HEALTHCARE – OPERATING FUNDS SURVEY

2019

NEPC, LLC

BOSTON | ATLANTA | CHARLOTTE | CHICAGO | DETROIT | LAS VEGAS | PORTLAND | SAN FRANCISCO

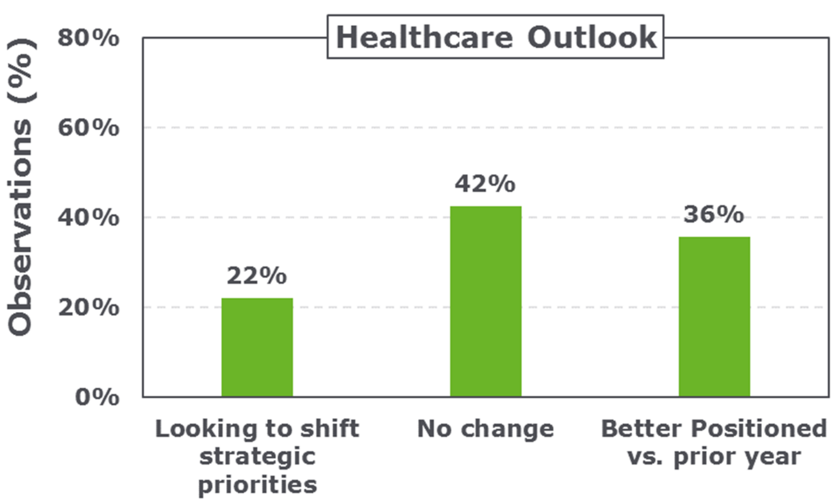
KEY TAKEAWAYS

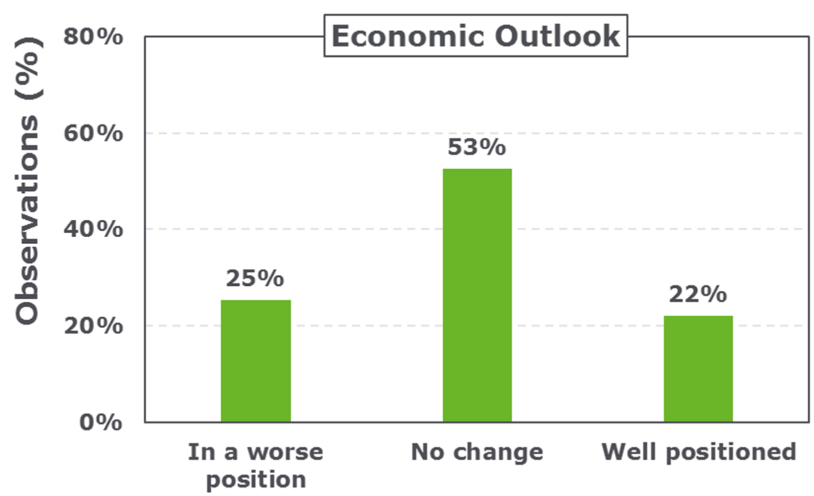
- Survey participants experienced mostly negative returns in 2018, prompting a reduction in investment risk
- Economic outlook and organizational priorities remained consistent year-over-year
- Most respondents expect equity markets to increase 6%+ in 2019
- Despite high expectations for US equity returns, investment portfolios are unlikely to change

CONSISTENT ECONOMIC AND HEALTHCARE OUTLOOK

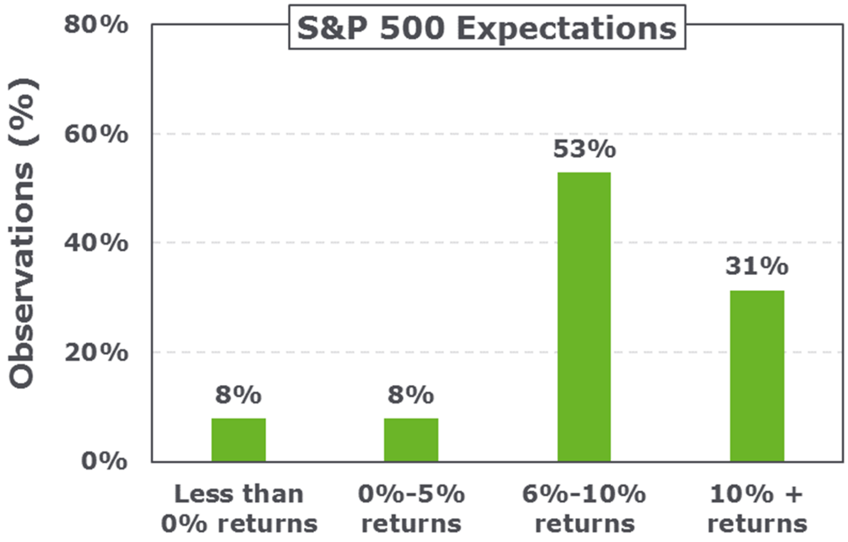
Overall, healthcare systems appear to have maintained a similar, positive outlook from prior year

		Organizational Outook			
		Looking to shift strategic priorities	No change	Better positioned vs. prior year	Total
Economic Outlook	Well positioned	5%	7%	10%	22%
	No change	12%	27%	14%	53%
	In a worse position	5%	9%	12%	25%
Total		22%	42%	36%	100%

