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German Drugmaker Merck Flaunts Russian Expansion as Others Flee

By Howard Amos

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DARMSTADT, Germany — The Russian head of pharmaceutical and chemical giant Merck dreams of one day supplying golden pigment to gild the onion domes of Orthodox churches.

The German company is several years into a Russian expansion drive that top executives said remains unaltered despite a looming economic recession, a state-mandated localization drive, and deteriorating relations between Russia and the West over the Ukraine crisis.

"It is crucial to capture the niche markets," said Jurgen Konig, the head of Merck in Russia who was parachuted into the country to spearhead local growth after stints in South Korea and Pakistan.

Unlike its competitors, Merck is increasing its headcount on the ground: The company currently employes about 220 people, and expects to have over 300 by the end of the year. It is also looking to steadily boost the 150 million euros ($167 million) worth of sales it recorded in Russia last year.

Low Base, Fast Growth

Russia is already an established market for foreign drug manufacturers, with some estimates suggesting domestic production meets less than 20 percent of the market's needs. Leading players include France's Sanofi and Swiss-based Novartis, which both say they have over 1,000 employees in Russia.

From Merck's headquarters in the German city of Darmstadt, the hometown of the last Russian empress, Alexandra Feodorovna, chief executive Karl-Ludwig Kley was keen to highlight the long-established drugmaker's new focus on Russia.

"We gave gone through a major transformation of the company in the last seven or eight years and enlarged our portfolio considerably," Kley told The Moscow Times in an interview. "Relative to others we are late [to the Russian market], the base is low ... so you have to grow faster."

Merck, which saw 11.3 billion euros ($12.7) of sales last year, is also a chemical manufacturer known for producing the liquid crystals used to make display screens.

In Russia, the company is concentrating on health care and biotechnology products that are supplied to hospitals, research institutes and laboratories. It also has sidelines in other materials, including pigments used in the Lada-brand cars made by Russia's AvtoVAZ.

Approaching Recession

Merck's bullishness on Russia's prospects marks it out from other pharmaceutical companies, which have sought to trim staff numbers as the market stagnates amid a looming economic recession.

Inflation, running at levels not seen since 2002, means the Russian pharmaceutical market will grow 12 percent in ruble terms while shrinking 18 percent in dollar terms to $24.8 billion this year, according to forecasts by marketing agency DSM Group, cited by business daily Vedomosti last month. Russian officials expect the economy as a whole to contract by almost 3 percent this year.

Kley declined to comment on Merck's forecasts for the Russian pharmaceutical market. He also refused to give detailed figures to quantify Merck's expansion plans, but he said that the company was expecting double-digit growth in Russia in the coming years.

"I believe that we will see a recovery of the economy," said Kley. "When we decide to be present in a country like Russia we do it for the long term. ... Expansion is a rolling process that takes years."

Localization

Aside from the deteriorating investment climate, Merck in Russia also has to contend with a government-led drive to reduce the country's reliance on imported medicines. In May 2014, Prime Minister Dmitry Medvedev said that 90 percent of a list of strategically significant medicines should be domestically produced by 2018.

Merck has taken some steps towards localization through a partnership with the country's largest drugmaker, Pharmstandard, to produce and distribute Rebif, a medicine used to treat multiple sclerosis.

"They [Pharmstandard] will do the filling, finishing and packaging for us," said Kley. Merck made 1.8 billion euros ($2 billion) worldwide from sales of Rebif in 2014 — its most popular drug.

Kley made it clear there were limits to localization: all global supplies of Rebif, for example, are manufactured at one plant in Switzerland. "The complete value chain cannot be localized," he said, and added that even where it was possible, moving toward domestic production was a slow process that usually lasts years.

While looking to localize on the request of the government, Merck is also doing the opposite with other products as part of its new Russian strategy. "In the past we had given a number of our health care products to partners to market them in Russia, but in recent years we have started a process to repatriate those products," according to Kley.

Sanctions

Bans on some high technological imports were among the penalties imposed on Russia as part of the 2014 Western sanctions over the Kremlin's role in the Ukraine crisis — but Merck executives dismiss any notion that future sanctions, if the situation in Ukraine worsens, could touch their industry.

Prohibiting medicines that save lives is highly unlikely, according to Kley.

Similarly, Merck sees no barrier to working in Crimea, the southern Ukrainian region annexed by the Kremlin last year, because it argues that people should have access to medical treatment regardless of where they live.

In any case, for a global company like Merck, rolling the dice on Russia isn't the big gamble it might be for a smaller company. Only about 1 percent of its sales come from Russia, according to Kley, and so the company can brush past crises like the ruble's nearly 50 percent fall against the U.S. dollar last year.

"We are not overly dependent on Russia," he said. "We can deal with it."

The Moscow Times was a guest of Merck in Darmstadt.

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