

OTC DRUGS BECOMING MORE LIKE CONSUMER GOODS

— BUSINESS OPPORTUNITIES EXTENDING TO OTHER INDUSTRY PLAYERS—

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Summary

- In many advanced countries, the lineup of OTC (over-the-counter) drugs available to consumers is expanding. Meanwhile, in emerging countries, the use of OTC drugs is increasing while related healthcare systems themselves are still being put in place, and as such, future market growth is expected.
- OTC drugs have strong brand loyalty, relative to general consumer goods. Going forward, however, it is also anticipated that retailers with strong sales capabilities will be able to strengthen the market presence of their private label products.
- Business opportunities are expanding for companies in other industries as well, such as for adding new marketing functions to leading brand OTC drugs, and operational development through the utilization of customer data obtained as a result of including OTC drugs as part of their own healthcare-related consumer goods and services.

REORGANIZATION IN THE PHARMACEUTICAL INDUSTRY

The pharmaceutical industry, which has a global market value of more than US\$1 trillion, is an industry comprised of ethical pharmaceuticals, which are prescribed by medical institutions and practitioners, and OTC drug products, which are general-purpose medications that do not require prescriptions. In the ethical pharmaceuticals business, large profits can be expected if a drug can be developed and brought to market successfully, but a long time is needed to recoup the investment. The advancement of medical technologies, such as in the areas of regenerative medicine and gene therapy, is leading to an increase in costs and time needed for research and development of new drugs. On the other hand, the OTC drug business is one where stable profits can be expected, although returns are not as lucrative as in the ethical pharmaceuticals. The ongoing industry reorganization involving major acquisitions in recent years has led to a tendency among pharmaceutical companies to separate these two business areas with different characteristics. As a result, pharmaceutical companies have divided into two camps, one specializing in ethical pharmaceuticals, including new drugs, and the other focusing on OTC drug products. There are also some integrated companies that maintain operations for both new drugs and OTC drugs, such as Johnson & Johnson and Sanofi. But most of the major pharmaceutical companies have carved out a position for themselves by focusing on either new drug development or OTC drugs, which are similar to consumer goods (Fig. 1).

Figure 1: Classification of Pharmaceuticals Companies by Strategy

	FOCUS ON R&D	INTEGRATED	FOCUS ON OTC MEDICINES
Company	Roche Pfizer Novartis Merck & Co. GlaxoSmithKline (GSK) Bristol-Myers Squibb	Johnson & Johnson Bayer Sanofi	GSK Consumer Healthcare Reckitt Benckiser (RB) P&G Taisho Pharmaceutical Perrigo
Strategic focus	Ethical Pharmaceuticals	Ethical & OTC Medicines	OTC Medicines, Supplements, etc.

Source: Compiled by MGSSI

For example, the UK pharmaceutical major GlaxoSmithKline (GSK) acquired a 36.5% equity stake in an OTC joint venture from Novartis in 2018 for US\$13 billion. Then at the end of the same year, GSK established a joint venture with Pfizer's consumer healthcare business (OTC drugs, vitamins, etc.) to spin off an OTC business, and announced that the name of the new company will be GSK Consumer Healthcare. As a result, the new company has become the largest OTC drug company with sales expected to exceed US\$10 billion (Fig. 2). Among Japanese companies, Taisho Pharmaceutical announced in December 2018 that it will acquire France's OTC drug manufacturer UPSA, owned by the US pharmaceutical company Bristol-Myers Squibb, for US\$1.6 billion. Some industry watchers even speculate that Takeda Pharmaceutical, which transformed itself into a global, R&D-driven pharmaceuticals company with its acquisition of Irish drug giant Shire Plc. in 2018, may part with its OTC drug business, including such brands as Alinamin.

