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Responding To Challenges In The Chinese Healthcare Market

Part II: Local Product Procurement

[This is the second in a three-part series]

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The Chinese healthcare sector was once extremely attractive to multinationals who were able to sell their patented drugs and medical devices to a captive Chinese market. But those days have gone as China sets out on a long-term plan to tackle spiralling healthcare costs and make the sector more efficient.

Not only has the unit cost of drugs and medical devices risen sharply – with the result that every patient in the country is costing the government more and more - but at the same time demand for these products is soaring as consumers reap the benefits of having access to innovative new drugs and medical devices.

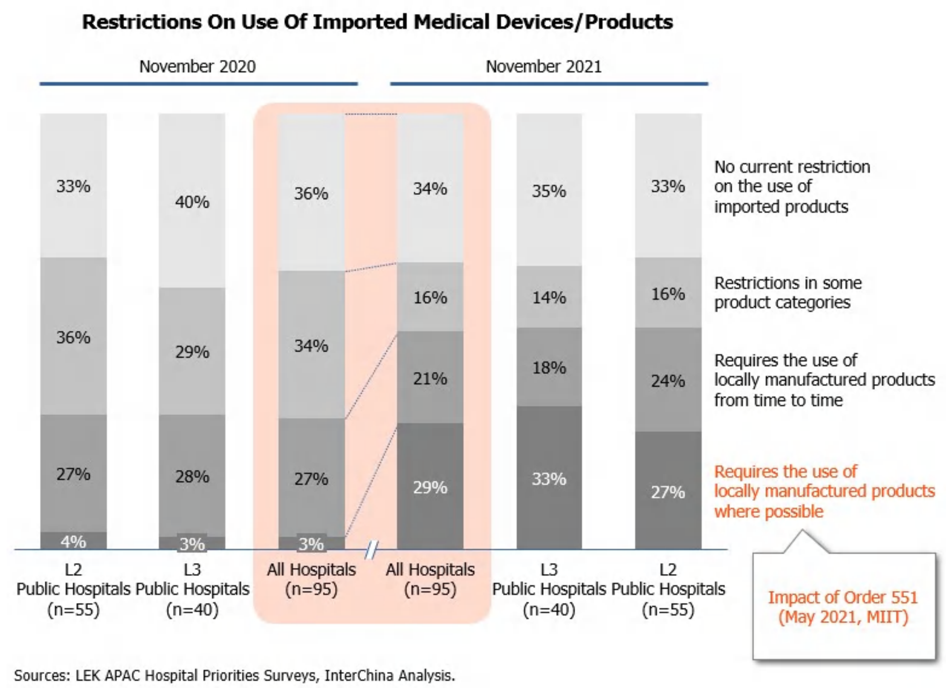
In a series of articles, we have been looking at the specific ways in which the government has tackled this huge issue and what multinationals need to be doing in response. We began our series with a look at the huge impact of the Volume Based Procurement (VBP) policy. In this second article we look at how a preference for the development of local manufacturing has become a core China strategy and what that means for multinationals.

Government focus

When the Chinese government first unveiled its Made in China 2025 initiative back in 2015 the healthcare sector had already been identified as a key area of focus in terms of developing home-grown players. Products including chemical drugs, traditional Chinese medicine, biopharma, medical devices and diagnostics were all earmarked for specific attention as part of the wider drive to reduce reliance on imports. Since then, there have been a series of policy announcements which have only further embedded this drive to support home-grown markets as much as possible.

For instance, in 2021 the MIIT (Ministry of Industry and Information Technology) and MoF (Ministry of Finance) issued 'document 551' which provides guidance on the procurement budget for 315 local products, including 178 medical items. This is also known as the 'buy local' directive and hospitals have been following suit, as the Chart#1 below clearly shows.

