



SARASIN

Emergency – Healthcare in Emerging Markets

October 2011



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Summary

Health plays a pivotal role in sustainable development. Emerging markets and developing countries have a lot of catching up to do in the area of public healthcare. This is confirmed in the United Nations' Millennium Development Goals. In most emerging market countries (see Chapter 1 for a definition) the coverage provided by health insurance schemes is inadequate. Patients either have to pay a large proportion of the costs themselves or have to rely on a public health system that is often not yet up to standard. The situation is made worse by the fact that even as economies continue to flourish, populations are growing older and civilisation or "lifestyle" diseases are on the increase.

Two factors are helping to improve the situation in emerging markets: an expanding middle class who can afford to spend more on healthcare, and a higher level of investment by governments in public health services. The Chinese government, for example, has set itself the goal of improving the level of basic healthcare. While only 20% of the Chinese population were covered by basic health insurance in 2005, this figure had already risen to 92% by 2009.

Healthcare companies working in the areas of pharmaceuticals, health services and medical technology stand to benefit from soaring demand. Local providers enjoy advantages over their competitors from industrialised nations because their products (such as generics) are well adapted to local conditions and they also receive preferential treatment from governments in some cases. The key advantages of providers from mature economies, however, are the quality of their products and their very strong brand recognition. Companies from emerging markets still need to close this gap. Their success depends on skilful management of both opportunities and risks. Some of these lie in the environmental, social and governance (ESG) domain. Issues such as quality assurance, product efficacy/tolerability, business ethics (corruption, etc.), working conditions and health & safety in produc-

tion are particularly relevant for healthcare companies in emerging markets – as they are for most companies.

Emerging markets will account for half of global growth in demand for pharmaceutical products in the period up to 2015. These markets tend to be dominated by local generics. Manufacturers of generics, such as South Africa's Aspen or India's Dr. Reddy's, have performed well in our sustainability analysis. In China, traditional Chinese medicine (TCM) is very important, and the dominant player here is China Shineway. Demand for medical technology is increasing as well, but so far we have not been able to identify a company from an emerging market with an adequate sustainability rating. Operators of hospitals and providers of laboratory services are also major beneficiaries of the ongoing expansion of healthcare. Life Healthcare from South Africa and DASA from Brazil are key players here.

Emerging markets have a lot of ground to make up

Improving healthcare provision in developing and emerging market countries is a key objective of sustainable development. The situation is improving in emerging market countries because the expanding middle classes can increasingly afford to pay for healthcare. The poorest sections of the population have to rely on a state-funded healthcare system. Many governments are having to increase available budgets, partly because the population is already growing too old in most emerging market countries, and lifestyle diseases are becoming more widespread.

Inadequate level of healthcare

Health plays a key role in sustainable development. Both emerging and developing economies urgently need to improve their health situation. This is also covered by the United Nations' Millennium Development Goals. Three of the eight goals to be achieved by 2015 are directly related to health.

Fig. 1: UN Millenium Development Goals (extract)

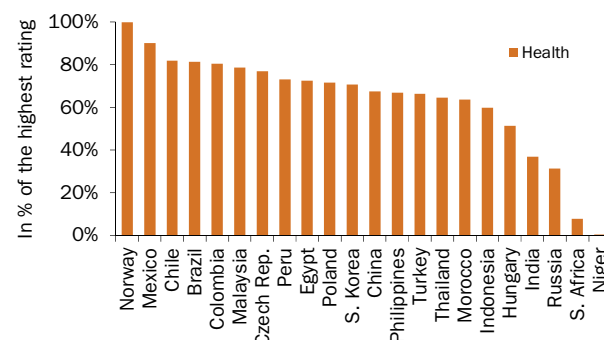
REDUCE CHILD MORTALITY	Reduce by two thirds, between 1990 and 2015, the under-five mortality rate.
IMPROVE MATERNAL HEALTH	Reduce by three quarters the maternal mortality ratio. Achieve universal access to reproductive health.
COMBAT HIV/AIDS, MALARIA AND OTHER DISEASES	Have halted by 2015 and begun to reverse the spread of HIV/AIDS. Have halted by 2015 and begun to reverse the incidence of malaria and other major diseases.

Source: UN

This study looks at the situation in emerging markets such as Brazil, India and China. Their economic progress is already at a far more advanced stage than developing countries and a further improvement in healthcare can be achieved through the combined efforts of the state, the private sector and consumers. Poorer economies, i.e. developing countries, mainly have to rely on outside support in this area. The results of the sustainability analysis performed by Bank Sarasin on sovereign states¹ show that newly industrialised economies like Russia, China and

South Africa perform much better in the field of healthcare than developing countries (represented by Niger in the next chart), but still lag behind industrialised nations (represented by Norway in the next chart). Indicators studied here include child mortality rates, life expectancy, life satisfaction and suicide rates.