Figure 2: Majors in Global OTC Drug Market

Country	Company	Retail sales (2017) (US\$1 million)	
			Share (%)
UK	GSK Consumer Healthcare	11,590	10.6 Note 1
US	Johnson & Johnson	8,082	7.4
Germany	Bayer	5,943	5.4
France	Sanofi	5,500	5.0
Germany	Reckitt Benckiser (RB)	3,542	3.2
US	P&G	3,180	2.9 Note 2
Japan	Taisho Pharmaceutical	1,668	1.5 Note 3
US	Mondelez International	1,590	1.5
US	Prestige Brands	945	0.9
Ireland	Perrigo	814	0.7

Note 1: Includes retail sales of OTC brands under GSK umbrella, and sales of OTC brands of Novartis and Pfizer

Note 2: Includes sales of Merck OTC brands

Note 3: Includes sales of Bristol-Myer Squibb OTC brands

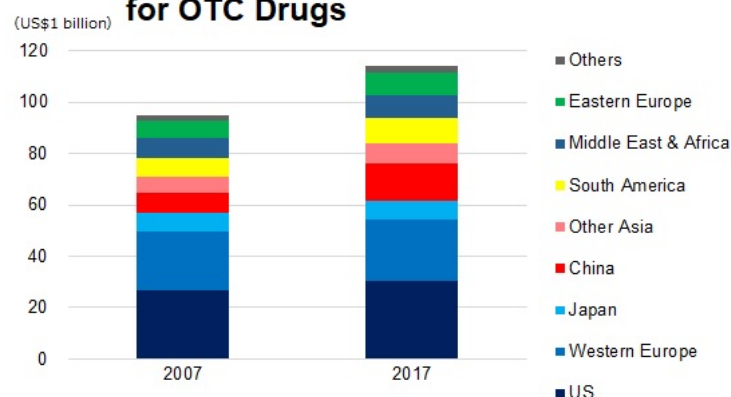
* Shaded areas indicate companies with operations centered on OTC drugs (consumer goods-type product lines).

Source: Compiled by MGSSI based on Euromonitor data, company announcements

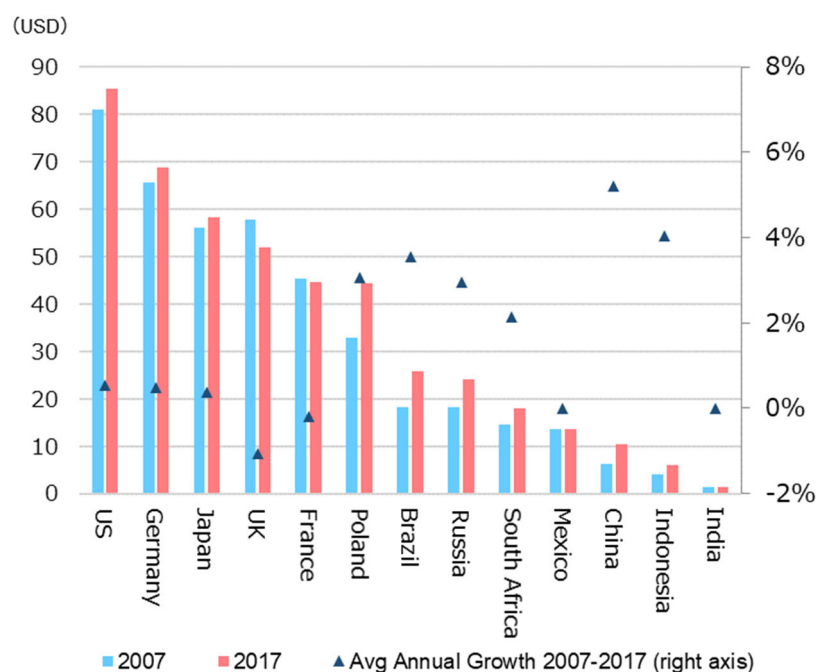
OTC DRUG MARKET OVERVIEW

The global OTC drug market ¹(retail sales) was worth US\$114 billion in 2017, and developed countries accounted for 57% of the total. By country, the US market is the largest, both in terms of overall size and on a per-capita spending basis (Figs. 3, 4).

¹ Figures in this report related to OTC drug market values, sales percentage by brand, and online pharmacy sales as a percentage of total sales are based on Euromonitor data.

Figure 3: Global Retail Market for OTC Drugs

Note: Based on inflation-adjusted real values
 Source: Compiled by MGSSI based on Euromonitor data

Figure 4: Per Capita Spending on OTC Drugs

Note: Based on inflation-adjusted real values
 Source: Compiled by MGSSI based on Euromonitor data

In the US, where there are many people who do not have medical insurance, it is customary for patients to purchase OTC drugs for mild symptoms from a nearby retailer without visiting a medical institution. In addition, many insurance policies available in the US provide some coverage for OTC drugs. Most recently in January 2019, medical insurance giant Anthem launched a partnership program with Walmart for policyholders of Medicare Advantage Plans, an insurance for elderly people, to give them better access to OTC drugs. The plan provides insurance coverage for OTC drugs purchased at Walmart by those senior consumers.

