Interview with Ewald Kreid / Lorenzo Corsini, Partner and Managing Director / Project Leader, Boston Consulting Group Austria

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Could you please provide an overview of your main scope of activities in Austria and the importance of healthcare and pharmaceuticals to Boston Consulting Group's (BCG) business model and revenue?

EK: BCG has been in Austria for 15 years and we are integrated into the German-Austrian system, meaning that many Austrians work in Germany and likewise for Germans working in Austria. Our global head of marketing is based in Vienna with her team. We have a fairly big office here with about 100 employees.

In terms of the importance of the Austrian market, we have one team covering all the markets of Germany, Austria and Switzerland, among which there are many common lines and common synergies.

Your expertise with BCG is in biopharmaceuticals, healthcare providers and medical devices and technologies. Who are your major customers and what are the specific needs at the moment of the pharma industry in Austria today?

Typically our main customers are large multinationals and we have developed the business over time with our colleagues from around the world. From time to time we also have local business customers, but most of our business is global by nature.

The topics have really shifted. Right now it is about cost efficiency, working with fewer resources and still making things effectively. For instance, when smaller businesses from Austria, Switzerland and Germany think of how to pool together their common resources all kinds of interesting structures can emerge. We also do some growth strategies for generics in Eastern Europe.

Private equity investors are also important for us from time to time, if they want to buy another player. Just before Christmas we came out with a publication in Austria on value based health care which looked at the whole healthcare sector – not just pharma – and how to maximize outcomes with given costs. But it was not just a cost reduction approach. We compared Austria to 11 other industrial countries by looking at the healthcare system, how mature it is in terms of measuring outcomes data and making them transparent and how to tie financial incentives in the system to outcomes data. An interesting finding of the report is that Austria as a relatively small and uniform country has many of the "basics" in place. But due to very strong traditions, mainly on the physician's side, the system is not applying that data. We have a lot of systems, but when it comes to analyzing, applying and tying decisions and budgets to certain quality outcomes, it is not being done.

We compared it to Sweden – a country that has pioneered the idea of making public quality information from hospitals using the data of outcomes to channel patients. This is something that is being debated in Austria but not yet applied.

Why do you think that is? Did you come to any conclusions as to why Austria is different?

Unfortunately we have always been a follower country. We are not very comfortable being pioneers. There are strong conditions here among the physicians chamber, that are still very much in the mindset of the 19th century model of workshops – every physician on their own. Many GPs have their own practice. This system is traditional, but not very efficient. Part of the reason is not applying an entrepreneurial or a changing mindset. Additionally, there are also very strong data protection rules in Austria.

Minister Stöger plans to integrate the entire information service of the health system by 2017.

EK: In this sense, surprisingly, BCG is on the government's side believing that they are doing the right things. But we will only get the results if those systems collect the data and use the data tied to outcome and decisions.

LC: A very surprising result of this whole study in Sweden is that the average result and outcome of the healthcare system there has high variations around its average. So there are hospitals that are really good, but others that are equally bad. They started making these registries public and the hospitals that scored lower were forced to adopt modern technologies and protocols of treating patients which measurably increased the performance of the whole country in many therapeutic

areas.

EK: Unfortunately, there is very fervent public debate over the structure of the healthcare system in Austria but it is very much a tradition of “small is beautiful.” The mindset is to be close to the patient and not industrialize, centralize or specialize like what other countries are doing. Part of the debate needs to be shaped in that direction and I give the government credit for trying to do so. But it takes time.

Many people we have spoken to have said that there is growth, but it is significantly slower to what was seen several years ago. So where do you think the company should be investing to make growth as strong as it used to be?

The Austrian market is interesting because it is relatively small but has also been benefitting from benign elements on pricing and competition. Even if a business was not big, it was profitable and stable while at the same time had a good base to expand and have synergies with neighboring countries. What has been changing have been high levels of competition, especially on the generics side.

There were also some companies that benefitted from the absence of large players. They were able to benefit from in-licensing agreements. Some of that will go away. The market is becoming more challenging.

For the big pharma companies, one great and unique characteristic of the Austrian market is its generic regulation.

We have two dimensions for characterizing the market. One dimension is price decay; the other is the volume of off-patent generic penetration. In very efficient generics markets such as Germany or the UK, you see a very strong price decay and uptick of generics. At the other extreme you have Japan where the market still has very few generics and high prices even after patent expiration.

Austria found itself in a very interesting “lower right corner.” We have quite strong price decay here but the originator keeps the volume share. Sometimes the volumes even go up. Why is that the case? Because the regulations are such that the generic does not have a big advantage. It’s the same price for everyone. So if a physician can prescribe a Teva drug for the same price as a Pfizer drug, why would he switch? That pricing regulation is contrary to other markets and it currently makes it quite attractive for the originator drugs after patent expiration.

Dr. Wartenberg said the same thing. On the other side, Mr. Huber of Pharmig said quite the opposite. Despite this arrangement the reimbursement system still tends to recommend physicians to prescribe generics – that there is no point for innovative companies to drop their prices because they are selecting generics regardless. In your experience, who do you

agree with more?

Look at the facts. There are mandatory price cuts so everyone has to go down; there is no choice. When you talk to the originators they will tell you that they are relatively happy with this arrangement because they keep their patients and their volumes.

