BB Healthcare Trust

Monthly News
May 2018

As at 05/31/2018	Value	1 Month (May)	YTD	Since Launch (ITD)
Share	121.50	8.48%	5.08%	25.32%
NAV	122.06	9.95%	10.51%	26.00%

Welcome to our May update. The halcyon days of summer are not officially upon us, but the British psyche errs to optimism on the weather front as spring comes to its end. This can lead to some unfortunate choices on the wardrobe and activity front as Zephyrus plays his games. No matter though, we Brits "keep calm and carry on". Apposite words for our Trust, as we traverse a challenging course through this volatile period.

Summary

BB Healthcare Trust is a high conviction, unconstrained, long-only vehicle invested in global healthcare equities with a max of 35 stocks. The target annual dividend is 3.5% of NAV and the fund offers an annual redemption option. BB Healthcare is managed by the healthcare investment trust team at Bellevue Asset Management, which also manages BB Biotech.

The Idyll of Summer awaits…

Over the month, the Trust's ex-income net asset value (NAV) rose 10.0% to 122.06p; a pleasing 6.2% outperformance versus our benchmark. Sterling continued its retreat, mitigating the currency-related losses suffered earlier in the year. We estimate that the relative appreciation of the dollar contributed 3.4% to the positive development of the NAV this month, although we are still carrying an overall negative currency impact of >6% since inception.

The MSCI healthcare benchmark rose 3.8% in sterling terms, but only and 0.2% in US dollars as healthcare again trod water through a noisy period, for both healthcare and the broader market (the MSCI World Index also moved by only 0.3% in dollars during the period).

With specific regard to healthcare, the key debate remains the potential impact of the US drug pricing policy initiatives outlined by the President Trump on May 10. As ever with pusillanimous politicians, rhetoric (bluster?) apes actual content. In fact, the worst-case scenarios of direct government price negotiation ("only works if you are willing to deny access") and wholesale drug importation ("a gimmick") were taken off the table (at least for the lifetime of this Administration).

HHS Secretary Azar has suggested that reactions to the Trump initiative are too complacent, emphasising that many of the Administration's goals can be implemented through Executive Orders. Time will tell, but the collective opinion of other members of Congress, the Healthcare Industry and innumerable Washington watchers suggests this is more bark than bite.

Sell in May and walk away?

Nonetheless, the take-away for investors was 'risk off' for drug stocks and the interconnected supply chain. One cannot ignore the reality that drug pricing is easy cannon fodder for the mid-term campaign, so this attitude is likely to persist for several months yet.

All this is going on whilst the overburdened generalist must contend with yet another Euro debt crisis, a volatile oil price, trade wars and ongoing geopolitical instability. Perhaps the person to first utter the fabled curse "may you live in interesting times" was addressing it to a custodian of other people's wealth!

Given such a backdrop, it is probably no surprise that Large-Cap pharma / Conglomerates, Biotech and the Distributors have been the worst performing sub-sectors this month (Figure one below). Although our holdings in the Large-Cap pharma category are limited to Shire (arguably now a special situation), we are exposed to the latter and we have been surprised at the extent to which the supply chain has been punished for the 'sins' of the manufacturers.

Valuations in this group now stand at multi-year lows (Figure 2). Even if brand drug price inflation does ameliorate, it is a still struggle to rationalise why the market has become so bearish, especially as the headwinds of year-on-year generic price erosion (which creates both inventory de-valuation risk and margin pressure for wholesalers) seem finally to be abating after a more than two year negative trend (cf. the recent strong performance from the generic group in Figure one). That said, it is also difficult to see what would prompt the fickle market to change its mind in the short term, although we are nothing if not patient.

BENCHMARK SUB-SECTOR PERFORMANCE AND WEIGHTINGS

Sub-Sector	Weighting	Performance (USD)	Performance (GBP)
Biotech	10.4%	-1.1%	2.4%
Conglomerate	12.5%	-2.2%	1.2%
Dental	0.6%	23.1%	27.5%
Diagnostics	1.9%	8.4%	12.3%
Distributors	1.9%	-9.2%	-5.9%
Facilities	1.1%	2.8%	6.5%
Generics	0.7%	8.9%	12.8%
Healthcare IT	1.2%	1.5%	5.2%
Managed Care	9.6%	0.2%	3.7%
Med-Tech	13.8%	2.3%	5.9%
Other HC	0.9%	0.3%	3.8%
Pharma	35.0%	-0.2%	3.4%
Services	2.6%	2.0%	5.7%
Specialty Pharma	3.5%	4.0%	7.7%
Tools	4.1%	-0.1%	3.5%

Source: Bloomberg/MSCI and Bellevue Asset Management. Weightings as of 30-04-18. Performance to 31-05-18.
*Note: DexCom is no longer in the benchmark, effectively removing the Health Tech sub-sector

Figure 2: forward P/E mutiples of US distributors are at multi-year lows

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Is it the drugs, or just pharma?

