EVALUESERVE

Global Healthcare M&A:

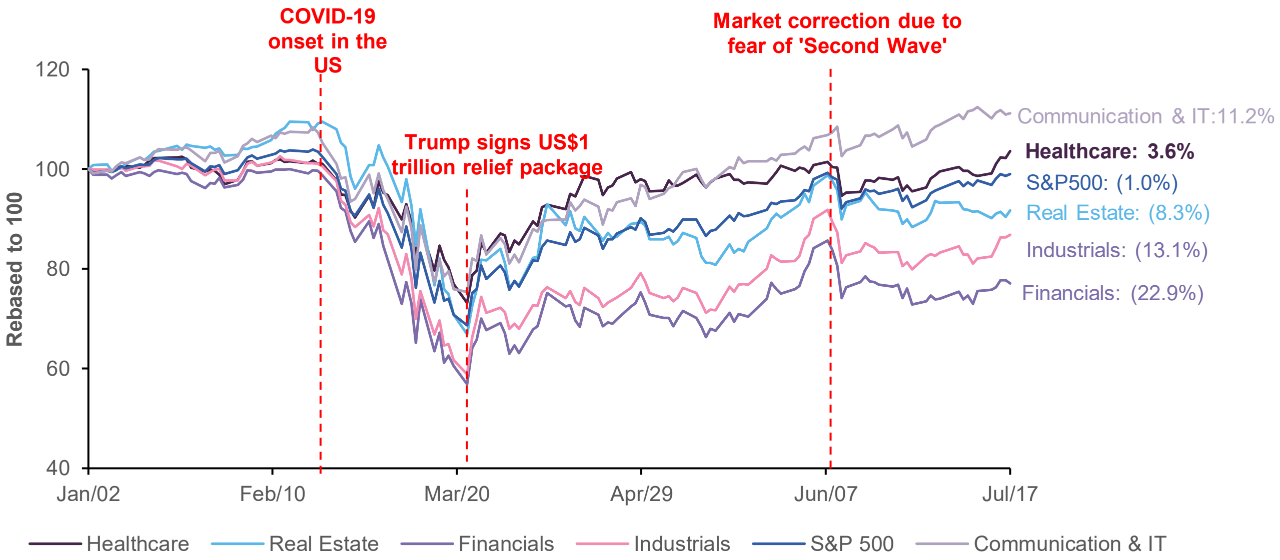
H1’20 Update

Global Healthcare M&A in H1 2020

The shock of the COVID-19 pandemic, and the lockdown measures adopted to contain it, have had a debilitating effect on the global economy. According to the World Bank, the global economy will likely contract by 5.2% in 2020. After several months of lockdown, many countries have started resuming business and economic activity. However, a second wave of COVID-19, which has affected more than 14 million people across the globe, has compelled governments to re-think their 'unlock' strategies.

In our previous update, we discussed how the healthcare industry showed resilience during the pandemic and continues to garner strong investor confidence due to robust demand. Moreover, owing to its 'defensive' nature, the healthcare industry has outperformed the broader market, except the communication and IT industry, which recently witnessed a strong rally due to higher adoption of internet-based services and apps (refer to US S&P Dow Jones Indices graph below). We believe the US healthcare industry has recovered from its lows in March, and the overall health of the market is showing strong signs of recovery after receiving a strong fiscal stimulus from the government.

US YTD Market Performance (2020)



	Healthcare	Real Estate	Financials	Industrials	Communication & IT	S&P 500
Post Covid-19 Performance	2.5%	(16.0%)	(22.7%)	(14.0%)	3.6%	(4.4%)

Source: S&P Dow Jones US market Indices; COVID-19 onset in the US market started from 20 Feb 2020

The healthcare industry has almost reached pre-COVID-19 levels because of broader market recovery, and as investor's factor in the aspects of the 'new normal.' It may seem that the market has bottomed out. However, the current recovery is expected to be highly volatile. The healthcare system is bracing for a potential second wave of infections, while the global economy is being forced to hit the 're-start' button without a proper antidote.

