U.S. COMMERCIAL SERVICE, SHANGHAI

Privatization of Healthcare in the Yangtze River Delta Region II

Hospital and Elder Care Submarkets

June 2014

U.S. Commercial Service

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Dear Healthcare Professional:

China's healthcare sector is experiencing unprecedented growth. Coupled with the country's increasing rates of chronic disease, its rapidly developing middle class and its aging population, this means that there are numerous opportunities for U.S. exporters of medical equipment and healthcare services. And as Chinese disposable income continues to dramatically rise, this trend should also continue to grow.

While there are excellent opportunities for U.S. companies throughout China, the affluent Yangtze River Delta (YRD) region offers an especially favorable business climate for American medical and health services companies. Privately owned hospitals and elder care facilities are increasingly favored by the growing middle class because of the higher standard of care offered by these companies, and given that Chinese companies are quite new to this market sector, U.S. firms can enjoy a significant advantage. Further, to help this budding new market, local governments are encouraging private and foreign investment in response to this citizen-driven demand for quality healthcare.

The Commercial Service in Shanghai is committed to helping American companies find new international business partners in the YRD, and towards that end, this report analyzes the private hospital and elder care subsectors. Despite some challenges, our research suggests that these submarkets are poised for dramatic growth.

Sincerely,
Joel Fischl
Principal Commercial Officer
U.S. Commercial Service, Shanghai

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Executive Summary

The world's most populous country is facing a healthcare crisis. China's rapid socioeconomic and demographic transitions are presenting unprecedented challenges to the country's healthcare system. The incidence rates of heart disease, strokes, diabetes, cancer, and chronic lung disease are surging, accounting for 80 percent of deaths and more than 70 percent of the country's healthcare expenditures, according to a 2012 World Health Organization statement. Meanwhile, China's population is aging quickly. By 2030, the number of Chinese aged over 60 is expected to double to 360 million. The country's leadership is concerned that the disparity in healthcare accessibility, quality, and affordability is constraining domestic consumption and could lead to social instability.

To address these health-related national security issues, the central government has made healthcare reform among its top priorities. The government has spent over $350 billion since 2009 to make healthcare more affordable for its 1.3 billion people. As part of the country's healthcare reforms, policies including the Opinions on Further Encouraging and Guiding Social Capital towards Medical Institutions (Circular 58) allow foreign investors to create for-profit and non-profit medical institutions in China. The country's 2011 Foreign Investment Industrial Guidance Catalog (2011 Catalog) has also removed some of the barriers that previously limited foreign investment in the medical sector, and now permits wholly foreign owned enterprises (WFOE) to establish medical institutions in the country. Furthermore, China's 12th Five-Year Plan (FYP), which runs from 2011 to 2015, provides the private sector a supplementary role, with the aim of raising standards of care and addressing the growing healthcare needs of those who can afford it. Beijing hopes that by opening the country's healthcare market to foreign investment it can focus the country's limited resources on improving its healthcare delivery system and expanding medical insurance programs in the relatively poor rural interior areas.

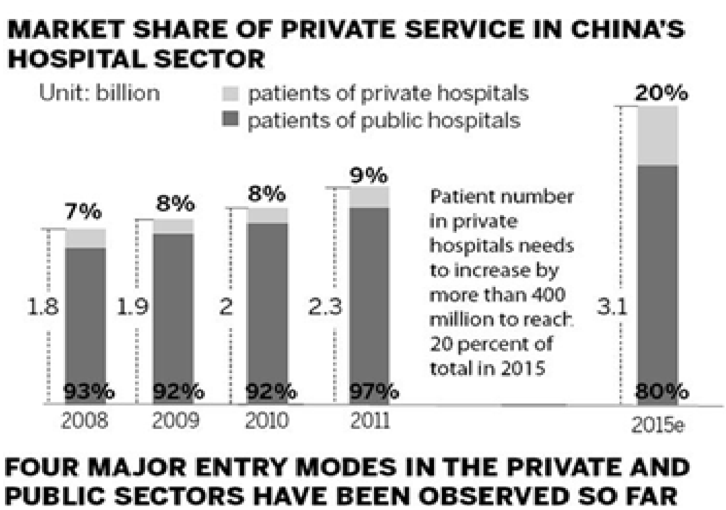
Although veterans of China's private healthcare market are bullish about the industry's future, they warn of major challenges, insisting foreign operators and investors will not make a quick profit in China's nascent private healthcare industry. However, the combination of reforms, strong healthcare demand, growing middle-class, and the aging population are creating growth opportunities for early entrants and a burgeoning market for those interested in China's private hospital and elder care submarkets.

