



US Healthcare Theme Update

Q4 2025

In a Nutshell

Out of the Biotech fire, into the Big Pharma haven

Summary

In January 2025 we re-initiated an exposure to Biotech amidst a deluge of policy noise. The re-election of Donald Trump, and a ‘Make America Healthy Again’ agenda led by RFK Jr, had led investors to exit drug makers at historically attractive prices. We saw an opportunity for innovation-led earnings growth and M&A to reverse this narrative.

In a little over six months our thesis played out as innovation-led breakthroughs and excellent stock picking from Polar Biotech, into which we had switched in March, lifted the theme’s absolute and relative return to extreme levels.

Outside of Biotech’s narrow leadership, the Healthcare sector remained a major equity laggard, with ‘Big Pharma’ weighed down by its perceived innovation problem (compounding the well-known political frictions). In November 2025, we crystallised our Biotech gain and initiated a passive exposure to the US Healthcare sector. The sector’s strong cash flows, high return on equity and de-rated earnings, coupled with the potential for AI to revolutionise big pharma’s product pipeline, offer ample compensation for – and a catalyst to remove – the doubts putting the brakes on returns.

The Healthcare sector has acted as a haven during periods of market stress. Though we do not forecast this, we welcome the opportunity to add a cheap, defensive tilt to our portfolios as market valuations (and those of Biotech) have risen rapidly of late.

Industry Developments

The appointment of Robert Kennedy Jr as Secretary of Health and Human Services in early 2025 has not led to a much-feared shift away from science-based decision making at the FDA, the body that approves new drugs in the US. The FDA approved 46 novel drugs in 2025, well above the historic average of 36 new drugs per year since 1993 (per chart below).

We expect US healthcare policy to remain volatile under the Trump administration and for AI to be increasingly useful, and potentially disruptive to, the Biotech sector. As Biotech has outperformed Healthcare through 2025, the relative risk-reward outlook for the Healthcare sector has improved materially.



Annual approvals of new molecular entities (NMEs) and biologics license applications (BLAs) by the FDA. The 46 approvals in 2025 maintains a rising trend of approvals

There was a rush of drug pricing agreements in late December between the Trump administration and a number of large pharma companies, removing one of the remaining sentiment overhangs on the sector. Elsewhere, the UK Government reached an agreement involving higher NHS payments for new drugs in exchange for 0% tariffs on UK pharma exports for the next three years.

On the innovation side, we reiterate that the fusion of AI and drug research will accelerate discovery times and reduce costs for diseases ranging from cancer to Alzheimer's. While consumers look set to be obvious winners, it is far less certain who the winners in industry will be.

The market, by re-rating Biotech and Tech in 2025, has made the bet that 'Big Pharma' will be a relative loser. This appears short-sighted. The ability for major Healthcare companies to replenish (or vastly expand) pipelines, and do so quickly (and at lower cost) is, we believe, higher than prevailing valuations and sentiment assumes.

How pharma is rewriting the AI playbook: Perspectives from industry leaders

AI-powered data analysis is accelerating pharma R&D, from discovery to clinical trials, leaders from across the pharma industry shared.