M&A in Global Healthcare Industry: Down but Not Out

Successful M&A requires robust due diligence and evaluation, as well as substantial collaborative effort. The COVID-19 outbreak and the accompanying impediments have shifted the timeline of various M&A deals. As expected, M&A in the healthcare industry too slowed down in Q2 2020, mainly due to global lockdown measures and a distressed deal-making environment. Some of the roadblocks for healthcare M&A observed in the last few months are as follows:

- Disruption to planned and ongoing clinical trials, primarily due to suspension of enrollment of patients and delays in initiation. These have made it difficult to ascertain the valuation of biopharma companies
- Higher focus on capital conservation and lower appetite for high-risk investments that are not immediately EBITDA accretive due to long payback period / low return on investment
- Significant supply chain disruptions (China being the epicenter) which has impacted both operations and access to markets

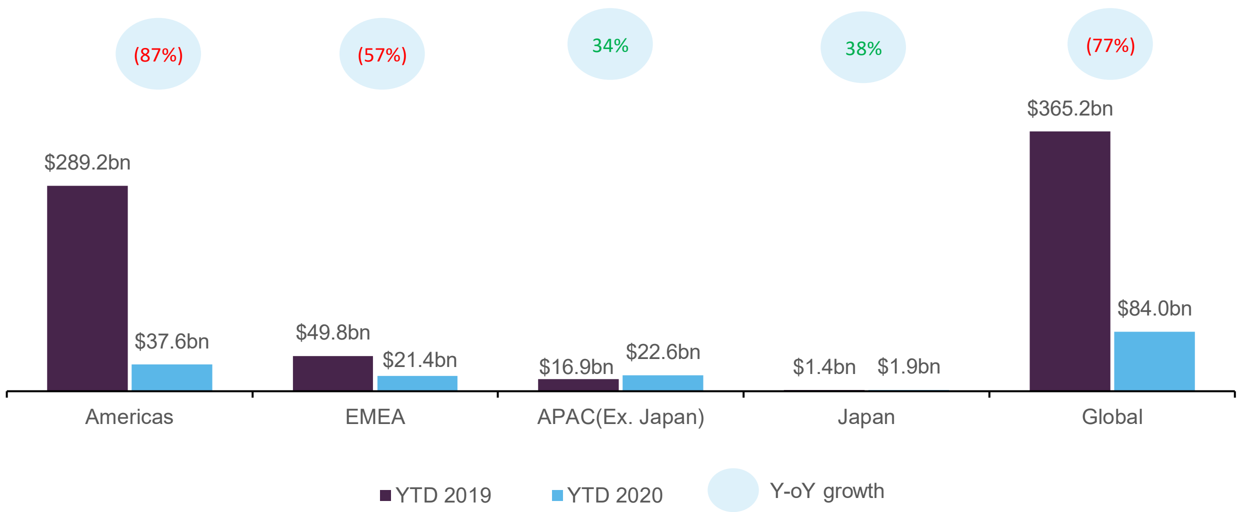
The industry has witnessed limited deal closures and is yet to see the conclusion of some 'big ticket' deals (such as the pending merger of Mylan's with Pfizer's Upjohn, Stryker's USD5.4bn bid for Wright Medical, and Thermo Fischer's USD11.5bn bid for Qiagen). The current status of these deals are as follows:

The closure of the Mylan-Upjohn deal has been delayed due to delays in approval process and is currently expected to close in Q4'20

The Stryker-Wright Medical deal has been postponed for an indefinite period due to uncertainties related to FTC approval and topline

The terms of the Thermo Fischer-Qiagen deal were amended following a valuation mismatch, highlighted by key stakeholders

Global YTD Healthcare M&A



Source: Refinitiv; deals as of 16 Jul 20; YTD 2019 figures represent approximate values

However, the APAC (including Japan) region has been witnessing strong signs of recovery in deal activity. Several deals which were under discussion previously are being re-initiated, thus providing well-timed opportunities for investment banks. Some of the major M&A announcements in Q2 2020 are as follows:

- ✓ In May, the Abbvie-Allergan deal was closed after it received regulatory approval from government authorities and the High Court of Ireland
- ✓ Lantheus and Progenics amended the terms of their merger in February 2020, and closed the deal in June 2020
- ✓ In June 2020, Novo Nordisk announced a USD2.1bn bid for Corvidia Therapeutics and Invitae placed a USD1.4bn bid for ArcherDx

Additionally, in May 2020 the news of AstraZeneca exploring a mega-merger with Gilead Sciences reflected that the drivers of pharmaceutical M&A remains intact; this emanates from a desire to bring new growth drivers in-house

Key Pending M&A Deals

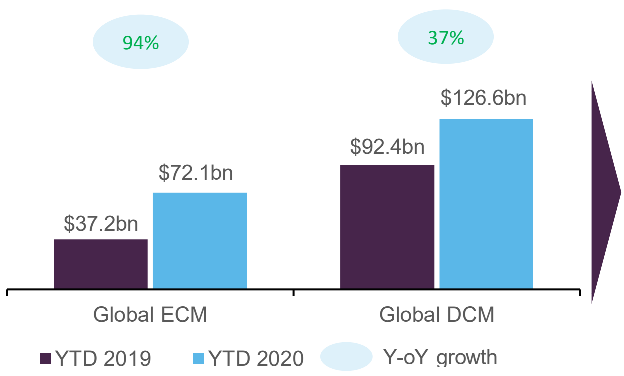
Announcement date	Acquirer	Target	Target's domicile	Deal Value (USD mn)	Expected timeline
Jun 22, 2020	Invitae	ArcherDx	US	1,400	Q4 2020
Jun 11, 2020	Novo Nordisk	Corvidia Therapeutics	US	2,100	Pending
May 8, 2020	Bain Capital	Nichii Gakkan	Japan	1,170	Q3 2020
Apr 30, 2020	Molina Healthcare	Magellan Complete Care	US	850	Q1 2021 (deal approved by FTC)
Mar 3, 2020	Thermo Fisher	Qiagen	The Netherlands	11,500	H2 2020 (terms amended due to valuation gap)
Mar 2, 2020	Hypera Pharma	Certain Takeda Brands	C/S America	825	H2 2020
Dec 18, 2019	Fujifilm	Hitachi's imaging biz	Japan	1,633	Delayed due to COVID-19
Nov 4, 2019	Stryker	Wright Medical	US	5,400	H2 2020 (FTC has raised questions about deal)
Jul 29, 2019	Mylan	Upjohn (Pfizer)	US	12,000	Q4 2020 (M&A terms amended)
Nov 13, 2018	Cipla	Avenue Therapeutics	US	180	Not defined (To buy remaining 67%, depending on US approval of IV Tramadol)

Source: Evaluate Pharma and company filings as of Jul 16, 2020

Healthcare Funding: Focus on Building 'Cash Runways'

Despite several short-term challenges, discussed in our previous update, the healthcare industry will likely witness an increase in M&A activity in H2 2020. Many governments and their respective central banks have rolled out financial relief packages to 'cushion' the impact of COVID-19, thereby ensuring sufficient liquidity in financial markets. This is further evident in the massive uptrend in activities in equity and debt capital markets (ECM and DCM), wherein investors have consistently recognized and added value to 'fortress balance sheets.' With the funding environment clearing out and adequate dry powder in hand, we can expect M&A activity to resume in the near future

Global YTD Healthcare ECM and DCM Activity



Source: Refinitiv; deals as of Jul 16, 2020; YTD 2019 figures represent approx. values

- ✓ Some issuers, especially those with good credit rating, are capitalizing on prevailing low-value coupons to strengthen their capital structure in the DCM.
- ✓ In the ECM, biopharma companies are leading the way with record levels of IPOs and follow-on deals, due to an increase in the number of roadshows, wall crossing events, and overnight offerings.
- ✓ Robust order books and after-market performances signify strong investor engagement in the industry