Introduction

Representatives from the U.S. Consulate General and the U.S. Commercial Service in Shanghai recently examined China's healthcare reforms. To gain insight into the development of the private healthcare industry in the Yangtze River Delta (YRD), consulate officials analyzed publicly available resources, in addition to interviewing over 40 local government officials, hospital and elder care administrators, venture capital fund managers, and physicians. This report aims to assist Americans by providing a comprehensive look into the opportunities and challenges that can be expected in the YRD's growing private hospital and elder care submarkets.

Providing Chinese citizens with broad access to affordable basic healthcare services is the primary objective of China's healthcare reforms. The country's goal of providing universal health coverage has been largely successful—with 96 percent of the current population having basic health insurance—but healthcare costs are quickly rising. According to a McKinsey & Company report, government efforts to broaden insurance coverage along with an aging population will cause healthcare spending in China to triple to approximately $1 trillion annually by 2020. By allowing private operators and investors to enter the country's healthcare market, the Chinese government hopes to diversify the market and meet the different demands of its entire population. Xu Su, Vice Director of the Shanghai Medical Reform Office stated that eventually state-owned hospitals will only offer basic and non-profitable services, while private hospitals and joint ventures (JVs)—which offer better service but are more costly—will target the high-end market.

Continuing in this trend, Premier Li Keqiang declared on August 2013 that the government will further reduce red tape costs in an effort to spur foreign investment into the type of privately funded care that is common in the West. Private hospitals in China—which numbered 9,097 in June 2012—will continue to increase in number due to the government's ambitious goal to have 20 percent of the nation's hospital beds privatized by 2015. The central government would also like to see the number of private elder care institutions increase to provide institution-based care to 3 percent of the total senior population—approximately 3 million



Source: MOH, China Health Statistical Yearbook 2012 and China Daily people—by the end of 2015.

Individuals involved in the YRD healthcare sector are optimistic about the upper-middle-class and affluent population's increased willingness to pay for premium health care services. Despite their optimism, industry veterans warn that the major challenges ahead will include licensing, staffing, and property procurement. It is important to note that given the current underutilization of private hospitals and elder care facilities, foreign operators and investors looking to make a quick profit are advised to reconsider their entrance into China's private healthcare industry.

The Rich, the Poor, and the Emerging Middle Class

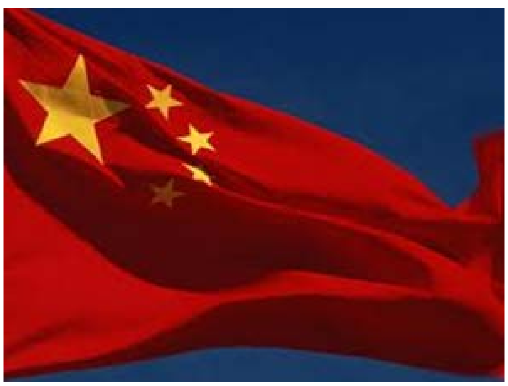
China is home to one-fifth of the world's dollar billionaires and is now third only to Japan and the United States in terms of millionaire households. Notably, residents of the YRD are some of China's wealthiest citizens, as demonstrated by the information obtained from both the National Bureau of Statistics and the Shanghai Statistics Bureau. It shows that the average disposable income of Shanghai's urban residents ($6,379) in 2012 was almost twice the national average for all urban residents ($3,912) in the country that year.

As the country becomes richer, income inequality deepens. This is most evident by the fact that as affluent Chinese households attain wealth that is comparable to their American counterparts, the overall individual incomes in the country continue to significantly lag behind those of the U.S. The majority of Chinese citizens cannot afford private healthcare; but this may soon change. According to a McKinsey & Company report, high-end and specialty medical institutions will continue to thrive, while general hospitals—both private and public (undergoing privatization)—become key investment opportunities.

Although China's upper-middle-class and affluent population segments can afford private healthcare, they typically seek treatment at Tier-3 or Tier-2 hospitals in large developed cities. Similarly, less-affluent patients seek treatment at community health centers where prices are considerably lower than private hospitals and clinics. A Rubicon Strategy Group report explained that private healthcare institutions primarily offer services to expatriates and affluent Chinese who either have insurance coverage or can afford to pay high out-of-pocket costs. While a majority of foreign healthcare intuitions in the YRD focus on serving high-income patients, a number of foreign healthcare operators have begun providing services to middle-class patients by signing management contracts with government-owned specialty clinics. Middle-class Chinese citizens are becoming more aware of Western medical safety standards and customer services levels, and as a result are willing to pay more for private healthcare.

Healthcare operators and investors looking to enter China's healthcare market should note that the country's public hospitals compete directly with private medical institutions and are categorized into three tiers. Tier-3 public hospitals are the most advanced and are normally located in large cities. These "provincial-level" hospitals usually have over 500 beds, VIP wards, and multiple specialty departments. Tier-2 hospitals are medium-sized "district hospitals" which can include a number of specialized departments. Finally, Tier-1 hospitals are small "community hospitals" and are primarily used for preventive care and general health conditions.

