

Jefferies Healthcare Temperature Check



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Diagnostics

Biotechnology

Pharmaceutical Services

Medical Technology

Consumer Health

Pharmaceuticals

Healthcare Services

Healthcare IT

Genetics

This research was conducted by Jefferies in partnership with FTI Consulting's Strategy & Research team, and is based on feedback from around 500 senior healthcare professionals, investors and consultants globally. Investors included both institutional and private equity. Respondents came from all healthcare sub-sectors, including biopharma, pharmaceuticals, biotechnology, diagnostics, medical technology, healthcare services, pharmaceutical services, genetics, consumer health, animal health, and healthcare IT.

Jefferies, the world's only independent full-service global investment banking firm, has served companies and investors for over 55 years. Headquartered in New York, with offices in over 30 cities around the world, the firm provides clients with capital markets and financial advisory services, institutional brokerage and securities research, as well as wealth management. The firm provides research and execution services in equity, fixed income, and foreign exchange markets, as well as a full range of investment banking services including underwriting, mergers and acquisitions, restructuring and recapitalisation, and other advisory services, with all businesses operating in the Americas, Europe and Asia.

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Foreword

by Tommy Erdei, Joint Global Head and European Head of Healthcare Investment Banking



I am delighted to introduce the inaugural Jefferies Healthcare Temperature Check report. We have launched the report to coincide with our 9th Annual Global Healthcare Conference in London. This year we expect to welcome approximately 2,000 delegates from around the world to what is the premiere corporate and institutional healthcare conference in Europe. It is therefore a timely moment to take stock of the industry and the expectations and concerns for 2019.

This report is based on views and sentiment from nearly 500 senior leaders within the Healthcare sector, from major investors to CEOs, and we believe it to be the biggest survey of its type, giving us a compelling snapshot of the agenda for 2019.

It is encouraging to see how optimistic many are, particularly against a backdrop of heightened volatility across markets, with around 90% of investors expecting to increase or maintain their allocation to healthcare stocks and most seeing the sector as an out performer of the wider market.

This buoyancy also translates across to M&A – 80% of respondents anticipate transaction activity to be higher, or at the same level, next year on top of the already strong increase observed in 2018. Within this, corporates are viewed as the key driver of deal flow next year as they

look to deploy large cash balances and access the low cost of funding to consolidate market positions or access new geographies and capabilities. However, risks posed by political, policy, regulatory and pricing uncertainty are stark with over 80% of respondents viewing these as being the most critical risks facing the Healthcare sector. When it comes to Brexit, while 22% of respondents believe it will have a very negative impact on the Healthcare sector, a majority of 64% view the likely impact to be neutral to slightly negative.

This view might explain, to some extent, the stronger performance of the sector with the healthcare constituents of the FTSE 350 rising nearly 12% over the last 12 months compared to a -6% decline in the broader FTSE 350 index over the same period. Whether this means we will actually see meaningful changes is less clear. Despite the extensive

rhetoric coming from US policymakers, drug reform is not anticipated by the majority ahead of the next US Presidential Election. In particular, institutional investors appear to be assuming no change in the near term. Interestingly, few perceive lack of innovation as a significant risk. Whether this is complacency remains to be seen.

We are highly focused on the global Healthcare market and Jefferies has established itself as the pre-eminent advisor to Healthcare companies across the world. As part of the importance of our franchise we have invested heavily in both our London and NY conferences and now this annual Temperature Check and we hope our current and future clients find these investments useful and important in helping them achieve their strategic objectives. We look forward to continuing to make these investments to support our great clients.

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Key findings



Geographic

Striking divergence with over two thirds of institutional investors and corporates believing North America to hold the greatest value opportunity for Healthcare investment in 2019, while three quarters of private equity view Europe more favourably.



M&A Environment

The M&A market remains buoyant. Four in five expect M&A to be at the same level or higher. Corporate executives are the most deal focused, with almost half expecting to be doing more deals in 2019.



Capital Markets Environment

Over three quarters will increase their exposure to the healthcare sector, or keep it stable, in 2019. There are limited fears of an asset inflation bubble, with most institutional investors thinking the market has further to go. The expectation is that healthcare stocks will outperform the wider market.



Innovation

Innovation is low on the 2019 agenda. Only 7% see lack of innovation as a major risk. Targeted therapies and gene therapy are viewed as the principal areas in which innovation has the potential to make a real difference.



Politics

Political uncertainty is a major concern. Pressure from regulators and political uncertainty are identified by over 80% as the greatest risks for the sector in 2019.



