



Healthcare Industry Report 2024

A brief insight into the healthcare sector

Oakwood Fund

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Overview

The post COVID-19 healthcare boom has resulted in a dynamic shift within the sector. With industry growth normalising and accounting for the 2021 anomaly, funding within healthcare is still strong and on an upward trajectory.

Life expectancy has increased as well as continuous findings of new treatments have led to labour shortages and a rising need for medical care, posing new challenges for the sector through both a rising and ageing population. A focus on AI and robotics provides long term solutions. Alongside global economic uncertainty, these are some of the key drivers that will impact healthcare in the upcoming years.

As the focus on AI grows stronger, the biotech sub-sector shows investor preference towards large-cap biotech stocks outperforming the wider industry.

The recent election of Trump may result in increasing import tariffs thus increasing costs of healthcare products in the short run. Companies will temper these tariffs through alternative supply chain routes. Despite short term uncertainties, firms will find solutions in the long term and US markets will correct and account for short term price changes.

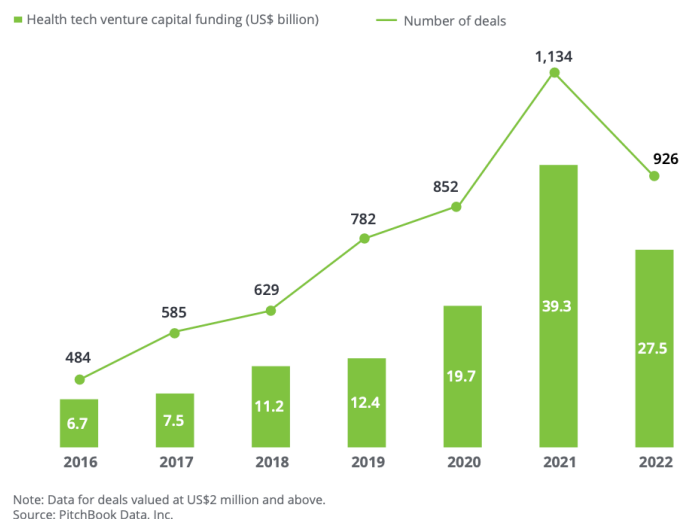
Looking at our current portfolio, both stocks present a good long-term growth opportunity over the next 5 years. Novo seems the less volatile of the two stocks with ClearPoint experiencing short-term fluctuations in stock price and is currently unprofitable. A close eye should be kept on the stock and a revaluation should take place post Q1 earnings of 2025.

Past Performance

Recent Industry Developments

With the recent COVID-19 pandemic, lingering effects of labour shortages and rising costs are more prevalent than ever. The sector has also been buoyed by new developments in the tech sector with integrations of AI as a means to address issues proposed by the pandemic. With the US healthcare sector being privatised, with health inequities potentially tripling to \$1trillion by 2040. As costs continue to escalate, affordability for healthcare has become a major concern. The healthcare workforce is also undergoing significant transformation and transitioning into a less labour-intensive sector.

Touching on AI further, the introduction of AI into the US healthcare system is predicted to save \$360 billion annually over the next 5 years. The global healthcare sector generated over 2.3 zettabytes of data worldwide in 2020 and the implementation of AI will be able to process and transfer data globally (1). AI can also analyse large datasets and spot potential health trends within a population, naked to the human eye. However, with the ever-growing and integration of AI, regulation is becoming more and more of a concern. With governments worldwide taking action to establish effective regulation. The disparity in approaches to regulation and monitoring differ from country to country which could pose additional challenges to healthcare providers and subsequently the sector as a whole.



Currently, 3.3 billion people live in countries that spend more on debt servicing than on healthcare and education. In countries like the US with privatised healthcare systems, the

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average individual spends \$12,500 on healthcare (1). On top of increasing costs, increasing average life expectancy, especially in developed countries, has resulted in a drive-in growing need for long-term care further increasing demand for healthcare workers already at full capacity with 87% of US healthcare workers listing staff shortages as their biggest challenge. With the WHO projecting a shortfall of 10 million healthcare staff by 2030, 55 countries fall under the number of healthcare workers deemed sufficient by the WHO (2). With an understaffed sector, burnout has been reported to a key cause of labour shortages, with 49% of US physicians reported to have had burnout in the past two years (3). A key solution is the integration of technology as stated before through AI to decrease job demands. Using technological tools, clinicians have reported saving near 7 minutes per patient. By reducing workloads and improving efficiency, further investment and improvements in technology will likely be the solution to current issues within the sector. However, these solutions do not address the ageing population driving higher healthcare costs per capita.