Country Profile



In February 2013, former Chinese Health Minister Chen Zhu called 2013, a "critical year" for health reform, explaining that the general public is expecting better healthcare. As reported in China's 2012 White Papers, about 260 million Chinese have been diagnosed with chronic diseases. As a result, state-owned Tier-3 hospitals were overwhelmed with heavy outpatient and inpatient workloads. This issue contributed to popular discontent with China's public health system.

To address its healthcare challenges, China announced an ambitious reform plan in 2009 when it committed to spending $125 billion in three years, with the goal of ultimately providing universal healthcare by 2020. The Chinese government is on track to complete its goal, as an estimated 96 percent of China's population currently benefit from basic healthcare insurance. Consequently, the per capita payouts by the country's insurance fund are skyrocketing, and rural populations are visiting more urban hospitals than closer rural clinics. Even though more Chinese citizens have access to healthcare, most Chinese citizens can only afford state-owned healthcare.

To relieve the public hospitals' burden in being unable to offer high quality care for those who can afford it, Beijing has opened the country's healthcare market to foreign companies and investors. For the country's 2011 catalog, the Chinese government moved medical institutions off the list of industries "restricted" to foreign investment and on to the list of "encouraged." China's 12th FYP on the Development of Chinese Elder Care also encouraged private capital, including foreign investment, to take part in the elder care market. The government considers senior living communities the most suitable and acceptable out-of-home elderly care model in China. Retirement home facilities are targeted to provide 3 percent of the nation's nursing beds by 2015. The central government's goal is to add almost 3.5 million new elder care beds by 2017.

In line with this goal, China's 2011 Catalog categorized service institutions for the elderly as "encouraged," demonstrating the government's desire to encourage foreign investment in the social welfare sector and allow foreign investment to be made via a WFOE. However, in December 2012, the Chinese government issued an amendment to the law. Under the new notice, the WFOE model is "expressly opened" only for Hong Kong and Macau investors, but foreign investment in a JV is still encouraged. The Chinese government released in June 2013 two draft rules on elderly care institutions in order to improve care for citizens age 60 and over.

Drafted by the Ministry of Civil Affairs, the rules clarify standard practices for nursing homes and stipulate parameters for the establishment of elder care facilities, including items regarding the number of beds and professional staff facilities are required to have. The draft rules call for allowing both qualified organizations and individuals to set up nursing homes for seniors. They also allow overseas institutions and individuals to set up these homes in China. County-level and above authorities are responsible for issuing such licenses. However, for foreign investors, although they are allowed to set up WFOEs or JVs, licenses can only be issued by provincial authorities or entrusted municipal authorities. Aside from this exception, there is no explicitly stated restriction on foreign investment in "service institutions for the elderly," which falls under the "encouraged" category in China's 2011 Catalog. Healthcare operators and investors can anticipate further relaxation of policies and more competition from foreign healthcare providers in the coming years.

Yangtze River Delta Region

Admin. Area	2012 Mid-Year Population	2012 Per Capita GDP (USD)	2012 Per Capita GDP (CNY)	Domestic Per Capita GDP Rank (out of 31)
Shanghai	23.639 million	$13,471	¥85,033	3
Jiangsu	79.093 million	$10,827	¥68,347	4
Zhejiang	54.700 million	$10,022	¥63,266	6
Mainland China	1.350 billion	$6,091	¥38,449	--

Source: Statistical Communiqué of the provinces on the 2012 National Economic and Social Development

The YRD metropolitan region, which includes Shanghai municipality, and parts of Jiangsu and Zhejiang provinces, is the most economically advanced region in China. It is home to around 120 million people, with Shanghai alone having 23.9 million residents.

As a result of China's economic prosperity, the standard of living has improved significantly in the YRD, fueling residents' awareness of the importance of personal health, as well as their demand for quality healthcare services from both public and private healthcare providers. Chinese citizens who have lived in Western countries are more likely to seek out private healthcare options than those who have never been abroad, according to professionals in the YRD's private healthcare industry. However, patient volume does not come easily. This is especially true in larger cities where Tier-3 public hospitals run VIP wards and private Chinese hospitals are plentiful.

The table above provides an idea of the per capita income of the *YRD*. Americans often describe the YRD as an easier base for business because the provincial and city governments are friendlier than Beijing towards Western business models. Beijing officials are reportedly unwilling to meet with prospective investors unless the project is valued at over $50 million dollars. Health Bureau officials in Hangzhou, the capital of Zhejiang province, are described as progressive and more in tune with the healthcare needs of the province's population. Similarly, Health Bureau officials in Nanjing, the capital of Jiangsu province, told U.S. Commercial officers that their city is very welcoming of foreign hospitals.