Brexit

Less than 3% believe Brexit will be positive, with two thirds expecting a negative impact and almost a quarter expecting it will have a 'very negative' impact.



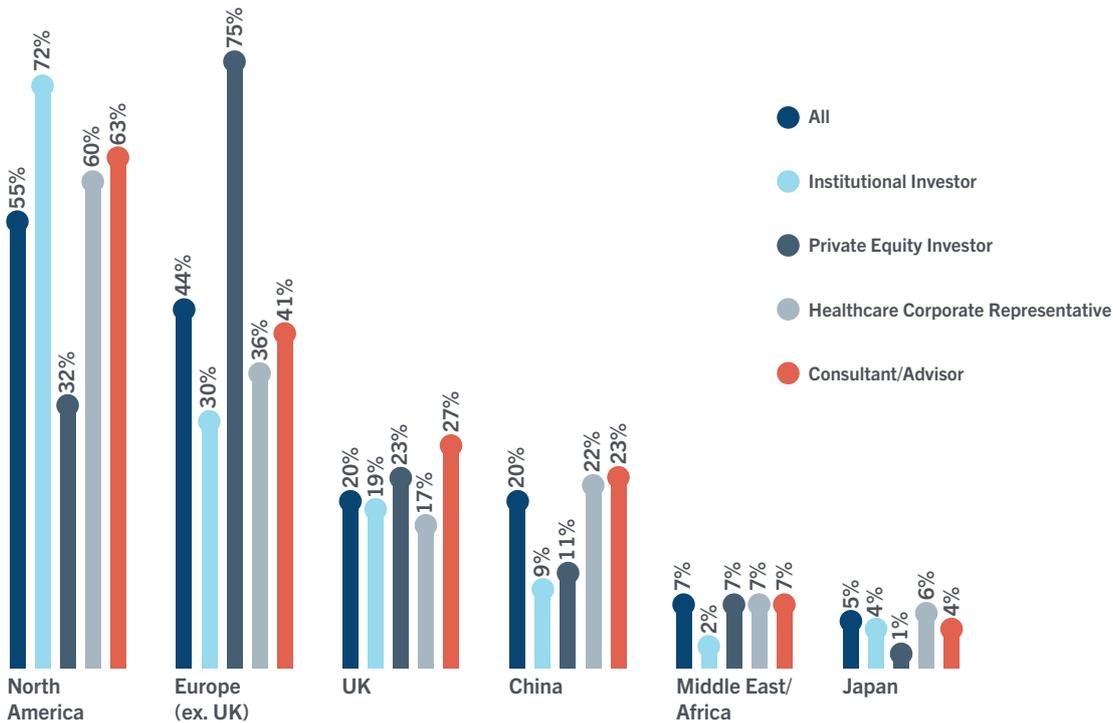
Drug Reform

Despite the rhetoric, investors do not believe there will be meaningful reform of US drug pricing before the US Presidential Election. Drug prices are expected to keep rising, but at a muted pace.

Finding value

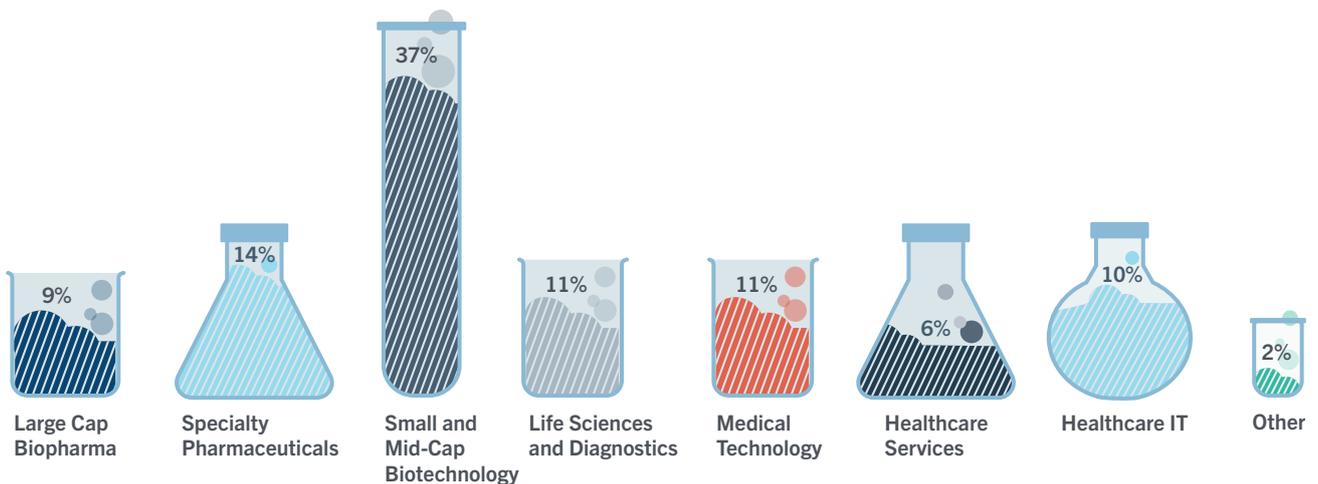
Identifying the geographic opportunities in Healthcare for 2019

