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MAY 2025

US Healthcare: Attractive Valuation for a Structural Growth Opportunity

US healthcare offers an attractively valued entry point for a strategic overweight allocation. This is despite considerable short-term uncertainty about the evolution of US policy. The sector is trading near historical lows globally; in the US, it is now trading at the deepest discount to the broader market in nearly 40 years based on relative forward price-earnings (PE) multiples. Its share of the broader market is at its lowest in 15 years.

While we acknowledge significant policy uncertainty in the sector, we believe that the current valuation, sustained outflows in recent years—and our view that investor sentiment already reflects significant risks—should limit the potential downside.

Meanwhile, we think healthcare offers strong structural growth prospects: it stands to benefit from the effects of an aging population and a growing need for social care as well as the potential benefits of greater long-term AI adoption. It also has a strong track record of delivering earnings growth at above market rates.

In the short-term, we think that a healthcare allocation can also play a stabilizing role amid macroeconomic uncertainty, given its defensive nature and history of resilience in previous equity market drawdowns.

Robertas Stancikas
Inigo Fraser Jenkins

Additional Contributors: Alla Harmsworth,
Harjaspreet Mand and Maureen Hughes

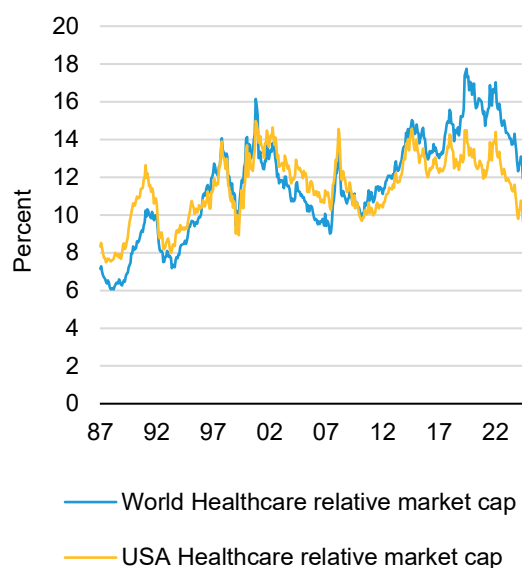
In our view, the macroeconomic and market environment in the coming years will be defined by the mega forces of demographics, deglobalization, a delayed energy transition and mounting public debt. Their impact points to an environment of structurally lower growth as well as higher and more volatile inflation, which in turn leads us to expect lower equity returns and higher market volatility than over the last 15 years. There is an open question: How much can AI offset some of these challenges, particularly through a broad-based productivity increase?

We believe that our outlook warrants a strategic overweight in the US healthcare sector. In the near term, there is uncertainty from US President Donald Trump's recently announced desire to force US drug prices down to align with the lowest international reference price. To what extent this can be implemented remains to be seen. However, at the same time, the sector could play an important role in diversifying away from heavy market concentration in tech as well as in stabilizing portfolios during market drawdowns. In the longer run, healthcare should be a structural beneficiary of an aging US population, with its pricing power enabling sustained real earnings growth—even in a world of structurally higher inflation. We also view the sector as one of the clearest potential AI beneficiaries. Multiple possible applications could increase productivity and cut drug-development costs, improve research and development (R&D) efficiency and effectiveness, and drive better customer services and care.

While we acknowledge considerable policy uncertainty surrounding US healthcare in particular, the current sector valuation and investors' positioning should limit the potential downside and provide an attractive entry point.

US healthcare's share of the overall equity market has fallen to its lowest in 15 years, currently standing at only 10% (*Display 1*). Today's negative sentiment toward the sector is also evident in its current valuation (*Display 2*) with the 12-month forward-PE multiple of US healthcare versus the market at an all-time low discount of 20%. Globally, the picture is similar, with healthcare trading significantly below the historical average valuation.

DISPLAY 1: US HEALTHCARE RELATIVE MARKET SHARE IS NEAR HISTORICAL LOWS

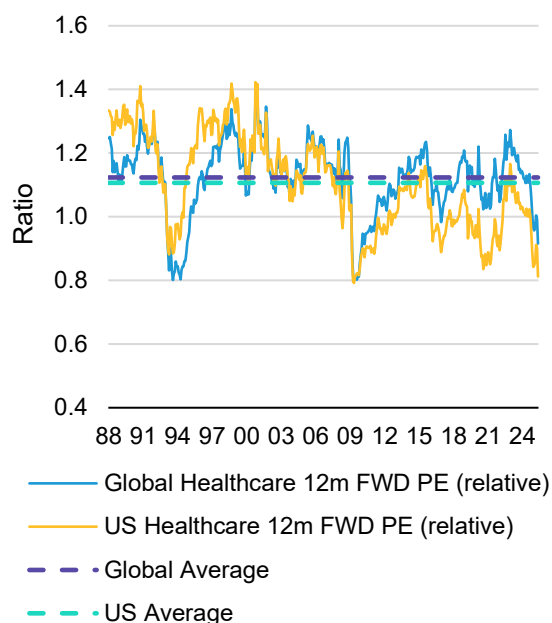


Past performance does not guarantee future results.

As of May 12, 2025

Source: LSEG Data & Analytics and AllianceBernstein (AB)

DISPLAY 2: US AND GLOBAL HEALTHCARE TRADE AT A DISCOUNT TO THE BROADER MARKET



Past performance does not guarantee future results.

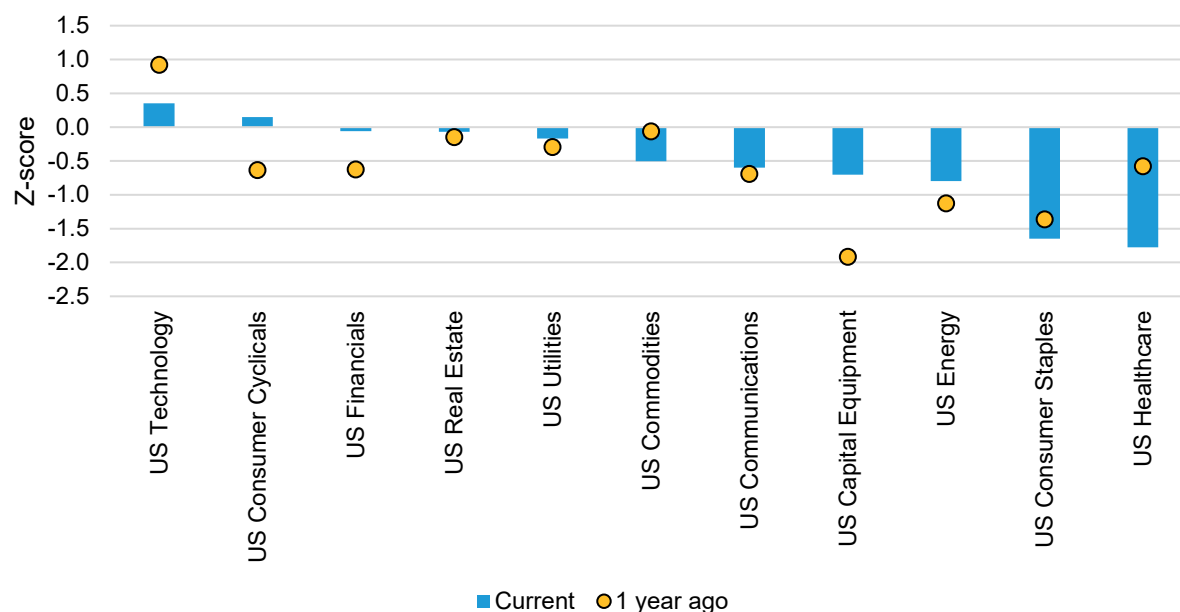
As of May 12, 2025

Source: Factset, IBES and AB

To put US healthcare into the context of the rest of the US market (*Display 3*), it is currently the cheapest sector on a relative basis, after a significant de-rating over the last year.