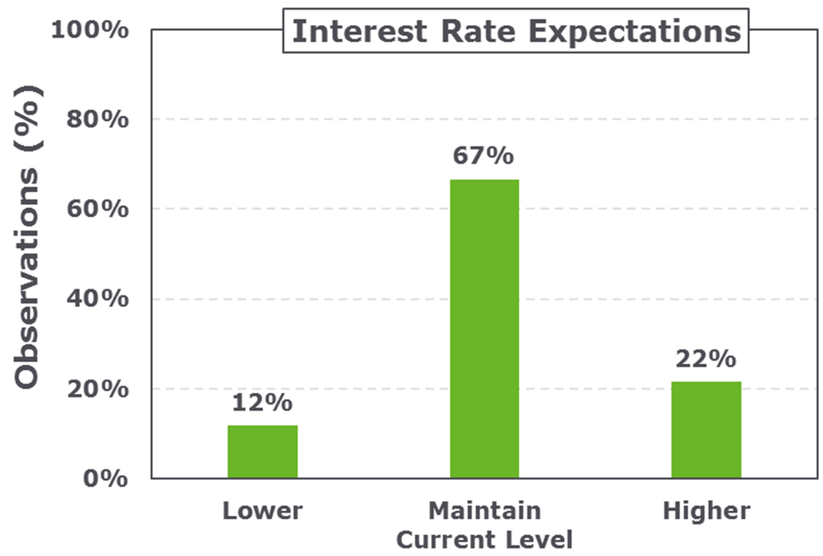




OPTIMISTIC MARKET OUTLOOK



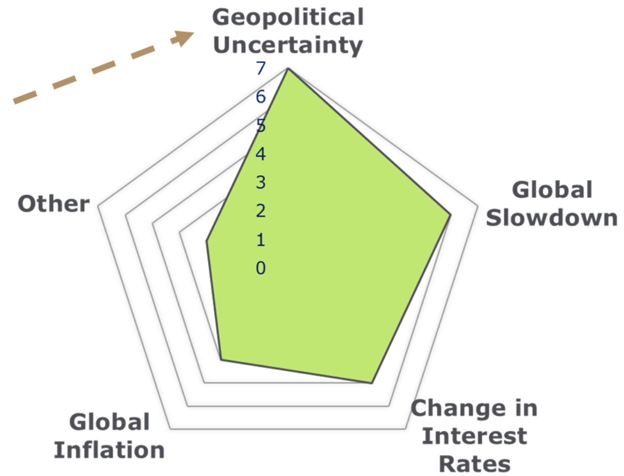
Strong equity outlook, perhaps supported by …

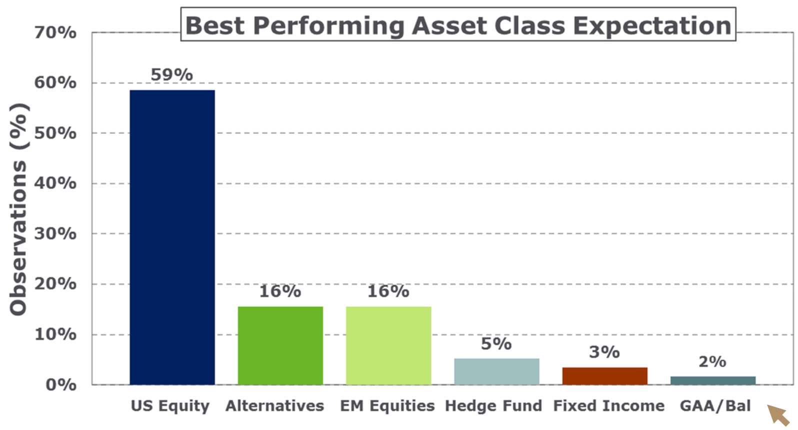


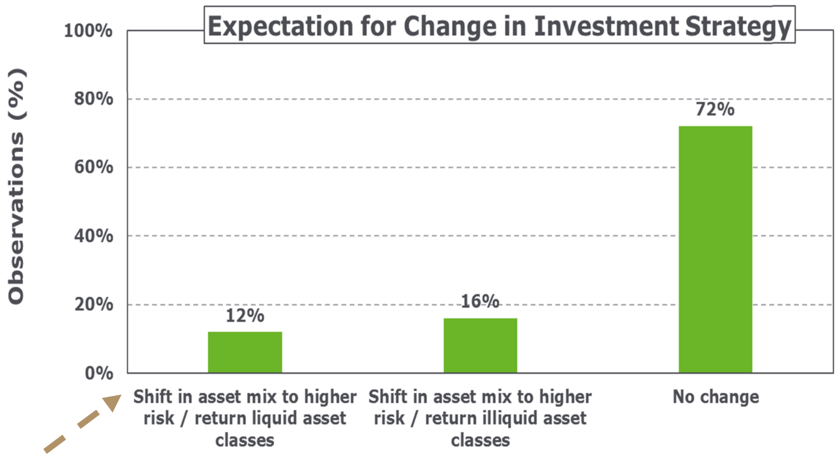
… limited expectations for near-term rate increases

INVESTMENT THREATS & OPPORTUNITIES

Geopolitical risk continues to be the greatest investment concern among respondents

