

Market commentary

China's healthcare industry at a turning point

China's economy has gone through some turbulent times since the coronavirus pandemic began more than two years ago. A rapid economic rebound after the initial shock was followed by renewed turbulence in 2021. This was triggered by the Chinese government's regulatory crackdowns on the tech, property and education industries aimed at alleviating social inequality. Regardless of these developments, China's healthcare sector has emerged as a key industry for the country's overall economic development. Since the outbreak of the coronavirus, the Chinese healthcare industry has made further significant progress in terms of quality and its international profile. This has made the sector more attractive to investors too.

From Von Remo Krauer, Senior Portfolio Manager Bellevue Healthcare Asia Pacific Fonds

China's healthcare sector already underwent a regulatory transformation years ago. Clinical trials and regulatory approval pathways in China have been increasingly aligned with international standards during the past seven years. At the same time, government procurement of generic drugs was centralized, increasing the financial muscle of government programs supporting innovative therapies. The 14th Five-Year Plan endorsed last year by the Communist Party defined innovative healthcare as a core element of its strategy for technological independence.

Many facts confirm that China's healthcare industry has indeed become a key economic factor. According to recent estimates, the sector will grow by 10% to 12% on average over the next few years, which is twice as fast as China's estimated GDP growth. A key driver of this fast growth is demographic change. In 2050, the percentage of people over 60 years old in China is projected to represent around a third of the total population. At the same time demand for high-quality healthcare services is increasing as China's rapidly growing middle class gets richer. In order to maintain social stability, the ruling Communist Party has prioritized the nationwide expansion of an independent, high-quality system of healthcare. Monetary and government spending policies are designed to promote this goal. Whereas the US central bank is expected to announce three rate hikes this year, China is moving in the opposite direction and easing its monetary policy.

Focus on quality wins out

In practical terms, the catch-up effects triggered by efforts to improve China's healthcare system mean two things. On the one hand, access to and the affordability of drugs and medical services remain important elements of government policies. On the other hand, the improved national framework is helping China to close the gap in innovative medical treatments with the West, with the US in particular. China, for example, now publishes the most scientific publications on biotechnology behind the US. According to a recent forecast from Bernstein Research and Evaluate Pharma, China's drug market will expand by 14% p.a. from 2018 to 2023 to USD 166 bn. During this same period, the share of patent-protected original medications is forecast to increase from 40% to 64% of total sales. This number is a clear indication that China has long shifted from a focus on "growth first" to "quality first" when it comes to drug R&D quality.

This progress goes hand in hand with the growing number of industry alliances involving Chinese companies. Chinese biotech companies are increasingly the partner of choice for drug R&D

development, approval and marketing purposes for international biopharmaceutical companies seeking to enter the Chinese market. For example, the number of active pharmaceutical ingredients from Chinese laboratories licensed out to international companies increased from 37 to 83 clinical candidates between 2018 and 2021. Meanwhile the number of licensing partnerships arranged with Chinese companies rose from 3 to 21. Compared to the number of agreements announced between US and European companies, these figures are still low. However, the upward trend is indicative of the general direction for the remainder of this decade.

Looking at therapeutic areas where China is making the fastest progress with promising clinical products, four areas stand out. In oncology, Chinese biotechs have advanced novel approaches with immunotherapies, bispecific antibodies, and adjuvant antibody-drug conjugates (ADCs). They have also made progress with cell and gene therapies. In diabetes, which is becoming a growing medical problem in China, domestic providers of diabetes treatment have been widening their share of the market. Last but not least, Chinese companies have and are developing and producing COVID-19 vaccines, antibodies and antiviral therapies. In order to meet requirements for US FDA approval, companies are starting to gather data from international as well as from Chinese clinical trials.

Legend Biotech is a prime example of a Chinese biotech company on the verge of a major international breakthrough. On February 28, an FDA advisory approved the company's CAR T-cell therapy for multiple myeloma. It has shown to be highly effective in clinical studies, so this could become the first made-in-China drug to qualify as a first-line treatment of this aggressive form of blood cancer.

What this means for investors

The increasing maturity of the Chinese healthcare sector has created attractive investment opportunities. Valuations are currently at low levels because the widespread sell-off in Chinese stocks in 2021 also dragged down healthcare stocks despite their generally strong fundamentals. New-drug approvals like the announcement Legend might make next week will increasingly bring the Chinese biotech industry into the spotlight of the international investment community in the coming years. Our long-standing expertise in emerging markets enables us to quickly identify tomorrow's winners in Asian healthcare markets such as China for our funds.

Author

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