PLANET PAPERS

A responsible recovery

Can the world make positive social and environmental choices when rebuilding our economy from the coronavirus pandemic?

Rathbones
Look forward

What would you do for our planet?

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A responsible recovery

This year of pandemic marks the start of the decade in which the UN's Sustainable Development Goals (SDGs) will be met or missed. On the face of it, we couldn't have asked for a worse start. Stewardship director Matt Crossman makes the case that we can and should 'build back better'.

The impact of COVID-19 exhausts superlatives. At the height of the crisis, seemingly every news report started with some combination of "never before", "not since" or "in living memory". As self-isolation met social distancing, schools closed and working from home became the new normal for most in a desk job. Meanwhile, those in more vulnerable jobs faced the twin threat of a global health crisis and an uncertain financial future.

Once the scale of the crisis became clear, the response was swift and powerful. Any talk of fiscal discipline was banished at once, as the UK government promised, in bizarre capital letters, to do "WHATEVER IT TAKES". French President Emmanuel Macron promised that no French firm would collapse, and governments and central banks across the developed world launched support packages worth trillions of dollars.

Meanwhile, the problems that grabbed the world's attention in 2019 – climate change in particular – are not going away. The nagging need for systemic reform of the global economy stays constant. Indeed, the pandemic only highlights the weaknesses of the current system. But it could also be a catalyst for accelerating the move towards a more responsible capitalism, and an opportunity to direct stimulus towards building a more sustainable economy. (You can read why Rathbones believes every long-term investor should care in our research report *Responsible capitalism*.)

Responsible recession

Despite stumbling out of the blocks owing to this unforeseen event, as a society we must remember the race to achieve the SDGs is a marathon not a sprint. If we are to build a more resilient economy with our stimulus, the steps we take to get the world moving in response to the short-term shock of COVID-19 must be done in alignment with the long-term necessity of meeting the SDGs.[1]

Global crises such as the COVID-19 pandemic have a peculiar feature – they are nobody's fault. The 2008 financial crisis created clear villains in the form of those creating speculative financial instruments; 'greedy bankers' were everyone's enemy. Bailouts of banks

[1] For more information on the Sustainable Development Goals see this article from Rathbone Greenbank, our specialist ethical, sustainable and impact investing team.

were necessary, but met with a public outcry. With a global pandemic, while you can argue about which government responded 'best', we can agree that we all face a common threat. Political divisions about who benefits most from the coming financial stimulus, and whether such moves are 'fair', are diminished. This is an opportunity of historic proportions – at the moment when society needs it most.

Though the 2008 crisis was of a very different nature, it does have lessons for how we respond to our current crisis.

Back in 2008, I was a 20-something postgrad student in voluntary isolation, holed up with my parents while I finished my studies. The key difference between my predicament back then and the one faced by today's students is that I was on leave from a fully fledged career, with a job to return to... or so I thought. The day before my final exam, Lehman Brothers collapsed. I'd focused on ethical and sustainable investing; would I have a career to go back to?

Back then, the knives were out for nascent Environmental Social and Governance funds, and the well-worn argument for investing in traditional, defensive stocks still echoes today: 'invest in stocks that have steady demand'. That means alcohol, tobacco and arms companies, whose demand doesn't tend to be affected by the vagaries of the market. For the income seeking investor, it's a case of 'any port in a storm' – or any dividend in a pandemic. Then as now, 'values' are seemingly in conflict with seeking value; can we afford to push responsible capitalism in the current environment?

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It won't come as a surprise to learn that we think we can and should. Rathbones has been a signatory to the UN-sponsored Principles for Responsible Investment for over a decade.[2] Today we see the need to practise responsible capitalism as greater than ever.

Sustainable stimulus

How much of a shock was COVID-19? It's clear to us that a more responsible form of capitalism could have helped prevent the worst impacts of the pandemic. The warning signs about the vulnerability of our globalised world were there for everyone to see. Bill Gates, one of history's greatest capitalists, was sounding the alarm back in 2015:

[2] Our involvement in the UN PRI was spearheaded by the team at Rathbone Greenbank Investments, who have been part of Rathbones for over 20 years.

Past performance is not a reliable indicator of future performance.

"If anything kills over 10 million people in the next few decades, it's most likely to be a highly infectious virus rather than a war. Not missiles, but microbes... we're not ready for the next epidemic."

