Interview with Henning Sommermeyer, Founder, Pronaos

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Dr. Sommermeyer, you've spent approximately two decades working for pharmaceutical companies throughout Europe. From a personal standpoint, why did you decide to leave the industry and found a consultancy?

I started my career in research, and then moved to marketing and strategic planning. After ten years spent in headquarter functions, I began to work as a general manager in European countries: Portugal, Poland, and the Czech Republic. Initially, I worked for 14 years for Bayer AG; in Poland, I was headhunted to lead the Czech subsidiary of another German company, Altana.

I planned to stay in the Czech Republic for three years, and then move on. However, Altana was purchased by Nycomed, and I was offered a position to head the integration in the Czech market. I was interested in the job for a simple reason: I had done many things in the pharmaceutical industry, but I had never led the integration of two organizations.

It was an exciting experience for me, especially because Nycomed was very interested in growing the business. When I joined Altana, the operation in the Czech Republic had revenues of approximately 8Mn EUR. By the time I left in 2010, turnover was 32Mn EUR.

By 2010, it had become clear that Nycomed, as a company held by private equity investors, was being prepared for sale. The organization was ultimately taken over by Takeda. I thought that this would be a good point in my life to try something new. Over the preceding ten years, I had

essentially acted like an entrepreneur, and I thought that I could actually realize the dream and own my own business. I was 50, and I thought that it was now or never.

What are the key challenges that pharmaceutical companies face in this region today?

I joined the pharmaceutical industry because I found that it was a highly profitable and complex industry that delivered products that contribute to the greater good. We improve the health of society, which is a great endeavor to undertake in your professional life. The industry is still profitable today, but margins are very much decreased. Previously, a general manager would have been dissatisfied with a 40% profit margin—today, 20% is a pretty good target.

Furthermore, in the past, the industry had a very simplistic approach. A company would create a me-too product with some small added value, launch it, and enjoy good business with very reasonable profit. Nowadays, this situation has totally changed. Companies must deliver innovation that is clearly proven to be superior to existing products. Supporting data must be comprehensive and grounded in reality. Me-too products will indeed get access to the market if they fulfill legal requirements—but they will be priced like a generic. This has been a significant change for the industry.

Another change is that general managers now have to be very cost-sensitive. Previously, production costs were 10% of sales. Sales force cost was 25%. Marketing and promotion: 10%. After administrative costs and regulatory affairs, we would end up at approximately 40% profit. Now, things are changing. We have to ensure a return on investment. For the old guard of pharma managers, this is quite a challenge. Headquarters are telling them that they will not pay for certain things anymore. 20 years ago, this was practically unheard of.

What is spurring these changes? Is it the influx of competitors? Is it the limitation of healthcare budgets?

Indeed, the healthcare system is no longer funded in such a way that the authorities can easily afford coverage. Governments are starting to ask, ‘if I have to pay for this, what do I really get in return?’ Me-too’s will not be given a premium of ten times the generic price. Why should they? It was foolish to believe that such trends would continue. We lived in paradise, but paradise has been closed recently.

We must adjust to the new environment. We must focus on real innovation, and demonstrate that price is justified. In countries like Germany, this fact is already well advanced. In the Czech Republic, the authorities are too becoming increasingly scrupulous. The government is

benchmarking what is ongoing in other countries. Whereas before, Czech lawmakers were more or less isolated, they are now very much aware of the situation elsewhere in Europe. When Hungary thinks of a good idea to cut costs, we can be sure that the Czech authorities are evaluating whether it would fit their situation.

Another element, and one that is particularly relevant in the Czech Republic, is that it is in the hands of the general manager to get a favorable price and reimbursement level for new products—to approach payers and negotiate. This is where the challenge starts. Supporting data for product registration is centralized, so the manager gets, say, U.S. clinical statistics, which is not very useful for his discussions with the local payers.

Let’s assume the manager gets everything done. He gets a price that is accepted by headquarters—which is not always the case, because sometimes the given price is not accepted by HQ and the product launch does not move forward. Sometimes, the price is not high enough, and given the fact that the Czech market is small, HQ feels that they will damage their global business by moving forward with such a product launch. In the Czech Republic, price levels are generally quite low, because of a referential pricing mechanism the cross-references several other low-price countries in the E.U. The question becomes whether the country will see all innovative products early in their life cycle, or whether the patient will have access to innovation later in time. This is a question that we have to balance.

