Vietnam Industry Primer

January 2021

Vietnam: Pharmaceutical

A raw gem for patient investors

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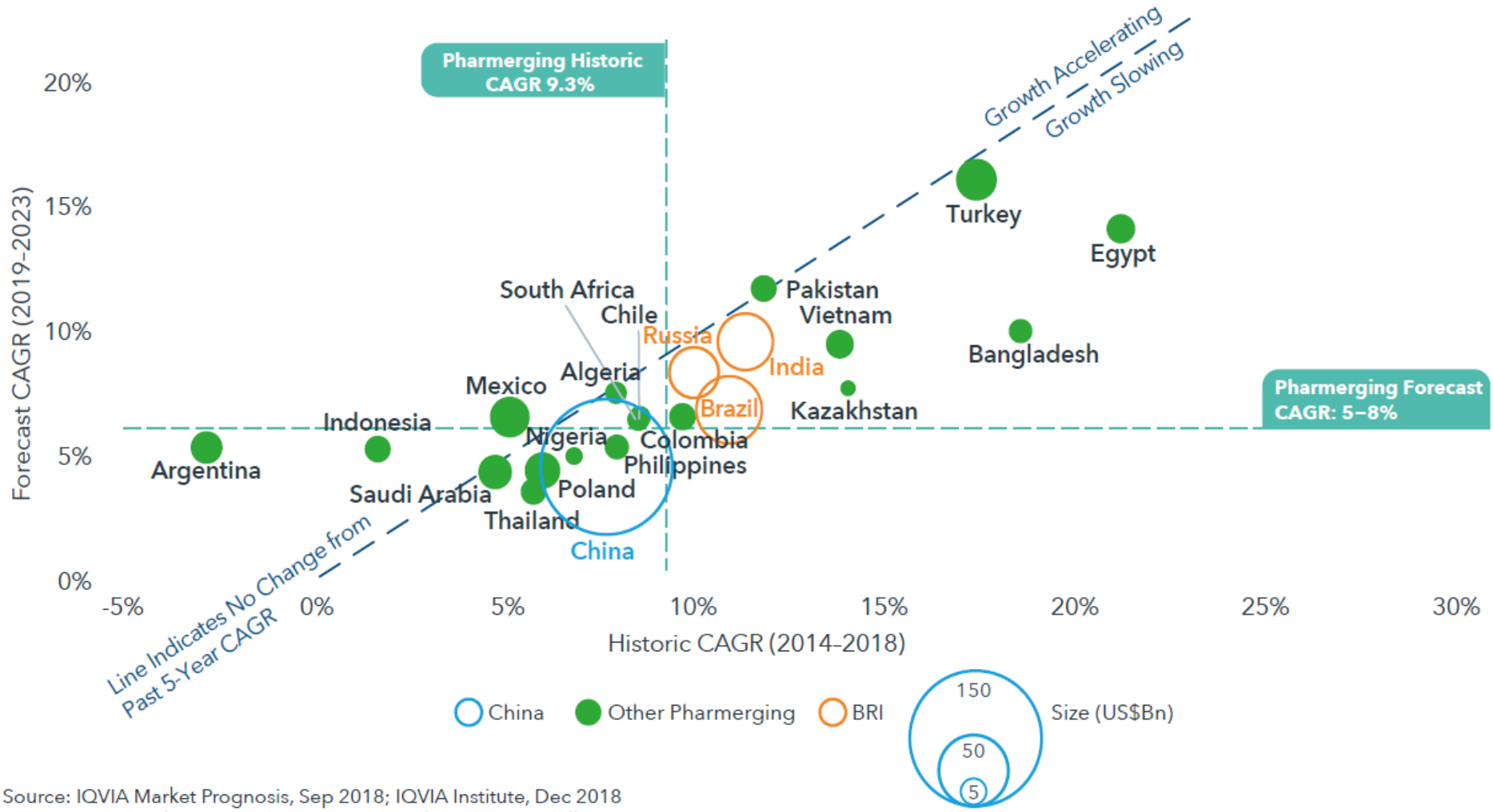
Executive summary

- In general, compared with other countries in Asia Pacific area, Vietnam pharmaceutical industry is expected to have significant growth rate. However, the domestic sector is still at the last stage of the global value chain, and the local pharmaceutical manufacturers need technology transfer from foreign companies
- For the value chain of Vietnam pharmaceutical sector:
  - Raw material (API and equivalents) have highest proportion in cost of manufactured goods, which heavily depend on imported material. Imported API accounts for 80-90% of API demand in Vietnam, with China and India are the two largest API suppliers
  - In recent years, companies with EU-GMP factories (IMP, PME) have outstanding profitability. On base-case scenario, an EU-GMP plants need 4 years to reach profitability, but they have lower production cost than Global pharma companies.
  - For distribution channel, ETC channel is the key for the sector growth; with Category 1+2 (generic drugs) take the highest share. The Category 1 and 2 are dominated by foreign players; while for local manufacturers (Pymepharco, Imexpharm and Tenamyd Pharma) are the key players because they currently own EU-GMP factories. Companies are required to distribute through bidding method, regulated clearly by Circular 15/2019/TT-BYT, which will give priority for qualified contractor with lower evaluated price, this is the advantages for local high-quality generics manufacturers
  - Because of those advantages, there is a trend of developing EU/PICS-GMP factories in Vietnam, in order to win high-value contract packages from ETC channel. Companies with strong financial position with use their own capital, while others will mobilize fund from foreign strategic investors. They will also consider dealing with each other to divide the market share, because of not bidding for imported drugs if that drug line has at least 3 registration numbers of 3 domestic producers.
  - Their strategy is supported by government's policies, when they give priority to local generics manufacturers who achieve EU/PICS-GMP standards. .
- OTC channel is under fierce competition, between modern drug-store chains and mom-and-pop pharmacies. Medicine and Supplement take the largest shares in a pharmacy's revenue.
- Non-communicable diseases (Oncology, diabetes, etc.) will be the key growth for pharmaceutical industry. However, there is currently no high-quality local generics manufacturers those have related product lines.
- For investors who looks for a good investment opportunity, they also pay attention to selling expense and account receivable turnover, those demonstrate the company's business performance

