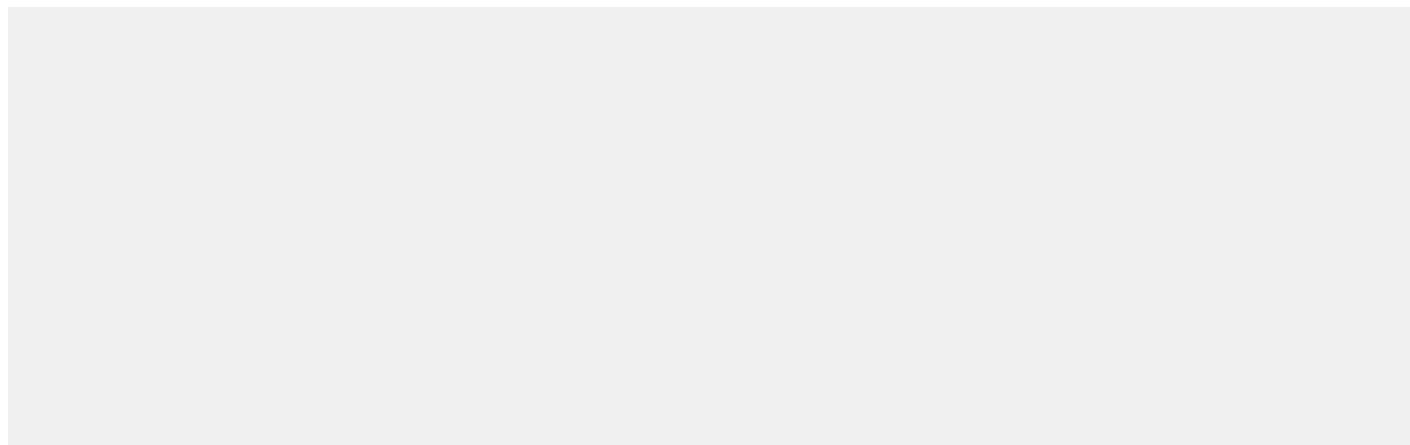


Interview with Laszlo Sugar, General Director, Valenta



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Valenta was established in 1997 as Otechestvennyye Lekarstva, and today represents the consolidation of several facilities and business holding groups. Can you give our readers an overview of the company's history of development, and an idea of your current size and organizational structure?

Initially, the shareholders of Valenta purchased and privatized a facility in Schelkovo, and in subsequent years they purchased additional facilities in Novosibirsk and Krasnoyarsk. They began to develop a generic, hospital-focused portfolio with a huge amount of products.

This went on for some time, and then one day they realized that the generics business is better run as a branded business, and they converted the company, over the space of a few years, into a branded generics and original drugs organization. We currently have two strategies: one is obtaining Russian patents, and developing original molecules from scratch. Our other strategy is to find niche products that we can brand as generics. Since the decision to become a brand-focused company took effect, 95% of our total turnover comes from branded products. We are, today, no longer a 'generic generic' producer.

The company's sales are currently around 4.5Bn RUB—about 110Mn EUR. In 2008, we sold two facilities out of three (leaving only the original Schelkovo plant), and we exited the hospital business. We now focus on the out-of-pocket business. We have less than 7% of our business in government tenders—this is company policy. Most probably, we have the highest EBITDA ratio in the sector: over 40% in 2010. Our profit is driven by 14 products, which provide over 85% of our

turnover.

We are a highly concentrated marketing company. We are also manufacturers, we but we wholly divide issues of marketing and issues of production. Our belief is that production is one business, and sales is a different business—with a different philosophy, different people, and different management structure.

We are an Rx company. This means that, although we have OTC products, the way we promote is Rx-based. We market our products to professional societies—meaning doctors and pharmacists. Our medical reps are all doctors, and we actively invest in their education. This specialization is paramount, as we speak with doctors as partners, and our sales processes are complicated; we are speaking of original products that have never before existed. It takes much to convince a professional society even to accept a clinical trial. Valenta spends a lot on clinical studies. We believe in convicting people with facts, rather than strong pressure. We are not in mass media—not even with our OTC products.

We are very cautious regarding our finances. We have no debts, and grow from cash flow. We carefully analyze the cash, and never spend more than what we have. Our efficiencies are very high.