The problem is two-fold: for the general manager, it is a business problem, because he cannot sell his drug in this market. On the other hand, the population does not get access to a particular therapeutic standard. How do we find a balance between ensuring patient access, and getting appropriate prices? There is a lot of discussion ongoing on prices and budget impact, but what I believe is missing in this country is a discussion regarding the standards of therapy that we aim to establish. What is the investment level we are ready to contribute to healthcare, and what are we expecting in terms of healthcare service for the population?

Having spoken with a number of pharmaceutical managers here, they seem to have the same complaint: the government focuses mostly on cost, rather than the need for innovative medicine. Minister Heger, on the other hand, remarked that additional funds are simply not forthcoming, so the government is limited in their ability to finance such medicines. There seems to be an impasse.

This is the root of the issue. The industry says that it needs a particular price or it cannot move forward. The Minister says that he does not have the money. If these are the positions, I do not see a platform for compromise.

Let’s look, for instance, at osteoporosis. If we do a ranking, and see how much is spent on treatment of severe osteoporosis (e.g., with PTH) across the world, the Czech Republic is in the upper part of the lower third. The top country is Greece! The question is where osteoporosis treatment is going. The drugs are relatively expensive, and the system has determined a particular number of patients that may be treated every year.

For instance, let’s assume 1000 Czech females can be treated for this disease every year. This gives us a budget frame. Where is this number coming from? I was never able to get an answer. The next thought is how the number develops over time. Is there a plan? The authorities might say that they would like to prioritize osteoporosis treatment over other aspects of healthcare, because if the disease is not treated, there is high likelihood of hospitalization and even death. Thereby, a strategy could be developed, and a compromise could be found. We must figure out what must be contributed by the industry, and what must be contributed by the healthcare system.

On the part of the authorities, let’s assume that their plan, based on demographics and E.U. standards, is to reach 2500 patients, rather than 1000, over the next five years. The contribution from the pharmaceutical industry, given the five-year security and guarantee of a particular rise in volume, is the supply of the drug. The payer, in turn, receives an economic benefit in terms of less hospitalization.

In order to realize such synergies, the authorities need to have a perspective beyond pharmaceuticals when they look at healthcare. They have to establish a complex outlook, and move away from thinking about the budget impact of drugs.

Some of our interviewees have commented that the government seems to be very interested in ad-hoc measures, such as flat price cuts, rather than broader strategizing and long-term perspectives.

Indeed, we need to invest in systems that allow us to do something beyond a 7 percent price cut. We must create a healthcare system that is able to speak to the industry on more sophisticated terms. If pharmaceutical companies claim that their drugs can affect less healthcare utilization in areas beyond the pharma product, the government should welcome this, and ask for a demonstration in the Czech Republic. Both parties should come together, and collect the data.

In some countries, we have even seen the rise of risk-sharing agreements between the authorities and the industry. I am not a particular fan of such agreements, because they have certain downsides—but this is one model. In principle, the dialogue should focus not only on pricing, but also on the collaborative development of standards of care for the population. This must be the vision. Both parties must be blamed for not yet having what, I admit, is a complicated discussion.

In Germany, for instance, companies bring an expensive product to market, but they are able to argue its merits beyond price. Amongst other reasons, this is because each hospital has a quality report that they must submit to the public. If they have low-cost pharmaceuticals, but their service is not well rated, government cuts the hospital's reimbursement.

If the industry and the Czech government do not enter into such a discussion, the industry is losing, and the healthcare system is also losing. All that is happening is that costs are being shifted to another part of the budget. The longer we delay this discussion, the more expensive the problem will become. It is no surprise that the German healthcare system is sitting on 23Bn EUR of savings—the authorities there did a very fantastic job. They told the industry that they would only pay for quality. Such a discussion really serves both parties.

How does Pronaos factor into this picture?

Keeping in mind the challenges of the market and what it takes to find success, we work in several directions. Firstly, having spent 20 years working in the pharmaceutical industry throughout a number of countries in Europe, I am today approached by companies that seek my expertise in establishing their business in certain markets.

Initially, the idea was very simple: Western European companies could come to me to establish their business in Central and Eastern Europe. This was a major portion of my business last year, when I helped establish entities in Poland, Czech Republic, and Slovakia for an Italian healthcare company. Companies like this find the CEE markets interesting, but are a bit overwhelmed by the local requirements—hence, they look for consultants that have relevant local knowledge. At the same time, they want for such consultants to also have a Western background; this makes them more comfortable. Essentially, they look for someone that can bridge West and East.

