GLOBAL HEALTHCARE CORPORATE M&A REPORT 2016

BAIN & COMPANY

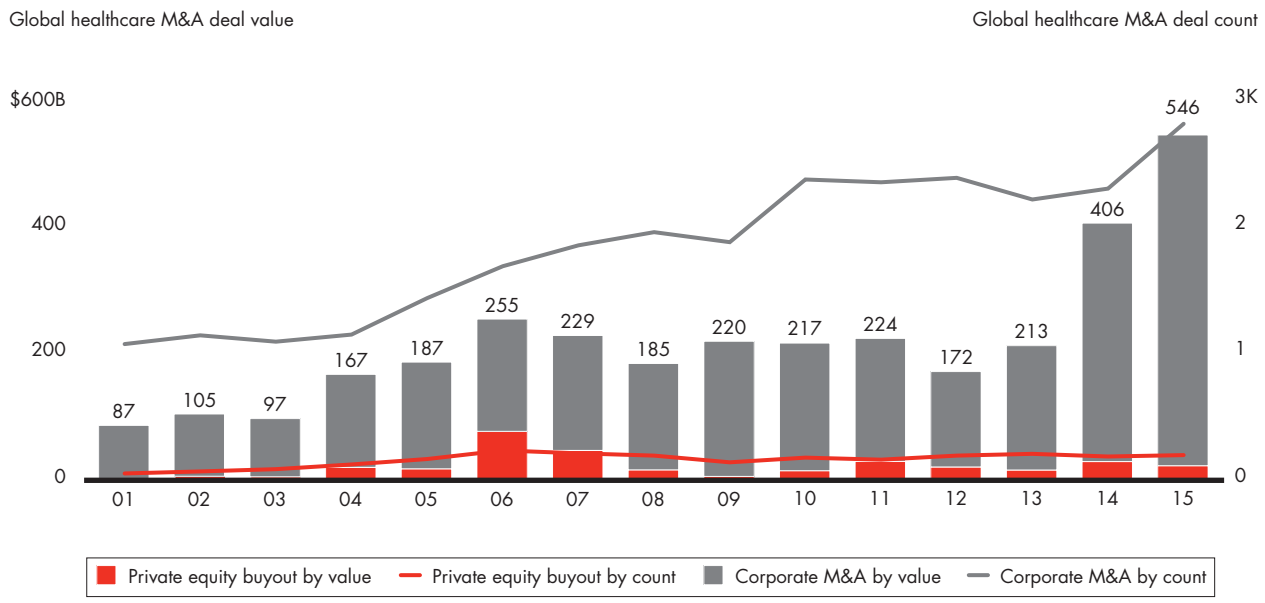
Healthcare M&A reached $546 billion in announced deal value in 2015—a 2.5 times increase over the previous decade's average annual value *(see Figure 1)*. Corporate buyers, which make up the largest share of healthcare M&A by far, likewise set a new record: $523 billion. Megamergers fueled much of the increase in value. Five deals over $20 billion were announced during the year (excluding the Pfizer-Allergan deal, which was called off in April 2016 and is excluded from this report's analysis), which represented a third of healthcare M&A deal value. But even without these megamergers, corporate M&A in healthcare would have been well in excess of the average annual deal value of the previous decade, as corporate buyers pursued deals of all sizes *(see Figure 2)*.

Other industries joined healthcare in setting records, and global M&A deal value reached a new high of approximately $5 trillion in 2015.[1] Yet healthcare activity stood out, with growth in healthcare deals significantly outpacing growth in overall M&A deals over the past three years *(see Figure 3)*. From 2012 to 2015, overall M&A grew at a compound annual growth rate (CAGR) of 24% while healthcare M&A grew more than twice as fast, at a 50% CAGR.

What is driving all of this M&A activity? The macro environment has favored M&A for several years. Tepid economic growth has made organic growth more challenging, spurring many firms to turn to inorganic methods to fuel meaningful topline improvements. The wide availability of inexpensive debt and strong equity values (albeit with more volatility beginning in the second half of 2015, as discussed later in this report) made M&A an attractive option. And in some cases, financial benefits like tax inversions also drove M&A activity.

Beyond these macro conditions, several industry-specific trends further fueled the healthcare M&A boom. First, demand for healthcare is surging given the rise of chronic and lifestyle diseases, aging populations in many developed markets and a growing middle class in many developing regions. As a result, there will be continued pressure

Figure 1: Corporate megamergers accounted for most of the increase in healthcare M&A



Note: Excludes spin-offs, add-ons, loan-to-own transactions and acquisitions of bankrupt assets; based on announcement date; includes announced deals that are completed or pending, with data subject to change; deal value does not account for deals with undisclosed values
Source: Dealogic; AVCJ; Bain analysis

globally to contain healthcare costs, which have consistently outrun GDP growth. Innovation is bringing new drugs, devices, technology and analytics to market. And new government regulations aim to improve quality and increase access to healthcare. Taken together, these trends are shifting the way that healthcare is delivered across the globe, triggering consolidation along the value chain as firms position themselves to emerge as winners.

