

Healthcare's Challenges Present Significant Opportunities for Investors

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Healthcare has been a broadly disappointing sector for investors in recent years. Unsurprisingly, many of the largest and longest-lasting impacts of the COVID-19 pandemic have been concentrated in the industry, from nurse and physician shortages, to unpredictable utilization of healthcare services, to a volatile biotech and life sciences funding environment.

Many market participants attempt to trade around these disruptions or wait on the sidelines for some level of equilibrium, the arrival of which is difficult to predict. At Riverbridge, we believe healthcare is one of the most important sectors in our economy for investors and business leaders alike to take a long-term approach.

According to the Centers for Medicare and Medicaid Services (CMS), National Healthcare Expenditure (NHE) reached \$4.9 trillion in 2023, equating to roughly \$14,600 per person in the United States and 17.6% of US GDP.¹ Costs have long outpaced inflation and are projected to continue to do so, creating tension between the dual necessities of quality and economical care. The regulatory, political, and financial complexities of the industry are challenging for all stakeholders. Yet within these challenges exist numerous long-term opportunities for adaptable, innovative businesses to improve access, affordability, and outcomes for patients.

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One side effect of recent disruptions in healthcare is that many investors have lost sight of ongoing long-term trends that will shape the next decade and beyond. These trends include caring for an aging population, developing innovative therapies, modernizing the industry's IT infrastructure, and the shift from an uncoordinated, fee-for-service model to a value-based care model. In each area, the challenges are coupled with ample opportunity.

Adults over age 65 require 50% more healthcare resources than the average person.² Thus, America's demographic shift has created—and will continue to create—upward pressure on healthcare spending. This will present opportunities for businesses that can deliver quality care in lower-cost settings than a hospital and/or provide treatments, services, or technologies to manage chronic diseases and keep patients in their homes.

Scientific breakthroughs have allowed researchers to develop more targeted and more effective treatments. However, such treatments have also become more cumbersome to develop, manufacture, commercialize, and administer due to their complex biologic compositions. As a result of this increasing complexity, a life sciences ecosystem has developed to innovate around these challenges and support the pharma and biotech industry. Danaher (DHR), for example, has built a formidable position offering a range of tools, technologies, and services to advance drug discovery

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and support end-to-end bioprocessing workflows. The company's solutions address everything from the initial cell line development to filtration and final drug product fill—helping customers optimize the production and yield of biologic therapies.

Despite these great technological and scientific advancements, much of the healthcare industry is operating on outdated IT infrastructure. As with many highly regulated industries, systems remain siloed and uncommunicative. This increases the difficulty of coordinating and integrating data flow with patient care. Longer-term, IT modernization—including the utilization of Artificial Intelligence—will unlock insights to identify and manage health issues more effectively. When combined with the ongoing consumerization of healthcare and innovation in wearables and patient monitoring, this will create opportunities to make a constrained healthcare labor force more productive and keep more patients out of high-cost care settings.

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All three of these trends are occurring in the context of a slow but durable shift in how providers are paid. Thus far, healthcare has primarily operated under a fee-for-service model, in which providers are incentivized for treating acute episodes instead of prevention. This limits care coordination and economic alignment between payers and providers. Progress toward a value-based reimbursement model based on patient outcomes has not been linear but is becoming increasingly more common, underscored by CMS's goal to have 100% of Medicare beneficiaries involved in accountable care relationships—in which providers have a stake in the quality and total cost of a patient's care—by 2030.³

Privia Health (PRVA), for example, is a company that has identified the opportunity in enabling physician practices to shift toward value-based care. Privia's technology platform helps independent physicians to more effectively run their practices, improving care for its patients and reducing administrative burden. Simultaneously, the company has built the capabilities and partnerships with payers to help such practices transition to value-based care arrangements over time. Its business and technology platform were designed with the long term in mind, engaging in care and risk models that range across different patient populations

as well as a variety of reimbursement structures. Privia can flexibly serve today's needs and navigate the evolving healthcare ecosystem as a strategic partner at any stage of a practice's transition to value-based care arrangements.

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Riverbridge's approach to investing in healthcare is representative of our overall investment approach. We seek enduring business models that are not dependent on a narrow set of circumstances to be successful. Throughout the Riverbridge portfolios, we focus on finding companies that are built for long-term adaptability. Self-financed businesses capable of consistent unit growth regardless of the economic environment are well positioned to traverse the challenges and capture the opportunities presented over time in our ever-evolving world.

¹ Centers for Medicare & Medicaid Services. (n.d.). National health expenditure data: Fact sheet. U.S. Department of Health and Human Services. Retrieved January 8, 2025, from <https://www.cms.gov/data-research/statistics-trends-and-reports/national-health-expenditure-data/nhe-fact-sheet>

² Centers for Medicare & Medicaid Services. (n.d.). National health expenditure data: Fact sheet. U.S. Department of Health and Human Services. Retrieved January 8, 2025, from <https://www.cms.gov/data-research/statistics-trends-and-reports/national-health-expenditure-data/nhe-fact-sheet>

³ U.S. Department of Health and Human Services, Centers for Medicare & Medicaid Services. (October 29, 2024). Medicare Shared Savings Program continues to deliver meaningful savings and high-quality health care. [Press Release] <https://www.cms.gov/newsroom/press-releases/medicare-shared-savings-program-continues-deliver-meaningful-savings-and-high-quality-health-care>

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