SPARK CAPITAL

INVESTMENT BANKING NEWSLETTER
HEALTHCARE AND LIFESCIENCES

FEBRUARY 2018

FROM THE DIRECTOR'S DESK

Dear Reader,

It gives me great pleasure to welcome you to the inaugural edition of the Healthcare & Lifesciences newsletter by Spark Capital.

Healthcare & Lifesciences has been one of the key focus sectors for us at Spark Capital. We have been fortunate to have worked with some of the most promising companies and capital providers over last few years coupled with our efforts to bring some of the new concepts/formats to the investing market. We thought it would be an exciting idea for us to pen down our views on deal making and trends shaping this space and share it with our clients and well-wishers on a bimonthly basis.

CY17 was an active year for us at the Healthcare & Lifesciences Investment Banking franchise. We helped Omni Hospitals raise structured debt and were instrumental in helping a South India based pharma company refinance their credit from a private sector bank. We helped arrange foreign debt for the Singapore subsidiary of a fast growing pharma company based in India. Through our equities platform, we helped facilitate block trades in the counters for Healthcare Global (HCG) and Narayana Hrudulaya (NH). All of this in addition to the several transactions that are at various stages of execution are a reflection of our belief in our full-service abilities to provide diverse solutions to our clientele suiting their requirements and life cycle of evolution.

Our understanding of the space coupled with our continued engagement with various stakeholders brings us to what we believe will be the big key trends that could play out over calendar 2018 and potentially next couple of years:

1. Regulatory activism in healthcare services/devices to stay – But should have limited impact on balance:

This topic dominated sound-bites through the last 12 months and also had its fair share of shadow on deal making – the views in the market ranged from 'it's all over for healthcare services in India' to 'we want to continue to invest but tread with little caution and with some margin of safety in entry multiples'. However, a fair share of smart money and strategic operators also believed this could be merely noise that you live with and may not have much impact. Given divergent views, perhaps it is most opportune that we decided to do a little deep dive on this burning topic, which we believe will figure in most domestic healthcare services/ devices deal discussions over next 12 months too. I hope you find the article titled *'Decoding The Regulatory Black Box – More Myths Than Facts'* included later in the newsletter, an interesting read.

2. Pace of deal-making a little slow but the interest remains robust – a 'new normal' emerging:

CY17 saw a marked slow-down in the broader Healthcare & Lifesciences deal making activity – both on strategics' and financial investors' side. Compared to 105 and 119 deals in CY15 and CY16, there were only 77 deals consummated in CY17. Even the cumulative value came down to USD 818 Mn in CY17 compared to USD 1,285 Mn and USD 1,240 Mn in CY15 and CY16. There were multiple factors at play in our view causing a 'mini-storm' of sorts. On the pharma side, US pricing pressure and FDA issues took focus away from acquisition lead growth initiatives, while on the healthcare and medical devices, there was an overhang of regulatory activism. One of the key trends we saw in the year 2017 was investors' relentless focus on execution ability as well as sustainable profitability/ unit economics of the businesses – a trend that we would continue to see sustaining itself in CY18. To be sure, the overall interest in the sector is quite robust as per our market read given compelling macro factors and significant dry powder earmarked for the sector. We think CY17 saw early signs of emergence of a 'new normal' in Healthcare & Lifesciences deal making and CY18 could reinforce it further.

3. IPOs solidly on the table as an exit/liquidity option – scaled-up players could benefit from scarcity premium and valuation arbitrage:

To use a cliché, capital markets have been in the pink of health, given strong macro tailwinds, improved liquidity and general rebound in listed equity markets globally. Interestingly, despite this being so, the Healthcare & Lifesciences index in India was a clear laggard in calendar 2017 (near flat return v/s 28% for benchmark index). This was largely on account of pharma sector headwinds and a combination of 'price and time correction' in some of the listed healthcare services stocks. That said, the valuation multiples for scaled up plays and first-time stories are still compelling and therefore we would continue to see many PE backed (and in some cases non-PE backed companies), explore public market listings as a serious option on the table for liquidity/exit. This could include players across the healthcare spectrum – viz domestic pharma companies, med equipment/ devices players and healthcare services/ delivery

FROM THE DIRECTOR’S DESK

providers. Our perspective is that while good valuation is a serious reason to list a company, one should also take into account other important factors such as the company’s preparedness, stage of evolution/institutionalisation and founders’ long-term game plan.

4. Domestic consolidation driven by scale and/or synergies would accelerate in 2018 across different segments:

On the domestic pharma side, this could be driven by portfolio gaps or succession issues coupled with good demand by suitors and attractive valuations especially for brands/divisions focusing on chronic therapy segments. For healthcare services segments such as diagnostics, single specialty and devices, PE backed consolidation primarily to scale up and ‘platformize’ their portfolio companies could be a major motivation. We could see some strategic interest in these segments as well to largely get the ‘alpha’ in the growth of their flagship companies as well as a way to get immediate market access in a new region. On the advanced diagnostic side, most of the pure-play companies are sub-scale leading to some consolidation (such as the recently announced Strand-HCG Triesta). The hospital players could also see consolidation, either on account of mid-cap or standalone asset chains being bolted-on by PE players (or for their portfolio companies) or by select strategic players. In our baseline scenario, over next couple of years, we think some such healthcare platforms could emerge in India.

In addition, we see several other smaller trends emerge and gain steam, namely:

a. Structured capital gaining in prominence as an alternative to equity deals in Healthcare & Lifesciences – driven by high liquidity in the structured capital segment, providing exit to investors in sub-segments faced with temporary headwinds as well as founders’ desire to defer dilution event to retain larger equity share of value creation;

b. Multi-specialty hospital chains expanding footprint while increasingly preferring asset light growth. This sector continues to attract meaningful international strategic interest and emergence of new suitors beyond the ‘usual suspects’;

c. Single asset hospitals finding it challenging to remain profitable and lending themselves to consolidation;

d. Rapid growth in online pharmacies and home health companies driven by increased awareness and adoption.

We are also quite positive on the ambitious National Health Protection Scheme recently announced in the Union Budget 2018. We believe the coverage of 500 million population and Rs. 5 lakh cover per family could be a game changer for healthcare services. However, the devil is in the detail and the key is to understand the implementation roadmap.

As part of this newsletter, we also wanted to bring in a direct perspective from leading industry operators in certain select segments. For this edition, we have picked diagnostics segment and accordingly have included interviews of a couple of leading companies in the segment in our ‘Expert Speak’ section. I would like to take this opportunity to wholeheartedly thank and express our gratitude to Dr. A Velumani, Founder, Chairman & Managing Director, Thyrocare Technologies and Dr. Sanjay Arora, Founder & Managing Director, Suburban Diagnostics, for being of great help and for providing their thoughts in the interview captured later in this newsletter.

Also covered in this edition are some of the latest developments in deal making. We are sure the section on “From our Equities Desk” would be an interesting read.

