



SPECIAL INDUSTRY REPORT

EXECUTIVE SUMMARY

HOSPITAL ACQUISITIONS INDONESIA

SINGAPORE, JULY 2019



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WHY THERE IS SO LITTLE M&A ACTION IN INDONESIA'S HOSPITAL SECTOR

Simon G. Bell, Singapore, 12 July 2019

M&A activity in sectors such as financial services, insurance, energy, and technology flourish in Indonesia. At the same time the healthcare sector remains surprisingly stagnant. Investors tend to focus on alternate markets in South-East Asia and more attractive industries within the Indonesian Economy.

No Deals are Better than Bad Deals

Investors have rightly decided that no deals are better than bad deals.

Owners routinely expect valuations that exceed the next 30 to 50 years of profit. This is either a result of a total disconnect from the reality of what their businesses are actually worth, a lack of interest in selling, as a result of plain old greed; or sometimes a combination of all three factors. We have certainly found that the more we look into the financials of a potential target, the less likely we are to be interested in pursuing the deal.

In an industry dominated by independent small business owners, usually either a family business or a small group of doctors, Indonesian hospitals often have less than 120 beds and generate revenues of US\$4 million or less. In such a fragmented environment we would expect that owners would be keen to exit their business but we have found this to generally not be the case.

On rare occasions, there is a legitimate impediment to a reasonable and acceptable valuation of the business and its assets for both the seller and the buyer. This occurs when the land and the building are of a dis-proportionate value when compared to the revenue the business generates.

Lessons from Evaluating more than 100 Deals

After evaluating more than 100 possible deals in Indonesia over the past 14 months, we have gained some useful insights into the industry.

Our experience is that there is a general lack of business sophistication, coupled with a regulatory environment that is not particularly conducive to closing acquisitions. Ownership restrictions on foreign investment also adds to the difficulties of closing deals. There are always issues and challenges when pursuing an aggressive acquisition campaign for businesses in any industry and in any country. In Indonesia, we would summarise the issues and challenges to rapid and large-scale growth as follows:

- Lack of motivated sellers;
- Difficulty in securing direct access to owners;
- Unsophisticated sellers;
- Limited preparation of key data and reports;
- Sellers not entering into agreements in good faith;
- Fraudulent financials and unethical business practices;
- Uncertainty around financial results and valuations;
- Valuation expectations that make no commercial sense; and
- A legal system that makes it difficult to enforce contract law.

Owners Consistently Forget They are Competing for Investment

Hospital owners seem to consistently forget they are competing for investors with companies from other sectors and other key markets in Asia. The lack of investment we are seeing is a natural result of the quality of the deals available. It is also holding back the industry in some very important areas.

Invested capital, smartly deployed, is one of the key drivers that stimulate the advancement of an industry. The relatively low level of investment in Indonesia's healthcare sector is:

- Reducing competition;
- Limiting the upskilling of human capital;
- Curbing innovation and best practices;
- Limiting the range and quality of services;
- Curtailing access to patient-centric care models;
- Inhibiting access to critical equipment; and
- Slowing advancements in digitalisation, AI, advanced R&D and telehealth.

The Indonesian healthcare industry is fragmented and under-served. It is in major need of investment, development and disruption from both domestic and international players. Determined individuals and companies that are willing to blaze a trail by bringing order and simplicity to chaos and complexity will reap substantial rewards. We believe there is a significant opportunity to make a meaningful contribution to the Indonesian healthcare sector.