Healthcare Sector

In March 2013, the former Shanghai Municipal Health Bureau announced that the city government would adopt new policies to encourage overseas private investment, in an effort to meet the demand for medical services and further health reform. The city promised what it calls "favorable policies" covering finance, tax, and land, which attempts to attract talented professionals with incentives that include housing and children's schooling. American healthcare operators interested in establishing themselves in the YRD will need to carefully discuss with and seek applicable policy and subsidy support from the local provincial and city governments.

Expanding the size, efficiency, and diversity of China's healthcare sector to meet growing consumer demands were key aims of the guidelines released by China's State Council on October 14, 2013. The guidelines introduced policies that it says will lower healthcare costs, expand health insurance coverage, and increase industry competitiveness. In doing so, the guidelines call for increased government investment and participation of the private sector to help foster a RMB 8 trillion (USD $1.3 trillion) health services market by 2020.

Following the release of the guidelines, on October 16, the Ministry of Finance MOF) revealed that it will allocate RMB 2.22 billion ($364 million) to support the development of health services and pension services. The funds are to be used by local governments to support health and pension services, business services, and market regulation. The MOF announcement laid out three goals as "next steps" in developing health and pension services:

1. Increased investment in rural health services and pension services;

2. Establishment of pilot programs in selected provinces, cities, and counties to facilitate the integration of health and pension services with other sectors; and

3. Additional investment subsidies and discounted local government-sponsored loans to attract private investment in pension and health services.

(Source: US-China Business Council)

Chinese physicians are considered public-servants in state-owned hospitals. Some have been tempted to accept gratuities from pharmaceutical companies, patients, or their families, and prescribe expensive and unnecessary medicine and tests to supplement their low pay. This is a reality described by the Chinese media as well as entry-level physicians working at one of Shanghai's most prominent Tier-3 hospitals. In an effort to curtail this practice, the Minister of Health, Chen Zhu, declared at a press conference in 2013, that more than 50 percent of all Chinese county-level hospitals must stop their reliance on drug sales as a major source of income.

The Shanghai Health Bureau's March 2013 announcement also indicated that the city is encouraging social investment in the local health market, especially in elder care, rehabilitation, mental health, pediatrics, obstetrics, and traditional Chinese medicine. Private hospitals offering these services were promised priority admission to the medical insurance program.

Source: www.perkinswill.com

American operators and investors should be aware that two medical districts are being created in Shanghai: the Pudong International Medical Center and the new Hongqiao International Medical Center. The new international medical centers will include several specialized hospitals currently under construction. According to the medical center's website, the development goals indicate that by year 2015 they are scheduled to finish stage 1 of construction, meet the demand for high-end services in Shanghai and Yangtze River Delta, and become a top hub area for modern high-end medical services in China. Between years 2016-2020 they hope to complete Stage 2 of construction, making it an international general medical center. The centers will work jointly with global leading hospitals, overseas medical groups, and local state-owned hospitals to meet the demand of the high-end market, according to Xu Su, Vice Director of the Shanghai Medical Reform Office. The Vice Director added, "We will also encourage local medical experts to open their own clinics in the shared facility center. Physicians will be encouraged to practice medicine in more than one health facility in line with international practices." The Shanghai government is encouraging future private hospitals located in these areas to cater to high net worth patients as Shanghai's city-level hospitals are scheduled to close their VIP wards by 2015 to focus on providing basic healthcare services.

According to the municipality's Healthcare Bureau, as of March 2013, Shanghai was home to 1,379 private medical institutions: 169 hospitals, 1,201 outpatient clinics, and 9 medical testing centers.

Among them are 8 JV hospitals and 12 JV clinics. Of the 169 hospitals, only 5 have over 200 beds; 80 have 30 to 200 beds; and 84 have fewer than 30 beds. Very few of these are general hospitals, and most specialize in gynecology or are specialist male clinics.

The oncology market in China is expected be a core growth opportunity for foreign investors and operators. Shanghai's cancer rate remains higher than the national average—cancer is the city's second-biggest killer—with nearly 50,000 new cases and 30,000 deaths every year according to a February 2013 announcement by the Shanghai Center of Disease Control and Prevention. Officials announced the city's cancer rate is more than 350 out of every 100,000 people, while the national rate is 286.

One top public Tier-3 cancer hospital in Shanghai logs over 1.4 million outpatient and emergency visits per year, making it one of the busiest in China. The average wait time for a bed at the hospital is three weeks. The institution's good reputation and low cost, thanks to government subsidies, attract patients from well beyond the YRD who make up over three-fourths of the hospital's patients. Foreign oncologists working at a private cancer center in the YRD said many patients will only visit their center after becoming unsatisfied with Shanghai tertiary hospitals. Unfortunately, by then, patients are typically reported to have advanced cancers that are heavily pretreated.