Fig. 2: Sarasin's national healthcare ratings (2006)



Source: Sarasin

The significant gap between developing countries underscores the fact that even a fairly well-developed level of basic healthcare (as provided in most newly industrialised economies) produces a significant improvement. Child mortality rates are around three for every 1,000 newborns in Norway, for example, compared with six in Poland, 25 in Indonesia and 83 in Niger. It takes a lot of time and money to keep on narrowing the gap with the position of the western world. Latin America has some of the best emerging market countries when it comes to healthcare, led by Mexico, Chile and Brazil. All three have had a comparatively well-developed healthcare system for

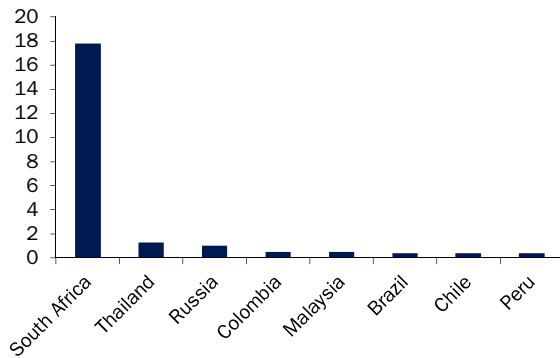
¹ The world in a dilemma between prosperity and resource protection, Bank Sarasin, March 2010

Emerging markets have a lot of ground to make up

some time now, and above all enjoy a high level of life satisfaction.²

These countries still face a number of challenges in the further development of their healthcare systems. In most emerging markets the level of cover provided by health insurance schemes is inadequate and patients therefore have to pay a large portion of their treatment costs themselves, if they can actually afford to. Infectious diseases are particularly relevant here. Some countries have been very badly affected by HIV/Aids. This is the biggest problem facing South Africa's healthcare system, for example.

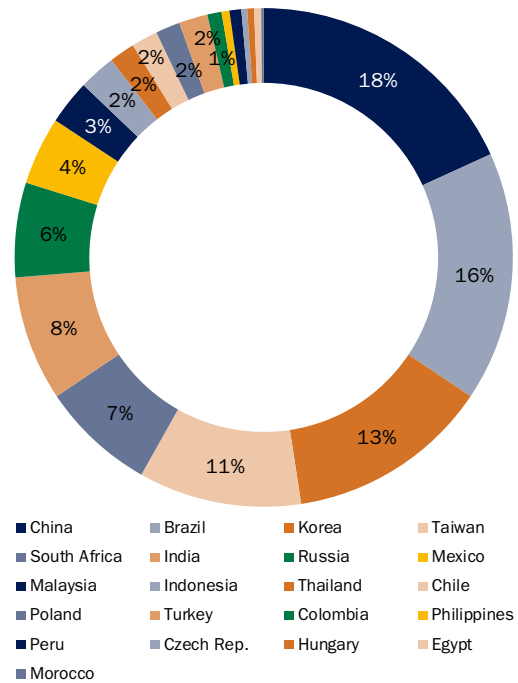
Fig. 3: Prevalence of HIV, total (% of population ages 15-49)



Source: World Bank

When referring to emerging markets in this study, we use the same definition applied for the country composition of the MSCI Emerging Markets Stock Indexes. Apart from the standard of prosperity, measured by per capita national income (USD 1,000 - 12,000) this also takes into account the accessibility of national capital markets to investors, as well as market capitalisation. For this reason, a number of countries with higher incomes also fall into the category of emerging markets according to the MSCI system.

Fig. 4: Capitalisation quotas of countries in the MSCI³ Emerging Markets Index (08/31/11)



Source: MSCI

Demand for healthcare rising due to ageing populations...

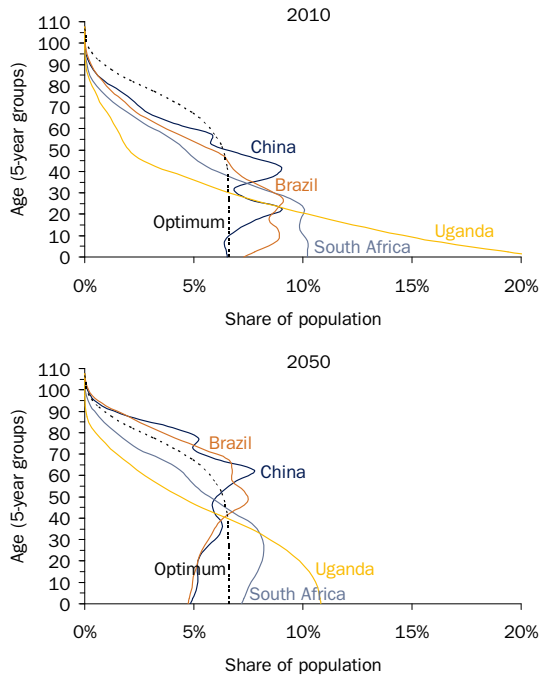
Demand for healthcare is set to rise. As in industrialised nations, the average age of the population in some emerging markets will shoot up over the next few decades. The best way to examine the age distribution of a specific population is by means of an age pyramid. The ideal structure is the beehive shape (the optimum line in Fig. 5), where the population figure remains constant over time.

