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What's next for pharma in emerging markets?

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Succeeding in emerging markets has been a challenging undertaking for multinational pharma companies, but those that adapt their end-to-end model for emerging markets could well thrive.

A few years ago, multinational pharma companies seeking growth and respite from market uncertainty in Europe and the United States found a haven in emerging markets. Their rapid economic growth triggered an expansion in healthcare coverage and the emergence of a new cohort of consumers able to afford larger out-of-pocket spending on drugs. But early euphoria was soon replaced by a more somber outlook. Some emerging markets either suffered downturns or showed weaker growth forecasts as commodity prices fell; some healthcare systems struggled to scale up adequately their provision of care; and local companies became increasingly effective competitors in the pharma market. Furthermore, multinationals themselves often found it difficult to scale up in emerging markets, with particular challenges in talent recruitment, compliance, and organizational setup.

By contrast, developed markets like the United States were doing rather well. Pipelines have been refreshed—for instance, the top ten pharma companies have some 650 products in development for oncology[1]—and new drugs are showing great promise. So should multinationals turn their attention away from emerging markets?

Although that might be tempting in the short run, we believe emerging markets are following a predictable cycle that will likely return them to a positive outlook before long—perhaps as soon as the current wave of launches is complete. In fact, we believe emerging markets could still see a doubling of pharma revenues for the top 20 markets in the next ten years (exhibit). The opportunity remains attractive even if we do not account for China, a large and strategic market for most pharma companies, independent of their strategy in emerging markets.

To capture opportunities for growth in these markets, multinationals must be prepared to take a long-term view, continue investing in emerging markets, and take calculated risks (see sidebar "Three insights"). To succeed in this and move on from the old "go and grow" mind-set, they need to (1) define clear long-term strategic objectives for emerging markets, (2) adapt the business model to the nature of emerging markets, and (3) build an agile organization tailored to emerging-market needs.

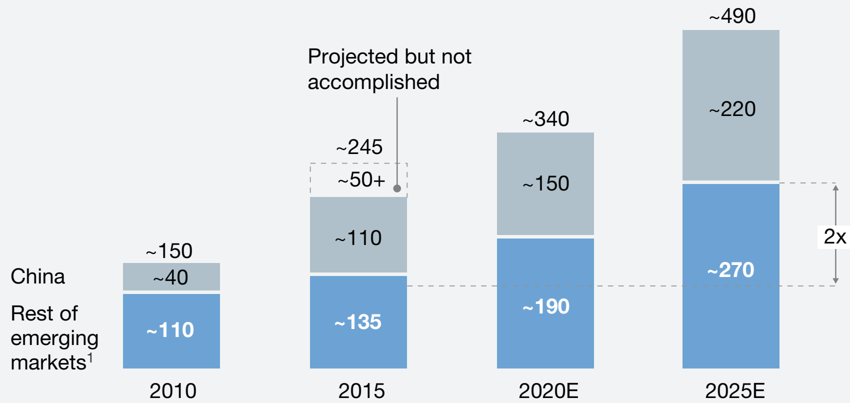
[1] Evaluate/pipeline.

Exhibit

Despite a mixed picture in recent years, the outlook remains positive on emerging markets in the long term.

Emerging-market pharma revenues

Pharma-market projections,
$ billion



[1]Brazil, India, Russia; Tier 3: Algeria, Argentina, Bangladesh, Chile, Colombia, Egypt, Indonesia, Kazakhstan, Mexico, Nigeria, Pakistan, Philippines, Poland, South Africa, Saudi Arabia, Turkey, Vietnam.

McKinsey&Company | Source: BMI Research (May 2017); IMS Global Use of Medicines

Clearly define the long-term strategic objectives

Some pharma multinationals capture opportunities from time to time in emerging markets, without clearly outlining the role of emerging markets in their overall strategy. Others are more purposeful, adjusting expectations and resetting aspirations with a longer-term perspective, as well as identifying how to achieve wider business goals from their emerging-market presence (see sidebar "Which markets?"). In addition to looking for scale and growth, these successful multinationals have broadly used their emerging-market activities to pursue three strategic objectives:

- Grow and expand patient access. With many underdiagnosed and undertreated diseases, emerging markets still offer an attractive growth prospect for pharma companies, as several of these countries see rapidly rising incomes, better-informed patients, and expanding access to healthcare. Furthermore, operating in emerging markets requires multinationals to make their medicines available to lower-income countries and patients. Forming partnerships or voluntary licensing deals can help them broaden patient access, build their reputation, and attract incremental revenues while keeping a lid on investment.