I am sure you would find this newsletter insightful and assure you of taking any feedback (including critique!) you may have on board for subsequent editions – planned once every two months. We hope you enjoy reading it as much as we did putting it together. ”

With best wishes,

Virendra Pandey

Director and Head – Healthcare & Lifesciences, Investment Banking

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FROM OUR EQUITIES DESK

Insights from Spark's Institutional Equities Desk

EXPERT SPEAK

Spark fact file

Investment Banking

USD 5.5 Bn
Total transaction value till date

USD 3.7 Bn
Capital raised till date

USD 1.8 Bn
M&A transaction value till date

300+
Number of fund relationships globally

USD 700 Mn
Average annual deal closure value for the last 3 years

11
No. of transactions > USD 100 Mn

~USD 1.2 Bn
Current value of transactions being executed

Healthcare & Lifesciences

~USD 450 Mn
Total transaction value till date

~USD 150 Mn
Current value of transactions being executed

BADSHAH OF B2B

INSIGHTS FROM AN INDUSTRY VETERAN

Thyrocare
Think Thyroid. Think Thyrocare.

We interacted with Dr. A. Velumani, Founder, Chairman & Managing Director of Thyrocare Technologies, on the company's disruptive journey in the B2B diagnostics market and various macro developments impacting the sector

Dr. A. Velumani
Founder, Chairman & Managing Director, Thyrocare

Thyrocare Technologies Limited is India's first and most advanced Totally Automated Laboratory having its strong presence in more than 2000 cities / towns in India and internationally. Thyrocare operates with a Centralized Processing Laboratory (CPL) in Mumbai – India for esoteric tests; and Regional Processing Laboratories in major metro cities of India and other parts of Asia.

1. One of the main questions that have perplexed investors over the past 12-15 months is how Thyrocare growing at a much faster clip than most of its peers. What would you attribute this to?

The single biggest factor, in my opinion, why we have grown consistently over the past several quarters is our pricing policy. We are the leaders in the diagnostic services market with a very tight pricing across our test menu which is evident from the difference in the prices between our facilities and that of the others in the organized market.

Having said that, it is interesting to note that despite lower realization per sample, our margins are higher than our peers and consistently so. The key here lies in the volumes. We are able to load our infrastructure with very high volumes owing to our pricing policy which then helps in better allocation of fixed costs and higher margins. In fact, when we started out with the lower price points, it was thought that it was an attempt to gain market share and that we will increase our prices in the medium to long term. Contrary to that, we have allowed our pricing to be more competitive compared to when we started and continue to enjoy the benefits of the pricing disruption which we created in the B2B market. Our business model has always been to have an optimum test menu size and a lean process, which is unique in its own way and very difficult for competition to replicate at the prices at which we work.

Another important factor is that our business model is inherently based on working with the local incumbents rather than having to grow by necessarily displacing them. And we have successfully demonstrated to them the win-win situation we can create by working together. Our quality and pricing ensures higher footfalls at their centres which helps their growth – and adds to our consistent growth profile as well.

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EXPERT SPEAK

Full Service, Mid-Market I-Bank

- Investment Banking (VC, PE, M&A, IPO, QIP, PIPE)
- Institutional Equities
- Fixed Income solutions
- Investment Advisory

Knowledge Banking

- Dedicated sector teams with deep domain expertise
- Ability to bring new ideas to the market
  - Vasan (2009)
  - Medall (2009)
  - Vaatsalya (2011)
  - Cloudnine (2013)
  - Apollo Health & Lifestyle (2015)

Relationship Banking

- Several clients for whom we have closed multiple transactions
- Consummated ~USD 300 Mn of transaction value in repeat business

Deep Distribution

- Extensive reach to over 300 funds across
  - Private Equity & Hedge Funds
  - Family Offices
  - Sovereign Funds
  - Corporates

2. If pricing is key to growth, what is stopping peers from engaging in price competition since none of them have followed in your footsteps on pricing as aggressively?

Unfortunately, the game is no longer just about pricing for a lot of peers now. The key to pricing tightly is also to be able to manage costs. If you look at some of the cost structures of competing firms, it does not allow for the kind of disruption we brought into the B2B market a decade ago. In fact, in my opinion, the B2B market is the most disrupted market – the B2C market yet to see a disruption anywhere close to what has already happened in the B2B market.

So even if competing firms were to compete with me on price, unless they rationalize their cost structures, such pricing cuts will only cause them to bleed on profits. Thyrocare's pricing is also a function of its volumes – it is not possible to sustain our pricing without our volumes and our volumes can come only from the kind of pricing we follow.

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3. Thyrocare's model of B2B diagnostics is at a stark contrast to the brand-based B2C model that most other chains in the market today seem to be employing. How important do you feel branding is in the diagnostic market in India?

A lot of efforts in the diagnostic industry has gone into creating and nurturing brands, some of which have been in existence for over two decades. And while branding is important, my belief is that India is a very price sensitive market and hence price continues to hold pole position for a large part of the population in deciding which service provider to choose. To draw an analogy, Jet Airways was the biggest and most powerful brand in Indian aviation before the advent of Indigo. And Indigo did to the aviation industry the exact same thing that Thyrocare did to the Indian diagnostic market – cut frills, manage costs and disrupt pricing. And today, Indigo's brand value is almost as good as that of Jet Airways, if not better.

There is no doubt in my mind that branding is an important factor and hence even we have invested heavily in brand building – especially for a company that largely derives its revenue from the B2B business model. However we are of the strong opinion that our branding and marketing spend indirectly helps our network partners grow their recall value in their home markets thereby bringing higher business for them and hence for us.

But from a pure B2C perspective, in my opinion, the extent of spend on brand building does not justify the incremental revenue per patient. Anyone who can provide comparable service at competitive prices will emerge as the winner in the Indian diagnostic market.

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4. What are your views on the competitive intensity in this space?

Competition has clearly gone up in the segment. This is aided in part by the absence of any significant entry barriers in this space including lack of regulatory oversight, low capital requirements and higher return ratios compared to other segments of healthcare. In general, there have been more entrants in the market over the last decade compared to those who have been displaced or consolidated – this is a good barometer of the increasing competitive intensity.

The diagnostic industry is unique in the sense that there are high profits at low volumes – aided by lack of compliance costs and overheads – and high profits at high volumes – aided by efficiencies of scale and kicking in of operational leverage. However, one can see a sharp decline in profitability as one attains a mid-scale set-up, partly due to a step function in compliance and equipment costs and a sharp spike in overheads including rentals, manpower costs and other infrastructure costs. Therefore people who enter the business make good money to start with and even if the profitability declines as they grow, they revert to their earlier sub-scale operations but don't exit. Very few players tide the growth stage and go on to become large meaningful players.

Therefore, to summarize, most competition comes from smaller, un-organized players who make good money with their sub-scale operations and have no desire to grow but are also too small to allow for consolidation by a bigger player.

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EXPERT SPEAK

Select Sector Transactions

August 2017
Exclusive Advisor
To
OMNI Hospitals
Structured Debt
By
IFMR Capital
Undisclosed

June 2017
Exclusive Advisor
To
A South India pharma company
Banking Facilities
By
A private sector bank
~USD 12 Mn

Multiple tranches - 2017
Advisor
To
Select Institutional Buyers
Block Deal
In
HCG
Undisclosed

Multiple tranches - 2017
Advisor
To
Select Institutional Buyers
Block Deal
In
NH Narayana Health
Undisclosed

5. On an associated point, are you also witnessing shift of volumes from the unorganized market to the organized players and is that process gaining momentum?

The shift is happening but the growth of the industry is happening at a much faster pace. So while the industry is growing, both segments of the market are growing with it but given that the number of organized players are small, it is difficult to peg the extent of this shift in an ever growing market. At a macro level, some part of the common population are moving from so called unbranded diagnostics to more branded diagnostic players, which is broadly what people talk of as unorganized to organized market shift, and in a way that is helping us.

