials in the filing and **finalized** its all-cash purchase on Nov. 6.

“AmerisourceBergen is very diligent, very careful when it comes to what businesses they want to operate,” says Vishnu Lekraj, a health care analyst at Chicago-based **Morningstar**.

A spokeswoman for Ameri-sourceBergen declines to comment.

Born and raised in Israel, Jonas spent most of his childhood on a small chicken farm north of Tel Aviv. After wrapping up a required stint in the Israeli military, he moved to London in 1965 at age 21 before heading to the U.S. for college a year later. He spent his freshman year at Northern Illinois University in DeKalb, then transferred to Roosevelt University in Chicago, where he earned a bachelor's in finance and accounting and an MBA.

After four years as a Chicago-based trade representative for the Israeli government, working to stimulate business throughout the Midwest, he joined Baxter, a company he encountered while on the job. Jonas worked his way up the ranks at the Deerfield-based medical products maker. His management roles included running a Baxter subsidiary in Israel and buying and selling businesses worldwide. He retired from Baxter in 2000, but that didn't last. “I was looking for a deal to start a company,” he says.

In 2003, he spent \$3.5 million for \$22 million worth of hospital contracts from Baxter, which did compounding as part of a business segment. Baxter was losing money on it because the company sold the entire compounding product, everything from the IV bag to the drug but didn't charge for the service. Jonas says he focused on service and getting more customers on board. PharMEDium also outsourced the various compounding pieces, retaining final assembly and delivery.

“He had the ability to focus on those kinds of things that we weren't interested in,” says David Drohan, who was president of Baxter's medication delivery division when it was sold. “Small businesses like that, that have a real opportunity on the outside, tend to lose focus in a big corporation because every business is fighting for funding.”

Rush University Medical Center is among PharMEDium's clients. It buys anesthesia syringes, ready-made to inject into a patient's IV for surgery, says Thomas Wheeler, corporate director of pharmacy. Decades ago, anesthesiologists would dilute their own drugs and label vials with a piece of tape. No expiration date. No sense of who made it. The practice was time-consuming for the doctor, potentially dangerous if the drug expired and was used on another patient and wasteful if the hospital didn't use the whole dose, since it couldn't sit on the shelf for long.

SUCCESSFUL INVESTMENT

While it tends to be cheaper to compound drugs in-house, Wheeler says, “all told, almost every hospital I'm aware of benefits from this kind of service. The turnaround for surgery now is so quick that in the larger hospitals minutes count.”

Still, like other hospitals, Rush mixes most of its drugs itself, including antibiotics, which vary from patient to patient.

Baird Capital's Pan won't say how much Baird made when it sold its stake in PharMEDium two years ago, but

he says it was “the most successful investment our firm has ever made.” (Baird opened in 1989.)

As for Jonas, who relinquished his roles as CEO and board chairman in 2014, he says he's already busy with his next ventures, including an Israeli IT company and a business that sells wristbands to quell nausea.