In the US, the extent of the divergence in performance between the pharma-like Large-Cap biotechnology stocks versus their innovation-led Small and Mid-Cap brethren is also noteworthy: +1.6% versus +11.0% respectively year-to-date. Pharma's woes are not just political; we have seen mixed pipeline news flow, compounding already diminishing R&D returns and driving slowing revenue growth that argues for a structurally lower forward P/E ratios even before any additional "political risk adjustment" is factored in.

The dubious but much vaunted saviour of assiduous M&A (recall that early January healthcare rally) has yet to emerge in a meaningful way. Moreover, investors are rightly sceptical that value can be engendered in such a way. The market has become rather efficient (nay, even generous) at pricing early stage assets and some promising areas (gene therapy, cell therapies, immuno-oncology) feel crowded with pipeline candidates. There seems to be no free lunch on offer through the mercurial talents of Wall Street's Masters of the Universe.

A rising interest rate environment in the US is unlikely to help either, as larger institutions allocate their capital to other, highly liquid, parts of the market that will be benefit structurally from a higher rate environment (financials etc.). Taking a step back though, one should not conflate large cap pharma with drugs in the wider sense: therapeutic innovations continue to abound and it does feel to us that SMID Biotech will remain the best place to gain therapeutic exposure.

Who doesn't love going to the dentist?

The Dental group is also worthy of mention. Align has been a stellar performer this month. Having traded sideways through April amid concerns of competitor offerings (which we have long argued were misplaced), the stock rose 38% in May as the company predictably raised its medium-term outlook and expectations for the size of the addressable opportunity for clear aligners. This was on the back of several new product launches that expand the range of patients treatable with this approach.

This expansion of the perceived market opportunity was not unexpected. However, the strength of the message that Align is more confident on medium-term growth even as competitors roll out their own offers is powerful indeed and the rationale behind their confidence (principally that they are the only ones out there creating footfall into the dentist's office through various direct-to-consumer approaches) hard to argue with. We continue to see Align as a core long-term holding for the Trust.

Around the 'world' in 80 (ish) meetings - thoughts from the road

As telegraphed in the previous factsheet, the team spent much of May on the road seeing current shareholders and prospective investors. We feel it is important that we maintain a regular dialogue with the stakeholders, even outside of any formal capital-raising activity, and it is interesting to consider the issues discussed most widely in such meetings.

To the extent that there was an over-arching theme to these conversations, it would be that investors are seeking to understand the balance between the undoubted growth opportunity in healthcare products and services with society's ability to pay for them. This is not surprising and this is probably one of the great existential questions of our time; the modern version of the 'irresistible force paradox'.

We must continue to have healthcare and it needs to meet a growing need, but our ability to pay for it is finite. Rudimental human dignity implies there is no paradox –the force of demand will prevail and we will end up finding a way to pay. As we have stated many times before, part of this must come from productivity gains. The opportunity for such improvements is huge in the current, grossly inefficient healthcare system.

The successful products and services of the future must either serve currently unmet need or lower the cost of care delivery (for a defined level of outcomes quality). Some investors struggle conceptually with the scale of the change opportunity, tending to frame it relative to their personal experiences of our benighted National Health Service here in the UK, which is perceived (rightly in our view) as resistant to change and dogmatic versus other healthcare systems.

In contrast to our little island, the global healthcare system is vast and thus the opportunities legion. Many developing countries will leapfrog our ageing infrastructure and put in place systems much better suited to managing an ageing population than our own and even here change will come, albeit more slowly than in markets like the United States.

Developments within the Trust

The Trust's premium to Net Asset Value (which averaged 2.3% from inception to the end of April 2018) returned toward the end of the month and we re-commenced our tap issuance programme, issuing a further 2.3m shares in May. The portfolio has reduced to 28 holdings, as we have exited positions in Tesaro (Biotech) and Philips (Med-Tech); the former on risk/reward and the latter on current valuation vs. further potential upside. Our leverage ratio has declined slightly to 8.4% (previously 8.9%). We expect the proceeds from these position exits will be fully reinvested in the coming days.

Please do feel free to submit any questions raised by the discussion in the factsheet to: shareholder_questions@bbhealthcaretrust.co.uk and we will endeavour to respond in a timely fashion.

