

# CalPERS Investment Committee

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## HEP and Partnership with CalPERS

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Investment Considerations

# Health Evolution Partners' History

**2006**

McKinsey study on improving CalPERS' health industry returns

- Response to downturn in CalPERS' health care investment returns in early 2000s
- Take advantage of CalPERS' full capabilities as both a leading institutional investor and health care purchaser

**2007**

CalPERS Healthcare Investment Initiative (HII) RFP

- Select General Partner to construct specialized investment platform and strategy
- Ensure CalPERS' capital is invested in the highest returning sectors of health care globally

**2007**

HEP awarded role as manager of HII

- HEP is CalPERS' preferred partner for identifying and evaluating health care industry investments
- Mandate to build an investment institution that can diversify across \$10 trillion global health care industry

**2008-09**

HEP funds launched

- Growth Buyouts: \$500M fund targeting control investments in fast-growing companies in health care's key sub-sectors
- Spectrum: \$200M diversified portfolio of leading health care funds and selective co-investments

# Health Evolution Partners Today

- Institutionalized investment firm
  - Investment and operating team fully-operational
  - Strong differentiation among private equity firms
  
- Funds in full scale operation
  - Growth Buyout Fund:
    - Nine direct investments totalling \$354M
    - One exit in 2011 generated 2.6x
  - Spectrum Fund:
    - Fully-committed with 10 fund commitments and 3 direct investments
  
- Specialized platform for health care eco-system
  - Strategic partnerships with McKesson, Optum, Dell, Merck, Oracle, Pfizer, Verizon
  - Close working relationship between HEP and CalPERS' Health Benefits Branch
  - In-house team manages extensive network of the health care industry's leaders
  - Host a high-impact health industry CEO Conference, the Leadership Summit

# Leveraging HEP's Network in Every Phase

## More effective **ORIGINATION**

- Building a strong brand
- Developing and nurturing relationships
- Demonstrating access to relevant industry participants

## Better informed **DUE DILIGENCE**

- Validating company representations with industry buyers and end users
- Evaluating regulatory and reimbursement risk

## Stronger **PORTFOLIO MGMT. & VALUE CREATION**

- Introducing HEP portfolio to new customers
- Recruiting for management teams and boards
- Identifying IT leverage opportunities

## Improved opportunities for **EXIT**

- Showcasing our companies to opinion leaders
- Engaging potential buyers early

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# High Growth, Disruptive Global Health Care Landscape

## Rapid spending growth forecasted in most countries

- US health care growing at 3X GDP growth
- GCC and BRIC nation health care industries growing in excess of 15% CAGR
- China finally rebuilding their health care system after radical decentralization
- Need for substantial infrastructure and services investments in nearly all countries including the United States

## Widespread privatization of finance and delivery

- Leverage private investment to build (rebuild) care delivery infrastructure
- Use private sector to manage costs and extract more value
- US-style private insurance and population management entering most countries

## Globalization of selected health care markets

- Race among countries for who leads global health IT market
- Global access essential to biotechnology and device makers
- Cost control and quality management diffusing from the United States into the global market

US remains the world's pioneer in consumer-driven care

# US Health Care Industry Today

- Affordable Care Act (ACA) roll-out continues following recent Supreme Court decision
  - Schedule remains in place for regulatory rule-making
  - Near-term Congressional changes seem unlikely, short of new deficit reduction actions
  
- Many uncertainties that existed before Supreme Court remain
  - Health Insurance Exchange (HIX) participation predictions vary widely
  - Private insurance and employer coverage still adapting to restructured insurance market
  
- Medicaid now faces lower enrollment target
  - State participation in ACA-driven Medicaid expansion clouded by electoral rhetoric; states are turning to savings from private managed care to close budget gaps
  - Period of experimentation in care management
  
- Election and FY2014 federal and state budgets bring uncertainty
  - Federal elections will bring changes to ACA irrespective of who wins
  - Full impact of state budgets on Medicaid and ACA implementation won't be known for some time

# US Health Care Industry Trends

- **Volume and Demand** will rise sharply, in turn increasing costs
- **Cost Pressure** will intensify reimbursement cuts (which often backfire)
- **Robust Demand** for specialized health care infrastructure and real estate
- **Physician Shortages**, and potentially hospital bed shortages, are looming
- **Life Science Development** will resume, but less robustly than before
- **Consumer Responsibility** for prevention and treatment decisions will rise

