SCRIP MAGAZINE

Survival strategies

Contract sales organisations are facing stiff competition in a dynamic marketplace, particularly in France. Jean-Michel Peny looks at the French market and the survival strategies such companies are having to adopt

Pharmaceutical companies spend the largest proportion of their overall budgets on sales and marketing with good reason. A recent survey by Andersen Consulting found that 42% of the difference in financial performance across pharma companies can be explained by superior sales and marketing capabilities. In the US, pharma companies spend around US$5 billion a year on their sales forces and the total headcount of medical representatives for the top 50 pharma companies is now estimated to be more than 70,000.

As sales forces costs represent as much as 20% of total pharma sales, pharma companies often see this as a potential area to cut costs. The use of contract sales organisations (CSOs) is increasingly being seen as a way to convert long-term fixed costs into short-term variable ones through outsourcing. CSOs provide a flexible workforce that can easily adapt to whatever is required throughout the lifecycle of pharma's products.

Despite this flexibility, CSOs have not caught on everywhere. In Germany and Italy, employment legislation precludes the use of CSOs, while in Southern Europe the predominance of 'relationship selling' also acts as a barrier to their use. However, CSOs have become widespread in the US, the UK and France. And in recent years, the market has become highly competitive, no more so, perhaps, than in France, where excessive CSO capacity, along with more stringent pharma purchasing policies, have lead to a deterioration in market profitability. In this context, CSOs need to develop robust strategies to protect, and even restore, their bottom lines to survive in this turbulent environment.

Dedicated or syndicated?

Primarily, CSOs offer two kinds of service – dedicated and syndicated sales forces. In France, certain players, such as MBO and CLI Innovation, focus on contract sales forces with recruitment activities for medical representatives and area managers. Others, such as Innovex or Cider Santé, offer multiple services, including clinical development, marketing and sales activities (see Figure 1).

Dedicated sales forces function in the same way as in-house sales teams, without being part of the company's headcount. They are used mainly to support the launch of new products or defend the position of existing ones. They can be managed either by the CSO or the pharma company itself. Agreements are signed for at least one year and tend to cover three or four products. For their part, CSOs receive a fee ranging from €533 to €915 (US$463 to US$796) per month per representative, on top of their operating costs.

Syndicated teams are managed by CSOs but they promote products from different pharma companies. Three to four detail positions are generally offered. Some CSOs rotate the presentation order every week or month. This is important because the detailing time is limited to an average 10-12 minutes per call, so products in third and fourth position receive little time, if any. In general, syndicated teams promote products from non-competing therapeutic areas.

Syndicated teams are also used for product launches or to resist a new competitor, and are particularly suited to seasonal products such as anti-infectives. Contracts are usually signed on a four-month renewable basis and 72 representatives make up a standard team. The average price per call is around €11.43, plus possible incentives for good performance. The figure is necessarily averaged for all products because so many teams rotate their detailing positions.

In a dedicated team, representatives are recruited in accordance with the pharma company's specifications. In both cases, the pharma company, via either a trainer or product manager, ensures product training. Sales techniques training is covered by CSOs.

Recruitment activities are another important part of CSO business. CSOs recruit not only for themselves but also for pharma. Innovex, for example, has a database containing the résumés of 7,000 medical representatives. In 2000, MBO led the market with a turnover of €0.9 million,

	Contract sales forces headcount: Syndicated	Dedicated	Total	Recruitment	Marketing consulting	Product nursing	Other services
Cider Santé	420	720	1,140	+	+	Fornet	Clinical services 30 pharmacy reps
MBO	250[1]	600	850	+		Proxatis	
Repsco	240	290	530	+			
Ventiv Health	300	200	500	+	+	Socopharm	Clinical service
Innovex	140	360	500	+	+	Novex Pharma	Clinical services
GTF	197	215	412	+	+	Tonipharm	Business tourism 25 pharmacy reps
CL Innovation	144	260	404	+			
Arvem	320	40	360	+			
Promedis	265	70	335	+		Cypea	ETMS[2] services 20 pharmacy reps
Expand	204	96	300			Vigalis	
PMS	0	136	136	+	+		15 pharmacy reps
Total	2,480	2,987	5,467				

New entrant (since 1999)

[1]Part-time medical representatives corresponding to 140 full-time equivalents; [2]ETMS, electronic territory management systems

Figure 1: The size and services offered by leading CSOs in France. Source: Smart Pharma Consulting

having recruited 300 medical representatives for internal pharma sales forces. Some CSOs have partnerships with medical sales schools while others, like GTF, possess their own school. CSOs do not recruit from their own clients, but they do from competitors and non-client companies. And their methods are rapid and effective, enabling them to build up a team of 80-100 representatives in less than two or three months.