Despite Shanghai's high cancer rate, the oncologists described their center as "underutilized," but pointed to growing patient volume. The oncologists also warned that it is difficult to obtain full disclosure from many Chinese patients. They said that during initial medical consultations, patients deliberately leave out important facts. They reasoned this may stem from a lack of trust or fear of offending their Chinese physician.

Provincial and city governments in the YRD have expressed interest in having foreign healthcare operators and investors establish elder care institutions that specialize in dementia care and rehabilitation. This sentiment was echoed by the China Council for the Promotion of International Trade in Hangzhou, which stressed that hospice care is also needed. In June 2012, the Shanghai Industry and Commerce Administrative Bureau declared its support for foreign participation in high-end elder care services in Shanghai. It is now encouraging registration of both local and foreign commercial elder care services in the city's Pudong District. Dementia affects 10 million people in China, of which over 90 percent of dementia cases in the country are undiagnosed, according to a study published in the British Journal of Psychiatry.

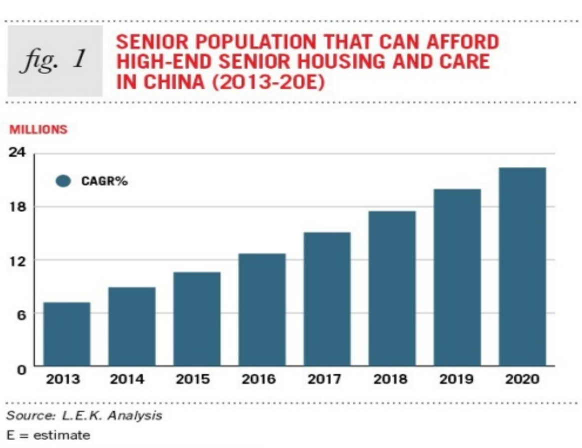
The city's support for elder care is timely: according to the Shanghai Health and Family Planning Commission, the city has more than 3.67 million registered residents aged 60 and above, more than 25 percent of the population. By 2020, the ratio is said to potentially rise to one-third of the total population.

The Shanghai municipal government envisions a "90-7-3" system, where 90 percent of the city's elderly receive home-based care from family or visiting nurses, 7 percent receive community nursing services at senior day care centers, and 3 percent pay for private senior facilities. Local governments nationwide have embraced a similar system. However, nearly 70 percent of elderly people in Shanghai would prefer their children to take care of them at home rather than rely on community services, according to a Shanghai Statistics Bureau survey published in 2013.

During the Shanghai International Forum on Senior Care in August 2013, it was announced that Minhang District will build the first senior nursing pilot zone in Shanghai. The Shanghai Daily reported the zone will have 10,000 specialized beds for seniors and will be completed around 2015. The pilot zone will include professional senior's apartments, communities (Continuing Care Retirement Community) and nursing stations in the neighborhoods. Currently, there are approximately 620 nursing homes for elderly people in Shanghai with around 100,000 beds, according to Minhang District Party Secretary Sun Chao. Secretary Sun further explained that while the majority of senior citizens live at home, their children do not have the time to take care of them, and he hopes that the trial zone will be a model for other regions in the city.

Consumer Spending Power

McKinsey & Company estimates that by 2022, more than 75 percent of China's urban consumers will earn between $9,000 and $34,000 per year. This range falls in between the average income of Brazil and Italy in terms of purchasing-power-parity. Just 4 percent of urban Chinese households were within this range in 2000, but 68 percent were in 2012.



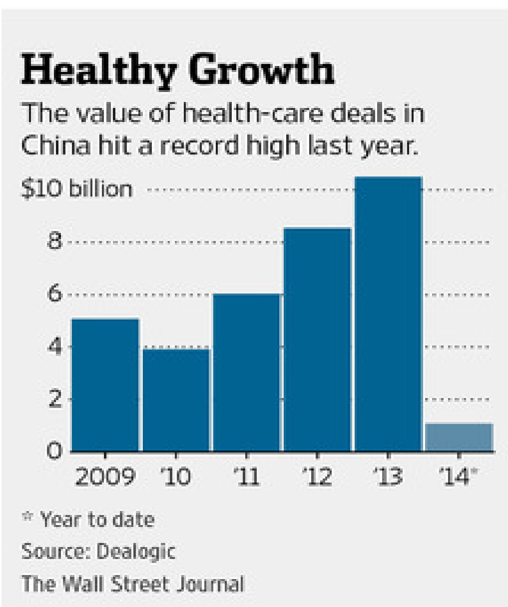
Source: http://www.chinabusinessreview.com/looking-after-chinas-elderly

Although the Chinese are becoming more affluent, the country's per capita gross domestic product (GDP) was just $6,091 in 2012. In an article written by the Global Managing Director of McKinsey & Company, "China's mass middle-class–with annual household incomes of between $9,000 and $16,000–are dominant, accounting for 54 percent of all urban households; upper middle-class households, with incomes of $16,000 to $34,000, represent only 14 percent." By 2022, the article predicts the mass middle-class will dwindle to 22 percent of urban households with the upper middle-class becoming the new mainstream, accounting for 54 percent of all urban households and 56 percent of urban private consumption.