I. Pharmaceutical Overview

VIETNAM: PHARMACEUTICAL OVERVIEW

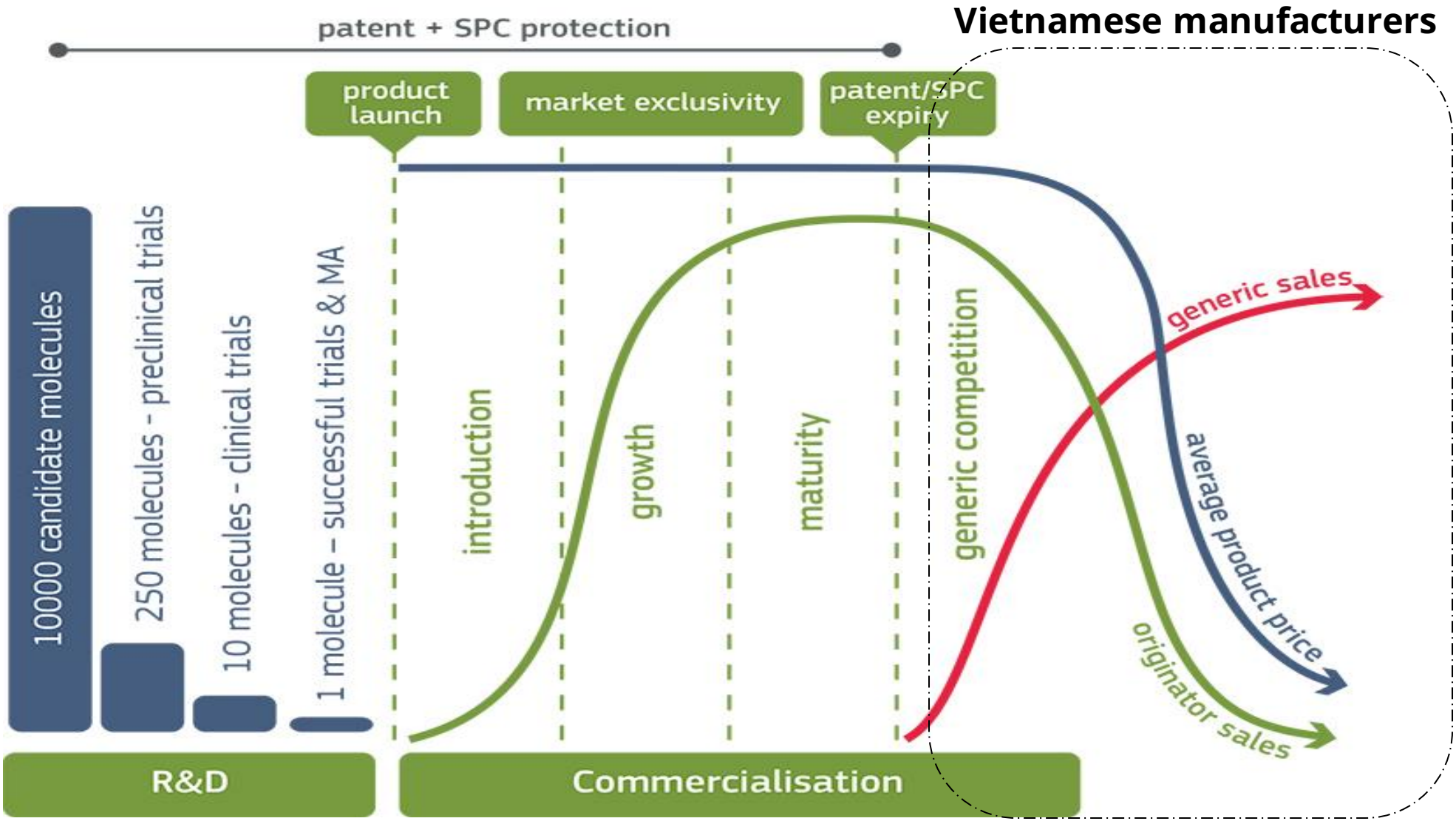
Comparison of pharmaceutical statistic in Asia Pacific



Source: IQVIA Market Prognosis, Sep 2018; IQVIA Institute, Dec 2018
Notes: BRI = Brazil, Russia, India; Argentina is plotted in U.S. dollars

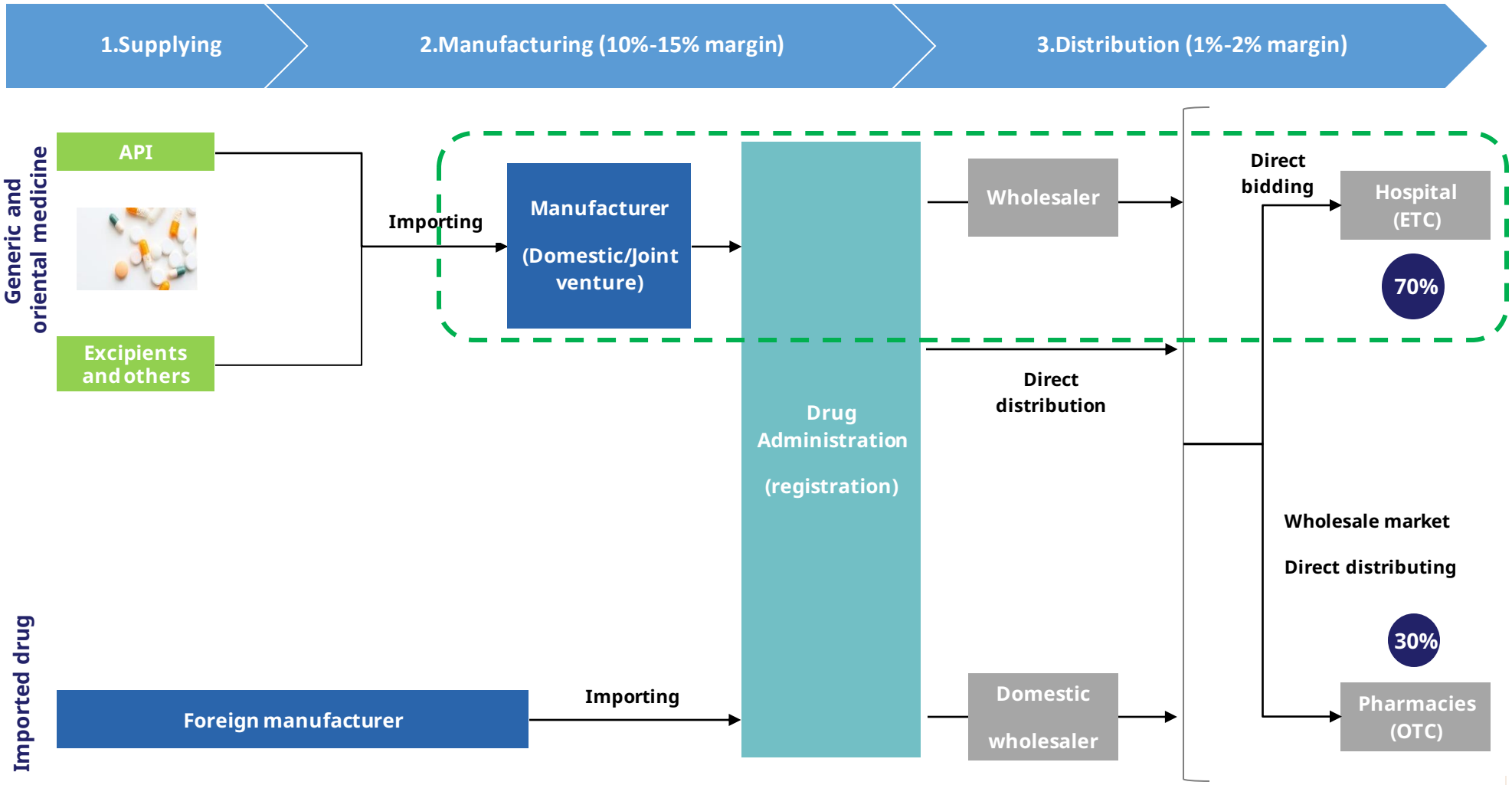
VIETNAM: PHARMACEUTICAL OVERVIEW

Vietnam is still at the last stage of the value chain



VIETNAM: PHARMACEUTICAL OVERVIEW

Value chain of Vietnam pharmaceutical sector



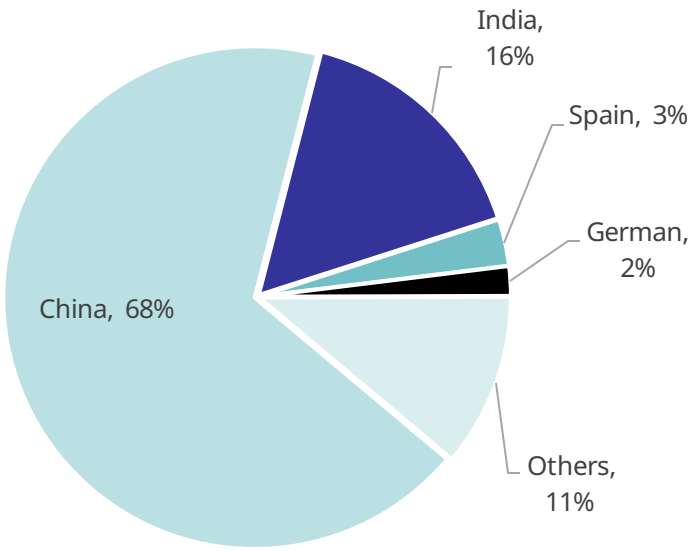
Market size can reach USD 8bn by 2024, with CAGR (2019-2024) is around 9%