In five years time there will be more pressure on the generics side to make it more attractive. That will continue. Longer term, if countries watch how successful from a payer perspective the German system is with these tenders, our expectation is that there will be a greater concentration of purchasing and price decay.

LC: It is a question of incentive for the doctors of whether they can continue prescribing the originator or if there is a mechanism to switch to the generic. In Germany you have that because the physician can prescribe whatever he wants, but the patient gets the drug that his health insurance is paying for. That's not necessarily the case in Austria.

EK: As long as you have the system which allows prescribers some freedom we will see that. If it switches to a system where payers concentrate their purchasing on one or two choices, which we don't have in Austria, then things can change. It is really driven by the payer.

What qualities does Austria have in terms of being an attractive country for healthcare investment?

LC: Most of the bigger companies have a scientific sales force for their own patent drugs and this is why the local subsidiaries tend to be sales and marketing. Any research activities will probably be centered around Vienna. You have a strong university there, so good access to talented graduates. There's also a bio center and biochemistry facilities at the university.

EK: At the risk of sounding unpatriotic, when I look at the typical healthcare investors and why they tend to invest, my conclusion is that Austria is not and will not continue to be a major place of investment. Big pharma is retrenching. Factories and R&D centers are being shut down and opened in the BRIC markets. Then there are smaller and medium sized companies and, yes we have a fair share of them, but not more than in Germany and certainly less than Switzerland, the UK, the US and Israel. There is some investment in private providers in certain countries. A lot will be coming in emerging markets but that is also not strong in Austria because the public health system is relatively well developed and there doesn't seem to be huge areas of growth for private providers.

I don't see a lot of investment coming our way. If anything, it will be more a case of smaller R&D type start-up investments. Logistics and transport linked to healthcare could be a possible hub for this area around specialized healthcare.

How do you think Austria can begin competing to build a more attractive investment environment in that arena?

The idea of clusters for certain regions is an interesting one. There is a risk of that going away, but also an opportunity to have more of them because these markets have all reached a certain phase of maturity. They are not growing any more so there is a move to make them more cost effective and have one central location. That would require having more open access to scientists and people who can move to Vienna.

You've spent a number of years working in Russia and Switzerland. How does the healthcare environment here compare to those two countries?

The interesting thing in Switzerland is that you have private sick funds which serve as a driver of innovation. It is a bit like the system that Obama is trying to put in place in the US – you have to choose a sick fund, but the one that fits your personal preference. That creates a lot of room for efficiency and specialization in the system. We do not have that in Austria. We still have a traditional system where you can choose your insurance provider but the actual sick fund you are given is based on where you live and where you work. There is a lack of competition and innovation linked to that structure. We are missing competition and innovation in the payer and provider space which is still too politically dominated.

What is your five year vision for the future of the Austrian healthcare system?

I think it is very easy. You just have to look to Germany!

I think we are going to see more reforms in the provider sector – not every city can have a hospital for everything, for instance. I think we are going to see more cost pressure for post-patent generics. In general the big question and the bigger tug of war is between the traditional physicians chambers and the reformist payers. Can the payers go for efficiency, cost, size and outcomes vs. the GPs who want to conserve what they have now?

What do you think is the model that could perform better in Austria?

We are doing a study on this now. Year after year we are seeing more efficient generic markets working which means less profit pools in pure off-patent generics. That means that some smaller companies will be exiting the market.

Areas like OTC have become more attractive. They are less prone to this type of competition and you have more opportunities to promote them. Companies will focus on their innovative assets. Some will be trying to play the branded generics game which will be more and more difficult.

Do you see a big future for branded generics?

Only in areas where there is patient-physician choice. The big battle is with biosimilars. A very interesting area is medical devices. It is moving very fast, has less commoditization and is ripe for further innovation.

You mentioned biosimilars. Can you tell us a little more about the situation here in Austria? As in many other markets the government is attempting to treat them as generics. Do you see that as changing?

LC: It is more or less the same all throughout Europe. There is a centralized registration procedure with the European Medicines Agency (EMA), and currently, biosimilars for only a handful of biological active ingredients are registered. The big question is how the monoclonal antibodies will perform. It is a completely infant market. There are some experienced companies but all will depend on the experience of the big sellers. When you will have more biosimilars in the second half of this decade, then you can really judge the market. The market is growing, but is still small compared to what its potential can be.

And the regulations surrounding them – are they well prepared?

EK: I think we will see slow uptakes of biosimilars in Austria. They are already quite conservative on the small molecules, so here it is more of a question of trust since it is not the same process.

Another interesting area is the question of distribution chains. Some companies are trying new models to bypass distributors. Some companies are trying direct selling and online pharmacies. In the next five years we will see more liberalization happening here – new models of distribution emerging and more efficiency taking more cost out. That will create new opportunities for some of the players especially in the online world.

What is the situation between smaller biotechnology companies as spin-offs from local universities and big pharma? Other interviewees tell us that big pharma has been moving away from investing at an early level to minimize risk, but are also exploring different tactics they can implement to possibly change that. Any thoughts on that process?

It’s an issue for Austria more so than other countries because our companies are relatively small and need fair amounts of start up capital before they can become relevant or attractive. That market is less developed than in the US or Switzerland which presents a bit of a handicap. We have government agencies to provide some funding, but what is really missing is the private side of the equation.

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