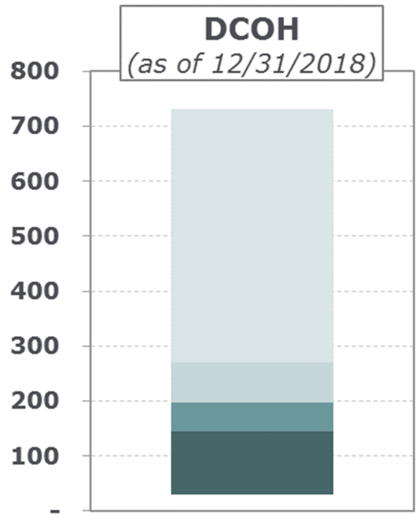


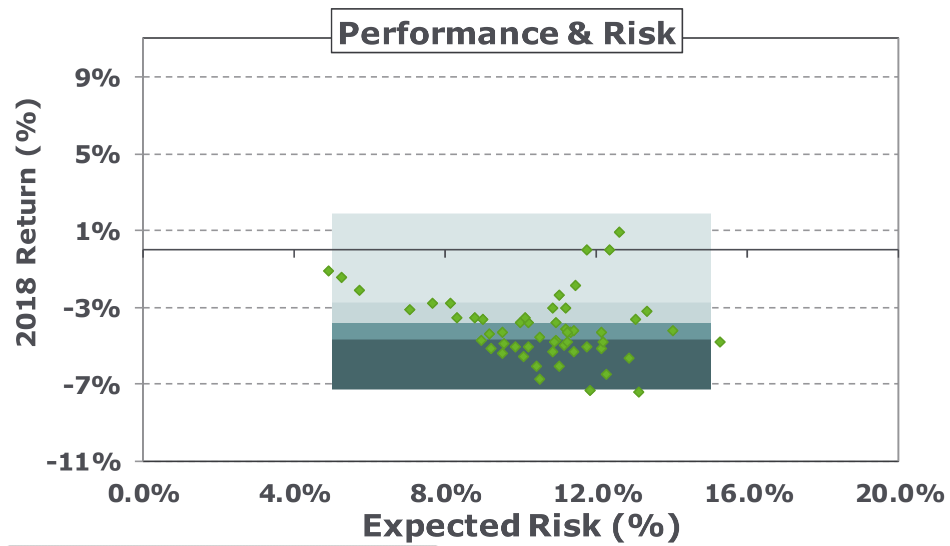


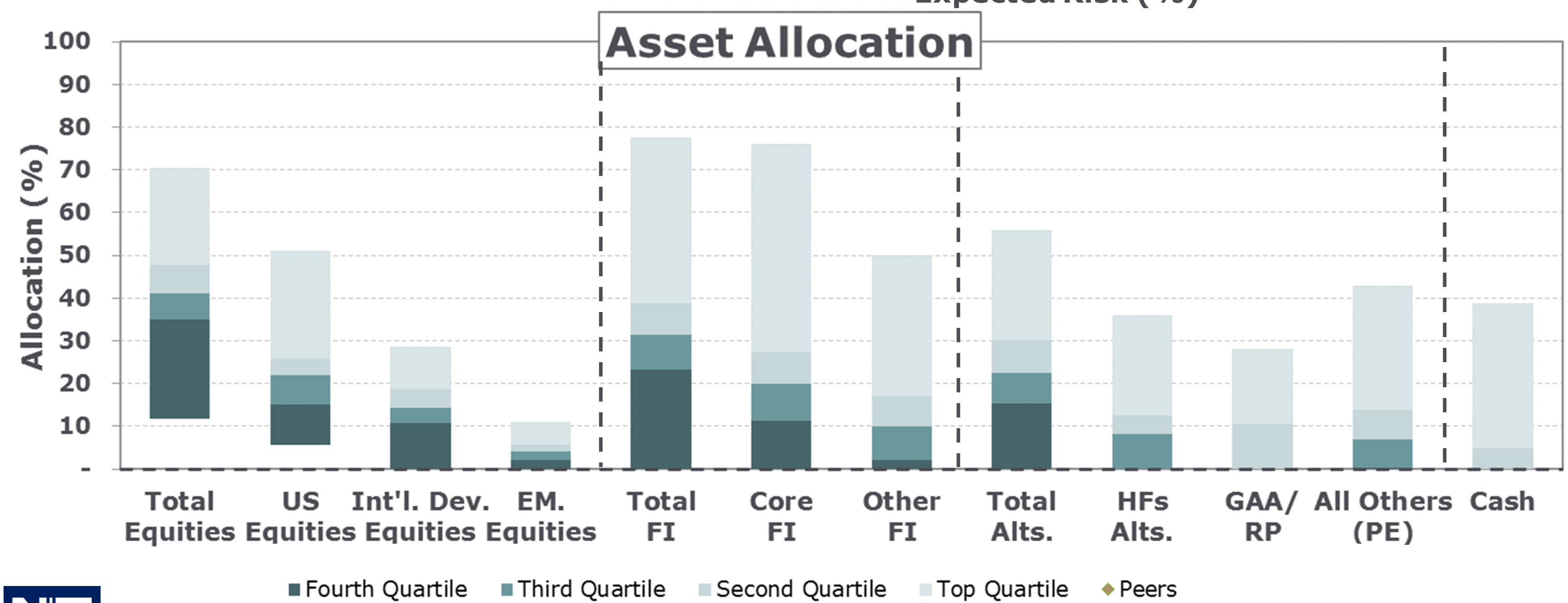


Despite significant YoY increase in return expectations for US Equities, investment portfolio strategies are unlikely to change

