China: Behind the Screen – An Interview with Peter Young of Young & Partners
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China is driving much of the growth in global pharmaceutical sales, with a rare consensus among big pharma CEOs that no company can be a player without having a big stake in the country. To shed some light on the market's potential, Pharm Exec sat down with Peter Young, president and managing partner of Young & Partners, who has just returned from an industry-sponsored trip to China, where he met with government and industry officials to review the investment and M&A climate for medicines.

You have just returned from a visit to China related to the development of the biotech and life sciences sector. What is the state of the economy at present? How will the external pressures on China to stimulate domestic consumption rather than export-led growth impact the overall climate for business investment?

China has continued to grow its economy and was able to do so even through the global recession and financial crisis of 2008-2009. In addition, expansion in consumer spending has been fairly robust and driving an increasing emphasis on domestic consumption as a source of economic growth and less on export driven growth. Although most people expect growth to continue, I noted during my visit some signs of disruption. Trends to watch include an overheated housing and construction market, significant manufacturing cost inflation (particularly with regard to energy, raw materials, and labor) and increasing tension between the "haves" and "have nots," as income disparities have increased. In this latter case, the Chinese central government in Beijing is working hard to slowly prick the housing bubble, control cost inflation, and head off internal tensions, but these are all difficult problems to solve. Also, as is the case in the US and Europe, there is concern that the economy will be adversely affected when the government stimulus programs enacted last year subside. Thus, while it is hard to bet against continued strong growth of the Chinese economy, the challenges to continued high growth are increasing.

There have also been a number of high profile claims by foreign companies that the environment for foreign companies has become more difficult with regard to regulations, import/export policies, etc.

What is the state of health care services in China today and what role does pharmaceutical therapy play in the mix?

There is a general belief that the healthcare system in China is not functioning well. The list of problems is long. First, basic medical insurance coverage is poor throughout the country and access to services covered by insurance is unequal. Although the Chinese government is trying to tackle this problem, the number of Chinese who have insurance coverage is extremely low. Most people have to pay for medical care themselves, particularly outside the major cities and industrial centers. As is the case in many developing countries, an unanticipated financial hit from a serious illness can push the aspiring middle class family into financial distress. It is clear that the Chinese government is working to create stronger health care coverage and safety nets, but it is expensive and will take time.

Second, the Chinese healthcare system is built around hospitals; most physicians work for these institutions. The majority of the hospitals are government owned and struggle to maintain profitability and adequate resources. Outside the big cities, the quality of the hospitals and their resources falls dramatically. Drugs sold to patients are a major source of income for hospitals and physicians employed by them which clearly creates a conflict of interest with regard to what drugs are prescribed and in what quantity.

What is unique about the Chinese pharmaceutical market, particularly in terms of the strategic positions of local Chinese and foreign-based pharma companies?

The structure of the Chinese health care system and the way in which drugs are prescribed has a significant impact on marketing and distribution strategies. For example, it is easier than in Western markets to get to the prescribing decision-makers because they are concentrated in the hospital network. There is also a large and important market for traditional Chinese medicines. Third, the local industry consists of thousands of independent players all operating in an environment that is much less regulated than in the West. The government is working to further build up its capacity to regulate manufacturing and promote the safety and efficacy of pharmaceutical ingredients, but there is a long way to go relative to the standards in place in the US, Europe, and Japan. Last, although there have been great strides with regard to intellectual property rights, the rules and the enforcement of rules is not strong enough. This is a challenge for both Chinese and non-Chinese pharmaceutical companies.

Are you optimistic or pessimistic about the prospects for the foreign-based industry in China?

I am optimistic because the Chinese market is large and spending on health care will grow dramatically as medical insurance coverage improves and personal income escalates. Even though the distribution of income is skewed, the spending power of the rich and the emerging middle class is substantial. Expenditures on healthcare and, specifically pharmaceuticals, are growing very rapidly. Ultimately, the Chinese government will make progress with healthcare reform and improving the delivery of health care since it is a policy imperative critical to maintaining social stability. But the changes will take time. For some time, foreign companies have followed a variety of paths in China to try to achieve success. In fact, foreign companies bring many valuable assets to the table that are of great benefit to the Chinese. If China wants to build a world-class base in biopharma, it will have to encourage the participation of foreign pharma companies while managing the growth of its domestic companies.

Is there any hidden insight from your trip that should inform our thinking about health care in China?

The aging transition in China will occur much faster than what we have seen in other countries. I had a number of conversations with experts on aging during my trip, and it is clear that the demographics will shift fairly quickly to create a shortage of younger workers and a bulge in older, retired people. A major contributor to this scenario is the prolonged “one family, one child” policy that China enforced for many years, but has more recently curtailed. This will result in a premature aging of the population: although it will create new opportunities for pharma companies in managing chronic diseases around cardiovascular, pain and diabetes, the downside is labor shortages and an end to the inexpensive wages that helped fuel growth in the past.