As an example, if we are growing say at a CAGR of 25%, 2% of that growth can be attributed to this shift that is being referred to.

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6. Thyrocare has also ventured in some new testing lines like testing for Tuberculosis, which is somewhat of a departure from the lifestyle/chronic testing only model that you have been doing. What are your plans on that front?

I think this is an interesting area for us to focus on. Tuberculosis is neither a chronic illness nor is it very acute – it takes around one year for the treatment to pan out and in that sense one could call it semi-chronic. The selection of the ailment has also been done keeping in mind two things – one does not need to have immediate test results which means that all work in this aspect can continue as per existing TAT protocols and secondly, there is no major player focusing on tuberculosis in a big way. Hence we call it FocusTB.

We believe that the market offers immense potential and given the right investment, branding and support, it could emerge as one of the material drivers of our growth going forward.

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7. What are your views on platform consolidation in diagnostics – on the lines of what is being attempted in some healthcare sub-segments? What do you think are the benefits and pitfalls of that model?

My view is that it is a doable idea but it is a very difficult proposition to execute. Most importantly, I believe that the front end customer facing operations must be detached from the testing labs if this consolidation model was to be successful. Currently, any such consolidation will result in coming together of many partners, all of whom do the testing at the same premises where the customer sample is being collected. In order to truly derive benefits of scale, testing needs to be centralized while consolidation of front end outlets under one umbrella could be beneficial.

Additionally, there are operational issues like governance structures, capital allocations and growth benchmarks that need to be pre-defined and then driven by a common link in the system. So as I said, it is very doable but very difficult and someone who can pull it off will derive tremendous synergies and value in the long run.

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Select Sector Transactions

November 2016
Exclusive Advisor
To
Apollo
Private Equity Fund Raise
By
IFC
USD 68 Mn

July 2016
Exclusive Advisor
To
CORONA Remedies Pvt. Ltd.
Private Equity Fund Raise
By
Creador
USD 18 Mn

May 2016
Exclusive Advisor
To
RAMESH HOSPITALS
Majority Stake Acquisition
By
Aster
USD 28 Mn

March 2015
Exclusive Advisor
To
HealthHiway
Private Equity Fund Raise
From
Piramal
Undisclosed

NOT JUST '*SUBURBAN*' ANYMORE

Expanding Horizons For Customer Experience

SUBURBAN DIAGNOSTICS

We interviewed Dr. Sanjay Arora, Founder and Managing Director of one of West India's most prolific organized diagnostic chain and picked his brains on the challenges facing B2C diagnostic industry today and what he believes is the way forward on several macro trends shaping the industry

Dr. Sanjay Arora
Founder & Managing Director, Suburban Diagnostics

1. After the dream run over the last decade, there is an emerging consensus amongst organized diagnostic players that growing organically is getting increasingly difficult. What, in your opinion, are the factors that are making organic growth challenging for organized diagnostics in India?

There are multiple perspectives to this.

Diagnostics is still not a pull business – unlike getting a haircut where a customer shows up at the salon once every two months or less – and hence the diagnostic revenue profile is not annuity-like by definition. Bulk of healthcare continues to remain push driven – including diagnostics – which means that there has to be an incidence of anomaly in healthy well-being for someone to visit a diagnostic test centre. Unless we are able to create a pull factor, there will always be an initial hiccup to growth.

Secondly, there is a lot of credibility and trust factor in this domain given the doctor-patient relationship dynamics. A large part of India still operates at the level where there is a personalised connect between the patient and the service provider; trust and admiration that is built over years. Also, convenience plays a stronger role compared to service and quality – although that is slowly changing with people realizing that it's a matter of health and hence the local mom and pop diagnostic centre may not have the best facilities; but this change will take time.

Therefore even if the brand pull is great for a lot of the diagnostic chains in the home market, outside of the home market, displacing a local incumbent with years of operational history may be a difficult task. This is especially true in places where there is a strong local incumbent providing quality service over a long period of time. In many such cases, a lot more groundwork needs to be done by the new diagnostic chain despite its strong brand to stir the patients' propensity to shift.

Thirdly, diagnostics in India continues to be largely an out of pocket expense. Therefore the willingness of people to spend and prioritize wellness tests or preventive health checks is still very limited, which in a way dovetails into the

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EXPERT SPEAK

Select Sector Transactions

May & Nov. 2014
Exclusive Advisor
To
vasan healthcare – from a tradition of care
Private Equity Fund Raise
From
GIC SEQUOIA WESTBRIDGE CAPITAL
USD 68 Mn

September 2014
Exclusive Advisor
To
OMNI Hospitals
Minority Stake Acquisition
By
ASK PRAVI CAPITAL ADVISORS
Undisclosed

July 2014
Exclusive Advisor
To
OMNI Hospitals
Majority Stake Acquisition
By
UDAI
Undisclosed

October 2013
Exclusive Advisor
To
cloudnine
Private Equity Fund Raise
From
SEQUOIA matrix PARTNERS INDIA
USD 17 Mn

point mentioned earlier about diagnostics still not being a pull business. Insurance coverage for sectors like diagnostics, home health, etc. will be a watershed event changing the way need for diagnostics is perceived in India.

And lastly there is little barrier to entry – especially in pathology where capital requirements are also limited. This combined with the fact that India is still largely a price sensitive market means that local players with little overheads and hence better pricing power (at least for routine tests) will continue to farm business despite organized and branded players' presence in the market.

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2. Two operational models in diagnostics have emerged in India – the B2C model and the B2B model. A number of B2C companies also have a large B2B business. What are your views on each and how do you see the industry panning out as regards preference amongst the two models?

Different players in the market have grown through different routes and hence the jury is still out in the market as to which is the better model. But personally for us and that's how we continue to drive growth at Suburban Diagnostics, we believe that B2C is the preferred approach. I guess from a clinical perspective, there is a lot more value that a customer facing B2C chain can add to a patient and hence there is a lot of medical satisfaction in running a B2C diagnostic business. B2C business also has a higher ticket value, one can focus on repeat customers having known the test patterns and there is also a strong brand element here which makes the model very attractive.

Having said that, the B2C model is also a very difficult model to succeed in – there are multiple things that you need to focus on and get right for the business model to find some traction. One needs to be persistent, costs need to be tightly controlled (especially given customer demands) and selection of geographies to enter needs to be carefully thought through. Additionally there also needs to be focus on conveying the right marketing message, build a very strong network credibility and doctor connect and one needs to do this over and over again as seeds of expansion are sown with growth.

The B2B model on the other hand is based on one's ability to drive volumes through to the system and hence by definition is an extremely competitive and price focused market. For example, strong organized branded diagnostic chains who never discounted their services on the B2C side in their home market are entering newer markets with heavy discounts on the B2B side, which is then forcing incumbents in these markets to further discount their services. I believe that this is a very dangerous spiral but that's the nature of the business on the B2B side which has become a heavy discount game rather than focus on where one can add clinical value to a patient.

What has also happened in the market is that a lot of the players have had to revise their business models to accommodate the changing business dynamics in the diagnostic landscape. So players that started primarily as B2C companies and had been so for over a decade and a half are now looking at B2B given that competition is eating into some of their original business. Also players that are expanding into newer geographies are targeting to get to scale quickly in that geography via the B2B route and will hopefully look at that effect rubbing off on the B2C business.

