

Weekly Report

What are the consequences of the new health care legislation ?

After months of speculation we finally get a certain level of clarity. The most positive point is certainly that a Public Plan Option has not passed. Many issues are however still unclear as the House did not only approve the Senate bill, which has been passed in December, but also agreed to an amendment. This second bill will be presented as a budget reconciliation tool to the Senate as it requires only a simple majority vote. Senate Republicans fiercely oppose the provisions, which have been added by the House and will use every procedural tactic they can to block the reconciliation bill. If the Senate succeeds in making changes (the deadline is March 29), the House would need to vote on it again before President Obama can sign it into law. The two bills together would cost \$ 940 billion over 10 years and cover 32 million uninsured Americans according to Congressional Budget Office estimates. The overhaul would be financed largely through new taxes. The reconciliation bill would add a 3.8 % Medicare tax on high income earners to the higher Medicare payroll tax, which has already been included in the Senate bill. Industry fees under the reconciliation plan would be higher than in the Senate bill or transformed into an excise tax. Generally, medical device makers, the pharmaceutical industry and insurers would in most cases face higher costs, partially offset by more volume. The increased level of insured lives seems to benefit PBM and drug distributors (ESRX, MHS, ABC, CAH, MCK) as well as Medicaid companies (AGP, CNC, MOH) and acute care companies (CYH, HMA, THC).

Foreign Exchange

The USD seems the major beneficiary of several concurrent trends. Interest rate hikes by India and potentially China, which might slow down the economic recovery, are substantially reducing investors' risk appetite. Remarks by the IMF, advanced economies were facing acute challenges in tackling public debt, had the same effect. The Greek situation stills clouds the EUR. Rumors of another discount rate hike by the Federal Reserve have now circulated for several days. We indeed expect a swift normalization of the discount rate, forcing depository institutions to borrow in private markets rather than from the Fed. Substantial liquidity drainage, starting seriously next month and an eventual rise in the Fed fund rate expected in early autumn will continue to support the USD also on a medium term perspective. We anticipate that the Fed will raise rates at a more rapid way than what is generally expected. Additionally, the USD will lose the status of the carry trade currency of choice. The Asian- and commodity-sensitive AUD is anticipated to suffer in the current setting.

	Short-term trend	Last
EURUSD	→	1.3490
USDCHF	→	1.0627
USDJPY	→	90.017
GBPUSD	↑	1.5014

Fixed Income

India surprised markets by increasing the benchmark reverse repurchase rate to 3.5 % from a record low of 3.25 % and the repurchase rate to 5 % from 4.75 %. Heightened inflation concerns have reportedly triggered this action, which was only expected in April. India is set to raise rates again next month in order to successfully battle acute price pressures. The proactive move by the Indian central bank additionally raised fears of an imminent rate hike of the Chinese central bank. Sharply rising price indicators and spiraling house prices would justify such a step. Uncertainty in respect to higher interest rates, which potentially endanger the economic recovery, are denting demand for higher-yielding currencies and are favoring USD investments. At the same time, investors are increasingly worried of yet another massive cost of \$ 940 billion stemming from the health care reform, demanding higher premiums. The liquidity withdrawal programs, which will switch into higher gear after finishing the planned \$ 1.26 trillion of agency mortgage-backed securities purchase program, will undoubtedly lead to higher interest rates.

	Forecast end 10	Last
US 10y T %	4.80	3.69
Fed funds	2.25	0-0.25
Bund 10y %	4.00	3.08
ECB rates	1.25	1.00

Stocks

From the above-mentioned names in the healthcare space we like Express Scripts (ESRX) for some time. Despite its vertiginous chart the stock seems still at least 10 % undervalued on a fundamental basis. The company should experience accelerating profit growth on faster pace of generic introduction in the mail channel. In the acute care field our favorite name is Health Management Associates (HMA). The company owns over 50 facilities in 15 states with concentration in Florida and Mississippi. After having experienced some management turnover, the company seems now on an upward trend with substantial recruitment of new physicians and improvements in the emergency room area. The company reported solid results and the 2010 outlook suggests that the turnaround initiatives gain traction. The impact of the health care reform on our current holding DaVita (DVA) seems neutral as all patients are already covered for dialysis. At the same time, it will not be affected by cuts as is the case for many other sub-sectors. We expect further operating margin expansion as the payment environment will increasingly be bundled.

	Forecast end 10	Last
S&P 500	1230	1148
NASDAQ	2450	2358
DJ STOXX 600	270	257
SMI	7000	6825