ASSET ALLOCATION VS. TOTAL UNIVERSE





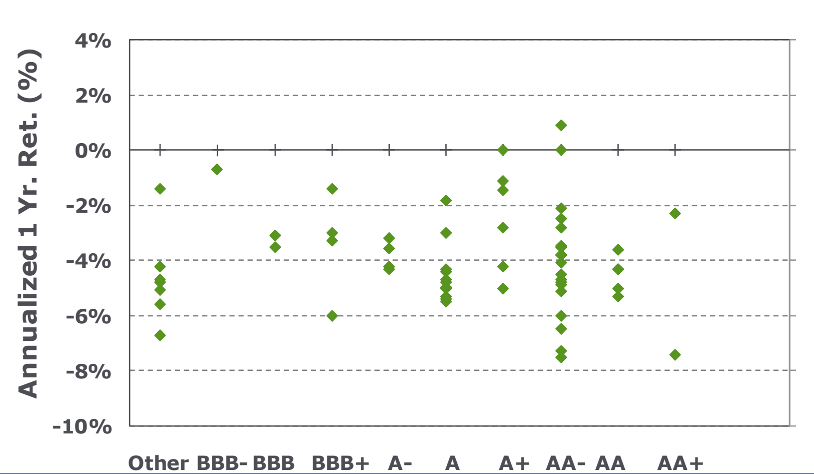


Note: 68 observations
Expected risk estimated using NEPC 2019 assumptions

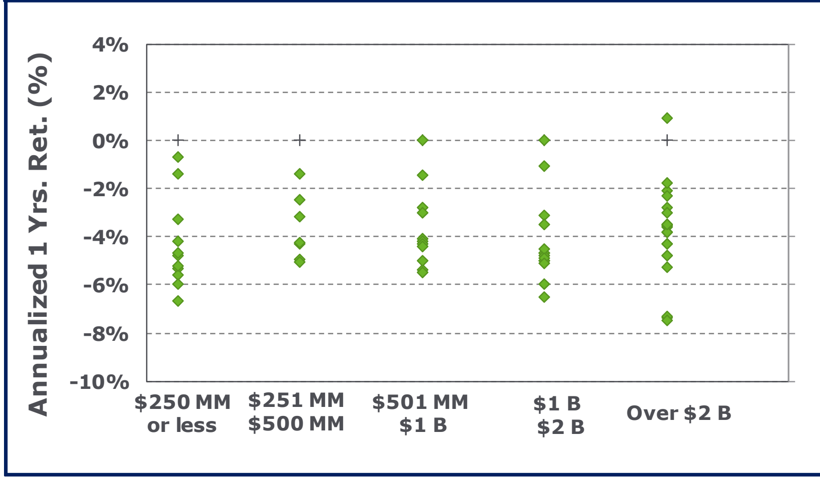
ACTUAL RETURNS RELATIVE TO SYSTEM METRICS

1 year annualized net of fees as of 12/31/2018

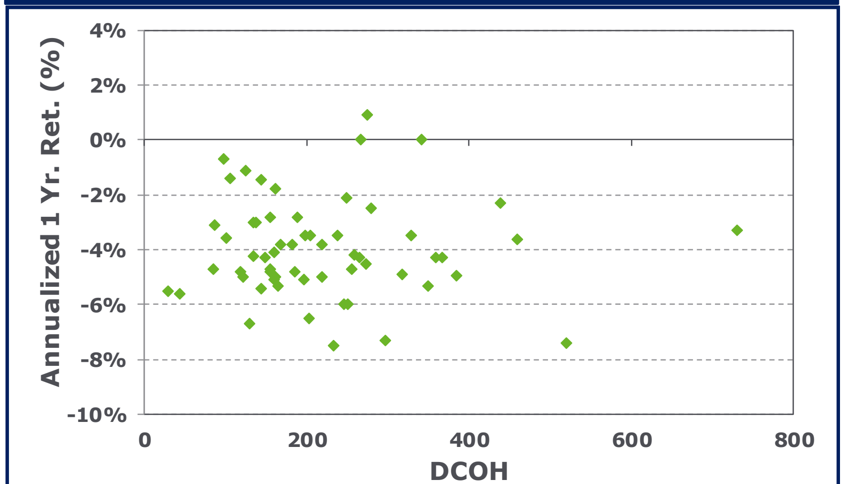
Credit ratings had no material impact on returns



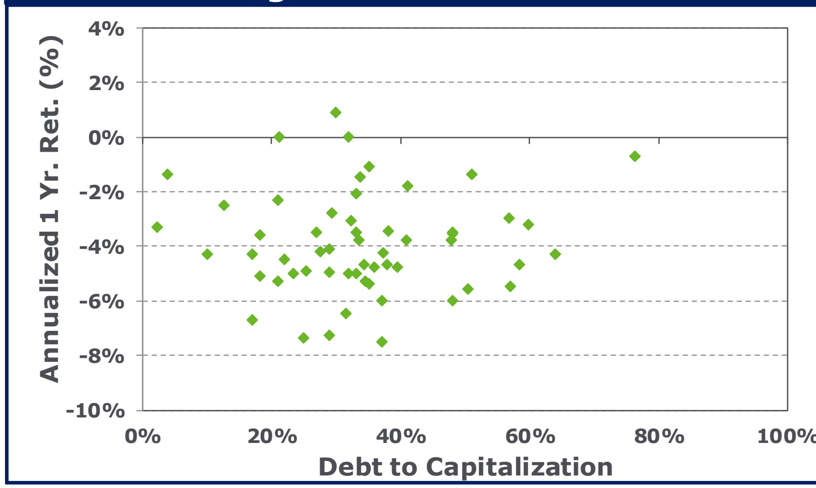
Larger systems appear to have protected more than smaller peers over past year



