

# Interview with Eric Zwisler, President, Cardinal Health China

---

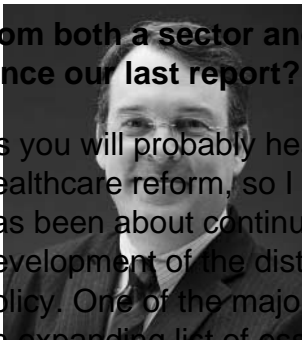
11.01.2013

Tags:

[Cardinal Health China](#)

---

**As the head of Zuellig in 2009. Obviously, a lot has changed since then; from both a sector and corporate point of view, what have been the most important changes since our last report?**



As you will probably hear from other people, the most significant changes here are a result of healthcare reform, so I won't go into that. But the healthcare reform as it relates to distribution has been about continuing to drive scope and scale of the large players, and in many ways using the development of the distribution channel as an instrument of implementing government healthcare policy. One of the major parts of that policy is being able to reach lower tier markets and cities with an expanding list of essential products.

As a major change, that's by far the most important, and there are many sub-changes which have occurred as a result of that: acquisitions, certain large companies forming national platforms, access to government supported and sponsored funds to grow the business, and at the same time development of and investment in enhanced logistics capabilities.

From a corporate perspective, Cardinal Health acquired Zuellig Pharma's China business at the end of 2010. That acquisition was completed and driven by the need to platform Zuellig Pharma's China business for rapid expansion and investment. And Cardinal Health had the interest and the capability to participate in the China market and to meet those investment requirements under the strategic vision and longer-term view of the market here.

**You had founded Zuellig China back in 1993. Have there been any strategic changes since the acquisition, and how is the trajectory nearly two years out?**

Part of the changes have been around speed, execution, and investment levels, and our continued drive to have direct access to end customers, hospitals, and retail pharmacies. As a result, the speed of acquisitions to support that has increased substantially. We've completed a number of acquisitions, and we will continue to acquire companies.

We saw \$90m earmarked for acquisitions this year alone.

Right, and this is a platform to drive the business forward. Historically, our platform was more pharmaceutical-based and quite focused on a very close relationship with multinational suppliers. Cardinal Health will continue that focus in the business, but the strategic focus in development has all been about the capabilities into the market with end-customers that can be implemented on our

---

platform of local distribution. This means we're very much focused on developing value-added capabilities to drive business and satisfy our hospital and retail pharmacy customers.

**We read a quote from you about the community health care focus in China's healthcare reform, and the implications for the distribution sector. You said, "across the board, this is not exactly, as they say in Chinese, a piece of fatty meat. It's more of a bone kind of market." Have the healthcare reforms put more fat on the bone of the distribution segment?**

The community health centres and lower tier markets are basically the essential drug market – the large volume, low-value products that are necessary and absolutely essential to public health. That business, in community health care, and lower tier areas, is driven by volume and public health considerations. They are high volume and low profitability. Whether it's an attractive market or not depends on being able to compete in China on those high volume, low-value, low-margin businesses. For some people, it's an attractive market and they do participate in it. Cardinal Health finds that, given we're a foreign company operating at a higher cost and service levels, our value equations tend to be more at the patented and more specialized end of the market.

**We read another quote from you stating that, though it may be a bit controversial, you thought the importance of relationships in this market is overstated, and that when markets are inefficient, relationships are important. Have relationships then, as distribution becomes more efficient, lessened in importance? What opportunity would such a shift present to a multinational like Cardinal Health?**

Relationships will always play a part of the business in China, and it's just a matter of emphasis – whether you platform your business based on relationships, or value plus relationships. Of course, you must differentiate yourself someplace in how you do your business, and relationships are one way. Product characteristics are another way, and so are patents, medical education programs, pricing, etc. Policies in China have become much more clear and able to differentiate between what are patented and what are non-patented or off-patent products and generics. As we've gone through this period in the last few years, certain multinational products and many price decreases have increasingly taken originator, off-patent products and pushed them into the generic field, which means the level of differentiation is less and less. However, there are still differentiations based on quality, original patent holding, medical education, promotion capabilities behind individual products, etc. As the Chinese government becomes more regular in how they view generic or patented products, there is some sense that in the off-patent area, relationships do become important in pushing the business forward. However, in terms of compliance and relationships, the pharma market has become more compliant and that, to me, means there is less reliance on relationships than in the past – albeit relationships do remain important.

