

ISSUES FOR
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INVESTORS

MAY 2010

PHARMA AND HEALTHCARE IN ASIA

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Our approach is based on analysis of material ESG factors, which change according to sector and market. We provide our clients with local market knowledge of important regulatory landscapes in Asia, along with a fresh perspective on local operational and sectoral issues. We offer an annual subscription model for our monthly sectoral or thematic reports and give our clients access to the underlying data. Reports can also be commissioned (by investors or foundations) and kept for internal use or be offered for general distribution, as part of an general effort to promote ESG integration into the Asian investment process. Our analysts conduct seminars and webinars to discuss findings, often with contributions from experts, companies and policy-makers.

Responsible Research was founded in 2008 by our Board who have been instrumental in promoting Corporate Social Responsibility (CSR) and SRI practices in Asia for over 10 years and have significant experience in the regions emerging investment markets. This team of five works in collaboration with our full time Asian-based responsible investment analysts and the Responsible Research Alliance, a group of consultants with subject matter expertise. Together they provide a valuable balance of market and ESG knowledge, academic rigour, process management, data management, customer relationship management and senior level contacts.

Many of our clients are signatories to the UN backed Principles of Responsible Investment (PRI), an investor initiative. As signatories they commit to incorporate ESG issues into their investment analysis and to support the development of ESG tools, metrics and methodologies. As a signatory to the PRI we voluntarily contribute time and resources to the Emerging Markets Disclosure Project and other collaborative initiatives. Responsible Research is also a strong supporter of independence in research, without which conflict and bias can deliver investment risk. The company is one of the founding members of the Asian Association of Independent Research Providers and also of the Asian Water Project.

Responsible Research acknowledges the contributions and support of:

Lauren Compere
Boston Common Asset Management

Nancy Frohman
Singapore Health Foundation

Rohit Malpani
Oxfam America

Stewart Adkins
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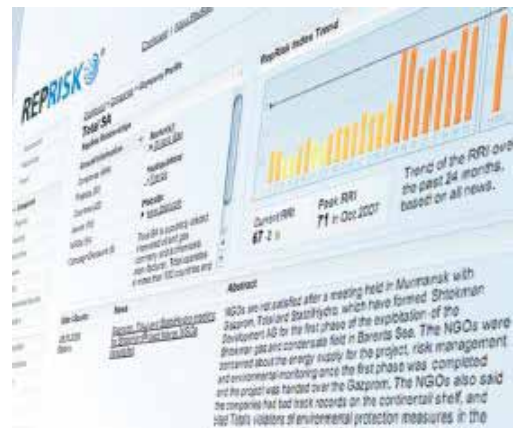


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EXECUTIVE SUMMARY

The healthcare industry in Asia is characterized by stark contrasts between developed countries like Singapore and Hong Kong and the emerging economies of India, China and Indonesia. There are glaring differences even within countries that make regional generalisations challenging.

The industry in Asia is growing much faster than that in the west and promises handsome returns. National insurance coverage is expanding very fast in most of the countries, improving affordability, and governments are spending massively to overhaul their healthcare delivery infrastructure. All this potential, however, comes laden with significant, environmental, social and governance (ESG) issues, giving responsible investors a number of additional factors to consider in their investment decision-making process.

This report covers the potential risks to earnings in both the pharma and healthcare industries due to non-financial ESG issues. It covers the ten countries featured in the MSCI All country (AC) Asia ex Japan Index, namely China, India, Indonesia, Philippines, Thailand, Malaysia, South Korea, Hong Kong, Taiwan and Singapore. We also provide a summary of the frontier markets of Pakistan, Vietnam and Cambodia. Several of these countries are also covered in detail in other sections in the report where we highlight ESG risks by using case studies from the region and offer global best practice examples. During our research, we interviewed several key individuals driving the Access to Medicines and Healthcare debate, from organisations such as Oxfam's Pharma Futures. These interviews provide additional insights for responsible investors in the region.

In order to confirm regional best practices, we ranked 37 of the largest listed companies in the Pharma and Healthcare sector based on their performance according to a comprehensive set of 23 environmental, social and governance criteria. These criteria can also serve as a basis for engagement with companies for investors looking to practice more active ownership in this sector.

The results show that Dr. Reddy's leads the field in the pharma sector and Fortis is well ahead in the healthcare rankings. These two well-managed companies stand in stark contrast to poor performers such as TTY Biopharma and Shanghai Pharma.

Access to Medicines and Access to Healthcare are the biggest social issues faced by the sector. Unlike Europe and the United States, healthcare financing in Asia is mostly out-of-pocket and, given the significant proportion of the population living below the poverty line, companies are under huge pressure to significantly modify pricing, intellectual property and research and development strategies until government structures are in place to support the 'bottom of the triangle'. Surprisingly, this holds true for generic drugs manufacturers as well as the MNCs, given that they have slowly but steadily increased their prices dramatically over the last decade. Similarly, given the grossly inadequate healthcare infrastructure (using measurements such as number of hospital beds and medical personnel per person) in countries like India, private sector healthcare providers are encouraged to accept certain responsibilities and expand beyond their traditional profit centres in the Asian mega-cities.

The gravest potential risks to earnings from the 'Access to Medicines and Healthcare' issues arises from governments deciding to impose compulsory licensing and pricing caps on drugs. This has happened already in the Philippines and Thailand. Additionally, issues such as product safety, ethical clinical trials and non-discrimination are often not taken seriously by the industry, despite several cases where there have been substantial financial implications for violations. We believe that, as a result of the ASEAN harmonization process, Good Manufacturing Practices (GMP) will begin to be implemented and product quality will improve. Companies that have not put into place policies and guidelines to comply with these practices will face heightened threats of closure actions by regulatory bodies.

Environmental issues such as climate change, energy efficiency, water usage and waste management could pose serious risks to company earnings in the future



due to trends such as carbon taxes, emissions trading and increased water pricing. We highlight these risks through the use of case studies illustrating companies like Zhejiang Pharma, which received hefty fines due to water pollution in China. Governance issues continue to affect the Pharma industry, in particular due to conflicting interests from many different stakeholders. The issue of unethical marketing practices is covered and we also focus on the poor standards of corporate governance and the complexity of government relations in the Chinese pharma industry.

Asia is fast emerging as a hub for innovations such as stem cell research and biogenetic manufacturing. Singapore has already established itself as a centre for high-end biotechnological research. There are, however, several ethical and reputational concerns involved for responsible investors, including ethical boundaries, use of cadavers and organ donation.

Complementary and alternative medical systems such as Traditional Chinese and Aryurvedic Medicine, whilst allowing patients to avoid the use of modern pharmacological drugs, still have issues to consider such as the poor training of medical personnel, inadequate long term clinical trials into the long-term side-effects and contra-indications. There are also concerns that the profits from the IP owned by generations of traditional medicine men and women is being exploited commercially with little or no compensation reaching those who developed the techniques and cures. This has resulted in calls for more responsible bio-prospecting in developing countries.

The report ends with a comprehensive discussion on a host of socio-economic health issues which may impact earnings for companies in other sectors. These include issues such as lack of primary healthcare infrastructure, clean drinking water and vaccinations, changing diets, lifestyles and disease profiles, mental health and maternity/paternity leave issues.

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