² The independent think-tank "the new economics foundation (nef)" measures individual life satisfaction based on a number of global surveys.

³ Morgan Stanley Capital International (MSCI) is a US financial services group which calculates and publishes numerous international stock indexes.

Emerging markets have a lot of ground to make up

Fig. 5: Age distribution in national populations (2010 and 2050)



Source: United Nations, Bank Sarasin

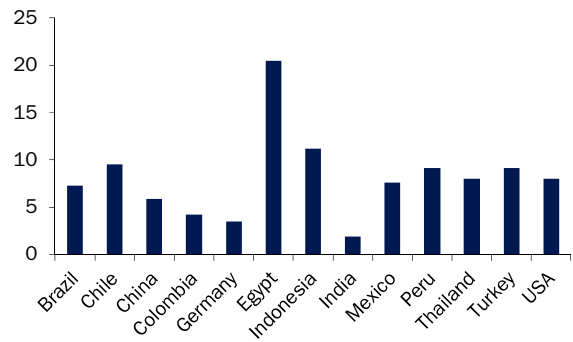
Although Brazil's population has a relatively low average age at just 29, for example (compared with 37 in the USA and 40 in Europe), it is actually ageing at a faster rate than the global average. The number of Brazilians over 65 will increase by more than 40% during this decade. This is likely to result in a one percent increase in annual healthcare spending. In China the trend is extreme mainly because of the one-child policy. China's rate of population growth has fallen sharply over the last decade and the proportion of old people will climb significantly over the next few decades. There is no sign of the government relaxing its one-child policy. Russia's population is actually shrinking and has a very high proportion of senior citizens. Only India's population continues to grow. It is estimated that the number of Indians of working age will rise by around 300 million over the next 25 years.

... and lifestyle diseases

As economies develop, people's lifestyles are changing as well. One in ten people are now reported to be diabetic in China – the same level as in the USA. The rate is similar in the urban regions of India, and is around 3% of the population in rural areas. Overall this equates to some 40 million diabetics in India, the highest figure of

any country in the world. One of the causes is obesity. In many emerging market countries obesity in the under-fives has now reached similar levels to the USA. Even in India, the incidence of cardiovascular disease is forecast to double over the period 2000 to 2015. Healthcare systems in these countries are not yet equipped to cope with the spread of these lifestyle diseases.

Fig. 6: Prevalence of overweight (% of children under 5)

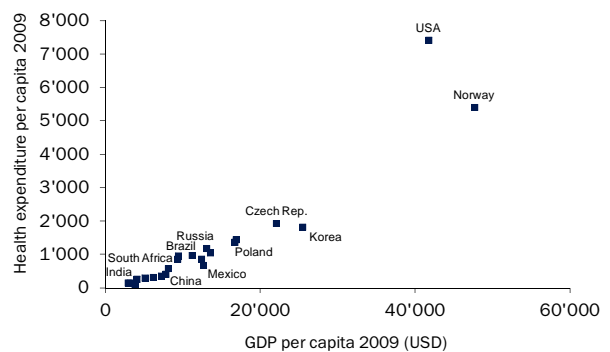


Source: World Bank (latest available year)

Middle classes invest in health

Most emerging market countries are seeing a rapid expansion of their middle classes. According to the World Bank, the middle classes will grow by more than 800 million people by 2030, with half of them living in China and India. The same trend can be observed in Latin America, where the middle classes have grown significantly since 2003 and now make up around 50% of the population. In Brazil alone, the economic success of the past seven years has enabled around 30 million people (15% of the population) to join the middle classes.

Fig. 7: Health expenditure per capita vs. GDP per capita (purchasing power parity in USD)



Source: World Bank

Emerging markets have a lot of ground to make up

Higher disposable incomes generally mean higher healthcare budgets as well. More spending on health will also shift the focus of treatment towards chronic conditions such as cardiovascular disease, diabetes and cancer.