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HEP and Partnership with CalPERS

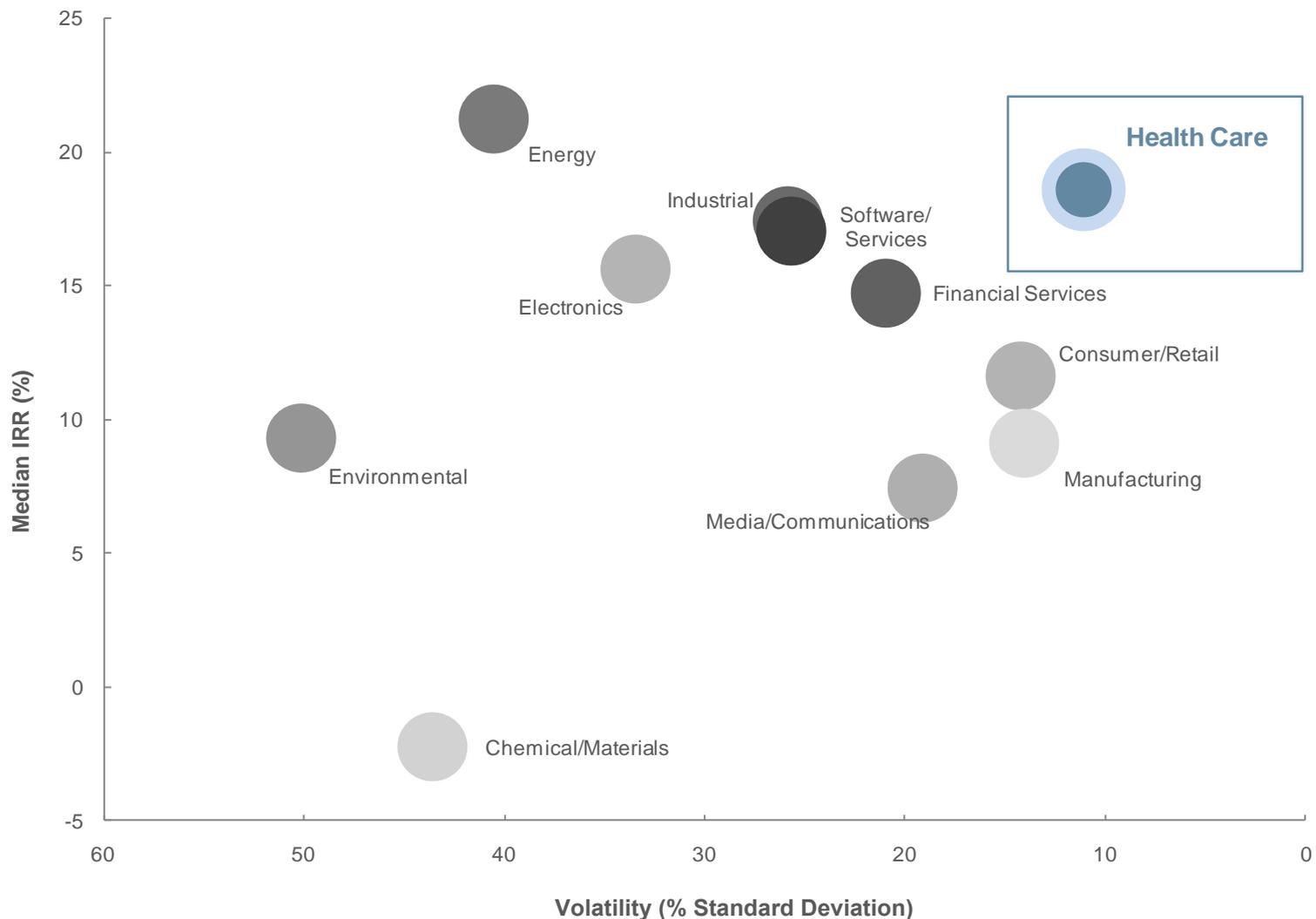
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# Health Care's Consistent High Performance



Source: Cambridge Associates Private Equity Report (1996-2011)

# Seeking Strong Health Care Investment Returns

## INDUSTRY TREND

## HEP INVESTMENT THESIS

### Volume and Demand

Expanded capacity to meet basic services needs in US and other countries

### Cost Pressure

Demonstrated low cost alternatives and cost management solutions

### Robust Demand

Health care real estate, including offices, surgery centers, and senior living, particularly aimed at specialized populations

