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ANALYZING BUSINESS MODEL, NARRATIVE AND NUMBERS OF GSK (GLAXOSMITHKLINE)

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Abstract

Global pharmaceutical companies face several challenges, most notably generic competition, patent expiration, regulatory issues and pressure from patients for delivering added value. This paper shall study the case of one of the leading global pharmaceutical companies, GSK (GlaxoSmithKline). New strategic priorities, including research and development (R&D) strategy set by the company shall be analyzed. The main research methodology used in the paper is quantitative. Research was conducted through content and case analysis, procedure created from materials collected via secondary research sources. The aim of the paper is to identify the key stakeholders in the pharmaceutical industry and to what extent their actions affect the firms' sustainable financial performance, correspondingly, to explore the new strategic priorities of GSK. The paper shall start with the review of pharmaceutical business, followed by the brief information about GSK. The business model and R&D activities shall be scrutinized. Policy implications and conclusions shall be provided. As the analysis reveal, in an ambiguous business environment, simplifying business model and diversifying activities empowers employees and facilitates decision-making process. For a global actor, it is essential to have a diversified range of portfolio and to evade reliance on a sole blockbuster. Remarkably, for the purpose of long-term sustainability and revenue generation, investing more in R&D is pivotal. In addition, focusing on specific scientific areas could be advantageous. Moreover, profound partnership with scientific institutions, business partners and academia could be beneficial for pharmaceutical companies.

Keywords: GSK (GlaxoSmithKline), Pharmaceutical Industry, Business Model, Financial Performance, Strategy

1. Introduction

GSK is a global company, spanning over 150 counties and employing approximately 100,000 peoples. This leading pharmaceutical company operates in three major directions: in pharmaceuticals, vaccines and consumer healthcare (Prange and Kattenbach, 2019). The company has a wide range of portfolio of innovative and established medicines. GSK focuses greatly on R&D activities, specifically within the areas of immune system, genetics and innovative technologies (GSK, 2020). GSK's strategy to "deliver more products of value" tended to be the response of the following obstacles: patent longevity and aging portfolio of drugs. For the purpose of minimizing the risk of dependency on a sole blockbuster, the focus was shifted

from producing individual blockbuster to generating large portfolio of medicines (GSK, 2009). For achieving this objective, the company had to invest more capital in R&D activities and to concentrate hugely on acquiring patents.

Within the history of past years, the major denouncing fact of pharma companies was their inability to reduce the prices on HIV drugs as millions of patients in Africa and Asia died because they could not afford disease medication. After this case, protection of patent, in order to maintain high prices, became even more crucial. Nevertheless, patents tend to endorse R&D activities and invention of new drugs to better meet customer expectations and to create value. The main reason why GSK hunted to evade the reliance on individual blockbuster was rooted in GSK's bygone challenges to recoup from financial slump after the expiration of patent life of the best-selling medicine Zantac. Even though R&D expenditure was increased, the company was unable to replace Zantac with new medicine that could recuperate lost revenues (Froud *et al.* 2006). As a response, R&D productivity was set as company's main and a potential source of competitive advantage. GSK implemented noteworthy changes in the development of R&D activities. The company focused their operations mainly on 8 therapy areas, created Drug Performance Units (DPU) within Centers of Excellence for Drug Discovery (CEDD) and a global Drug Discovery Investment Board. The company was also concentrating on the development of high variety of medicines portfolio and was working on improving its pipeline. The company got FDA approvals for cancer vaccine Cervarix, oncology drug Votrient and Arzerra for oncology and rheumatoid arthritis, as well as supplemental biologics license application (sBLA) for its influenza A (H1N1) pandemic vaccine, allowing the company to manufacture a flu vaccine for use in adults (GSK, 2020).