DISPLAY 3: US HEALTHCARE IS THE CHEAPEST SECTOR IN THE MARKET

12-MONTH FORWARD PE RELATIVE TO THE MARKET (Z-SCORE)



Current analysis does not guarantee future results.

As of May 12, 2025

Source: Factset and AB

Outside of the Global Financial Crisis and COVID-19 pandemic, mid-1993 and the end of 2016 were the only other periods that saw similar healthcare discounts to the broader market. Both episodes were also characterized by significant policy uncertainty for the industry.

Shortly after Bill Clinton's election as US President in 1992, he made healthcare reform the cornerstone of the administration's first-term agenda, aiming to overhaul the system and provide universal healthcare for all Americans. Other suggested policy measures included health-insurance reform, the establishment of regional healthcare alliances in each state to compete for customers, consumer choice of health plans, and provisions for Medicaid beneficiaries. Government oversight and regulation of the sector would have been significantly expanded to ensure standards for quality and affordability.

In 2016, the market was worried about the potential repeal and replacement of the Affordable Care Act (ACA), a move that was one of the centerpieces of Donald Trump's campaign for his first term in office. At the time, the healthcare sector was under intense scrutiny over drug-pricing policies and the potential tax implications of proposed high-profile mergers such as Pfizer and Allergan. In the background were growing worries about the impact of the impending patent-expiration cliff in the pharmaceuticals segment.

Today, the focus is on Trump's recent announcement that the lowest international price for a drug should set the price paid in the US. It remains to be seen to what extent this rule can actually be implemented in practice, but it certainly introduces a new level of uncertainty.

In addition, there are broader political headwinds from the new leadership at the Department of Health and Human Services (HHS) and proposed deep cuts to Medicaid. These could add up to \$800 billion in spending reductions over the next decade—with significant impacts on managed-care providers and hospital operators. Meanwhile, HHS is directly challenging big pharmaceutical companies and vaccine manufacturers. It has also advocated for big changes to healthcare regulations as well.

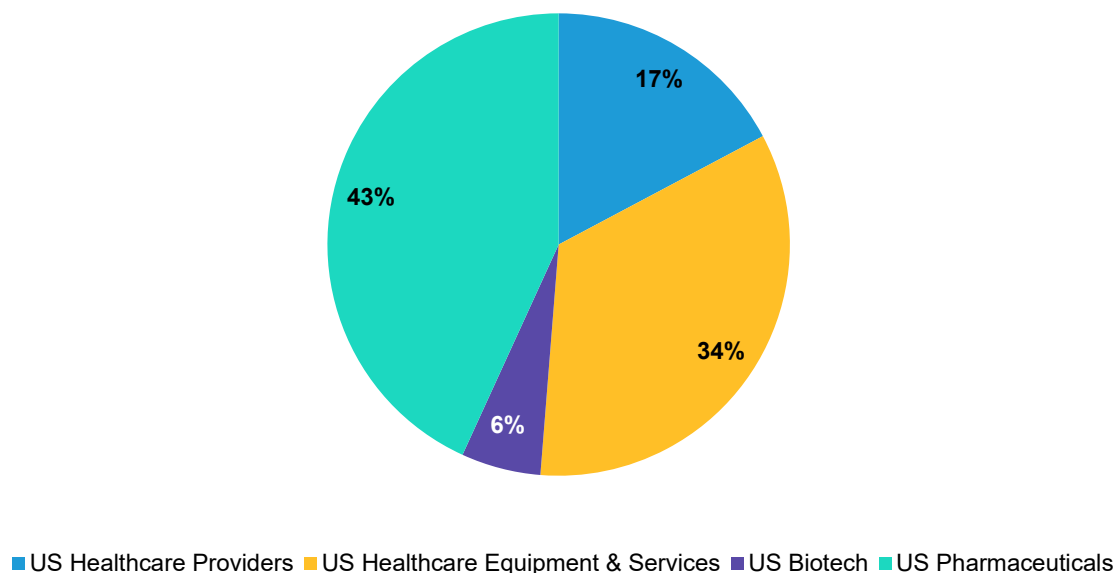
as existing practices and policies. This not only increases uncertainty but creates a risk of inadvertent disruption, as evidenced by the recent resignation of Food and Drug Agency veteran Peter Marks.¹

There is also a considerable overhang of uncertainty around potential significant changes to Pharmacy Benefit Manager (PBM) business practices. While the ultimate scope of reform is still highly uncertain, the proposed reforms so far pose a significant threat to PBM profitability.

However, we think there are circumstances in this bout of turmoil that should limit the ultimate impact of the proposed reforms. Radical healthcare reform is still not the top priority for the current administration, which is focused on tariffs, immigration and tax reform. Moreover, any radically disruptive healthcare legislation would be hard to pass, given the Republican Party's narrow majority in Congress. When it comes to Medicaid, public attitudes are very supportive: 77% of the overall population and 75% of Republicans view it favorably.²

Another mitigating factor is that the structure of the healthcare sector today is much different than it used to be. Historically, it had been dominated by pharmaceutical companies, but they are now less than 50% of the overall market's capitalization. Also, other industries, such as healthcare equipment and biotech, play important roles and offer different and diversifying earnings and return streams (*Display 4*).

DISPLAY 4: THE US HEALTHCARE SECTOR'S STRUCTURE (PERCENT OF MARKET CAPITALIZATION)



Current analysis does not guarantee future results.

