Interview Part Two: Deloitte Algeria â?? Arnaud de Rincquesen, Managing Partner

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In the second part of this interview, the managing partner of Deloitte Algeria sheds light on opportunity and risk in the Algerian pharma market. He explains the distorting effect of strict joint venture rules and outlines the many challenges in navigating Algeriaâ??s regulatory and legal frameworks while at the same time affirming the countryâ??s considerable underlying potential and solid structural foundations.

To read the first part of this interview, click here.

To what extent is the Algerian pharmaceuticals sector of strategic interest to Deloitte?

The pharmaceuticals sector is of strategic interest to Deloitte because it is composed of a large number of indigenous, family-run SMEs many of which require assistance in terms of financial structuring and execution of growth strategies. Pharmaceuticals also represent an industry that is growing in importance because the government has committed to dramatically raising the level of local production within the next 5 years and seeks to establish the country as a regional leader in biotechnology.

Working with highly consolidated markets such as Algerian energy and telecoms industries must require a thoroughly different approach to working with the local pharmaceutical sector which is dominated by B2B and B2C businesses. How does your office go about handling such a diverse workload?

Anything to do with auditing, integrated services and tax can all be handled by our local team. For some of the more complex consulting functions, we are free to rely on the support of other Deloitte offices. If we are dealing with a pharmaceutical client and we feel that the project could do with someone with a medical background, then the first port of call would most probably be the Paris office. Sometimes we even have recourse to Deloitteâ??s Belgian and Quebecois labour pools. Nevertheless, slowly but surely, we are extending our capabilities. Our current growth rate of 20 percent per annum is testament to that. For the moment, the main factor is to have the sorts of generalists that can correctly identify the problems our clients are encountering and then specialists can be brought in on a case-by-case basis if required.

As you mentioned, the composition of the Algerian pharmaceutical industry â?? with a single state entity, a mix of large multinationals and a proliferation of local SMEs â?? makes it potentially very interesting to a firm like Deloitte. What have been your main interactions with the local pharma market in recent years?

A couple of years ago we were commissioned by the big American laboratories and their association, PhARMA, to undertake an important study into Algeriaâ??s prospects for becoming a regional biotechnology hub by the year 2020. The idea was that the country would eventually become a biotech centre of excellence across the Middle East and North Africa (MENA) and that this would be achieved through public sector and private sector collaboration. The lead firm at the time was Pfizer and we actually presented our findings to the Minister of Health and Prime Minister.

What became clear from that study was that Algeria needs to accelerate the capabilities of its educational apparatus and achieve a much higher level of coordination between the universities, research institutes and private sector laboratories. One particular challenge is that few Algerians who study abroad return to take up employment in their home country so there is a shortfall of qualified scientists and skilled laboratory technicians to be found on the local market.

The other significant challenge is that private sector indigenous firms in the healthcare and pharmaceutical sector tend to be highly fragmented. There seem to be a high volume of very small outfits and a distinct lack of willingness to consolidate the market to a level where suitable size investments in R&D can be made. This is also acting as a break on the development of the local industry.

The business strategies of many of these small, family owned firms are actually highly risky because all medications sold on the market naturally have to receive government authorisation. There is always a risk that the state will withdraw licenses for a healthcare product that you are producing or that they will alter the reimbursement conditions meaning that the end consumers will have to be willing and able to purchase your product by themselves. If you have diversified your business, through mergers and acquisitions, to a point where you possess multiple product lines, then the failure of one product can be compensated for by the others. If, however, your business is so small that you are reliant of sales from a single product then the entire venture can quickly become endangered.

Achieving economies of scale is also highly useful when negotiating with suppliers and making purchase orders for the raw ingredients for the production of medicaments. Holding a sizeable share of the market would also be influential when making applications for patents. This is something that many smaller Algerian firms still have to implement in their strategies. They need to remember that market leader Sanofi-Aventis is itself essentially an amalgamation of many smaller firms.

