



Poised for Growth: Prospects for Southeast Asia's Private Healthcare Providers

Southeast Asia (SEA) is emerging as the bright spot for private healthcare provider investments, with increasing demand for private health services supported by strong growth fundamentals and the inherent gap in public healthcare infrastructure. Growth drivers for private healthcare demand include rising economic development and incomes, an underdeveloped healthcare infrastructure, increased healthcare spending, changes in population demographics, more favorable government regulations and a thriving medical tourism industry in the region.

Rising GDP and healthcare spending. Sustained economic development in SEA has led to a rise in incomes, increasing the consumer base of those who are willing to pay for healthcare. It also raised average life expectancy from 52.1 years in 1965-1970 to 69.3 years in 2005-2010. Healthcare spending is increasing rapidly as governments try to upgrade the underdeveloped infrastructure needed to support the rising demand for healthcare. Compared with the average of around 50 hospital beds per 10,000

people for members of the Organization for Economic Cooperation and Development (OECD), SEA countries range between 5 and 25 beds per 10,000 people.

Despite increased spending in recent years, average healthcare expenditure per capita in SEA still remains far below the OECD average (US\$643 versus US\$4,741 in 2014), signifying high growth potential for the region. Figure 1 illustrates the robust per capita growth rates of healthcare spending projected for SEA in the near future. Some markets, like Indonesia, will experience accelerated growth with the rollout of universal healthcare to cover their entire populations.

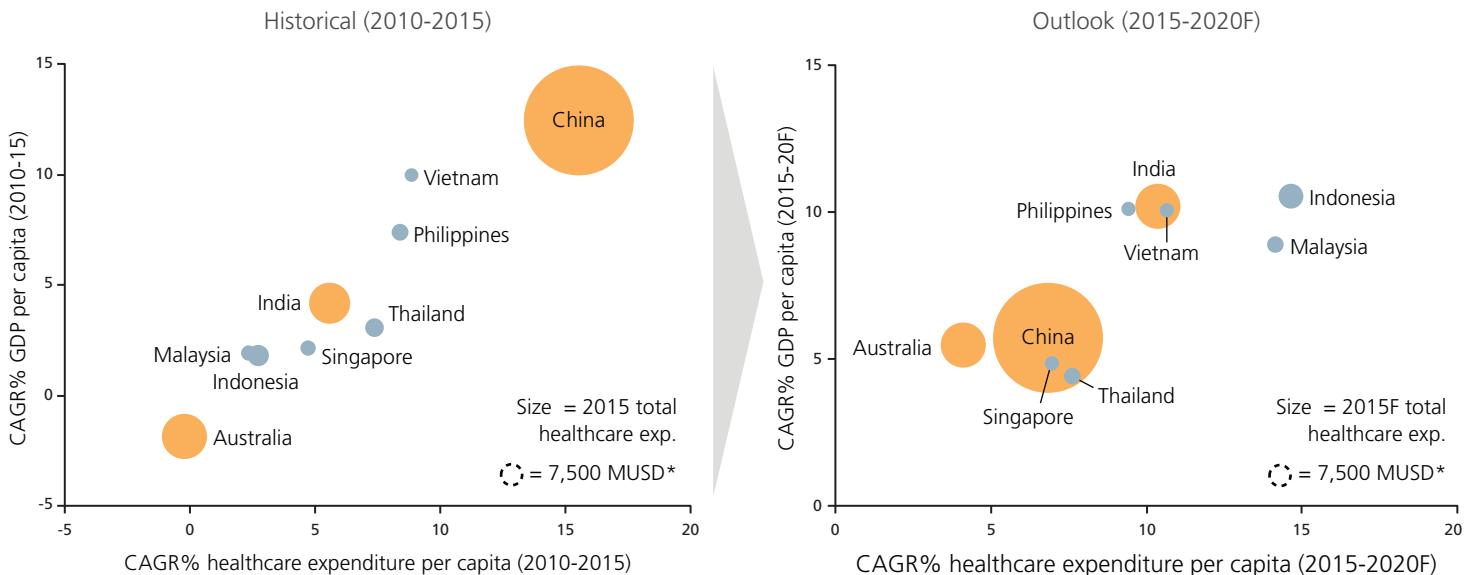
Changing population demographics and the rise of chronic diseases. Figure 2 highlights the increase in the middle-to-affluent-class population in SEA from 344 million in 2015 to 382 million by 2020, increasing the pool of consumers who can afford private healthcare. Changes, including more urbanized lifestyle and an increasingly aging population, have led to a rise in chronic diseases, which accounts for approximately 70% of disease burden in the region, fast approaching the 80% level in OECD countries. Chronic diseases will increase the demand for access to healthcare. With universal healthcare programs providing affordable access for lower-income populations, the more affluent will increasingly turn to private healthcare providers for better-quality services. Out-of-pocket payments have been increasing due to increased incomes, and the demand for private health insurance is growing.