II. Value chain analysis

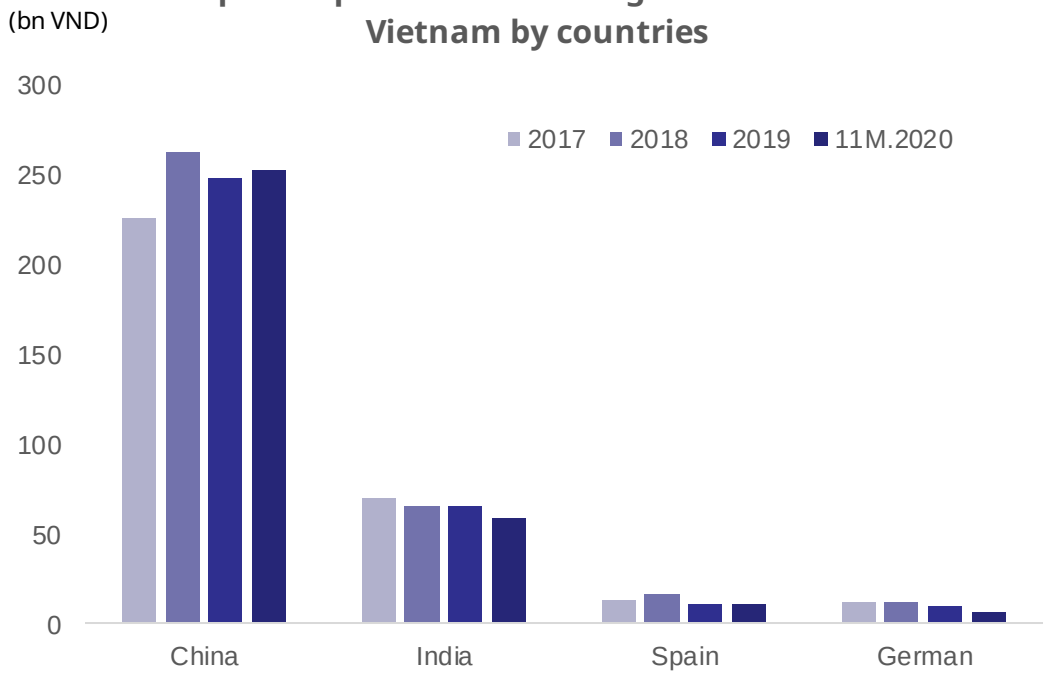
VALUE CHAIN ANALYSIS

Imported API is the main material for pharmaceutical manufacturers

Imported pharmaceutical ingredient value in Vietnam, 11M.2020



Imported pharmaceutical ingredient value in Vietnam by countries



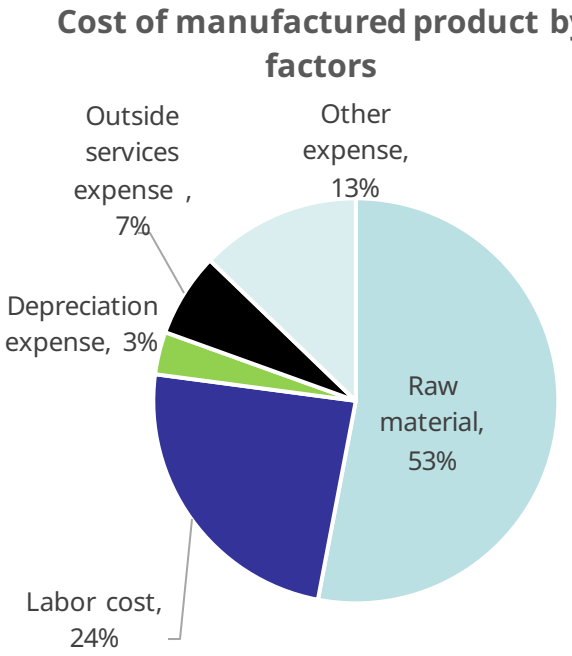
Imported API accounts for 80-90% of API demand in Vietnam.

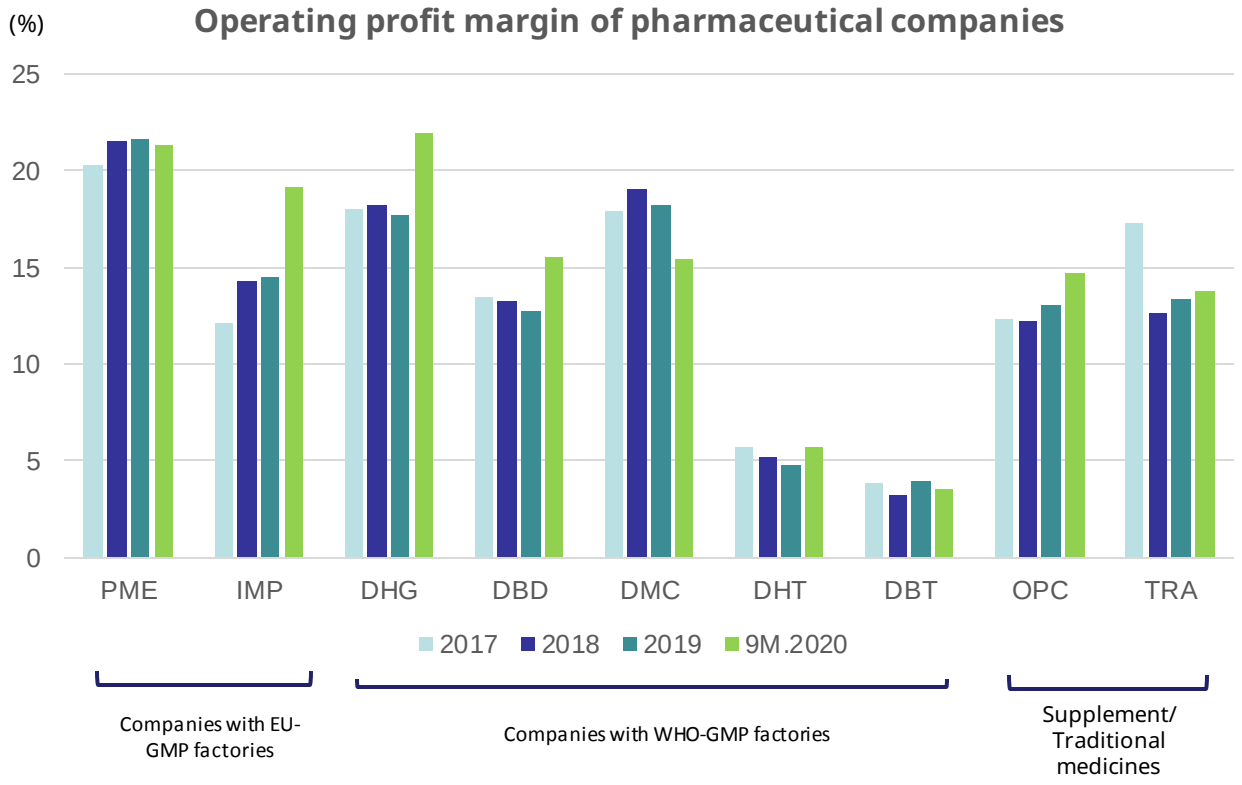
China and India are the two largest API suppliers for Vietnam, accounting for 69% and 16.7% of API import value in 2020, respectively. Material imported from these countries are mostly used by low-level factories (WHO-GMP standard or equivalent)

With European countries (Spain, German...), imported material will be used by higher-level factories (EU/PICs-GMP or equivalent) and have long-term purchase commitment, so that the price of materials from these countries are more stable than from China and India

VALUE CHAIN ANALYSIS

Profitability of pharmaceutical manufacturers is heavily affected by material and labor cost





Raw material (API and equivalent) have highest proportion in cost of manufactured goods (account for 60% of total cost); labor cost (mostly for pharmacist) also accounts for a significant portion.