DCOH had a less defined influence on returns

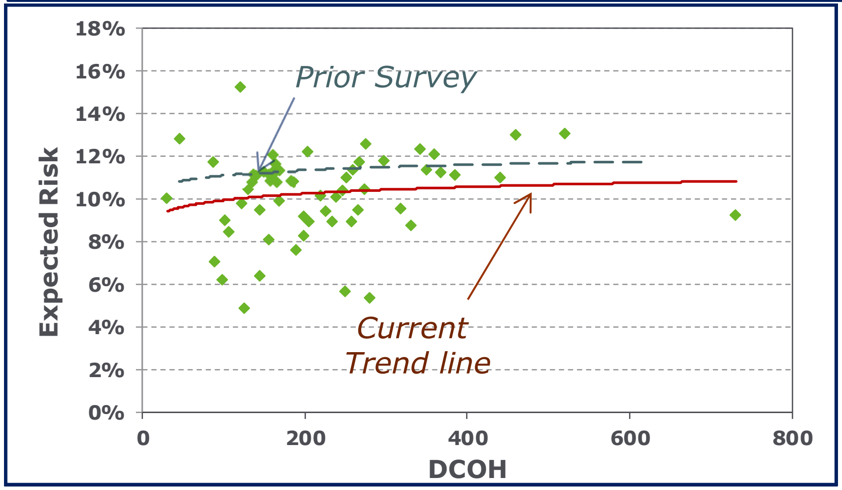


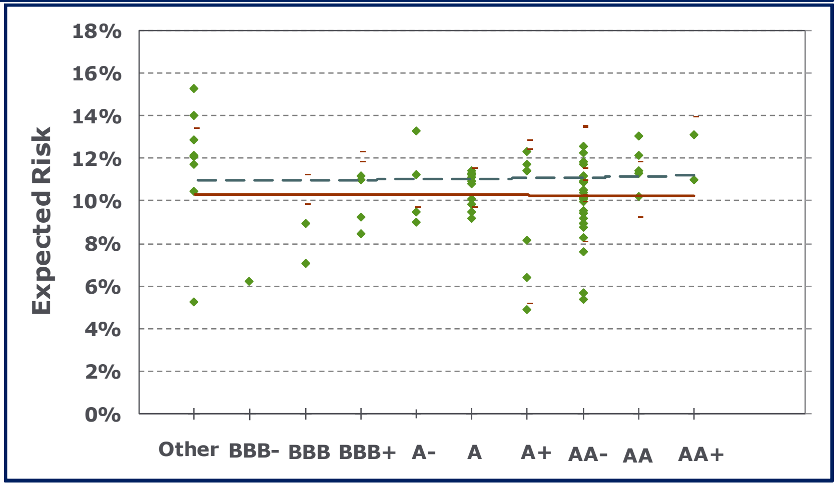
Over the last year Debt to Cap had no meaningful correlation with returns



EXPECTED RISK VS. DCOH AND QUALITY

Participants appear to have reduced their risk exposure over the prior year





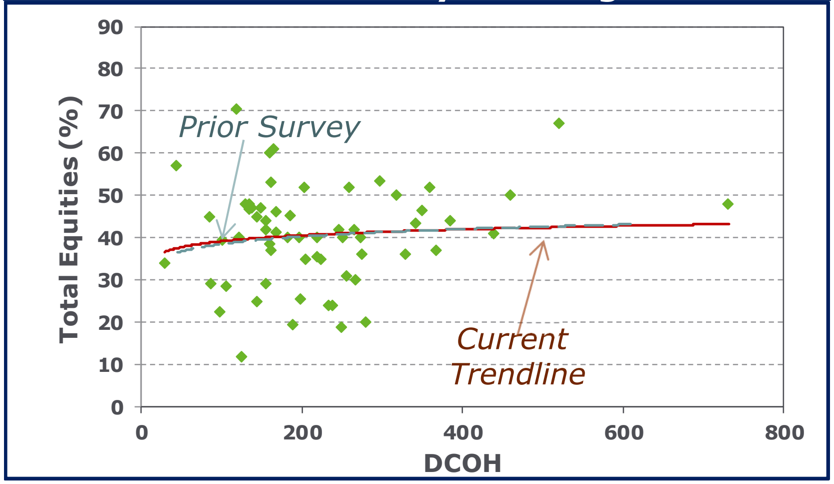
After observing an increased risk profile last year, participants reduced their risk profile following a spike in 2018 volatility.

Observation is consistent across DCOH and ratings.

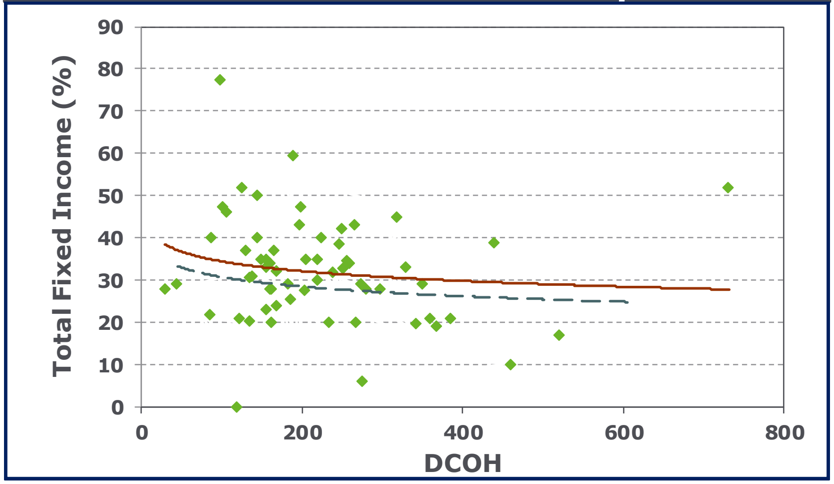
Note: Expected risk estimated using NEPC 2019 & 2018 assumptions

