China clampdown on GSK linked to drug costs

In mid-July, the Chinese government made public their investigations into corrupt practices by GlaxoSmithKline (GSK), the London-based pharma. Arrests and media-fuelled furor ensued and since then, allegations have spread to other multinational big pharmas. Most analysts agree the crackdown is symbolic—intended ultimately to push down drug prices in the Chinese pharma market—rather than a decisive attack against international drug makers. For the companies and their academic liaisons, the repercussions are likely to be short lived. But for Chinese authorities, these events provide a policy precedent with lasting effects.

In early July, China's police authorities announced that four senior GSK Chinese executives were arrested on corruption charges for bribing Chinese doctors and officials to prescribe the pharma's products to boost sales. After that, the investigations deepened, resulting in the arrests of a dozen GSK staff in Beijing and Zhengzhou. GSK's service suppliers, travel agencies in particular, were also affected.

GSK reportedly paid above the real price for the services it bought from travel agencies. The agency then kept that money in its accounts, making it available to bribe doctors and officials and fund other corrupt practices. Shanghai-based Linjiang International Travel Agency, whose heads were also arrested, and some unidentified travel agencies and consulting companies went to great lengths to withdraw and hide the overpaid money to circumvent strict internal financial regulations. Chinese police said that the money involved in these deals could reach \$500 million.

Chinese police also reportedly visited other international pharmas including Belgium-based UCB's China operations and those of London-based AstraZeneca.

Media coverage has turned the investigations into a scandal. In mid-August, local Chinese newspapers reported unproven bribery scandals of Paris-based Sanofi, Basel-based Novartis and US pharma Eli Lilly of Indianapolis, by quoting their former drug sales representatives. Both companies responded they would make serious investigations into these claims.

The wave of bribery investigations taking place across pharma are perplexing, particularly in a country where bribes are thought to be a necessary evil to ensure effective marketing. But analysts refute the possibility that international pharmas are under particular attack in China. "The bribery investigations against GSK and other foreign pharmaceutical firms are aimed at cleaning [up] China's notorious medical sector and controlling drug prices," says Yinglian Hu, an associate profes-

sor at Beijing-based think tank, the Chinese Academy of Governance.

Hu has been advising the Chinese Ministry of Health and the China Food and Drug Administration. He says China's medical reform, launched in 2008 to lower medical costs and expand health insurance coverage, has achieved a milestone in lowering drug prices in grassroots hospitals. But major hospitals still dispense high-priced branded drugs purchased from international pharmas.

Most domestic pharmas produce generic drugs only. Their low prices are driven down even further by local companies competing in biddings organized by hospitals or local health agencies. With such disparity between the pricing of drugs from domestic and international companies, the focus of investigations began with firms providing branded goods. "Although bribing doctors is a widespread practice in China, some international pharmas might have profited much more due to their higher drug prices. Thus, they are more likely to become targets of investigations," Hu says.

Dakun Hou, president of Beijing-based pharmaceutical consultancy KelvinKing, agrees. "The government likes to use a symbolic move to signal some policy intentions, such as lowering prices."

GSK has been responsive and cooperated with the Chinese government. After a meeting with the Chinese Ministry of Public Security, Abbas Hussain, GSK's president international for Europe, Japan, emerging markets & Asia Pacific, said in a statement released on July 22, "...savings made as a result of proposed changes to our operational model will be passed on in the form of price reductions, ensuring our medicines are more affordable to Chinese patients."

So far, there is no indication that GSK has received any penalties. Neither have any doctors or officials been reportedly arrested, although in some Chinese cities like Shanghai, doctors are required to report to authorities if they have taken a bribe.

"Doctors are generally paid too low in China, and there is no way to root out bribery—despite the investigations," Hou says.

He thinks the investigation's impact on drug prices could be limited, too, because major hospitals rely on drug sales for their profits. The influence could be minimal, particularly for high-priced biotech drugs, as nearly all of them are prescription drugs used in hospitals.

The arrests are unlikely to deter international companies from maintaining a Chinese presence. Given China's huge market potential, it is unlikely that any international pharma will reduce their China presence, experts agree.

Peter Park/AP/Getty Images

GSK was singled out first, others soon followed. China unleashed a crackdown on the industry over accusations of bribery and misconduct.

China's pharmaceutical market is expected to soar to 2.3 trillion yuan (\$377 billion) by 2020, up from 926.1 billion yuan (\$151.8 billion) in 2012, according to a report published in late 2012 by the Chinese Academy of Social Sciences.

For pharma R&D in China, the impact of the investigations will be felt, but will abate with time, according to Li Chen, founder and CEO of Shanghai-based Hua Medicine. Chen was founder and former chief scientist of Roche China R&D Center.

"Due to the investigations, the exchanges between international pharmas and Chinese academics and local firms are dramatically reduced in the short term," says Chen, whose company has received approval to run clinical trials in China for a diabetes drug candidate licensed from Roche.

His view was backed by a senior research director at an international pharma's Shanghai R&D center, who did not wish to be identified. "Because a lot of GSK's claimed corruptions are in the form of sponsorships for doctors' academic meetings, now we, and actually many international pharmas in China that I know of, have suspended any money-involving new cooperation with Chinese academics and hospitals for this year."

Chen emphasizes that China is already an integrated part of international pharmaceutical R&D, and the corruption investigations are unlikely to change this. Instead, he expects increased cooperation, including mutual drug licensing, between Chinese local pharmas, academics and international pharmas.

"Foreign pharmas will not be scared away. The move to discipline the Chinese medical market should eventually benefit those international pharmas which have more competitive products," Hu says.

Hepeng Jia Ithaca, New York