The key I guess lies in having a right mix of B2B and B2C businesses. Most diagnostics businesses in my opinion will have a J-curve history where at the bottom of the J, the B2B component outstrips their B2C revenue profile but as the scale expands and the company grows, the balance shifts towards the B2C side. Ideal operations in my opinion could target a 65% B2C business and a 35% B2B business mix and that is the mix we would ideally want to have for Suburban going forward.

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3. Coming to the split between the pathology and the radiology business, do you think some component of radiology is important for a pathology focused operations?

That's a question that is both easy and difficult to answer. The easy answer is

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EXPERT SPEAK

Select Sector Transactions

July 2013
Exclusive Advisor
To
OMNI Hospitals
Private Equity Fund Raise
From
ASK PRAVI
Undisclosed

March 2013
Exclusive Advisor
To
SUTHERLAND GLOBAL SERVICES
Minority Stake Acquisition
In
Apollo Health Street
USD 182 Mn

March 2012
Exclusive Advisor
To
vasan healthcare
Private Equity Fund Raise
From
GIC
USD 100 Mn

March 2012
Exclusive Advisor
To
MEDALL
Private Equity Fund Raise
From
PEEPUL
USD 32 Mn

that it is not essential for a pathology focused player to have any component of radiology. There are enough and more examples of very successful pathology-only businesses that continue to do exceedingly well. Suburban Diagnostics, when we started operations, was also a pathology only business and it was only over a period of time that we started introducing radiology services from a completeness of test menu perspective. On the flip side, most of the chains down South or chains started by radiologists across the country started off as being pure radiology diagnostic service providers and have added pathology services only later to ride on the brand pull they enjoy in the market. In fact, some continue to focus successfully only on radiology till date.

But when the insurance sector started opening up in India, they started to look at an opportunity for partnering with a comprehensive diagnostic service provider, which was the time a lot of investments were made in the radiology business. From a Suburban Diagnostics perspective, the way we look at having radiology diagnostic services is to be able to offer the complete suite of preventive diagnostic services – just to make health aspirational, to create that true pull factor. So we probably will continue to have services like ECG, ultrasound, stress tests and X-Rays but don't think we will invest heavily into MRI and CT Scan equipment and associated services. The idea is to be able to service the corporate wellness side of things and also the preventive health check requirements of our customers.

Besides, adding a host of radiology services to our offerings has bolstered our market positioning. We are proponents of the fact that comprehensive diagnostics is not just a blood test, but goes beyond that. It's the right mix of pathology and radiology services in conjunction with each other, that provides the clinician a 360 degree view of the patient situation and leads to a comprehensive and reliable diagnosis.

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4. Talking about the regulatory landscape in India for diagnostics – if regulation does come in, our view is that it will be better for the organized players given that there will be an increased cost of compliance and doing business for unorganized players. But it will also mean that there could be some noise around pricing which may be a negative for the industry. What are your thoughts on the regulatory aspect of doing business?

In my view, as long as the intent on regulating the sector is right, regulation could be a good trigger for the diagnostic business in India. In my view any regulation should aim to *create a level playing field* so that no one has any undue advantage or any disadvantage – it should facilitate people who are below standard to move up to a standard threshold and at the same time it should be able to weed out people and businesses who are unqualified or cut corners, from the industry. I guess any regulation is most universally accepted when it also acts as a facilitator for business. Giving an analogy that I like, it (regulation) should be like the banks of a river which guides the river flow (industry) as it moves along rather than being like a dam that prevents the flow altogether.

As far as pricing is concerned, I guess there has to be a clear distinction between what are costs associated with the treatment and what are the costs of consumable and products. I guess in the current parlance, people are mistaking recipe costs for raw material costs – the recipe cost in my view is significantly higher compared to the raw material costs. And the reason for that is that there are add-ons in terms of manpower costs, infrastructure costs, costs of providing the right service setting and cost of the knowledge of the medical practitioner imparting that knowledge, among others. If raw material costs are alone being thought of as determinants in price fixation, then I guess more thought needs to go in to make the policy a win-win for all stakeholders.

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5. There are also very interesting businesses that are emerging doing high-end esoteric tests and a lot of PE money is funding these new businesses. How do you think this sub-segment will shape up in times to come?

I guess there are interesting segments in which a lot of work is happening – molecular biology, flow cytometry and

EXPERT SPEAK

Select Sector Transactions

March 2012
Exclusive Advisor
To
vasan healthcare
Majority Stake Acquisition
In
SHEKAR NETHRALAYA
Undisclosed

June 2011
Exclusive Advisor
To
Vaatsalya
Private Equity Fund Raise
From
AQUARIUS
Undisclosed

October 2010
Exclusive Advisor
To
vasan healthcare
Private Equity Fund Raise
In
SEQUOIA WESTBRIDGE CAPITAL
USD 26 Mn

January 2010
Exclusive Advisor
To
MEDALL
Majority Stake Acquisition
In
CLUMAX DIAGNOSTICS
USD 11 Mn

genomics to name a few. Also, with the tremendous advancements in technology, what is specialized today will become routine tomorrow – at least that is what empirical evidence shows us. Healthcare is evolving and it is difficult to know where the next disruption will come from. I am pretty sure that technology will have a big role to play in this but I guess it is also important for strategic players and for private capital providers to invest in such segments with an eye on the long term. If we don't invest today, we will be left playing a catch-up game in the long run.

Healthcare is getting more personalized, it is becoming more individual specific and genomics will play a big role in how medicinal protocols and practices will be decided. Medicines that work on an individual may not necessarily work for another and if one is able to personalise the diagnostics, the therapeutics and the outcome, it's a win-win for everybody and I am pretty certain that molecular diagnostics, genomics and genetic studies have a big role to play in this personalization of healthcare. So while the routine pathology market itself is big enough, players building such niche will become increasingly relevant in times to come, especially organized diagnostic chains intending to offer an ever-increasing bouquet of tests to their customers.

The unfortunate part however is that, as a country, today we are still grappling with basic issues of health and hygiene, lack of infrastructure and most of our diagnostic facilities and resources are still only geared up to face infectious diseases and basic ailments. These issues are still very prevalent and unless we think of the bigger picture of improving our health indices and the health economic parameters, uptake for such specialized services will remain very limited and sub-scale

• • •

6. In a lot of ways, diagnostic service providers are also the first brush of a patient with organized healthcare (with the exception of a GP) and hence are the first ones to experience and build connect with the patients, build repeat value and much more. Given this first level connect, do you think branch out to associated areas like home healthcare, wellness clinics or chronic disease management is a good idea for diagnostic companies?

These are good thoughts. Home healthcare is going to happen and incidence of home healthcare will increase in India over the next decade or two. So looking at this in a focused disease profile manner rather than looking at it generically is the way to go. So perhaps looking specific segments like lifestyle diseases, women health, bone health, diabetes management or chronic disease management or working with cases of infectious diseases presents a great case for a deep dive and creating a niche for oneself. All in all, I guess it is a very attractive opportunity and I am personally very excited about it.

However from an investment perspective, one really needs to weigh the pros and cons of entering such associated segments and therapeutic areas. Especially for diagnostic chains, in my opinion, it is best to maintain neutrality and ensure that one does not really create any conflict of interest between the various stakeholders that one has to interact with as part of the business.

