











# Healthcare Industries

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## What are Healthcare Industries?

 <p><b>Pharmaceuticals, Biotechnology &amp; Life Sciences</b></p>	 <p><b>Healthcare Equipment &amp; Services</b></p>
	
	
	

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## What Makes Them Special?



### Research & Development

Development of new drugs can be highly profitable, so a strong incentive to spend on R&D



### Uncertainty

Success of new drugs highly uncertain, making forecasting future revenue challenging



### Collaboration

Due to the high costs of developing new drugs there are often joint ventures created



### Tax Breaks

To encourage the social benefit of new drug discoveries, many countries offer lower tax rates as an incentive

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## Treatment of Research and Development Costs

### US GAAP

All acquired R&D assets should be capitalized

All other R&D costs should be expensed, excluding software costs

### IFRS

All acquired R&D assets should be capitalized

All research costs should be expensed

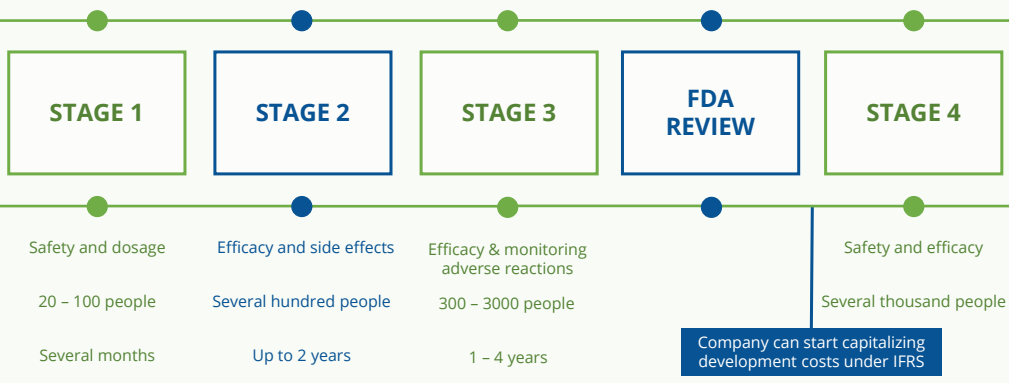
Development costs capitalized after feasibility of asset established

Must be able to complete intangible asset, to be able to use it or sell it

Must be able to demonstrate how the asset will generate future economic benefits

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## Stages of Clinical Trials



The Group considers that, in the case of the development of Pharmaceutical products, the aforementioned requirements are met **when the drugs have been approved for marketing by the health authorities** in the case of new products developed under patent, or, in the case of biosimilars or generics, when the application for marketing authorization is filed.