Dynamic marketplace

The French contract sales forces market has undergone profound restructuring over the past three years as international players have taken over domestic companies. In 1998, the US contract research organisation, Quintiles, through its CSO arm Innovex, acquired two privately owned French firms, the CSO, T2A, and the recruitment agency Serval. The same year, Snyder Healthcare, also of the US and which became Ventiv Health in 1999, acquired the French recruitment and CSO agencies, CLI Pharma and Publimed. Meanwhile, that year, the UK financial institution, Permira (formerly Shroder Ventures), took over Expand, a pioneer in the French CSO market which, after 30 years leading the field, had to face up to the fallout from risky investments and management errors.

Although the entry of both Innovex and Ventiv Health onto the French CSO market has brought these companies new sources of sales growth, no other tangible advantages have been conferred. France, like all major national pharma markets, has its own set of drivers and regulations. These differences between markets make it difficult to share costs, competencies and clients. They also go some way to explaining why Innovex and Ventiv Health operate more like multinational than international organisations.

Despite these entrants to the French market, most indigenous CSOs are small, privately owned companies with little or no overseas activities. The absence of high entry barriers has lead to the arrival of new local players like Promedis-Arvem, MBO and PMS in 1999, Repsco in 2000, and CL Innovation and VMP in 2001. However, the market remains concentrated with the top ten CSOs accounting for 90% of total sales in value terms and competition is intense, leading to pressure on pricing.

Challenges

Competition on price has recently increased for several reasons. One is that companies such as GlaxoSmithKline, Bristol-Myers Squibb and Sanofi-Synthélabo have put in place purchasing departments which organise invitations to tender and negotiate price discounts with their suppliers, including CSOs.

The arrival of newcomers such as MBO, or spin-offs like Promedis, Arvem or Repsco, has also spurred competition. In just three years, MBO has become the second largest CSO in France with 850 medical representatives and its turnover was expected to reach €36 million last year. Other new companies, CL Innovation and VMP, were founded and are managed by the former owners of CLI and T2A respectively. They can therefore capitalise on both their knowledge of the CSO business and their strong links with the pharma industry.

CSOs operate in a fixed-costs business with operating margins estimated to be as low as 4-8%. Thus, any fluctuation in either sales force workload and/or average price levels has a strong impact on their bottom line. Nevertheless, some CSOs have been cutting prices drastically, sometimes to below €7-8 per call per product in their syndicated sales forces.

Against this background, medical representatives, especially those from CSOs, are finding it harder to call on targeted physicians. As many as 70% of France's 58,000 general practitioners now only accept visits once or twice a year through appointments. In an effort to circumvent these limits, pharma and dedicated CSO representatives make follow-up calls after medical meetings or clinical studies in which they have involved physicians. Syndicated sales forces are seriously threatened by these limitations because they cannot benefit from these extra calls and because their fees are dependent on the number of calls made during the contact period.

Competition is not only increasing among CSOs, their clients may also become competitors

Competition is not only increasing among CSOs, their clients may also become competitors. Some pharma companies have started outsourcing the promotion of their products to other pharma sales forces. When Novo Nordisk launched its first oral anti-diabetic Novonorm in 2000, for example, it signed a three-year deal with Roche rather than a CSO. Novo Nordisk selected Roche because of its experience of the metabolic diseases market, where its anti-obesity drug Xenical operates.

CSOs may also find their best representatives are poached by their clients internal sales teams. In 2001, Merck & Co took over two dedicated sales forces from its historical partner, Cider Santé. This integration represents a theoretical 15% loss of profits for the company which, with 1,140 representatives, is also France's largest CSO.

Increasingly, pharma companies are avoiding putting all their outsourced products with the same CSO. Although the contract sales market has grown at an average rate of 10-12% over the past three years, established players have not necessarily benefited. Financial difficulties, unstable management and recent merger and acquisition activity among CSOs have lead pharma companies to spread their risks. Thus, all the top 20 pharma groups work with more than one CSO.

However, CSOs still have an important role as they employ 20% of the 25,000 medical representatives visiting physicians. Against all the odds, the recent pharma mergers and acquisitions have not reduced demand for their services. On the contrary, the uncertainty about the size of sales forces required during the transition phase has driven their use.

For smaller pharma companies that cannot afford an in-house sales team, CSOs are a valuable option especially if they are dependent on narrow or single product lines. CSOs give companies a flexibility that translates into significant savings. Pharma companies can save 30% and 20% on a full cost basis, depending on whether a syndicated or a dedicated team promotes their product.

