CHAPTER 13 – Direct Foreign Investment

Foreign Investment in China on the Increase

Pharmaceuticals produced by Sino-foreign joint ventures in China and imported drugs account for one third of the Chinese market. Approximately 1,700 joint ventures are now established in China, with investment totaling around USD 2 billion, with 40% of all Chinese pharmaceutical enterprises having utilized overseas capital. Of the 25 largest multinational pharmaceutical companies, 20 have established a presence, with 40 of the 50 most popular brands of drugs in China produced by Sino-foreign joint ventures.

In terms of sales volume, the no.1 joint venture is Xi'an-Janssen Pharmaceutical, a collaboration between US company Johnson & Johnson and the Shanxi Provincial Corporation of Pharmaceutical Industries. Tianjin Smith Kline & French Laboratories, owned 55% by the UK company SmithKline Beecham, leads the OTC market, and Shanghai Squibb Pharmaceuticals products, partly owned by the US company Bristol-Myers Squibb, has been successful in both urban hospitals and the OTC market.

New joint ventures include Shanghai Sankyo Pharmaceutical, between the Japanese company Sankyo, 95% majority owner, and Shanghai Zhangjiang Science and Technology Park Development, which markets six of Sankyo's products. A total of USD 30 million has been invested in Roche Taishan (Shanghai) Vitamin Products, which is now the largest producer of Vitamin A.

Local Company	Foreign Owning Company	Domestic Owning Company/Partne
Bayer	95% Bayer, China (Bayer, Germany)	5% BETIDC
Beijing Fresenius	75% Fresenius Kabi, China (Fresenius, Germa	
Boehringer Ingelheim Shanghai	90% Boehringer Ingelheim, Germany	10% Sine
China Otsuka	50% Otsuka, Japan	50% China National Pharmaceutical Industry Corporation
Gruenenthal-San Huan	75% Gruenenthal, Germany	25% San Huan
Roche	70% Roche, Switzerland	
Sino-American Shanghai Squibb	50% Bristol-Myers Squibb, USA	Shanghai Trust Corp State Pharmaceutical Administration of China
SSPC	51% Fresenius Kabi, Germany (Fresenius, Germany)	49% China National Pharmaceutical Industry Corporation
Tianjin SmithKline & French	55% SmithKline Beecham, UK	
Xi'an-Janssen	52% Janssen, Belgium (Johnson & Johnson,	48% Shanxi Provincial Corp of Pharmaceutical Industries

Source: Pharmaceutical Company Directory

The above table lists some of the Sino-foreign joint ventures operating in China, according to IMS HEALTH's Pharmaceutical Company Directory.

The rate at which foreign companies are establishing joint ventures with Chinese enterprises and increasing their financial investment has significantly increased in the last two years. Earlier in 2000, Celera Genomics acquired a 47.5% stake in Shanghai GeneCore BioTechnologies, with a view to expanding globally and gaining access to new sources of genetic information. Hong Kong company

China Continental acquired a stake in Yang Tian Pharmaceutical, the largest Chinese-owned drug maker, which manufactures, markets and distributes Western and traditional Chinese medicines. Dutch company Nutricia has invested USD 20 million to form a wholly-owned subsidiary Nutricia Pharmaceutical (Wuxi), to produce the company's proprietary enteral nutritional products. In June 2000, French company Servier and China Huajin Pharmaceutical Co. set up a new joint venture; Servier Tianjin Pharmaceutical Co. Construction would start later this year, with a view to commence production in 2003.

In a move to improve the competitive edge of China's pharmaceutical industry in the international market, the State Economic and Trade Commission (SETC) announced plans to build twelve big pharmaceutical firms, which would be on a par with the world's leading drug producers. The Chinese market is highly fragmented with a large number of manufacturers and distributors. There are over 6,000 pharmaceutical firms in China, many of which are small local enterprises. During the next five years the SETC expects these enterprises to play a significant role in the domestic and international arena, and they will be granted priority for technical renovation and research and development. China has set up 200 research institutes for biotechnology and 140 enterprises are engaged in related development and production.

The commission also supports foreign pharmaceutical companies in expanding their business from manufacturing to R&D, and setting up centers to develop new products together with domestic institutes and hospitals. Foreign-funded research centers would be exempt from import tariff and custom taxes; business taxes would also be exempt if foreign companies transferred technology to China.

Difficulties faced by foreign firms entering the Chinese market include lack of protection of intellectual property rights (IPR), drug counterfeiting, price controls, other trade barriers, limited social security, medical insurance and prescription coverage. The priority, from a company standpoint, is the pricing structure and IPR. China will have to address these issues if it is to join the World Trade Organization (WTO), as it would have to follow the WTO's IPR provisions and trading practices. If these issues can be resolved, companies stand to increase their share of the Chinese market for finished versions of Western drugs from US$720 million to US$1.6 billion.

Analyzing the pharmaceutical industry by province, the region of Jiangsu is expected to expand substantially from an output value of CNY 18.5 billion (CNY=Renminbi) in 1999 to CNY 21.5 billion in 2000. The Zhejiang Province in eastern China recorded an output value of CNY 18.55 billion in 1999, an increase of 28.4% on 1998. China's commercial capital Shanghai plans to record an output value of CNY 165 billion, an increase of 14% on 1999.

Questions

1. Explain the motivation for the recent direct foreign investment by the largest multinational pharmaceutical companies.

2. Describe some of the obstacles faced by multinational firms that have engaged in DFI in China.

3. Explain why the majority of multinational pharmaceutical companies are producing prescription drugs in China rather than simply exporting them to China?

4. Why are the majority of the multinational pharmaceutical companies using the joint venture model?