The investment lessons learned from the NHS

The cost stranglehold on the NHS remains, but it's not all bad news. Jim Lydotes, lead portfolio manager for the Pinnacle BNY Mellon Global Infrastructure Yield Fund finds hope in two underinvested areas of the healthcare space.

Jim Lydotes holds up the UK's National Health Service as a global standard for how privatisation ought to work. And yet the NHS – a source of national pride for many Britons – is effectively a victim of its own success and it is increasingly stretched and facing ongoing budget constraints. Yet therein lies a new wave of investment opportunities, he says.

Lydotes, portfolio manager for the Pinnacle BNY Mellon Global Infrastructure Yield Fund, says the social infrastructure space is becoming more interesting from an investment perspective because the demands on medical care facilities, schools, hospitals and the like are growing, while budgets are not. Therefore, this opens up a rich opportunity set where the private sector's appetite to support government-run institutions is ideally placed. As the babyboomer generation ages – with many now in retirement – healthcare and NHS waitlists are facing more pressure because they lack sufficient infrastructure to meet this growing demand, therefore Lydotes and his team are witnessing partnerships, of sorts, taking place, where the government is leveraging the underutilised private sector.

With less than 20% of the UK population covered by private healthcare, a surplus of underused facilities exists in many private hospitals, so the overheads to pick up the NHS's excess care need not increase.

Lydotes explains: "There are huge fixed costs to running a hospital: the staff; an X-ray machine or MRI scanners, for example. So the fixed costs are there anyway, but in terms of the incremental revenue generated through using [those machines] a few more times a day, 100% is going towards the bottom line."

The team favours healthcare real estate investment trusts (REITs) as the vehicle of choice to access this sector. Healthcare, he says, as a defensive sector, means regardless of the point in the market cycle, it will be in favour. The challenge is around valuations in the sector, and finding opportunities for capital.

Lydotes adds: "Healthcare has a great end market, as people will always need it. But you need to find comfort around pricing and supply. In the UK, we have met with and been talking to private hospitals outside London but the math really has to add up and, as yet, we have not seen many elsewhere that are adding up as viable investment options."

It's not just a UK problem. The manager says between now and 2030, there is expected to be a 40% increase in the number of hospital beds needed in the US, with much of that requirement being met by the private sector.

"What we have identified is that the healthcare REIT segment will be the source of capital to bring to market in the next 10-12 years. As the oldest babyboomer is now 72 years old, we are starting to see the demographic shifts as we are knocking on the door of 10 years of tremendous demand from the boomers, with a sharp inflection in demand."

Giving new meaning to long-term care?

The story goes beyond just hospital beds, he says. With tremendous demand for age care, in the US in particular, a recent movement has been for facilities that offer a "continuum of care" from senior residential housing that offers its residents a journey through the later stages of life without the need for physical and emotional upheaval.

He says there has been a long-held stigma around these types of infrastructure assets where the length of stay for a customer was less than a year.

However now, Lydotes is seeing the rise of companies offering a more complete service; starting with independent living facilities that then can offer residents, after living there for 20 years or so, the opportunity to remain on the same site and take advantage of more intensive care services as required.

Looking past the emotional stigma, Lydotes feels the space is a ripe asset class with 8% dividend yields not uncommon in certain "deep value" strata of the healthcare REIT sector.

He also highlights that this particular aspect of healthcare looks poised for an upward inflection as the 'baby bust' generation matures.

"Everyone focuses on the baby boom as driving demand," he says. "But the baby bust was 10 years before that, around the 1930s where birth rates fell off during wartime. Those people are now massively underrepresented but we still expect to see an inflection of care needs over the next few years."

About the Team

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