We asked respondents to select all the regions in which they saw the most significant value opportunities for 2019. North America is believed to be the greatest value opportunity among institutional investors and corporates, but notably an overwhelming majority of private equity investors view Europe more favourably. The UK, China and rest of the World, in the eyes of the industry, represent fewer opportunities for 2019.



Which will be the best performers in next 12 months?

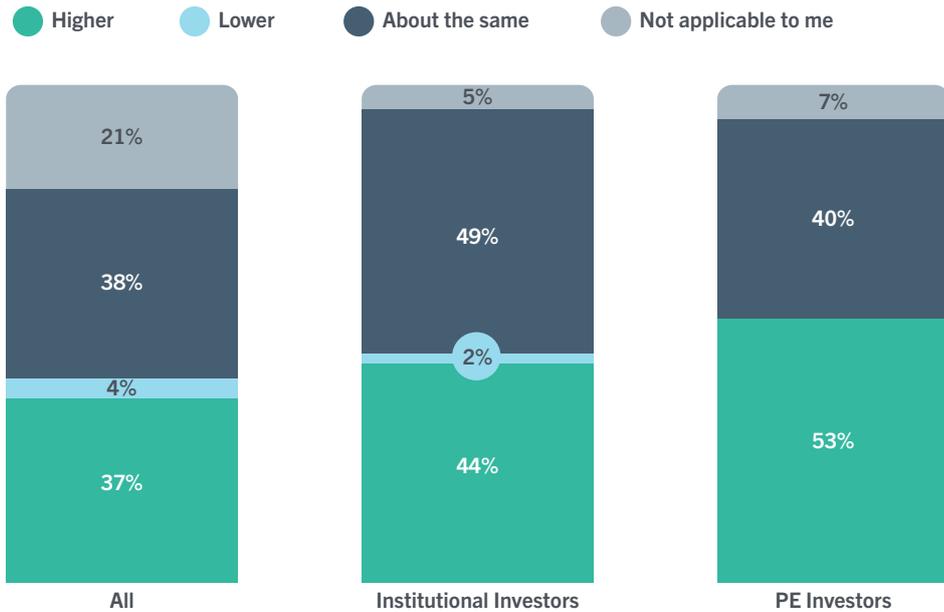
Looking to which sub-sectors are viewed as having the most upside over the course of 2019, small and mid-cap biotech is clearly viewed as having the most potential with over one third of respondents citing this as the likely best performer. There is a relatively evenly mixed view of which other sub-sectors offer value, although of note is the limited appetite for healthcare services or large-cap biopharmaceuticals.