Outside services and other cost (13% of total cost) **are mainly used to serve for marketing activities**

In recent years, companies with EU-GMP factories (IMP, PME) have outstanding profitability

VALUE CHAIN ANALYSIS

An EU-GMP plants need 4-5 years to reach profitability

Source: jobandsalaryabroad.com, Jetro

CONSTRUCTING

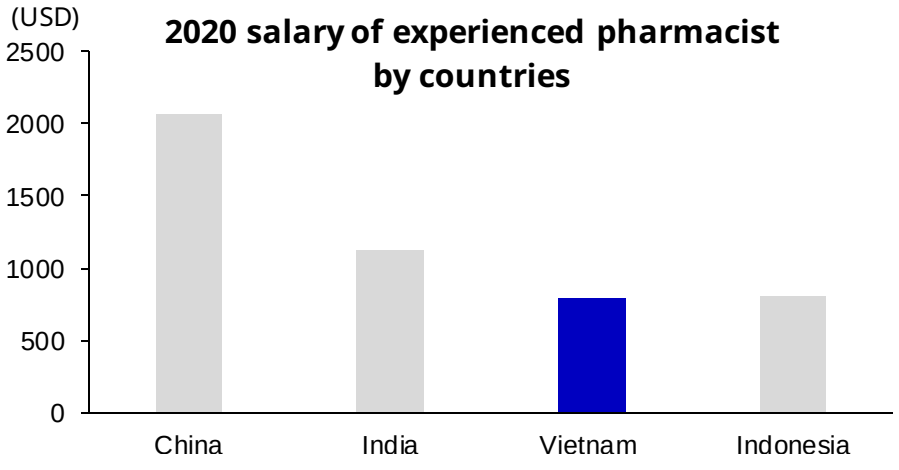
- The minimal amount for a high-standard factory is USD 10mn
- **Construction time: 18-24 months**
- Device & Equipment; Imported from Europe countries/America/Japan (for EU/PICs-GMP plants) or China/Hong Kong/Taiwan (for WHO-GMP plants)

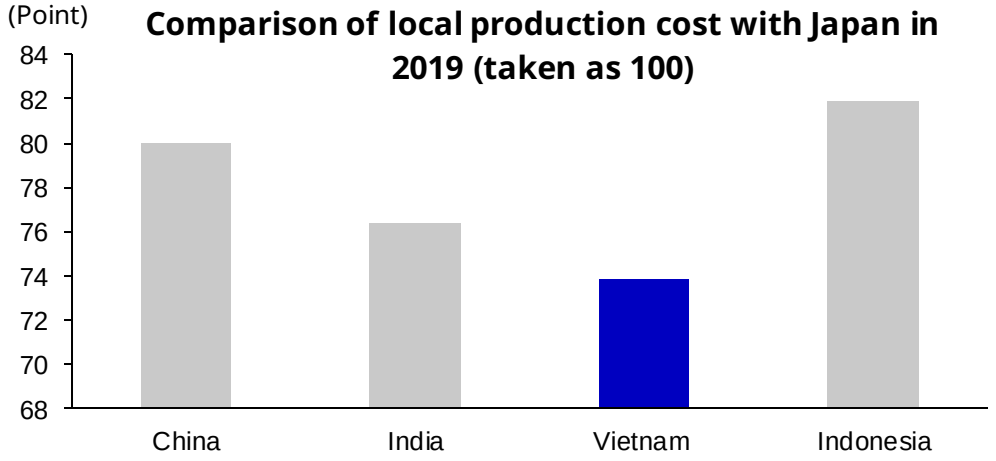
LICENSING

- WHO-GMP standard: Reviewed by Ministry of Health, with review period is 3-6 months
- EU/PICs-GMP standard: reviewed by experts from country that is considered Stringent Regulatory Authorities (SRA), with **review period is 12-18 months**

BIDDING & DISTRIBUTING

- Drug lines need the registration from the Ministry of Health before they can be distributed on the market.
- The registered period is 3-6 months, however it maybe prolonged
- On ETC channel, a package contract usually lasts 2 years -> **products from the factory need 1-2 years to penetrate the entire market,** when the old contracts are expired



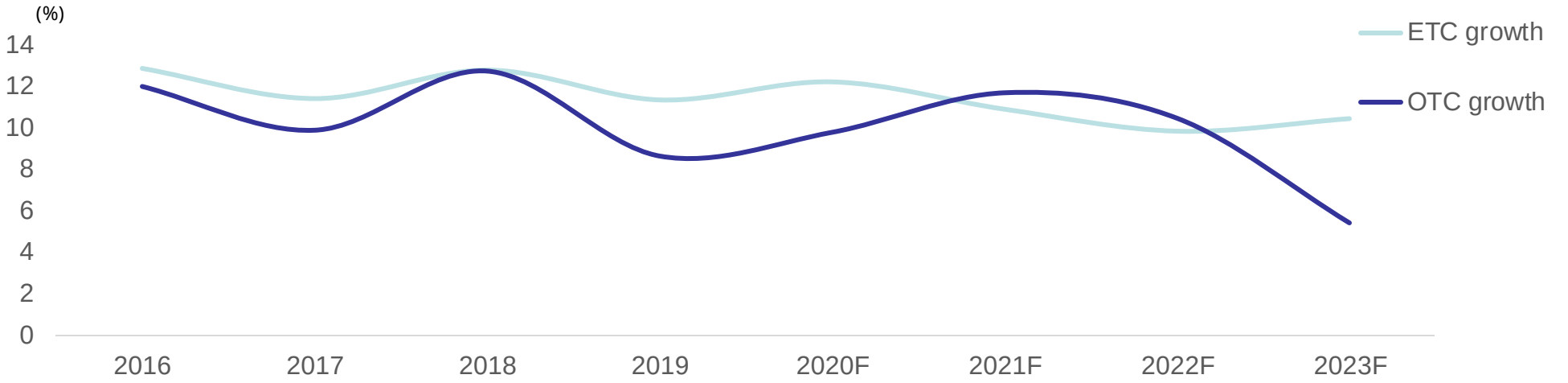


On base-case scenario, an EU-GMP plants need 4 years to reach profitability. But they have lower production cost than China and India (where factories of global companies are located)

