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BB Healthcare ups gearing to tap into small stock weakness

By **Michelle McGagh**, **Jamie Colvin** / 21 Mar, 2022

BB Healthcare (BBH) has changed its name but kept faith in smaller healthcare companies after the sector sell-off by increasing its borrowing to take advantage of lowly valuations. The £1bn closed-end fund, which has rebranded as **Bellevue Healthcare Trust**, suffered as the healthcare sector endured its longest sell-off since 1994 having been the darling of the coronavirus pandemic, with small and medium-sized stocks suffering the worst of the downturn in sentiment.
Commenting in the investment trust's recent annual results fund managers Paul Major and Brett Darke were stoic about the damage the falls have done to their portfolio and said they planned to increase the gearing – or borrowing – in the fund to snap up stock bargains.

BBH reported a 10.3% total investment return for the year to 30 November, which lagged the 16.3% rise in the MSCI World Healthcare index, and the defensive sector fell further behind the MSCI World index, which advanced 23.3%.

This year has proved difficult with the shares down 10%, with the 12-month return, including dividends, shrinking by 4.2%, due to a 'violent intra-sector rotation' in response to high inflation, rising interest rates, a tech-sell off, and war between Russia and Ukraine that have darkened the outlook for global economic growth.

Major and Darke said they were 'somewhat lost for a compelling explanation' as to why healthcare had shouldered such a heavy burden, although the trust's five-year performance remains credible with a total shareholder return of 83% that beats the MSCI World Healthcare return of 70%.

‘Nothing fundamental has changed in the last four weeks, or even four months,’ they said. ‘There are more people alive than before. They are older and they will get sick, with increasingly complex conditions – these are irrefutable truths.

Gearing that at 30 November stood at 4.9% of net asset value (NAV) has doubled to 10%, according to data from Numis Securities.

‘If the last two years have taught us anything, it is that everything changes very quickly in such a febrile environment,’ they said.

Despite the year-to-date fall, the trust has avoided falling to a discount enabling it issue £18.6m of shares, which combined with the £35.1m increase in borrowings has given them the cash to add to existing holdings and add three new companies ‘one each in tools, diagnostics, and medical technology sub-sectors’, though they did not disclose the names.

‘One of these is a repurchase of a company that we have owned before but exited on valuation grounds,’ they said.

In post-results briefing this month, Major (above) said the healthcare sector was the best hedge against inflation, citing its strong performance against gold and the consumer prices index (CPI) over the last 25 years, with the exception of the financial crash in 2008 when gold performed better.

Major, who also runs the WS Bellevue Healthcare open-ended fund with Darke, was optimistic about the sector that spends $10tn globally, buoyed by continuous and reliable demand, which will be boosted by ageing populations suffering from chronic pain.
‘While people talk about inflation and stagflation, the data is unarguable: the best hedge you’ve got against inflation is to buy the one thing that nobody wants to consume, but has no choice and will consume: healthcare,’ he said.

While the managers are anticipating a bounce back in healthcare stocks, they said market corrections ‘can go on for much longer than one may realise’, citing the 2000 tech crash as a ‘classic example of prolonged suffering’.

‘We cannot be confident that the mid-cap healthcare rout is close to its denouncement, but we can objectively discern value when we see it, and that time is now,’ they said.