More bulls than bears

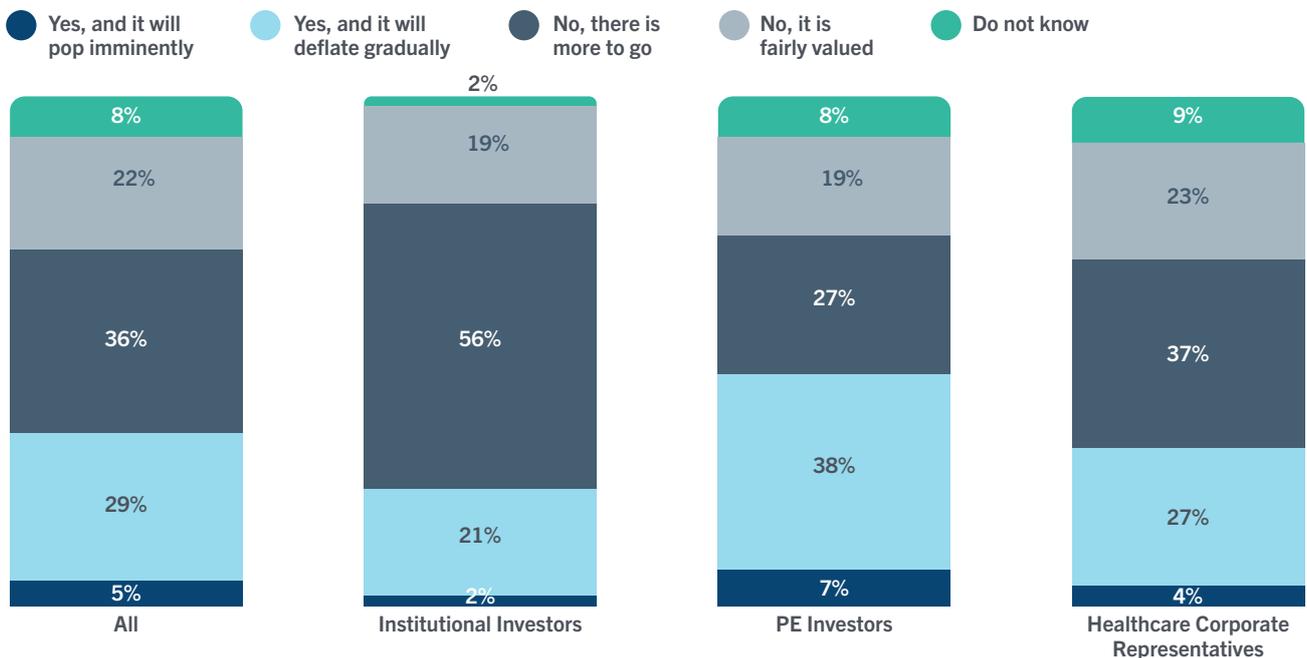
Healthcare sector exposures in 2019

Investors appear positive on the outlook for the sector, based on expected exposures for 2019. 93% of both institutional investors and private equity investors expect to increase exposure or keep it at the same level. The volatility and re-ratings observed across markets in recent months have accentuated the attractive balance of defensive characteristics and growth opportunities offered by the Healthcare sector.



Asset pricing in Healthcare

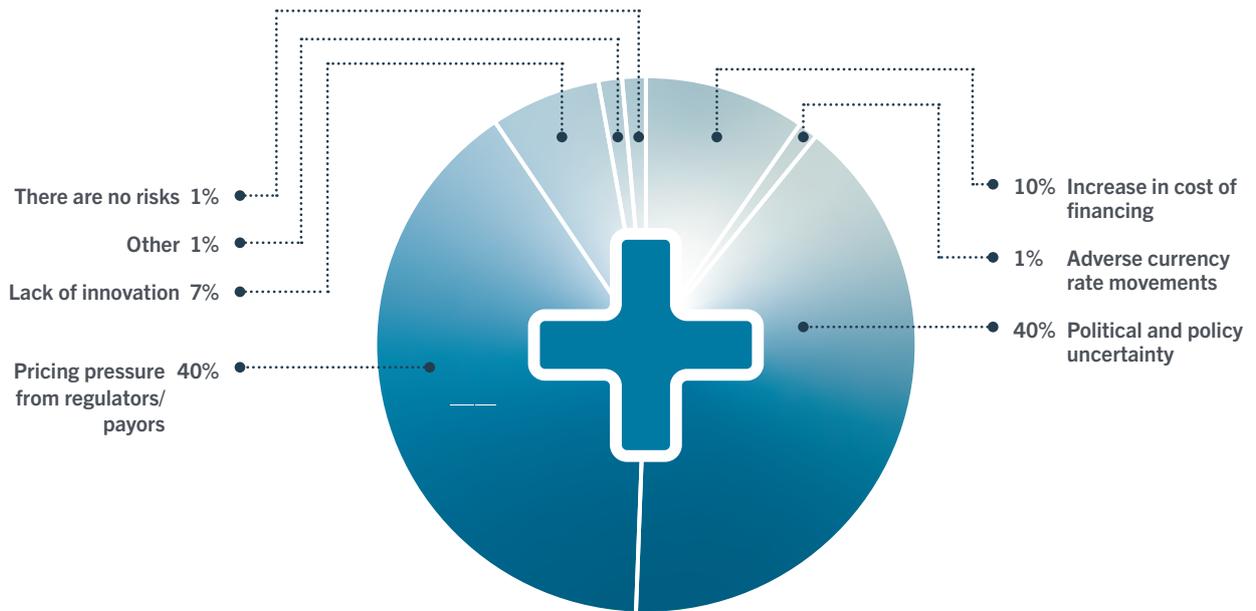
Expectations of increased exposure are reflected in views on valuation. 75% of institutional investors believe it is fairly valued, with over half believing there is more to go, and these views are relatively consistent with those from the company side. Private equity investors, however, are more cautious with nearly 45% believing there to be an asset inflation bubble.