2. A diversified global market

Pharmaceutical industry, as being one of the utmost rising sectors across the world, is facing several challenges that call for companies to form the business model which entails cost-recovery strategy and capital-market understanding of those strategies (Froud *et al.* 2006). Mounting populations, increasing foreign direct investments and potential prosperous niches in emerging markets create vaster prospects for pharmaceutical companies to generate high revenues (Riley, 2008). The economy comprises with the interaction of individuals, organizations and governmental agencies (Rizhamadze, 2019). Separating patient from doctor, state and insurance firms, public and private sector customers become more insensitive to prices of prescription drugs. Passing the cost to the third party, funding body, usually state or insurance firms, has played huge role in shifting price sensitivity in a drug pricing system (Froud *et al.* 2006). Despite the price insensitiveness in recent years, major pharmaceutical companies have been accused of using the approach of 'Select only Best' establishing higher prices on drugs in developing countries, and giving rich people, who are able to pay western prices for medicines, opportunity to get the product while leaving poor out of condition to purchase. GSK's strategy to respond to the challenge of regulatory issue has been cutting the prices of medicines in developing countries. Moreover, GSK and other companies have been forced to reduce prices by health care systems in developing countries. In 2009, the Philippines imposed sharp reductions for all drug manufacturers, and Turkey was also poised to demand substantial cuts (Jack, 2013). For the purpose of boosting company's reputation, young CEO of GSK, Andrew Witty made a bold philanthropic move like donating one-fifths of all profits in poor countries for building healthcare system, pricing malaria vaccine at only 5% above the cost for lower-income countries (Weeden, 2011).

As some of the needs inside developing countries have not been fully exploited and satisfied, pharmaceutical companies seize every opportunity to boost their activities in emerging markets. GSK was no different, in particular, it shifted its direction to emerging countries, carving to reap the benefits of new-fangled markets and to increase annual sales growth. GSK selected a new market direction and picked BRIC countries- Brazil, Russia, India, China alongside Korea, Mexico and Turkey. Analyzing the revenues from these markets, Table 1 shows the growth potential.

Table 1. Pharmaceutical turnover by geographic area of GSK

Group turnover by geographic region	2018 GBP/m	2017 GBP/m	2016 GBP/m	2015 GBP/m	2014 GBP/m
USA	11,982	11,263	10,197	8,222	7,409
Europe	7,973	7,943	7,476	6,435	6,284
International	10,866	10,980	10,216	9,266	9,313
Total	30,281	10,186	27,889	23,923	23,006

Source: GSK (2018)

The figures show that diversification strategy of GSK turned out successful. By diversifying activities and operations in different markets, the company is likely to benefit from currency fluctuation as well (Jack, 2013). Apart from diversifying the business and concentrating on emerging markets, introducing the wide variety of products and acquiring off-patent brands from other pharmaceutical companies gave GSK possibility to compete effectively and efficiently for government purchase drug contracts. According to GSK's CEO, Andrew Witty: "We work like crazy to come up with the next great medicine, knowing that it is likely to get used an awful lot in developed countries, but we could do something for developing countries (Boseley, 2009).

3. A simplified operating model

The global recession and financial crisis has forced companies to discover some hidden complications behind the stable business environment. Because of complex operating models, some companies found it difficult to recover from crisis. This urgent situation called for companies to establish new operating model, or alter existing one, in a much more effective and efficient way. Pharmaceutical firms were redesigning business model for improving resource allocation and increasing the return on investment. Business model for pharmaceutical companies encompasses the simple outline of network structure and the creation of physician social networks (Ding *et al.* 2014). The model itself recaps the way organization functions and generates value for stakeholders. It assists the company implement testing and enables communication within people not involved in the development of core strategy (Lynch, 2018). For pharmaceutical companies, the list of shareholders is quite various and could evolve within the phases of development as illustrated in Table 2. For example, during R&D phase, the main shareholders tend to be the management of the company, opinion leaders like consultants and educators who share the information with the representatives of medical field. When moving to next step of clinical trials, the stakeholders are regulatory institution which gives permission to trials, research and development unit and marketing for the purpose of selling and spreading the information. On the last phase, during licenses, the main shareholders appear to be the healthcare providers like doctors, nurses and hospitals, patient and general public, insurance companies and other institutional bodies.