• • •

DECODING THE REGULATORY *BLACK BOX – MORE MYTHS THAN FACTS* (1/4)

Select Sector Transactions

December 2009
Exclusive Advisor
To
vasan healthcare
from a tradition of care
Private Equity Fund Raise
From
SEQUOIA WESTBRIDGE CAPITAL
USD 12 Mn

October 2009
Exclusive Advisor
To
MEDALL
Private Equity Fund Raise
From
PEEPUL
USD 19 Mn

February 2009
Exclusive Advisor
To
vasan healthcare
from a tradition of care
Private Equity Fund Raise
From
SEQUOIA
Undisclosed

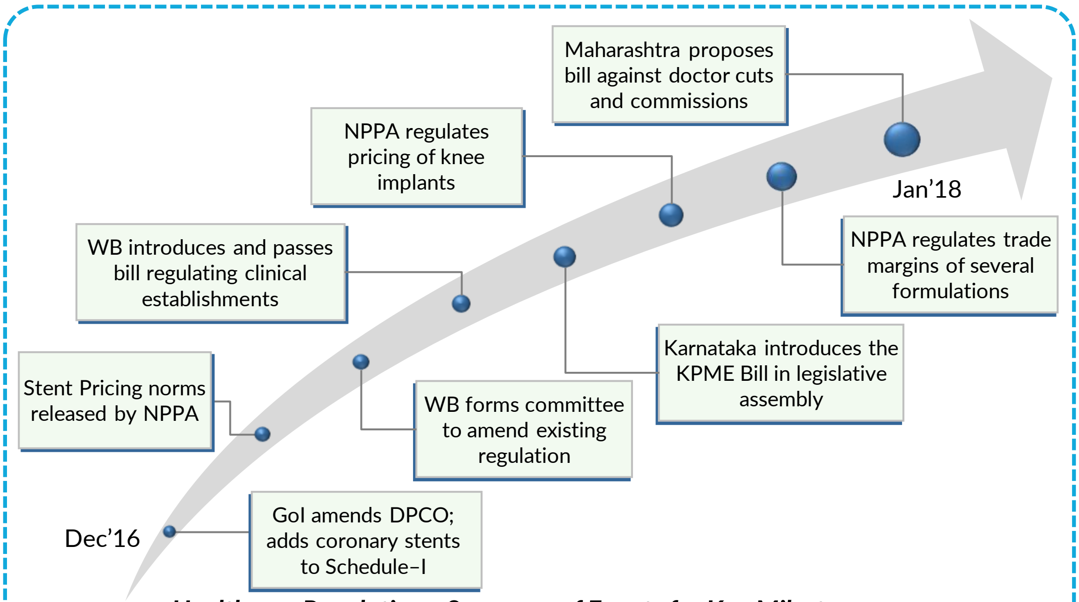
MYTH	VS.	FACT
For the ***first time healthcare regulations*** have been formulated by West Bengal & Karnataka		***Very similar regulations prevalent*** in West Bengal (since 2010) & Karnataka (since 2007), but *rhetoric is high this time around!*
Procedure Pricing has been set by State Governments and is already, or is expected to be, implemented		Items of fine print in the regulations, like pricing, left to committees and consultations – ***no diktat on procedure pricing as yet!***
Pricing is universal – expected to be followed by all private healthcare providers across patient categories		On ground intelligence indicates ***pricing to be implemented only for patients under government schemes*** – free pricing otherwise
Government activism on stents and knee implants was swift and unexpected – ***things are becoming ad-hoc!***		Govt. first included stents in Schedule-I of DPCO, asked for pricing info across channels, held consultations with players – ***nothing ad-hoc in the calibrated sequence of events!***
It's game over for MNCs – will not be able to compete on price with domestic devices manufacturers		NPPA mulling separate category for high-end stents and implants – ***MNCs to continue to play*** Increasing NPPA focus on capping trade margins and not prices – ***playing field to be levelled!***

Perhaps the single biggest dampener in deal making in Healthcare and Lifesciences in 2017 was the constant flux in regulatory landscape – staring from state specific legislations to a nationwide curb on stents and knee implant pricing and finally a limit on trade margins (in some cases the trade margin was set at zero!) for essential drugs and consumables.

Given several important state elections in 2018 (including Karnataka) and the impending general elections in 2019, we believe that 2018 will see continuing regulatory changes. Interestingly however, price regulation in healthcare was part of neither of the political party manifesto leading into the general and state elections. Product pricing (which continues to be primarily a central government subject matter) may continue to be under pressure but implementing procedure pricing caps (matter of state subject) will be difficult to execute.

Given the scale of regulatory activism, we thought it best to take a closer look at the events that shaped CY17.

DECODING THE REGULATORY *BLACK BOX* – *MORE MYTHS THAN FACTS* (2/4)



Healthcare Regulation - Sequence of Events for Key Milestones

Caps introduced on cardiac stent pricing

On December 21, 2016, the government amended the DPCO and added "coronary stents" (including drug eluting stents or DES) under Schedule-I of DPCO. Oher items added to Schedule-I were disposable hypodermic syringes and needles and intra ocular lenses, among others.

As a background, India treats drugs as essential commodities and has enacted a price control order (i.e. DPCO) to ensure access and availability of these drugs. The DPCO mandates that drugs which are part of its schedule (i.e. Schedule-I) shall not be sold at a price higher than the ceiling price fixed by the government. These drugs are called Scheduled Drugs. The applicability of DPCO, which essentially deals with drugs, to medical devices was one of the first of its kind and hence caught many by surprise. Under the "Make in India" policy of 2015, medical devices was flagged off as one of the sectors of focus. This event implicitly underlined medical device industry's significance and sent clear signals that it has the attention of the government. The intent of the NPPA could also be gauged from the fact that it sought information on Price to Retailer / Price to Stockists / Price to Hospital, the Moving Annual Turnover and Maximum Retail Price from manufacturers, importers and marketers before inclusion of stents as Scheduled Drugs. Consultations were held in January' 17 and finally on February 13, 2017, it fixed prices for various categories of stents slashing existing rates in some cases by as much as 80%.

The order was valid for one year, with renewal in February, 2018. Then in February 2018, much against expectations, stent prices were reduced further. Additionally, it was made mandatory to provide billing details separately for certain consumables used in cardiac processes.

Impact:

a. Price data published shows that control majorly cuts into the margins of the distributors and hospitals - Impact on P&L of cardiac heavy healthcare delivery players was felt immediately with a steep immediate reduction in EBITDA for the specialty

b. Market share of MNC stent makers dropped by 6% to 33% - Indian players gained share; Chinese made an entry

c. The order set the tone for price caps on knee implants and price activism on other devices and consumables

d. Given prices were capped irrespective of the generational advancement and/or therapeutic superiority, MNCs rushed to withdraw their high end-stents from Indian markets – NPPA has recognized this and has written to the ministry asking for a separate category for high-end stents, which will most likely not be subject to pricing caps or at least not as aggressive ones

Select Other Sector Transactions

January 2018
Exclusive Advisor
To
GO COLORS!
Private Equity Fund Raise
By
ICICI Venture
~USD 15 Mn

December 2017
Exclusive Advisor
To
Nextwave Multimedia
Majority Stake Acquisition
By
Nazara
Undisclosed

December 2017
Advisor
To
SK Finance
Private Equity Fund Raise
From
NORWEST Venture Partners, evolvence India, Baring Private Equity Partners India
~USD 32 Mn