VALUE CHAIN ANALYSIS

ETC channel is the key for the sector growth

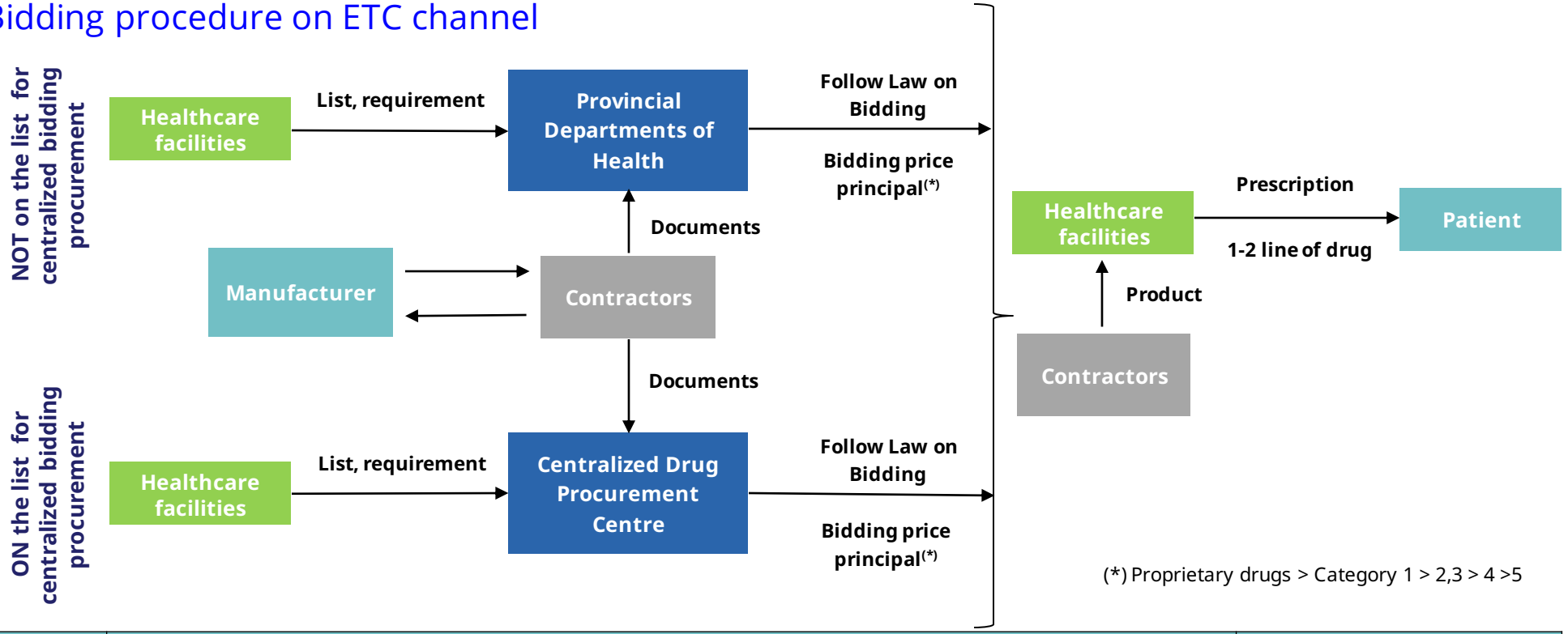
Source: Fitch Solutions



ETC (70% of market size)	OTC (30% of market size)
▪ Including hospitals, clinics and medical centers, etc; concentrate in Hanoi and Hochiminh city ▪ This is the market that manufacturers are aiming for, because if getting successful **they can decrease sales costs and management costs, and be easier to reach the sale volume's economy of scale.** ▪ Companies are required to distribute through bidding method, **regulated clearly by Circular 15/2019/TT-BYT,** in which will give priority for contractor has lowest evaluated price, this is the advantages for domestic manufacturers because they have lower labor cost and production cost than foreign competitors ▪ **The increasing proportion of people participating in public health insurance** (coverage ratio is 90.9% in 2020) is the positive impact on ETC channel's growth rate, when encouraging people to go to medical facilities for examination and treatment instead of buy drug from OTC channel.	▪ Vietnam had more than 57,000 pharmacies and drugstores - one of the countries with the highest pharmacy density ▪ Fierce competition between Domestic drugs/ Foreign drugs, and even illegal drugs ▪ Profit margin of pharmacies is limited by **"Retail margin percent"** - the ratio (%) of retail margin to buying price at a drug retailer ▪ Specific drugs (addictive drugs, injection drugs, High-dose antibiotic) are rarely sold through this channel

VALUE CHAIN ANALYSIS

Bidding procedure on ETC channel

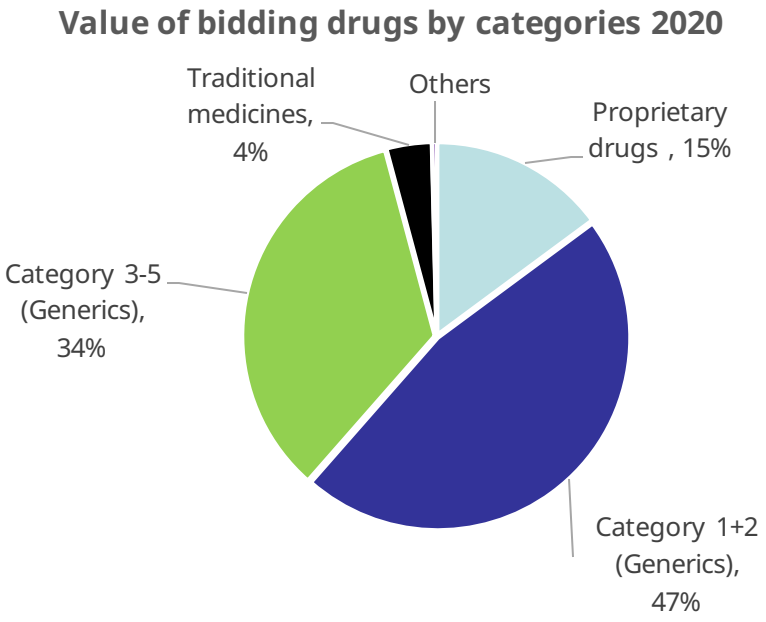


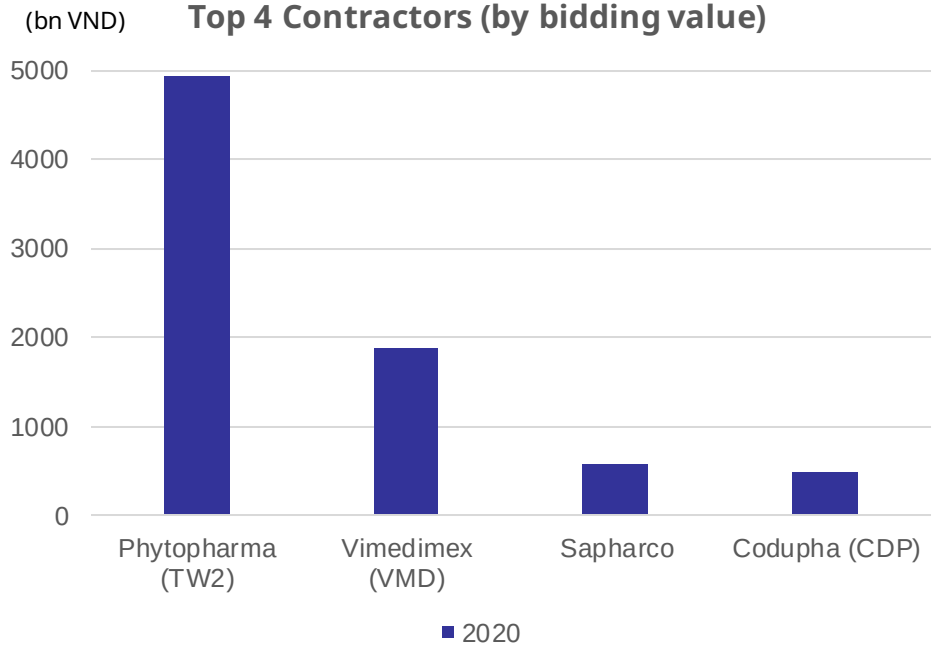
Category	Qualification	Key-players
1	• Drugs manufactured entirely by a manufacturing line satisfying EU-GMP requirements or equivalent requirements in a country that is considered SRA • Drugs on the list of proprietary drugs or reference biological	Global companies PME & STADA joint venture
2	• Drugs manufactured entirely by a manufacturing line satisfying EU/PICs-GMP requirements and granted certificates by the drug authority of Vietnam • Drugs manufactured entirely by a manufacturing line in a country that is a member state of PIC/s and ICH, satisfying PIC/s- GMP requirements	Global companies IMP, Tenamyd Pharma
3,4&5	• Drugs manufactured by a manufacturing line satisfying WHO-GMP requirements or lower	Vietnamese companies

VALUE CHAIN ANALYSIS

Category 1+2 (generic drugs) take the highest share

ETC
(70% of market size)





Category 1+2 (generic drugs) take the highest share: 80% of total value is from Foreign companies; while for Vietnamese manufacturers, PME, IMP and Tenamyd Pharma are the key players. The main reason is that selling prices on Category 1&2 are maintained higher than Category 3-5

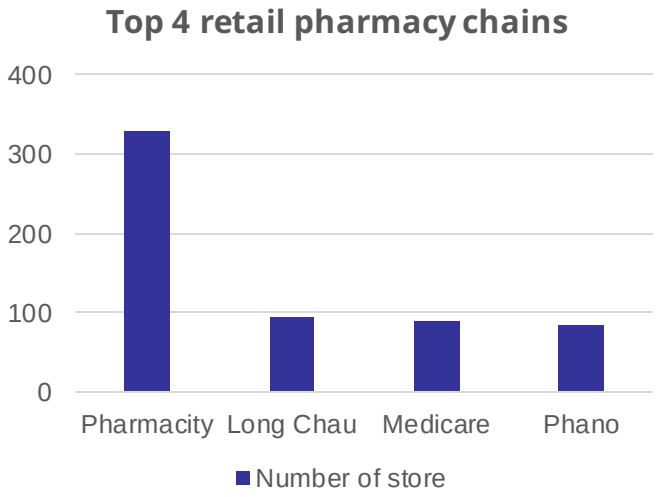
Antibiotic (Cephalosparin, Amoxicilin, etc.), Cardiovascular drugs and Oncology (cancer) drugs are the most popular product lines

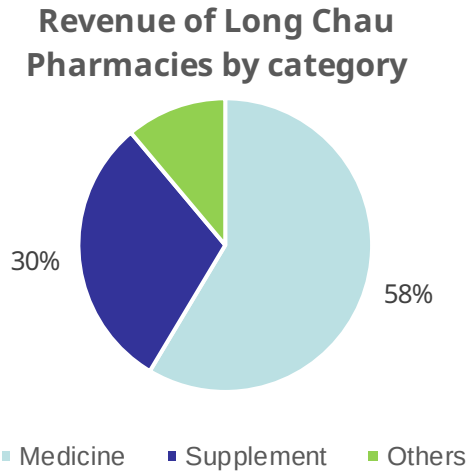
In recent years, after the new ETC bidding regulation has been promulgated, domestic companies tend to focus on production and leave the distribution to key distributors (Phytopharma, Vimedimex, etc.)

