

The Healthcare market in Brazil

Brazilian Healthcare market: one of the most promising and attractive in the world



Context

Fifth largest country in area and population, with 8.51 million square kilometers and about 196 million inhabitants, Brazil recorded in 2012, a Gross Domestic Product (GDP) of US\$ 2.2 trillion, the seventh largest on the planet. Market estimates indicate that, in this decade, the country may be consolidated as the fifth largest global economy.

For almost two decades the country has been undergoing a process of economic stabilization which ensured tremendous social advances to Brazilians. Most notably, for over two years national unemployment rate hovers around 5% of the economically active population, which represents, in the view of many experts, a situation of full employment. This improvement is also reflected in rising wages and escalating consumption, boosted by strong credit growth combined with lower interest rates and government tax incentives for durable goods, the white line, automobiles and construction.

That meant, over time, an amazing and positive process of development and social evolution, which allowed the entry of 40 million Brazilians into the middle class, strongly boosting the consumer market. In 2012, consumption of 194 million Brazilians accounted for 61% of the national GDP, and even in a year of recovery from the effects of the

global financial crisis - intensified in Europe - the Brazilian territory was the main destination for direct foreign investment in Latin America, receiving \$ 65.3 billion.

Brazil has a fast growing consumer market, positioned in several segments as one of the largest in the world. The power of its domestic market in consumer goods and services has been particularly promising in the healthcare and pharma industries.

Based on those macroeconomic indicators an outlook for the Brazilian healthcare industry is also optimistic, considering the market growth drivers listed below:

- purchasing power increase
- new entrants into the emergent middle class
- consumers are willing to pay for better healthcare services/treatment
- favorable demographic conditions
- increasing elderly population
- government initiatives attract investments
- consolidation driving strategic movements

Our vision

Understanding the Brazilian healthcare market as complex, asymmetric, fragmented, with high demand, and government involvement/support, amongst others, may be a starting point to better understand the opportunities and challenges to whom intends to be, or is already part of it.

The drivers of demand mentioned above together with strong government support has been a growth propellant. Public and private interests have been joined through PPP's (Public Private Partnerships), rising investments, increasing efficiency and reducing gaps in the healthcare public system.

In parallel, strategic and financial players are leading the consolidation process. By acquiring or merging companies, these groups or platforms have been created in varied segments of the health industry, like medical or dental plans, hospitals, clinics, laboratories (diagnosis/imaging), pharmaceuticals, drug wholesale, pharmacy chains, medical devices and others.

In the Brazilian pharma industry, the government plans to attract local production and research centers focused on value added medicines, which will increase the importance of Brazilian pharmaceutical market.

Primary healthcare program is key to prevent diseases, shifting from a model based on curative care in hospitals to a preventive care in local communities, reducing costs and pressure on clinics and hospitals.

Finally, on certain segments of the Brazilian healthcare industry it is still possible to find competitors with huge discrepancies in terms of facilities, technology, management etc.. So, issues like cost reduction, process review, upgrade in management information system, training of medical and administrative teams, updating of equipment, are just part of a long list of gaps commonly found in most of the companies, public or private, profit or non-profit organizations.

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The Healthcare sector in Brazil is marked by a significant number of particularities and for being very complex. However, this sector has undergone profound changes and a new business paradigm, making the Brazilian Healthcare market one of the most promising and attractive in the world.

Among the local characteristics, is the fact that it is the only country in the world to have a system of free and universal public health - ie, taxes paid by Brazilians cover all types of consultations and treatments offered by System Unified Health System (SUS) without charging any additional user - but at the same time, private sector spending is greater than that of the government. For example, in 2009, the Union, states and municipalities allocated around R\$ 79 billion (\$ 39 billion) to SUS, while the private network contributed approximately R\$ 91 billion (\$ 45 billion).