Private Healthcare Providers in Southeast Asia: Poised for Continued Growth was written by **Zafar Momin**, Managing Director, **Calvin Wijaya**, Senior Associate Consultant, **Pattanit Chareonkul**, Associate Consultant, and **Paul Bernardo**, Life Science Specialist, in L.E.K. Consulting's Singapore office.

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Figure 1

Growth in incomes and healthcare expenditures for selected SEA and Asian countries (2010-2020F)



*MUSD (millions of U.D. dollars)

Source: Country healthcare statistics, World Bank, L.E.K. analysis

Favorable government regulations and universal healthcare.

Countries such as Thailand, Indonesia, Vietnam and the Philippines are striving to provide universal healthcare coverage for all their citizens, which is straining the resources and service quality in public hospitals due to the accelerated uptake. Governments have been slow to address the need for significant investment in public hospital infrastructure and for a greater number of healthcare professionals. For example, public hospitals are often overcrowded and plagued with shortages of doctors, medical supplies and diagnostic equipment, which affects their ability to deliver high-quality care. To expand healthcare offerings beyond the public sector, governments are providing incentives such as tax holidays, and raising the caps for foreign equity ownership to encourage private healthcare providers to fill the demand/supply gap.

Additional contributors to healthcare demand growth

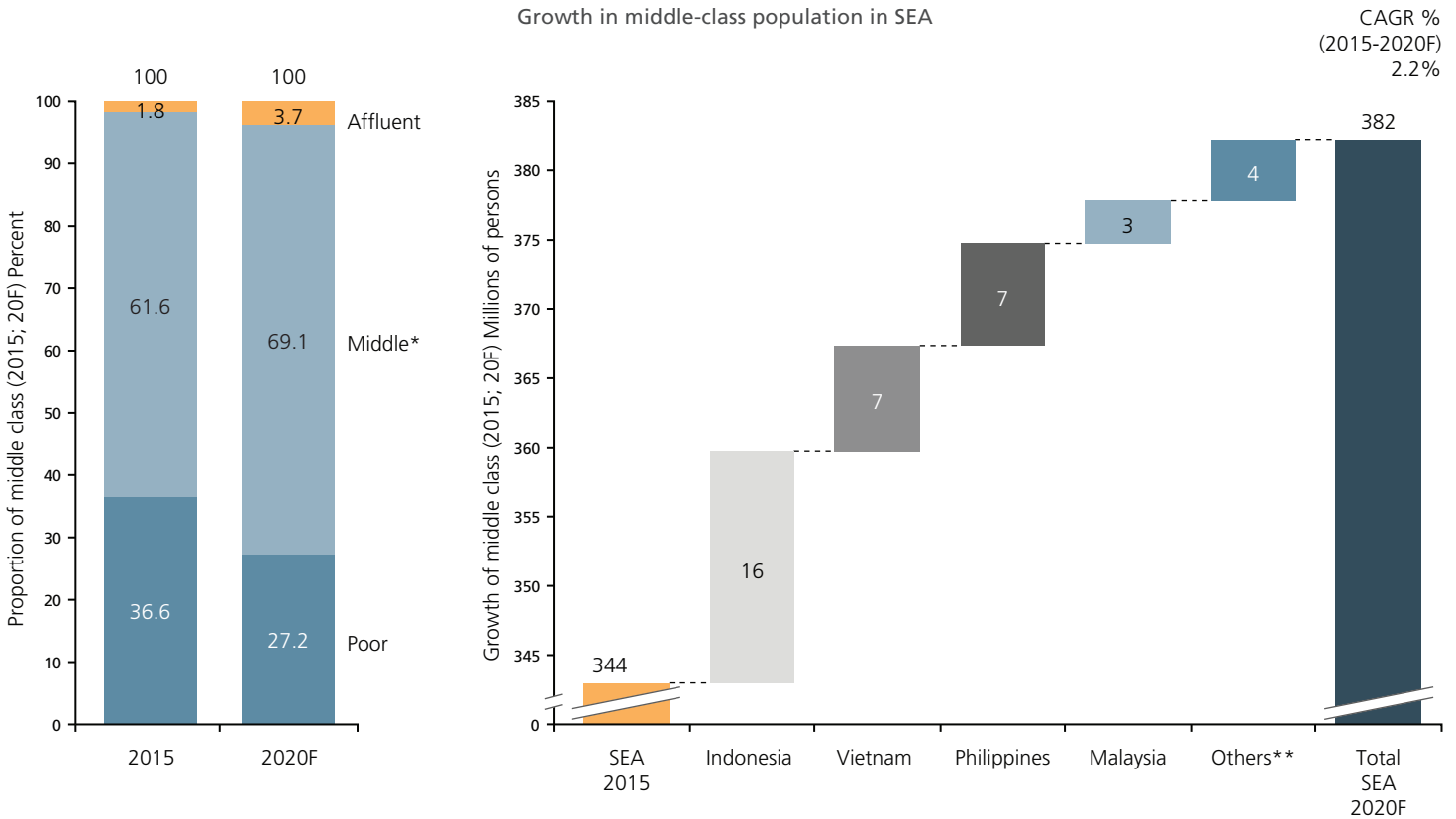
There is strong evidence that the private healthcare provider market will continue its growth trajectory for the near future. At least two additional factors will contribute to its trajectory — geographic expansion of medical infrastructure beyond Tier 1 cities, and medical tourism.