The number of elderly who are able to afford high-end senior housing is expected to reach roughly 22 million by 2020, and seniors currently living in Tier-1 cities, which are China's largest and wealthiest, account for approximately 10 percent of that total.

Confidence Prevails Despite Major Challenges

Healthcare professionals of the Yangtze River Delta Region say that now is the time to enter the markets for private hospitals and elder care. In order to be successful in these markets, professionals stress the need for companies to make a long-term commitment to China and have regular interaction with the appropriate government offices. Since there is no tried-and-true business model in China, it is also essential for companies to be flexible and for business plans to remain fluid.



Source: Investors Rush into China Healthcare. Wall Street Journal

The relaxation of previous restrictive policies is the driving force behind the current boom in the private hospital and elder care submarkets. China's Foreign Investment Guide, effective January 2011, paved the way for healthcare industry modifications. Such modifications included moving hospitals and other "medical institutions" from the category of "restricted" to "permitted." With this change, private and foreign healthcare providers entered the market fairly quickly. The National Health and Family Planning Commission, formerly known as the Ministry of Health (MOH), projects that by 2015, 20 percent of the country's hospital beds as well as inpatient and outpatient volume will be managed by private hospitals.

Statistical evidence also demonstrated that the central and Yangtze River Delta region governments are welcoming more private investment. In June 2012, there were 9,097 private hospitals in China, which was almost 21 percent more than the number of private hospitals in 2011. Shanghai's

National Health and Family Planning Commission estimates that over 300 private hospitals have been approved in Shanghai alone over the past 3 years; these cover 6 percent of the city's health services. Despite the growth in the number of private hospitals, profit has not come easy for most private medical institutions. Healthcare operators estimate that only 3 to 20 percent of the YRD population can afford private healthcare. This issue is the cause of why many hospitals, clinics, and elder care facilities suffer from the "empty hospital syndrome." Compounding this issue, many state-owned hospitals rarely refer patients to private institutions since it is not in their economic interests. Government subsidies to state-owned hospitals are based on inpatient and outpatient numbers, so referrals to private institutions are uncommon.

Private hospitals have been able to overcome the issue of referrals by having an internal referral system. Gaining a reputation for high-quality care and integrity are vital to increasing overall patient volume, according to industry professionals. These professionals also note that hiring well-known Chinese physicians can be the cornerstone of success for medical institutions hoping to attract higher-income Chinese patients. When given a choice of physicians, Chinese patients prefer distinguished Chinese physicians over Western ones.

American healthcare operators looking to export their services to China should remain cognizant that it will take time to create value in private healthcare services, and wealthy Chinese people will be the driving force in starting a new trend of value. Private healthcare operators predict that in the next decade, the rise of a large, urban, affluent population in China will make up the majority of their patients. Still, private institutions find ways to expand by catering to less affluent populations as well. For example, the first large-scale U.S. joint-venture hospital in China will offer all major specialties and will serve public-and private-paying patients.

An Overburdened Public Healthcare Industry

According to the former Ministry of Health, in March 2012, the ratio of public hospitals to private ones was 3:2. Even though public hospitals outnumbered private hospitals, the estimated wait times at public hospitals was 30 minutes longer than private hospitals. Patients at famous, state-owned Tier-3 hospitals often wait in line for an average of four to five hours before seeing a physician. This appointment is usually three to four minutes long with little to no privacy.

KEY HEALTH STATISTICS	CHINA	U.S.	JAPAN	WORLDWIDE
Hospital Beds / 10,000 Population	42	30	137	30
Number of Physicians	1,905,436	749,566	274,992	8,652,107
Physicians / 10,000 Population	14.2	24.2	21.4	14.2
2000 percent of GDP Spent on Healthcare	4.60 percent	13.40 percent	7.70 percent	5.80 percent
2009 percent of GDP Spent on Healthcare	5.10 percent	17.60 percent	9.50 percent	6.60 percent
2000 Government Spending as percent of Healthcare	38.30 percent	43.20 percent	80.80 percent	57.60 percent
2009 Government Spending as percent of Healthcare	52.50 percent	47.70 percent	82.30 percent	61 percent
2000 Per Capita Healthcare Spending in US$	$43	$4,703	$1,974	$106
2009 Per Capita Healthcare Spending in US$	$191	$7,960	$3,045	$292
Gross National Income per capita	$7,640	$47,360	$34,640	$6,965

Source: WHO Global Healthcare Statistics: 2012

Although China's 2012 White Papers claim that it is becoming more convenient for people to receive medical care, the general public finds the government's inability to provide basic healthcare in the event of a health crisis. This is one of the reasons why the national savings rate is close to 40 percent of Gross Domestic Product (GDP).The lack of healthcare support is most evident within elder care. The number of people aged over 60 reached 194 million last year and is expected to top 200 million this year. A China Daily article recently highlighted the lengths a Beijing woman went in order to find a bed in a state-owned residence home for her aging father. The woman reportedly knocked on the doors of several institutions, including one of the best, and was told that she would have to join a waiting list of several thousand. The article underscores the reality that many Chinese citizens face when finding a bed at a senior residence home.

