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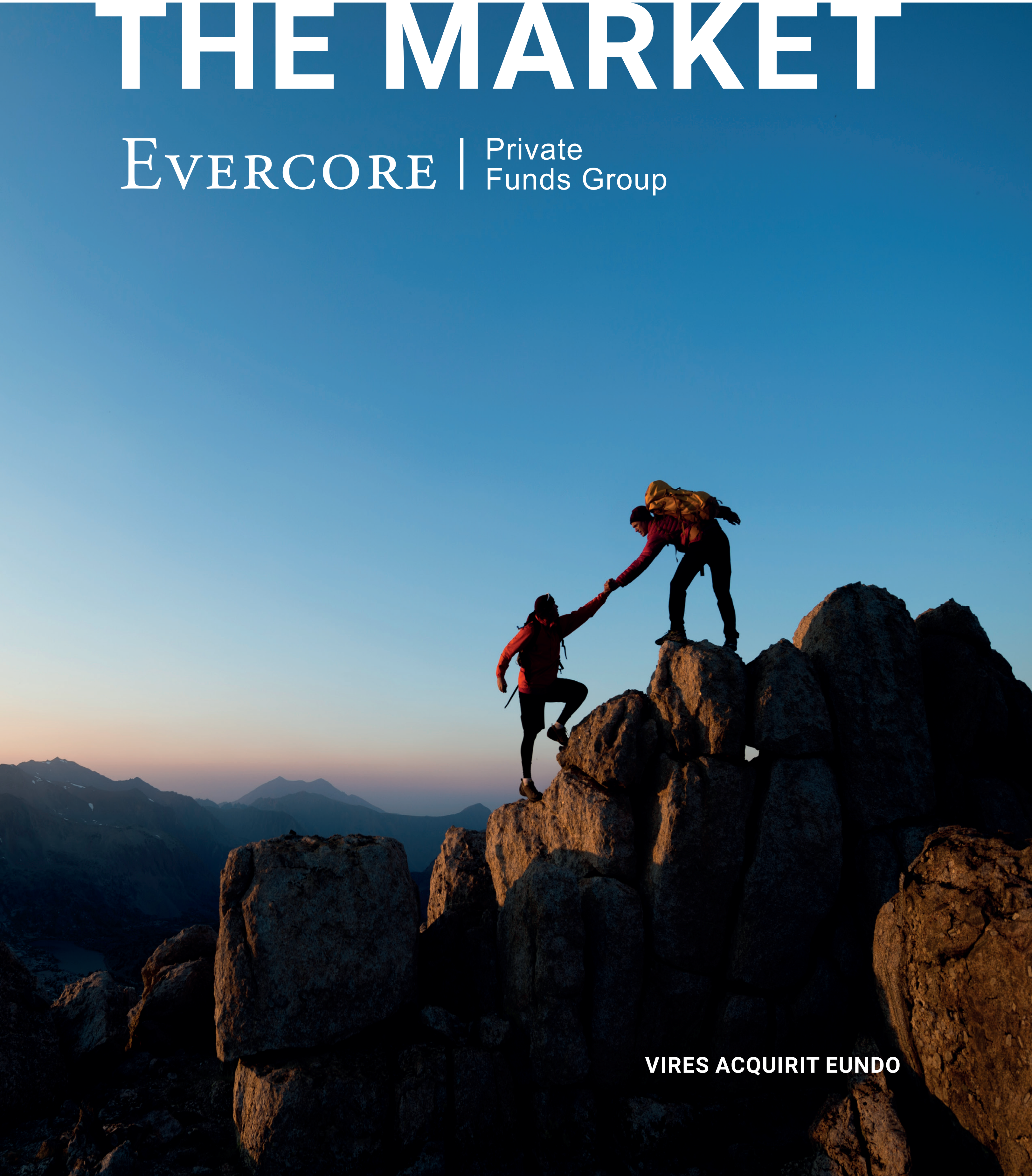

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The importance of healthcare as an investment sector

BY JO NATAURI, FOUNDER OF INVIDIA CAPITAL MANAGEMENT

The US healthcare sector, valued at over $4.5 trillion and projected to make up nearly 20% of the nation's GDP by 2031,[1] is not only a cornerstone of the economy but also a dynamic space for innovation and investment. This sector's significance spans personal, political and societal dimensions, attracting sustained private equity interest, which has tripled in the past decade. As an industry that has historically outperformed other sectors across economic cycles, healthcare remains an attractive area of investment with potential to drive large-scale change and improve millions of lives across the US.