Companies' attitudes towards CSOs are beginning to change. For many years CSOs were regarded as armies of low quality medical representatives. Some pharma companies now regard them as long-term partners. For example, Cider Santé has managed sales forces promoting Merck & Co products for more than 20 years. Such long-term relationships create effective exit barriers as a new team will take months, if not years, to develop the same credibility with physicians.

Survival strategies

To survive in the current environment, CSOs must consider three issues: their optimal size; how to protect margins; and whether they should diversify.

Size does not seem to affect the likelihood of success. In 1999, market leader Cider Santé lost €0.3 million (US$0.26 million), but the following year it achieved a profit of €0.4 million – just 0.5% of its sales. Expand, meanwhile, downsized its

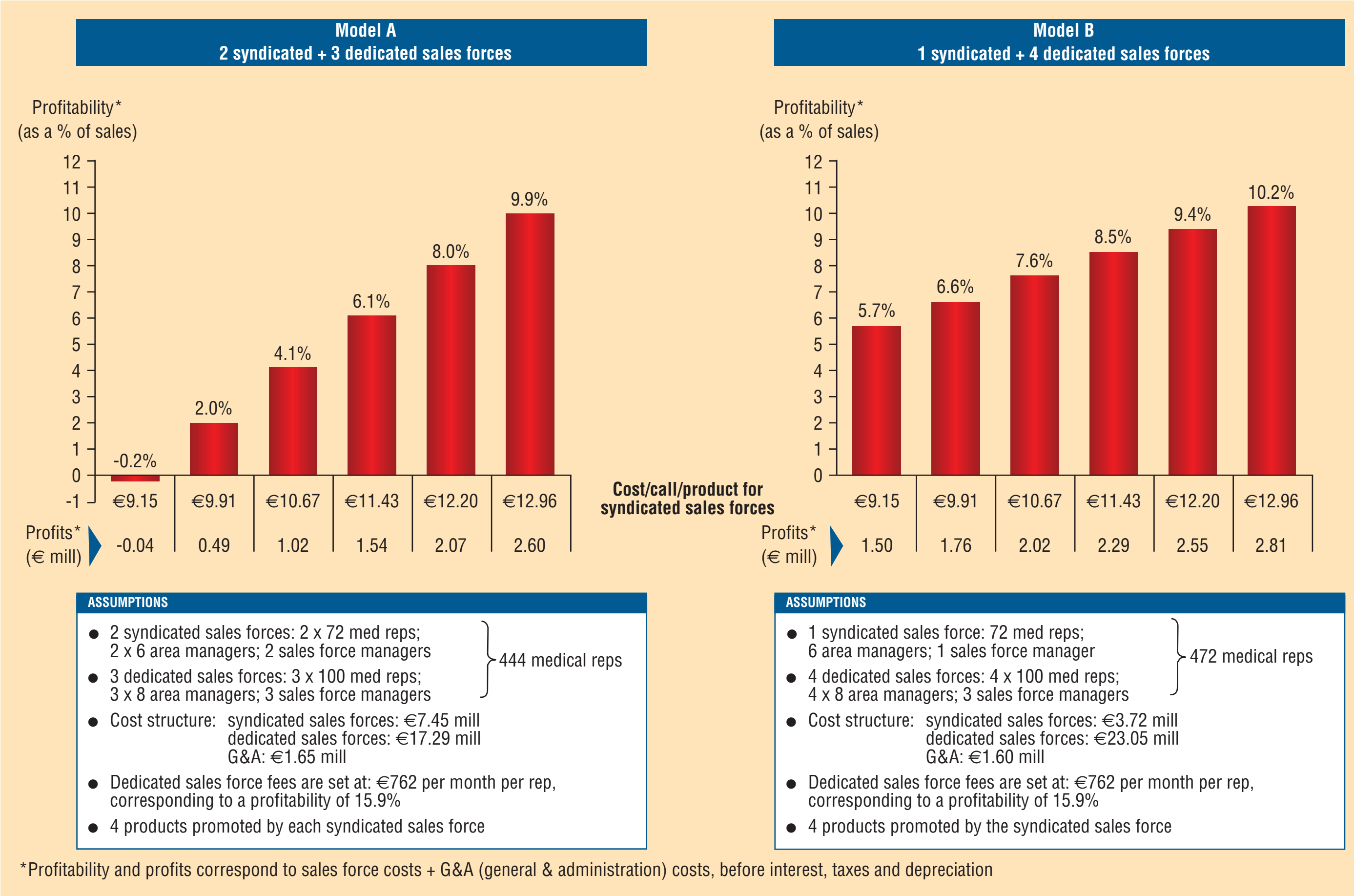

Figure 2: Two profit models illustrating the current structures of several leading CSOs in France.
Source: Smart Pharma Consulting

sales forces from 1,300 representatives in 1999 to 600 in 2000 to reduce its €6.1 million loss. Both companies were strongly hit by price competition and the difficulties of keeping their syndicated sales forces busy with four products.