Table 2. Different stakeholders within the pharmaceutical environment

Phase: R&D	Phase: Clinical trial	Phase: Patent
Stakeholders: • Main Company • Key Opinion Leaders • Marketing	*Stakeholders:* • Regulatory Institutions • R&D • Marketing	*Stakeholders:* • Health Provider • General Public (Patient) • Insurance Companies • Governmental institutions

Source: Author's own preparation

Therefore, considering the complexity of shareholders, meeting their needs was a daunting task for GSK. New restructuring strategy pushed the company to reduce costs which in turn caused job losses in one market while creating jobs in other markets. According to company CEO, Andrew Witty, the new restructuring strategy caused 100,000 net job losses that were humble, especially 2,200 job losses from European and US sales staff that has been

balanced by identical hiring in developing countries (Jack, 2013). The restructuring had also an impact on earnings in 2009 when the restructuring began. Earnings per share dropped from 26.6P to 22.3P in 2009 in the 1st quarter. In overall, simplified operating model developed by GSK turned out to be effective and efficient. It gave freedom and autonomy to employees and empowered them in decision making process. The company has reorganized one single commercial support structure for Europe, Emerging Markets and Asia Pacific/Japan (GSK, 2008). In 2018, turnover was £30.8 billion. The US was the largest single commercial market, representing 39% of revenue, followed by International at 35% and Europe at 26% (GSK, 2018).

4. R&D activities

During the years 2008-2014, GSK concentrated on R&D activities inside the firm through discovery performance units and focused on developing a higher volume of mid-size products. GSK's internal research and development efforts acted as a basis for the discovering and distributing pharmaceuticals to the poorest countries. The company reformed the structure of R&D in the hope of developing novel vaccines, pharmaceuticals and healthcare products. Consequently, the emphasis was shifted to mergers and eight therapy areas were highlighted: biopharmaceuticals, immune-inflammation, infectious diseases, metabolic pathways, neuroscience, oncology, ophthalmology and respiratory (White and Bruton, 2011). From pipeline point of view, approvals of new vaccines and drugs reduced the risk of dependency on individual blockbuster. On 1st April 2013, The Association of the British Pharmaceutical Industry (ABPI) introduced the tax regime that allowed UK companies to pay a reduced rate of corporation tax on profits attributable to patents and certain other form of intellectual property known as The Patent box. The new initiative introduced by UK government, enabled UK to become the cradle of the latest generation of biological medicines. The idea of Patent Box was to encourage companies to locate the high-level value jobs and related activities within the development and exploitation of the patents in the UK (TSO, 2011).

Nevertheless, the trend is now shifting in the contradictory route with corporations breaking their R&D forces into smaller more autonomous groups outsourcing and thus trusting progressively biotech for innovation (Ellery and Hansen, 2012). The efficiency of R&D is when there is the efficiency balance with the input in R&D and the output (Gassmann *et al.* 2018). In 2014, GSK announced restructuring of R&D efforts thus eliminating 900 US employees, mostly laid off and staff reallocation would take place within the firm's Research Triangle Park in North Carolina (Vence, 2014). Also, it is country specific to keep the balance of importing pharmaceuticals and local production, as sometimes importation may be more effective financially (Gleeson *et al.* 2019). In the creation of public policies, it is very important that short-term policy is coherent with long-term policy (Cergic, 2019).

Table 3. R&D expenditures of GSK in the years 2017-2018

	2018	**2017 (Revised)**		**Growth**
	GBP/m	GBP/m	GBP/%	CER%
Discovery	892	1,007	(11)	(10)
Development	1,332	1,423	(6)	(6)
Facilities and Central Support Functions	600	576	4	6
Total Pharmaceuticals	2,824	3,006	(6)	(5)
Vaccines R&D	673	621	8	8
Consumer Healthcare R&D	238	235	1	3
Items Reconciling Adjusted	3,735	3,862	(3)	(2)
R&D to Total R&D	158	614		
Research and Development	3,893	4,476	(13)	(12)

Source: GSK (2018)

As Table 3 illustrates, R&D expenditure in 2018 was lower than in 2017 by 12%. This was the result of restructuring costs primarily due to the withdraw of Tanzeum in 2017 and lower intangible impairments, as well as the outcome of R&D prioritization. This was partly offset by increased investment in Oncology and costs payable to a third party concerning the use of a Priority Review Voucher (GSK, 2018).

