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Seeking an Innovative Pharmaceutical Industry

By Dmitry Genkin

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Do you care about where the medications you take were produced? The Industry and Trade Ministry certainly does. In 2008, the ministry first announced its "Strategy for the development of pharmaceutical manufacturing in Russia," and the plan was immediately criticized as too ambitious by industry analysts and journalists. The aim was to raise the share of locally produced pharmaceuticals to 50 percent of domestic consumption (in monetary terms) by 2020, compared with 23 percent to 25 percent in 2008.

President Dmitry Medvedev stressed that target again in his state-of-the-nation address Tuesday and added that 60 percent of "innovative medicines" sold in Russia should be produced domestically.

This detail, "in monetary terms," is essential. The share of domestically produced drugs by volume is much more impressive, accounting for approximately three-quarters of local demand, according to industry analysts. Why is this? Simple: Russian pharmaceutical

companies on the whole produce extremely low-priced drugs.

Can the Industry and Trade Ministry persuade Russians to purchase even higher volumes of cheap, out-dated medications? The ministry's intent, of course, is different. Russian companies should produce higher-value and more innovative drugs, the strategy states. This is a real challenge, given that the development of one new medicine can take 10 years or more.

One more note here. The Russian government is not only a regulator for the pharmaceuticals market. It is also the largest consumer, buying about 25 percent of all medications sold in the country.

But being overly ambitious doesn't automatically mean being wrong. You may say it is almost impossible to create an innovative pharmaceuticals industry in 10 or 12 years — as required by the strategy. But it would be wrong to say that pharmaceutical research and development is not viable in Russia.

Another point, and the one that I believe is the most important, is that some people are skeptical about a government strategy simply because it was created by the government. Becoming innovative is not something that only the Industry and Trade Ministry wants. It is also something that companies need. The Russian pharmaceuticals market is changing, and you cannot be among the leaders with dated products like citramon and analgin in your portfolio. I will try to explain why.

Government purchases are the main driver of the Russian pharmaceutical market today. As DSM Group reported recently, government expenditures rose 10 percent to 12 percent in the first half of 2010 compared with the first half 2009, while retail sales through pharmacies showed a far slower growth rate of about 4 percent over the same period. So opportunities to grow faster and earn more exist — if the federal government or local governments are eager to buy your products.

What can the authorities purchase? Theoretically, the government is responsible for buying medications for people who have diseases that are considered the most serious, such as oncological or cardiovascular diseases.

Treatment requires new and expensive drugs, which are sometimes too expensive for the average Russian citizen. Pharmacy consumers, meanwhile, are generally more concerned about treating their colds or headaches. That can also be challenging, of course, but industry analysts report that average prices in retail channels are lower.

The consumption of pharmaceutical products in Russia is also changing. Fewer and fewer people are treating common illnesses with old-fashioned medications like citramon. Looking back to 2002, we see that 25 percent of medications sold in Russian pharmacies cost 30 rubles or less, according to Pharmexpert data. By 2009, this share had decreased to 8 percent.

"People understand that it is impossible to treat cancer with activated carbon, which means the share of extremely cheap medications will continue to decrease in the future," former Pharmexpert top manager David Melik-Gusseinov wrote in his research this year.

In fact, pharmaceutical companies in Russia do not have much choice if they are interested in

further growth.

The largest producers, which used to rely on over-the-counter medications, are now changing their portfolios, and one of the local pharmaceutical giants is currently investing millions of rubles in R&D projects.

At the same time, pharmaceutical research and development is not the sole responsibility of industry leaders. There are several smaller companies in the sector.

While their names may not be familiar to most readers, they are healthy, profitable businesses. Such smaller companies may choose to bring their products to market themselves, or to sell the rights to larger pharmaceutical producers.

Here in Russia we have not seen many such deals yet, but in some cases pharmaceutical giants are prepared to pay millions of dollars, or even tens of millions of dollars, for the rights to new medications.

There are many stories about entrepreneurs who managed to create large IT companies from only a web site with minimal startup capital — just because the idea was interesting and relevant.

In the pharmaceutical industry the story is a little different and much more complicated, but the principle is the same. If you have a good idea, you can make money; if, of course, you are lucky enough to pass through pre-clinical and clinical trials and prove your idea can treat a disease effectively.

If the government is eager to support such ideas, this is good news for local pharmaceutical companies. Because I have no doubt that innovative pharmaceutical producers can be successful in Russia. And I hope there will be Russian companies among them, not only multinationals.

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