December 2017
Exclusive Advisor
To
Specsmakers
Private Equity Fund Raise
By
8° EIGHT ROADS
~USD 10 Mn

SPARK CAPITAL

DECODING THE REGULATORY *BLACK BOX – MORE MYTHS THAN FACTS (3/4)*

Select Other Sector Transactions

November 2017
Exclusive Advisor
To
Quess
51% Acquisition
of
TATA BUSINESS SUPPORT SERVICES LIMITED
~USD 24 Mn

November 2017
Advisor
To
KINARA
Private Equity Fund Raise
From
unitus capital, Gaja Capital, GAWA Capital
~USD 15 Mn

October 2017
Advisor
To
Yellow Diamond
IPO
~USD 74 Mn

September 2017
Exclusive Advisor
To
intellect Design for Digital
Rights Issue
USD 31 Mn

State Activism – City of Joy not so joyful for Healthcare Delivery Providers

On February 22, 2017, the Chief Minister of Bengal called for a 'live telecasted' meeting with all major private healthcare players and communicated her displeasure at their operations and pricing. This set the context for setting up of a panel to recommend changes to existing legislature regulating healthcare delivery in the state.

The result of the above was The West Bengal Clinical Establishments (Registration, Regulation and Transparency) Act, 2017(the "Act"), which was introduced and passed by the Assembly on March 17, 2017. The term clinical establishments was defined to include almost any form of private healthcare delivery service provider in the state including diagnostic service providers. The Act sought to replace an earlier version under a similar name passed in 2010. Key provisions were as under:

- Compensation to be provided to patients/kin due to medical negligence ranging from Rs. 3 – 10 lakh
- Provide necessary medical treatment to victims of accidents / sudden calamities, without taking into consideration the ability of the patient to pay the costs
- Free services to 10% of IPD and 20% of OPD patients for hospitals constructed on government land
- Every establishment with 100+ beds required to declare bed charges, ICU charges and package rates which can't be altered
- Strictly follow the fixed rates and charges including the package rates
- No delay in releasing the dead body of patients to their representatives due to billing or other issues, including inability to pay the treatment cost
- Monetary penalties for non-compliance including for provisions to hold management responsible and cause repeal of license to operate

The 2010 law, which was repealed, also had similar provisions (**it had a rate charge for hospital services as far back as 2002**), *but added scrutiny for the Act came from latter 5 provisions mentioned above, and the fine print being construed as the State wanting to become the 'nodal pricing agency' for all private healthcare procedures.*

Impact:

a. The Act and the media coverage surrounding it cast a dampener on private investment in the state

b. P&L of all major delivery providers was under stress for FY17 and H1FY18

c. Our on ground checks suggest that while no such pricing caps were proposed, presence of a regulation could result in continued uncertainty

KPME – Karnataka's Tryst with Regulation

One of the reasons why Karnataka's attempts at regulating private healthcare drew attention of the entire nation was that Karnataka is one of the most penetrated state as far as private healthcare infrastructure is concerned. Some of India's best known hospital chains and finest medical talent resides in Karnataka. It is also perhaps one of the most invested state in the country by private capital providers.

Like in Kolkata, the Karnataka Private Medical Establishments Act, 2017 (the "KPME") also replaced an earlier law with a similar name that dated back to 2007. A committee headed by Justice (Retd.) Vikramjit Sen, set up to recommend changes to the 2007 law tabled its report in May 2017. Amongst the other recommendations of the committee, the most controversial was the provision to also bring government hospitals under the KPME fold. The government contended that nearly 12 insurance companies had complained that the PMEs (private medical establishments) were overcharging and that it had paid over Rs. 1,000 crore since 2003 to the 250-odd private hospitals. Amendments to the 2007 law, tabled in the legislative assembly on June 13, 2017, had the following key provisions that later became the main bone of contention between the industry and the government:

- KPME expressly provided for charges to be fixed by the State Government including package rates for bed charges, OT, ICU, ventilator care and procedures
- Modification to charges to account for change in course of treatment was disallowed unless expressly consented to by the patient

SPARK CAPITAL

DECODING THE REGULATORY *BLACK BOX – MORE MYTHS THAN FACTS* (4/4)

Select Other Sector Transactions

July 2017
Exclusive Advisor
To
FIVE STAR
Private Equity Fund Raise
By
SEQUOIA, Morgan Stanley, NORWEST, matrix
~USD 52 Mn

March 2017
Exclusive Advisor
To
hffc
Private Equity Fund Raise
By
truenorth
USD 100 Mn

March 2017
Exclusive Advisor
To
CreditAccess Asia
Private Equity Fund Raise
By
ADB
USD 32 Mn

February 2017
Co-Book Running Lead Manager
To
BSE
IPO
USD 183 Mn

- Final bill to not exceed estimates provided to patient
- No delay in releasing the dead body of patients or service recipients to their representatives due to billing or other issues, including inability to pay the treatment cost
- Provision for imprisonment for up to five years for contravention of provisions of KPME by medical practitioners

Just like in Kolkata, several provisions were existent even in the 2007 law but amendments were viewed as an attempt to regulate pricing and profitability.

The bill was referred to a standing committee after protests from medical practitioners on June 16, 2017. Consultations ensued but, with a deadlock looming large, a state wide strike was called in November lasting several days. Finally a compromise was reached with imprisonment provisions being diluted and the bill was passed on November 17, 2017. The Governor assented to the same in January, 2018 and KPME came into force from February 10, 2018.

Impact:

a. One of the biggest factors in causing discomfort in investment in healthcare delivery services

b. Price caps in place for now only for patients of government schemes

c. Decision on pricing and execution of recommendations left to several sub-committees – our on ground checks suggest status quo for now

d. Other states like Maharashtra have introduced bills to stop doctors' commissions both ways and in fact have categorized these as corruption practices to be probed by the anti-corruption bureau with criminal charges

Knee Implants go under scalpel of Price Control

Following coronary stents, the government imposed a price ceiling on knee replacement systems ("Knee Implants") for a period of one year by way of a notification dated August 17, 2017. Notification categorized Knee Implants into two major Categories: Primary Knee Replacement Systems and Revision Knee Replacement Systems. Under each category there are 4 sub-categories and under each such sub-category, there are four super-sub-categories. Ceiling prices have been prescribed for aforementioned super-sub-categories. As an example, pricing pre-Notification of Rs. 1.7 lakh capped to Rs. 39,000 and pricing pre-Notification of Rs. 1.2 lakh capped to Rs. 24,000.

In hindsight, this was an expected move but then the Notification came as surprise to many especially since Knee Implants were hitherto not recognised as 'essential' and because the government fixed maximum trade margin for distributors and hospitals between 4%–16% depending on the category of Knee Implants, which was significantly lower than existing margins. Also, the provisions of the DPCO technically allow NPPA to determine price and not margins and hence the move was seen as unprecedented in many ways.

What happens next is anybody's guess, especially since the Medical Device Rules, 2017 make all medical devices fall within the ambit of DPCO from January 1, 2018 and become subject to the government's residuary power to fix ceiling prices. The language of the provision that gives residual power to the government is broad enough to allow the government to fix ceiling price of any medical device. News reports suggest that there is a new Pharmaceutical Policy in the making which would seek to regulate trade margins specifically, something the current one does not envisage at all.