Governments are expanding public healthcare

In contrast to the middle classes, poorer sections of the population will benefit above all from the increased spending on public healthcare. The biggest emerging economies are stepping up their healthcare spending (as a percentage of GDP) towards the same level as in industrialised nations. In China and India this figure is still only around 4%, compared with 5% in Russia and 8% in Brazil. Among the various emerging economies, eastern European countries and South Korea have the highest level of healthcare spending (not surprisingly). The average for countries with higher incomes is around 11%.

China wants universal healthcare

The Chinese government has set itself the target of significantly improving the level of basic medical care for all its citizens. While only 20% of the Chinese population were covered by basic health insurance in 2005, this figure had already risen to 92% by 2009. The target is universal healthcare for all by 2020. Government spending on public health is therefore predicted to rise by around 20-25% p.a. in the coming years. Even if there are phases of slower economic growth, spending plans are unlikely to be significantly affected as the government sees the improvement of healthcare provision as making a vital contribution towards maintaining social harmony.

Brazil can afford to spend more

Brazil's healthcare sector should enjoy dynamic growth over the next 10 years as well. Predicted annual growth rates in the region of 10-12% will be driven mainly by an increase in private health insurance, higher disposable incomes and more people in employment and also in retirement. Per capita spending over the period 2003 to 2007 showed a high annual growth rate averaging around 10%. The public health system has been in place since 1988, but is in need of an overhaul due to poor efficiency. Basic health services are provided, but do not cover drug treatment, except in hospitals. Patients with private health insurance enjoy a much better level of service, and therefore more effective treatment as well. In Brazil the mortality rate of citizens with no private insurance is

roughly twice as high as for privately insured patients for most types of disease.

South Africa: the sick patient

South Africa is afflicted by numerous contagious diseases, especially tuberculosis and HIV. 50% of all deaths are attributable to Aids. According to the World Health Organization (WHO), the impact of disease on South Africa is four times greater than in industrialised countries and twice as bad as other emerging market countries. There are plans to introduce health insurance for the entire population, but it is still unclear how this will be funded and what shape it will take. However, the government has put incentives in place to help promote low-cost health insurance schemes. Over the past three years the number of South Africans with private insurance has increased by 4%. Any improvement in the healthcare situation in South Africa also requires more effective prevention.

Indians pay most of their own healthcare costs

In India the state provides basic healthcare which is available to everyone free of charge. However, the system has not been sufficiently developed yet, which means that private hospitals still carry out more than half of the medical treatments. Less than 5% of the population have health insurance, and people tend to pay the bulk of their treatment costs out of their own pocket. A basic level of healthcare was introduced in 2007 to improve the situation for families under the poverty line. This covers the most important treatments, but not any medicines required.

Conclusion

The level of medical care in most emerging economies is far from adequate. In recent years, however, the trend has moved in the right direction thanks to a growing middle class and higher levels of government spending on public health. This is positive news for more sustainable development and crucial for maintaining and improving social harmony within these countries. At the same time markets for medical products and services are growing.

Sustainability of healthcare companies

Bank Sarasin applies industry-specific indicators in order to assess the environmental, social and governance aspects of companies. The main emphasis in the healthcare sector is on issues such as quality and efficacy of medical products, as well as ethical business practices, such as in the area of marketing. Companies taking a progressive approach to these issues are able to minimise risks and gain competitive advantages. In the Sarasin sustainability analysis, emerging market healthcare companies are compared with their global competitors.

Sustainable corporate governance reduces risks

Companies stand to benefit from the growing demand for healthcare products and services in emerging economies. Their success depends on skilful management of both the opportunities and risks. Some of these risks lie in the environmental, social and governance (ESG) domain.

trialised nations. We expect emerging market companies that take a progressive attitude towards environmental, social and governance aspects to be best positioned to close the gap with their western counterparts.

Fig. 8: Sustainability risks for the healthcare sector

Sustainability topics	Risks
Quality, efficacy and tolerance of products	<ul style="list-style-type: none"> • Delayed or denied approval • Product recalls • High compensation claims for damages • Brand damage
Cost/benefit ratio of products	<ul style="list-style-type: none"> • Low acceptance by health insurance companies, special health authorities (e.g. NICE in the UK and IQWiG in Germany) etc.
Quality and safety in production processes	<ul style="list-style-type: none"> • Production stoppages by regulatory authorities • Damage to facilities and the environment, and health risks for employees due to faults and accidents • Loss of revenue
Marketing practices (advertising, pricing, etc.)	<ul style="list-style-type: none"> • Fines and settlements for illegal methods • Loss of customer confidence • Greater regulatory pressure
Competitive behaviour	<ul style="list-style-type: none"> • Fines imposed for corruption, price fixing, etc.
Access to medicines in developing countries	<ul style="list-style-type: none"> • Damage to reputation • Compulsory licensing by governments
Working conditions	<ul style="list-style-type: none"> • High staff turnover rates • Difficulty recruiting staff • War for talents
Energy and water efficiency	<ul style="list-style-type: none"> • Costs inflated by high energy prices • Production locations in regions with water shortages