Latent growth potential beyond Tier 1 cities. Hospital infrastructure in most SEA markets is uneven and tends to be concentrated around Tier 1 cities; hence, there is significant room for geographic expansion. As the healthcare provider market becomes more mature in the Tier 1 cities, providers and investors

are shifting their focus to address the unmet needs of patients in small but fast-growing cities. Several such Tier 2 and Tier 3 cities have been growing in terms of population, income, infrastructural connectivity, workforce size and political clout. In Indonesia, Siloam Hospitals plans to grow its provider business by establishing 50 hospitals (from the current 20 hospitals) and 24 clinic units in 30 cities and regions, bolstering its bed capacity to over 10,000 beds to serve 15 million patients. In Malaysia, KPJ is adding nine new hospitals to the current 25 hospitals, as well as expanding existing hospitals to grow from 2,912 beds to 4,392 beds by 2018. BDMS, the largest healthcare provider in Thailand, with 43 hospitals across the country, plans to build two new hospitals in Surat and Chiang Rai, as well as expand and upgrade 10 of its existing hospitals. The growth is not just in adding hospital beds but also in providing specialized care in key areas that are lacking in up-country and remote areas.

Medical tourism. The growth of the highly lucrative medical tourism business has resulted in an increasing number of private hospitals in the SEA region seeking international certifications such as JCI (Joint Commission International) accreditation to expand patient capture beyond SEA. Thailand, Malaysia and Singapore have traditionally been the major destinations for medical tourism due to government healthcare promotion support, availability of internationally accredited facilities and staff, and high standards

Figure 2
Growth in middle-class population in SEA



Note: *Middle-class income strata: \$1000-\$1500 USD. **Includes Singapore, Brunei, Thailand, Laos and Cambodia
Source: Economic Intelligence Unit; Euromonitor, International Monetary Fund

of care. In 2012 alone, Thailand, Malaysia and Singapore drew 2.53 million, 700 thousand and 850 thousand medical tourists, respectively, from within SEA as well as the Middle East and Western countries, generating over US\$4.83 billion in total revenue. From 2011 to 2015, medical tourist arrivals have grown at 12% and 4% compounded annual growth rates for Thailand and Singapore, respectively. Thailand receives approximately four times more medical tourists than Singapore, but the per capita spend is lower due to decreased costs across medical procedures.

Foreign patients are a major contributor to private hospital revenue, particularly because patients come for advanced medical procedures, which generate higher revenue per patient. For example, in Thailand, foreign patients accounted for roughly 40%-60% of private hospitals' revenue and will continue to be the key revenue growth driver. In Thailand, both Bumrungrad and BDMS are upgrading facilities and increasing bed capacity to capture the growing influx of foreign medical tourists.

Traditionally, patients from developing countries sought treatment in developed countries; however, the reverse flow of patients has been increasing in recent years. Nationality profiles of medical tourists are increasingly diversified, with more intensive promotional effort from top private hospital chains to capture affluent overseas patients. For example, Parkway Pantai leverages its international referral network to attract patients across Asia and the Middle East to its medical hub in Singapore, which provides customized inpatient and ancillary services such as visa application.