The best compromise between size and risk containment is probably obtained with forces of 300-400 representatives. Beyond this, economies of scale slow down significantly while the difficulties of keeping the sales forces fully occupied accelerate. This optimum size corresponds to five or six sales forces, each having to promote three to four products, meaning that 15-24 products should be under contract with pharma companies. Ideally, there should only be two syndicated sales forces, the remaining teams should be dedicated.

To maintain healthy profit margins, CSOs need to control their expenses. Sales force costs – including salaries, cars, travel expenses and management – represent as much as 90% of total costs.

Detailed analysis shows that CSOs that have syndicated teams, where each representative promotes four products, start to make profits above fees of €11.6 per call per product. Where only three products are promoted, €15.5 per call per product needs to be charged to break even. However, no pharma company pays these prices. CSO profitability is therefore highly sensitive to the number of products promoted by its syndicated sales forces. For dedicated teams, CSOs can generate an average operating margin of 11% with fees of €762 per representative per month. The two profit models presented in Figure 2 are close to the current structures of several leading CSOs. The weight of syndicated personnel in the total sales force headcount plays an important role on the bottom line. Besides, as seen in these models, CSO margins are not only low, but highly vulnerable to price discounts. To survive in this competitive market, CSOs must fight to maintain reasonable prices.

To be in a position to do this, they have no choice but to improve the quality of their services. They must therefore invest heavily in staff development. Medical representatives need to manage their territory efficiently, know their products, including those of their competitors, and have good sales techniques. The top priority of area managers, meanwhile, should be to develop the competencies of their medical representatives. Dual call sessions are by far their best opportunity to coach their medical representatives. On average CSO area managers spend 55% of their working days in coaching sessions compared with 40% of pharma sales managers. This is because the latter spend more time in meetings, organising congresses and opinion leader management.

Since 1992, medical representatives have had to graduate from 600 hours of training in a registered school. In order to manage their territory better, they receive a database of information about their targeted physicians and sophisticated equipment to transfer activity reports. Few CSOs have equipped their staff with such systems because the costs are usually prohibitive. Nevertheless, market research into physicians' recollection of the promotion messages (recall-tests) has shown that it is not unusual for CSOs to obtain better recall test results than pharma teams promoting the same product.

In order to address quality, CSOs must invest not only in training but also in support tools to enable the representatives to do their jobs effectively. This is the strategic option adopted by Expand, which has equipped all its medical representatives with personal digital assistants (PDA) containing electronic territory management system (ETMS) functions.

To ensure good quality calls, CSOs must also set realistic call targets for their representatives. If medical representatives have to struggle to do six or seven calls a day, as is often the case, inevitably it will be at the expense of the quality of the contact. Representatives may be tempted to meet non-targeted physicians or keep visiting those physicians who do not limit their call frequency. Probably the best approach is to determine an adjusted objective of calls to be carried out per day for each medical representative. This specific objective could vary between 4.5 and 7.5 contacts a day on average, depending on the difficulties of making the call, the medical representative's experience and knowledge of the territory.

If CSOs put quality first, they will obtain better results and generate more business. They will also be in a position to increase their fees, which will directly improve their profitability. This virtuous circle will be completed by their ability to pay their sales representatives more, which will improve staff retention and attract the best candidates for vacancies. However, to initiate this virtuous circle, the CSOs will first need to invest heavily in quality programmes.

Diversification

Diversification has been seen by many CSOs as a way to protect themselves in this challenging market. Product nursing is one option that has become popular recently among leading CSOs. For instance, MBO manages a €40 million portfolio of mature products belonging to Bristol-Myers Squibb. The marketing and the promotion of these products are ensured by Proxatis, MBO's nursing product subsidiary. Bristol-Myers Squibb has preferred to outsource its promotion and to concentrate its internal resources on newer products with a greater potential for sales growth and cash contribution.