An announcement in March 2013 by the Minister of Civil Affairs, Li Liguo, promised that the Chinese government would roll out preferential policies for private investors in industries that provide services to the aged. Private investors in some regions will receive subsidies in addition to tax reductions to set up care centers and perform their daily operations. However, private elder care operators and investors should be aware that while the Chinese government is encouraging foreign investment, China's poverty levels for the elderly are high relative to the United States. According to the results of the China Health and Retirement Longitudinal study (2011-2012)— the first large-scale survey of Chinese over the age of 60, 22.9 percent—or 42.4 million—live in poverty on an annual income of less than $523 a year.

Still, private elder care operators in the YRD are confident about the fledgling market's potential due to China's aging population. However, they advise caution, clarifying that the Chinese government is still developing its laws on private elder care and that people are not willing to pay for services they are not familiar with. Overall, the elder care submarket is still young and private elder care institutions remain underutilized like many private hospitals.

A way to alleviate such issues is to build relationships with the local government and relevant health and civil affairs bureaus before entering China. Negotiations regarding subsidies and reimbursement agreements should also begin early.

Competitors: Politically Domestic but Commercially Foreign

The Cross-straits Economic Cooperation Framework Agreement between China and Taiwan in 2010 allows investors from Taiwan to establish wholly-owned hospitals in Shanghai and Jiangsu province. The agreement also includes Fujian, Guangdong, and Hainan provinces. Similar agreements with Hong Kong and Macau allow the two Special Administrative Regions to set up wholly-owned hospitals in Shanghai, Chongqing, Fujian, Guangdong, and Hainan provinces. When the Shanghai Landseed International Hospital opened for business in 2012, it became the first wholly Taiwan invested hospital in the Chinese mainland. However, Taiwanese hospitals like Landseed and BENQ are essentially empty according to executives working for private hospitals in Shanghai. Healthcare veterans in the YRD have said that other than speaking a common language and having firsthand knowledge of the Mainland China market, "politically domestic but commercially foreign competitors" do not have an advantage over American operators in China's private healthcare space.

With no change in sight for financial lending reform, wholly foreign owned medical institutions will continue to rely on foreign loans for financing, which puts them at a disadvantage relative to Chinese institutions that are eligible for low-interest loans from Chinese banks. Therefore, even though the Chinese have given a green light to foreign investors and provided a fairly level playing field, only investors from Taiwan, Hong Kong, and Macau can easily open the door, according to industry professionals.

It remains challenging for Taiwanese hospitals to compete with their counterparts in the Chinese mainland since Taiwanese hospitals are not covered by China's health insurance. Moreover, Taiwanese physicians are not allowed to transfer their license to practice medicine in China. While Taiwanese physicians need to pass all the necessary exams to practice in China, the Chinese government also stipulates that a hospital needs to hire "senior" or "director-level" physicians for certain departments, positions which are only open to mainland physicians. These have become major problems that increase the cost of running hospitals in Mainland China for Taiwanese companies, according to a July 2013 Want China Times article.

Industry Challenges: Licensing and Regulations

Obtaining the license to open and operate a private hospital in China is a complicated and lengthy process since it involves attaining legal representation. Most healthcare operators have found that most opposition toward getting a license or permit comes from the local level. As the Chinese saying goes, "The central government has policies, the local government has counter-policies." This means while the central government in Beijing determines China's laws and regulations, decentralization puts the implementation and enforcement in the hands of the provincial and city governments. This method of enforcement can lead to inconsistent interpretation of national regulations from province to province and city to city. As a result, the private healthcare sector has largely remained untapped.

In addition to licensing, establishing a clientele in China is also a lengthy process since it requires time to build a reputation and gain a patient's trust. Word-of-mouth methods are seen to be the most effective marketing method, while targeting wealthy customers is not.

As foreign healthcare companies are looking to enter the China market, it is important to note the effects of China's One Child Policy on society. The policy created a concept known as the "421" family structure. This means that once grown, the only-child is responsible for both parents and four grandparents. In China, the concept of filial piety still exists, so secondary care-giving is usually not the preferred option but will be considered if that family member's medical requirements cannot be met at home. Since this market is relatively new, China has no developed regulations and many American elder care operators are forced to self-regulate and use U.S. standards.

