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Aging population likely to boost health care demand

by Dexter Tan

Gains in global life expectancy is estimated to climb by more than a full year from 73 to 74.1 years— bringing the number of people age over 65 to more than 300mn worldwide, or nearly 9% of the population. Health care spending is projected to expand by 4.1% annually over the next three years, up from 1.3% between 2012 and 2016. The demand for medical services would likely benefit healthcare companies as their credit profiles have improved. As shown in Figure 1a, the Aggregate RMI-CRI 1-year Probability of Default (Agg PD) for healthcare firms has been lower than the global aggregate 1-year PD since the year 2000.

Health care providers are profitable and have low default risk but profitability is falling. Companies in the sector face revenue pressure and struggle to improve operating margins despite higher health care demand. The need to keep up with clinical technology advances, infrastructure upgrades and rising manpower costs have pressured the firms' bottom lines. As global health care spending is expected to reach USD 8.7tn in 2020 from USD 7tn in 2015, competition within the industry could intensify as more firms enter the market.

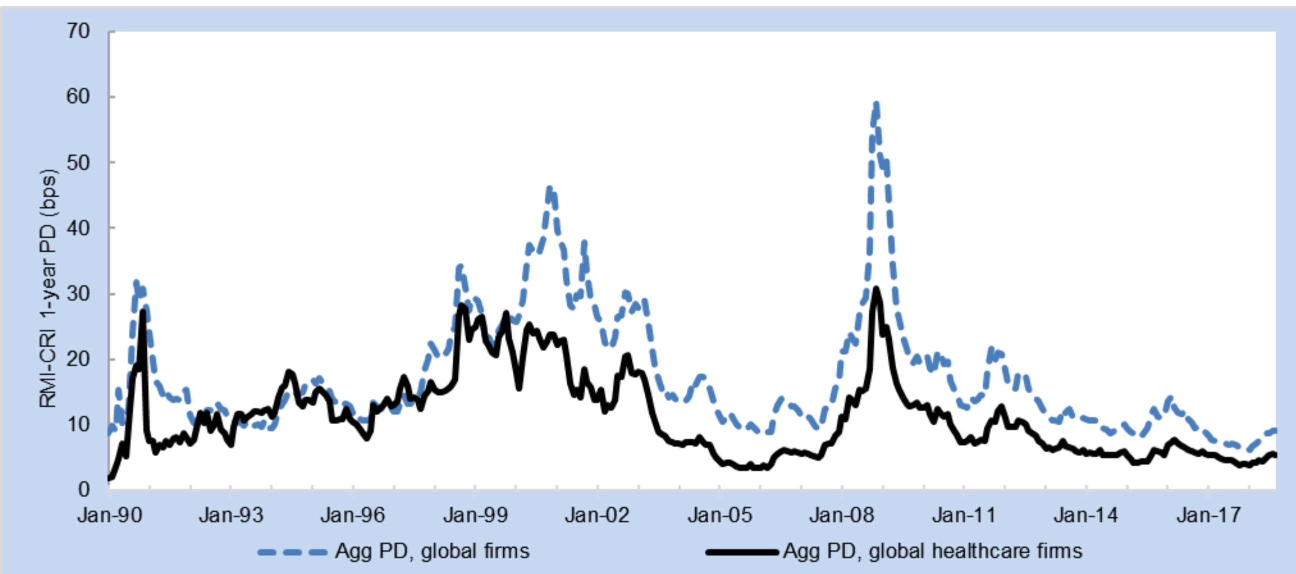
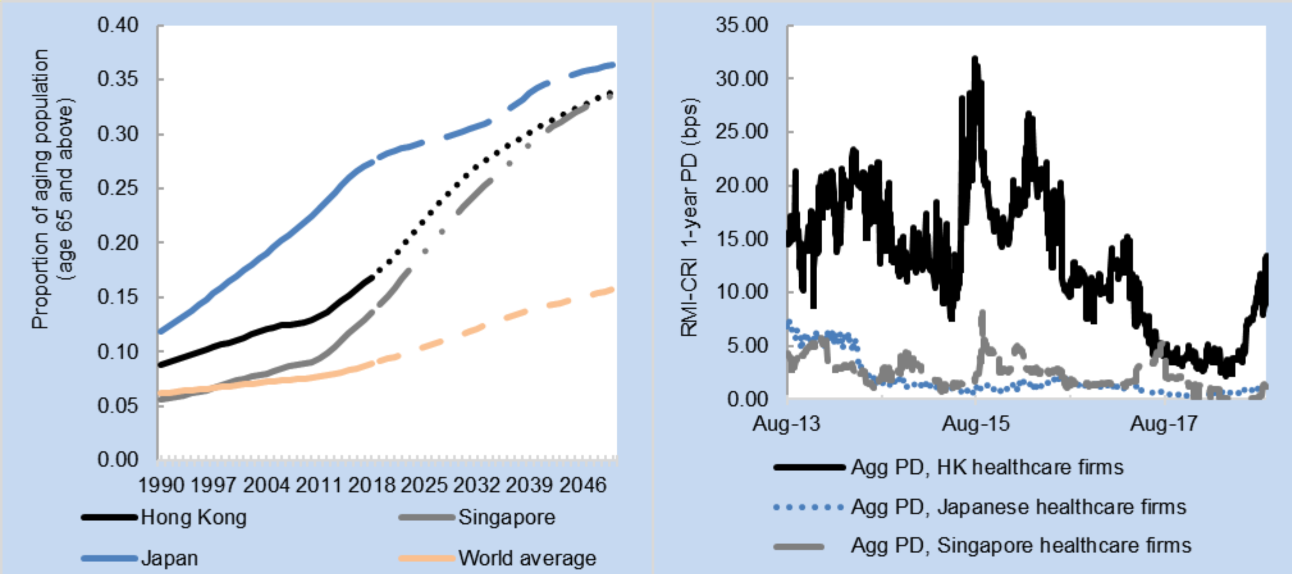