Let's look more closely at one of your products. According to Pharmexpert, your original flu drug Ingavirin was the second-most popular prescription drug in Russia last year—behind only to Viagra—and the only Russian-produced drug to make the top-ten list. What is the significance of this achievement?

I am an economist by education, so I must first say that everything depends on the statistics that you have. To my mind, Ingavirin and Viagra are not comparable, and there are thousands of products that sell much more than Ingavirin.

So let's forget this ranking for a moment. Irrespective of ranking, it is certainly true that we took this antiviral product from having zero market weight, to a product that, if you go to the pharmacy—and there is no company specifically paying for their position—the pharmacist will offer Ingavirin to you as a first choice.

We spent a huge amount of money on trials, and we convinced federal and regional opinion leaders one by one regarding the efficacy of this product, and its added value over and above competitors.

But do not forget: there was a flu pandemic. Of course, we had a great product; however, generally, antiviral products are not interesting. No one would have ever heard about a product like

Tamiflu before a pandemic. The same may be said for Ingavirin: there was a pandemic, so there was high interest. It is very important to be on time, with much luck, in the right place. We had just launched the product, and on the day of launch, the pandemic started! We were ready, we did our job, we professionally promoted the product, and the market demanded Ingavirin.

Can you replicate this kind of success?

We have, many times. Many of our products have been very successful.

We are not in a rush. We are very quiet, and we know results. They depend 95% on God, or luck, or fate—call it what you will. For the other 5%, you work every single day. If you do your job, success will likely come to you. It may come sooner, it may come later, but it will come. Our strategy, again, is to run thorough and accurate clinical trials, and prove our value through results.

Is it difficult to operate in a market where both Russian physicians and Russian patients seem to have an automatic inclination toward Western medicines?

I would not say that the issue is in being Western or non-Western. The issue is that there have historically been very few well-documented Russian products, and the education that Russian doctors have received informs their professional opinions.

Russian doctors generally only trust drugs whose clinical trials involve placebo-controlled, double-blind, multi-center testing. This is not a Western or non-Western matter. If you want to convince them, you bring them your results, depicting this manner of strict trial. This is the way we work.

I do not believe that the best way to divide this market is into Western and non-Western medicine. If we are to divide the market, we should look at price. There are medicines that are approximately 100-150 RUB, that those with lower income are forced to buy. Even if the doctor prescribes a higher-value brand, they simply may not be able to afford it. Not everyone can afford 12 EUR for Ingavirin, especially if they have to take several medicines.

Beyond the 100-150 RUB range, you have the middle range, and you have the high range. I believe that we have found a niche in targeting those who want to spend 10-15 EUR for a medicine that is offered to them with the support of a decent doctor. Our target group of patients is urban dwellers with decent salaries that visit skilled and well-educated physicians. Altogether, we are talking to the upper middle class. All of our products are in this price range, and this is one idiosyncrasy of the company.

Prior to the interview, you mentioned that in 2008, this company was bankrupted. How have you been able to return the organization to profitability?

I took this position in August of 2008, and I found that, at the time, we were \$100Mn in debt. We had no cash, and no growth.

To come back from that, you pray, and you work very hard. We refinanced the company, and we made many structural changes. First of all, I personally sign every single bill that is over 5000 RUB. This is one of the reasons why we have a high EBITDA.

In one year, we returned to positive growth, and returned all of our credit. This is the third year in a row that we have 38% growth.

The company was for sale in 2008, and the price was \$80Mn. This year, the company is worth over \$400Mn in cash, and we have decided not to sell—we make too much money! We made a strategic plan for five years, that we presented to our customers and shareholders. They liked it, and decided that Valenta is no longer for sale.

What was the substance of the five-year strategy you presented?

The next five years will not differ from our current strategy. We expect organic growth, because we do not see any reasonable acquisition targets on the market.

We have certain principles for including products into our portfolio. We are doing less research than in previous years into original molecules, and mainly focusing on adding branded generic brands. We look to add products that we can defend somehow—either because there is a difference in the delivery system, or there is a niche in the market, or the market has forgotten a very strong product.

For example, we have a gastroenterology product called Trimedat. The product—the substance—was on this market for 15 years. It was very successful, and then disappeared. We brought this substance back to market as Trimedat, and in one year, we made \$4Mn in sales. This year, we expect to double our sales, and triple in the year after. With no special effort! We know the way. It is an OTC product, and we are working with professionals in our marketing efforts. It is simply the kind of product that if you try it, you will never again want to take a competitor drug.

