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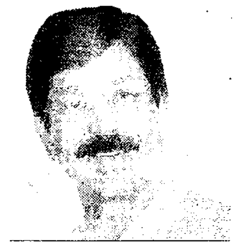
Poor pharma policy

The premium valuations that Indian pharma companies have commanded so far could take a hit



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THE Union Cabinet rejected the proposal of the Department of Industrial Policy and Promotion (DIPP) to limit Foreign Direct Investment (FDI) in domestic manufacturers in rare and critical drugs. The Cabinet decided that the current policy in brownfield and greenfield projects in the pharmaceutical sector will continue to be subject to the additional condition that in all cases of FDI in brownfield pharmaceuticals, there shall be no non-compete clause in any of the *inter se* agreements.

The DIPP and the Cabinet are of the opinion that if a promoter sells one facility or operation, he should not be barred from starting another venture.

The DIPP has notified the new FDI policy for the pharmaceutical sector and it retains its old norms of keeping the FDI cap at 100% for the sector. Moreover, greenfield FDI proposals will be allowed through the automatic route while brownfield FDI will be vetted by the Foreign Investment Promotion Board (FIPB). But a new clause has been added as per which non-compete clauses will not be allowed for pharmaceutical M&A involving FDI.

The new policy says that non-compete clause will be allowed only in special circumstances, and such requests will have to be vetted through FIPB. However, the press note on the new policy doesn't shed any light on what precisely constitutes special circumstances for allowing non-compete clause. It is a normal practice by any buyer and seller to have a non-compete clause as it helps to avoid confusion in the market place.

The move to have no non-compete clause will hit the premium valuation which the pharmaceutical companies have commanded so far. The government needs to clarify under what special circumstances the non-compete clause would be allowed. However, leaving it to the discretion of FIPB may not be a good idea.

It is important to take a look at the DIPP argument as it runs counter to the Indian entrepreneur spirits. Exclusion of non-compete clause for every M&A deal may dampen investments in the domestic market. FIPB should use this clause selectively and only in cases where shortages will occur or future R&D will suffer.

Given the current scenario, the fear of a monopolistic situation and thereby leading to price increases or the fear of the production being diverted to global market is completely without any rational basis.

Acquisition of Indian companies started in 2008 with Japan, Daiichi Sankyo taking over Ranbaxy laboratory. This has been followed by many—Sanofi buying Shantha Biotech, Matrix Lab taking Mylan, PiramalHealthcare by Abbott Laboratories and the latest, Mylan acquiring Agila Specialties.

There is no data to substantiate on record since 2008 to show that it has led to any monopolistic situation or non-ability of the products. On the contrary, we have seen these companies introduce 341 new drugs and formulations in the domestic market since May 2009 and the Department of Pharmaceutical (DoP) price analysis shows almost no changes in prices. There are misplaced concerns that acquisitions in brownfield may lead to shortages and increase in drug prices in the country.

The government must seriously think to build an ecosystem to encourage innovation and R&D in the pharmaceutical sector. It is imperative to create a secure environment that fosters protection through intellectual property rights and it would certainly encourage investments in R&D thereby making the domestic market conducive for FDIs.

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Policy.