Bellevue Asset Management

Market commentary May 27, 2020

A safe place in the event of unexpected coronavirus troubles

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The medtech & services sector continued to display its defensive qualities amid the corona crisis and performed relatively well while the market tanked. Covid-19 is likely to have an only mild, temporary effect on this sector's fundamental factors. The sector's resilience can be traced to the non-cyclical nature of market demand for its solutions. Many health problems must still be treated regardless of the crisis (e.g. heart issues, bone fractures, etc.). That said, during the height of the pandemic, less urgent procedures such as hip and knee replacement surgery did have to be postponed. These operations were not permanently canceled, though – they will be performed at a later point in time, which will boost underlying demand when the time comes. Even a recession would have little impact on the medtech & services sector because demand as well as prices are very stable, the latter due to the reimbursement of costs from health insurers.

Return to normalcy

The course of the global Covid-19 pandemic and the availability of diagnostic tests are factors that will help to usher the world back to a normal state. Germany is already in the midst of the recovery phase. In the US, several states have eased stay-at-home orders and a general return to normalcy there is likely from mid-June on. This projected development corresponds to the desired outcome we outlined at the beginning of the crisis.

The trends are pointing in the right direction, especially considering that statements by government officials and medical associations support the forecast of a market recovery in the fourth quarter of 2020. We therefore expect a return to normal market growth by year-end – and we might already see a sequential acceleration in growth in the third quarter. Against the backdrop of the largely positive company earnings announcements for the first quarter of 2020, this scenario is also encouraging for investors.

US health insurance stocks heavily discounted

Inexpensive US health insurers strong in administering managed care benefits that the US government has turned to in an effort to make the healthcare system more efficient would be hardly affected by a recession and are thus a good hedge for any unexpected Covid-19 troubles. Neither Joe Biden nor Donald Trump have advocated policies that would be negative for the managed care sector. A future rise in costs can be calculated into the health insurance premiums that insurers charge for 2021. Despite its clearly better-than-average outlook, this sub-sector is trading at a 20% discount to the S&P 500 and therefore offers significant upside potential.

A significant acceleration in growth is particularly likely at insurers that specialize in Medicaid, the government program for low-income households, or in health insurance marketplaces. Even insurers who do much of their business in the commercial health insurance segment are likely to report an only mid-single-digit decline in earnings next year, which would be due to a decline in the number of insured persons.

Focus on large caps

Large cap stocks are overweighted in the fund's portfolio, which enhances its stability. Considering the above, besides the Medicaid players such as Centene and Molina, insurers that are strong in administering Medicare benefits, Humana for instance, appear attractive. Other portfolio companies that offer good upside are Stryker, a manufacturer of orthopedic and surgical implants, and Inspire Medical, which is concentrating on innovative approaches for treating patients with obstructive sleep apnea.

Significant outperformance

BB Adamant Medtech & Services’ 3-year performance of nearly 55% represents an excess performance of more than 36 percentage points over the MSCI World Net Index. The fund has performed even better compared to the EuroStoxx 50 Index, racking up an excess performance of more than 67 percentage points. The fund's trailing 12-month performance is 13%, which beats the performance of the MSCI World by 10 percentage points (all data as of May 22, 2020).

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