Source: Bank Sarasin

Sustainability risks present a challenge for the entire healthcare sector, but their relevance to emerging markets can occasionally be rather different. For example, quality assurance or corruption are important themes. Reputational risks and brand value are also becoming more relevant for healthcare companies in emerging markets. They are in direct competition with Western companies that have invested substantial amounts in building up quality assurance systems and strong brands. For many consumers in emerging markets, this is precisely a key argument for favouring branded products from indus-

Good quality and efficacy are essential

Because the level of healthcare is inadequate in most emerging and developing countries, any expansion at all in healthcare provision produces immediate social benefit. But quality, efficacy and tolerability are clearly vital aspects here. Comprehensive quality assurance systems are necessary, and manufacturers based in emerging markets often have room for improvement in this area. Quality problems have arisen with Chinese pharmaceutical companies in recent years, for example. Companies who already engage in export tend to be more advanced in the field of quality assurance. For example, they must satisfy criteria imposed by the FDA, America's drug approvals authority. But approval bodies in emerging markets are also starting to raise their quality standards and are paying far greater attention to the cost/benefit relationship. Private providers can also excel in the area of healthcare services (hospitals, etc.). Improvements come from quality management systems which encourage the systematic training of staff and benchmarking.

Fig. 9: Subsectors of the healthcare industry

Medical technology
Equipment and devices (e.g. cardiovascular, orthopadics, diagnostics), and also consumables such as syringes, bandages, etc.
Healthcare services
Hospitals, nursing homes, etc., as well as dialysis units, laboratory services, etc.
Distributors and wholesalers of products, as well as IT services
Pharmaceuticals and biotechnology
Drug development, manufacture and marketing
Products based on genetic analysis and manufacture (mostly protein-based therapy)
Analytical tools, instruments and consumables

Source: MSCI

Price level is important for emerging markets

Affordability is an important factor for emerging economies especially, in order to assure the availability of the products and services to low-income sections of the population. This is even more important given the fact that most patients have to pay the bulk of their medication costs themselves. Manufacturers in emerging economies are focused on these markets and are therefore attuned to local conditions when it comes to pricing. They are able to benefit from lower production costs than companies based in industrialised nations. Generics are a good example: manufacturers in emerging countries have built up a strong market position here. In the export business too, generics produced especially by Indian companies have managed to capture a significant market share in the USA, for example. Western companies have to slash their product prices in order to establish a foothold in emerging markets. Some of the big drug manufacturers in industrialised countries are now fulfilling their social responsibility by offering medicines to treat mainly infectious diseases such as malaria, tuberculosis and HIV at cost price in emerging markets and by conducting research into what are generally known as "neglected diseases".

Corruption still rife

To ensure a healthcare market develops properly, special attention needs to be paid to prevent corruption (bribing doctors, hospitals, etc.) and price fixing. Corruption is rife in the healthcare sector, as confirmed by the NGO Transparency International. The European Healthcare Fraud &

Corruption Network claims that even in the European Union around 6% of national healthcare budgets are lost to corruption and fraud; this figure is most probably significantly higher in emerging markets. In China, for example, corruption can restrict the ability of the pharmaceutical market to function efficiently. Chinese hospitals are the most important sales channel for medicines and finance themselves to a large extent from the sales commissions they are paid. Pharmaceutical companies generally employ a lot of sales people to boost their turnover. More efforts are now being made globally to try and fight corruption. Indian authorities are also working on the introduction of a new code of conduct to combat the spread of unethical marketing methods in the pharmaceutical industry. This includes, among other things, a ban on expensive gifts to doctors and restrictions imposed on sponsored conferences, etc. Some Western companies already have their own experiences in industrialised nations and in some cases have been obliged to pay out significant amounts in fines and settlements. When examining the sustainability credentials of companies, we focus on the measures they take in the area of business ethics. This includes, for example, the existence of a code of ethical business conduct instilled in employees through appropriate training measures. Or whether violations can be reported internally and anonymously ("whistle blowing"). In addition, a check is made on companies' potential transgressions in this area in the past.

Cost savings through energy efficiency

Especially in the pharmaceutical industry, environmental protection has a significant impact on companies' sustainability. Manufacturing drugs is a very energy- and water-intensive business due to the complex processes involved and the rigorous hygiene standards. Cost savings are also possible in this area by systematically improving efficiency. Water consumption is particularly relevant for emerging markets. Pharmaceutical production sites located in arid zones need to pay special attention to water consumption and supply. When it comes to environmental protection, safety is also a key aspect. Apart from the potential consequences for the environment and for employees' health, malfunctions and accidents (e.g. fires, etc.) can also result not only in production stoppages but also the imposition of tougher regulations and penalties by the supervisory authorities. In the production of medical technology, where outsourcing is common, environmental guidelines are particularly important for suppliers.