Benefits for Owners, Staff and Patients

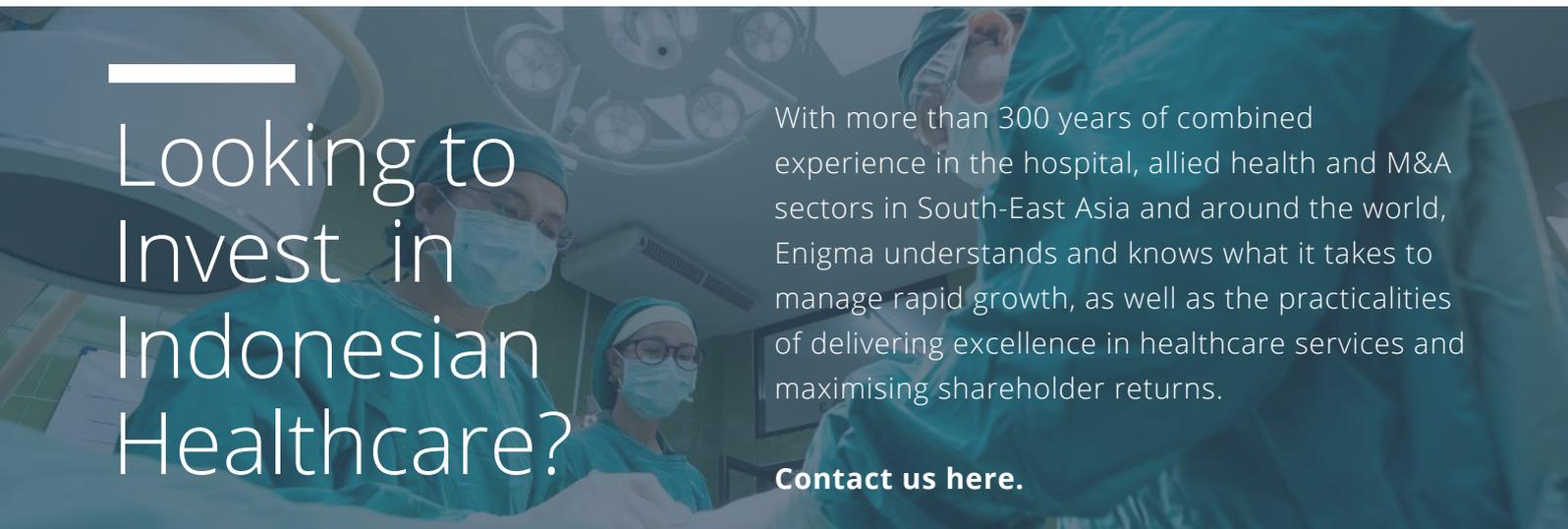
Unrealistic expectations from owners kill deals more than any other single factor. The bottom line is that owners who divest 100% of their business benefit from a large payment based on the profits of their business; in advance at an agreed discounted rate. They also no longer have the responsibilities of managing the business. Owners that divest a majority but remain in the deal gain the additional benefits of the revenue growth and cost efficiencies created through consolidation and professional management.

Greenfield Versus Acquisition-based Growth

Healthcare assets are currently overvalued with valuations often significantly exceeding 20 times EBITDA. This means it often makes more sense to develop greenfield which tend to take between two and half to five years to achieve EBITDA break-even. The simple opportunity cost assessment in our view is on the one hand: up to 5 years before EBITDA-break-even is achieved (this can be much quicker) versus paying in excess of 20 times EBITDA for an operating hospital. We believe a dual-strategy of acquiring assets at reasonable valuations coupled with the development of greenfield projects presents the most compelling strategy for long-term quantum growth in Indonesia.

Consolidate, Optimise and Expand

Enigma's strategy is to consolidate, optimise and expand. We are committed to becoming the dominant player in this market segment and we are playing the long game. We are consistently asking ourselves why the industry will be better because of our presence? How we can improve what was there before, and how we can create something that would not be possible without us? Ultimately the key to success is motivated sellers with reasonable expectations. Currently, we see very few motivated sellers, however, the consensus is that valuations are only going in one direction in the coming years and so many potential players are waiting to see what happens. With determined effort, however, we are confident we can orchestrate the symphony required for success much earlier: a motivated seller, a willing buyer and a commercial arrangement that is mutually acceptable.



Looking to
Invest in
Indonesian
Healthcare?

With more than 300 years of combined experience in the hospital, allied health and M&A sectors in South-East Asia and around the world, Enigma understands and knows what it takes to manage rapid growth, as well as the practicalities of delivering excellence in healthcare services and maximising shareholder returns.

Contact us here.



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Simon G. Bell

Mr. Bell is the Chairman and CEO of Enigma Healthcare. Enigma is committed to acquiring up to 50 hospitals and clinics across Southeast Asia over the coming three years. Enigma is currently focused on acquisitions in Vietnam and Indonesia. If you are serious about divesting a majority share of your business we are interested in both hospitals and groups of clinics. Contact us for more information here.

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