I did not anticipate that, as I made my way around Eastern Europe, I would also be introduced to a number of players that would like to go the opposite way: they want to head West. Today, I am also helping Eastern Europeans to establish Western European subsidiaries. My clients' size varies; however, to give you an idea, the Italian company I mentioned, known as Bracco, generates approximately 1Bn EUR in turnover worldwide.

Why would a company with 1Bn EUR in revenues turn to such a small consultancy, rather than approaching one of the more traditional industry service providers?

In the pharmaceutical industry, everyone knows each other—we are a family. People develop a certain reputation over the course of their career, for better or worse. I am able to generate

business thanks to a strong reputation and a large network. Especially in this part of the world, trust is a pivotal. You absolutely want to do business with someone whom you can trust. On my part, I would also turn down an offer to consult for a company that I felt I could not put my faith in.

However, reputation or not, you are quite correct: I must still offer additional advantages relative to the major consultancies. One differentiator is the following. In my experience, these consultancies send very smart, highly educated young people to their clients, and these young people are armed with great ideas and fantastic color PowerPoint presentations. The issue is that they have never sold a drug pack to a single living customer. In this respect, I am able to truly set myself apart.

My business model is quite innovative, as well. I bring together teams of experienced individuals on a project-by-project basis. I have only three people on my permanent payroll: myself, my accountant, and my assistant. I do not have to charge huge overhead—yet I am able to bring together project teams that have perhaps 20 people. These can be either freelancers that work by my side on the project, or staff members from the client company itself. For instance, when we set up Bracco in CEE, half of the team was internal Bracco staff, and they reported to me as project leader.

Here we see another differentiator. Many consultancies will advise their clients on a certain matter, but if the approach doesn’t work, it is up to the client to fix the problem. My approach of integrating the company team with the consultancy team ensures that we all have mutual challenges that we work together to fix.

The disadvantage of the model is that many clients expressly ask that I lead their project, and this fact makes my business strategy un-scalable. Hence, I am currently developing two additional branches that should leverage my business. One branch will help companies to gain new products for their portfolio by introducing them to relevant partners and structuring a deal. In such cases, I will be paid a fee on the turnover of the product over a certain period. This approach is highly scalable. The other branch involves investment into a variety of market opportunities—and this, too, will hopefully prove quite scalable.

A final direction of my work is my cooperation with a company called CEEOR. CEEOR’s first focus is on pharmaco-economics. When we began our discussion, I mentioned that something needs to be done about the way this industry offers its value proposition. As an organization working in this sphere, CEEOR has a very interesting future. I have a long-term interest in this topic and I find that CEEOR is well positioned to educate the system regarding the provision and analysis of health-economics figures.

CEEOR also conducts market research, with a concentration on sales force effectiveness (SFE). This is the sphere in which we specifically cooperate. CEEOR has the technology to monitor SFE, and I, having spent some years as a pharmaceutical general manager, understand the need. As I said previously, the industry's productivity is in decline. We no longer enjoy the same margins. As a manager, you have to think about costs, and when you look at your profit/loss statement, it is immediately apparent that your biggest cost is your sales force. Depending upon the company's portfolio, sales people typically account for up to 35% of overhead. The idea behind SFE is very simple: as the biggest ticket in your profit/loss accounting, you must take care that this aspect of your operations is working!

Administration is typically 3-7% of your costs. If you cut administrative cost in half, you enjoy up to 3.5% more profit. The impact is extremely small. On the other hand, if you optimize your sales force, you can really see an improvement in your numbers.

Many companies are today asking how they can make their sales people more efficient. There is a lot of room for good consultants in this field.

As a consultancy looking into a number of varied opportunities, can you synthesize for our readers your broad vision for Pronaos?

If the pharmaceutical industry is looking into particular projects that require resources above and beyond their current set-up, this is where I can serve them. I do so on an attractive cost basis, and in concert with people that have strong operational experience—not only theoretical experience.

Here in the Czech Republic, the focus for Proanos is to help clients to get a better return on their investment, with a special focus on sales force—their biggest cost driver. Together with CEEOR, we can give clients the structure and tools to get the most out of their people.

We focus on outcomes. I was a general manager for ten years, and I have many times purchased consulting services. What is the remaining benefit one year after the consultant left? In many cases, I cannot even say, because it was not measured. This is consultants' first major mistake: lack of measurement of outcomes.

We are interested in something sustainable. We can help strategically, and we can help you to implement. We get our success stories out of your success stories.

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