In summary, the medical tourism sector will remain an exciting space for private hospital players, although the proliferation and professionalization of private hospital chains in the region will also mean a tougher competition landscape in the future.

Challenges to growth in SEA's private healthcare provider landscape

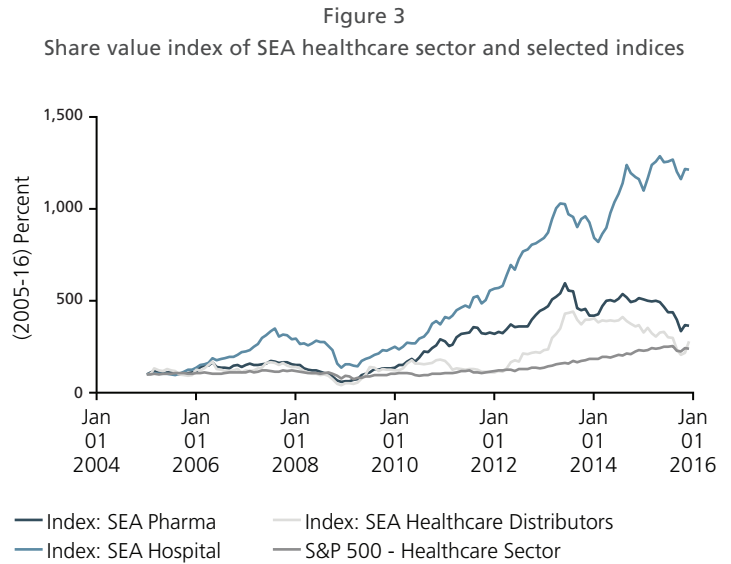
Key challenges in the provider landscape include high market valuations, inadequate supply of doctors and nurses, uncertainty over patients' willingness to pay, dilution of quality of care standards, and inability to provide cost-effective healthcare delivery.

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High market valuations. In SEA, the private hospital sector has outperformed other sectors in terms of share value growth over the past decade. Average valuation for SEA private hospitals stands at 24x EBITDA multiple or 60x PE ratio, which is high compared with hospitals in other regions (Figures 3-5). These high valuations mean that future investments will come at a premium, which may result in lower returns and longer payback periods if companies cannot maintain their growth trajectories.

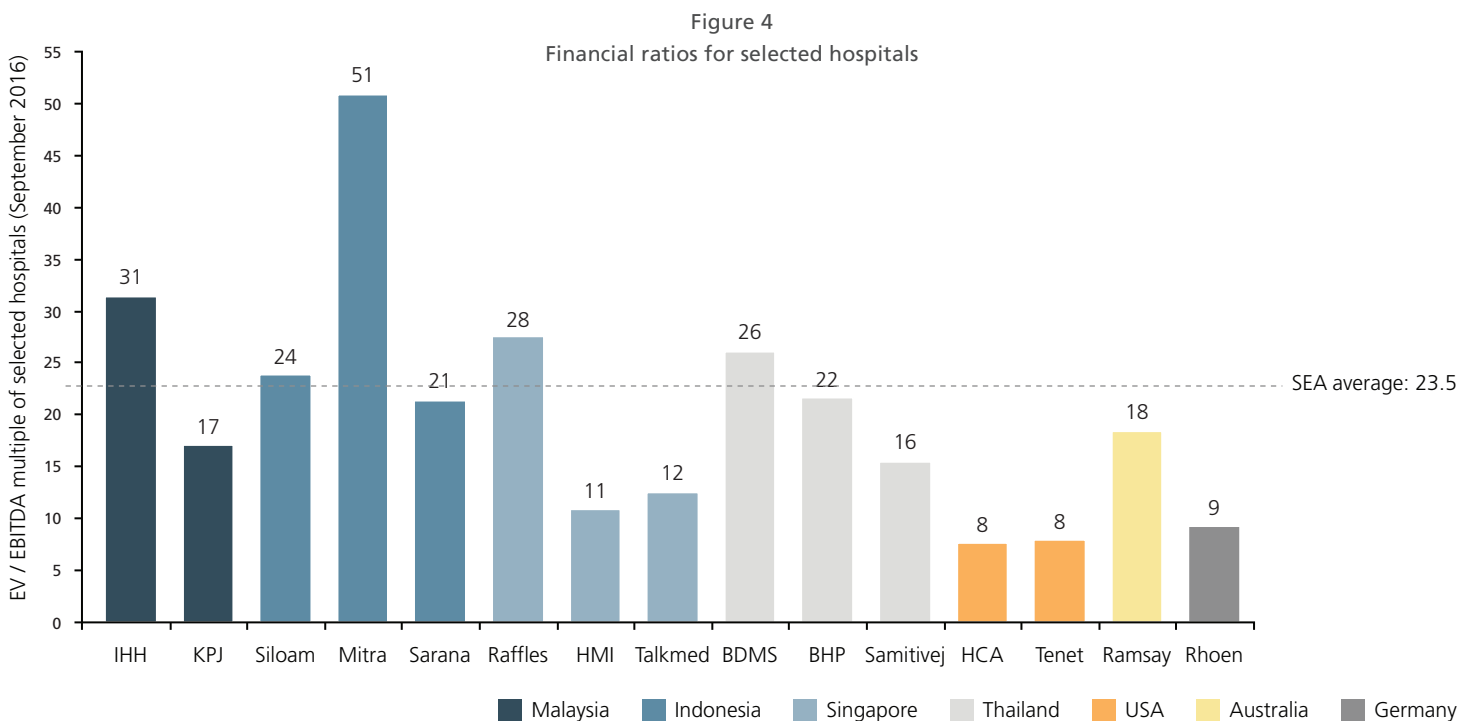
Investor optimism in the sector and increased M&A activity have contributed to the high valuation of existing healthcare providers. Over the past decade, the SEA healthcare sector witnessed almost 100 deals in the private provider segment worth almost US\$7 billion. Key players such as IHH, Siloam, BDMS and KPJ are acquiring or building capacity to capture potential growth across provider segments, while trying to gain economies of scale and scope. Several corporate and private equity investors, such as Mitsui & Co., CVC and Quadria Capital, have also been quite focused on and active in this sector in the region. Singapore, Malaysia and Thailand led the region as M&A hotspots, although this may change in the future subject to relative attractiveness in other countries and a more favorable foreign investment climate in this sector.