As of February 28, 2025

Source: LSEG Data & Analytics and AB

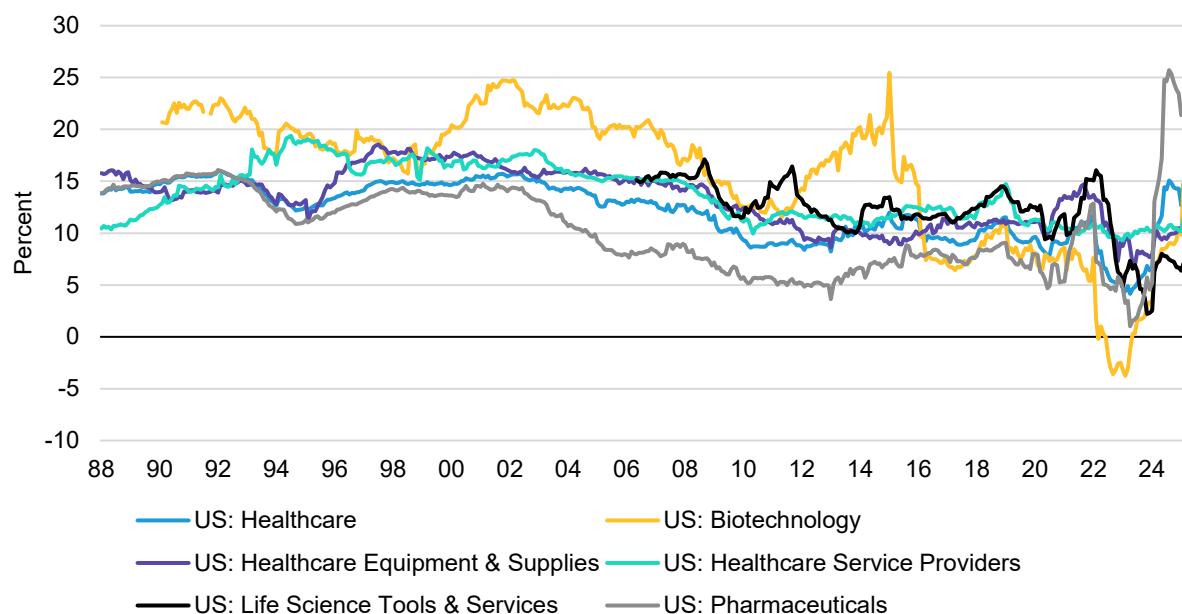
Looking at long-term earnings expectations by industry, medtech has historically been a source of high earnings growth, and biotech's long-term growth prospects have improved a lot in recent years (*Display 5*). Bernstein's Medical Technologies &

¹ <https://www.nytimes.com/2025/03/28/health/fda-vaccines-rfk-jr-peter-marks.html>

² <https://www.kff.org/health-costs/poll-finding/kff-health-tracking-poll-public-weighs-health-care-spending-and-other-priorities-for-incoming-administration/>

Services sector analysts note³ that medtech should be resilient to political uncertainty, because it constitutes only 7% of US healthcare spending, less than half of the 15% spend for pharmaceuticals, which receives much more political focus. Also, most medtech devices are purchased by hospitals, so pricing dynamics keep price levels much steadier over time, as cost-sensitive hospitals try to secure the best prices they can. The team also notes that medtech supply chains are fairly insulated from China: they moved to minimize shipments from China during the trade war in Trump's first presidency, and the COVID-19 pandemic forced medtechs to invest in supply-chain resilience.

DISPLAY 5: CONSENSUS LONG-TERM EARNINGS GROWTH ESTIMATES FOR HEALTHCARE SUB-SECTORS



Current analysis does not guarantee future results.

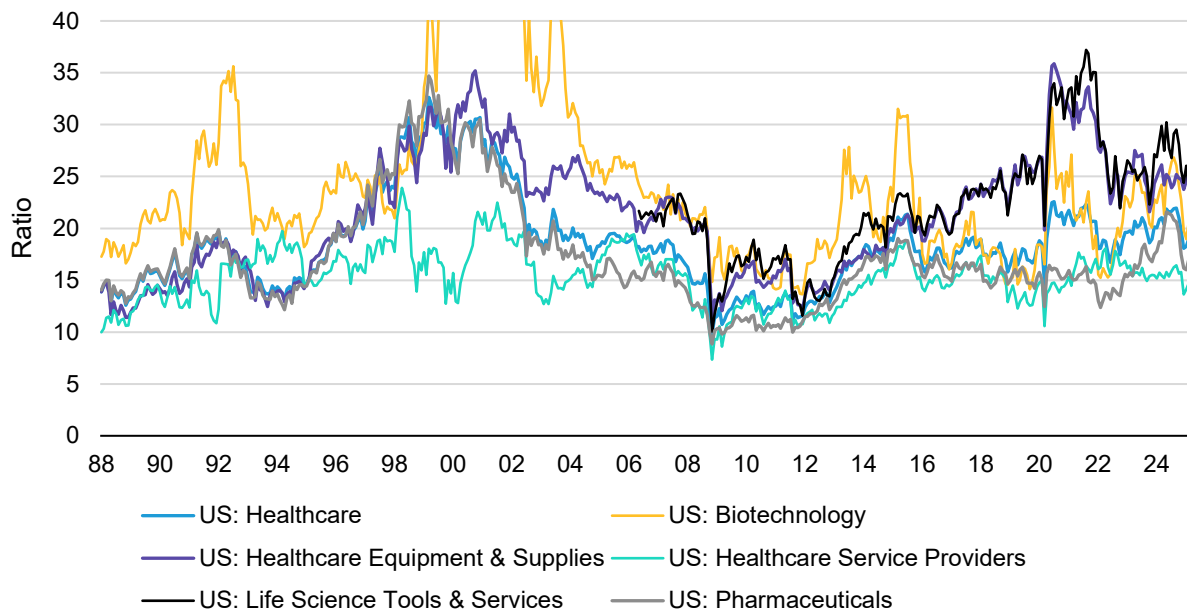
As of May 12, 2025

Source: Factset, IBES and AB

Much political uncertainty has already been priced into US healthcare, so we think potential downside from here should be limited. In addition to its overall discount to the broader market that we discussed earlier, the Healthcare Providers & Services Index, which includes the largest PBMs such as United Health, Cigna and CVS, is trading close to all-time relative lows based on 12-month-forward PE multiples (*Display 6*). The pharmaceuticals sub-industry valuation multiple has fallen by 30% over the last year, putting it considerably below its historical average.

³ [European Medtech: Chaos in DC... A 30,000 foot view on tariffs, DOGE, and healthcare policy under Trump 2.0](#)

DISPLAY 6: US HEALTHCARE INDUSTRY 12-MONTH FORWARD PE MULTIPLES



Current analysis does not guarantee future results.

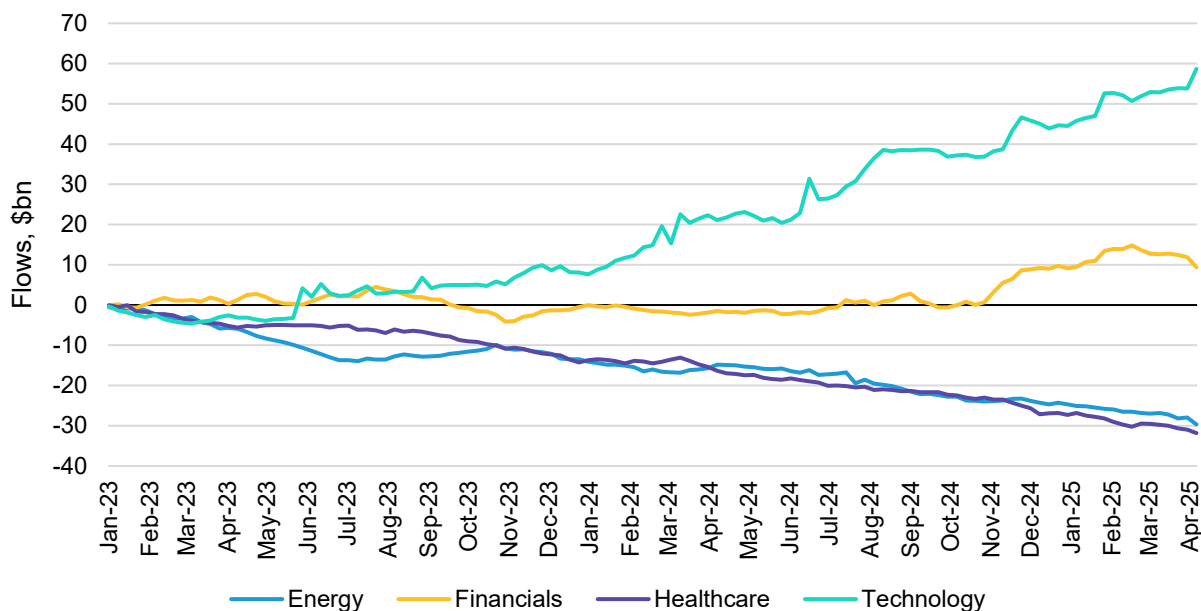
As of May 12, 2025

Source: IBES, Factset and AB

Negative investor sentiment is also clearly evident in flows (*Display 7*). Over the last two years, healthcare has seen the largest outflows among US sectors— nearly \$32 billion. This suggests investors are underweight the sector, which should be another key factor mitigating the potential downside.

