

# Cash Flow and Carey



**Robert Carey, CFA**  
Chief Market Strategist



This chart is for illustrative purposes only and not indicative of any actual investment. The illustration excludes the effects of taxes and brokerage commissions and other expenses incurred when investing. Investors cannot invest directly in an index. The NASDAQ Biotechnology Index is a modified market capitalization-weighted index designed to measure the performance of all NASDAQ stocks in the biotechnology sector. The Standard and Poor's 500 Health Care Index is a capitalization-weighted index focused on health care stocks.

The information presented is not intended to constitute an investment recommendation for, or advice to, any specific person. By providing this information, First Trust is not undertaking to give advice in any fiduciary capacity within the meaning of ERISA, the Internal Revenue Code or any other regulatory framework. Financial advisors are responsible for evaluating investment risks independently and for exercising independent judgment in determining whether investments are appropriate for their clients.

## Just What The Doctor Ordered

### S&P 500 Health Care Index & NASDAQ Biotechnology Index Total Returns

| Index                      | 2021 & 2022 Combined Total Return | 5/31/22 - 12/30/22 Total Return | YTD Total Return |
|----------------------------|-----------------------------------|---------------------------------|------------------|
| S&P 500 Health Care Index  | 23.67%                            | 4.11%                           | -1.87%           |
| NASDAQ Biotechnology Index | -10.08%                           | 14.07%                          | 3.50%            |

Source: Bloomberg. **Past Performance is no guarantee of future results.**  
YTD total returns through 1/31/2023

### View from the Observation Deck

Today's table highlights the total returns for the S&P 500 Health Care Index and the NASDAQ Biotechnology Index over three time periods. As shown in the table, biotechnology stocks underperformed the broader health care index over the combined 2021 and 2022 calendar years by a huge margin. Recently, however, the tables have turned, and the NASDAQ Biotechnology Index has posted significant outperformance relative to the S&P 500 Health Care Index.

#### The cost of bringing novel drugs and therapies to market provoked the ire of politicians.

Bringing a new drug to market costs companies an average of \$2.6 billion and can be a 10 to 15-year commitment, according to Ryan Issakainen, Exchange-Traded Fund Strategist at First Trust Advisors L.P. This tremendous outlay of capital combined with the amount of time required to research and develop new drugs resulted in sky-high drug prices for consumers in 2022. In fact, the median annual price of all novel drugs approved by the U.S. Food and Drug Administration stood at \$222,003 in 2022, according to Reuters. As sky-high prices drew the attention of politicians, concerns about the possibility of increased regulation led to lower equity prices. For the combined 2021 and 2022 calendar years, the NASDAQ Biotechnology Index posted a total return of -10.08% as compared to the S&P 500 Health Care Index which came in at 23.67%.

#### A potentially looser regulatory environment has been a catalyst for biotech companies.

Beginning in the second-half of 2022, the NASDAQ Biotechnology Index experienced new life, reversing course and notching a 9.96 percentage point lead over the S&P 500 Health Care Index through the end of the year. Biotechnology's outperformance has continued through the first month of 2023, with the NASDAQ Biotechnology Index outperforming the S&P Health Care Index by 5.37 percentage points year-to-date. Notably, the turnaround for biotechnology stocks occurred in the second half of 2022, along with the mid-term elections. In our view, expectations of a looser regulatory environment were a considerable catalyst for this reversal.

### Takeaway

Pressured by the possibility of increased regulation and tighter price controls, biotechnology stocks underperformed the broader health care index over the combined 2021 and 2022 calendar years. Once the mid-term elections were in the rearview mirror and the impact of the Inflation Reduction Act was better understood, the NASDAQ Biotechnology Index surged, outpacing the S&P 500 Health Care Index in the second-half of 2022 and year-to-date in 2023. Should the regulatory environment remain stable, it is our opinion that biotechnology stocks may represent a unique, long-term opportunity for investors.