**How does the split between rural and urban growth rates affect Cardinal Health's strategy in China? What implications are there for robust, double-digit growth in rural areas coupled with near flatlines in areas like Shanghai?**

You can go back to the statistics, but in general terms, more developed and penetrated cities have seen dramatic slowdowns in growth, and we all know and feel it. The approach that MNCs take to the more developed regions is about maintaining and continuing to push forward with products but with lowered expectations. These are also very expensive markets to participate in, and they start to look like the rest of the world in terms of how they have to be managed and operated. Growth is coming, variously from second tier or lower tier markets, what would be classed as county level hospitals. If you want to segment the market that way, the viable growth, or where there's enough volume to support development and investment, are coming from second tier cities, provincial capitals, and then some of the surrounding third tier cities and more developed areas.

---

The lower tier market, which is mainly at the county level, is developing, but is still at a point where many companies are looking for alternatives in how to approach them. Some companies have thousands of sales reps, at a higher and higher cost these days, they aren't in a position to double the number to cover all these areas, and there are questions whether there is sufficient volume out of these areas to make them profitable or worthwhile. Generally speaking, that's the view. And while some people are trying different things, and certain joint ventures are being formed, you can point to news from Hisun and Pfizer, or MSD and Simcere, and there are many more examples of MNCs working with local wholesale and distribution companies to penetrate that market. By and large, it appears that for a number of reasons, it will continue for a while to remain outsourced to third party services providing coverage of those markets. The volume out of those markets, even though the growth rates may be high at a county level, is off a very small base. Most production is still coming off urban areas, and it's the secondary cities which are really driving the growth these days.

**Last year Cardinal Health in China inaugurated its CHC division. How important is your focus on retail, and what does it mean strategically?**

CHC is about taking non-prescription products, both OTC and healthcare, and working together with retail pharmacies to try to develop that channel. Retail pharmacies are relatively simple operations focused on prescription pharmaceuticals. They don't look anything like a front-of-store/back-of-store operation we see in the US or Europe and some parts of Asia. The strategic move here is to work with and develop that channel, and to use it to offer additional profitability from non-prescription pharmaceutical business. The channel is currently quite underdeveloped, it won't be a case of slam dunk overnight success. Cardinal Health is committed to CHC, it's an important channel, and we believe in it for the medium to long term as the healthcare reforms continue to be implemented in China. It's commonly said that as the profitability for the dispensing of products is reduced or becomes zero at the hospital, that there will be a movement of dispensing away from the hospital at some point. I'm not saying it's going to go binary, on and off, but we believe that in the longer term, that movement and the retail pharmacy participation and development will be increasingly important. Therefore, it's important to have a well-developed knowledge and participation in the retail pharmacy channel, and Cardinal Health believes we can do that through consumer healthcare products.

How this changes in the future, and how dispensing patterns change, is all open right now. There are many different factors, including patient preference and security of supply chain, as retail pharmacies are one of the primary entry points for fake products, and because of the sheer number of registered pharmacies, amounting to some 400,000 now, it remains relatively hard to manage and control them. Patients themselves may not want to have products dispensed by retail pharmacies, as a general rule. It's not clear how the development will go.

**You strike us as a very calm and controlled manager. Are there any things keeping you up at night, or checking your Blackberry on the weekends?**

Everybody faces the issue of regulation and when we talk about regulation, it's not just about SFDA or product registrations. Right now, the amount of regulation and people who have an impact on your business is enormous, from government people, industry and commerce, tax, customs and you name it. They're all increasingly active and often under conflicting rules, regulations, intents, and purposes. We spend an increasingly large amount of time sorting through all that while maintaining normal levels of operation.

Another area is compliance. It's a daily topic and issue in this market, particularly for an American company doing business here. Cardinal Health is compliant. That has its own set of definitions,

which can be tracked back to FCPA, not to mention the local China anti-bribery and anti-corruption acts. We do, in performance and action, fulfil them all. We, being the only significant directly-managed foreign distribution company in China, are competing against other companies that have different understandings of those rules and practices, and that means we have to work harder to provide compliant value, rather than non-compliant expediency. That is always an issue with our people and customers and in our business, and one we have to deal with it on a daily basis.