The government has set an ambitious target for local production of pharmaceuticals. The goal is that 70 percent of medicines consumed on the domestic market should be manufactured locally. How realistic is this? And what is your outlook for the â??Made in Algeriaâ?• brand?

It very much depends on the type of medicines that the government wants to have Algeria producing locally. Production of generics is not going to be of much interest to European and American multinationals, but it does appeal to Indian and South African business groups, because the cost and quality of manufacturing in Algeria is going to be pretty much identical to in their home markets.

There are also certain market niches that have yet to be properly exploited such as the local production of insulin. Diabetes is prevalent across the Maghreb as the burden of lifestyle disease increases so there is a demand market out there that is waiting to be satisfied. There is a limited production of insulin and yet any manufacturer bold enough to start local production would be assured of being able to sell their end product. Local production of certain vaccines would equally make a lot of sense because there is a guaranteed domestic demand for those vaccines used in obligatory inoculations.

So far, locally produced pharmaceuticals tend to be mainly of the dry variety. This is because, as soon as you start dealing with injectable and liquid products, then the base ingredients, manufacturing, storage and packaging become more complicated and the required investment levels increase considerably. Accessing that investment on the local market is not always easy, because the banks and lending institutions tend to be very risk adverse. It is very hard to see molecules for some of the more complex illnesses ever being produced here, because of the baseline expenses involved in the production process and the difficulties of securing access to funding.

Another factor that will encourage local production is the favourable export conditions. The fiscal terms for exporting pharmaceutical products from Algeria are actually very favourable because the government is keen to readdress the balance of payments in an environment where imports are paid for in Euros, but exports in US dollars. Personally, I believe the government is right to set an ambitious target of 70 percent. The sector needs to be challenged if it is to realise its proper potential.

Could you please give some examples of the types of pharmaceutical client you are currently working with?

Right now, we are working with a couple of producers of dry pharmaceuticals. These companies started off as distributors, and over time have branched out into production as well. Most of the chemical ingredients they use for their products have to be imported and they have had to work hard to obtain the necessary authorisations and laboratory validation of their final products. The core challenges they have faced have been navigating a very onerous and bureaucratic administrative framework and securing financing to make the necessary investments. Both have good strategies in place and we will be working closely with them to help them optimise their financial structuring.

Another of the eccentricities of the Algerian pharmaceutical sector has been the lack of a centralised distribution. Unlike many countries where cooperatives have been established to fulfil this function, the producers of medicaments also have to shoulder the logistical burden of distributing to thousands of pharmacies. Cash-flow can also quickly become an issue because of the time it takes the pharmacies to pay for the products that they have acquired. This makes it essential for foreign firms entering the market to identify decent local partners that know the distribution terrain of the local market, that are familiar with the types of prescriptions being written by the local doctors and that already have extensive local networks in place. Deloitte is currently working with a number of producers form Poland, India and Spain that are keen to invest in the Algerian market and engage in technology transfer, but need to identify suitable local partners and define optimum market entry strategies.

From your own experience in setting up Deloitteâ??s Algerian office, what are the secrets to success in the Algerian market for incoming foreign firms?

The Algerian market has its own unique characteristics and it is crucial to understand this if you are to be successful here. It is impossible to conduct business remotely. You have to be physically present and set up a local office. A hallmark of Deloitteâ??s own strategy for Algeria has actually been to first work with local clients so as to learn the ropes, familiarise ourselves with the detail of the domestic market, and gain a better understanding of the local dynamics. Where Deloitte can help is in facilitating and speeding up this process. We can assist with identifying partners and conducting the due diligence for acquisitions and joint ventures. We can ensure that a firmâ??s market integration is in accordance with the local regulatory and legal frameworks and can leverage our research and analytic capabilities to assist in the formulation of appropriate business development and exit strategies. The other main area where we can offer guidance and support is of course in the financial structuring of new entities that are being created.

Each particular sector has its own features, but for the pharmaceutical sector, for example, it is fundamental that an incoming foreign producer understands that they will have to take on responsibility for distribution and they have to consider the required effort to integrate local work forces.

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