Sub-Sector Insight:

Biotech makes up about 11% of the wider Healthcare industry. Biotech stocks represent companies that develop treatments, conduct research, and provide medical technologies. A focus on profitability within the Biotech sector has never been stronger. Since the tightening of monetary policy with Bank of England base rate increasing from 0.1% in 2021 to as high as 5.25% in mid-2024, Investors now place much greater emphasis on large, reliable Biotech stocks as opposed to riskier, up and comers (4). This is due to most smaller Biotech stocks operating at a loss for years before a final product comes onto the market. Operating at a loss during a 5% interest rate environment is not sustainable for most companies, leaving them with high levels of debt or causing bankruptcy. Smaller Biotech stocks are also at higher risk of not getting commercial approval on their products from the MHRA, the UK regulator, or in the US, the FDA. This has the potential to cause smaller Biotech stocks entering financial difficulties. Many pharmaceutical companies have resorted to looking to be bought out by industry leaders such as AstraZeneca. As a result of this, Investors have flocked to large-cap Biotech stocks. Over the last 12 months and 3 years large-cap Biotech stocks have outperformed other healthcare sectors.

For example, Vertex Pharmaceuticals (VRTX) is up 32.39% in the last 12 months and 156% in the last 3 years. They specialise in cystic fibrosis medication such as ivacaftor and lumacaftor (5). United Therapeutics Corporation (UTHR) is up 62.55% in the last 12 months and 94.06% in the last 3 years. They specialise in life-extending technologies for patients with lung disease or organ failures (6). Meanwhile, the wider Biotech industry is up 20.05% in the last 12 months but down 17.53% over the last 3 years due to the sector adjusting to post pandemic slowdowns in demand.

Analyst insight:

This section analyses the performance of the healthcare industry in Q3 of 2024. The S&P 500 health index has diverged from the growth trend of the overall market settling on a 1-year performance disparity from 32% to 12%. This is due to the broader rally of big technology (AI) and consumer discretionary sectors as robust consumer spending continues, reflected in retail trade. There has been post COVID-19 pain felt by firms that have struggled to come up with anything promising such as Moderna. The stock has highly underperformed -45% y/y (7). However, they have now moved onto using their mRNA platform to develop other vaccines but

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also expand margins to make their Covid-19 operation successful again. This provides some hope and gives some ground for a possible turnaround story going forward.

Next, we shift our focus onto Medicare's price negotiations as mandated by the inflation reduction act. Imbruvica is set to face a price reduction of up to 38% in 2026 straining revenues and margins as a result. In summary, pharma companies with greater exposure to Medicare part D and B will see the most negatives sales impacts. With reduced margins, a close eye should be kept on whether competition and innovation take a hit because of these government interventions. Another development that deserves insight was Eli Lil and their weight-loss/diabetes drugs Zepbound and Mounjaro coming up short on Q-3 earnings day, joined by rising operating expenses saw their EPS release at \$1.18 compared to the \$1.47 analyst consensus (8). Their direct competitor of weight loss drugs Novo Nordisk also followed suite with subpar sales numbers in Ozempic and Wegovy compared to higher analyst expectations. This is reflected in their respective share prices. Going forward it will be interesting how these highly touted weight loss drugs perform and whether these revenue misses are setting a new precedent or are isolated growing pains in a new market.



Future Outlook

Macroeconomic Outlook:

Over the next 3 months, the macroeconomic environment is likely to shift. With the upcoming re-election of Trump, the beginning of 2025 could be an uncertain time for the Healthcare industry. Throughout his election campaign, Trump promises to implement tariffs of 20% on all imports into the US and a unique 60% tariff on Chinese imports. Importantly, the additional cost of the tariff is paid by the importing economy, not the exporting economy. This means the tariff will mean 20%-60% higher prices for US consumers on imported goods (9).