Over the past decade, private equity investments in healthcare have grown threefold, driven by new market dynamics and innovations, catalysed by the pandemic.[2] These changes have introduced a multitude of fresh opportunities, bringing a wave of accelerated innovation across the industry not just in terms of products, but also in healthcare delivery services driven by the adoption of new technologies. The attraction of investing in healthcare is only matched by the complexity of a highly diverse industry where multiple constituents and regulatory considerations often drive outcomes.

Invidia Capital Management was founded in 2024 to harness these long-term investment opportunities emerging within the healthcare sector. Based in New York, Invidia is a healthcare-focused private equity firm specialising in mid-market investments across North America. Under the leadership of Jo Natauri, formerly Global Head of Private Healthcare Investing at Goldman Sachs, Invidia has been established with a vision to build a world-class firm committed to advancing healthcare through strategic investments and a culture of integrity. Guided by a team of seasoned healthcare experts, Invidia's approach aims to drive impactful value for patients, providers and payors alike, aligning with the firm's mission to bring meaningful improvements to the complex healthcare ecosystem. By investing in healthcare's evolving landscape, Invidia seeks to unlock opportunities created by sustained innovation and increasing demand.

Innovation and permanent demand supports long-term healthcare thesis

The healthcare sector's sustained innovation and permanent demand create a strong foundation for long-term investment opportunities. According to the US Bureau of Economic Analysis, healthcare innovation accounts for at least 18% of real per capita growth.[2,3] Biopharma research and development ("R&D") spending also demonstrated a compound annual growth rate ("CAGR") of 12% worldwide and 15% in the US from 1986 to 2023.[4] Declines in R&D spending during economic downturns have generally been short-lived. In terms of costs, since 1990, nursing, healthcare technology and home healthcare professions have experienced consistent growth (excluding 2020) driven by underlying healthcare demand increases.[5] Health insurance premiums for workers and employers increased by 4% per year from 2013 to 2023, with 65% of US workers covered by self-funded plans, up from about 50% in 2000.[6] Looking ahead, healthcare profit pools are expected to grow from $583 billion in 2022 to $819 billion by 2027, a CAGR of 7%.[7] Inflation is also projected to increase healthcare spending by more than 4% through to 2032.[8]

Innovation is essential for improving health outcomes, but, within healthcare, it is often a lengthy and costly endeavor. A recent study estimated that the average cost of developing a new drug is nearly $900 million, accounting for failures and capital costs.[9] With only an 8% success rate in clinical trials, the risk of commercial success remains high, even when new drugs show safety and efficacy.[10] By supporting these companies, investors help ensure that potentially transformative therapies have sufficient funding to achieve their promise, driving improved health outcomes.

The complex nature of the healthcare sector is primed for PE-driven transformation

Despite increased healthcare spending, the US continues to lag in health outcomes.[2] A report from the Commonwealth Fund ranks the US last among ten peer countries based on five key metrics: access to care, care process, administrative efficiency, equity and health outcomes.[2] A significant cause of this disconnect is the fragmented nature of the country's healthcare system, composed of multiple, independent care networks, insurers, payors and benefit managers leading to increased friction for patients navigating the system.

The complexity of the US healthcare system leads to inefficiencies in data sharing, which drive up costs and increase the risk of medical errors. For example, compliance with the Health Insurance Portability and Accountability Act (HIPAA) regulations costs approximately $8.3 billion annually, yet the regulations have done little to facilitate effective data sharing among patients and providers.[11] Organisations that fail to comply with regulations face additional costs, averaging $10 million.[11] Provider shortages, largely driven by burnout from excessive administrative burdens and record-keeping requirements, also reduce access to care. In a recent survey, 53% of US physicians reported feeling burnt out and 23% exhibited signs of depression, with both trends worsening since the Covid-19 pandemic.[12,13] The increasing demand for cost-effective and outcome-improving solutions creates significant opportunities. However, identifying the right ones that can deliver real value and achieve the healthcare improvements we need remains challenging. Understanding key trends can guide investors toward opportunities for true value creation by unlocking either product or service expansion.