Limited supply of doctors and nurses. There is a shortage of doctors and nurses in the region, and local medical schools lack the capacity to meet the growing demand. Regulations, such as



Source: CapitalIQ

Thailand's local language requirements, may limit the entry of foreign doctors. Compared with the OECD average of over 30 doctors per 10,000 people, SEA countries have between two and 20 doctors per 10,000 people, with Indonesia being one of the big laggards in generating an adequate supply of physicians.



Source: Bloomberg

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Furthermore, physician reputation is a strong factor in patient choice, which will place a premium on acquiring experienced staff and drive up operating costs. Private healthcare providers may need to consider innovative solutions to fulfill staffing needs, such as telemedicine or exchange programs and collaborations with prominent doctors and institutions. For example, BDMS in Thailand has strong collaborations with M.D. Anderson Cancer Center and the Stanford University Department of Orthopaedic Surgery.

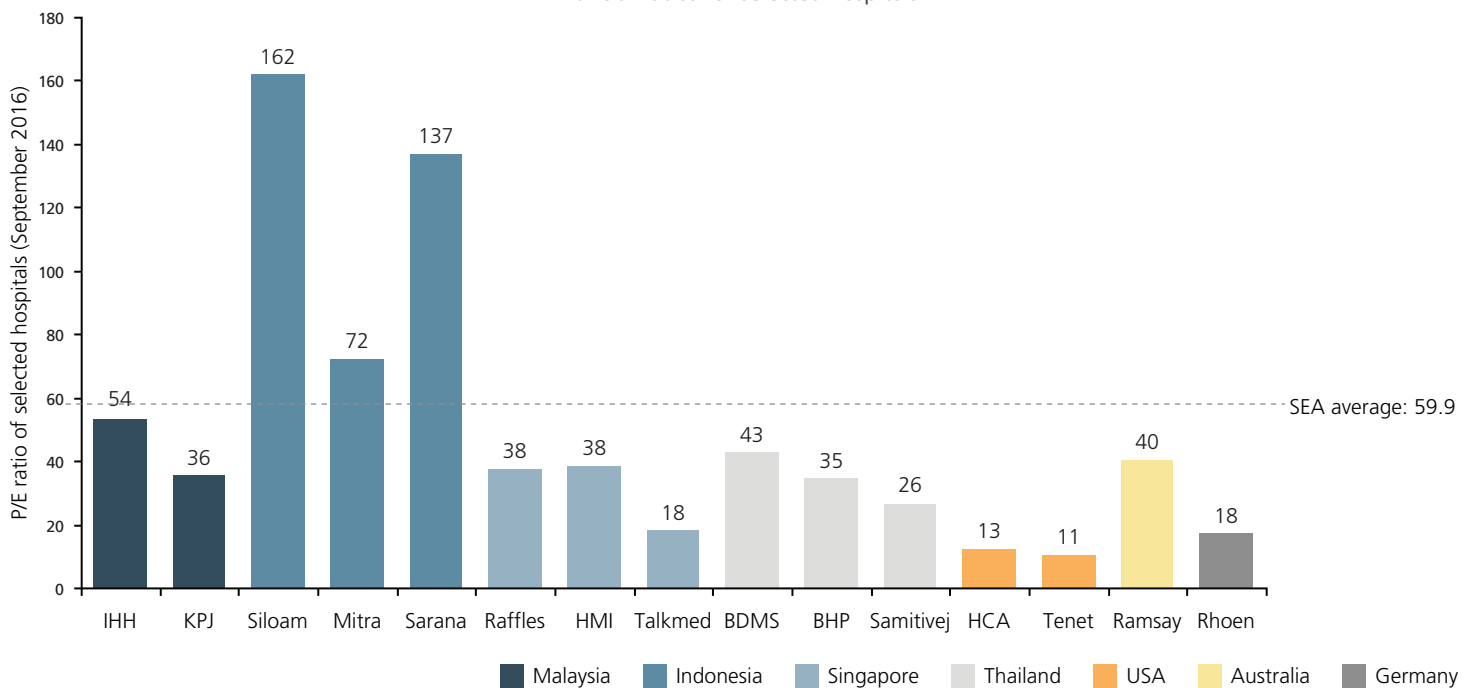
Patients' willingness to pay. Patients are becoming much better informed and more demanding in terms of the price and quality of service expected. Furthermore, differences in the cost of procedures between countries coupled with cheaper travel costs may drive patients away from their local healthcare providers to foreign providers that deliver a similar level of care at a more agreeable price. As competition intensifies in the region, providers must be able to create a rewarding patient experience with high-quality service.

Dilution of standards. As private healthcare providers add capacity, the quality of service and standards could become harder to maintain. Longer waiting hours, lack of medical attention and medical errors may diminish the hospital brand. The use of IT solutions, such as EMR and automated pharmacies, is becoming essential to maintaining high service and quality standards, but the high cost and integration issues may limit their adoption.

Cost-effectiveness. Stakeholders will need to evaluate their operations and performance to increase efficiency in the face of cost pressures. Government initiatives to limit healthcare costs and improve transparency have been launched in several SEA countries. For example, Indonesia's e-catalogue system lists the prices of all pharmaceuticals and medical devices registered in the country. Thailand uses e-procurement and e-tender processes to secure bulk medical supplies at discounted prices. Providers are shifting surgical procedures to day care and outpatient treatment to increase turnover and profitability; for instance, Malaysia's volume of cataract surgeries has shifted from 39% outpatient surgeries in 2002 to over 52% since 2010.