EXTRACT FROM LABORATORIS FARMACEUTICOS ROVI'S FINANCIAL STATEMENTS

## Revenue Forecasting

### Existing Products

Revenues typically forecast on a product-by-product basis

Incorporate impact of end of patent period

### Pipeline Products

Revenues typically forecast on a product-by-product basis

Probability weighted expected future revenues

#### Assumptions Include

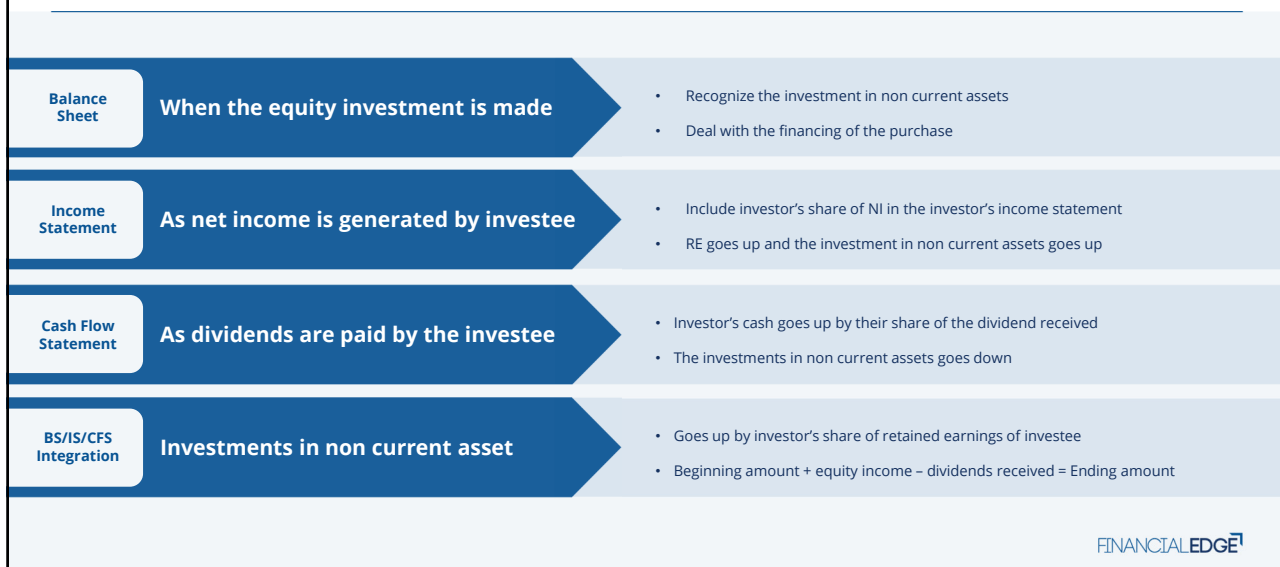
Probability of Success

Market Size

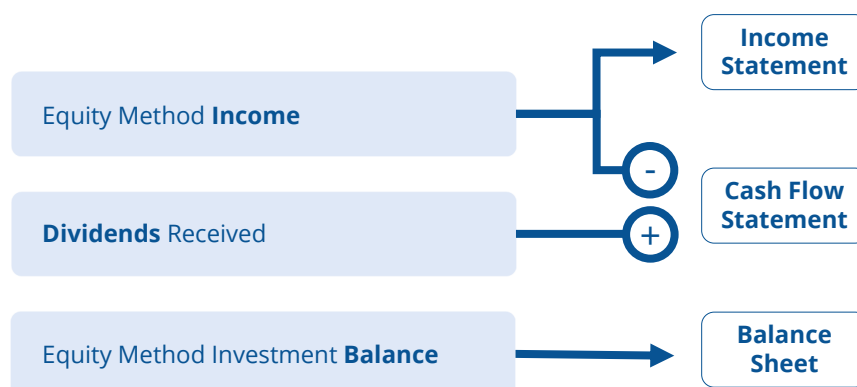
Profit Margins

Direct vs Indirect Sales

## Accounting for Joint Ventures



## Forecasting Joint Ventures



## Forecasting Joint Ventures



Investment balance held **constant** in balance sheet

Implied dividend **payout ratio of 100%**



Equity Method Investments



Income Statement



Cash Flow Statement



Balance Sheet

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## Taxation of Pharmaceutical Firms

### R&D Tax Credits

Used to encourage innovation

Company can offset a proportion of money spent on R&D against tax liability

Effective tax rate may be lower than statutory tax rate

### Deferred Tax

Early year losses can lead to substantial deferred tax assets

R&D tax credits can create deferred tax assets if recognition is deferred

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## Taxation of Pharmaceutical Firms

### Extracts from **Laboratoris Farmaceuticos Rovi** Tax Note

Amounts in € 000s	2019	2018
<b>Profit before tax</b>	<b>41,880</b>	<b>16,660</b>
<b>Tax calculated at domestic tax rate of 25%</b>	<b>(10,471)</b>	<b>(4,170)</b>
Share of profit of joint ventures	(49)	6
Movement on brought forward tax losses asset	5,437	1,313
Adjustment corporate income tax prior years	(140)	57
Non-tax deductible expenses	(112)	(271)
Tax differences in subsidiaries results	86	(135)
Movement on capitalized R&D tax credits	2,494	4,235
Other tax credits applied	148	180
<b>Income tax expense</b>	<b>(2,607)</b>	<b>1,215</b>

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## Understanding the Financial Statements

### Extracts from **Laboratoris Farmaceuticos Rovi** Balance Sheet

Amounts in € 000s	2019	2018
Property, plant & equipment	131,608	95,837
Intangible assets	45,079	34,650
Investment in joint ventures	1,843	2,038
Deferred tax assets	14,660	16,036
Other non-current assets	136	135
<b>Total non-current assets</b>	<b>193,326</b>	<b>148,696</b>
Inventories	158,811	94,861
Trade and other receivables	81,541	60,180
Other current assets	10,107	3,452
Cash and cash equivalents	67,426	95,511
<b>Total assets</b>	<b>511,211</b>	<b>402,700</b>

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## Understanding the Financial Statements

### Extracts from **Laboratoris Farmaceuticos Rovi** Balance Sheet Cont.

Amounts in € 000s	2019	2018
Financial debt	72,104	16,589
Deferred income tax liabilities	1,078	1,243
Other non-current liabilities	8,934	9,884
<b>Total non-current liabilities</b>	<b>82,116</b>	<b>27,716</b>
Financial debt	12,701	17,635
Trade and other payables	91,914	68,165
Other current liabilities	2,094	1,712
<b>Total liabilities</b>	<b>188,825</b>	<b>115,228</b>
Equity	322,386	287,472
<b>Total liabilities and equity</b>	<b>511,211</b>	<b>402,700</b>

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## Understanding the Financial Statements

### Extracts from **Laboratoris Farmaceuticos Rovi** Income Statement

Amounts in € 000s	2019	2018
<b>Revenue</b>	<b>382,463</b>	<b>304,789</b>
Cost of sales	166,605	128,611
R&D expenses	29,304	32,376
Selling, general, admin and other expenses	125,495	114,300
Share of profit / (loss) in joint ventures	(195)	24
<b>EBITDA</b>	<b>60,864</b>	<b>29,526</b>
Depreciation and amortization	18,216	12,044
Finance costs - net	768	802
<b>Income before tax</b>	<b>41,880</b>	<b>16,680</b>
Tax expense / (gain)	2,607	(1,215)
<b>Net income</b>	<b>39,273</b>	<b>17,895</b>

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## Analyzing Healthcare Industries



### Financial KPIs

Return on research capital (RORC)

Return on equity



### Valuation metrics

P/E

EV/EBITDA