DISPLAY 7: HEAVY HEALTHCARE OUTFLOWS OVER THE PAST TWO YEARS

US EQUITY SECTOR FLOWS SINCE 2023



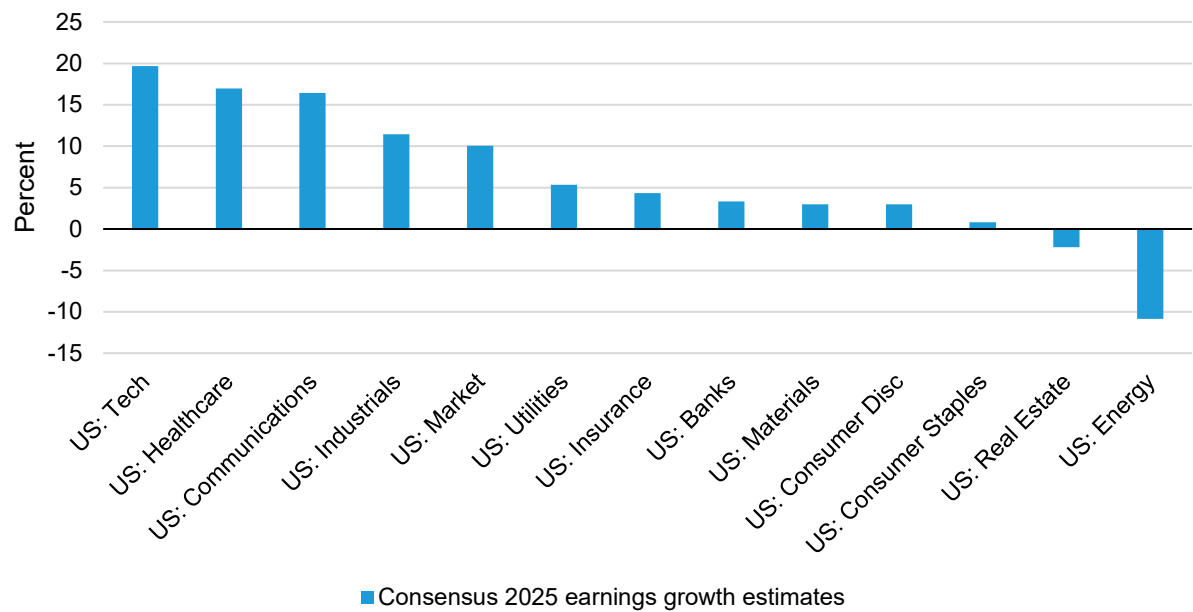
Current analysis does not guarantee future results.

As of April 9, 2025

Source: EPFR and AB

Investors' pessimism contrasts sharply with strong earnings-growth potential, both near term and over the long run. This year, the consensus calls for healthcare earnings to grow by 17% (*Display 8*), which would put the sector within the top few sectors in terms of growth. This forecast has fallen by two percentage points in recent weeks but remains significantly above the 10.0% growth expectation for the overall equity market. Long-term growth prospects look favorable, too (*Display 9*): the medium-term earnings outlook for healthcare is second only to technology.

DISPLAY 8: HEALTHCARE EARNINGS GROWTH IS PROJECTED TO NEARLY MATCH TECH IN 2025

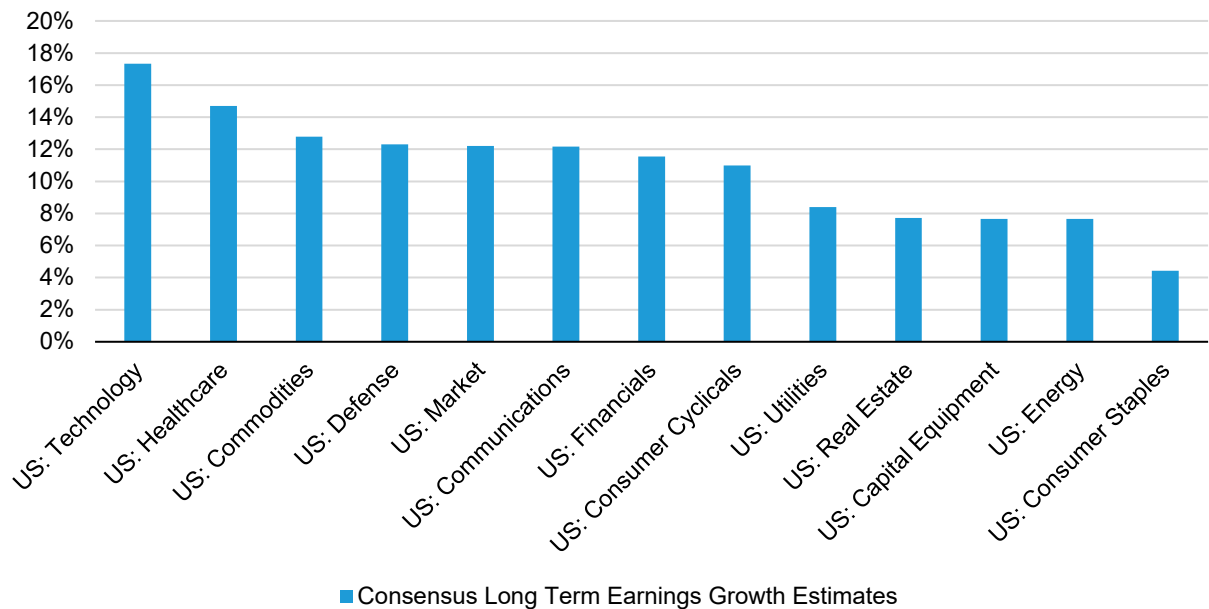


Current analysis does not guarantee future results.

As of May 12, 2025

Source: IBES, LSEG Data & Analytics and AB

DISPLAY 9: LONG-TERM HEALTHCARE EARNINGS ALSO LOOK FAVORABLE



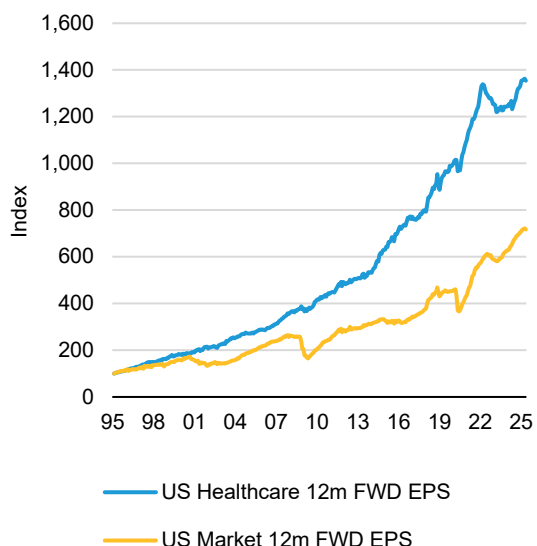
Current analysis does not guarantee future results.