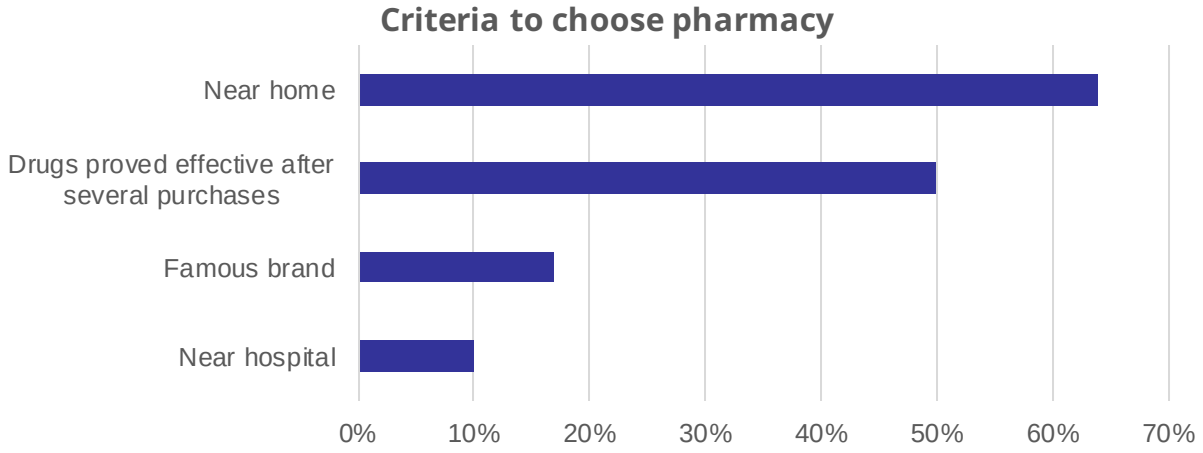
VALUE CHAIN ANALYSIS

There are fierce competition between pharmacy chains and traditional pharmacies

OTC
(30% of market size)







There are fierce competition in OTC channel, between pharmacy chains and traditional pharmacies. Revenue of Pharmacity – the largest pharmacy chain – attained USD 56mil in 2019, take only 3% of total market share

Medicine and Supplement take the largest shares in a pharmacy's revenue. While Medicine has highest profit margin, pharmacy need supplement – in spite of lower margin for retailer – to attract customers

According to customer's criteria, pharmacy chains – in order to gain market share – need to focus on:

- Improving the quality of pharmacist's advisory
- Increasing the number of SKU, especially high-quality drug lines

III. Pharmaceutical sector trends

PHARMACEUTICAL SECTOR TRENDS

High-quality generics will attract attention

	Foreign companies	Vietnamese companies
Proprietary drugs	**100% proprietary drugs are manufactured by foreign companies** Key players: Novartis (Switzerland), Bayer AG (Germany), Sanofi (France) Because Vietnamese government is prohibiting foreign manufacturers from directly contributing drugs to domestic market, foreign companies will establish legal entities in Vietnam for the contribution **There are difficulties for establishing local manufacturing presence and technology transfer**: ambiguous policies and a perceived lack of incentive, the transition requirements from Representative Office to a Foreign Invested Enterprise (FIE) are confusing and time-consuming	Vietnamese companies can not manufacture proprietary drugs, due to the following disadvantages: • Clinical trials: Circular No. 29/2018/TT-BYT are providing the comparatively lengthy and complicated clinical trial application process • Lack of Clinical trial centers, Central clinical trials association and authorization and qualified organizations for standard GCP/ICH safety training • Public-Private Collaborations: regulations and incentives in Vietnam are less applicable to pharmaceutical industry • The R&D cost is high compared with sector's scale (around USD 2.2bn, with timeline for research process is 10 years in average)
High-quality generics (EU-PICs-GMP and equivalent)	**This market is dominated by Global companies** Foreign companies will give priority to acquiring a domestic company in order to: • Shorten the establishing and granting process • Take advantages from domestic companies: infrastructure, land, human resources, distribution channel • Many enterprises are targeted for restructuring and divestment of state capital, while they have long history of operation • High-quality labor cost in Vietnam is lower than countries that dominate in pharmaceutical manufacturing (China, India)	Key players: Pymepharco (PME VN), Imexpharm (IMP VN), Tenamyd Pharma Competitive advantages: Low-cost producer There are 2 trends that domestic companies are aiming for: • Companies with strong financial position (IMP, Tenamyd, Pharbaco) will establish EU/PICS-GMP factories in order to win high-value contract packages on ETC channel. They also consider dealing with each other to divide the market share, in order to take advantage of Circular No. 03/2019/TT-BYT - not open bidding for imported drugs if that drug line has at least 3 registration numbers of 3 domestic producers • Other companies (PME, Mekophar) will sell their shares to foreign strategic investors, and use the fund to establish high-tech factories. Their products will be exported, or bid on ETC channel
Common generics (WHO-GMP and lower)	The participation mainly comes from Indian and Chinese companies	This market is dominated by Vietnamese companies, with nearly 180 companies that met WHO-GMP standard Key players: Binh Dinh Pharma (DBD VN), Hau Giang Pharma (DHG VN) Vietnamese government has protection policies for Common generics that domestically produced and granted certificates in Vietnam
Traditional drug	The participation comes from Chinese companies	This market is dominated by Vietnamese companies

PHARMACEUTICAL SECTOR TRENDS

EU/PICs-GMP qualification is the future

Company	Qualification	Main drug lines	Remark
Pymepharco (PME VN)	EU-GMP	antibiotic - Cephalosparin	
Pymepharco (PME VN) – Hoang Van Thu manufacturer	EU-GMP	Non-betalactam	Expected to be granted in 2021
Imexpharm (IMP VN) - Binh Duong manufacturer	EU-GMP	antibiotic - Cephalosparin	
Imexpharm (IMP VN) - Vinh Loc manufacturer	EU-GMP	antibiotic - Penixilin & Amoxicilin	
Imexpharm (IMP VN) – High-tech manufacturer	EU-GMP	Non-betalactam	Expected to be granted in 2021
Hau Giang Pharmaceutical (DHG VN)	Japan-GMP (equivalent to EU-GMP)	Effervescent tablets	They also have PIC/s - GMPs production line,but they need the certificate from country that considered SRA
Pharbaco (PBC VN)	EU-GMP	antibiotic - Cephalosparin	The product line will be granted in period 2021-2022
2/9 Pharmaceutical (NDP VN)	EU-GMP	antibiotic - Cephalosparin	Expected to manufacturing from 2022
Binh Dinh Pharmaceutical (DBD VN)	EU-GMP	Cancer	The product line will be granted in period 2021-2022
Ha Tay Pharmaceutical (DHT VN)	EU-GMP	N/A	Expected to manufacturing from 2022
Traphaco (TRA VN)	EU-GMP	Eye/nose drops	Expected to manufacturing from 2022
Mekophar (MKP VN)	Japan-GMP	Antibiotic, Analgesic – antipyretic	Current products are used only for exporting

