BB Healthcare Trust

ad hoc update
October 30, 2018

Share class BB Healthcare Trust (LSE) / GBP

Standardised discrete performance (%)

12-month total return	Sept 17 - Sept 18	Dec 16 - Sept 18*
NAV return (inc. dividends)	30.2%	55.9%
Share price	31.4%	56.0%
MSCI WHC Total Return Index	14.4%	34.1%

Sources: Bloomberg & Bellevue Asset Management AG, 30.09.2018

NAV return is adjusted for dividends paid during period (but not assuming reinvestment)

*Trust incepted on 2 December 2016. Therefore 12 months of perfromance data does not exist for the calendar year.

Note: Past performance is not a guide to future performance. The value of an investment and the income from it may fall as well as rise and is not guaranteed

Wow, just wow. October has been cruel. Described often as the most beautiful month, with bright days and iridescent landscapes, there has been little to cheer the investor, nor any clear signs that the volatility is firmly behind us.

Given the magnitude of the market's gyrations and the impact this has had on the Trust, we felt it appropriate to send an email update to investors ahead of the monthly Factsheet, which will (as usual), be published in the second week of November.

We have broken this email down into to three sections – a macro overview, the impact on our portfolio and our planned actions as a consequence of these significant moves (all data is to the close on Friday 26th October and in sterling. All views and opinions contained within are the views of Bellevue Asset Management AG and believed to be correct at the time of publication).

The macro/market perspective

This has been a very broad market sell-off. In sterling terms, the MSCI World Index has fallen 7.8% thus far during October. The FTSE 100 is down 7.6%, the EuroStoxx50 down 8.0%, the S&P500 down 7.4%, NASDAQ down 9.6% and the Nikkei and Hang Seng >9.4%.

We could list interminable statistics about the extremity of this current situation; suffice to say it matches the ferocity of the 2008 credit crunch correction on several measures. One thing that has changed since 10 years ago is the proportion of trading that is done algorithmically and by quant/ETF strategies; this has more than doubled over a decade. Indeed, it is estimated that long-only active fund managers are now only about 10% of volumes.

Leaving aside the exacerbation of volatility by computerised trading, the reasons for this sharp correction are much discussed and, as ever, a confluence of factors is to blame. We consider interest rates and wider market valuation to be the most important.

Firstly, the valuation context. All of this comes on the backdrop of a 7-year bull run for global stock markets: the MSCI World Index hit an all-time high at the end of August 2018 (of 1,678), up 221% from the Februar 2009 low at the height of the credit crisis and 107% above its previous high in October of 2007.

Although the past is of limited value as a guide to the future, it is undeniable that the headline "record markets" makes people nervous and the chart below certainly suggests that the market was toward the top of the recent normal range in terms of pricing in shorter-term growth. This is not necessarily a warning flag, but only so long as investors believe that growth rates can be sustained at current levels or higher and, thus far, economic growth has been showing a strong and potentially accelerating trend (US GDP growth has accelerated from around 4% in 2017 to 5.5% currently).

Source: Bloomberg/MSCI and Bellevue Asset Management.

Now to US interest rates. The policy response to the credit crisis was quantitative easing, ushering in a period of cheap money that helped to supercharge investor returns through a quest for yield driving up asset prices and cheap money being used to buy back stock and enhance EPS growth. There are now a considerable number of market participants who have never experienced a 'normal' interest rate environment, compounding the fear around the impact of rates normalising. In addition, the global stock of dollar-denominated debt held at the corporate and consumer level around the world has grown enormously (the BIS estimates that U.S. denominated debt to non-bank borrowers reached $11.5 trillion in March 2018).

Front and centre of the correction has been commentary around forward interest rate guidance in the US, with the path to more normal rates now seemingly steeper than anticipated due to a strong US economy. Higher borrowing costs will dampen consumer discretionary expenditure and also crimp corporate profits, the two acting synergistically to slow growth amongst cyclical companies.

Compounding these two woes are concerns over global trade, with tariffs increasing input costs along a globally linked and impenetrably complex supply chain. It is perhaps no surprise then that the double-digit fallers sector-wise within the Index have been Technology, Industrials, Basic Materials and Oil & Gas.