Private healthcare providers will also seek to reduce their costs without compromising service quality, such as by consolidating large orders and staggering supply deliveries to ensure sufficient on-site inventories. IT solutions will become increasingly essential for managing, coordinating and delivering quality, cost-effective healthcare. Even hospital suppliers will face pressure to find innovative solutions to remain competitive, such as shifting from product-focused offerings (e.g., syringes and needles) to customer-focused value-based solutions (e.g., insulin self-administering kits). Stakeholders are increasingly turning to IT-based solutions and value-chain solutions to gain and maintain a strong competitive advantage.

Figure 5
Financial ratios for selected hospitals



Source: Bloomberg

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Conclusion

The outlook for investments in the private healthcare provider landscape in SEA continues to be positive due to strong growth fundamentals, but investors need to be cautious of the issues, which may dampen their returns. The high valuations of private healthcare providers require that they continue to meet their growth targets in the face of mounting costs. These challenging growth targets will require providing access to and delivery of

better standards of care at competitive prices. This challenge will require incumbents and new entrants to focus on realizing greater cost efficiencies, demonstrate progressive management thinking to evolve the traditional business models and physician engagement models, leverage data and technology to enhance operations and quality of care, and engage increasingly in collaborative partnerships to deliver greater value and affordable healthcare.



About the Author

Zafar Momin is a Managing Director and Head of L.E.K.'s Southeast Asia practice. Zafar has over 25 years of experience in strategy consulting and industry. He has provided strategic advice to a wide range of clients on strategy, operations, marketing & sales, mergers & acquisitions and performance improvement.

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