Early Warning System - Case 17

Pharmaceutical company

Final methodological assessment - prepared by the EWS secretariat with the approval of relevant EWS network members

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Background

The case concerns units of a multinational pharmaceutical group in four EU member states, A, B, C and D. It involves a restructuring of two subsidiaries in country A, which are part of a European storage and distribution centre for the group. They are owned by a holding company in country D.

The restructuring took place in late 2015. Before the restructuring, the pharmaceutical products handled by the country A units were owned by other companies of the group, located abroad. After the restructuring, the A companies show large purchases and sales of pharmaceutical products in their accounts. This had a big impact on the national accounts (NA) and balance of payments (BOP) in country A, with big increases in imports, exports, output and intermediate consumption, but little impact on value added. In 2018, the A units were reclassified to wholesale trade, and the recording as trade margin reduced the impact on output and intermediate consumption in NA.

In 2019, the NSI in country A was reconsidering the issue of economic ownership, based on additional information provided by the companies. If they were not seen as the economic owners of the products they handle, the imports and exports recorded in A's NA and BOP would go down. This raised the question of consistent recording with the other countries involved in the manufacturing and sales of the products.

Findings

Country A's NSI had discussions with the company about economic ownership. It was decided to follow the company's annual accounts and assume that, from December 2015 onwards, the units in A are the economic owners of the goods they handle.

In country B, the group has factories classified in NACE 21.20 *Manufacture of pharmaceutical preparations*. The statistics show large exports from the factories to the A companies both before and after 2015.

In country C, the group has factories in NACE 21 and trading companies in NACE 46 *Wholesale trade, except of motor vehicles and motorcycles*. Investigations by the NSI have shown that most of the exports and imports of goods to and from A are related to processing in the country C factories. In the NA revision in 2019, these flows were removed from NA and BOP, and were replaced by the export of processing services.

In country D, the group has a holding company in NACE 70 *Activities of head offices; management consultancy activities*, and a wholesale trading company in NACE 46. The production recorded in national accounts for these units is not in relation to industrial production nor to processing fees.

Agreed recording

Based on the available information, a common way of recording in national accounts and balance of payments has been agreed among the four countries. It refers to the situation from 2016 onwards:

- The units in country A are considered the economic owners of the pharmaceutical products they handle.
- Exports of pharmaceutical products from country B to A is recorded.
- The group's manufacturing units in country C perform processing services for company units in A, recorded as exports of services from C to A.
- Property income flows between country A and the holding company in D and are recorded (as before).