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**COMPETITION ISSUES IN THE DISTRIBUTION OF PHARMACEUTICALS**

**Contribution from China**

-- Session III --

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Ms Cristiana Vitale, Senior Competition Expert, OECD Competition Division  
Tel: +33 1 45 24 85 30, Email: cristiana.vitale@oecd.org

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## COMPETITION ISSUES IN THE DISTRIBUTION OF PHARMACEUTICALS

-- China\* --

### 1. Introduction to Distribution of Pharmaceutical in China

#### 1.1 *Brief on the sector of pharmaceutical distribution*

1. The Chinese pharmaceutical market is in a stage of rapid growth. It is fundamental that the reform of health care is deepening and the Chinese government continues to increase investment in health sector. Under this circumstance, the coverage of health insurance is keep expanding, and the pharmaceutical market acquires fast development with contribution of economic growth and aging population. In 2012, the total sales in pharmaceutical distribution sector of China rose 18.5% to 1100 billion RMB (approximately 134 billion euros) that exceeds 1000 billion RMB for the first time in history. It is expected that the share of China in the pharmaceutical market of the world will increase from 3% at present to 7.5% in 2015, which makes China become the second largest consuming country of pharmaceutical in the world.

2. Up to the end of 2011, there are over 10 thousand pharmaceutical wholesalers in China with the total sales of 500 billion RMB (approximately 61 billion euros), increasing 17.6% than last year. At the retail level, there are about 420 thousand pharmaceutical stores, including 270 thousand individual stores and 150 thousand stores controlled by 2600 chain store companies, which realize the total sales of 200 billion RMB (approximately 24.4 billion euros) with the increase of 16% compared with last year. Over 100 companies acquire qualifications to sell pharmaceutical on the Internet.

3. From the aspect of territory, the pharmaceutical distribution concentrates on economically developed areas, such as the east, north and central south of China, and Beijing, Shanghai and Guangdong province etc. In 2012, the proportions of total sales of the six regions are respectively: East China 40.5%, North China 18.9%, Central South China 20%, Southwest China 12%, Northeast China 5% and Northwest China 3.6%. However, the sales of top three regions take 79.4% of the market. The top ten provincial markets are, in order, Shanghai, Beijing, Guangdong, Jiangsu, Anhui, Zhejiang, Shandong, Chongqing, Tianjin and Henan, which accumulate to the market share of 66.2% in China.

### 2. The business model of pharmaceutical wholesale in China

#### 2.1 *Direct selling model*

4. The direct selling model is also called direct distribution model, which means that pharmaceutical products are directly distributed from the upstream supplier (such as producer or commercial dealer) to the retail terminals (such as hospital or retail store) through only one dealer. This model has advantages such as high gross margin, strong control power to retail terminal, and strong negotiating power on price and distribution right with the upstream pharmaceutical producers. It is important that this flattened or

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\* Contribution submitted by Mr. Yang Jianhui, an official from the Ministry of Commerce of the People's Republic of China.

simplified distribution has become one of the most significant trends in pharmaceutical sector of China. There are a lot of practices on distribution management during public bidding procurement process in some provinces.

## **2.2 Allocation model**

5. The allocation model is also called distribution model, which means that pharmaceutical products are distributed through several layers of dealers before reaching the end users. This model could help to cover a wide range of market, accelerate cash flow, decrease the risk of bad debts, and avoid cash to be occupied at retail terminals. Because the producers or upstream dealers do not need to market on retail terminals, the cost to build the distribution channel is relatively lower and the speed is faster. Meanwhile, this model's gross margin is not high. With the implementation of a public procurement system that the province purchases its pharmaceutical demand together through bidding, the allocation model is not any more the main distribution method.

## **2.3 Fast wholesale model**

6. Fast wholesale model aims to sell pharmaceutical to the rural markets and border areas between urban and rural places. In practice, upstream dealers acquire large quantity pharmaceutical from producers, and then quickly distribute to small wholesalers, retail stores and hospitals with only small profit margins, which therefore speed up its cash flow. The model has advantages such as flexible distribution, low cost of building distribution channel, competitive price and quick cash flow. However, because of the improved management by the government and expanded coverage of medical insurance at rural areas, the fast wholesale model is being less used.

## **2.4 Agent model**

7. Agent model is much more complex than other models. It has varied operation methods, such as using import agent, broker, and legal person agent. The model is helpful to operate in a specific territory market, decrease the marketing cost, and easy to quickly reach and control the retail terminals. The profit margin is therefore relatively high. With the implementation of bidding system, the agent model is more challenging but will still last some time in China.

## **2.5 The third party logistic model**

8. In order to reduce the operating cost, the pharmaceutical producers or dealers would outsource the logistic business to the professional third party with the qualification to transport pharmaceutical. Through a particular communication system, the producers or dealers keep close contacts with the third party and realize its control and management during the whole process of logistic. The model is highly professional, and easy to achieve scale economy and low logistic cost. It is expected to be more frequently used by the large or medium sized pharmaceutical dealers in China.