As of May 12, 2025

Source: Factset, IBES and AB

As *Displays 10* and *11* show, healthcare also has a strong track record of outpacing market earnings growth. Since 1995, annualized earnings growth for the sector was 9.1% versus 6.8% for the broader market.

DISPLAY 10: US HEALTHCARE HAS A STRONG TRACK RECORD OF EARNINGS GROWTH...

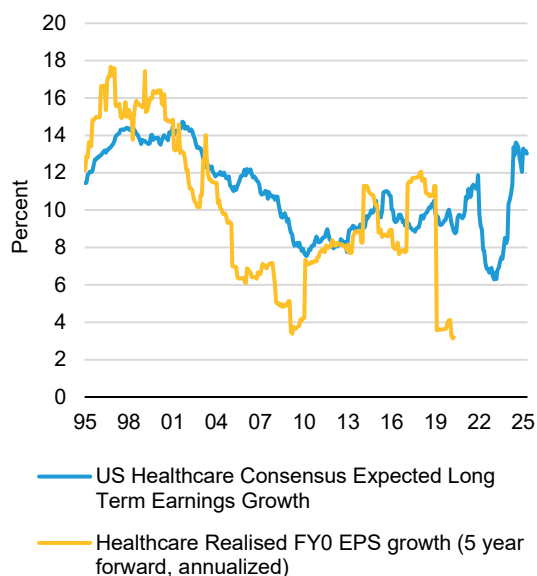


Historical analysis does not guarantee future results.

As of May 12, 2025

Source: IBES, LSEG Data & Analytics and AB

DISPLAY 11: ...AND MEETING ANALYST CONSENSUS EXPECTATIONS FOR LONG-TERM GROWTH



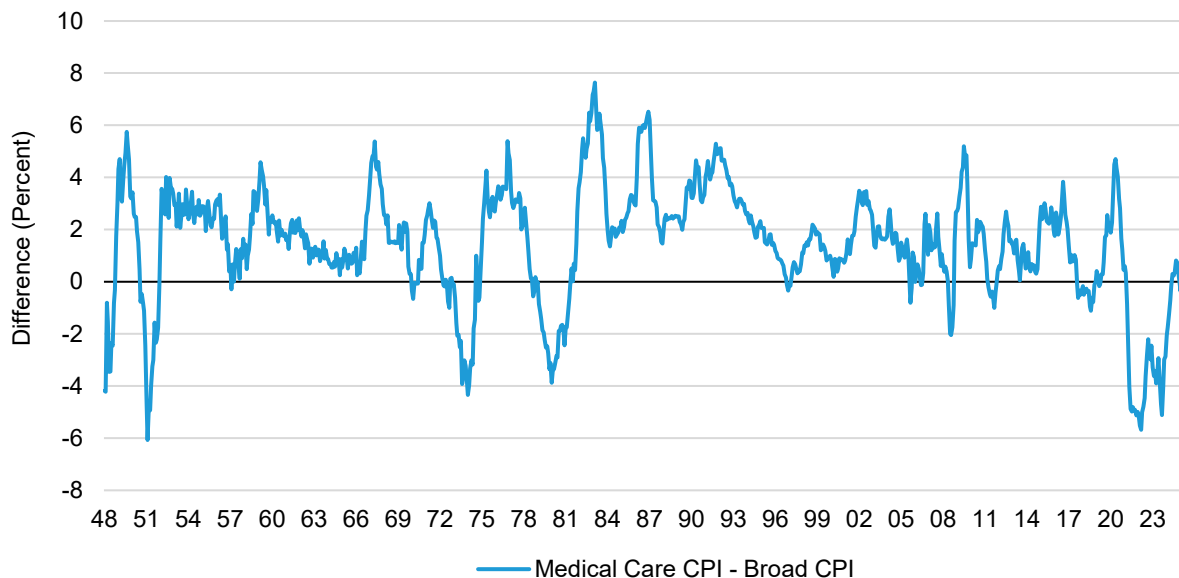
Historical analysis does not guarantee future results.

As of May 12, 2025

Source: IBES, LSEG Data & Analytics and AB

Over nearly 80 years, medical-care and drug inflation has grown faster than the overall Consumer Price Index (*Display 12*). To us, this is evidence of the strong pricing power in the sector, and it demonstrates healthcare's ability to deliver real earnings growth. As we noted in our recent research, [we expect inflation to be structurally higher and more volatile in the coming years](#). We also believe that the ability to grow earnings above inflation will become increasingly more valuable in this new macro regime; over time, that should warrant a premium valuation multiple.

DISPLAY 12: MEDICAL-CARE INFLATION HAS EXCEEDED BROAD CPI



Current analysis does not guarantee future results.

As of April 30, 2025

Source: LSEG Data & Analytics and AB

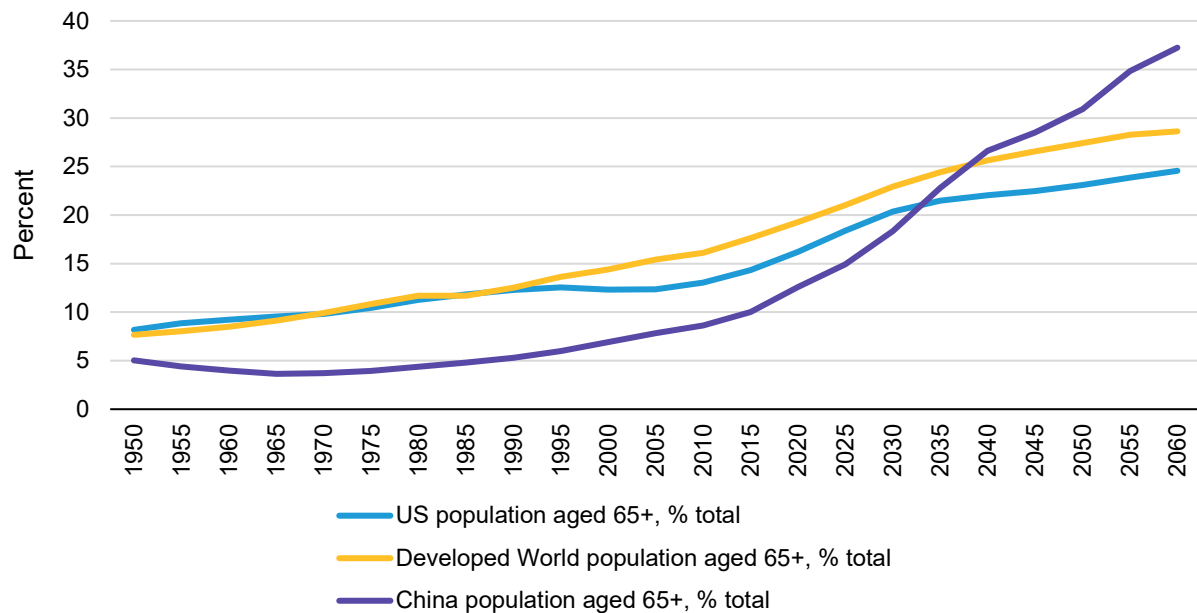
The US equity market is very heavily concentrated in the high-growth but expensive Magnificent Seven stocks. We think it would be prudent for investors to diversify the sources of growth in their portfolios, and that US healthcare exposure can be effective in that role—especially because it doesn't come at a significant valuation premium right now.