Is China a more exciting place to do business now, or when you first arrived 20 years ago? Surely there are different opportunities now, compared with a previously much more open space.

It's difficult to compare because, of course, after 20 years, the concept of excitement loses a bit of its edge! To speak to the changes, early on there was a lot more open space, as you mention, and a lot more chance to create and move forward with the business. Early on in China's opening, there was a relative directness, innocence, and openness. As things have developed, the competition, the size of the stakes when you compete, investments, the rewards or possible losses are much greater. Implementing large company and large operations management practices and ways of doing things are very important. I wouldn't use the word "exciting" to describe any changes. China is now a much harder place to do business. You've got much more hooked-in and knowledgeable local competition that is moving forward very quickly. That difference between us and our competitors and how we define ourselves is much smaller. I'm not saying better or worse, because local competitors are better than we are at a lot of things just as we like to think we are better at a lot of things so that definition is much, much tighter, and it's much harder to compete in a much more sophisticated environment.

**If we compare the distribution breakdown in the USA, Japan, and China, we see some startling figures. In the USA, there are 70 players, and the top 3 account for 96% market share. In Japan, there are 130 players, and the top 3 control 70%, but in China, there are 13,000 players and the top 3 control just 21%. In the USA, one third of all industry volume passes through the Cardinal Health supply chain at some point. Is this the vision for China as well?**

The China market will continue to consolidate, which is pretty obvious, and the consolidation which has occurred so far is primarily financial. Looking at the big three, there's not a lot of operational consolidation. At Cardinal in the US, we basically have one country, one centre, one headquarters, and we run things as one. In Chinese, we call it "Yi Ti Hua", to run things as one company which covers the country. In China, things are different. Operational consolidation is the next step to really use scale to drive business and profitability, and everybody knows that. So you have to be careful when you look at the numbers, because they will suggest the market is more consolidated than in fact it is.

Cardinal's vision in China is to be a significant player here, to be significant in product areas and markets where we can compete, and to be relevant and significant and have a volume-based competitive advantage. What that means is that there are areas in the market, like essential drugs, and other high-volume, low-value products, which is getting a boost from healthcare policy support, but as a foreign company, we're not going to compete, or compete as effectively, in these areas for quite some time. We will continue, as the market develops, to participate in that part of the business where we have competitive advantage. For example, our local distribution companies have a large generics business to deal directly with hospitals, and will continue to develop that segment. One of Cardinal Health's strengths is in running its system as one company, with common practices, platforms, and management. Starting that way, with that kind of oneness in the market, will be, over the long-term, an advantage as we develop.

---

**Paint us a picture of that development: What's your vision for the next five years? Where do you want to bring Cardinal Health, and how are you going to get there?**

First of all, we want to be a lot bigger in our direct access to the market, which means our ability to supply directly to retail pharmacies and hospitals with local operating companies, so we'll continue to acquire. On that platform, we will continue to develop our capabilities in the types of products that we handle, expanding from primarily a prescription pharmaceutical base to other kinds of healthcare products, such as CHC, retail channel, and other products in the hospital, clinic, and retail setting. We can't just talk about products and product categories, because a lot of what wholesalers do revolves around services to customers and suppliers. If you come back in five years, you can expect to see Cardinal Health as a significant service player in certain aspects of outsourced operations for hospitals and retail pharmacies, like we do in the US.

Of course, as with any country moving from a manufacturing to a service base, it's not easy. Cardinal Health's ability to compete in service-based products, and the value we bring, will be much higher than in just the commodity-side of the services, logistics, and straight distribution environment.

The most important point is that no matter what happens with growth rates or changes here in China, the market is here to stay and develop, and you have to be involved and invested here. Things will undoubtedly go through ups and downs, which is why it's necessary to have steady, dependable partnerships to carry through, no matter the issue of market access, compliance, and otherwise. Cardinal Health is a long-term player in China that brings the practices, services, and transparency that MNCs are used to enjoying overseas, with a very long and successful period in China, and the scope and scale to work together to be a true route-to-market partner.

[See more interviews](#)

---