Why now? As noted above, the high valuations of the market in the wider context can only be justified if earnings growth looks sustainable. With clouds already building on the horizon, some weaker-than-expected numbers from key 'bellwethers' has been all the incentive investors needed to pull money from the market. Given the previous points about the algorithmic nature of buying and selling, such corrections rapidly become a self-fulfilling prophecy and, in the short-term at least, it is intuitive to limit exposure to equities with any of the following characteristics: high financial leverage, cyclical earnings, significant exposure to emerging markets and consumer discretionary products.

That said, money within equities has to go somewhere and the flight is toward defensives, which are things like utilities and, normally, healthcare.

It is also toward liquidity and thus up the market capitalisation curve. It is easier to pull out of larger, more liquid names. The impact of this rotation can be seen in comparing mega-cap Indices such as the EU-wide Stoxx50 (-8.0% MTD) with the broader Stoxx600 (down 8.3% MTD). Even within healthcare, the 4% of the MSCI World Healthcare that we define as small/mid-cap (i.e. companies less than $10bn in value) has declined 13.0% MTD, versus down 6.5% for the other 95% of the Index.

This made for an overall decline in the MSCI World Healthcare Index of 6.9% during October, not that far ahead of the wider market. So much for defensive attributes! It thus follows that the specific questions for a healthcare investor, which will return to, are whether such a fall can be justified on fundamentals; has the growth outlook for our industry really changed and, was it 'expensive' like the wider market in the first place.

The impact on the Trust

Whilst the MSCI World Healthcare Index has declined 6.9% during October, the Trusts Net Asset Value has fallen 15.5% over the same period, with this significant underperformance wiping out most of the outperformance over the Index that we had accrued through Calendar 2018. We are of course very disappointed with this outcome, but not entirely surprised, given the nature of the wider macro performance across the equity market.

Many of you will recall our investment thesis since launch – to own a concentrated portfolio of healthcare stocks that we believe will deliver the best returns over a rolling three to five year investment horizon. Stock selection is without regard to market capitalisation, geography or any benchmark and based on detailed due diligence. We have also committed to remaining as close to fully invested as possible, seeing it as the investor's decision as to how to allocate between equities and cash or any other asset class.

The parameters outlined above do not support rotating in and out of stocks quickly; we are very far from being a momentum hedge fund. We are effectively committed to making a bed and lying in it, which does leave one at some risk in a rapidly evolving market situation. It is worth recalling this same approach had worked well until the end of September, with the Trust delivering a US$ return since inception of 62% versus 39% for the benchmark. However, our portfolio construction left us very exposed to the macro-thematic trends that have dominated this month.

The table below illustrates our current sub-sector exposures and the month-to-date performance.

Sub-Sector	MTD Perf.	Subsector allocation
Biotech	-11.4%	18.1%
Medtech	-10.3%	14.0%
Diagnostics	-15.4%	14.0%
Managed Care	-2.1%	11.7%
Specialty Pharma	-10.5%	10.1%
Healthcare IT	-18.8%	7.1%
Dental	-34.9%	6.0%
Services	-7.2%	5.1%
Pharma	-4.5%	4.0%
Distributors	-7.9%	3.9%
Other HC	-1.4%	3.5%
Health Tech	n.a.	2.5%
Conglomerates	-3.0%	0.0%
Facilities	-6.9%	0.0%
Generics	-9.9%	0.0%
Tools	-12.9%	0.0%

Source: Bloomberg/MSCI and Bellevue Asset Management.

As noted previously, Small/Mid-cap has been punished more severely than Mega/Large-cap. Where the benchmark is 95% in the Mega/Large category, we are 49% in Small/Mid. We have kept our gross and net exposures close together, holding on average enough cash over the month to offset our borrowings and this has helped to mitigate downside, but only to a very limited extent. The table above shows that is not just stock selection, but sub-sector performance that has been the issue, the macro tail is wagging the dog and we believe it would have been difficult to have performed materially better owning alternative stocks in many of these categories. This is in stark contrast to the more typical market conditions up to the end of September, where stock picking has been the driver of alpha generation.