### Physician Shortages

Low cost extenders, new sites of care, and telemedicine solutions

### Life Science Development

Distribution channels to ROW, asset-backed lending, secondaries and consolidation

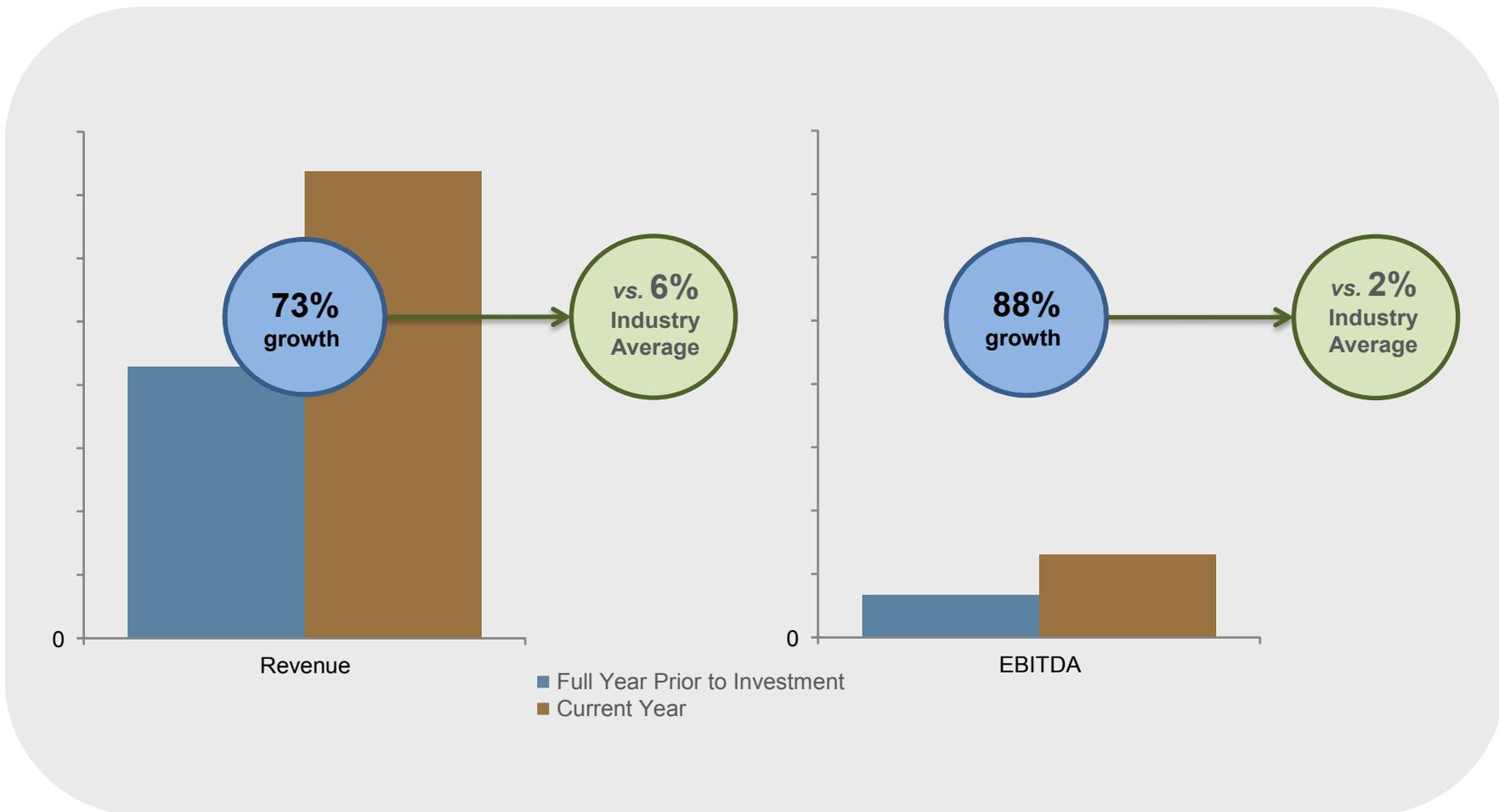
### Consumer Responsibility

Low cost information tools and financial management solutions

# HEP's Overarching Investment Strategy

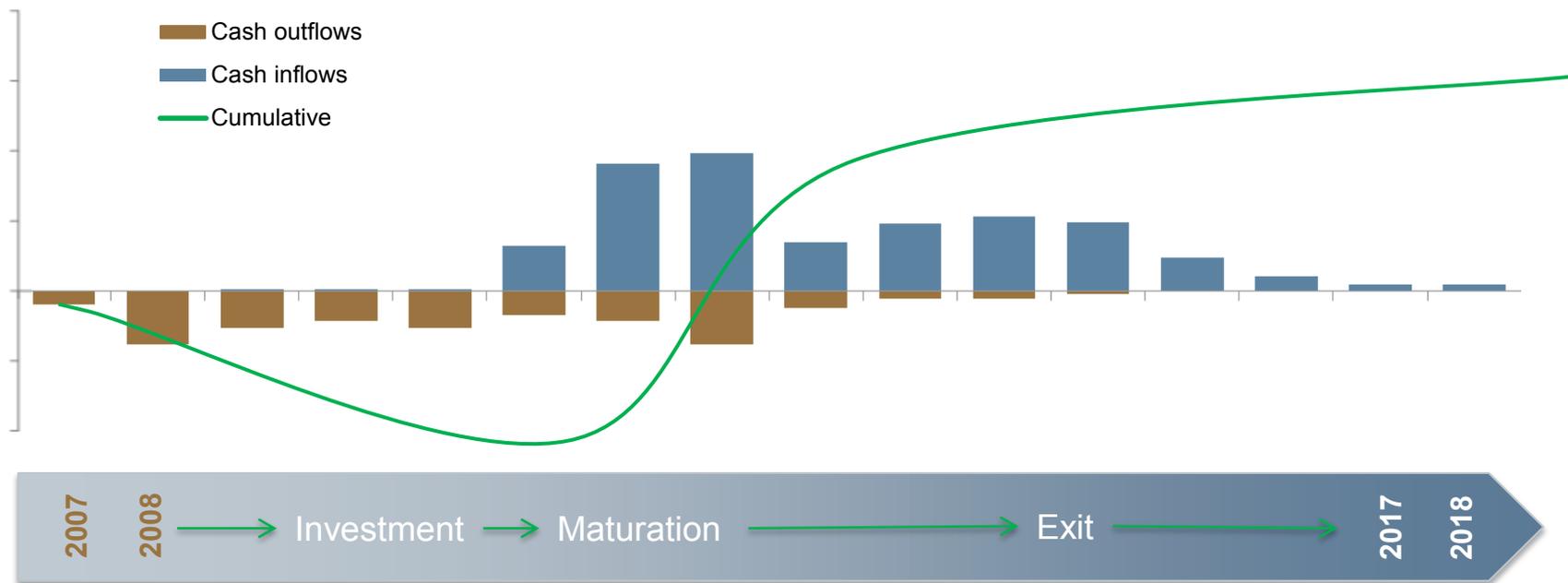
- Allocate into desirable sectors and asset classes of health care
- Invest in market leaders
  - Seek companies with significant growth potential
  - Complement direct investments with fund investments and vice versa
- Manage downside risk
  - Limit reliance on leverage to meet target returns, but utilize it appropriately
  - Diversify across life sciences, health care services, health IT
  - Balance cost-growth (reimbursement-sensitive) with cost-reduction opportunities
- Drive earnings growth through value creation
  - Align management's compensation with key performance indicators
  - Mentor and develop management bench
  - Institute good governance and board processes
  - Leverage our operating partner talent in Growth Buyouts companies

# Value Creation Leading Indicators



Numbers represent unrealized investments in Growth Buyouts Fund I. Current Year represents 2012 budget. Slide represents organic and acquisitive growth. Industry info is estimated and based on the following sources: *S&P Healthcare Index* as well as HEP analysis.

# HEP Fund Lifecycle



	Vintage	Capital Committed (millions)	Cash In (millions)	Cash Out (millions)	Cash Out & Remaining Value	Net IRR	Net Multiple	Target IRR	Target Multiple
<b>Growth Buyout Fund I</b>	2009	\$ 505	\$ 393	\$ 61	\$ 333	0.5%	1.0x	20%	2.5x
<b>Spectrum Fund I</b>	2007	\$ 200	\$ 116	\$ 2	\$ 103	-4.7%	0.9x	18%	2.0x