In the meanwhile the NPPA in November and December 2017 has already introduced price ceilings for several formulations. In a first, it fixed the institutional procurement price as the ceiling price without adding any trade margin for 14 formulations including glucose injections, morphine tablets and emergency injections. This it did again by invoking para 19 of the DPCO – citing extra-ordinary circumstances – much in the same way it capped prices for knee implants.

Several component makers' industry bodies (e.g. for needles and syringes) are voluntarily talking of self-regulation for capping their trade margins to 75% over discounted ex-factory prices including GST.

Interesting times lie ahead!

RECENT HEALTHCARE & LIFESCIENCES INDIA TRANSACTIONS

Select Other Sector Transactions

August 2016
Exclusive Advisor
To
Qwikcilver
Private Equity Fund Raise
From
Sistema, helion, Accel Partners, amazon
USD 10 Mn

June 2016
Exclusive Advisor
To
Suryoday
Enabling Dreams. Empowering Lives.
Private Equity Fund Raise
By
IDFC, Ask Pravi, HDFC Life, LNB Group, Americorp Group, Gaja Capital
USD 32 Mn

March 2016
Exclusive Advisor
To
UNBXD
Private Equity Fund Raise
From
Nirvana, ICP Inventus Capital Partners, IDG Ventures, Indian Angel Network
Undisclosed

February 2016
Exclusive Advisor
To
Sumeru Frozen Foods
Buyout
By
Peepul
Undisclosed

A M&A Transactions in the Sector

Company	Description	Buyer / Investor	Transaction Date	Deal size
Triesta Sciences	Acquired by	Strand	January 2018	Undisclosed
Shreya	Digeplex and associated brands Acquired by	Piramal	November 2017	USD 14 Mn
Strides Shasun	India Branded Business Acquired by	Eris	November 2017	USD 76 Mn
Unichem Laboratories Ltd.	Domestic Formulations Business Acquired by	Torrent Pharma	November 2017	USD 556 Mn
Symbiomix Therapeutics	Acquired by	Lupin Pharmaceuticals, Inc.	October 2017	USD 150 Mn

B Private Equity Transactions in the Sector

Company	Description	Buyer / Investor	Transaction Date	Deal size
Strand	Invested into By	Quadria Capital	February 2018	USD 13 Mn
Asian Institute of Medical Sciences	Invested into By	CDC	February 2018	USD 21 Mn
SMT	Invested into By	Morgan Stanley Global Private Equity, Samara Capital	December 2017	USD 36 Mn
Indiabulls Pharmaceuticals	Invested into By	Clermont	December 2017	USD 24 Mn

C Equity Capital Market Transactions in the Sector

Company	Transaction type	Launch date	Deal size
Aster	Initial Public Offering	February 2018	USD 140 Mn
Natco	Qualified Institutions Placement	December 2017	USD 142 Mn
Shalby Multi-Specialty Hospitals	Initial Public Offering	December 2017	USD 79 Mn
Granules	Qualified Institutions Placement	December 2017	USD 47 Mn

Source: Deal Databases
Deals between Oct'17-Feb'18

LATEST NEWS AND ANNOUNCEMENTS

Select Other Sector Transactions

January 2016
Exclusive Advisor
To
CreditAccess Asia
Structured Capital Raise
From
Olympus Capital Asia
USD 30 Mn

December 2015
Exclusive Advisor
To
aasaanjobs
Private Equity Fund Raise
From
Aspada, ICP Inventus Capital Partners, IDG Ventures India
Undisclosed

November 2015
Joint Advisor
To
POLARIS live your dream
Majority Stake Acquisition
By
virtusa
USD 270 Mn

November 2015
Exclusive Advisor
To
Sportz Village
Private Equity Fund Raise
From
Gaja Capital
~USD 10 Mn

Stent Pricing

NPPA SEEKS NEW CATEGORY FOR HIGH END STENTS

Move comes as companies withdraw new generation stents from market

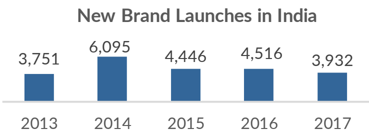
NPPA has written to the Union Health Secretary on January 9 requesting for an urgent meet of the cardiac stents core committee of the NLEM to reconsider and review need for a new category of drug eluting stents – provided stent makers are able to prove generational superiority.

Move comes as Abott announced non-introduction of its latest stent Xience Sierra in India and after withdrawal of Xience Alpine series in Sept'17. Boston Scientific is also considering withdrawing high end stents.

Pharma

BRAND LAUNCHES IN 2017 LOWEST IN 4 YEARS!

Slowdown in approvals or a sign of things to come?



The domestic pharma industry growth rate was the lowest in eight years as the business was impacted by roll out of the goods and services tax (GST) regime and also delayed product approvals by the National Pharma Pricing Authority (NPPA).

Anti-malarials and anti-infectives recorded negative growth while cardio-therapy growth was down to single digits (6.7%) (from double digit growth recorded for last few years).

Regulation

STRICTER PRICE ACTION TO HIT MARKET SOON, WARNS REGULATOR

More pain ahead?

"The pricing regime will be strict than what it is so far. The government is answerable to the people," NPPA Chairman Bhupendra Singh said at an Indian Drug Manufacturers Association event in Mumbai earlier in January, 2018.

Singh said trade margins for 25 per cent of drugs sold in the country ranged from 100% – 1,200%.

Earlier in Q3FY18, price caps were introduced for various drugs and formulations and trade margin caps were introduced for some items.

Pharma

INDIAN PHARMA RUSHES TO "MAKE IN AMERICA"

Hope to advantage from tax arbitrage under newly announced Trump tax policy

Several Indian drug makers who have large operations in the US are now pushing to acquire assets, thereby either investing in greenfield manufacturing facilities or through brownfield M&As.

The government reduced tax for American companies to 21% from 35% – ~15% difference between Indian and US tax rates is a big lure for Indian pharma companies, a sector that derives 40% of revenues from USA.

Indian drug companies' search for US manufacturing assets is also to push up the portfolio of complex generics products—expected to be the next big growth driver.

M&A

PHARMA M&A: BUYING ITS WAY BACK TO GROWTH

Cost rationalization and risk sharing with PEs makes it an attractive bet!

Sector's revenue to increase by 9% p.a. till FY20, with overseas revenue growing by a mere 1% in 2018 and then improving. But for domestic growth of 10-11%, overall figure would look worse.

In light of the above, the reason for Indian pharmaceutical companies being keen on global acquisitions is not hard to fathom, even if the sales of the portfolio on offer are declining. While stemming a sales decline may be difficult, improving profits by cost rationalization could be possible.

Also, some acquirers are unlisted (no quarterly performance pressures), have low debt and partnering with PE firms ensures risk dispersion and higher acceptability amongst shareholders.

SPARK CAPITAL

Source: News Publications

LATEST NEWS AND ANNOUNCEMENTS

Select Other Sector Transactions

Sept 2015 onwards
Exclusive Advisor
To
Select Institutional Buyers

Secondary Stake Acquisition
In
NSE
~USD 403 Mn

May 2015
Exclusive Advisor
To
ISFC
India Shelter Finance Corporation
Private Equity Fund Raise
From
NEXUS VENTURE PARTNERS SEQUOIA
WESTBRIDGE CAPITAL
USD 43 Mn

May 2015
Exclusive Advisor
To
SHRIRAM City
MONEY WHEN YOU NEED IT MOST
Minority Stake Acquisition
In
CEYLINCO INSURANCE PLC
~USD 16 Mn

April 2015
Exclusive Advisor
To
enzen
Structured Capital Raise
From
KKR
USD 60 Mn

Home Health

MARKET FOR HOME HEALTHCARE SERVICES IN INDIA TO DOUBLE IN A YEAR

Estimated at ~USD 3.20 Bn in 2016

Still in a nascent stage; largely serviced by unorganized players, start-ups and recent hospital initiatives.