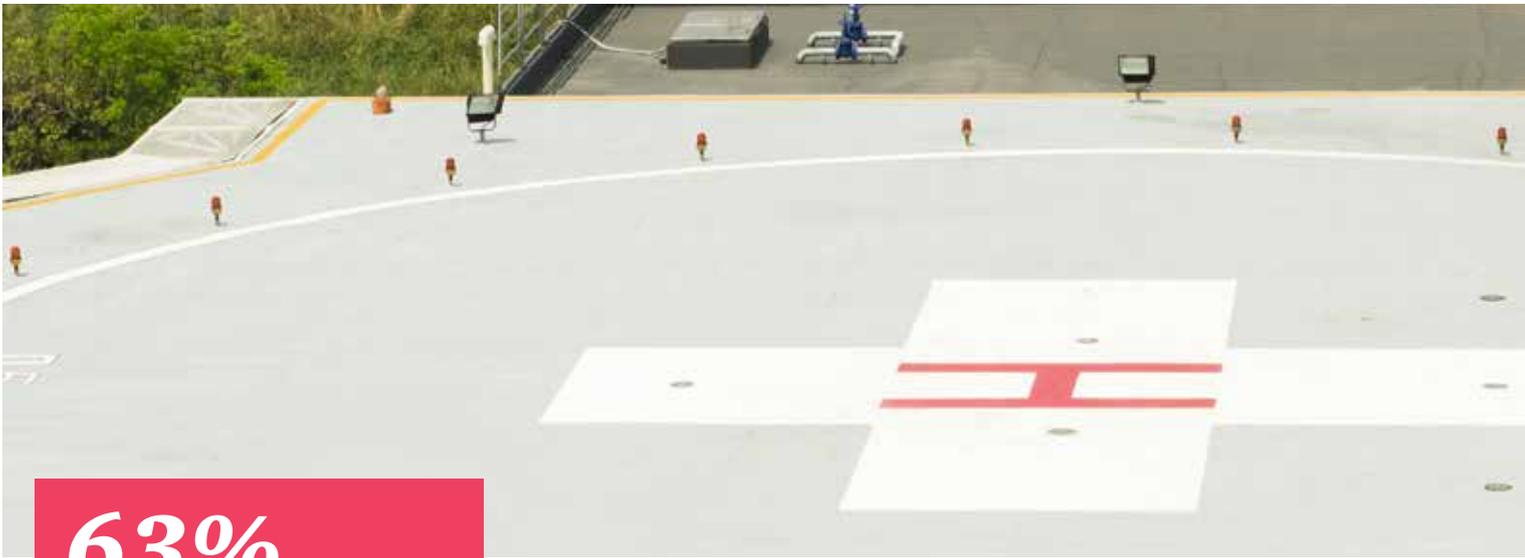
The SUS is a fundamental structure for healthcare in Brazil, as an important part of the Brazilians are not able to access the private system. However, with income growth and the expansion of the labor market, more and more people choose to hire private planes because they understand that the services provided are of higher quality compared to those offered by the public system.

Structure

The private market is distributed among individual agents, whereby the service user pay individually or collectively paying through groups or health insurance plans administered by private companies, cooperatives medical organizations philanthropic or self-management. On another side lie the service providers: hospitals, clinics, laboratories, pharmaceutical industry and others.

The regulation of activities is different for each sector agent. Administrators and health insurance plans are highly standardized and supervised by the National Health Agency (ANS), while providers are supervised mainly by the National Agency for Sanitary Surveillance (ANVISA).

In the field of public health, NHS management focuses on the Ministry of Health, which transfers revenue to states, municipalities and university hospitals, and charities, supervising the activities.



63%

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Plans and health insurance

As an example of the private healthcare market, operators and insurers ended 2012 with about 48 million beneficiaries of medical plans only. In 2009 there were 41 million, which meant, in three years, an increase of 17%. There is also the private dental segment, which ended 2012 with approximately 18.44 million beneficiaries, a market with annual growth in recent years, above 10%.

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The market is highly fragmented: the seven largest operators, all with more than a million lives insured, hold 29.2% of all beneficiaries and

the largest company does not have even 8% of market share. Due to this fragmentation, the ANS has encouraged consolidation and has given significant sanctions to groups that do not meet regulatory requirements and quality standards.

Operators have been more concerned with improving their management and operational control in order to remain profitable in a highly competitive environment. A tremendous challenge, it is worth emphasizing, because in line with the global trend, industry costs in Brazil are on the rise, mainly due to the ongoing technological developments and human longevity.

The country still has a so called “demographic bonus”, estimated to last until 2025, whereby the population of working age is greater than the general population. It is expected that by 2025, Brazil go into an aging period, greatly expanding the participation of the elderly in the total population. Even the end of the demographic bonus period represents, according to experts, a significant market opportunity for Brazilian Healthcare, as the aging population will increase demand for health services. In this situation, given the weaknesses of the public service, beneficiaries will give preference to private plans.



Hospitals, clinics and laboratories

Another field that already shows signs of important changes is the provision of services, especially in hospitals. In Brazil, no hospital group has national coverage: all private hospitals operate only regionally. The greatest proof of the fragmentation of this market is that no Brazilian private hospital owns 1% of market share based on beds. The largest private hospitals in the country are philanthropic and/or nonprofit. In this segment there is a huge demand for new investment, but the Brazilian legislation restricts international investments in hospitals. This is the cause of a major national movement, led by hospitals, to amend the legislation so as to allow international groups to acquire hospitals, in line with the pharmaceutical industry, market plans and health insurance and laboratories.