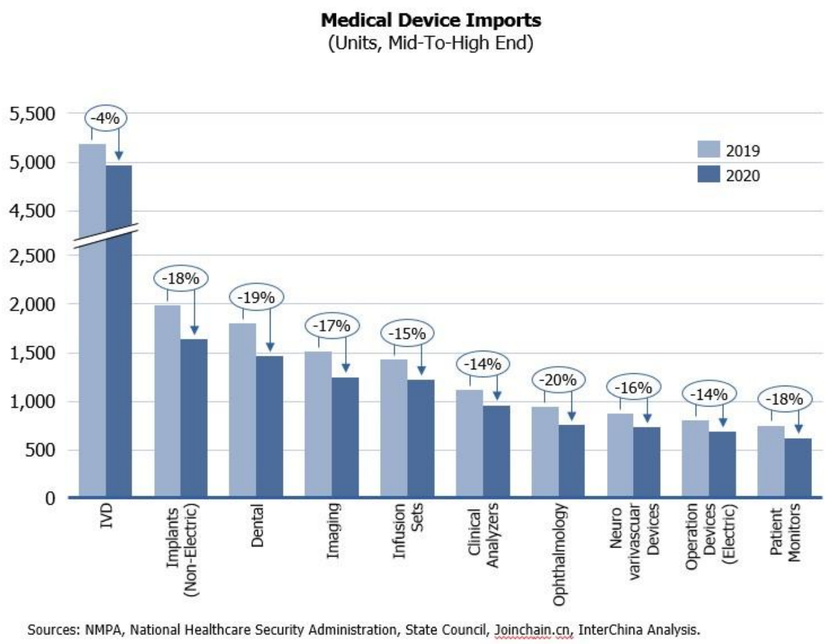
Chart #1



Impact

The impact of these policies today is significant. As the Chart#2 below shows, if you take just one year between 2019 and 2020 there was a huge reduction in the importation of mid- to high-end medical devices. The ophthalmology sector saw a fall of 20%, while sub-sectors such as implants, dental, imaging, and patient monitors, all saw falls approaching this figure too.

Chart #2



How multinationals should respond

In our last article we discussed how multinationals need a constant focus on innovation to succeed in this tough new environment. But we also discussed the importance of revamping supply chains, and central to this debate is the extent to which multinationals continue to set up their own to set up their own manufacturing sites in China, or whether they pursue a M&A strategy and acquire Chinese companies with facilities instead.

The response will depend on where each specific multinational sits in China, and also the specific markets they operate in. For instance, companies operating in areas such as therapeutics or diagnostics – making products such as dental implants, medical films and infusion sets – will typically be more active in local production already as these products are more likely to come under VBP.

Acquisitions?

Some multinationals will realise that the acquisition route is the preferred model if they want to be a serious player in the country. But if China already accounts for a big share of a multinational's global business (and especially if it already has extensive production facilities in the country) then its executives are likely to have more leverage and buy-in from head office to roll-out more investment in own plant and facilities. Alternatively, multinationals could opt for a mix of having both their own production facilities and acquiring local factories.

So, in short, multinationals essentially have three options:

Option One: Set up own local production with own product license

A number of multinationals are already employing this strategy. For instance, GE Healthcare has four production sites in Beijing, Wuxi, Shanghai and Tianjin, while Philips has plants in Suzhou and Shenzhen for imaging and patient monitoring respectively.

Thermo Fisher Scientific has had two plants in China since 2010. This year it also built its first single use manufacturing site in the Asia-Pacific region in Hangzhou which is described as a one-stop service for biomanufacturing. The factory offers integrated clinical and commercial packaging and labelling capabilities.

Option Two: Own local production and also consider acquisitions

Examples here include US medical devices company Medtronic which already has factories in Shanghai and Chengdu, but has also fully acquired Kanghui and Kangdi for orthopaedics and surgical products. Fellow US medical technology company BD has three factories in Suzhou, and in 2019 it acquired Jiangsu Pengyao pharma for IV infusion.

Option Three: Acquire a local company with the product licence under the acquired company

PerkinElmer has made two acquisitions in China, Suzhou SYM-BIO and Shanghai Haoyuan for diagnostic products. Other examples include Stryker which acquired Trauson for orthopaedics products, and Danaher which bought Suzhou Xitogen Technology for flow cytometry in 2019.

Towards a localised products strategy

Whichever model multinationals choose, the key is to ensure that their strategy is successful in terms of winning tenders. As the table of recent tenders in Chart #3 shows, this can be done either through a wholly owned manufacturing facility, or through a Chinese partner.