ASSET ALLOCATION vs. DCOH

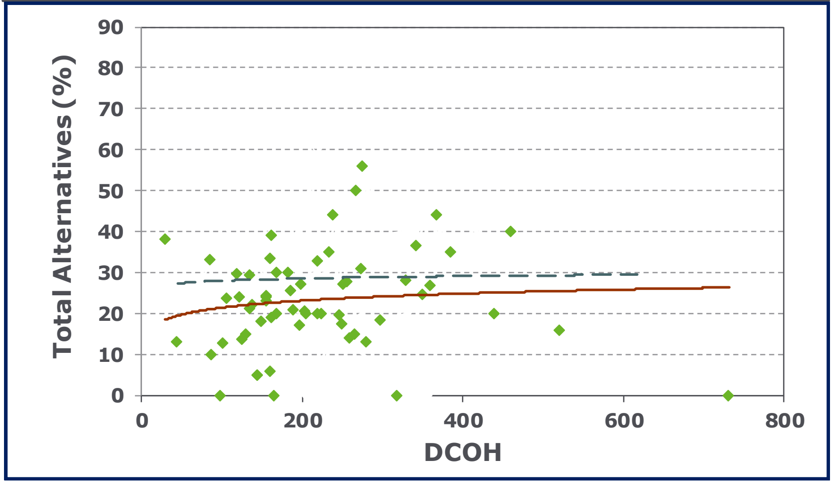
Equities:
Utilization relatively unchanged YoY



Fixed Income:
Lower allocation as DCOH improves



Alternatives:
Allocation declined YoY

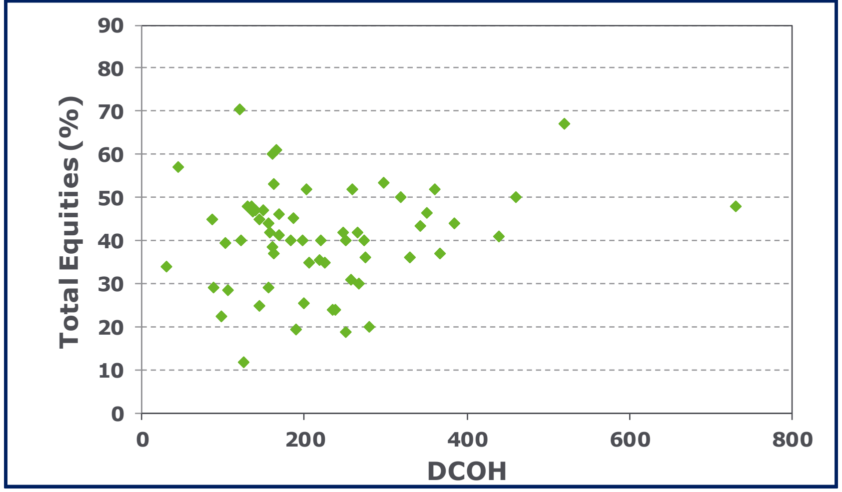


Appears participants increased fixed income exposure at the expense of alternatives

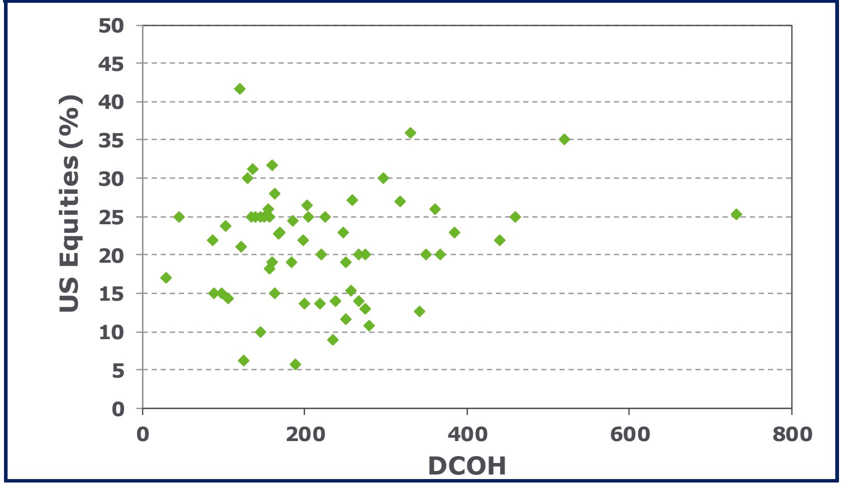
APPENDIX

EQUITIES

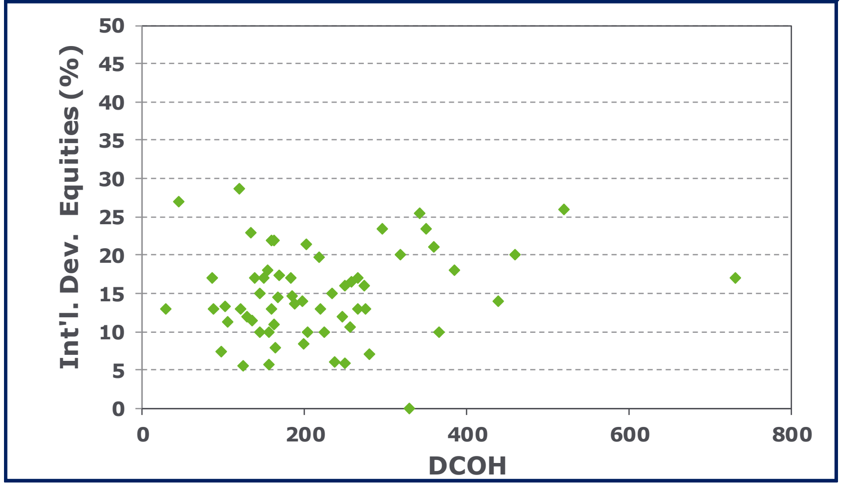
Respondents with high DCOH generally hold sizable equity exposure