He went further, noting that we had all we needed to be better prepared – the technology, the building blocks of a response system – but not the will to spend a little to save millions of lives. A similar thing could be said of investment in antibiotics, the bedrock of the global healthcare system, where investment has slowed to a historically low rate and been largely abandoned by big pharmaceutical companies. But the response to COVID-19 has shown us that capitalism has enormous power for good when it comes to finding solutions to urgent medical needs, and that gives us hope for the future of antibiotics too, which we explore in the next section 'A healthy recovery'.

A 'sustainable stimulus' isn't a new concept. There was talk and then delivery of a green stimulus in the wake of the 2008 financial crisis as key players like the US and China focused recovery efforts on cleantech and renewables. Writing at the time, HSBC estimated that governments around the world "allocated more than $430 billion in fiscal stimulus to key climate change investment themes." The following decade saw two major and significant developments: the drastic fall in the cost of solar power, and the collapse in investor confidence in coal. Correlation is not causation, but it's fair to assert that such targeted stimulus had the double benefit of getting the economy moving and delivering on global goals.

Now it's a question of converting plans into action. Leading economists, including Nicholas Stern and Joseph

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Stiglitz, have made the case for fiscal recovery packages that meet both economic and climate goals, such as investment in clean physical infrastructure, retrofitting buildings for greater energy efficiency and natural resources. To this end, Rathbones has recently signed an investor letter, coordinated by the UK Business Group Alliance for Net Zero and the Institutional Investors Group on Climate Change, calling on the UK government to ensure that the economic recovery plans support a sustainable, inclusive and resilient UK economy, aligned with the UK's target of net zero emissions by 2050.[3]

Our hope is that rather than be a hindrance to investing in a sustainable future, the pandemic will prove to be a catalyst. As Vladimir Lenin wrote, "There are decades where nothing happens; and there are weeks where decades happen."

A rapid acceleration in some positive changes, such as the move to more flexible working, is one silver lining in the dark economic cloud that COVID-19 has cast over the world. Global governments have a window of opportunity to shape a decade of recovery that will address the yawning gap in wealth inequality, improve health and education and tackle climate change.

Our actions now will affect the decade before us – could a truly sustainable economy rise from the ashes of COVID-19?

[3] Rathbone Global Sustainability Annual Review 2020, COVID-19: *An opportunity to build back better?*

Now it's a question of converting plans into action.

Our actions now will affect the decade before us

A healthy recovery

As we noted in our 2019 report *Responsible capitalism*, long-term profits depend on a healthy, well-paid, socially mobile workforce. But capitalism doesn't always allocate capital to the most useful areas. And one area where this mismatch is in need of a more responsible capitalism is the global healthcare system.

Imagine you're a business owner and you're presented with an enormous gap in your market that needs filling and there's a dearth of competition. Sounds good so far. But what if, by their very nature, the products that would fill that gap are not only unprofitable to begin with, but become less valuable the more people use them? What would you do? Probably move on to something else.

This, in a nutshell, is the issue facing the pharmaceutical industry, which the world depends on to provide a bedrock of the modern healthcare system – antibiotics. COVID-19 is a fast moving pandemic – antimicrobial resistance (AMR) a slow-burning and insidious one.

It would be hard to exaggerate the success of antibiotics in saving lives and their importance to the functioning of the global economy. In the pre-antibiotic age, the simplest of bacterial infections could prove fatal, rendering everything from surgical procedures to childbirth potentially life threatening.

Widespread overuse has enabled infectious bacteria to evolve and strengthen their resistance to antibiotics. Consequently, AMR is now recognised as one of the most significant threats to public health. If a product becomes less effective the more it's used, that's not good for business; the financial and societal rewards seem to be at odds. Not surprisingly, investment in new antibiotics has slowed to the lowest rate in history, and big pharmaceutical companies have largely abandoned the field.

It's estimated that about 70,000 people die a year from infections that are resistant to antibiotics, and that number is forecast to grow to 10 million a year by 2050 if the current trend of growth in resistance continues, dwarfing the death rate of COVID-19. This is one of today's urgent challenges, and a healthy, functioning responsible capitalism is needed to address it.

It's an exciting time to be in biotechnology and advanced pharmaceuticals. The convergence of big data and artificial intelligence along with huge advances in the field of genetics has created a vastly promising new frontier for both industries. But neither industry seems aware that the very basis on which its business model is built is under severe pressure. The modern healthcare system is built on the ability to control infection, and our tools in that fight – antibiotics – had entered into their own crisis even before COVID-19 hit.

Capitalism as a force for good

History abounds with examples of capitalism facilitating great investment in energy, technology and vital infrastructure, and in laying the groundwork for social mobility. But we know capitalism, when it's narrowly focused on delivering returns for shareholders, does not always allocate capital to the most useful areas. This is known in economic shorthand as a 'market failure' – an area where the true cost or value of an asset isn't priced in. Antibiotics are a classic case.