Sustainability of healthcare companies

Environmental standards often tend to be comparatively low in emerging markets in areas such as wastewater, waste disposal, etc.

Environmental aspects are also relevant for the provision of health services. Improving the energy efficiency of hospitals, for example, can reduce operating costs by as much as 5%. No specific data is available for emerging markets, but in Germany consumption levels per hospital bed are in the region of 8000 kilowatt hours (kWh) of electricity and 25,000 kWh of heat every year. This works out at roughly 3500 euros per bed or, to put it differently, the typical annual heat consumption of two modern detached houses. Around 40% electricity and 32% heat savings are possible, depending on the situation. An efficient waste disposal system is also essential for any well-managed hospital. It is especially important to make sure that any waste disposal contractors are carefully monitored. A few years ago there was a public scandal in South Africa when medical waste was illegally dumped.

Nursing staff in short supply

Working conditions are an important aspect of sustainability and can significantly influence the work rate of employees, and moreover their motivation to work. Given the shortage of qualified nursing staff, it is becoming increasingly important to be an attractive employer. This is a pressing issue in hospitals and dialysis units not only in industrialised but also emerging countries, such as the USA and South Africa, for example. America is trying to tackle this shortage by recruiting nursing staff from emerging countries, but this in turn makes the local employment situation more difficult in those markets. One of the main reasons for the shortage of staff tends to be the tough working conditions: long and irregular working hours, poor pay and recognition, and time pressure. For companies providing healthcare services, recruiting and retaining qualified staff is therefore a top priority, and employers offering good working conditions have a competitive advantage.

Corporate governance generally poorer

Another important issue for emerging market investors is corporate governance, which is also assessed as part of the sustainability analysis process. In general, however, it is still at a less advanced level than in industrialised countries. Since the financial crisis at the end of the nineties in Asia and Russia, more attention has been

paid to this issue in emerging markets. According to the Asian Corporate Governance Association, however, only Taiwan and Thailand have made significant progress in the area of corporate governance. The best performers are Hong Kong and Singapore, if they qualify as emerging markets. The rankings are summarised in Fig. 10. This shows how many marks are needed in order to reach an excellent score (meeting 80% or more of the requirements).

Fig. 10: Corporate Governance Ranking ACGA

Country	Score in % 2010	Gap to Benchmark (80%)
Singapore	67	(-13)
Hong Kong	65	(-15)
Taiwan	55	(-25)
Thailand	55	(-25)
Malaysia	52	(-28)
India	49	(-31)
China	49	(-31)
Korea	45	(-35)
Indonesia	40	(-40)
Philippines	37	(-43)

Source: Asian Corporate Governance Association/CLSA

Key themes in a governance analysis include ownership structure / controlling shareholders, voting rights, independence of the board of directors, government influence, takeover rules, accounting standards, etc.

Conclusion

The most important sustainability aspects for healthcare companies in emerging markets include quality assurance, pricing, business ethics (corruption, etc.), environmental protection, working conditions and corporate governance. A proactive and systematic approach to these issues is the sign of a well-managed company. It helps to improve efficiency and competitiveness. It enables companies to participate in the long run in the growing importance of healthcare markets in emerging regions. Sustainability analysis allows investors to systematically incorporate these aspects into their investment decisions.

Healthy investment opportunities

Linking together the themes of emerging markets and healthcare makes sense as far as sustainable investments are concerned. Investment opportunities and social benefits go hand-in-hand. The improvement of healthcare provision in emerging markets increases demand for healthcare products and services, particularly among local providers. Since on average less attention is still being paid to sustainability aspects in emerging market companies, it is more difficult to identify companies that meet high sustainability standards, however. But exceptional opportunities present themselves to the handful of progressive companies in this area, as they stand out from the competition.

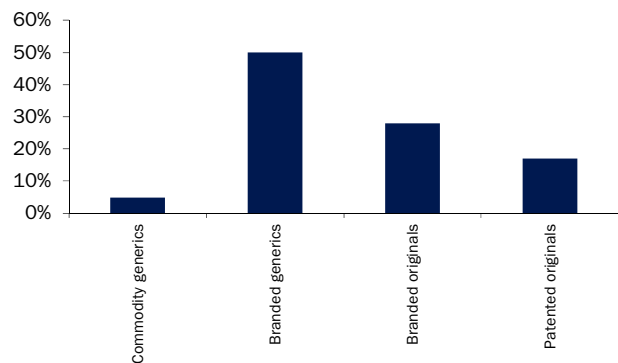
Dynamic pharmaceutical industry

The healthcare industry has changed significantly in emerging markets in recent years and is about to undergo further radical changes. Demand is soaring: according to Deutsche Bank estimates, emerging markets will account for half the growth in global demand for pharmaceutical products up to 2015. Half of this will come from BRIC countries. China is the biggest market here, and is predicted to grow by around 25% per year according to IMS Health. As mentioned previously, changes in China are being driven by the rapid pace of economic growth and the associated rise in disposable incomes, the reform of the healthcare system, the ageing population and relentless urbanisation. To keep costs down, governments are particularly keen on generics, but more innovative pharmaceutical products will become more widespread as healthcare systems gradually improve.

