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Big Pharma is Hurt

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Cutting down R&D inefficiency and restoring the trust of investors and consumers are key to curing the industry's ills.

A whopping US$550 billion. That's how much value the global pharmaceutical industry lost from 2000 to 2010, according to a 2012 report by consultancy firm McKinsey & Company. This led McKinsey to dub it the "decade of doubt". Comparatively, the 1980s and 1990s had generated over US$1 trillion in shareholder value.

"The major blockbusters that came off patent – the so-called patent cliff – were not replaced by new blockbusters," explained **Nigel Brooksby**, Chairman of the UK Life Sciences Board. "I'm talking about drugs such as Lipitor by Pfizer, and Plavix from my old company, Sanofi-Aventis, and all those drugs that generate over one billion dollars in sales a year."

"These all arrived at about the same time, so that clearly destroyed some of the shareholder value. It wouldn't have been a problem if there had been a pipeline of innovative new products, but there was a lack of R&D innovation."

Higher R&D investment, lower returns

It's not that spending on R&D is lacking, Brooksby tells *Perspectives@SMU*. In fact, there has been a huge increase.

"We need a new model for R&D, and that model needs constant evaluation and constant measurement to see if it's working."

"The actual spending on R&D accelerated by 60 percent over that time period, and the spending as a percentage of sales increased from 10 to 16 percent. Therefore, the pharmaceutical industry was spending more but achieving less."

Given that worldwide sales grew from US$200 billion in 1995 to US$800 billion in 2009, the six percent increase in R&D spending translates into a much larger outlay in absolute dollar terms. Why did it then not lead to greater returns? The McKinsey report explains that "most low-hanging fruit has already been picked". This means too many firms are spending on areas that are already well-researched and developed, so significant breakthroughs are unlikely.

Even if they do manage a breakthrough, there could be less reward in doing so than during the good years **.**

"What has also changed is the time of exclusivity you get into a therapeutic class of drugs," explains Brooksby, the key speaker at the SMU Institute of Innovation & Entrepreneurship event, 'Past, Present and Future Pharma'. "When I joined the industry in 1972, I was working for Wellcome, now GlaxoSmithKline. We discovered a series of new drugs, and we had several years of exclusivity before the next member of the same class of drugs arrived. Now it could be weeks or even days before a competing drug shows up, so the competition is getting harder, for sure."

Lack of confidence

Big Pharma is also suffering from a decline in confidence from both investors and consumers. The economic return on R&D investment for the 10 largest pharmaceutical firms has dipped from 15 percent in the mid 1990s to about 5 percent around 2010, which makes shareholders wonder if they should continue investing .

What also hurts the industry is public perception. It is becoming a commonly held belief that pharmaceutical firms are more concerned with their commercial interests than the safety of its products. For example, Johnson & Johnson's US$2.2 billion settlement with the US Federal Government over charges of illegal marketing to drives sales of its Risperdal drug and two other drugs is likely to deal a blow the reputation of the company, which is already grappling with hundreds of lawsuits related to complaints about Risperdal causing male breast growth.

The Risperdal fiasco is the latest entry into the industry's hall of shame, which includes Merck's arthritis drug Vioxx and Bayer's Baycol, which lowers cholesterol levels. Vioxx caused heart attacks while Baycol users died of organ failure. Merck and Bayer ended up paying billions of dollars in damages.

"Every company needs to review and revise governance standards to win back the trust of stakeholders and shareholders," Brooksby notes. "In the past decade, R&D has been poorly managed and poorly measured**.** We need a new model for R&D, and that model needs constant evaluation and constant measurement to see if it's working."

The way forward

Brooksby says the top 10 pharmaceutical companies are aiming for a 10 percent long-term economic return on R&D investment.

“I think the industry is still going to grow. In constant dollar terms, the industry will grow by four percent in the next couple of years. IMS Health (a healthcare intelligence firm) says that the average growth rate in the mature markets – by that, I mean Europe and North America – is going be around 1.7 percent. In the emerging markets, the rate of growth in the emerging markets is around 12 percent, with the greatest growth in terms of absolute dollars coming from the BRIC (Brazil, Russia, India, China) countries.”

Brooksby adds that future R&D and innovations should bear these consumers in mind and develop the right product portfolio for them. There is also a need to revamp how drugs are sold to medical institutions and doctors.

“The old model of employing armies of sales representatives to call on doctors is dying. We’ve seen a dramatic reduction in the numbers of reps, and this must continue. This modernisation of the sales and marketing effort in the mature markets must accelerate,” Brooksby points out.

“What we’re doing now in emerging markets might not be what we’ll be doing in five to 10 years, so we need to address the longer term in the emerging markets.”