Estimated at ~USD 3.20 Bn in 2016, and expected to grow to ~USD 4.46 Bn by 2018 and USD 6.21 Bn in 2020 as per estimates and analysis of Cyber Media Research Limited.

Any insurance coverage to the space to be a further add on trigger for growth in the sector.

Markets

WORST BEHIND US?

Growth in healthcare index comes months after lacklustre performance

The S&P BSE Healthcare index grew ~11.7% between October 1, 2017 and January 30, 2018, which was only a shade lower to the ~14% growth in the S&P BSE Sensex over the same period.

The rise comes after a lacklustre first nine months of the calendar where it fell nearly ~12% despite the strong growth in S&P BSE Sensex. The trend is in line with growth in global healthcare indices like Nasdaq (~10%) and Hang Seng (~18%), among others.

Insolvency

LENDERS KEEN TO EXPLORE NCLT OPTION FOR STRESSED PHARMA ASSETS

Orchid Pharma already on the block

"Some of the assets are good with manufacturing sites being approved by the US Food & Drug Administration, the UK's Medicines and Healthcare Products Regulatory Agency and other regulators and agencies depending on type of asset. All these demonstrate the potential of these companies", said a source close to the process.

Under the insolvency and bankruptcy code, the creditors along with the resolution professional have to invite and finalise resolution or revival plans from interested bidders, buyers and even the promoters within 270 days, failing which the assets of the company would be put up for liquidation.

USFDA Activism

INDIAN PHARMA COS GET RECORD USFDA GENERIC DRUG NODS

...despite regulatory pressure from USFDA and unprecedented number of warning letters

Domestic pharma companies received more than 300 approvals in 2017 to launch generic drugs in the US, which is an all-time high. The clearances came despite regulatory pressure from the USFDA, and unprecedented warning letters issued to facilities.

The final approvals for Indian players are up by nearly 43% from 211 in 2016, and corner about 40% of all global filings in the highly lucrative around $70-billion US market. This, even as all drug biggies — including Zydus, Sun Pharma, Dr Reddy's and Cipla — faced regulatory ire, while some were pulled up for manufacturing lapses by the US regulator during last year.

Liquidity Events

COMPANIES LOOK TO CAPITAL MARKETS FOR FUNDS; PROVIDE EXIT TO PE INVESTORS

Slew of IPOs lined up

Even as Shalby's IPO scraped through and the stock continues to remain under pressure, an increasing number of companies are looking at an IPO option for fund raising and providing an exit to their investors.

Amongst companies that will come to market over the next 3-6 months include Bharat Biotech, Bharat Serums, Krishna Institute of Medical Sciences and Aster DM Hospitals to name a few.

The move comes in light of an increased investor interest in India's capital markets, growing liquidity and a general improvement in macro environment.

Source: News Publications

FROM OUR EQUITIES DESK

Institutional Equities Highlights

198
Stocks under coverage

USD 1.2 Tn
Total market cap of stocks under coverage

INR 260 Bn
Total cash market volume in H1FY18

350+
Number of fund relationships globally

"Go-to" broker for stocks in the mid-market space

THOMSON REUTERS 2017 INDIA ANALYST AWARDS

THOMSON REUTERS ANALYST AWARDS 2017 WINNER

Institutional Investor

5th position in 2017
All India research team
Amongst 2 Indian Houses in Top 5

Healthcare & Lifesciences

19
Stocks under coverage

~USD 85 Bn
Total market cap of Stocks under coverage

Key snippets from some interesting notes by Spark's Equities Team

1 *Initiation of Coverage on Indian Diagnostic Services Sector*

- Play on India's growing healthcare demand and well-positioned to benefit from the country's changing demographics, rising incidence of lifestyle-related illnesses and greater adoption of Evidence-based Medicine (EBM)
- **Industry is highly fragmented** with regional and pan-India chains accounting for only ~15% of the market – consolidation of the industry will be gradual given several structural characteristics including dominance of hospital-based labs, low entry barriers, lax regulatory environment and strong regional incumbents
- While pan-India chains have embarked on an aggressive growth path with greater focus on high-end testing and wellness segments, **expect pressures on volume growth, pricing and margins**, as regional chains (some of which are PE-backed), compete fiercely to defend their turf
- Key thoughts: (1) Highly fragmented market with low entry barriers; (2) Still a 'hyper-regional' play; (3) PE-backed players driving competition and pricing pressures, especially in the B2B segment; and (4) Growth pressures and greater focus on quality should lead to gradual consolidation in the long-term
- **Initiate coverage with a cautious outlook on the sector**

2 *Pharmaceuticals – "Complex" Story will be "Rewarding"*

- **Pricing challenges in US yet to bottom out** – Indian players have had a patchy track record in complex generics, lagging their global peers in high-value generic segments, partly due to approvals delays on account of GMP compliance issues but believe **Indian pharma's complex generic prospects are improving**
- Key reasons: (1) **Strengthening of pipelines** in recent years – top 10 Indian pharma companies spent ~$12bn under R&D and capex in the last 3 years (vs. <$5bn in the preceding 3 years) – a significant portion of the spending was towards building complex generic pipelines for US; (2) **Streamlining of approval process** for complex products by the FDA; and (3) **Improving GMP compliance** –recent trend of successful inspections and EIRs should aid approvals
- **In the end, it has to be "Specialty"**: Believe complex generics (including biosimilars) will get crowded eventually and a higher exposure to branded/specialty segments will be a more sustainable strategy for larger generic companies in the long run
- Given the complexities in specialty pharma business execution, **in the medium-term, execution on complex generic opportunities will remain critical for growth**

3 *Pharmaceutical Outsourcing – Opportunities Galore*

- Outsourcing of non-core research and manufacturing activities – a major trend in the global pharmaceutical industry for over a decade
- Early stage drug discovery, manufacturing clinical trial quantities of drug substances and API manufacturing – some key areas for Indian CMOs and CROs. **Indian industry players have heterogeneous areas of expertise, service offerings and customer profile**
- R&D productivity improves, but **drug discovery cost increasing** – key driver for outsourcing
- Increase in **VC funding for pharma / biotech industries in recent years bodes well** for the industry - these typically are companies without their own development/manufacturing capabilities and are a significant source of business for CROs and CMOs

SPARK CAPITAL

Source: SPARK Research

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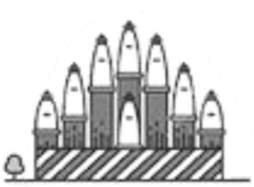
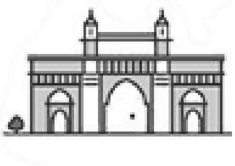


BENGALURU
Unit Nos. 503 & 504, 5th Floor, Prestige Towers,
No. 99/100, Residency Road,
Bengaluru – 560 025



MUMBAI
Unit No. 1116-C, 11th Floor, ONE BKC,
Bandra Kurla Complex,
Mumbai – 400 051

SPARK CAPITAL