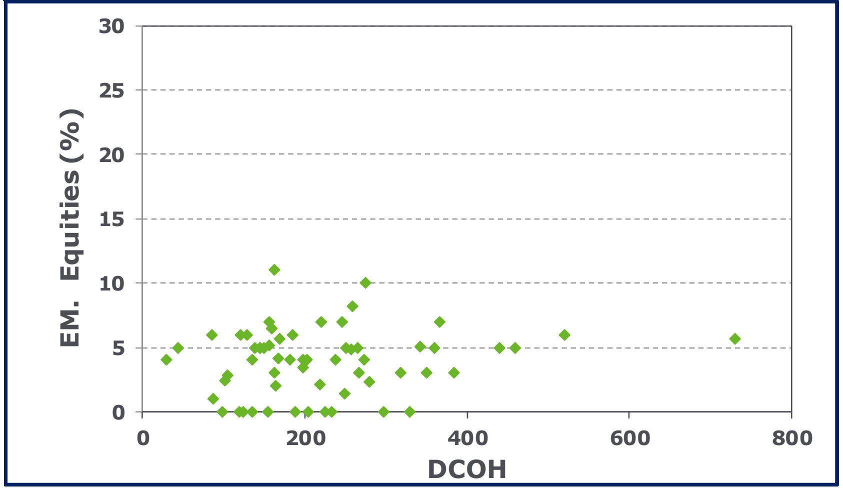
General consensus appears to be no more than 35% allocation to US Equities



Int'l Dev Equity usage appears meaningful, but generally no more than 25%

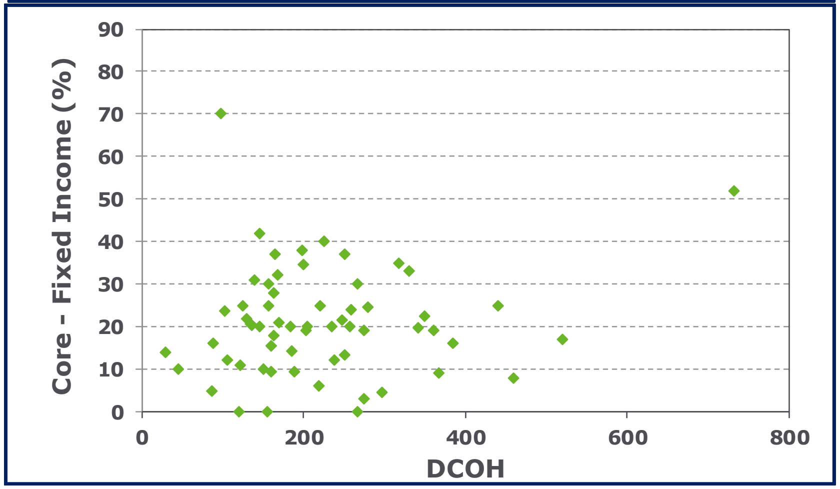


EME usage remains stable, despite lower expectations from the asset class YoY

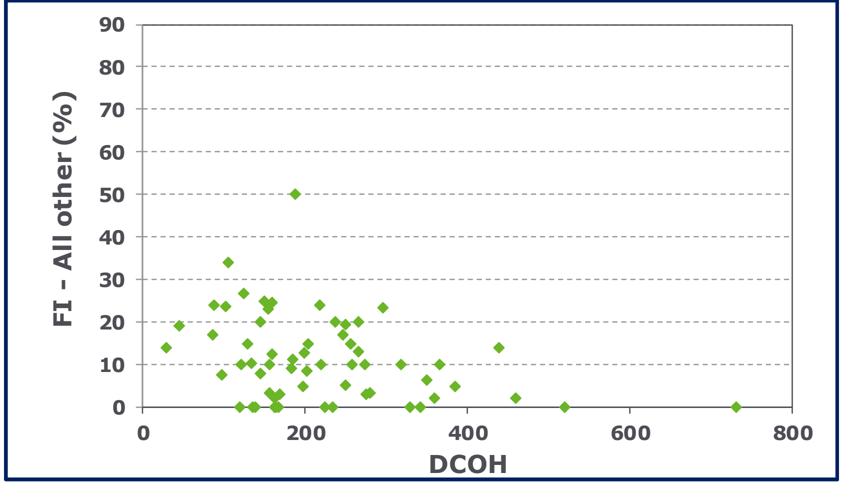


FIXED INCOME

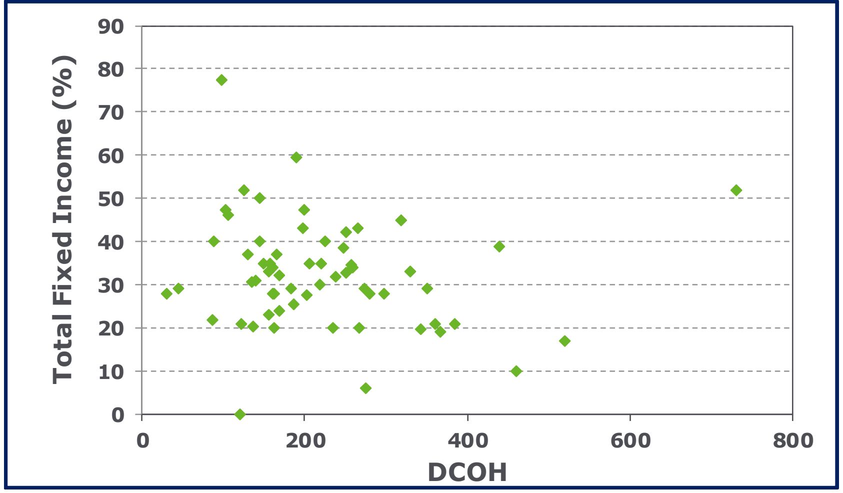
Core Fixed Income remains a building block in most portfolios