Figure 1: Aggregate 1-year PDs for healthcare firms and global firms. *Source: RMI-CRI*



Figures 2a & 2b: Proportion of aging population in the fastest aging economies and the aggregate 1-year PD for health care firms. *Source: RMI-CRI, Bloomberg, World Bank*

The World Bank estimates that more than 7.6bn people live in the world today and the number is projected to increase to 9.7bn by 2050. Birth rates in developed economies are dropping rapidly and many of these countries may not have enough young workers to support an aging population. Populations in developing nations such as Africa on the other hand, are growing at record pace, as numbers are set to grow to 2.5bn by 2050. Japan, Singapore and Hong Kong (HK) are among countries that are projected to have the highest aging population in the world by 2050. HK and Singapore will have the fastest aging population rate in the next five years while Japan holds the world record for the highest proportion of senior citizens, as nearly 28 percent of the country are age 65 and above.

Listed biotechnology and medical providers domiciled in these economies have benefitted from the elevated demand for health care in the region. This is seen from their aggregate credit profiles tracked by the low RMI-CRI 1-year Agg PDs in Figure 2b. The median probability of firms defaulting on their debt obligations within a year remain below 15bps; Japan domiciled and Singapore domiciled health care providers have lower default risks than Hong Kong domiciled healthcare firms. The market value of Hong Kong domiciled firms has dropped more than other similar listed firms in Japan and Singapore. C-Mer Eye Care, a HK initial public offering that was 1500 times oversubscribed and soared 101 percent in its exchange debut in January, has witnessed a 71 percent drop in its market capitalization from its peak.

The outlook for the healthcare sector is positive as demand is thought to be recession-resistant and noncyclical. Companies however have to keep up with the changing demographic and regulatory landscapes in several countries. In the EU, governments have been under pressure by taxpayers to provide more efficient health care services and legislators introduced a new medical device regime last year. In China, regulators recently amended their distribution system for drugs and medical devices and the US also changed its FDA approval process to introduce more generic drugs to the market.

Credit News

Creditors in China see strong-arm tactics from local governments

Sep 28. China's local authorities are still intervening on default negotiations even after its top banking regulator pushed for market-based approaches two years ago. The interventions went as far as asking creditors not to take legal actions against the defaulter and to maintain credit lines particularly in cases of larger firms seen as important to the economy. Although China authorities have attempted to develop judicial infrastructures to handle defaults, court-mediated bankruptcy is still rare as it involves larger losses. Moody's Investors Service in Hong Kong stated that until the legal mechanisms are established, official interventions can be useful to calm creditors and provide solutions for temporary credit crunches. (Business Times)