In addition, for medications that have been sold under prescription for many years, efficacy and safety are proven in the market. In many developed countries, with a trend of approval being given for those prescription medications to be sold as OTC drugs, the lineup of OTC drug products available to consumers is expanding. For example, in Japan, the antipyretic analgesic Loxonin S was approved for OTC sales in 2010; retail sales of the product reached ¥7.0 billion in 2017, more than double from ¥3.4 billion in 2011. Alesion, a treatment for allergic rhinitis, was approved for OTC sales in the same year, and retail sales climbed to ¥2.4 billion by 2017, from ¥200 million in 2011. Many of the products that have been switched to OTC status are for acute but mild illnesses, such as the common cold or hay fever, but since 2013, medications for treating lifestyle diseases

have been appearing on the OTC retail market. One such product is Epadal T, a treatment for improving slightly higher-than-normal triglyceride levels. The self-medication taxation system was also established in 2017, allowing individuals who undergo regular health checkups to take income tax deductions for annual purchases of ¥12,000 or more of medications switched to OTC. This deduction applies even if the amount is less than ¥100,000, which had been the standard eligible for the application for deductions. The new system is thus seen as an effort on the part of the government to encourage individuals to manage their own health.

The market for OTC drugs in emerging economies is growing, with the market in China alone having doubled over the past 10 years, and a look at per-capita spending on OTC drugs also shows sharp growth in many countries (Fig. 4). The emerging economies are still in the process of establishing effective drug-related systems, and the use of OTC drugs is incorporated into this process development and expanding at the same time. Going forward, increasing income levels will likely give rise to greater health awareness, but medical institutions and services are still lacking. As such, further expansion of the OTC drug market is anticipated.

STRONG BRAND LOYALTY AND PRIVATE LABEL DEVELOPMENT TRENDS

OTC drugs are basically similar in nature to daily consumables, such as food and cosmetics products, in a sense that consumers select what they want and purchase the products at retail stores or through online shops. For this reason, in the OTC drugs business, in addition to the core requirements of drug efficacy, safety, and reliability, a product's brand value and retailer's sales capabilities are also important.

Looking at OTC drugs by brand, the top brands in terms of sales vary depending on the country, and there are many local brands offered by global companies and many local brands offered by local companies. But the most common aspect of these products is that long-standing brands have strong brand loyalty. Of the top 10 brands in the global market for OTC drugs, despite some changes in company ownership of the brands in the past 10 years, there has been little in the way of brand replacement (Fig. 5). The brand with the highest sales in the global OTC drug market is Vicks, which has a history of over 100 years. Since 1985, the brand has been sold under the umbrella of consumer products giant Proctor & Gamble (P&G). Also, Bayer Aspirin, which has a history of 120 years since its market appearance in 1899, still retains strong brand recognition, although its ranking in terms of sales has slipped slightly in recent years.

Figure 5: Global Sales Ranking of OTC Drug Brands (2018)

Sales Ranking		Brand	Product Category	Company Listed underneath: previous owner of the brand (most recent)	Sales (US\$1 million)
2018	2009				
1	2	Vicks	Antitussive expectorant, Cold medicine	P&G Vicks Chemical Company (-1984)	1,742
2	3	Halls	Antitussive expectorant	Mondelez International Kraft Foods (-2011)	1,523
3	1	Tylenol	Antipyretic analgesic	Johnson & Johnson McNeil Laboratories (-1958)	1,361
4	4	Advil	Antipyretic analgesic	Pfizer	1,356
5	7	Panadol	Antipyretic analgesia	GlaxoSmithKline (GSK) Eastman Kodak (-1993)	1,091
6	6	Voltaren	Analgesic anti-inflammatory agent	GlaxoSmithKline (GSK) Novartis (-2014)	1,026
7	5	Bayer Aspirin	Antipyretic analgesic	Bayer	952
8	8	Mucinex	Antipyretic analgesic	Reckitt Benckiser (RB) Adams Respiratory Therapeutics (-2007)	782
9	10	Nicorette	Nicotine replacement therapy	Johnson & Johnson	735
10	8	Claritin	Allergic rhinitis treatment	Bayer Merck (-2013)	730

Source: Compiled by MGSSI based on Euromonitor, individual company data

Similar trends can be seen in each country. In Japan, for example, the No. 1 brand in the OTC market is Taisho Pharmaceutical's cough suppressant and expectorant Pabron, which was released in 1927. The No. 2 brand is Rohto Pharmaceutical's Rohto Eye Drops, first sold in 1909. For all of these brands, we can see that a long brand history has contributed to establishing credibility for each product and building brand strength.

