Global Trends in MedTech – 2021

A Consolidating Supply Chain?
A Tiering Supply Chain? Both?

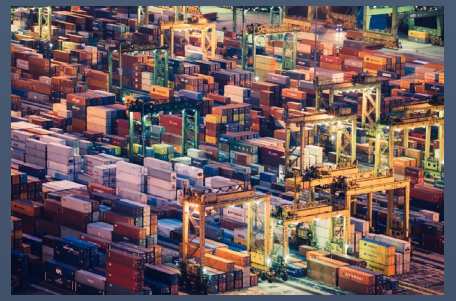
MPO
MEDICAL PRODUCT OUTSOURCING

MPO Webinar Series
February 24, 2021

Three Events

Tuesday, February 23

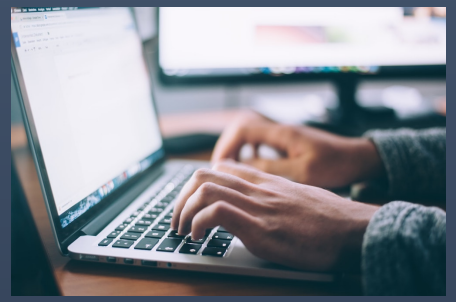
The OEM Landscape and Business Drivers



Wednesday, February 24

A Consolidating Supply Chain?

A Tiering Supply Chain? Both?



Thursday, February 25

Panel Discussion of *MedTech's Global Trends*

About A.S. Freeman Advisors

Tony Freeman

A.S. Freeman ADVISORS, LLC

- Merger and acquisition advisory services
- Corporate strategy in support of transactions
- Focus on precision manufacturing and specialty materials markets
- Publishes *Global Trends: Medical Device and Diagnostic OEM Strategy and Implications for the Supply Chain*

Perspective: Looking Out 3 to 10 Years

- Focus on the “seismic trends” driving the industry
- Three- to 10-year horizon
- Source materials:
  - OEM presentations to analysts and investors
  - Publicly-traded contract manufacturer (CM) presentations

Summary of Yesterday's Presentation: *The OEM Landscape and Business Drivers*

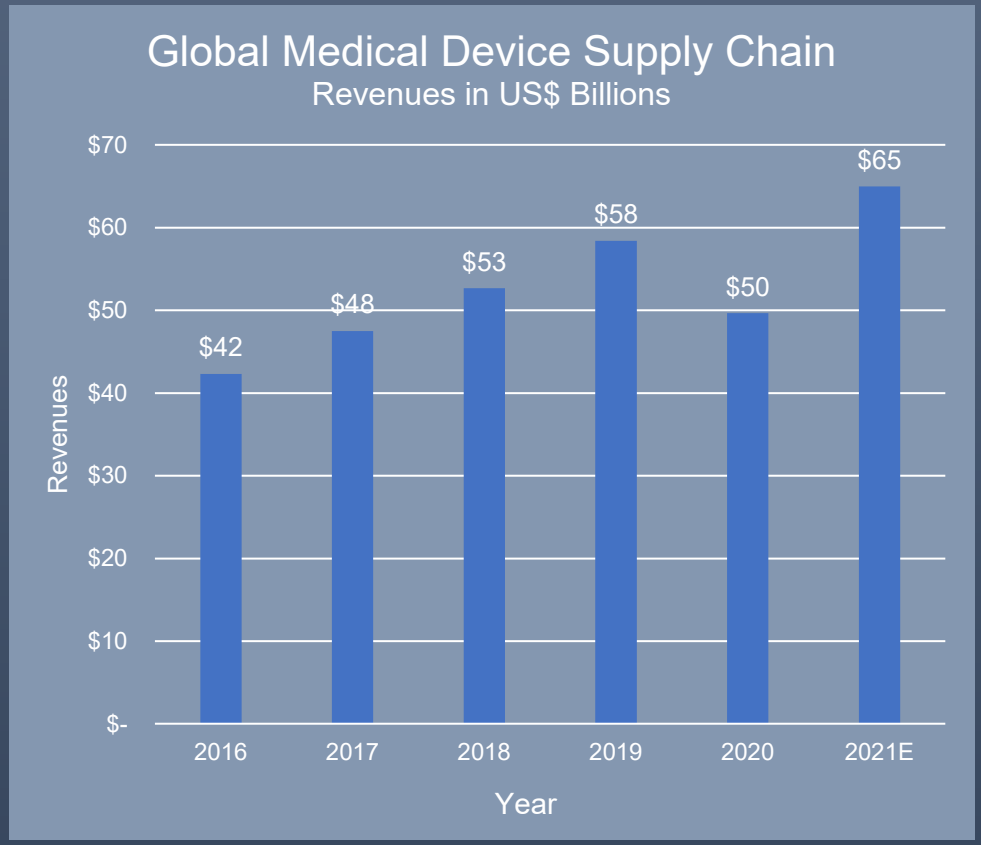
- Specialization
  - OEMs focusing specific areas of medical practice, less "many products for many specialties"
- Digitization
  - Rise of digital devices and networked care systems

