

February 26, 2016

Dear clients and colleagues,

Earlier in February, we attended the LEERINK Partners 5th Annual Global Healthcare Conference in New York City. Well attended by different industry leaders from biopharma, producers of medical devices, insurance companies, distributors and service providers, this conference was insightful, utilizing expert panels, one-on-one meetings and fireside chats.

Health care trends will continue to be strong for the foreseeable future, with a growth rate estimated at 5.8% in the US (Source: Center for Medicare Services). Global Alpha has overweight positions in the equipment provider and service sectors where there is a wide selection of profitable companies with good growth profiles.

The conference had a blockbuster headline: **Cancer cure within 15-20 years**. As the research industry now has enough data on cancer's complex genetic matrix (individual cancers and all their mutations), we can expect the development of gene-specific drugs to grow swiftly over the next decade.

The medical cost of cancer will reach \$207 billion by 2020, surpassing heart disease and diabetes. As better treatments become available, survival rates of some types of cancers increase by 10% annually. As well, the number of cancer patients grows by 10% per year, mostly caused by an aging population. It is therefore not farfetched to envision the emergence of a healthy genetic testing industry and thriving therapeutic/rehabilitation services industry.

One of these expanding markets we are watching is the outpatient rehabilitation industry, a \$19 billion market in the US. US Physical Therapy, a position in our Global Small Cap portfolio, is a clear consolidator in the physical therapy space, an area which up until now has focused more on bone, muscle and nerve pain. We remain extremely excited about the developing business models of specialty care services (such as cancer and neurology) as these industries develop to address the needs of the mass of patients that continues to increase in both size and complexity.

At the conference, we attended presentations by cancer and other drug development companies. In general, Global Alpha looks for companies with extremely low risk clinical profiles. We tend to favour existing commercial businesses that offer us a strong drug pipeline at a deep discount.

Biosimilars emerging as large drug patents expire

Biosimilars are the generic substitute for biological drugs, and they already represent a global market estimated to be worth \$2.29 billion in 2015. Biosimilars are poised to grow at a compound annual rate of 22.1% until 2020. The top five drugs targeted by biosimilar producers are Avastin, Enbrel, Herceptin, Humira and Rituxan, which together generate annual revenues of approximately \$50 billion. In the E.U., where they are already competing with biologics, biosimilars are sold at a 30% discount to the branded biologic drugs. Despite of the approval of 21 biosimilars in Europe, only 18% of physicians are aware of these generic versions of biologics. The largest hurdle to FDA approval in this hyper-growth industry is the required Phase 3 Similarity

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Study. New, less expensive and timely regulatory processes are being studied to help hasten approval of new drugs.

The biosimilar market is presently dominated by large companies such as Sandoz and Hospira. However, a select group of companies in our investment universe will gain market share as this area continues to develop.

We attended the fireside chat presentations and met with the management of two Global Alpha holdings: WebMD and Cynosure.

WebMD president David J. Schlanger spoke confidently while explaining in simple terms the driving trends of medical web dynamics. In addition to providing better information flow to doctors, drug companies are under growing pressure to launch blockbuster drugs in a time-efficient manner. As the development period for drugs becomes longer, the time a company has exclusive marketing rights under patent becomes shorter. Efficiency of launch and marketing dollars are therefore critical. As the most important web-based portal, it is hard not to select WebMD as a marketing partner.

Cynosure management reaffirmed the successful launch of its key new product, SculpSure Contour. SculpSure is a heat-based lipolysis device used to treat stubborn fat. Its addressable market is estimated to be the 1.3 billion adults aged 18 and older that are overweight (BMI 25-30). The procedure is 25 minutes long without any incisions. Cynosure is a leading aesthetics company with over 50,000 devices installed in 132 countries.

Other presentations we were able to attend included Intersect, Zeltiq, Depomed, Enanta, Acadia, Cempra, Momenta, Medcines, GW Pharmaceuticals, Agios, Bio-Techne, Corium, Inogen, Acceleron, Nxstage, Globus, Abiomed, Conmed, Macrogenics, Luminex, Sucampo, Endochoice, Evolent and Foundation Medicine.

Continued M&A in the sector

2015 was a stellar year for M&A in this sector, with \$605 billion in takeovers. Cash repatriation acted as the rationale in some cases, such as the \$43 billion Medtronic acquisition of Covidien (triggering \$10 billion in cash availability). In the large cap space there are numerous companies with significant cash balances on their balance sheets, so it is difficult not to forecast a good year in the small- and mid-cap M&A health care environment.

As for medical devices, the conference exposed us to impressive technology companies that should dominate their space going forward as a result of respectable early adoption rates with leading practitioners. This gives us some interesting homework to do.

Have a nice weekend.

The Global Alpha Team

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