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# Spotlight on Healthcare – A Special Industry Report (Second of a Series)

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We continue our special series on healthcare with a look this week at how the sector is playing out in the capital markets. (See also our Lead Lead Spotlight with Brad Raymond, Head of Investment Banking at Stifel Financial).

As we covered last week, healthcare benefits from tailwinds unique to the industry. Those characteristics have created certain dynamics that have made the sector popular with both issuers and investors.

Few sectors match the sheer breadth to which healthcare has grown across the economic landscape in recent years. In 1990, according to the Bureau of Labor Statistics, manufacturers employed more workers than any other industry. By 2003, retailers, interestingly, held that position. Twelve years after that, post-recession, healthcare related businesses reigned as the number one employer in the country.

Favorable demographic and technological trends have positioned healthcare in the sights of capital providers. Attendees at Proskauer's Private Credit Insights conference in January saw a survey of private credit participants' views on select topics.

To the question "In which industries is your organization interested in/considering investing in over the next 12 months?," 87% answered healthcare. Business services (at 98%) was the only sector with a higher percentage. Manufacturing, consumer goods/retail, and technology followed next in order of interest.

What drives this level of intended participation? Returns for one thing. A recent McKinsey study reported that in the twenty-five year period between 1990 and 2015, global healthcare led all sectors with a total return to shareholders of 13%. Consumer staples at 11% came in second. (Returns were calculated using publicly available revenue growth weighed by each sector's market cap).

Does the degree of interest in healthcare match the actual pace of investing? In the period 2012-2015 (per McKinsey), healthcare divestitures from large corporates grew at almost a 50% per year clip – from $37 billion to $114 billion. Yet private investments in the space only increased modestly, from $12.7 billion to $14.6 billion.

In part, we suspect this is due to the challenging nature of financing spin-offs. Lack of audits and the need to set up entire independent financial and operating networks can be daunting for private equity sponsors with limited resources. However, for those that specialize in healthcare the rewards can be great.

"Specialize" is the key word. The managing partner of a healthcare focused sponsor put it this way: "We don't invest in healthcare companies. It's way too broad an industry. We have very focused criteria in select sub-sectors. For example, we like IT-driven services. But the device arena is challenged by technological change. And of course reimbursement is a big factor that varies with each specialty group."

Another veteran healthcare banker agreed. “As a provider, demand for healthcare is not the problem. It’s about what you end up getting paid.”

*Next week we continue our special series with more insights from healthcare-focused private equity firms.*