The innovation driving investment in digital health

The healthcare industry is facing increasing challenges, with budgets going down, qualified talent becoming harder to find and waiting times for patients on the rise. However, the huge pressure on national health systems to improve health outcomes and bring down costs is driving high levels of innovation within digital health, Romain Ellul, managing director of healthcare at Bryan Garnier & Co, explains.

Historically, Europe has lagged the US in terms of healthcare digitalisation. In 2021, 73% of hospitals in the US were digitalised versus just 19% in Germany for example. This has prompted efforts by European governments to implement modernisation plans, which is boosting investment interest in digital health in Europe. In addition, the pandemic was a catalyst for the digitalisation of healthcare. Healthcare delivery was completely disrupted by the pandemic, resulting in new models of care such as digital and homecare being tested, which proved to be more accessible, flexible, agile and efficient. As a result, investment in digital health skyrocketed, both during Covid-19 and in the period that has followed.

Private equity and venture capital funds raised record amounts of capital and increased their exposure to healthcare and digital health. They continue to aggressively seek opportunities in the sector. In addition, healthcare special purpose acquisition companies (SPACs) have been on the rise, with record levels of capital available to invest in the sector. M&A activity in healthcare has also soared, at record valuation levels.

But where is capital flowing? What are the hot areas of healthcare innovation that are attracting investment interest?

- AI to support, enhance or replace human diagnostics
- Telehealth to improve accessibility and breakdown the geographical barriers to accessing healthcare experts
- Advanced medical imaging to capture higher resolution patient data and improve diagnostics
- Digital therapeutics to enhance and support drug and traditional therapies.

Reality check

There is still a lot of interest in healthcare and digital health in particular is one of the most innovative subsectors that continues to experience investment interest. However, the hype has died down and markets have slowed down. A lot of money has poured into the sector and now investors are waiting to see the results.

In Q1 of this year, we have seen:

- Digital health funding decrease by 36% when compared to Q4 of 2021.
- Mega-round funding decrease by more than half, as investors backed fewer $100 million+ deals in digital health startups quarter on quarter.
- A significant drop in digital health IPOs.

In addition, public digital health companies have seen their valuations fall. For example, Teladoc is now worth $4.6bn after falling 77% in a year; Babylon Health dropped by 88% over 52 weeks to a value of half a billion dollars and Pear Therapeutics' value decreased by 63% in a year.

There are always ups and downs in innovative industries, especially in such extraordinary times, and, in this case, it is possible that the hype surrounding digital health led to investors overreacting, which can help to explain both the very high valuations and the significant falls.

Now, investors and strategics are being pickier with assets and looking for specific solutions that add-value. Investors want quality digital health technologies that can deliver clinical results, cut through rigorous regulation and have the ability to scale.

The regulatory tailwinds driving the growth of digital therapies

An area of digital health which is gaining traction as investors search for quality assets is digital therapeutics. Since the FDA in the US first approved the prescription of a digital therapy in 2017, tens of therapies have followed.

In Europe, access to quality care is heavily restricted by geographical location, which results in only 25% of patients receiving the mental health support they need. In addition, there is an average waiting time of 5 months for access to mental health therapy in Europe, demonstrating the shortage of available support. Digital therapies can help to overcome these hurdles and also offer a non-drug alternative, which 75% of patients have indicated they prefer. The impact of the pandemic on mental health globally created an even greater need for these solutions.

We expect that many more products will come onstream with substantial financing and investor support, especially given the regulatory tailwinds coming from European governments as they attempt to increase the adoption of digital therapeutics.

In November 2019, Germany passed the Digitales Versorgungs Gesetz (DVG), a law to improve healthcare delivery through innovation and digitalisation. The scheme, known as DiGA (Digital Health Applications), allows patients to be fully reimbursed by their insurance provider when they are prescribed digital therapies. This regulatory change in Germany increases the legitimacy of digital therapies in the minds of patients and practitioners. From an investor's perspective, it deals with the previously tricky question of who would pay for these therapies.

In Germany, the market size for DiGA is expected to reach €125 million in 2022. France has also announced it intends to replicate a DiGA-like framework to enable rapid access to digital therapeutics, the new rules are expected to come into force in July this year. In May 2022, NICE (National Institute for Health and Care Excellence) in the UK made a groundbreaking move by approving the prescription of an app called Sleepio for insomniacs, bolstering investment in digital health.

A phygital approach

Despite the growth of digital health and its endorsement by governments, we are seeing more and more digital companies either signing partnerships or investing in some kind of physical presence or direct human interaction as well. In addition, historical bricks and mortar healthcare players, such as hospitals and clinics are investing in digital solutions, in order to combine the best of both worlds.

On their own, digital health solutions may not be enough. In the US, recent legal issues surrounding the delivery of abortions as a result of telehealth consultations highlight the constraints of a purely digital approach. Similarly, an online mental health service is under investigation by the US Department of Justice in relation to its advertisement and prescription of controlled substances including Adderall and Xanax.

We believe the answer lies in a phygital system: a combination of both physical / human and digital. We are increasingly seeing the physical and digital worlds coming together, for example the use of innovations such as the parallel use of sensors and digital applications, biopsies and AI, and robotics implants and digital applications. Remote patient monitoring is also a good illustration of the physical and digital worlds coming together.

The healthcare sector has traditionally been averse to digitalisation. However, considering the growing demand for healthcare services that are efficient and cost-effective, integrating digital solutions will definitively lower the cost of care and improve access to healthcare. For a phygital approach to work efficiently, practitioners, patients, governments, payors and pharmaceutical actors will have to familiarise themselves with digital health solutions to find the best value chain and division of labour between physical and digital.

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