We have much left to do with Ingavirin, and with a product called Phenotropil. In fact, two of our products are on the plateau—all of the others are only just entering their maturity. Therefore, we expect a high rate of organic development.

By 2015, we expect to add 6-8 new products to our portfolio, in strong synergy with what we have today. Synergy means either the same therapeutic group, or the same clientele. We will continue to focus on the out-of-pocket business, and steer clear of government tenders! We will continue our strong clinical trial practices. We are also building a new factory.

We look for cash—always. There is no project that receives the green light in this company if we do not see sound cash backing for it.

What do you believe are the key components of your managerial strategy in making this company successful?

First of all, as I have said, it is important to distinguish production and marketing. Production is a chemical business. Marketing is a people business.

One of the key components that was introduced in this company is strong analytics. Marketing is often a lot of talk, with no foundation in logic—which I do not like. We believe that there are things that you cannot measure, but you can certainly measure results. For example, sometimes we have to go to the radio to market our product—but if we go to the radio, first we check opportunity costs; subsequently, we want measurable, significant results. In a city where perhaps we should go with radio immediately, we prefer to not choose this option at first, just so I can set a baseline standard and be better positioned to measure my results should we choose to go with the radio some months later.

We have 8 or 10 mathematicians working in this company. They do not understand what we are selling, but they have to work with the products. The product manager may describe some beautiful strategy, but our mathematicians will in turn say that it sounds fantastic, but there is no cash in it. This was introduced two years ago, and our staff started to learn mathematics. This is my main concern: to teach people to speak less without arguments.

I feel that everybody in the company—apart from the mathematicians—should have a strong understanding of what we do. On the weekend, I go to pharmacies, and I have a business card that says “Laszlo Sugar, Senior Medical Representative.” I sell the same package as my medical reps, because I have to understand what they do and the main challenges they face. I expect the same understanding from my entire staff.

When I came to Valenta, I acquired a plate that now sits on my conference desk. The purpose of the plate is the following. In our first meeting in my office, we had 10 people shouting at each other, and I could not understand anything. So we instituted a system wherein anybody who

interrupts anyone else has to put 100 rubbles into the plate. Thousands of rubbles came, and people started to feel that 100 rubbles every ten minutes becomes quite expensive. They started to wait, and to listen to each other. I am not joking—this is a true story. Now, at our meetings, everyone processes and weighs each other's arguments. Then they answer. We have had less need for meetings altogether.

We have fired a lot of people—anybody who could not prove their value to the organization. The bankruptcy crisis was a good moment for us. Truly, I fired people not because we were bankrupt or we could not survive; I fired people to make the organization more efficient. But during a crisis, you can justifiably raise your hands and fire a thousand people. Now that we are doing well, I would be hard-pressed to do so. In a single day, we fired 200 people from the office. It was well planned, and well executed. Since then, our employees understood that work is not a beauty contest.

Again, we are a small company. We work on a personal basis with our clients; we know the opinion leaders; our instruments are based on personal relationships. I believe that people naturally have an aversion to working with each other, because they have certain prejudices, and they are afraid of each other. This is life.

Take the simple version of the Theory of Game: two players, A, and B, could vote to cooperate or not cooperate in each of a set of ten rounds. Their objective is to score the most points they can. The rules are thus: if both do not cooperate, both score zero. If one cooperates, and the other does not, the one who does not cooperate gets two points, and the one who cooperates gets zero. (Imagine you are standing at a red light. One car runs the light, and does not cooperate. He gets two points. Everyone else gets zero.) If both cooperate, then both get one point. What is the best strategy to win the game? One way is to cooperate for 9 rounds, and then not cooperate on the tenth. Then one player gets 11 points, and the other player is left with 9. However, humans are clever: knowing that player A might plan to not cooperate on the 9th round, player B may preempt his loss and not cooperate on the 8th round—"I know that you know that I know." This effect then trickles down to earlier and earlier rounds. People mistrust each other! From the beginning, both players will likely not cooperate on each round, and each game will wind up at zero total points. Both loose, trying to win.