- Create an innovation hotbed. Multinationals with global operations across emerging markets can leverage the cross-fertilization of ideas across mature and emerging markets. In particular, emerging markets can be at the forefront of innovation and a test bed for innovative business models and technologies. For example, to address challenges in local healthcare systems, Asia and Africa lead innovation on the business-model front for pharma, through innovative digital health and home delivery channels. Furthermore, some markets, such as China, can also drive pipeline innovation, as per recent trials in oncology, hepatitis C virus, and diabetes.

Three insights

Pharma companies can draw useful lessons when developing their strategy from the following insights about emerging markets:

- Size and growth are telling. By 2025, the largest emerging markets[1] will together account for 38 percent of the world's GDP, 36 percent of private consumption, and 31 percent of the pharma market, as well as two-thirds of the population.[2] Furthermore, in the next ten years, nearly one billion new people will be added to the middle class in emerging markets. This is happening in the midst of an overall increase in access. As an example, nearly 51 percent of the population in the Asia–Pacific region is expected to come under some form of universal health coverage in the next five to ten years.

- Persistence pays off. Growing economies are inherently volatile. In the past decade alone, some countries have experienced downturns followed by recovery. Companies that maintained a presence in tough times reap rewards for their commitment; those that leave often struggle to return. Success in the next cycle may depend on keeping faith during the present one.

- Successful emerging-market models exist. Across industries, companies headquartered in emerging markets have fared better than their developed-world peers.[3] This could be attributed to their agility: they reinvest more, are quicker to reallocate assets, and pursue growth-oriented business models adapted to the local needs in emerging markets.

[1] China, Brazil, India, Russia; Algeria, Argentina, Bangladesh, Chile, Colombia, Egypt, Indonesia, Kazakhstan, Mexico, Nigeria, Pakistan, Philippines, Poland, Saudi Arabia, South Africa, Turkey, and Vietnam.

[2] Sources include BMI Research, IHS, Oxford Economics, and the United Nations.

[3] Yuval Atsmon, Michael Kloss, and Sven Smit, "Parsing the growth advantage of emerging-market companies," *McKinsey Quarterly*, May 2012, McKinsey.com.

- Diversify risk. Emerging markets can enable companies to hedge against *top-line risk* by providing an income stream to help offset disappointing launch performance or loss of exclusivity in developed markets; against *pipeline risk* by generating sales from mature products to support the development of innovative new products; and against *currency and economic risk* by extending the footprint of the business to a wider range of markets.

Adapt the business model

Successful companies don't simply replicate the business model they use in developed economies but adapt it to the challenges of emerging markets. The following five lessons stand out:

Prioritize your portfolio country by country. Products that are commercially successful in developed markets won't necessarily do as well in emerging markets, due to their price levels, local clinical pathways, or disease prevalence for an emerging market. This calls for a careful mapping of products for each country in emerging markets. For mature products, companies could pursue a traditional approach to differentiation based on share of voice, key-account management, and other familiar elements, while specialty products call for a more innovative approach involving both public and private partnerships, strong market-access capabilities, and novel pricing models.

Explore new commercial models and channels. Building partnerships across the value chain can help companies shape the market and address unmet needs in emerging markets in areas such as screening, diagnostics, and supply chain. In particular, companies should adapt their channel mix to local requirements. For example, they could develop tendering capabilities,

Which markets?

With opportunities in emerging markets less abundant than before, most multinationals will need to calibrate their footprint. Similar to the United States, Europe, and Japan, China is among the strategic top three to five countries for many pharma companies. The question on emerging-market presence then becomes more about where to focus beyond China. Naturally, the largest economies in emerging markets are a given, namely Russia, Brazil, India, and South Africa. The key questions for these countries are what to expect from each of these markets and how to adjust posture: build up, maintain the current posture, or scale down?

Beyond this first wave of countries, not all markets will be commercially viable. This will depend on a multitude of factors: economic and political stability, affordability, intellectual-property risks, and competitive intensity. Additionally, for originators, a voluntary license might already be in place, a trend that has seen acceleration even with innovative products—for example, the Medicines Patent Pool now has a significant number of innovative drugs available through a voluntary license. All these criteria together effectively rule out 50 to 100 countries as viable commercial markets.