Given the complexity of the industry, Invidia has assembled a distinguished set of Senior Advisers and a broader executive network comprised of healthcare leaders to provide strategic input and guidance on navigating the sector. Between these two groups and the team's broader individual networks, Invidia has developed a diverse set of connections across the sector, built over decades of the team's experience and a large number of transactions at prior firms. In so doing, Invidia intends to focus on investment opportunities underpinned by long-term, sustainable growth trends within healthcare. The four primary focus areas of opportunity are:

1. Supporting R&D and innovation: Investing in companies that drive science and R&D in healthcare, underpinned by a belief in the sector's perpetual demand for innovation. This area allows Invidia to strive to capitalise on advancements in science that will continue to shape healthcare in the long term.

2. Tech-enabled services: While healthcare is resistant to direct tech disruption, Invidia believes that tech-enablement enhances efficiency, diagnosis and patient outcomes, making this area ripe for growth.

3. Delivery transformation: Changes in where and how healthcare is delivered have accelerated post-Covid-19. With financial pressure on hospitals and shifts in patient preferences, Invidia believes that opportunities exist in areas like outpatient services, telehealth and urgent care centres that offer lower-cost and accessible alternatives.

4. Consumer-oriented healthcare: As healthcare costs rise, consumers are increasingly responsible for their care choices and costs. This shift can create opportunities in sectors focused on consumer-driven healthcare solutions, including digital health and at-home diagnostics.

Long-term tailwinds, including continued R&D spending and innovation potential, position these target sub-sectors for sustainable growth.

Continued adoption of technology will transform healthcare

Rapid innovation in the technology sector, especially as it relates to utilisation of large data sets, are expected to continue to have an outsized impact on the healthcare industry. Currently, about 30% of all data generated worldwide is healthcare-related and health data is expected to grow faster than in other sectors.[14] Big data approaches are improving the efficiency and accuracy of disease diagnosis, drug development and the identification of factors that influence therapy response. However, challenges in healthcare data collection, storage and sharing create inefficiencies and increase the risk of medical errors. Innovative solutions leveraging artificial intelligence ("AI") and machine learning offer significant potential to address these issues. Yet, the feasibility of deploying tech-based solutions across the healthcare ecosystem remains uncertain. On average, hospitals use 16 different electronic health record systems across affiliated practices and 98% of referrals are still done by fax, despite the availability of electronic options.[15, 16] Entrenched behaviours, resistance to change and the learning curve associated with new systems can limit the real-world value of innovation. Investing in companies that not only develop solutions for healthcare needs but also have strategies to drive adoption can be key to delivering quality care for patients and improving provider productivity.

Opportunities in a post-pandemic healthcare landscape

The Covid-19 pandemic accelerated provider burnout, exacerbated primary care and nursing shortages and led to hospital closures, especially in rural and low-income areas. While these challenges hinder access to timely and effective care, they also present opportunities for companies that can address these issues. Outsourcing equipment, for instance, can help reduce capital expenditures and improve health equity. A mobile MRI unit that travels between facilities can increase access to imaging technology at a cost that is lower than installing systems in multiple locations. Additionally, approaches that enable home-based care, telemedicine and care delivery in retail settings are poised for growth. Prior to the pandemic, only about 1% of medical and behavioural health visits were conducted virtually; today, that figure stands at 25%.[17] The at-home diagnostic testing market has also grown, now valued at $45.6 billion, and is expected to expand by over 10% annually through 2031.[18] Private equity investors appear to have an opportunity to achieve substantial return on investment ("ROI") by supporting companies that leverage virtual communication to increase access, enhance patient-provider interactions, improve adherence to treatment and expand care delivery beyond traditional clinical settings.

Conclusion

In addition to the growth in healthcare-related spending and investment, there are multiple underlying tailwinds that private equity investors should consider: the ageing population, increasing incidence of chronic disease and persistent health inequities. Supporting companies that facilitate interconnectivity across the healthcare landscape, create new care delivery and payment models and enable safer, more effective health interventions is important for addressing these challenges. These initiatives also create exciting opportunities for investors such as Invidia, who have the experience to assess the complexities of the regulatory environment and the specific technologies needed to achieve these goals. With this understanding, private equity investors seek to deliver meaningful results for patients, providers and the healthcare system as a whole while achieving significant ROI.

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