Paul Major, Daniel Koller and Brett Darke

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SUB SECTOR BREAKDOWN

Med-Tech	19.5%
Biotech	15.4%
Managed Care	9.7%
Dental	8.9%
Specialty Pharma	8.6%
Health Tech	7.7%
Diagnostics	7.7%
Healthcare IT	5.7%
Pharma	5.0%
Distributors	4.2%
Services	4.0%
Other HC	3.4%

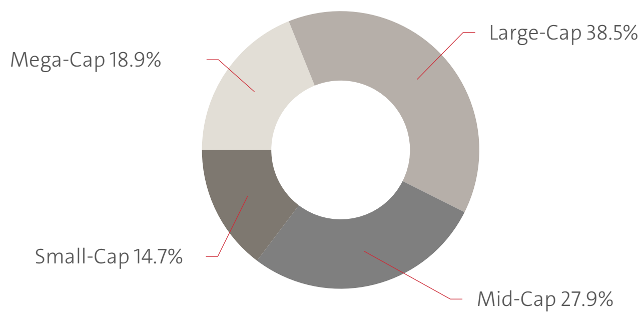
Source: Bellevue Asset Management, 31.05.2018

TOP 10 HOLIDINGS

Align Technology	8.9%
Anthem	6.5%
Illumina	5.9%
Teladoc	5.7%
Dexcom	5.2%
Shire	5.0%
Intuitive Surgical	4.7%
Celgene	4.4%
AmerisourceBergen	4.2%
Lonza	4.0%

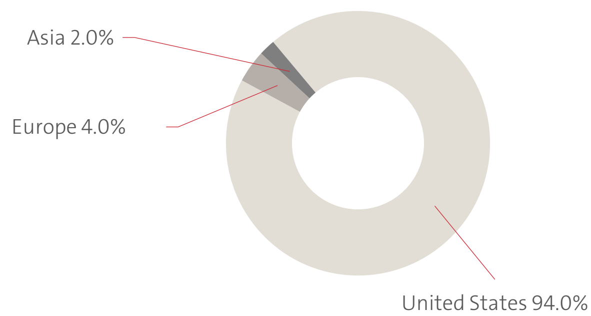
Source: Bellevue Asset Management, 31.05.2018

MARKET CAP BREAKDOWN



Source: Bellevue Asset Management, 31.05.2018

GEOGRAPHICAL BREAKDOWN (OPERATIONAL HQ)



Source: Bellevue Asset Management, 31.05.2018

"four companies representing ~12% of the portfolio have a non-US legal domicile (primarily for tax reasons) but operate out of the United States and their primary stock market listing (in terms of volume traded) is in the United States".

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INVESTMENT FOCUS

- The BB Healthcare Trust invests in a concentrated portfolio of listed equities in the global healthcare industry (maximum of 35 holdings)
- Managed by Bellevue Asset Management AG ("Bellevue"), who manage BB Biotech AG (ticker: BION SW), Europe's leading biotech investment trust
- The overall objective for the BB Healthcare Trust is to provide shareholders with capital growth and income over the long term
- The investable universe for BB Healthcare is the global healthcare industry including companies within industries such as pharmaceuticals, biotechnology, medical devices and equipment, healthcare insurers and facility operators, information technology (where the product or service supports, supplies or services the delivery of healthcare), drug retail, consumer healthcare and distribution
- There will be no restrictions on the constituents of BB Healthcare's portfolio by index benchmark, geography, market capitalisation or healthcare industry sub-sector. BB Healthcare will not seek to replicate the benchmark index in constructing its portfolio

FIVE GOOD REASONS

- Healthcare has a strong, fundamental demographic-driven growth outlook
- The Fund has a global and unconstrained investment remit
- It is a concentrated high conviction portfolio
- The Trust offers a combination of high quality healthcare exposure and a 3.5% dividend yield
- BB Healthcare has an experienced management team and strong board of directors

MANAGEMENT TEAM


Paul Major


Daniel Koller


Brett Darke

GENERAL INFORMATION

Issuer	BB Healthcare Trust (LSE main Market (Premium Segment, Offical List) UK Incorporated Investement Trust
Launch	December 2, 2016
Market capitalization	GBP 331.0 million
ISIN	GB00BZCNLL95
Investment Manager	Bellevue Asset Management AG; external AIFM
Investment objective	Generate both capital growth and income by investing in a portfolio of global healthcare stocks
Benchmark	MSCI World Healthcare Index (in GBP) - BB Healthcare Trust will not follow any benchmark
Investment policy	Bottom up, multi-cap, best ideas approach (unconstrained w.r.t benchmark)
Number of ordinary shares	271 979 768
Number of holdings	Max. 35 ideas
Gearing policy	Max. 20% of NAV
Dividend policy	Target annual dividend set at 3.5% of preceding year end NAV, to be paid in two equal instalments
Fee structure	0.95% flat fee on market cap (no performance fee)
Discount management	Annual redemption option at/close to NAV

DISCLAIMER

CONTACT

Bellevue Advisors Limited
Claude Mikkelsen, Director of Investor Relations
Phone: +44 (0) 203 326 29 83
Moblie Phone: +44 (0) 755 704 85 77
E-Mail: cmi@bellevue.ch
32 London Bridge Street
24th Floor
London, SE1 9SG, UK
www.bbhealthcaretrust.com