Corporate buyers pursued many of the recent healthcare deals to advance their category leadership strategies, aiming to build or bolster leadership positions across their portfolios. This approach follows a clear downstream customer trend, in which desire for vendor consolidation and more sophisticated procurement practices clearly favor the category leaders. Consider drugmaker Shire, which recently made three acquisitions to build its leadership position in rare diseases. Shire acquired NPS Pharmaceuticals for $5.2 billion (announced and closed in 2015), Dyax for $5.9 billion (announced in 2015 and closed in 2016) and Baxalta for $32 billion (announced in 2016). In the global dental market, Dentsply, a leader in dental consumables, announced in 2015 that it would acquire high-tech dental equipment manufacturer Sirona for $5.5 billion.

The value of these mergers will come from building scale in specific customer-defined categories rather than building scale broadly across the biopharma and medtech markets. Category leaders have deeper relationships with their customers, key opinion leaders and even regulators, which gives them better insight into the dynamics and evolution of the category. As a result, category leaders can better direct their R&D efforts and product portfolios to meet market needs, and they often attract the best talent and assets available. Shire's acquisitions, for example, do not simply broaden its portfolio of drugs; they also deepen the company's expertise in the rare disease market, including important capabilities like navigating the orphan drug approval process and managing targeted popula-

Figure 2: Corporate buyers have been active for all deal sizes

Corporate healthcare M&A deal value (by deal size range)