Results

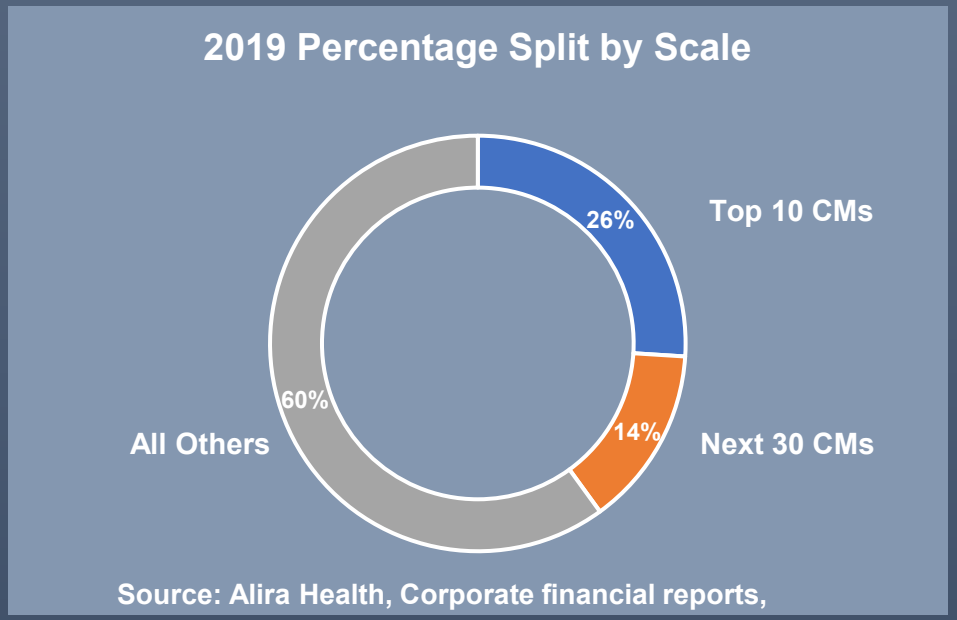
- Strong brand fortresses in targeted medical specialties
  - Market focus
  - Networks are hard to displace
- Change in OEM economics
  - Becoming health solution providers with a mix of products and services
  - New focus on data capture, analytics, and AI products
- Change in OEM product management and decision making
  - Rise of software, electronics, system integration, and data science managers
  - New people planning the next generation of devices