Where are the risks?

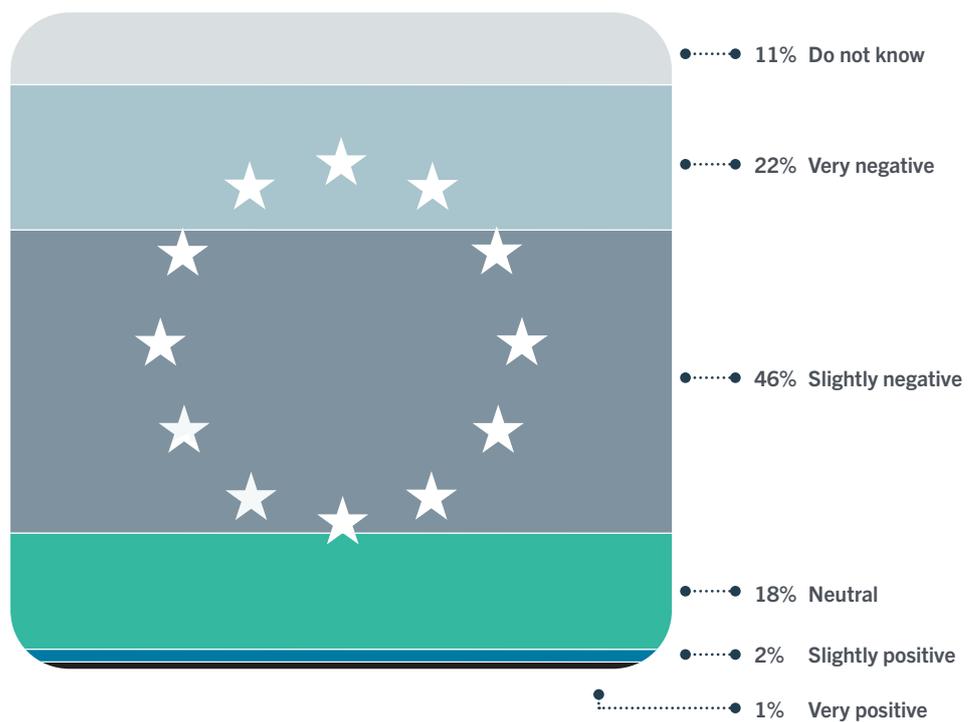
The greatest risk to Healthcare sector in 2019

Regulatory and political pressure is seen as the predominant risk for the sector in 2019. The threat is evenly split across pricing pressure and political uncertainty with 80% identifying these as the key risks.



Impact of Brexit on Healthcare sector in 2019

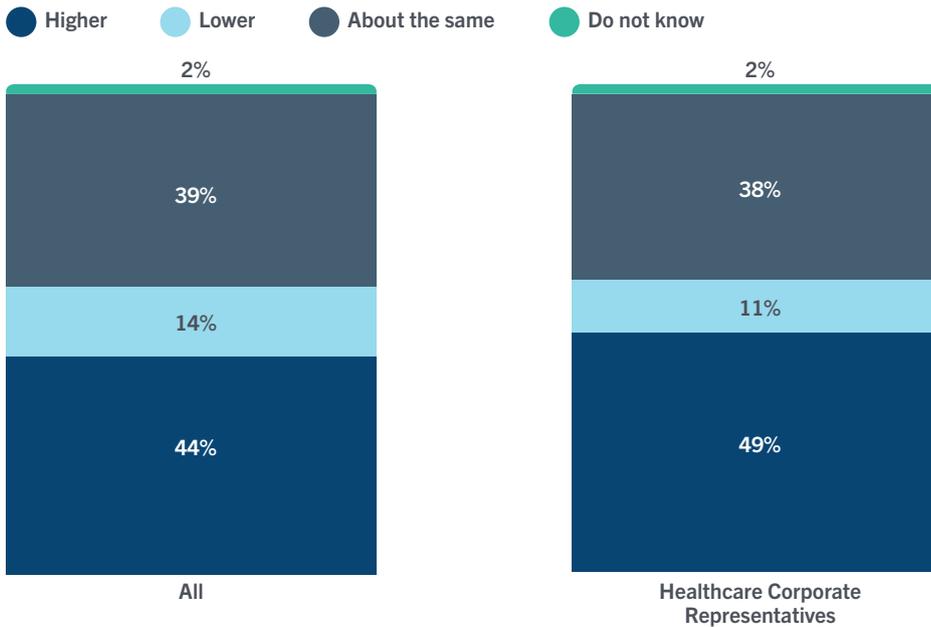
Brexit dominates the news agenda and the view from those operating in the Healthcare industry is clear. 22% believe Brexit will have a very negative impact. Fewer than 3% believe the impact will be positive. A majority, at 64%, believe it will be slightly negative or neutral, suggesting the impact may not be as bad as feared on the Healthcare sector. Views on Brexit are fairly consistent across respondents.