Tax change lures foreign investors to China policy-bank bonds

Sep 28. China recently announced that it would waive taxes for offshore investors in China's domestic bond market for three years in a bid to lure foreign money into its policy-bank bonds market. A few large foreign investors responded to this new changes by increasing their exposure to policy banks as it will give them extra yield with no additional credit risk as compared to central government bonds. However, some investors are waiting for further clarity on the recent tax changes. The policy-bank bonds also benefit from being highly liquid where they made up 35% of bond trading volumes in August, compared with 13% from treasury bonds. (Reuters)

India's shadow banking sector likely to face shake-up after default

Sep 28. India's shadow finance sector is expecting regulators to cancel licenses of smaller non-banking finance companies (NBFCs) due to inadequate capital and further tighten rules for new applicants. This happens after Infrastructure Financing and Leasing Services (IL&FS), a major financing company, defaulted on some of its debt obligations. The shadow banking sector comprises more than 11,400 firms with a combined balance sheet worth INR 22.1tn and is less regulated than the banking sector. NBFCs' loan books have grown at nearly twice the pace of banks and some of these companies, such as IL&FS, received top credit ratings. The rise in borrowing costs and weak liquidity in the sector may lead to a credit crunch in the NBFC sector with the smaller NBFCs being affected the most. (Reuters)

Prospect of rate rises precipitates bond fund outflows

Sep 28. Global bond funds have suffered the greatest outflows in more than half-a-year, as investors prepare themselves for a more hawkish posture from the Federal Reserve and the European Central Bank. Specifically, investors are weighing on the possibility that the Feds will raise interest rates quicker than markets have expected in 2019. Bond funds tracked by EPFR Global saw USD 6.1bn outflows in the seven days to September 26, the biggest weekly withdrawal since mid-February. Correspondingly, the yield of the Bloomberg Barclays Multiverse index peaked at 2.41%, the highest since 2013. Meanwhile, a renewed concern over Italy and a comment by the president of ECB regarding Europe's accelerated inflation in the coming months have caused the biggest outflows in European fixed-income funds. (FT)

Yields rise as Ghana considers USD 10bn century-bond sale

Sep 25. Ghana is preparing to sell USD 5bn to USD 10bn century bonds as the first tranche of a USD 50bn bonds to pay off existing debts, build factories, and overcome an estimated shortfall of USD 7bn in infrastructure spending. Ghana's plan comes in a time amidst cooling investors' interests in high-yield assets due to rising US rates. Emerging market dollar debt yields have climbed almost 100bps since April due to a sell-off as fears of contagion from the Argentina and Turkey's crises hit emerging markets. While China, Argentina, and Mexico have also previously issued 100-year debt, Aberdeen Standard Investments argued that they were previously done in a more favorable market conditions. Furthermore, the huge size of the bond issuance caused concerns as Ghana is still at a high risk of debt distress. (Bloomberg)

IMF boosts Argentina program to USD 57bn in bid to halt peso slide (Reuters)

Egypt seeks new debt investors with Euroclear, Asian foray (Bloomberg)

Hong Kong banks increase rates for the first time in 12 years (Business Times)

Regulatory Updates

Danske's laundering scandal drags down smaller Danish banks

Sep 26. Danske Bank's money laundering scandal is having stock market repercussions, affecting the performance of other Danish banks which were not involved in the scandal. Analyst has said the smaller banks might face a higher funding costs due to a spillover effect. Meanwhile, Danske Bank has suffered the most, losing approximately a third of its market value after it was revealed that more than USD 200bn flowed to its Estonian branch in the period 2007-2015. Amid the revelation of the scandal, The Systemic Risk Council urged the government to raise counter-cyclical buffers for Denmark's banks after noting that Denmark's financial system is highly affected by developments and risk perception in international markets. (Business Times)

European banks seek lighter-touch regulation in the US

Sep 25. As mid-tier US banks, between USD 50 – 250bn in global assets, were given relief around stress test and capital requirements under President Donald Trump's legislation, the European lenders are also seeking similar relaxed rules for their US operations. Currently, foreign banks with more than USD 50bn in US non-branch assets are required to hold all these assets in a single intermediate holding company for supervision purposes and are required to comply with enhanced prudential standards on capital, liquidity and stress testing. European bank representatives and US senators are raising the possibility of foreign retaliation for the unequal treatment and it may have impact on the international operations of US banks operating overseas. (FT)

RBI eases cash reserve rules to provide liquidity for banks (The Indian Express)

China standardizes bond issuance of overseas institutions (Xinhua)

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