

Case study – Glaxo's progress in China

Dr Brian Tempest

Dr Brian Tempest is a Doctor of Chemistry and has been involved in marketing, sales and management in the pharmaceutical industry since 1971. Since 1986 he has been Regional Director, Far East, of Glaxo Holdings plc, which has a world-wide network of manufacturing subsidiaries and associated companies specialising in the most advanced ethical drugs. He is responsible for several Glaxo companies in East Asia and has been involved closely in the establishment of Glaxo's new venture in China.

My role this afternoon is to give you an inside look into some joint venture negotiations which Glaxo is carrying out with the Chinese government. These negotiations concern the building of a pharmaceutical factory in the People's Republic of China on a green field site.

This is the order in which I would like to cover this case study.

- First of all I would like to introduce Glaxo to you.
- Secondly, briefly describe the market in China for pharmaceuticals,
- and take you through Glaxo's history in China.
- Lastly, explain to you where we are going and what we are doing at the moment.

Glaxo

Glaxo is a company which is very much better known by doctors and pharmacists, bankers and analysts. It is less known to the man in the street because our business is prescription ethical pharmaceuticals.

In the company's corporate statement we refer to 'medicines'. By medicines we are really talking about those products that are prescribed by a doctor or administered when you are in hospital. I am not talking about over-the-counter or consumer medicines and all my comments are based upon the ethical pharmaceutical business in China.

Looking at the business and the market that we are in, worldwide we estimate it to be worth about £56 billion and over the last five years or so there has been quite a healthy growth. Within that marketplace Glaxo ranks fourth and indeed we are the only British company in the top ten companies worldwide.

Growth for the four years up to December 1987 has been encouraging. Indeed you may have heard from our latest annual results that we now see ourselves ranking number two in worldwide pharmaceuticals.

Therapeutically, our range of products come from 18% of the world's pharmaceutical marketplace and so at the moment we are not selling any products that are represented in the other 82%. It is from this area we are expecting our new products in the future to come and it is by this route we are hoping to make the number one position worldwide.

So that is in a nutshell a brief introduction to Glaxo.

The market for pharmaceuticals in China

Let us now move to the market for pharmaceuticals in China. We estimate the market for pharmaceuticals in China is about the same size as the UK marketplace. In China there is a high volume of low unit cost products and clearly in the United Kingdom there is a lower volume but of higher cost products.

In addition, in mainland China there is a considerable volume of Chinese traditional medicines and, of course, it is also a marketplace where there is no protection of intellectual property rights.

As far as the options that are open to us in the pharmaceutical industry, we have basically two paths that we can follow of which the second brings a much bigger market than the first.

1. The first involves us selling our products at a foreign exchange price and this means that our salesmen have to do two jobs. First of all they have to convince a doctor or a hospital in mainland China that they want our product. Then the salesman has to go and negotiate a foreign exchange allowance in order to complete the purchase.
2. Of course, on the other hand, we can manufacture our products in a factory within the People's Republic of China and we can sell those products at a local currency price. At this moment in time Glaxo is going down both these paths.

Glaxo's history in China

In 1910 we had a regional office in Shanghai along with many other companies who were basing themselves in Shanghai at that time.

In 1948 we came out of Shanghai and the trade continued for our pharmaceutical medicines at a low level via Hong Kong. This trade built up and became greater and greater.

In 1985 we opened a trade office based in Hong Kong. That business has increased further and now we have set up a separate company which will handle the export/import trade out of Hong Kong and into mainland China.

In terms of importers, companies that are selling finished products into mainland China, we currently rank number

nine. There are a number of pharmaceutical companies not in the top ten worldwide and that is because half of those companies are selling cheap generics to the hospitals in mainland China.

The company within Glaxo that is now responsible for our export trade into China is called Glaxo China Limited. We have modest sales but a healthy growth. About ten salesmen work every day in most parts of the People's Republic of China and these men are Hong Kong Chinese, who speak Mandarin and Fujian dialects as well as Cantonese and English. They are high quality people, often educated in Europe or the USA.

Also we make much use of the 48 Group office in Beijing. We are now in the midst of setting up our own office so we will probably use that office less and less but I would recommend it to anybody who is starting out in China. We will certainly be continuing to use the Shanghai Group 48 office quite a lot in the future.

Where are Glaxo going today in the future?

I have introduced you to Glaxo, I have talked a little bit about the Chinese market and I have explained where we have been.

In terms of joint ventures in mainland China, there are currently six in operation. Four are fully operational, and two are in certain stages of construction and then there is ourselves.

By far, the most successful venture in China is one which makes intravenous fluids in Tianjin and then exports that product to Japan. This is remarkable for two reasons:

1. To make intravenous fluids you need a high level of sterility and purity – much greater than in many pharmaceuticals and, therefore, they are making a high quality product.
2. They are exporting to a marketplace which demands the highest in quality itself.