In a low rate environment, non-core allocations have a role in portfolios

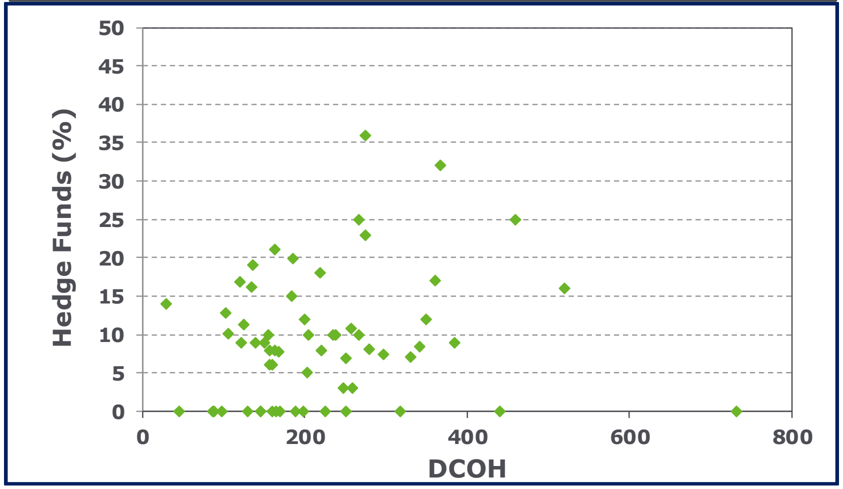


Total Fixed Income exposure declines as DCOH increases

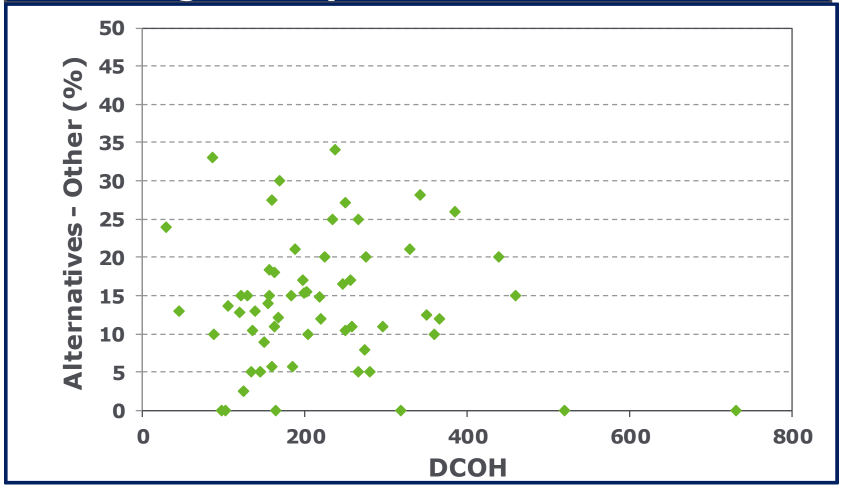


ALTERNATIVE INVESTMENTS

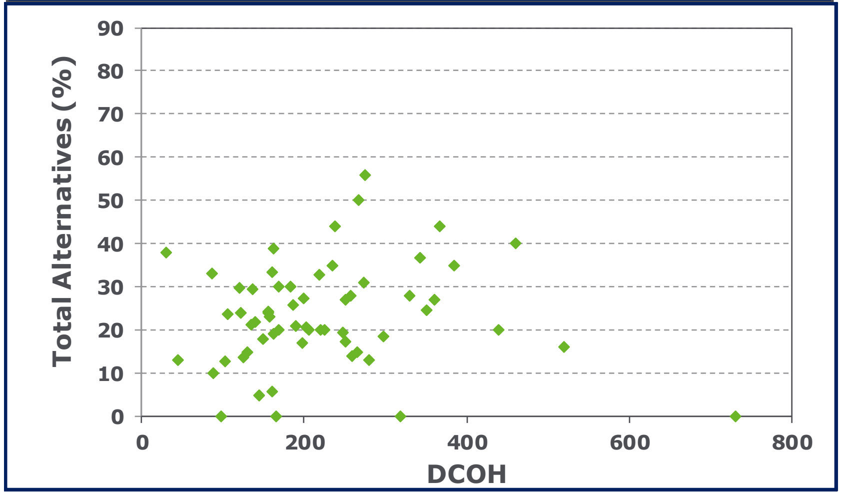
Hedge Fund exposure is diverse but increases with DCOH



Allocation to Other Alternatives varies but generally increases with DCOH



Majority of observations below 40%



ABOUT THE SURVEY

- **NEPC's annual Healthcare Operating Funds Survey gauges healthcare organizations' outlook on the economy and examines how healthcare operating pools are invested.**

- **NEPC's Healthcare Practice Group conducted the online survey during April and May 2019.**

- **68 healthcare organizations participated in this years' survey**
  – Respondents were primarily chief financial officers, treasurers and investment-related staff of healthcare organizations
  – Investment Pool Assets Under Management (AUM) ranged from under $250 million to over $2 billion
  – Median Days Cash on Hand (DCOH) of respondents: 198
  – Median Debt to Capitalization ratio of respondents: 33%

DISCLAIMER

- **Past performance is no guarantee of future results.**

- **Information on this analysis was provided by sources external to NEPC. While NEPC has exercised reasonable professional care in preparing this report, we cannot guarantee the accuracy of all source information contained within.**

- **59 of 68 respondents provided answers to questions on pages 3, 4 and 5**

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