In the medical device sector of the healthcare market, a recent change has been made to regulatory obligations for Class I and Class II devices. The Original Regulation required that registration certificates be obtained from the China Food and Drug Administration (CFDA) or its local offices for *all* medical devices—regardless of whether it was a Class I, Class II or Class III product—before the devices could be marketed in China. Under the Revised Regulation, no registration certificate is required for Class I medical devices, whether they are imported or manufactured in China. Instead, a filing with CFDA or its local offices will suffice. Recently, China has relaxed some of its stricter regulations, so large-scale policy changes are possible in the next coming years.

Industry Challenges: Professional Staff

Besides licensing and regulations, the next biggest hindrance for prospective healthcare operators in China is finding capable staff. A 2012 journal articles from *Health Policy and Planning* reported that 22 percent of the physicians that work in private hospitals are over the age of 60, whereas this figure is less than 3 percent in public hospitals. Private healthcare operators compete with their public counterparts for well respected, experienced Chinese physicians in their prime working years.

A health consultant and physician in Shanghai urged private healthcare institutions to have marketing based around bringing in big name physicians from famous Chinese hospitals such as Peking University First Hospital, Hengshan Hospital, Rujin Hospital, etc. Chinese patients typically want the most respected Chinese physicians available. This preference does not change even when Mandarin-speaking physicians or bilingual nurses are available. Having a local partner may benefit an American private healthcare company in recruiting a well-known Chinese physician, since the likelihood of attracting one to a private hospital built from scratch will be difficult. This difficulty may not apply to internationally renowned healthcare institutions.

Another obstacle in hiring qualified staff is that in 2009, the former MOH revised a rule under the Medical Practitioners Law, which allows Chinese physicians to work in multiple locations only with the approval from the primary hospital. According to a *Caixin* article, home institutions are known for disapproving requests unless the physician is an established senior physician or department chair.

Since most physicians are unwilling or unable to leave the public sector, most Chinese physicians that work in the private sector are either recent medical school graduates or retired physicians from public hospitals. Other obstacles preventing Chinese physicians from going into the private sector include retirement benefits and the inability to climb the professional ladder. Although the private sector offers a higher salary, many Chinese note that the total income (including pension) is greater in the public sector because physicians can expect to receive 80 to 90 percent of their salary in retirement. Chinese physicians also find that when joining the private sector, they are excluded from the traditional Chinese medical community and prominent associations.

The issue of staffing within the private sector is most evident within elder care. China will need 11 million caregivers to care for 33 million elderly with various disabilities. Unfortunately, China has a severe shortage of elder care professionals. Many Chinese avoid the profession because of the heavy workload, low pay, and social stigma attached to it. In order to properly care for the elderly, China will need to increase its efforts to recruit and train its staff. This challenge offers a good opportunity for foreign training companies.

Industry Challenges: Land

Similar to other commercial real estate projects, land acquisition can be very difficult. In China, patronage can trump "rule of law", and the land auction system can appear opaque. Foreign healthcare companies and investors in both the private hospital and elder care submarkets often rely heavily on local partners or property developers. Searching for a plot of land for two or three years is not uncommon.

Those looking to build a new hospital in Shanghai will find that building permits are only available in the city's Minhang, Changning, and Hongqiao suburban districts. Obtaining property in the largest YRD cities for any purpose is lengthy and expensive; this is true in all of China's first-tier cities. For foreign entities that need land but cannot afford to purchase it, joint ventures or working with a real estate developer can be more cost effective.

Conclusion

There is currently abundant room for growth in China's healthcare industry. At the moment, the country's healthcare spending only accounts for 5 percent of GDP. Relative to the healthcare spending in the United States and other OECD countries, which have health spending to GDP ratios of 17 and 10 percent, respectively, China's spending is low. The Chinese government does recognize the gap that exists between them and these other countries, and is redirecting its attention and investment to developing the healthcare industry (Source: US-China Business Council).

China's burgeoning private healthcare space offers many opportunities to American healthcare operators and investors. Private hospital and elder care companies are benefiting from the country's ongoing reforms, rapidly aging society, and increasing disposable incomes in the YRD. The demand for better- quality medical care is strengthening as the emerging middle-class adopts a more Western diet and sedentary life styles, causing the incidence of chronic diseases like diabetes to increase. Described as a once in a lifetime opportunity by healthcare professionals in the YRD, China's private hospital and elder care submarkets offer alluring prospects to American investors and operators looking to export their products and operational know-how.

Although China offers many opportunities, significant legal and operational challenges exist. To succeed, private medical institutions should not solely focus on general medicine but also specialize in fields that are growing in demand, such as cardiology, oncology, pediatrics, and geriatrics. Operators and investors looking to make quick profits will be frustrated by China's evolving private hospital and elder care submarkets. However, companies will find long-term success by refining their business practices to offer cost-effective health solutions for China's growing middle-class and their aging parents.