More Healthcare deals and transactions in 2019

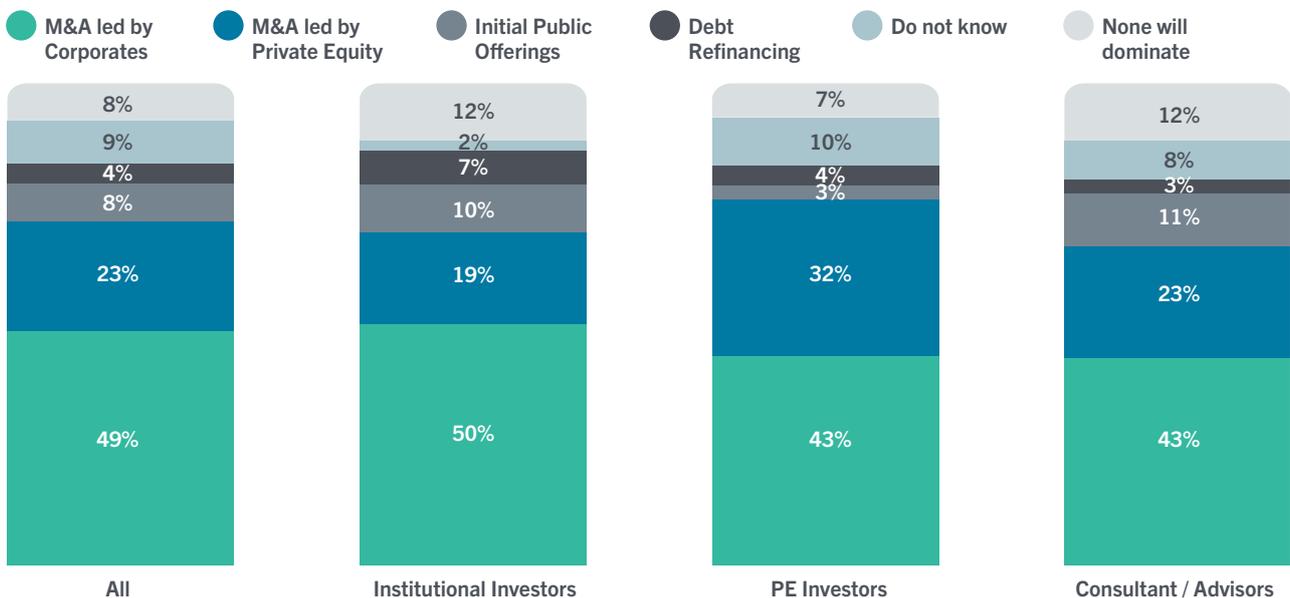
Level of M&A activity in 2019

The sector has seen significant M&A activity in 2018, and this trend is expected to continue. Over 80% of all respondents expect it to be the same level or higher in 2019 - with more predicting activity will increase. Healthcare corporate representatives are particularly bullish with nearly 50% anticipating a rise in M&A activity.