Private laboratories are also a significant niche: market estimates indicate global revenues of R\$ 20.2 billion/year (around US\$ 10 billion). Another important feature is that these groups have high profit margins and this is the Healthcare segment with most merger and acquisition (M & A) activity.

At the same time, there is a huge movement to enter the domestic market through greenfield investments, especially in regional markets underexplored such as the Northeast and Midwest of Brazil.

Pharmaceutical industry

The pharmaceutical industry in Brazil is expected to undergo significant changes in the coming years. This segment has a strong concentration: in 2009, according to IMS Health, the local industry had 378 players controlled by 45 laboratories that received 91.7% of the total sector revenue, which is \$ 15.1 billion. On the other hand, the local research laboratories received only \$ 140 million of the \$ 40 billion in global investments.

Another important challenge is the high concentration of the distribution network which lies in the hands of a few national and regional groups: 65% to 75% of pharmaceutical distribution is made by local distributors, while only 25% to 35% is delivered directly to retail.

However, the sector has benefited from the expansion of household income. From 2006 to 2009, drug sales grew 12.1% per year, and despite ANVISA, the market regulator, establishing additional rules for the marketing of drugs, there are no signs of a slowdown in the growth of this sector.

Public health

The pressure of high costs and the need for investment also begin to change the dynamics in public health. Change begins in the form of the first Public-Private Partnerships (PPPs) projects in health care. In these models, the government pays private agents through investment in infrastructure, technology and human capital for the operation of public hospitals.

There are at least two major PPP contracts already running and a number of similar projects are being set up in several Brazilian cities.

Why Healthcare in Brazil?

The country has compelling Healthcare demographic growth drivers, such as strong projected GDP per capita growth, which will lead to Increased Healthcare consumption, creation of formal jobs and an aging population.

The domestic market will continue to go through an important consolidation trend: Healthcare, Pharmaceuticals & Life Sciences.

Brazil has political and economic stability as well as strong legislation to protect investors.

Some trends include:

- Significant revenue increase in dental plans and home care services;
- Cost reduction, regulatory compliance, technology & innovation are areas of #1 priority to the future market leaders;
- Strong M&A activity with strategic and financial investors playing a role to a consolidation, because of fragmented segments and regulatory environment;
- Public-Private Partnerships (PPP's) will attract strategic investors to raise investments and efficiency on public health system;
- Increase in local production of medicines driven by government plans.



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How PwC can help

We have an extensive range of services and specialists that can greatly contribute to the generation of results in the chain of Healthcare:

- Financial advice on mergers and acquisitions to support the strategic discussion, evaluation of businesses or assets, structuring and tax planning;
- Review of the corporate governance structure, considering the formation of succession planing;
- Implementation of system indicators for managerial, financial and operational analysis. (Business Intelligence);
- Evaluation of the profile of the portfolio loss ratio of operators to identify measures to assist in reducing occurrences (disease management and preventive actions);
- Support the development of user satisfaction survey in order to create an action strategy approach focused on the beneficiary (loyalty);
- Assessment of the compensation model, identifying the cost elements of major procedures. This evaluation aims to change the model of payment by results/ performance and can be used to support the negotiation with the health plan for improving the compensation values, as well as assisting the entity's management to focus efforts on improving procedures to gain efficiency and cost reduction;
- Evaluation of operational management model. This assessment involves the analysis of internal processes and business operations in order to improve the flow of information and capturing data. This may also include analysis of the ERP level of use adopted in order to identify areas for improvement in efficiency. Furthermore, the evaluation may extend into areas such as portfolio and operating strategy;
- Development of strategic plan aimed at development aspects of the business, such as planning for medium and long term prospects of acquisitions and mergers, new product development, partnerships and/or channel affinities, and evaluation of the profile of beneficiaries vs. industry trends;
- Alignment of information technology with the strategy of the organization, seeking to identify solutions that contribute to improving the efficiency and agility of the business and add value in the delivery of patient services (eg mobile health); and
- Development of a mobile strategy aimed at providing better access to network providers and beneficiaries as well as strengthening user loyalty;
- Comprehensive audit and assurance services designed to deliver real value and underpin investors' confidence;
- Tax compliance, consulting and planning services combining a strong understanding of the business environment and tax knowledge.

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