Who benefits from this growth? Western and Japanese drug companies active in emerging markets, to some extent. They have a broad product range and an excellent reputation for quality. However, their success is constrained by a number of factors: prices need to be set lower than in most industrialised countries, locally required clinical tests (as in China) inflate costs, reimbursement is often limited to domestic products and – last but not least - emerging markets are dominated by local generics. The cost awareness of governments in emerging markets can also be seen when setting the prices for drugs (including generics). The Chinese government, for example, has recently cut prices several times as part of its campaign to combat inflation. The Turkish authorities are following a similar course, and drug prices in Turkey are already some 30-50% less than the lowest prices in Europe. Nevertheless, emerging mar-

kets are still very attractive due to their growth potential. Domestic pharmaceutical companies have for the most part grown more quickly in recent years than the activities of Western multinationals in emerging markets.

Fig. 11: Pharmaceutical markets in emerging regions



Source: DB, IMS Health, Astra Zeneca

In developed markets such as the USA generics are most common, while branded generics dominate emerging markets. In the latter markets, patients prefer brands they are familiar with and which they believe to be of better quality. Sales reps working for drug companies try to convince doctors, who write the prescriptions, about the benefits of that particular brand. In the case of non-branded generics, the focus is on the pharmacists.

India is the world's biggest generics producer, but most of the products are destined for export. The most important sales markets are the USA, Russia and South Africa. Activities in Latin America and Eastern Europe are being expanded. The domestic market has only gained in importance in the last few years. Our analysis of indian

Healthy investment opportunities

company **Dr. Reddy's Laboratories**, for example, produced a comparatively good sustainability rating. The company has a strong sustainability management system which covers relevant issues from environmental protection to access to medicines. To improve the latter, Dr. Reddy's entered into a partnership with GlaxoSmithKline (GSK). GSK has access to Dr. Reddy's portfolio and future pipeline of more than 100 branded pharmaceuticals and will develop and market products across emerging markets. The company has room for improvement in occupational safety, there were a number of fires in production facilities lately. In South Africa, the pharmaceutical company **Aspen** is the biggest producer of anti-retrovirals. In addition Aspen is helping to improve the supply of drugs in Africa by distributing GSK medicines. **Adcock Ingram** also achieved a good sustainability score. South Africa's second-biggest generics producer likewise makes an important contribution to improving the provision of medicines. It also launched a comprehensive environmental protection programme in 2010.

In China, traditional Chinese medicine (TCM) is very relevant and accounts for around a third of the market. TCM plays an important role in preserving traditional medical knowledge. The TCM sector is still very fragmented and there have repeatedly been quality problems in recent years among manufacturers. The government has therefore set itself the goal of modernising the TCM industry. Amongst other things, manufacturers have been required to comply with GMP criteria⁴ since 2008. Many smaller manufacturers have difficulty meeting these criteria, and in the past corruption has also been a barrier to their effective implementation. This presents an opportunity for larger manufacturers who have the necessary resources and know-how. They include **China Shineway**, the biggest manufacturer of injectable TCM medicines. It was also the first TCM company to introduce a certified integrated quality (ISO 9001), environmental (ISO 14001) and occupational health & safety management system (OHSAS 18001).

Fosun Pharma is a classic pharmaceutical company from China that meets relatively high environmental and social

standards. Fosun develops and manufactures drugs for the treatment of hepatitis, diabetes and TB, among others, and also produces medical technology. Fosun is the first Chinese pharmaceutical company to have published a sustainability report (2009). Fosun Pharma makes an important contribution to developing countries, where it supplies the WHO with malaria drugs, amongst other things. Over the past two years there have been no reports of corruption either at Fosun Pharma or China Shineway.

In Latin America, the Mexican company **Genomma Lab** performed well in our sustainability analysis. It is Mexico's biggest producer of over-the-counter (OTC) medicines and is also active in personal care products. Genomma is working to roll out the recently introduced ISO Standard 26000 for corporate social responsibility and imposes comprehensive environmental and social requirements on its suppliers. This is particularly relevant, since Genomma has outsourced its entire production to third-party contractors.