Nvidia And Eli Lilly To Build \$1 Billion AI-Powered Drug Discovery Lab

Source: McKinsey, Forbes

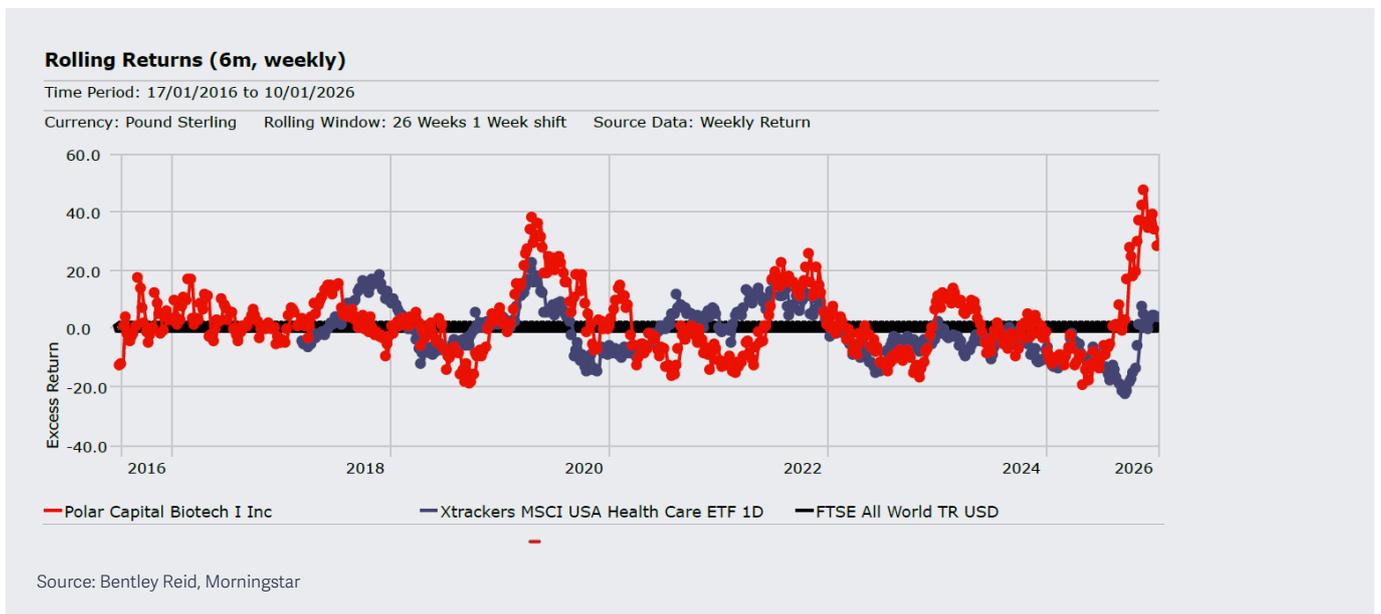
Big Pharma is investing heavily in AI to help discover new drugs. This may improve future sales and reduce the need for external acquisitions of Biotech companies

Performance

The Polar Biotech fund returned +12.1% (USD terms) through Q4 until our exit across our Balanced and Growth funds in November 2025, crystallising a FTSE All World-leading return of over 40.0% since investing in March 2025. Polar's Q4 return led a +3.1% gain for the Vanguard FTSE All World ETF and a +11.1% return for the Xtrackers MSCI USA Health Care ETF (into which we switched).

The Healthcare ETF went on to rally a further +5.9% during our holding period in Q4, leading the FTSE All World ETF by 4.0%.

The 6-month rolling performance chart below highlights the extreme relative outperformance of Polar Biotech (peaking at the point of our exit in November) and the strongly divergent performance of Healthcare.