'Big Ticket' ECM and DCM Deals in Healthcare

Offer Date	Company	Target's Domicile	Deal Value (USD mn)	Stock Exchange	Deal Type
Jul 9, 2020	Takeda Pharmaceutical	Japan	11,100	Tokyo	Debt
Jul 1, 2020	Hikma Pharmaceuticals	UK	500	LSE	Debt
Jul 1, 2020	Bayer	Germany	~6,800	Luxemburg	Debt
Jun 24, 2020	Merck & Co	US	4,500	NYSE	Debt
Jun 22, 2020	Upjohn (Pfizer)	US	11,500	–	Debt
Jun 19, 2020	SK Biopharmaceuticals	South Korea	~800	Korea Stock Exchange	IPO
Jun16, 2020	Royalty Pharma	US	~2,500	Nasdaq	IPO
Jun 12, 2020	Catalent	US	~550	NYSE	Follow-On
May 28, 2020	Argenx	US	530	Nasdaq	Follow-On
May 13, 2020	MyoKardia	US	551	Nasdaq	Follow-On

Source: Company filings as of Jul 16, 2020

Light at the End of the Tunnel Gets Brighter

Most healthcare companies seem to have weathered the financial distress caused by the pandemic in H1 2020. We believe the industry will recover from this situation as we acclimate to the changing environment. COVID-19 has highlighted the importance of the scale and resilience of a business portfolio. It has also changed the way in which governments and healthcare companies look at healthcare supply chains, regulatory approval, and technology. We foresee the following key M&A trends to drive deal-making in H2 2020:

1. **Earn-outs or contingent payments to bridge valuation gaps:** Considering the current uncertainties in financial forecasting and asset valuation, we believe companies will increasingly depend on earn-outs to bridge differences.
2. **Estimated high buying capacity of USD2tr among private equity firms:** The capital position of private equity firms offers them with opportunities to assess and capture resilient healthcare assets in the near term. In 2019, the disclosed value of private equity M&A deals in the healthcare industry stood at a record USD78.9bn (as per Bain Capital).
3. **Attractive valuations continue to drive multiple buy-out discussions:** We expect the hospital segment to witness multiple buy-out activities. We also expect the M&A push to be broad-based across major healthcare sub-sectors, as innovation gets rewarded by investors. These include companies which are directly involved in addressing the spread of COVID-19, like those focused on diagnostics and vaccine development, as well as consolidation among medical devices manufacturers, which have been severely impacted by recent restrictions on elective procedures.

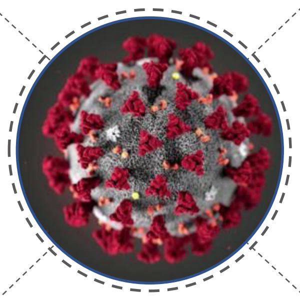
Key M&A trends across sub-sectors

Biopharma

Accelerated M&A to replenish drug pipelines and find synergies amid the race for a COVID-19 vaccine

Medical Devices

Focus on vertical integration of supply chains and resolution of production issues are set to result in M&A uptick



Healthcare Technology

A potential M&A hotspot, with the rising valuation of HealthTech and start-ups amid growing importance of contactless healthcare delivery

Healthcare Services

Mostly a buyer's market, wherein stressed assets are being forced to sell for much-needed cash infusion and other support to keep their doors open

Considering the importance of the healthcare industry's role during the current pandemic, we believe many new companies will enter this space with the objective of diversifying their business portfolio. The 'M&A handshake' has become a thing of the past however, organizations are discussing potential M&A by embracing various digital channels. Based on industry data and emerging trends / market sentiments, we expect the M&A environment to remain positive as companies seek deals to strategically re-position themselves.

We believe that attractive valuation, robust demand supported by supply chain normalization, and the re-opening of capital markets will accelerate M&A activity in late 2020 and early 2021.

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