In between, only a few pearls remain. Success requires identifying these dozen or so countries offering the best growth prospects, market size, affordability, and stability; deciding how to enter them, either organically or through partnerships; and grouping them to bring scale to existing clusters or regions. These countries may differ by therapeutic area as reimbursement mechanisms, disease prevalence, and national priorities do. Yet some countries often seem to be prioritized among these "pearls": for example, Indonesia, the Philippines, and Vietnam in Asia; Mexico, Colombia, and Argentina in Latin America; and Nigeria, Algeria, and members of the East African Community in Africa.

develop home delivery channels such as in Asia and Latin America, or launch digital patient platforms specifically tailored to patients' needs in emerging markets, such as telemedicine for remote areas. Additionally, companies could leverage more advanced analytics and digital solutions to target physicians and pharmacies at a granular level.

Pivot from traditional commercial approaches to access-driven ones.[2] Multinationals need to rethink their market-access approach by building strong local relationships with governments, upgrading market-access talent, deploying an innovative approach to pricing (for instance, using GDP-based models), and entering creative access partnerships (such as volume agreements with government institutions and outcome-based contracting).

Adjust to the needs of out-of-pocket and consumer markets. Out-of-pocket spend and private insurance make up a sizable share of healthcare expenditure in emerging markets, with some markets almost fully out-of-pocket. To capture this opportunity, companies should be more systematic in identifying patient pools that meet certain affordability criteria; focusing on the cities with the largest pools, including new emerging urban centers with growing middle classes; and at the same time testing scenarios for reaching a wider population at a lower price with a second brand. Companies also need to consider how to adapt to local consumer preferences (for instance, offering smaller blister packs to suit more frequent dispensing, often preferred in some markets) and financing needs (for example, forming partnerships with credit providers to offer loans, or collaborating with private insurers to create insurance policies targeting specific diseases). In addition, companies can explore approaches inspired by consumer industries—for example, loyalty programs, similar to those for retail and airlines, that help companies build their brands, and improve patients' adherence to chronic treatment.

Think beyond the commercial model. In pursuing opportunities to differentiate themselves, companies should look beyond sales and marketing. Even when R&D is organized globally, it can still adapt to local conditions by undertaking licensing and M&A to enrich the country portfolio, for instance, or by developing medicines specifically to meet local constraints, such as medicines' stability at higher temperatures. Local manufacturing too can act as a key differentiator, when it is not a requirement for entry. And supply-chain excellence can confer a competitive edge in markets such as sub-Saharan Africa, where getting drugs to patients via pharmacies and other channels remains a challenge.

Build an agile organization

To capture opportunities in emerging economies, multinationals should carefully design their organizations to support their emerging-market strategy and withstand volatility. Successful pharma companies tend to do the following:

Organize emerging and developed markets separately. This allows strategies to be adapted to each type of market, gives emerging markets a voice in R&D and at the corporate level, makes it easier to rotate local talent and share best practices between markets, and allows for more flexibility in rebalancing activities when volatility occurs. Some companies create regional structures specific to emerging markets, or group countries by archetype,

[2] See Jan Ascher, Boris Bogdan, Julio Dreszer, and Gaobo Zhou, "Pharma's next challenge," July 2015, McKinsey.com.

depending on their access environment; others take a bolder approach and group all emerging markets under a single arm, independent of geographic proximity, extending from Latin America to Asia and Africa.

Strike the right balance between global and local capabilities. Consolidating mission-critical capabilities above the country level creates a pool of expertise in functions such as pricing (with innovative pricing and contracting tools); digital and channel capabilities (with scalable tools and approaches, such as disease-screening applications and disease-management platforms); marketing support; and distributor management (such as a center of excellence to manage distributors across multiple countries). Conversely, the capabilities that make the most difference in engaging stakeholders in a market—especially sales, market access, and government affairs—should be organized locally, as they are key to building relationships and partnerships.

Improve foundational agility. To be able to maintain a long-term view of market prospects while adjusting quickly to short-term shocks and volatility, companies need flexible organizational structures supported by the right governance—such as above-country hubs with cross-country performance-management processes and budgets—that enable them to redeploy resources quickly to the most attractive geographies.

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Despite recent turbulence, emerging markets continue to represent an important source of value for multinational pharma companies. But simply being present in emerging markets is no longer enough to earn a good return. Instead, companies need to recognize the differences between emerging and developed markets, adapt their approach to these markets' characteristics and needs, commit to a long-term vision, adapt their business model, and build an agile organization fit for the purpose of capturing growth from new opportunities as they emerge. □

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