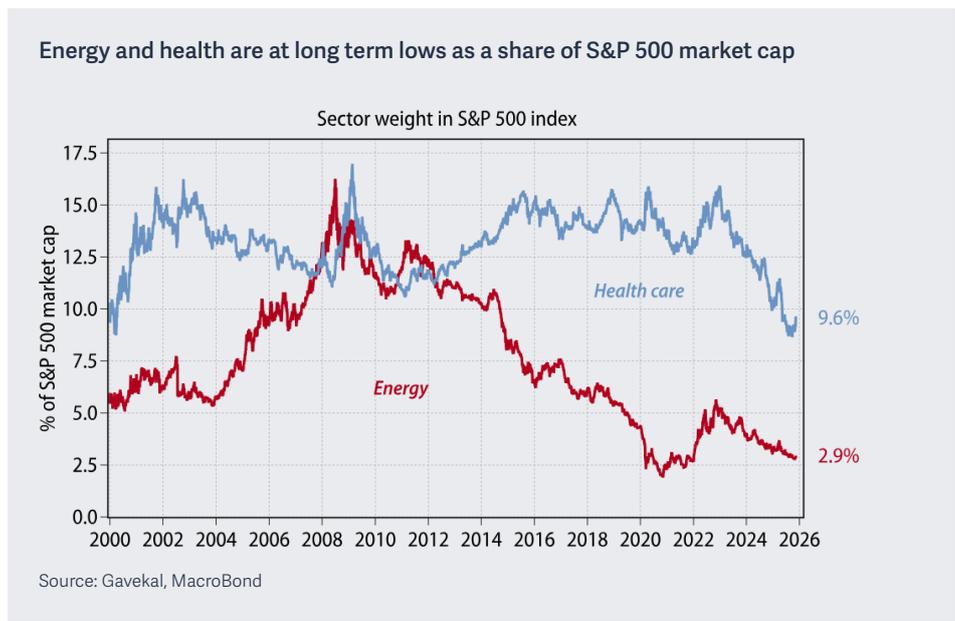


The scale of Biotech’s outperformance has elevated its near-term downside risk. This is a view shared by Polar’s manager, David Pinniger, in a cautionary commentary from January 2026:

“A number of 2025’s best performing Biotech companies now have sizeable M&A expectations attached to them (perhaps leading to extended valuations), given the brisk cadence of deal-making last year. We believe this could make them, and the broader sector, vulnerable to hitting an air pocket of performance early in 2026 if further M&A does not come through for these crowded names at a scale and frequency that satisfies expectations”.

Valuation

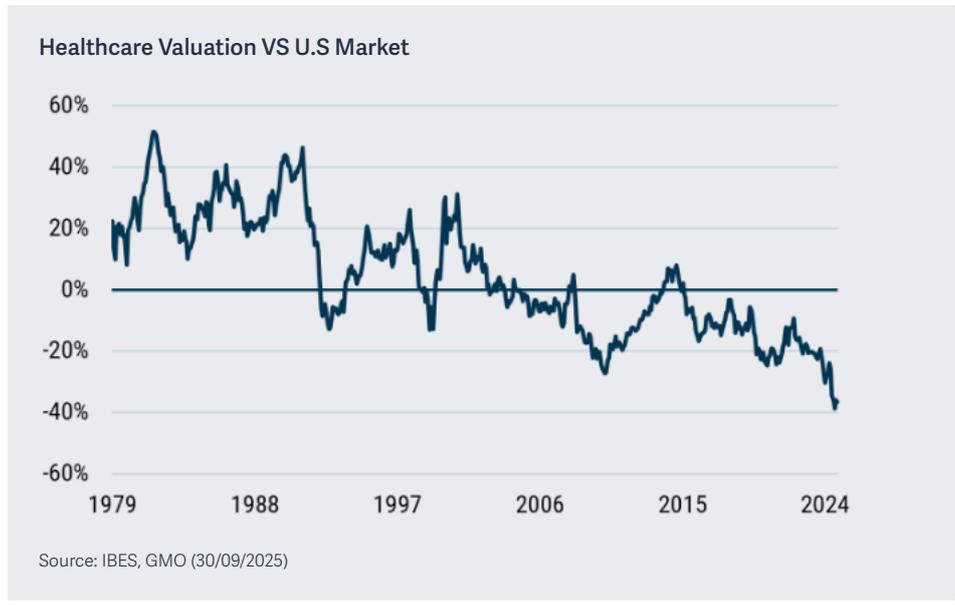
The multi-year underperformance of Healthcare has depressed the sector’s valuation and weight in major indices, falling to multi-year lows – levels from which it previously outperformed significantly during the Dot Com crash.



The Healthcare sector accounts for less than 10% of total S&P 500 market cap, down from 16% at its peak in 2022 as cyclicals have re-rated to a record share

Healthcare’s relative valuation also fell to a record low in 2025, driven by robust fundamental growth and a re-rating in the market.

Relative to Polar’s portfolio, the average Healthcare sector balance sheet is much less speculative than that of the typically smaller, pre-sales and earnings Biotech companies.



As GMO highlighted in January 2026, despite strong fundamentals and secular trends, the healthcare sector’s valuation relative to the market sits at a 50 year low

Positioning

We access the US Healthcare theme via the Xtrackers MSCI USA Health Care ETF, the cheapest available US Healthcare index tracker (0.12% annual fee).

The fund invests in 63 companies listed in the United States. Top holdings in this market cap weighted index include Eli Lilly, Johnson & Johnson and Abbvie (at 31st December 2025).

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