Chart #3

Multinational Solutions To Tenders With Local Product Procurement Requirement

	Year	Tender	Product	Supplier
Supplied By Own In-Country Production	2021	Xinjiang People Hospital	Pipette	ThermoFisher
	2022	Jiangxi Quannan County Hospital	Ceiling DR	GE Healthcare
	2022	Hainan National Health Commission	Patient monitor	GE Healthcare
	2022	Jiangsu Low Level Health Institutes	Doppler ultrasound	Philips Healthcare

	Year	Tender	Product	Supplier	Parent
Supplied By Acquired Company With In-Country Production	2021	Wuhan Hematology Center	Covid PCR test	SYM-BIO Biotechnology	Perkin Elmer
	2021	Fujian Hematology Center	HBV, HCV HIV test	Haoyuan Biotechnology	Perkin Elmer
	2021	Affiliated Hospital of Shanxi Datong Medical University	Skin stapler	Kangdi Medical	Medtronic
	2022	Sichuan Dazhou Tongchuan District Hospital	Gynecology operation table	Kanghui	Medtronic

Sources: www.bidcenter.com.cn, InterChina Analysis.

Next time

We take a closer look at a number of new medical insurance schemes and the impact they are having on the strategy of multinationals.

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Rick Woo is a Principal in InterChina's Strategy Practice. He has over 20 years experience in pharmaceutical and med devices sales in China and APAC, as well as rich strategic project management experience in Pharmaceuticals & Medical Devices sector.

About InterChina

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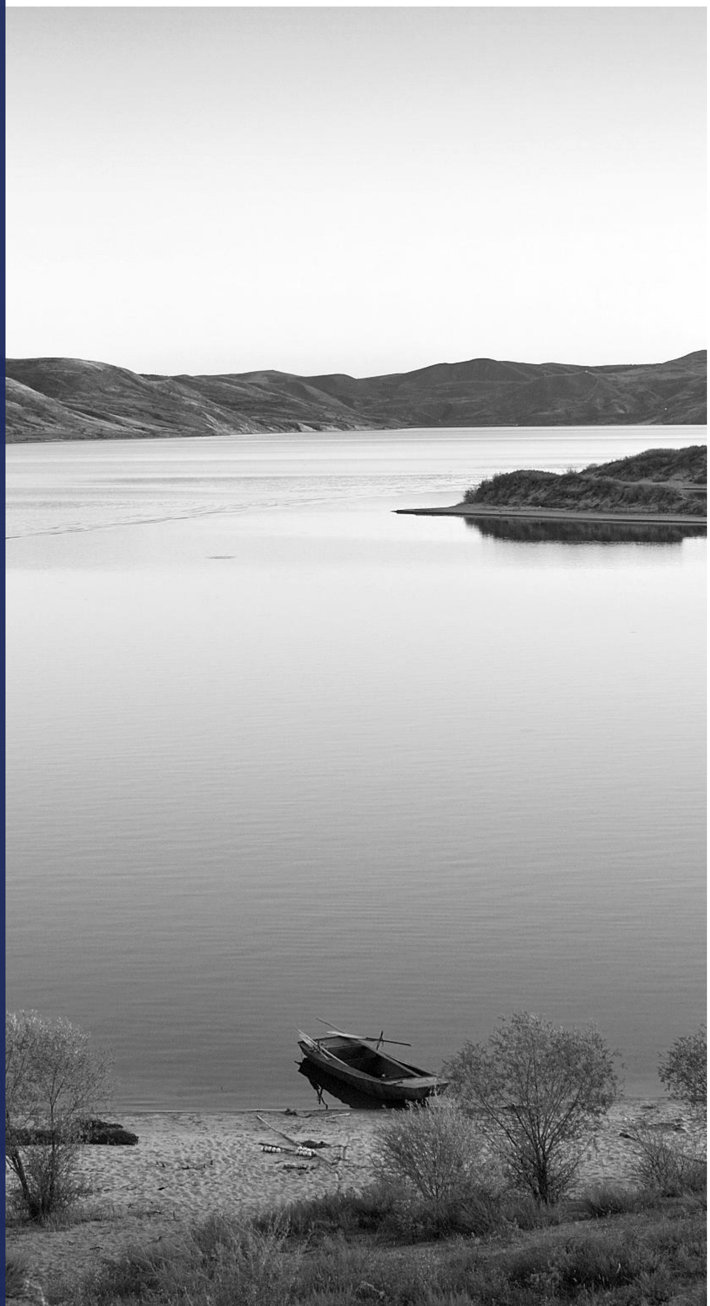

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