Chi-Med's Sinopharm Deal Opens Doors To China Market For Partners, CEO Says

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Executive Summary

The joint venture allows the newly formed subsidiary Hutchison Sinopharm to sell pharmaceuticals all over China and become a "super partner" for multinationals selling medicines in the country.

HONG KONG – The end-of-year deal by Chi-Med's drug R&D division Hutchison China MediTech Ltd. to establish a joint venture with Sinopharm Group Co. Ltd. will enable it to both market and distribute drugs "pan-China" and also establish itself as a "super partner" of multinationals by selling third-party medicines, according to Chi-Med CEO Christian Hogg.

The joint venture could put the China-based pharmaceutical and health care company in a "lead position," Hogg said of the deal that saw Chi-Med's wholly owned subsidiary invest $9.8 million into**Sinopharm Holding HuYong Pharmaceutical (Shanghai) Co.**, giving Chi-Med a 51% equity share of the new subsidiary, which will be renamed **Hutchison Whampoa Sinopharm Pharmaceuticals (Shanghai) Co. Ltd.**, also known as Hutchison Sinopharm.

Hogg told *PharmAsia News* just before the New Year that Chi-Med was "previously handicapped" in the China market because its business license only allowed the sale of products it manufactured. Putting the two companies together would overcome this hurdle and build on the pair's complementary qualities.

"There's no bigger and better than Sinopharm in China, and we are very well recognized too," Hogg said. "The value of the deal to Chi-Med is obvious because it allows the company, through the joint venture, to sell pharmaceuticals pan-China."

"As a commercial vehicle for multinationals to bring non-core products into China, the new entity opens wide doors since Sinopharm is basically without peers when it comes to distribution logistics in China; whereas what Chi-Med does really well is commercialization and marketing of products," Hogg added.

"We needed this vehicle. The fact that it is Sinopharm, the biggest distributor in China is fantastic. It allows us to tap into this network as a partner rather than just being a client and brings together the core strengths of both sides."

JV To Market Chi-Med, MNC Products

The joint venture intends to sell both Chi-Med pharmaceuticals and those of multinational companies, Hogg said. "We will be a 'super partner' to bring products in for multinationals. Most of these companies have a very broad portfolio of products. If they have a top 20 product and are looking for a good commercial partner to bring products into China – they will choose us."

In addition, the JV could also benefit from China's anti-corruption probes if multinational companies move to an outsourced sales model for off-patent drugs that are increasingly under pricing pressure. During its Aug. 23

earnings call, Sinopharm said that MNCs have already closed sales offices in some provinces and reps are visiting physicians less in the wake of the industry-wide corruption probe and pricing headwinds.

“With the implementation of more anti-corruption policies and the probes on prices, MNC drugs could face more pricing pressures, the sales model could change and global pharma companies could potentially exploit outsource sales models for the off-patent drugs,” the company told analysts on the call, according to a translation provided by Citi Research ("Sinopharm Positions Itself For MNCs That May Need To Change Sales Models In China" — *PharmAsia News,* Aug. 28, 2013 6:53 PM GMT).

Hogg said of the 51-49% equity structure Chi-Med hammered out with Sinopharm – rather than a 50-50 deal – “pulls all the strings together and is driven by the commercial focus. In theory you could say that we are in a leading position but we have to see how that will play out.”

The companies said Hutchison Sinopharm will provide “a platform for synergy” across the China Healthcare Division of Chi-Med by utilizing the services of Chi-Med’s 2,800-person prescription drug and over-the-counter drug sales team in China. In 2012 the China Healthcare Division and jointly controlled subsidiaries of Chi-Med posted $350.5 million in sales and a net profit of $15.5 million.

Huyong, which has fewer than 100 employees made a pre-tax profit for 2012 of $1 million and had gross assets of $29.9 million at the end of the year.

Hogg emphasized the money invested by Chi-Med would remain in the joint venture to boost its development and create new products. He expects the deal to receive regulatory approval in January 2014 or “soon after.”

Plenty Of Opportunity In A Big Market

As for the new joint-venture company’s competitors, “There are a few out there and they may be more established but they don’t have the pedigree of Sinopharm and China-Med. There’s plenty of opportunity for everyone, it’s a big market.”

One potential competitor in the space is **SciClone Pharmaceuticals Inc.**, a U.S.-listed, China-focused specialty pharma that sells off-patent medications in China for several big pharma, including**Pfizer Inc.** and **Baxter International Inc.** However, SciClone has seen its share of troubles recently, losing a major contract with **Sanofi**, as it looked to renegotiate terms to make its outsourced sales model more profitable ("China's Outsource Sales Model Takes A Big Step: SciClone Takes Out NovaMed" — *PharmAsia News,* Apr. 19, 2011 5:00 PM GMT) and ("SciClone CEO Friedhelm Blobel On Building A Specialty Pharma Business In China: An Interview With PharmAsia News (Part 2 of 2)" — *PharmAsia News,* Jan. 30, 2013 5:03 PM GMT).

As part of the central government’s 12th Five-Year Plan there has been significant investment in health care to drive forward “inclusive growth” or “quality over quantity.” This should continue for the next five to 10 years, Hogg said.

An aging populace, the effects of pollution, changes in diet and a subsequent rise in chronic diseases mean there is more of a burden on the domestic health care industry, providing gilt-edged opportunities for health care providers, notably international investors ("Shanghai Free Trade Zone Will Impact Foreign Investment In Health Care Sectors" — *PharmAsia News,* Dec. 5, 2013 7:55 PM GMT).

There has been 21% growth in pharmaceuticals for the past five years in China, accounting for $98 billion in retail sales value in 2012, according to a McKinsey & Company report published in collaboration with PharmAsia News. The report suggests the country’s pharmaceutical market will grow at a rate of 17% through 2020, realizing $310 billion in sales value ("New Growth Models In China: McKinsey-PharmAsia Summit Report Preview" — *PharmAsia News*, Oct. 15, 2013 8:40 AM GMT).