Areas of transaction activity

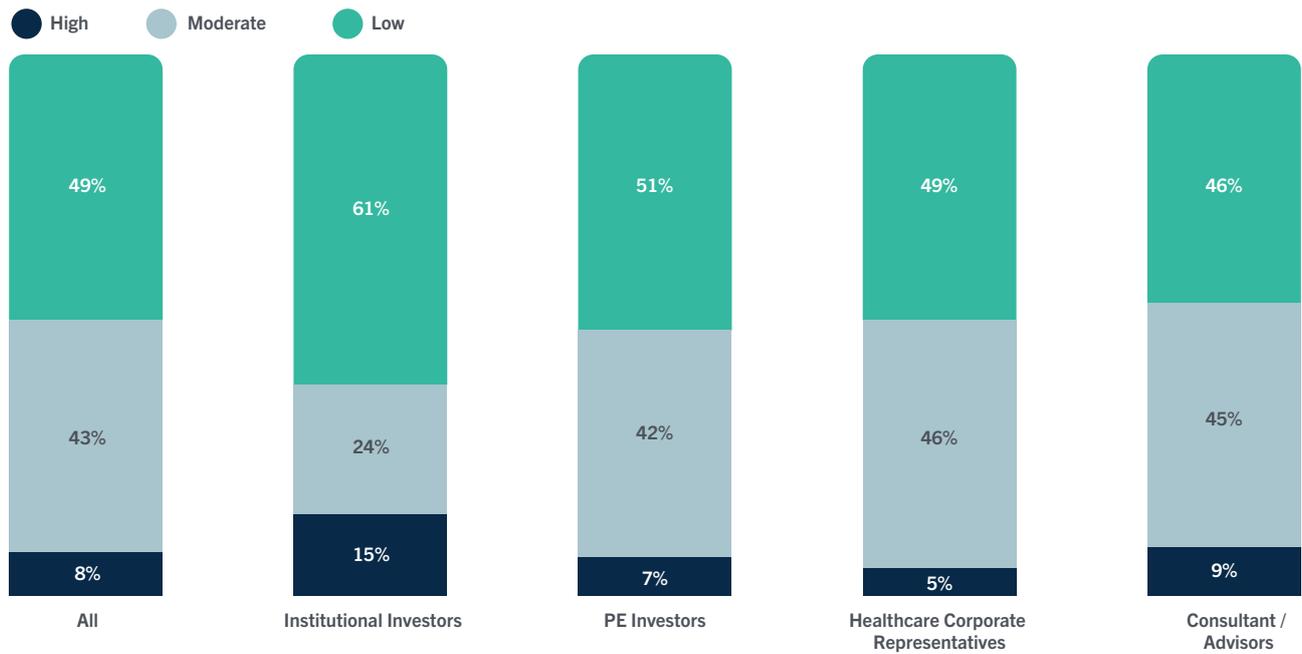
In terms of the key areas of transaction activity, responses suggest that consolidation will be a core driver. It is expected that corporates will be the most active instigators of M&A. In addition, private equity is also seen as a key source of deal flow. IPOs are not anticipated to be a major part of the landscape next year, in comparison to M&A.



What will happen to pricing?

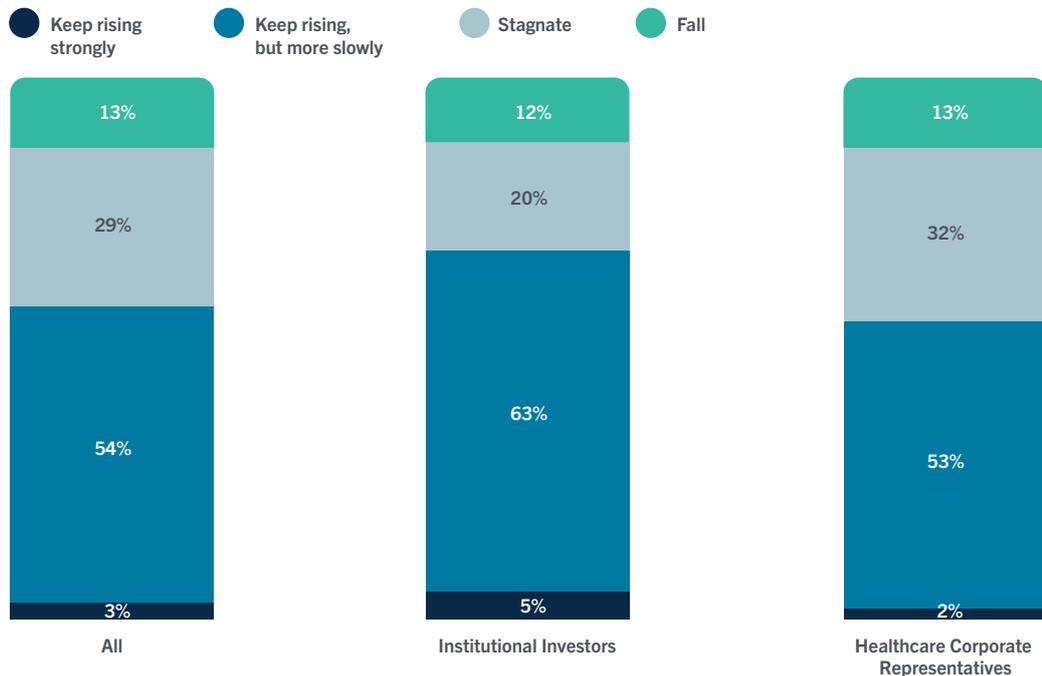
Expectation of reform to US drug pricing before next US Presidential Election

The industry is not overly concerned about the probability of reform in US drug pricing before the next Presidential Election, with 92% believing the likelihood to be moderate to low.