So there is a classic example of a high quality product being manufactured in mainland China today.

As far as the history of our own joint venture negotiations are concerned, Chongqing was first mentioned in negotiations early in February 1987 and we are now expecting our joint venture contracts in 50 days or so. After that, it will be another two years before our factory is in an operational state and making products.

The name of the joint venture will be 'Chongqing Glaxo Pharmaceuticals' – a 50/50 joint venture. We will have two Chinese partners:

- South West Number 3 factory is a local Chinese factory in Chongqing and
- SPAC (the State Pharmaceutical Administration of China) which reports directly into the State Council and is therefore a government corporation.

We plan to manufacture Ventolin aerosols which will be used in the treatment of asthma. We are located in Sichuan Province, which is inland and, in spite of the policy of developing the coastal zone, being in Chongqing, really does seem to be working for us. We have had great help and assistance and the fact that we seem to be one of few in that part of the world does seem to be working very much in our favour.

Finally, on this particular point we do intend to bring a lot of our Chinese employees to the UK and train them in our Liverpool factory and make sure they are fully trained in Liverpool before they take their positions in Chongqing.

Chongqing is in the province of Sichuan and is located on the Yangtze River up from the famous gorges.

It happens to be the biggest city in the world. I am told by the local inhabitants, it has a population of 14 million people. Its local industry is mainly pharmaceuticals and armaments. Dunlop are starting a contract there shortly, and fortunately a new Holiday Inn is about to be completed. Glaxo will, of course, be there and already has people located there.

We will be building our factory on a field. At the moment rice is being grown there. Just at the back of the piece of land there is a new road which actually comes down from a new airport, both of which are almost finished. One of the things that we have also had to do in readiness for the joint venture is to set a corporate structure which will enable us to represent all Glaxo's interests in the People's Republic of China. We also purchase raw materials from mainland China as well.

Glaxo China Enterprises is the parent company incorporated in the United Kingdom and this UK company is also the parent of Glaxo Hong Kong Limited. So we have a China company in readiness for 1997 as the parent of the Hong Kong domestic business, where we are the number one pharmaceutical company.

In conclusion

From the basis of our experience in pharmaceuticals and it is a very specific market, our own particular experience points to these factors as being important.

1. First of all I think it is very important to remember that Beijing is the centre. Glaxo has had an unfruitful experience in negotiating a joint venture in Shanghai. This basically fell apart because we had very good local friends but our connections in the centre were not as good as they might have been. In consequence, we were not aware that the central government was about to wrap up the corporation that was our joint venture partner at the time. I do stress that it is very important and throughout the Chongqing negotiations we have kept extremely close to all our friends and contacts in Beijing.
2. It is very important to make good friends and then to look after those friends and to entertain them and to make sure you are developing a good relationship. We recently sponsored the Sadlers Wells Royal Ballet Tour of mainland China through Guanzhou, Shanghai, Beijing, Tianjin. At the opening night of each of those performances we entertained about 100 people for a dinner. This was just part of our ongoing methods of making good and close friends with many levels of management related to the negotiators that we were dealing with on our joint venture.
3. The third point that I would recommend is to make realistic expectations. It is very easy to get carried away with numbers in

mainland China. We have set ourselves some very pessimistic expectations from a financial point of view and this is because our objectives of going into China are: to learn about doing business in China. We expect to get our returns from using that knowledge in the long-term and we can then turn that knowledge into making some significant profits.

I can say that so far both in terms of numbers and times we feel that we are proceeding better than our expectations.

My final point is that I would recommend you do not negotiate from the UK, but instead work from both Beijing and Hong Kong.

I am Chairman of Glaxo China Enterprises Ltd which is incorporated in the UK. I am located in the UK. The managing director is located in Hong Kong. He has delegated responsibilities from me for all the joint venture negotiations. In total he has got a head count of 150 staff through Hong Kong and China and a special joint venture negotiating team of 10 people. He is constantly in the People's Republic of China. He is constantly in Beijing and so far it is all going extremely well.

So my final message is an old Chinese proverb and that is 'A frog in the well cannot see the ocean, or a UK executive sat behind a UK desk in a UK office cannot clearly see all the opportunities in China, nor can he see all the problems in China'. I do recommend that you heavily delegate to your local management in Hong Kong and Beijing.

Postscript

The Joint Venture Contract was signed in Beijing on November 22 1988 and following receipt of all the necessary approvals from the Chinese Government the first Joint Venture Board Meeting took place on January 11 1989.

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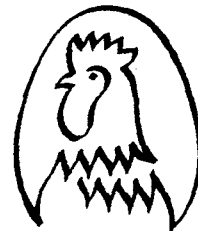
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