There are two ways out of this. One is to say that the game is infinite—there is no tenth round, so there is no moment where deciding not to cooperate will afford you a win. This is our first strategy: we try to convince our clients that we are playing an infinite game. They will die in this country, and we will die with them. This is what I said during the bankruptcy crisis to clients whose confidence was shaken: we are not a multinational company; we are a Russian company. We

cannot go to conduct our business in the U.S., and leave you here. We are here, and we will be here, no matter our difficulties. I told our clients that they do not have to like us just because we are Russian—but we truly have the same fate.

The second way out is this: one of the players decides to vote 'cooperate' three times, even when his opponent votes to not cooperate. This builds up trust. The opponent will then very likely cooperate on the third or fourth round. Assuming, again, that the game is infinite, our policy is to cooperate even when our clients do not, until we have their trust, and build a mutually cooperative relationship. Their reasons for cooperation will be logical, because we have proven our value as partners.

This is what we do with every product. First, our clients are skeptical because, as you mentioned earlier, there is a stigma against Russian products. They tell us to leave. We come back to the client and show them the results of our clinical trials. They tell us to leave the results on their desk and they will read it. We come back a third time and ask whether they would like to replicate the trial on a small scale, so they can personally oversee the process. They agree to a small trial. They choose not to cooperate twice; they cooperate on the third round. They appreciate the results, because our products are of excellent quality. From then on, we have a strong relationship.

You cannot make any mistake. If you ever once do not vote to cooperate, all trust will be lost.

It is a fact that the chief pulmonologist of Yekaterinburg, when we were launching Ingavirin, told me personally that he does not believe in our product, and then said the same on television! He only wanted to use Western medicine—namely, Tamiflu. One year passed, and he introduced our product in Yekaterinburg. We thanked him, and he told us that there was no thanks necessary; he said that we had convinced him with the results of our clinical trials. He said that he had given his parents Ingavirin instead of Tamiflu.

Our results-oriented strategy worked. Perhaps we could not sell as much as we wanted right away. But for the next twenty years, our product will be a leader, because opinion leaders, physicians, and pharmacists truly believe in its efficacy.

With my 14 products, I am steadily building trust. But again, it all comes back to the cash—I have to be careful that I have the resources. The number of clinical trials we can afford depends on the cash we make. This is what has changed this company. Earlier, Valenta had 200 good ideas, but had the available resources to really finance only two. They financed 200, so all were unfinished. Two weeks after I came to the company, I cut from 336 living projects, 334. I left two. Not because I am more clever than anyone else—everyone had the same choices. I simply understood that 336

was impossible.

It perhaps sounds easy. But during a crisis, strategists disappear. Someone has to cut projects, and someone has to fire two thousand people. Somebody has to take the blame.

Your strategy seems to be less derived of pathos, and more focused on numbers.

While that is true, as I have said before, this is a very personal business. At Valenta, we believe in personal responsibility, and everyone should understand his or her project from beginning to end. If they do, then I trust them. I even explain what is happening at the level of the board of directors—because the staff must know the way forward, and the reasoning behind it.

Another element that was introduced here is a new budgeting structure. We ask each product manager to come to me with a document illustrating their strategy for a particular product and what they would like to accomplish. It delineates their main challenges, and which of these challenges they believe they can solve over the next twelve months. Their first priority is financed in full; their second priority is financed by half; and their third priority is not financed. When their priorities are set, they tell me how much money they need to achieve their goals, and from there we more or less understand how much money the product will make in total revenue, and therefore how much to budget.

Once we create this document, I leave them to work and I do not interfere. I only try to be of help. For example, if they need to show their opinion leader the general manager of their company, I will always go and meet with this leader. However, in general, I try not to intervene and to let everyone be the owner of their budget. They take care of the smallest aspects of their business. On the weekends, they go to the restaurant and make sure they have the meat that their opinion leader likes, and they need not tell me they have done so, because I know they have.

We understand each other. I would not say that we do not very often quarrel, but if you heard this quarrel, you would not be able to understand who is the product manager and who is the general director. Rights are equal for those who bring something to the company! It is not a democracy—I am still the director, because I take the responsibility. But for their portion of the responsibility, I never interfere. Everybody is dedicated to his or her business, and they die for their business.

What is your final message to the international reader of Pharmaceutical Executive?

We are completely different from Western businesses: in size, definition, and the way we work. We are also different from Russian businesses, because everyone here wants to be responsible; this is not a typical characteristic for Russia.

Furthermore, we are efficient. He, who is not efficient, and hardworking, will cause a lot of damage!

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