Demand for equipment growing as well

Although not as big as pharmaceuticals, medical technology is still an important market. The trend towards local producers is particularly relevant for companies in emerging markets. In China, for example, over 80% of medical products were still being imported back in 2003, but this figure had already fallen below 50% by 2009. Manufacturers of medical equipment, instruments and devices stand to benefit from the systematic expansion and new construction of hospitals in China. Unfortunately there is very little systematic implementation of environmental and social standards by companies active in this segment. Because of this, none of the medical technology companies based in emerging markets have so far achieved an adequate sustainability rating. Initial signs of a more systematic approach can be seen in the Chinese company Mindray, however.

Services need to be expanded

Emerging markets have a lot of catching up to do in the use of diagnostic services. Diagnostics help to improve the efficacy and efficiency of the subsequent medical treatment. Laboratory services are still a very fragmented market at present, but some providers, such as Brazil's **DASA**, are growing through acquisitions and are trying to build up strong brands. DASA is Brazil's biggest laborato-

⁴ Good Manufacturing Practice (GMP) sets down guidelines for quality assurance in the production processes and the production environment for the manufacture of medicines and active ingredients. Relevant guidelines have been passed by both the EU and the US FDA, for example.

ry services company, with a market share of 12%. DASA has a quality management system certified to ISO 9001 and there have been no significant negative headlines concerning quality during the past two years. The company also takes a very systematic approach to environmental protection (ISO 14001) and offers good working conditions.

Hospital operators are also key beneficiaries of the expansion of healthcare provision. This is particularly the case in South Africa, where health insurance is being extended and there is substantial demand due to high infection rates as a result of HIV/Aids and tuberculosis, among other diseases. The state healthcare system is not capable of mastering these challenges on its own. Although the private healthcare sector covers just 16% of the population, it receives some 50% of spending on healthcare. **Life Healthcare** is very well positioned. The company owns 62 hospitals in South Africa and has a very strong track record in the areas of cost efficiency and quality. With many health insurance schemes, patients are only allowed to use approved hospitals. Life Healthcare is very well established and covers around 45% of these policyholders.

Early movers have achieved a high level

The companies mentioned which have scored well in Bank Sarasin's sustainability analysis have been most successful in integrating sustainability aspects into their business activity compared with other healthcare companies in emerging markets. These companies are still very limited in number. This is essentially because the concept of sustainable development in business, politics and society is still not particularly widespread.

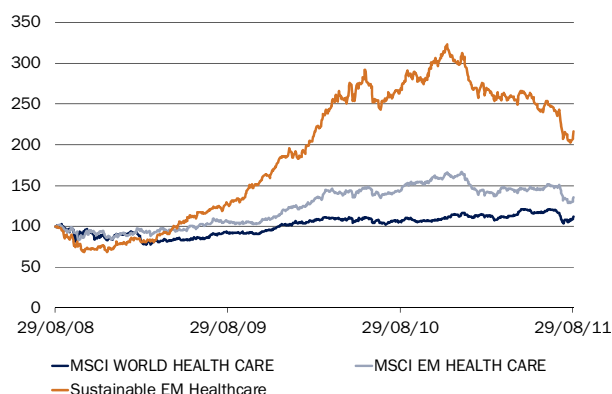
Given the growing importance of environmental and social risks, as well as the opportunities available in the healthcare sector when it comes to sustainable development in emerging markets, sustainability analysis is a useful tool for identifying high-quality companies. Companies willing to give systematic consideration to environmental, social and governance aspects enjoy a farsighted management style that focuses on quality. This enables them to participate more effectively in the changes which the healthcare sector is undergoing in emerging markets.

Good performance over the past three years

Viewed retrospectively, the inclusion of sustainability criteria would have had a very positive impact. The share

prices of the companies covered by our sustainability analysis have performed very well. Back testing over the past three years shows that they have comfortably outperformed the relevant benchmark indices⁵.

Fig. 12: Performance of selected titles vs. MSCI World Healthcare and MSCI EM Healthcare



Source: Bank Sarasin

Over the period 31 August 2008 to 31 August 2011, the shares (equally weighted on a USD basis) produced a gain of 117% on average, while the MSCI World Healthcare Index increased by 12% and the MSCI Emerging Markets Healthcare Index by 35%.

⁵ Back testing is based on the share price performance of Aspen Pharmacare, DASA, Fosun Pharma, China Shineway, Genomma Lab, Adcock Ingram and Dr. Reddy's. The orange line represents their average equally weighted performance. Life Healthcare could not be taken into consideration, as the company only listed on the stock market in June 2010. The calculation does not take into account any transaction costs, management fees and issuing commissions for investment products.

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