Long-term growth expectations for US healthcare should be achievable and supported by structural trends, namely the demographics of an aging population and the growing need for care. There are potential benefits from AI adoption, too, which we discuss in more detail below.

Demographics should be a strong structural tailwind for healthcare

Demographics will be a key mega-force defining the macroeconomic picture in the coming decades, as we see it, with the global population aging rapidly (*Display 13*). The share of the elderly population in the developed world, and China in particular, has risen over the last decade and is projected to grow substantially in the coming years. While the US has a comparably better demographic outlook, it faces the same trend.

DISPLAY 13: THE SHARE OF ELDERLY POPULATION LIKELY TO CLIMB ACROSS THE WORLD



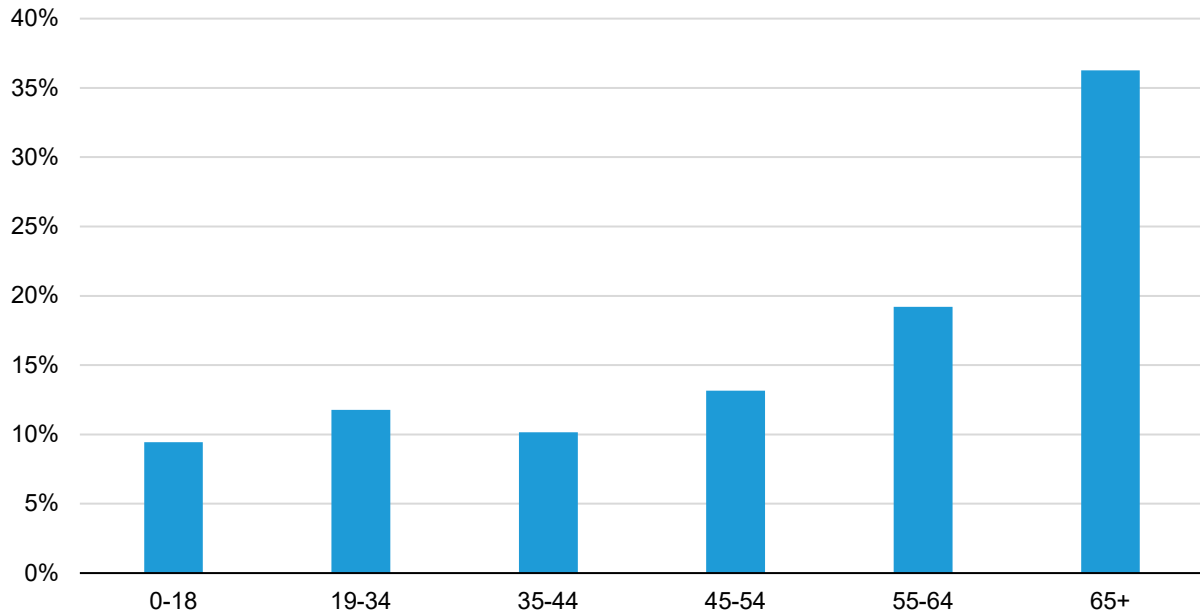
Current analysis does not guarantee future results.

As of March 5, 2025

Source: United Nations and AB

Those aged 65 and older account for a disproportionate share of overall healthcare spending (*Display 14*). So, as their share of the overall population grows, it will create a structural tailwind for higher spending on healthcare.

DISPLAY 14: THE ELDERLY ACCOUNT FOR A GREATER SHARE OF TOTAL US HEALTHCARE SPENDING
(PERCENT OF SPENDING BY AGE GROUP)



Current analysis does not guarantee future results.

Note: The results are based on 2021 survey data (for more info please see:

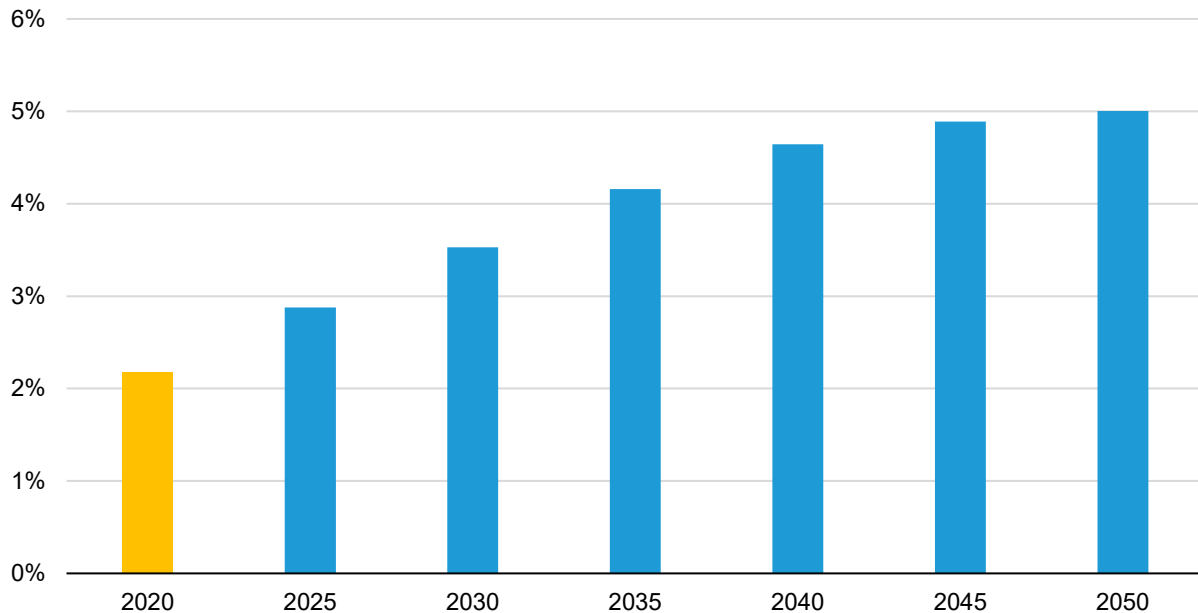
<https://www.healthsystemtracker.org/chart-collection/health-expenditures-vary-across-population/#Share%20of%20total%20population%20and%20total%20health%20spending,%20by%20age%20group,%202021>

As of March 5, 2024

Source: Peterson-KFF and AB

The share of very old people, aged 75 and older, is also growing rapidly. Unfortunately, this means an increasing prevalence of dementia and other diseases that require much greater care. We can illustrate this need by using United Nations demographic projections of people aged 75 and older. Our analysis suggests that the years through 2050 will see a large, sustained rise in the need for social care and social care facilities (*Display 15*).