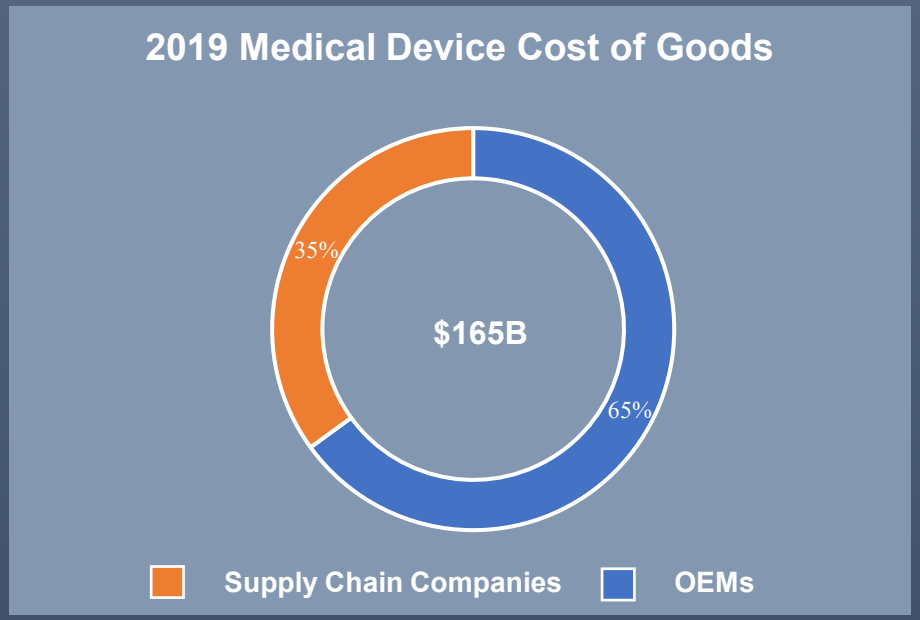
Supply Chain Size and Growth Rate

- Supply chain an estimated ~$50 billion in 2020. Murky from Covid.
- Likely $60 billion plus, adjusted for Covid pushouts
- Growing between 7.8% and 11.4% per annum through 2025. ASFA estimate 8-9%.



Concentration and Penetration





- Estimates range between 4,000 and 15,000 suppliers
- Top 10 suppliers represent 26% of revenues, top 40 suppliers represent 40% of total revenues
- Growth rate is projected from 7.8 to 11.5% per annum through 2025
- Outsourcing represents approximately 35% of total medical device manufacturing

Top 10 CMs

Company	
Jabil	Over $1 billion (2019E)
Flex	
TE Connectivity	
Sanmina	
Integer	
Plexus	
Celestica	
Viant	
Molex	Under $1 billion (2019E)
SMC	

- "Best guess" regarding Top 10 CMs and revenue ranges
- Split between organic growth and growth through acquisition