At the same time, the branding power of retailers with strong sales capabilities should not be ignored. Brick-and-mortar pharmacies and drug stores serve as the mainstream OTC drug distribution channels. They provide information on drug efficacy and ingredients, which are particularly important for pharmaceutical products, along with safety and reliability information. They also develop private label.

In many countries, the percentage of private label sales out of total OTC drug sales has been gradually rising, with the percentage in the US increasing from 25.8% in 2009, to 30.7% in 2018, and in Japan from 1.4% to 4.8% over the same period. In the US, in addition to private label medicine sales by the two leading drugstore chains, Walgreens and CVS Health, such sales by retail giants Walmart, Costco, and others are also growing. For example, private label products accounted for 57% of smoking cessation patch sales in 2018, up from 47% in 2009, and for 29.6% of sleep aid medication sales, up from 18.6%. The market share of private label products is expanding in many fields, including nicotine replacement therapies (smoking cessation products), sleep aid medications, external injury treatments, and gastrointestinal medicine.

In Japan, drugstore chain operator Matsumoto Kiyoshi and others are making progress in the development of private label products. By product category, private label products are especially increasing in the field of treatments for external injuries, which is considered a category for which consumers are less hesitant about using those products; sales of private label products in this category has expanded from 8.6% of total sales in 2009, to reach 24.7% in 2018.

GROWING PRESENCE OF ONLINE SALES

As mentioned above, brick-and-mortar pharmacies and drug stores heavily dominate the OTC drug distribution channels, with online stores accounting for a mere 2% of OTC drug sales in the US and 2.6% in Japan, which is lower than the online sales ratios for general consumer goods. However, Amazon is not only expanding its lineup in the US by handling products from Costco's Kirkland Signature brand, it has also started developing and marketing its own exclusive brands of OTC drugs in late 2017. For its Basic Care brand, which consists of over 60 items such as mouthwash products and allergy relief medications, Amazon outsources manufacturing to Perrigo, a leading Irish pharmaceutical company that is aggressively acquiring OTC drug brands. Amazon has launched OTC drug labels one after another, such as SoundHealth (a brand for throat lozenges and other cough and sore throat remedies), Wellness Basics, and Primary Health. Looking ahead, it is conceivable that emerging players in this field, such as Amazon, may extend its power to compete head-to-head with existing brands, and at the same time, Internet sales of OTC drugs in the US will likely increase because of the advantages in convenience and price competitiveness.

Bayer is already rushing to strengthen digital marketing, as it attributes the slump in its OTC drug earnings performance in recent years, especially in the US, to the rise of the "Amazon Effect". In China, the company has entered into a strategic alliance with the Alibaba Group's Alibaba Health Information Technology,² and has begun to analyze consumption trends of medical and health related products in Chinese cities. Going forward, Bayer's strategy is aimed at strengthening sales of its own brand in China by leveraging Alibaba Health's online shopping service and providing information on self-care to stimulate related consumption.

² With a pharmaceutical information and data management company, CITIC 21CN Co., Ltd. under the umbrella of the state-owned CITIC Group Corp. as a predecessor company, the company was established by the Alibaba Group in 2014. It is engaged in pharmaceutical product information management, the development of tracking systems to prevent counterfeit product distribution, and the online retailing of OTC drug products, health foods, cosmetics, and other products.

