Healthcare Groups In The ObamaCare Era

Invariably, jokes whose punch-lines involve a variation on, "My friend? I thought he was your friend!" work by virtue of their inherent misdirection. We seem to be at that point with the rollout of ObamaCare already as what should have been predictable outcomes from the law's design and embedded economics are being treated as unintended consequences.

I make this statement not with any political axe to grind, but rather by observing the reactions of groups within the healthcare sector; in keeping with the precept markets do not move violently or even reverse significantly when traders were right, the action in at least two of the eight groups within the sector, Services and Managed Care, suggest the markets were surprised. Please note how I say "surprised," rather than "wrong;" it is not the role of a market to forecast so much as to measure existing expectations and relative anxieties.

The October Surprise

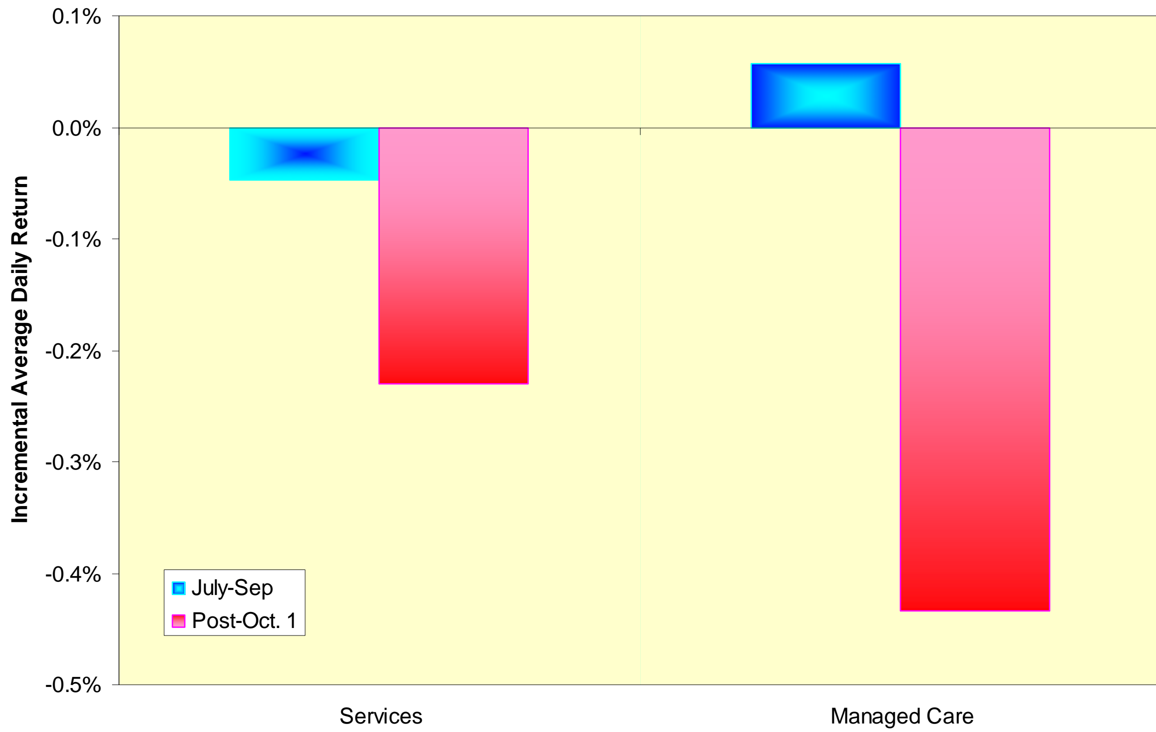
September and October have defied their pattern of being seasonally weak in 2013; the total return on the broad Russell 3000 (accessible as IWV) since the end of August has been 8.54%. If we shift the basis of comparison and the starting point of the analysis to the October 1, 2013 launch of the healthcare.gov Website and compare the returns for the SPDR Healthcare ETF (XLV) to the S&P 500 (SPY), we see the sector has underperformed 3.43% to 4.20%.

This lower absolute performance has been accompanied by higher levels of risk since the Website's launch. The XLV's implied volatility has increased relative to the SPY's and the sector's average five-year credit default swap costs have increased relative to the iBOXX investment-grade CDS index. Restated, the healthcare sector has turned into a higher-risk, lower-return investment since people started paying attention.

Managed Care And Services

The Managed Care group, which includes Aetna (AET), Cigna (CI), Humana (HUM), UnitedHealth (UNH) and WellPoint (WLP) had an October to forget with a return of -3.34%. The Services group, which includes Express Scripts (SRX), DaVita Healthcare (DVA), Laboratory Corp (LH) and Quest Diagnostics (DGX), did not fare much better, gaining a trivial 0.10%.

The performance of these groups relative to the broad market shifted lower from the previous July 2 – September 30, 2013 period; July 2nd is when the administration announced it would not enforce the employer mandate section of the Affordable Care Act. The incremental average daily return for the Services group of -0.05% during the first period fell to -0.23% after October 1st. Comparable numbers for the Managed Care group were 0.06% and -0.43%. Even over a small data sample we can be 73.1% confident the incremental return for Managed Care was significantly lower once the ACA started to come into effect.



A cynic, should one materialize anytime soon, might suggest returns within the healthcare sector will be unstable in both directions as the market has to accommodate to the law. This instability will increase frictional costs and lead to deadweight economic losses. The story is an evolving one and will need to be revisited frequently.