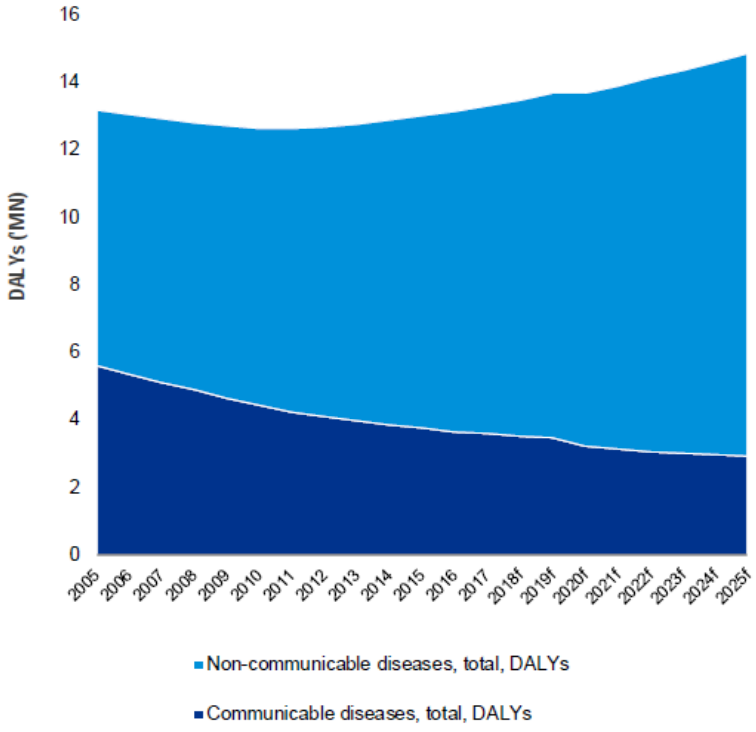
PHARMACEUTICAL SECTOR TRENDS

Drug lines for non-communicable diseases will be the key growth

Leading Therapy Areas Spending & Growth in Developed and Pharmerging Markets

Therapy areas	2023 Const US$ Spending	2019-2023 CAGR Const US$
Oncology	140-150	6-9%
Diabetes	115-125	7-10%
Respiratory	70-80	2-5%
Autoimmune	70-85	6-9%
Pain	40-48	0-3%
Antibiotics & Vaccines	40-48	0-3%

Vietnam's burden of disease projection



Non-communicable diseases (Oncology, diabetes, etc.) will be the key growth for pharmaceutical industry**.**

Binh Dinh Pharma (DBD VN) is one of the few companies with significant revenue from Oncology Drugs. However, their factories have not been granted for EU-GMP qualification.

PHARMACEUTICAL SECTOR TRENDS

Local generics' manufacturers continue to benefit from the policies

The tender circular 15/2020/TT-BYT introduced a system of price negotiations, in which Proprietary drugs will be added to the list for procurement through price negotiation.

Multinational companies may have to reduce prices to compete with generics in Group 1 or even lower, thereby eroding profits. While local generics' manufacturers who achieve EU-GMP standards in tenders will benefit from this policy

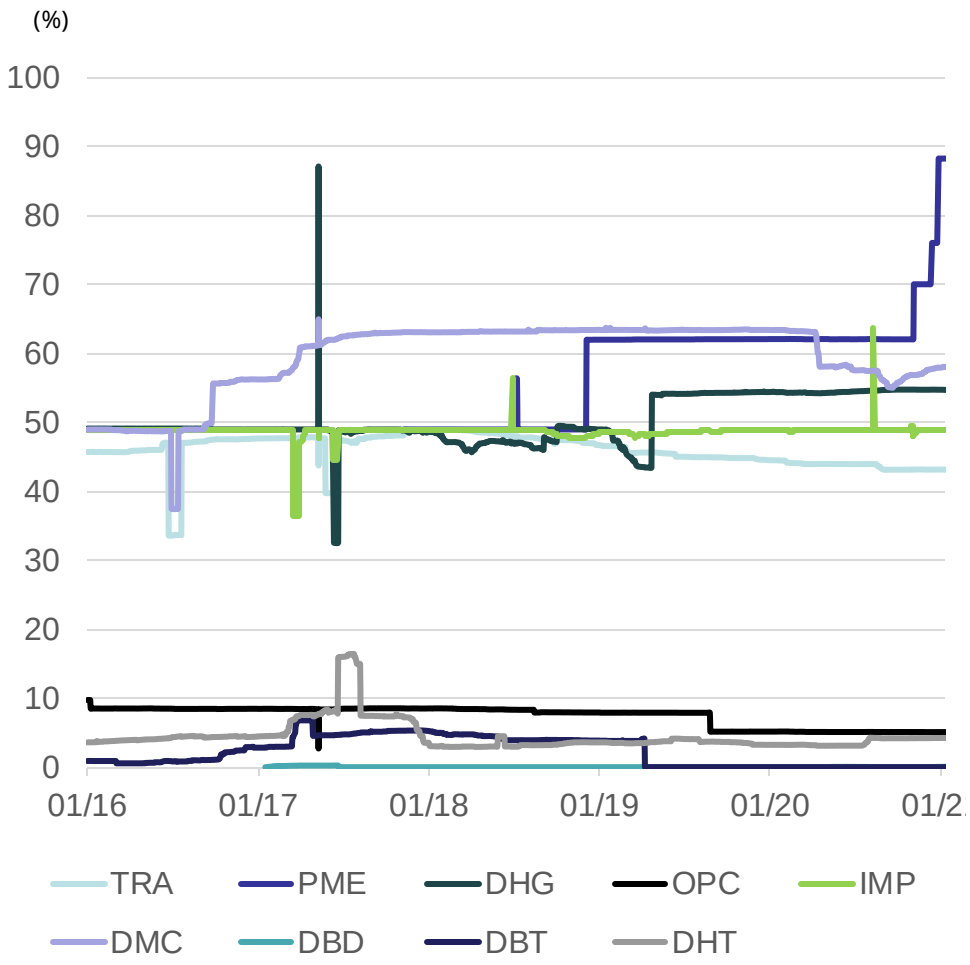
Budget pressure leas Social Health Insurance to encourage the use of generics in public hospitals and Proprietary drugs use will be capped. This is also a support factor for High-quality local generics' manufacturers

From 2021, people who have health insurance cards and go to the provincial-level hospitals, the full inpatient fee will be covered by Social Health Insurance. This policy will encourage patients to go to provincial-level hospitals – where local generics' manufacturers are given priority - for medical treatment.

PHARMACEUTICAL SECTOR TRENDS

Continued to be the target for M&A Activities of foreign companies

Foreign ownership of listed pharmaceutical companies



Company	Strategic Investor
PME VN	Stada Service Holding B.V
DHG VN	Taisho Pharmaceutical Holdings
IMP VN	SK Investment Vina I Pte.Ltd.
DMC VN	Abbott Laboratories (Chile)
DHT VN	ASKA Pharmaceutical (In process)

Vietnamese companies will continue to be the target for M&A activities of foreign companies, because of:

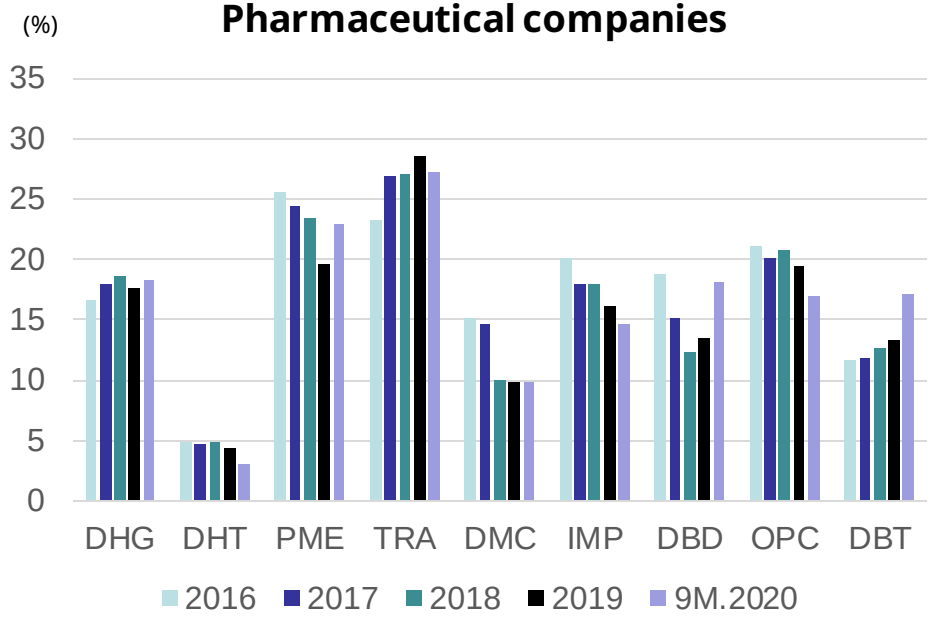
- Low production cost compared to neighboring countries (India, China, etc.)
- Protection policies for Local generics' manufacturers will be maintained in the following years in order to encourage for the technology transfer from foreign companies.
- Pharmaceutical companies have been allowed to increase their foreign ownership to 100% of total outstanding shares; meanwhile, the average ownership rate in listed companies is at 50% -60%.
- There are difficulties for Vietnamese pharmaceutical companies to mobilize capital from domestic investors, because of long payback period.

IV. Key accounting items

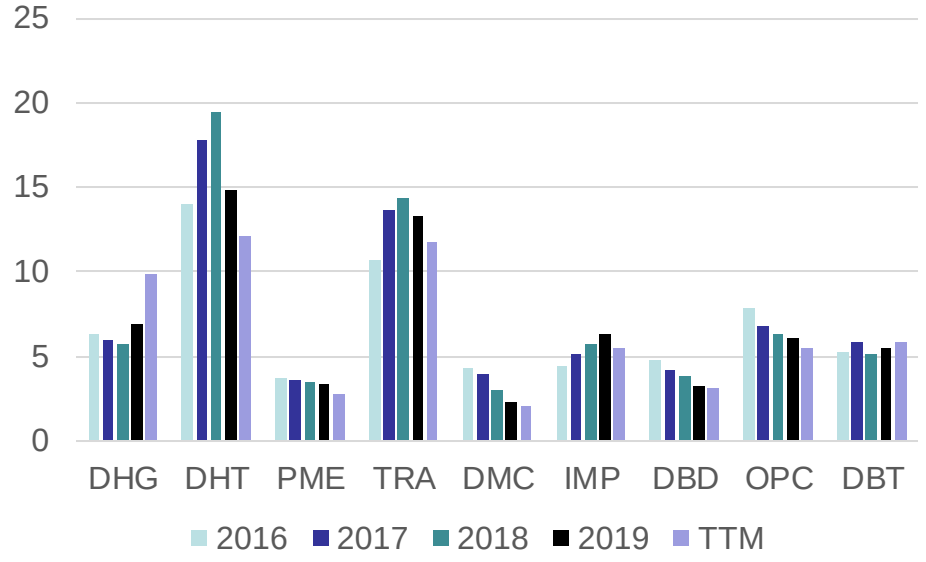
KEY ACCOUNTING ITEMS

Investors should pay attention to selling expense and account receivable turnover

Selling expense/Revenue of Pharmaceutical companies



Account receivable turnover of Pharmaceutical companies



Selling expense is an important item for a pharmaceutical company, when they need to expand distribution system, salary for pharmacists to introduce products to patients, and discount for distribution companies who participate in bidding to enter ETC channel

We should also pay attention to the company's **account receivable**, especially on ETC channel, when hospitals do not immediately pay the supplier upon receipt of products.

KEY ACCOUNTING ITEMS

Companies hold their plant in term of "Construction in progress" to avoid depreciation cost

Listed Pharmaceutical companies with new plant in process

Company	Construction in progress (End of Q3.2020) (bn VND)	Status of the new plant
PME VN	798.4	The construction is completed, waiting for being granted EU-GMP Qualification
IMP VN	551.2	The construction is completed, waiting for being granted EU-GMP Qualification
DBD VN	174.2	The construction is completed, waiting for being granted EU-GMP Qualification
PBC VN	1,019.1	In the process of construction

Some Vietnamese companies (IMP, PME, DBD) have completed the new plant's construction, however they still hold this asset in term of 'Construction in progress" until they have granted for EU-GMP qualification and put the plant into operation; with main purpose is delaying to recognize the depreciation cost.

Appendix: Selected companies profile

SELECTED COMPANIES PROFILE

	DHG PHARMA	Bidiphar	Traphaco
MAIN PRODUCTS	• Antibiotic • Analgesic – antipyretic	• Antibiotic • Oncology	• Traditional medicine • Supplement
POSITION	•Hau Giang Pharmaceutical (DHG VN) is one of the largest listed companies (in term of sales and capital) •They was also considered an enterprise with the most widespread and largest distribution network (35 branches in Vietnam) •Currently, they are operating two pharmaceutical plants which satisfy WHO - GMP standards. They also have product line that met PIC/S-GMP standard granted by Malaysia – country not considered as SRA	•Binh Dinh Pharmaceutical (DBD VN) is considered a pioneer in the pharmaceutical industry, as the first domestic company to manufacture oncology products •Currently, they are focusing on ETC channel, as one of the largest manufacturing companies in category 3 •They own a pharmaceutical plant that satisfy WHO - GMP standards	•Traphaco (TRA VN) is the traditional medicine manufacturer with highest market share in Vietnam. They own the raw material source and do not need to import from China •They own 3 traditional-medicine plants and 1 generic plant those met WHO – GMP standards. In which, the generic plant have been put into operation since 2017 with the main drug-line is Eye/nose drops
DEVELOPMENT STRATEGY	•Cooperate with Taisho – strategic investor – for technology transfer and upgrade their current plants to satisfy EU-GMP requirements or equivalent in order to win high-value generics contracts in category 1&2 on ETC channel. •They also expect that by cooperating with Taisho, they can export products to Japanese market	•Upgrading new product lines of Oncology drugs in order to satisfy EU-GMP standards and win high-value generics contracts in category 1&2 on ETC channel. However, they can not determine the time to be certified	•Upgrading new product lines of Eye/nose drops in order to satisfy EU-GMP standards and win high-value generics contracts in category 1&2 on ETC channel.

SELECTED COMPANIES PROFILE

	PMP	IMEXPHARM
MAIN PRODUCTS	• Antibiotic	• Antibiotic
POSITION	•Pymepharco (PME VN) is the only listed companies that can win contracts in category 1 – category with highest bidding price for generics drug •They also have a large distribution network (20 branches in Vietnam) •Currently, they are operating a pharmaceutical plants, with beta-lactam production lines that satisfy EU-GMP standard. They also have an non-betalactam plant waiting for being granted EU-GMP Qualification	•Imexpharm (IMP VN), together with PME, is one of a few companies have EU-GMP plants; they are taking the advantage of being a low-cost producer and having high-tech factories to gain market share from foreigner manufacturers •Currently, they are operating a WHO-GMP pharmaceutical plant and 2 EU-GMP pharmaceutical plant. They also have an non-betalactam plant waiting for being granted EU-GMP Qualification
DEVELOPMENT STRATEGY	•After being granted EU-GMP Qualification, they will put the Hoang Van Thu manufacturer into operation and take market share in category 1 generic contract •Stada Service Holding B.V will completely buy all stakes of PME, which will make it easier for them to transfer technology to the company	•After being granted EU-GMP Qualification, they will put the Binh Duong High-tech manufacturer (IMP4) into operation • For the cooperation between IMP and SK Investment Vina III Pte., they can not decide their cooperation strategy, until the Covid-19 pandemic has been controlled and they can discuss directly.