In 2018, GSK has identified prioritized areas for research and development for enriching the pipeline. It includes the immune system, human genetics and advanced technologies. The company is pursuing long-term priorities of innovation, performance and trust. Within R&D activities and in the purpose of advance scientific breakthrough and progress, the company is partnering with scientific institutions, business partners and academia (GSK, 2018). Firms in high-tech industries like pharmaceuticals are highly relied on a constant development of novel products. The faster its products become obsolete, the greater a firm's business risk is (Brigham and Houston, 2013). Without enhancing R&D productivity, the pharmaceutical companies will not be able to balance the loss generated due to patent expiration (Paul *et al.* 2010).

5. Conclusion and policy implications

In this fast altering world, where technological encounters are supreme and the political differences are austere, in a moment of chaos we have to deal effectively with global problems. In this uncertain pharmaceutical business environment, drug companies have to compete efficiently on producing generics and portfolio of medicines. The companies, particularly GSK, should be able to manage its pipelines and avoidance of relying on sole blockbuster in order to implement their strategies. To replace drugs that become off patent quickly by durable new patents, more expenditure should be incurred in R&D activities. Companies should also pay attention to new regulations and polices established by governments while developing their new pipelines. By analyzing the huge potential of emerging market, companies are likely to increase their sales revenue by diversifying their activities.

The greater challenge ahead for GSK rests to maintain balance between R&D and marketing, within research that is characterized by unpredictable timing, high expenses, and unpredictable results, and marketing characterized by predictable timing, and predictable results, as well as sustaining reputation and image for regulators, as they tend to be the one who determines possibility of making money within the industry, even though GSK's new strategy has been focusing on R&D activities, the one that emphasizes innovation and improved healthcare and welfare of patients. Nevertheless, the high expenditures on marketing are not generally visible to consumers because more focus on doctor, on prescriber and on informing. Detailing, as an attempt to educate doctors, physicians, tends to be one of the expensive marketing activities (Froud *et al.* 2006). In Addition, Brexit poses a big threat to pharmaceutical research and manufacturing in the UK. Despite the fact that the scale of the UK drugs industry is large, two-thirds of the medicines used in the UK are imported from the EU (Kollewe and Scruton, 2019). In response to this challenge, GSK has defined the approach to Brexit that is, arranging the retesting and certifying the medicines in Europe; updating packaging; securing additional warehousing and supporting employees in obtaining settled status or equivalent in both the UK and Europe (GSK, 2018).

Concluding, nowadays companies are confronting a variety of challenges in every aspect of its operations, be it production or service. Therefore, the ones that are successful in responding to rapid changes and evolving environments are the ones to reap the benefits associated with the change. Consequently, companies have to be diligent and proactive in initiating changes in different dimensions of business strategy, organizational structure, culture, human resource and technology. Change tends to be an enduring run-through of any prosperous business. For achieving success at all levels of organization, it is pivotal that it encompasses all levels equally, namely operational and strategic levels. In order to analyze and assess the strategy and its success, some other information should be exploited as well. We should go in profound explaining of company's resources and capabilities. In order to implement innovative strategy, analysts and consultants suggest that companies should participate hugely in creating more value for all shareholders. In order to accomplish it, sources of strategic

advantage, ways to master new mechanism and adapt to new approaches for developing strategy must be identified (Hagel and Brown, 2005). In overall, it is important to maintain and establish trust among shareholders and social responsibility among customers, and also, to ensure constant innovation and development thus creating both financial and nonfinancial value.

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