At a basic, surface level it makes sense for pharmaceutical companies to move away from producing new antibiotics. We've become so dependent on antibiotics, and we expect them to be cheap. Their true worth is not reflected in their price. All investment choices carry an opportunity cost, and there

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are many more lucrative options. To invest money in the development of a lifestyle drug could see five to 10 years of market dominance with little risk once brought to market – compare that with the low margins and diminishing effectiveness of antibiotics and the decision on where to spend your research dollars is a no brainer.

The industry is aware of the problem, but investors have not yet grasped the full implications. According to a 2016 report by former Goldman Sachs Chief Economist Lord Jim O'Neill, if 10 million people were to die every year as a result of AMR by 2050 as predicted, that would shave 2 to 3.5 percentage points from annual global GDP growth, potentially wiping it out if we assume a long-term trend rate of 3.5%.

While no individual company can shoulder the full blame, the failing at a sectoral level must be addressed. And it's not just a problem for the pharmaceutical industry. It's a massive risk for any company that builds its business on the modern healthcare system, and for society at large. Almost everything that happens in a modern hospital or clinic relies on antibiotics to make it safe. Where once Caesarean sections were a last resort, they are now elective for many women – enabled by widely available antibiotics to combat the risk of infection.

An ageing population is seeing more and more joint replacements – any and every such surgical intervention requires antibiotics to combat the ever-present risk of infection. It doesn't matter how good your new hip joint is – how excellent the materials, whether it was modelled on your specific physiology and delivered through 3D printing, or how personalised it is to your DNA. If you run the risk of dying of infection, contracting one of the growing number of superbugs, then what value is the medical technology?

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The same can be said about the excitement bubbling up in oncology, where immunotherapy – which works by influencing the body's immune system – is being heralded as the 'magic bullet' in the fight against cancer. No matter how much more effective the emerging class of cancer treatments, their use depends on a healthcare system that can protect vulnerable patients from infection.

"Antimicrobial resistance will take us back to a time when people feared common infections and risked their lives from minor surgery," said the head of the UN's World Health Organisation when he launched World Antibiotic Awareness Week in November 2017. "[It is] a global crisis that we cannot ignore."

What gives us hope?

Given that the maths doesn't work for antibiotics like it does for other pharmaceutical products, how can this obstacle be overcome and pharmaceutical companies be incentivised to produce them?

In response to this crisis, the AMR Industry Alliance was formed in 2016, made up of over 100 pharmaceutical and biotech companies and associations across 20 countries. It has since invested a combined $2 billion in AMR research and development (R&D). In 2018, the non-profit Access to Medicine Foundation launched an AMR Benchmark, tracking progress among the most active companies in this area.[4]

Governments have a big role to play. There are two basic approaches, known as 'push' and 'pull' incentives. So far incentives have generally involved public-private partnerships making grants to small companies for early stage R&D. These grants have been enough to help companies successfully develop new antibiotics, but not enough to get them from there to profitability. That's where pull incentives come in. As the name suggests, rather than pay upfront R&D costs, they reward success with larger doses of cash.

In particular, pull incentives were the brainchild of the British government's multi-year Review on Antimicrobial Resistance, which was headed by Lord O'Neill and completed in 2016. The review proposed giving a one-time "market entry reward" of $1 billion for new antibiotics, enough to cover

[4] Rathbone Greenbank is involved with the AMR Benchmark through its membership of the Access to Medicine Foundation's index (ATMI), which ranks major pharmaceutical companies on their efforts to make medicine available to poorer countries.

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typical R&D costs and enable the antibiotic to be profitable without encouraging over use.

In June this year the NHS announced an incentive scheme for pharmaceutical companies to provide new antibiotics to UK patients for the first time in decades. This first-of-its-kind subscription model, part of a UK action plan to contain and control AMR by 2040, pays providers upfront based on the value of their antibiotics to the public health system, rather than the amount used.

Another encouraging development stemming from such efforts has been the recently announced creation by leading pharmaceutical companies of the AMR Action Fund. The fund aims to start operating this year, with the goal of delivering two to four new antibiotics by 2030 through investing more than $1 billion in small biotech firms.

Government incentives, which will cost huge sums of money and deliver profits to the pharmaceutical industry, may be a politically unpalatable medicine. But they may prove to be an effective way of fixing this crisis, and a great example of responsible capitalism in action – an opportunity for investors to do well by doing some good.

How will the global economy heal from the health crisis?

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