In some cases, online sales for OTC drugs has become widespread due to the relaxation of relevant regulations. For instance, with Internet pharmacies gaining prominence in Germany, online sales as a percentage of total OTC drug sales in 2018 topped 17%, the highest in the world. This trend began around the year 2000 when online pharmacy venture DocMorris, headquartered in Heerlen, the Netherlands along the border of Germany, started offering online mail-order sales of pharmaceutical products to German residents at prices undercutting German market prices. At that time, online retailing of pharmaceutical products was prohibited in Germany, but in December 2003 the European Court of Justice ruled in favor of allowing cross-border online sales of OTC drugs.³ In response to this, Germany revised the German Pharmacies Act (Apothekengesetz) and drew up terms and conditions for granting authorization for the online sales of medicines. As a result, the number of brick-and-mortar pharmacies obtaining authorization for online mail-order sales has been increasing year by year, rising to nearly 3,000 in 2018.

At the same time as approving online drug retailing, Germany also enacted the Statutory Health Insurance Modernization Act (GMG) for the purpose of curbing medical expenses, and the range of drugs covered by insurance was reduced. As a result, medications prescribed for mild symptoms, such as for the common cold, as well as OTC drugs that had been covered by insurance in the past became exempt from insurance. This has spurred the online sales of OTC drug because, in addition to the low price of these products, purchases of these OTC drug can be made at any time without the constraints of business hours of actual stores. Driven by DocMorris, which was an early entrant to this market, online sales as a percentage of total OTC drug sales in Germany has expanded to around 17% at present, from 6.4% in 2008. In January 2019, the company forged an alliance with startup Cara Care, the developer of an app for individualized nutrition information, and launched new business for supplying OTC drug sales data to pharmaceutical companies. DocMorris is strengthening its market presence by offering services to both consumers and drug manufacturers.

Such dedicated online pharmacies could become a potent market player in the future, especially in emerging economies where actual pharmacies are not flourishing as businesses.

BUSINESS OPPORTUNITIES FOR COMPANIES IN OTHER INDUSTRIES

As examined so far, OTC drugs have the characteristics of daily consumables, and demand for such medicines is stable. In addition, although OTC drugs are characterized by strong brand loyalty compared to general consumer goods, retailers with powerful sales capabilities are expected to strengthen the market presence of their private labels in the future. Companies in other industries will likely discover new business opportunities in the unique characteristics of OTC drugs and trends in the industry.

One such possibility is that companies with solid sales capabilities and expertise could play a part in expanding the sales channels of OTC drugs that have strong brand recognition. With the influence of online pharmacies spreading, even the majors behind leading brands are rushing to strengthen their sales capabilities. For example, they can expand the sales of their top brands by providing new sales channels, such as general merchandisers, restaurants, and fitness clubs for potential new development in other countries.

On the other hand, health care-related consumer goods and service companies, such as those that offer health and wellness food, health-related equipment and information services, could also enhance their ability to attract customers, by including OTC drugs in their service offerings. Such a scenario might then motivate companies with strong brand recognition in other industries to sell their own private label products, outsourcing manufacturing of the products to OTC drug makers or OEM companies that lack brand power.

³ The Federal Union of German Associations of Pharmacists filed a lawsuit in the District Court of Frankfurt to stop the sale of pharmaceuticals over the Internet. As the lawsuit called for a judgment on whether the German domestic legal system was compatible with EC laws regarding Internet sales of medicines across borders, the district court referred the case to the European Court of Justice.

In either case, customer data from the OTC drug purchases can be used to promote their own products and services. As OTC drugs include many products that are used for a certain period or regularly, companies can draw on usage data for specific medicines to promote sales of a wide range of products and services related to healthy lifestyles, such as those having to do with nutrition, sleep, and exercise.

Meanwhile, as mentioned above, OTC drug-related reform and deregulation, including medical insurance and online retailing, carry the possibility of yielding new business opportunities. And, when engaging in the OTC drugs business, it is necessary to look at the systems, cultures, and practices of each country in detail. Changes are surely expected to take place in developed countries, but going forward, developments in the emerging economies that are in the process of building medical insurance systems also warrant attention. For example, in countries such as China, where the separation of dispensing and prescribing functions is not progressing, and most medicines are still prescribed through hospitals, the market for OTC drugs has considerable latent growth potential if policy measures are implemented to promote self-care solutions. Also, if systems for supporting online pharmacies are developed in emerging countries where online pharmacies are beginning to appear, it is expected that Internet retailing of OTC drugs to spread rapidly, as in the case of Germany. In these markets, companies in other industries also face prospects of enjoying the benefits of market growth, by partnering with leading local brands and emerging online pharmacy companies to develop business that combines healthcare-related products and services.