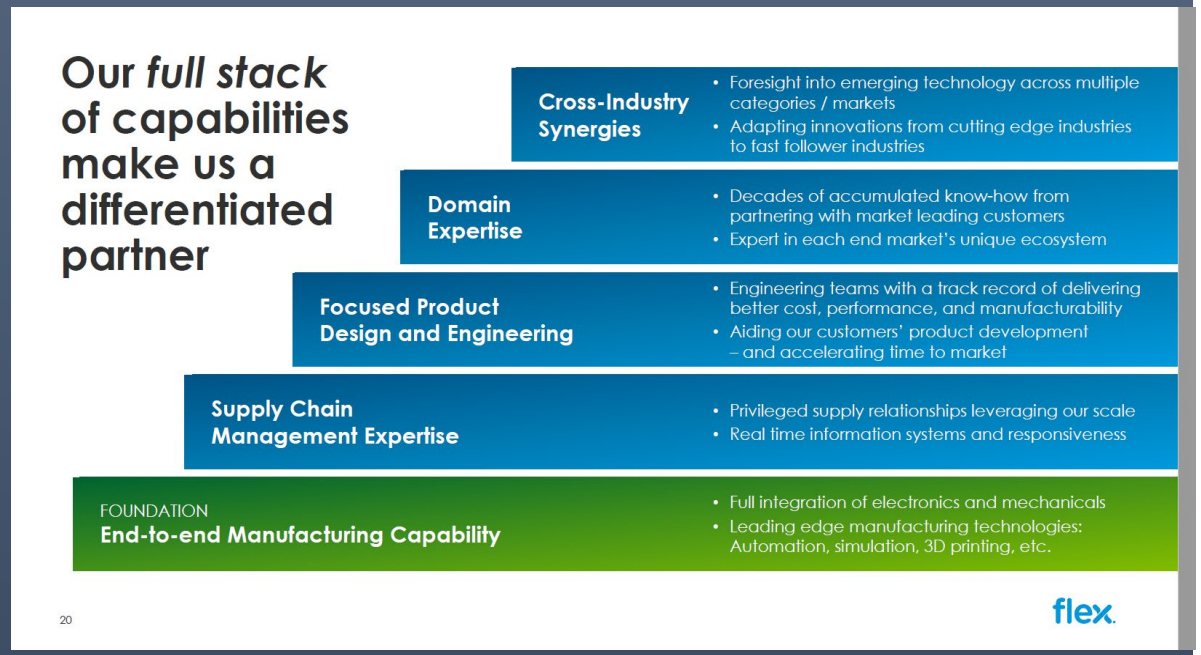
Jabil

- In 2018 took over 14 J&J manufacturing facilities serving DePuy, Synthes, and Ethicon Endo divisions. Roughly 6,000 employees
- Nothing happened
- Demonstrates large scale risk transfer works
- Additional facility transfers to supply chain companies are under consideration by major OEMs

Jabil's gross margin is 7.2% over the trailing twelve months

Flex

- Flex has a $2 billion medtech business
- Over 530,000 square feet of dedicated medical manufacturing
- Offers full spectrum of design and manufacturing services including:
  - Seminal design
  - Manufacture of digital and electromechanical devices
  - Global sourcing of materials and components
  - Multiple LCC presence



Flex gross margin is 6.47% over the trailing twelve months

OEM Direction Matches Top 10 Capabilities

- Rise of digital devices and ecosystems favor supplier with:
  - Electronics assembly expertise
  - Understanding of software and systems integration
  - Broad range manufacturing portfolio
  - Expert sourcing capabilities
- The Top 10 CMs have these capabilities
- Top 10 likely to capture the majority of outsourced flagship projects
  - Better match of capabilities to products of the future compared to “traditional” med device suppliers
  - Risk reduction – Single point of contact, financially stable

Future Structure of The Industry

- Favored few will increasingly be given choice over supply chain partners
- Prime contractor – subcontractors model
- Rise of tiered supply chain
  - Like aerospace?
  - Closer to auto, not as defined as aerospace

How Fast Will The Change Occur?

- Glacial and bumpy pace
  - Why move current products or products close to launch?
  - Risk of switching vendors on live projects
  - Aggressive defense from the current incumbents
  - Any misstep from the “majors” will be highly publicized
- A few big events – more facility transfers
- Five to ten year for the new supply chain to take form

Pricing

- Pricing will remain under pressure for the supply chain
- OEMs have begun to successfully extract margin as a price for large projects
- Few suppliers show rising consolidated gross margins

Offshoring vs. Reshoring

- Some have proposed that we are entering a reshoring period
  - Supply chain disruptions early in the pandemic
  - Rise of automation
  - Significant investment in plant and personnel in North America, Europe
- Offshoring will continue
  - Lower labor costs in Mexico, Central America, and Asia
  - No barrier to automating anywhere
  - Growth in Asian markets will reinforce Asian manufacturers' capabilities and scale
  - The major international CMs are skilled at sourcing quality components at a good price in countries med device manufacturers have shunned

Watch For Additional Risk Transfer From OEMs

- Risk transfer worked so why not try more?
  - Price pressures to become universal, particularly on established and legacy products
  - Extended payment terms are to be expected – the supply chain the OEM's bank for manufacturing
  - Watch for a rise in inventory holding requirements, another working capital transfer
- Larger companies better suited to take on these responsibilities

Where Will "Historically Profitable" Work Be Found For Smaller Suppliers?

- Specialization! Unique or exceptionally deep knowledge or expertise
- Experience with digital products
- Program management
- Exceptional customer service will become a more critical capability for holding customers

New Players Intersecting Existing Companies

- Digital technologies and cloud players
- Microsoft, AWS, IBM, Apple, others

For More Information

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