Views on drug pricing

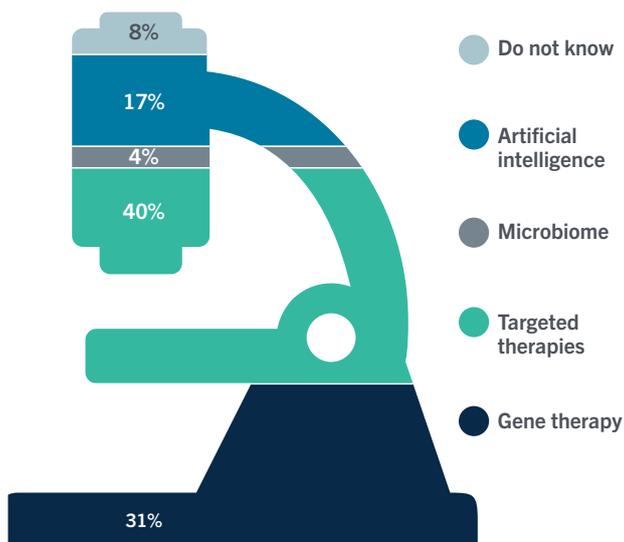
On drug pricing, significant increases are viewed as a thing of the past, with 54% expecting prices to rise only slowly, and 42% to stagnate or, in fact, fall. Notably, corporate executives are most pessimistic with 45% expecting price rises to cease, compared to 32% among institutional investors.



Where is the innovation?

Innovation within Biopharma

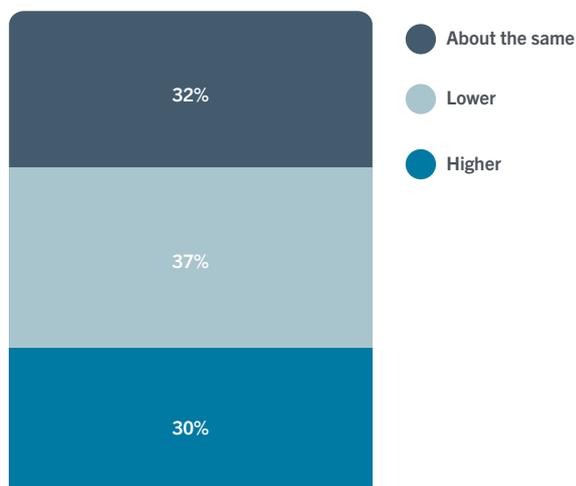
Targeted therapies and gene therapy are viewed as the principle areas in which innovation has the potential to make a real difference in 2019. While a much trumpeted theme, only 17% expect artificial intelligence to be the most important area of innovation next year.



Market outlook

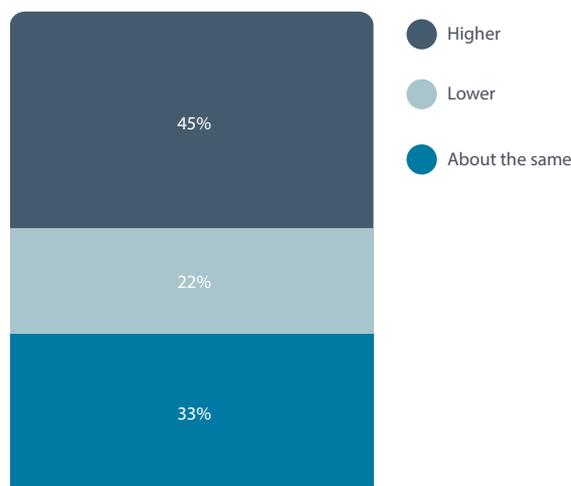
Expectations of FTSE 100 Index performance in 2019

There is no clear consensus from the industry as to the overall direction of the market in the next year, with responses balanced between up, down and flat. This is further evidence of the uncertainty surrounding political and policy developments and their impact on broader markets.



Expectations of MSCI World Health Care Index performance in 2019

In contrast to outlook for overall markets, there is more optimism around Healthcare specifically, with 78% of respondents expecting healthcare stocks to remain flat or increase in value. Only 22% anticipate a fall.



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