At first sight, product nursing agreements appear to be an attractive proposition for CSOs because they are signed for three- to five-year periods – much longer contracts than for dedicated or syndicated contracts sales teams. In practice, however, nursing agreements are not such a good deal. So far, these agreements have not brought CSOs the profits they were expecting. Three major reasons explain these disappointing results:

•Few mature products seem to respond well to promotion.

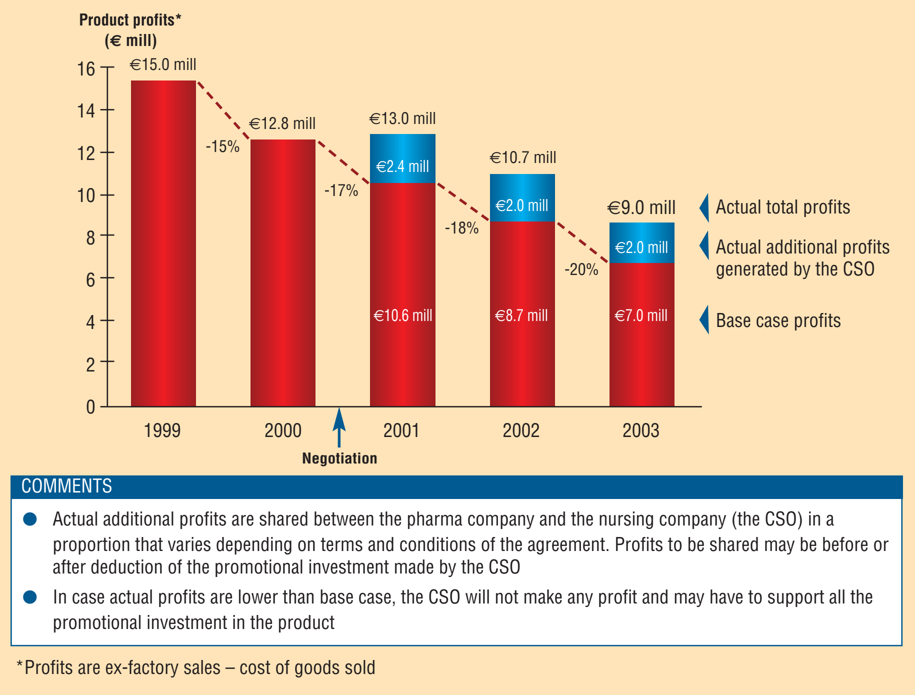

Figure 3: Financial model of a product nursing agreement.
Source: Smart Pharma Consulting

•It is extremely difficult to forecast the performance of mature products and CSOs have not paid enough attention to this when assessing a product's potential.

•The CSOs, in general, bear all the financial risks.

The last reason is because CSO profits come from the difference between the sales forecasted in the 'as is' or base case scenario and the nursing scenario as shown in Figure 3. Any profits are shared between the product owner and the CSOs in a 50/50 or 40/60 ratio. If the actual results are below the forecast, the CSOs bear all costs incurred.

Another diversification strategy taken by some CSOs has been to develop themselves as a 'one-stop shop'. This approach, adopted by Cider Santé, Innovex and Ventiv Health, which offer contract research, marketing, consulting and contract sales forces, also does not seem to work in practice. These three CSOs do not show the best financial results and most importantly, do not benefit from any sustainable competitive advantage resulting from their diversification. Clinical, marketing and sales services are separate businesses, with little or no synergies because the decision-makers are not the same; the competencies are different; and there is little or no possibility of making cost savings.

To survive in these challenging times, CSOs need to remain focused on contract sales forces activities, while reinforcing their presence in dedicated services at the expense of more risky and price-sensitive syndicated services.

Ideally, CSOs should cap their sales forces' headcount at 400 to 500 medical representatives, with one, or a maximum of two, syndicated sales forces. Another essential point is to follow a 'high quality-high price' strategy to try to protect their margins. They should avoid putting all their eggs in one basket. In other words, a wise objective would be not to have more than 20% or 30% of their business with the same pharma company. A CSO that is too dependent on one client is exposed to price pressure and is in a weaker position to negotiate. In addition, the loss of this predominant client would put the CSO at risk financially.

Product nursing is a risky option that should only be considered advisedly. Good product candidates, that are sensitive to promotion, are extremely rare. CSO demand for product nursing is so high that pharma companies can call all the shots. In the CSOs market, small is not only beautiful, small is also healthy. SM

Reference

1. J-M Peny et al. 'Cutting the cost of purchasing', *Scrip Magazine*, April, 1997.

•Jean-Michel Peny is president of the strategy and management consulting firm, Smart Pharma Consulting and a lecturer at the HEC and ESCP business schools in France.