DISPLAY 15: PROJECTED US NURSING AND RESIDENTIAL CARE WORKERS, % OF TOTAL



Current analysis does not guarantee future results.

Note the analysis uses UN demographic projections and assumes that 0.17 nursing and residential care workers will be needed for each person aged over 75.

As of December 2, 2024

Source: BLS, LSEG Data & Analytics and AB

The healthcare sector as an AI adoption beneficiary

Productivity gains resulting from widespread AI adoption are often presented as a possible solution to offset the negative impacts of deglobalization, demographics and climate change. While it is very hard to estimate the potential and durability of productivity gains at the overall level of the economy, especially at this early stage of adoption, we do see the healthcare sector as one of the clearest potential AI beneficiaries.

There have already been tangible AI-driven achievements in this arena, most notably the huge improvements in predicting protein structures by the AlphaFold AI program developed by DeepMind. Below, we consider other areas with a high likelihood of AI-enabled improvements:

- New-drug discovery could be improved and its cost lowered, and drug trials could be made more cost-effective. Novartis and Eli Lilly have already partnered with Isomorphic labs on AI-assisted drug development that capitalizes on the AlphaFold model.⁴
- In medtech, data analytics can be leveraged to enhance the use of hospital infrastructure, improve diagnostics and provide more personalized treatments to patients.
- The digitizing of medical records, better data management and workflow automation can free up doctors' time to focus on treatment, enabling them to see more patients. For example, in UnitedHealth Group's third quarter 2024 earnings call, CEO Andrew Witty noted that the company's nurses already use generative AI to review documents more efficiently and quickly. He also noted that AI is helping customer advocates with routine customer interactions and healthcare provider searches, giving them more time to focus on more complex customer inquiries.

⁴ <https://www.isomorphiclabs.com/articles/isomorphic-labs-kicks-off-2024-with-two-pharmaceutical-collaborations>

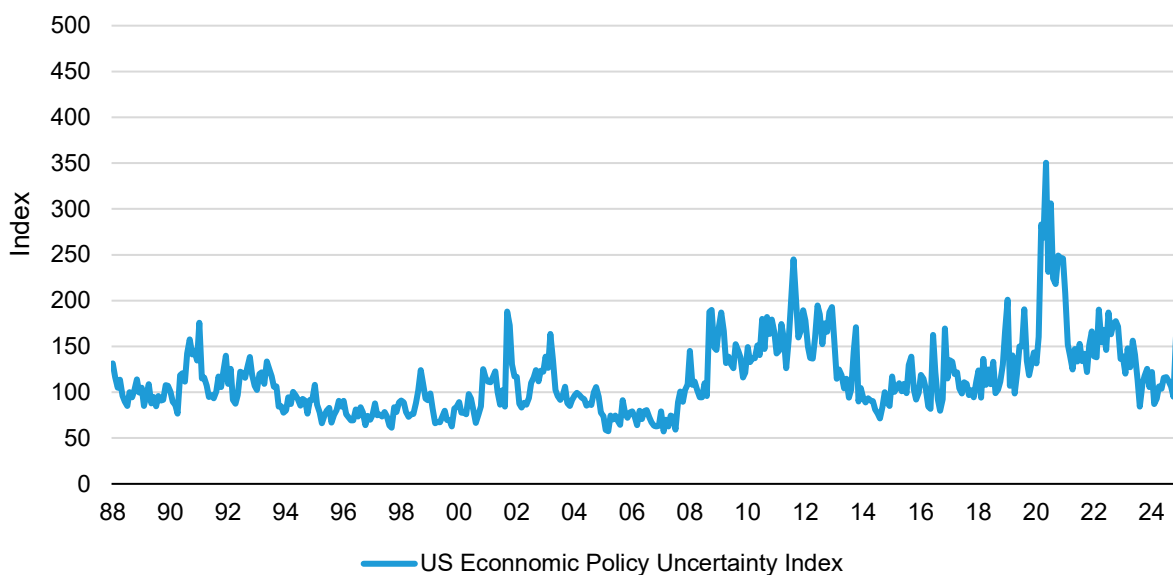
- AI-enabled data collection and the analysis of large-scale datasets can be used to develop more personalized treatment plans, help diagnose diseases earlier and reduce the need for invasive procedures. Ultimately, this leads to better patient outcomes and lower costs.
- Significant cost reductions are possible across the sector through lower R&D costs, enhanced operational efficiency, predictive medical-technology maintenance and automation of routine administrative tasks.

Healthcare exposure may play a stabilizing role in the portfolio

In the last few months, the US stock market has witnessed extreme bouts of turbulence; we expect high volatility to persist through this year and possibly beyond. Policy uncertainty in the US has reached extreme levels (*Display 16*) and we expect it to stay structurally higher for a while.

Despite the recent market correction, the Shiller PE ratio in the broader US equity market is 33x, firmly in the top decile versus history. Elevated valuations have historically indicated the risk of more severe future market drawdowns (*Display 17*), and drawdown risk is greater in the current climate of extreme market and geopolitical uncertainty.

DISPLAY 16: US POLICY UNCERTAINTY IS APPROACHING HISTORIC LEVELS

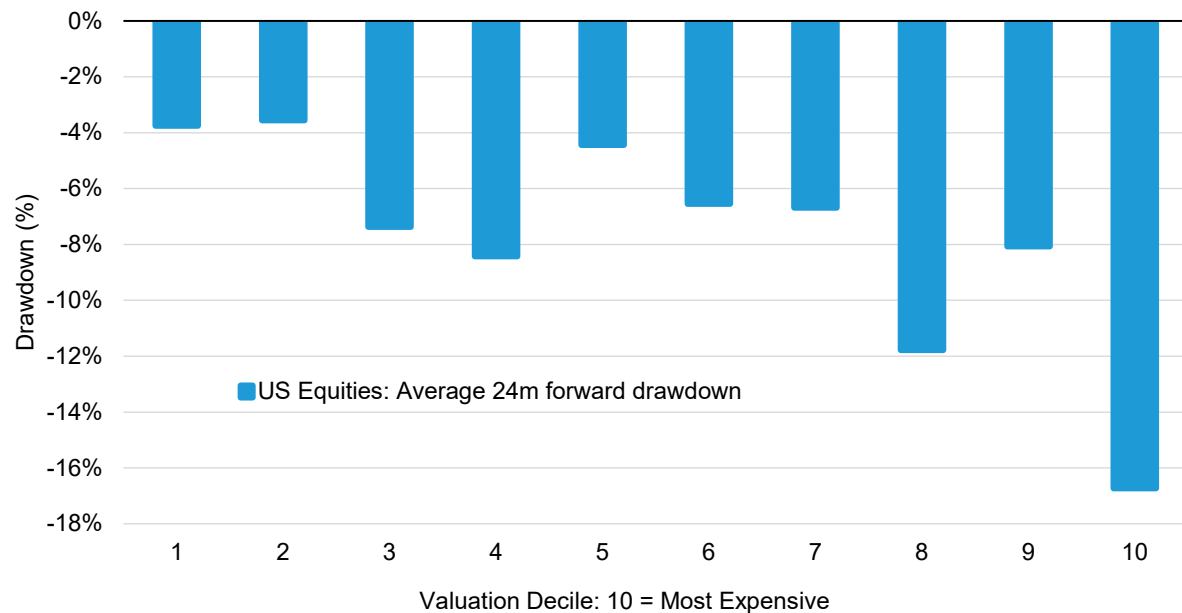


Current analysis does not guarantee future results.