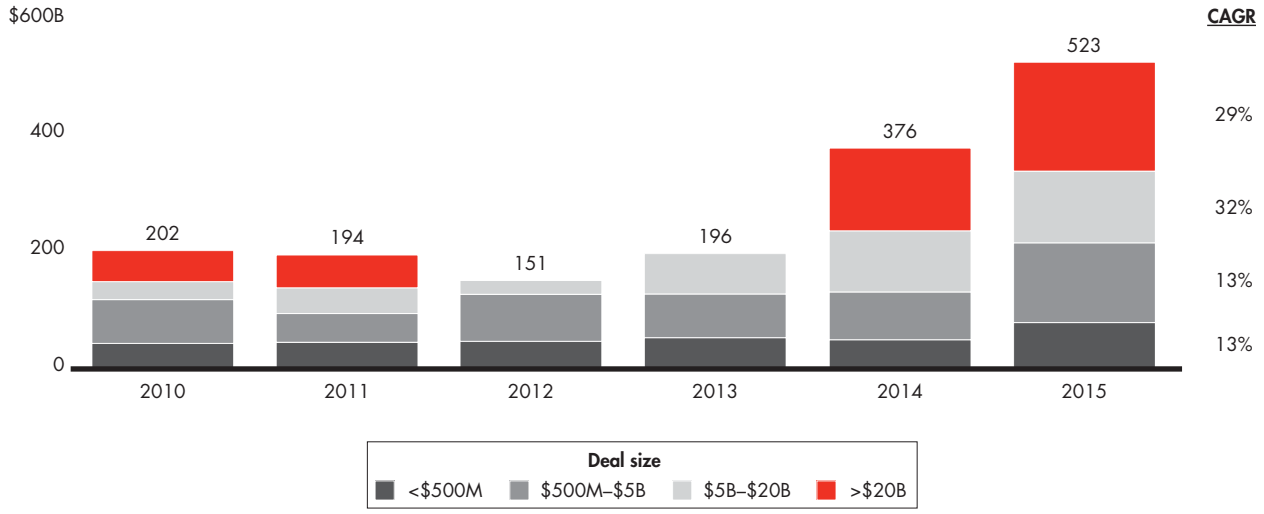


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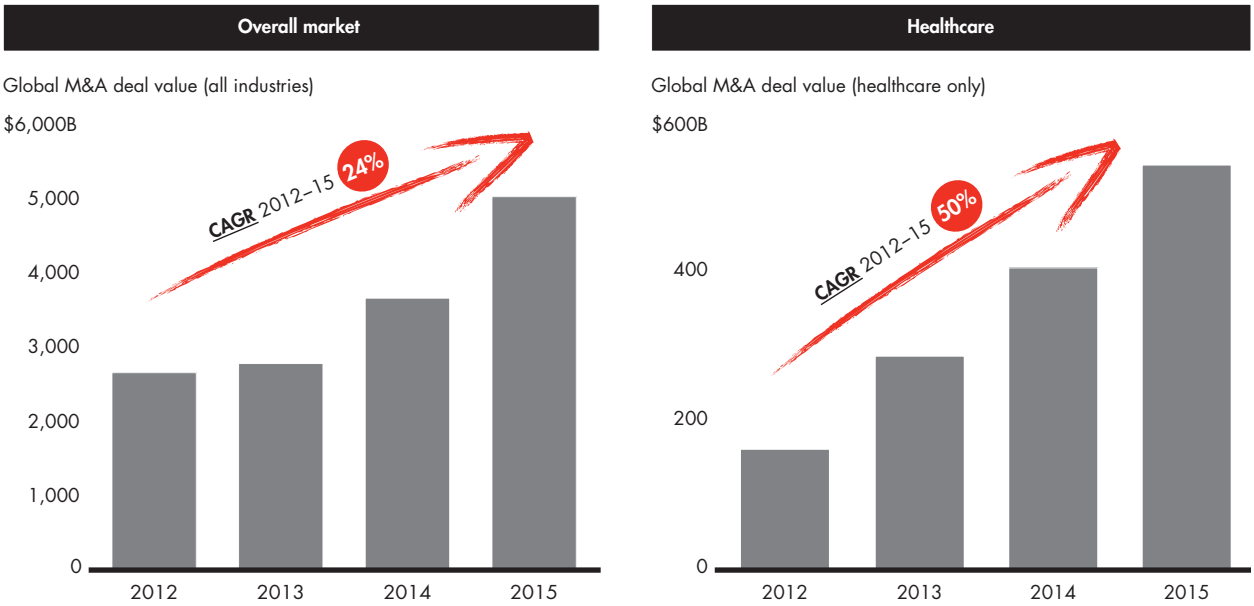
Figure 3: Healthcare M&A growth has outpaced the overall market since 2012



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tion clinical trials. And the combined Dentsply Sirona will have a more comprehensive product offering for its dental customers, as well as the right expertise to lead the charge as the equipment and consumables markets become more connected.

In the US payer sector, megamergers that were announced in 2015—for example, Anthem's $54 billion acquisition of Cigna and Aetna's $37 billion acquisition of Humana—were partly influenced by category leadership and the desire to move into new customer segments. Generally, in the payer and provider sectors, the category is relevant at the local level given patients' desire to have care delivered close to their homes. Providers' continued consolidation and expansion across the value chain—adding physician practices, insurance capabilities and new sites of care through M&A and partnerships—has catalyzed consolidation among payers. These payer deals also enable acquirers to better access higher-growth segments within the broader sector.

Another factor spurring healthcare M&A activity in recent years has been the financial benefit of tax inversions. Biopharma and medtech tend to be high-margin, global businesses, so a lower corporate tax rate can significantly benefit earnings. However, regulations are changing to curb the financial benefits of tax inversions, and some of these deals have been unwound because the strategic benefits alone are insufficient to offset the complexity that would come with the deal.

Implications for corporate buyers

Looking ahead, it is not clear how long the M&A bonanza will last, especially in light of the capital market volatility and strong possibility of a recession in the next few years. But M&A will continue to be an important avenue for

growth in healthcare, regardless of the economic cycle, and a downturn typically turns up attractive buying opportunities. All companies, then, can benefit by focusing on five fundamentals:

1. **Craft a clear strategy for leadership.** In a downturn, category leadership helps to maintain preferred vendor relationships with customers and provides resources to invest when competitors falter. Define the categories in which you want to play and articulate which moves—organic and inorganic—are required to win.

2. **Link deal diligence to your strategy.** Good targets that don't support the strategy distract management and waste time and resources. Have a clear thesis for how any acquisition will support your strategy, and validate it with due diligence. Start planning for integration early in order to anticipate likely challenges that could derail the strategic value of the deal.

3. **Build a repeatable M&A capability.** Bain research shows that organizations with an institutional M&A capability have greater deal success. Build a team that can identify the right deals; tailor the integration to focus on the most critical sources of value; and learn from any missteps along the way.

4. **Simplify your organization for growth.** Mergers can create a unique "unfreezing" period to reduce complexity throughout the organization, as employees already expect change. Identify products, geographies and capabilities that deliver profitable growth, and pare back or even carve out the rest.[2]

5. **Be creative in deal making.** Creative deal structures like asset swaps and partnerships with PE firms are on the rise for a reason: They match up assets with the right expertise. Don't be afraid to bring in deal partners or use creative structures to get access to the assets that help you execute your strategy and to divest assets that don't fit in your strategy.

Companies that excel in these activities raise the odds of over-delivering results from their M&A endeavors.

1 See the Bain Brief "Maximizing Your Merger's Potential" for more about overall M&A activity, including a discussion of three approaches to achieving a merger's full potential.

2 See the Bain Brief "Simplify to Grow in Healthcare" for more on this topic.

Note: Dealogic is the primary source for the M&A data in this report, supplemented with data from AVCJ and other public and private data sources. The dataset is based on deal announcement date and includes deals that are completed or pending, with data subject to change. Deal values do not account for deals with undisclosed values. Data excludes spin-offs, add-ons, loan-to-own transactions, acquisitions of bankrupt assets and private investments in public equity (PIPEs). The healthcare dataset includes healthcare-related deals that may be classified in other sectors by Dealogic. This methodology differs from that used in Bain's *Global Private Equity Report 2016, Asia-Pacific Private Equity Report 2016* and certain other Bain publications.

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