Thus far, five of our disclosed top 10 positions from September have reported Q3 earnings: Align, Bristol-Myers, Celgene, Illumina and Lonza. Two of these have had issues that have spooked the market (Align and Bristol), but the extent to which the issues raised in recent days alter our longer-term thesis is arguably very limited. In another week, the reaction would probably have been much more muted, but this is an earnings season where "good" or "in-line" simply is not good enough.

Very little of what we own is cyclical, consumer orientated or discretionary in nature. One must keep in mind that demand for Healthcare services is inelastic and the demographic trends are inexorably upward, so we have far less to fear from the rates cycle than other industries. Few of our companies have meaningful debt and few still will need to refinance said debt at punitive rates; the interest rate sensitivity of the portfolio is low (and managed care will benefit as rates rise).

Whilst Align is a consumer-focused play, the market growth will come from penetrating the teen market, taking share away from traditional fixed metal appliances. As such, we do not agree with those who suggest this is quasi luxury goods and that volumes will take a tumble in a slowing economy. Why then do we need to change the input assumptions that drive our earnings and cashflow models?

When considered in this context, the impact of the macro factors on our portfolio should be very limited. It is a Benjamin Graham famously noted; the market is a voting machine in the short-term not a rational weighing machine.

What next for BB Healthcare?

Having channelled some Benjamin Graham, it is perhaps worth also quoting his most famous pupil, Warren Buffet: be greedy when others are fearful. If we do not see the fundamentals as having changed and do not agree either that the market reaction was appropriate or valuations for our holdings were elevated, then there is only one logical course of action: to bolster our holdings in the existing portfolio.

We see this as a great time to invest. Indeed, we were discussing internally earlier in the month, after the first phase of the correction, that the PEG ratios for the areas we liked had gotten cheaper rather than more expensive over the Trust's life as our confidence in out-year numbers has risen.

We have thus announced today that we will look to raise additional money in order to capitalise on this short-term market dislocation; this is entirely consistent with our view that the 3-5 year growth opportunity has not changed.

We remain very firmly of the view that we are at a critical juncture for the healthcare industry, where the care paradigm must change in order to meet rising demand at reasonable overall levels of expenditure. As such, those companies offering compelling innovations that benefit patients and improve cost trends will continue to prosper. We thank you for your continued support of BB Healthcare Trust.

Paul Major, Daniel Koller and Brett Darke.

BB Healthcare Trust

ad hoc update
October 30, 2018

Share class BB Healthcare Trust (LSE) / GBP

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 313.0 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	313 877 794
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

BB Healthcare Trust PLC (the "Company") is a UK investment trust premium listed on the London Stock Exchange and is a member of the Association of Investment Companies. As this Company may implement a gearing policy investors should be aware that the share price movement may be more volatile than movements in the price of the underlying investments. **Past performance is not a guide to future performance. The value of an investment and the income from it may fall as well as rise and is not guaranteed. An investor may not get back the original amount invested.** Changes in the rates of exchange between currencies may cause the value of investment to fluctuate. Fluctuation may be particularly marked in the case of a higher volatility fund and the value of an investment may fall suddenly and substantially over time.. This document is for information purposes only and does not constitute an offer or invitation to purchase shares in the Company and has not been prepared in connection with any such offer or invitation. Investment trust share prices may not fully reflect underlying net asset values. There may be a difference between the prices at which you may purchase ("the offer price") or sell ("the bid price") a share on the stock market which is known as the "bid-offer" or "dealing" spread. This is set by the market markers and varies from share to share. This net asset value per share is calculated in accordance with the guidelines of the Association of Investment Companies. The net asset value is stated inclusive of income received. Any opinions on individual stocks are those of the Company's Portfolio Manager and no reliance should be given on such views. Any research in this document has been procured and may not have been acted upon by Bellevue Asset Management AG for its own purposes. The results are being made available to you only incidentally. The views expressed herein do not constitute investment or any other advice and are subject to change. They do not necessarily reflect the view of Bellevue Asset Management AG and no assurances are made as to their accuracy. Bellevue Advisors Limited is an Appointed Representative of Mirabella Advisers LLP, which is authorised and regulated by the FCA (RFN: 606792).

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