As of April 30, 2025

Source: LSEG Data & Analytics, www.policyuncertainty.com and AB

DISPLAY 17: HIGHER VALUATIONS HAVE BEEN ASSOCIATED WITH BIGGER MARKET DRAWDOWNS



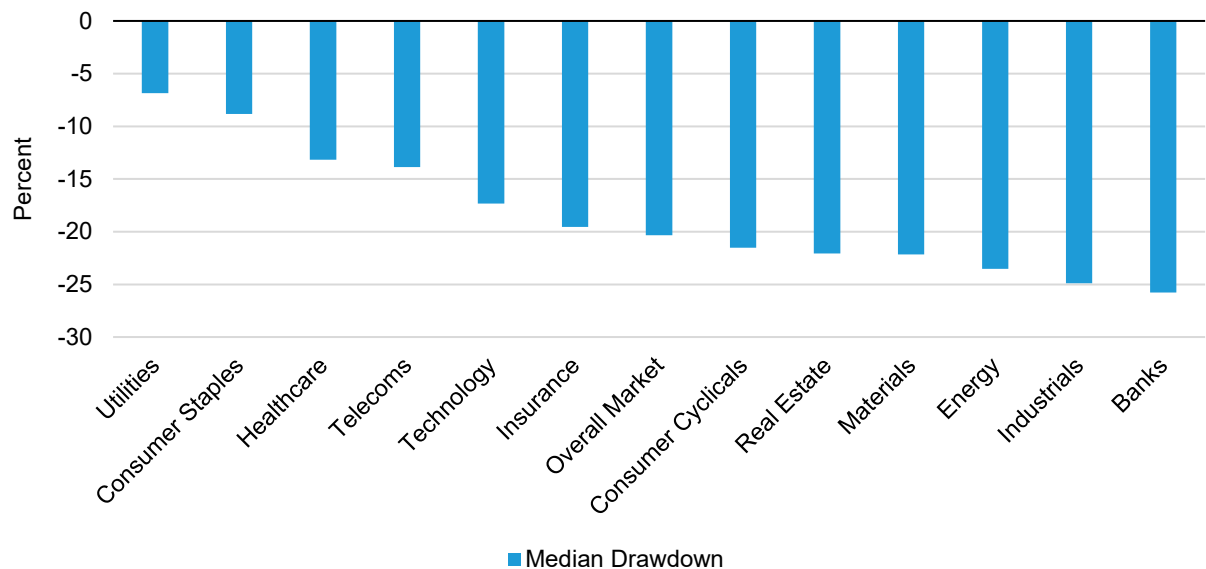
Current analysis does not guarantee future results.

Note: The analysis covers the period from January 1970 through to December 2024. Valuation is measured by the Shiller PE multiple.

Source: LSEG Data & Analytics, Robert Shiller's database and AB

Given the current state of the US equity market and the risk of drawdowns, we believe it would be prudent to consider adding assets to the portfolio to help weather market sell-offs. Historically, the healthcare sector has acted as a defensive allocation and has seen much lower drawdowns when market stress has been high (*Display 18*).

DISPLAY 18: MEDIAN US EQUITY SECTOR DRAWDOWN IN PERIODS OF MARKET STRESS



Current analysis does not guarantee future results.

The display shows the median drawdown for each sector from 1973 to 2025 in periods when the overall market drawdown was more than 10%.

Note: The analysis covers the period from January 1973 to January 2025.

Source: LSEG Data & Analytics and AB

The US economic growth outlook seems increasingly risky, which makes sectors with less potential downside worth pursuing. We've recently downgraded our growth forecast, now expecting only 0.5% growth in gross domestic product this year—with a significant probability of an outright recession. The current 12-month-forward PE multiple for the US healthcare sector is already at levels historically associated with a recession (*Display 19*), as defined by the OECD leading indicator. The absolute multiple for healthcare is also below those of other defensive sectors, such as consumer staples and utilities. Thus, we believe the potential downside to healthcare performance should be limited, even if US growth deteriorates into an actual recession.

DISPLAY 19: US SECTOR VALUATION AVERAGES AND THE BUSINESS CYCLE

	12m FWD PE Multiple												
	US	US Capital	US	US	US	US	US	US	US	US	US	US	US:
	Market	Equipment	Commodities	Consumer	Consumer	Defense	Energy	Financials	Healthcare	Real	Tech.	Comms.	Utilities
				Cyclicals	Staples					Estate			
Recovery	17.06	17.1	17.75	20.34	17.85	16.12	19.32	12.61	18.02	28.43	20.66	16.13	14.36
Expansion	17.48	18.03	16.81	20.73	18.41	17.4	17.3	13.07	19.44	27.63	21.38	17.2	15.01
Slowdown	17.22	17.72	15.16	20.58	18.02	17.1	16.01	12.66	19.19	26.31	21.6	16.86	15.07
Recession	15.66	15.59	14.87	18.77	17.15	14.41	15.81	11.68	17.84	23.02	18.81	15.63	14.06
Current Multiple	19.75	18.43	18.28	23.59	19.55	28.28	13.32	14.79	17.84	30.72	24.49	18.45	18.11

Current analysis does not guarantee future results.

Note: Periods of the economic cycles are defined by the US normalized seasonally adjusted composite leading indicator from the OECD.

Expansionary level (>100) and positive first differential of the leading indicator is classified as an 'expansion', an expansionary level with negative first differential is a 'slowdown', a contraction level (<100) and positive first differential is classified as a 'recovery' and a contraction level with negative first differential is a 'recession'.

As of April 20, 2025

Source: Factset, LSEG Data & Analytics and AB

Conclusion

It's true that a significant level of policy uncertainty surrounds the healthcare sector, as new US leadership has proposed a number of policies aimed at that part of the economy. But in our view, much of this cloudiness has been reflected in current valuations and investors' views toward the sector.

That should reduce the amount of downside in US healthcare, from our perspective. As the market currently stands, that translates into an attractive valuation for adding a strategic overweight to the sector. Investors can also access what we see as strong structural growth prospects from the effects of an aging population and AI efficiencies. And healthcare has the potential to cushion portfolios in a time of macro uncertainty, given its historically defensive nature.

Nashville 501 Commerce Street Nashville, TN 37203 United States (212) 969 1000	New York 66 Hudson Boulevard East New York, NY 10001 United States (212) 969 1000	London 60 London Wall London EC2M 5SJ United Kingdom +44 20 7470 0100	Singapore One Raffles Quay #27-11 South Tower Singapore 048583 +65 6230 4600
Tokyo Hibiya Parkfront 14F 2-1-6 Uchisaiwaicho, Chiyoda-ku Tokyo, 100-0011, Japan +81 3 5962 9000	Toronto 200 Bay Street, North Tower Suite 1203 Toronto, Ontario M5J 2J2, Canada (647) 375 2803	Sydney Level 32, Aurora Place 88 Phillip Street Sydney NSW 2000 Australia +61 02 9255 1200	Hong Kong 39th Floor, One Island East, Taikoo Place 18 Westlands Road Quarry Bay, Hong Kong +852 2918 7888

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