There is likely to be two main consequences of this: Firstly, for US Healthcare providers, there over-reliance on overseas supply chains in the production of pharmaceuticals could cause issues. In 2021, the US reported that “the country remains critically dependent on imports for a range of key pharmaceutical products and APIs (Active Pharmaceutical Ingredient)”. This reliance on the rest of the world for the pharmaceutical supply chain may mean that increased import costs translate into significantly higher drug costs and healthcare premiums for consumers both in the US and worldwide. With healthcare inequities already on the rise, further tariffs on healthcare imports will leave an even greater proportion without health insurance/coverage.

Secondly, Trump’s proposed tariffs negatively affect interest rates. Only recently has the head of the Federal Reserve, Jerome Powell, been in a position to cut interest rates which currently stand at 4.5% (10). Markets have been pricing in higher interest rates after the result of the US election as Trump’s tariffs will lead to higher inflation when introduced. This will mean the FED will have to hold rates higher and for longer in order to prevent further inflationary rises. For the Healthcare industry, where many firms operate at a loss in the development stages of new drugs, this might result in bigger losses and potential bankruptcies as smaller firms can’t stay afloat. The higher interest rates in the US may also have the added result of a strong dollar, which may cause US exports to become more expensive for the rest of the world. This would make them less internationally competitive with rival healthcare providers overseas. Potentially resulting in lower global market share for US healthcare providers in the Healthcare industry.

In summary, as the US prepares for the return of Trump, uncertainty over his economic policy is growing. If Trump decides to implement his tariffs, the result will be higher prices and inflation for US consumers, including in the healthcare sector, which is particularly reliant on imports. These higher costs will translate into higher prices for consumers and therefore potentially lower demand and profits for healthcare firms. Price rises will contribute to higher inflation, encourage interest rates to stay higher for longer, potentially resulting in greater losses for smaller healthcare firms. The higher interest rates will likely result in a stronger US dollar, resulting in less competitive exports for US healthcare providers furthering the divide in healthcare inequity.

Current Portfolio Analysis

Novo Nordisk A/S - A global healthcare company specializing in diabetes care, obesity management, and other serious chronic diseases.

Buy in – 01/12/23, \$99.86 per share, allocation of \$714.00 holding 7.15 shares.

Current market price, 05/12/24 - \$108.82

Gain/Loss – appreciation of 8.97%

Position value - \$778.06

Compared to market competitors, LLY, AZN, JNJ, MRK, Novo outperforms the majority with only LLY obtaining a higher price return. With the average ROI within the pharmaceutical sector at 4.1%, NVO exceeds market expectations.

Investment Rating: 3 - hold

The stock offers promising growth with strong financial metrics. The stock shows strong potential to hold as a growth stock with diluted EPS rising 27.2% since last year's quarter. The company is in control of 65% of their respective market in GPL-1 drugs treating obesity and type 2 diabetes meaning there is no shortage of demand for the product. Despite a P/E of 31.5, and recent sell-off leaving share prices at lows, its promising control over market share alongside strong financial growth, the stock is a definite hold and foresees promising returns as a hold-stock in the long term.

ClearPoint Neuro, Inc. - A healthcare company focused on developing platforms for performing minimally invasive neurosurgery.

Buy in – 15/03/24, \$7.17 per share, allocation of \$714.00, holding 99.58 shares.

Current market price, 05/12/24 - \$12.62

Gain/Loss – appreciation of 76.01%

Position Value - \$1,256.70

Market competitors consist of CVRX, DCTH, NPCE, ZIMV, NYXH. With an expectation for the neurosurgery market to expand at a CAGR of 4.4%. With CLPT providing equipment in the growing sector, the stock price has surged reflecting the increased demand in the product.

Investment Rating: 2 – hold/sell

With the stock having returned 76.01% since March already, the stock has experienced strong YoY growth, but the stock reacted negatively likely due to high valuation and weak sequential growth. Short term volatility is likely to occur but with improving margins and minimal cash burn, concerns about dilution can be eased. Despite a high revenue multiple, the stock has long-term potential and is

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undervalued in the long run. However, the stock is currently unprofitable and forecasted to remain unprofitable over the next 3 years and shareholders have been diluted in the past year. Accounting for concerns, a long-term hold is likely the best approach for this stock.

To summarise, both Novo and ClearPoint Neuro offer promising long-term upsides with a hold recommendation with a slight preference for Novo. As ClearPoint has unrealised profits of 76% and unprofitable in the short run, both holding for long-term growth and selling to redistribute returns are viable options.

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