

EUROPE EQUITIES

HEALTHCARE: AN EASY PILL TO SWALLOW?



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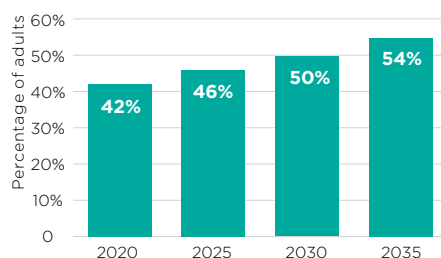
Around the world, people are living longer. The World Health Organization (WHO) estimates that 1 in 6 people will be aged 60 years or older by 2030. As societies age, the demand for healthcare services is likely to grow. That's why we view medical devices, pharmaceutical products and healthcare technology as promising long-term investment opportunities.

THE GLOBAL CHALLENGE OF AGEING AND OBESITY

Global life expectancies have improved significantly in recent years. Better access to health care, education and food, as well as declining child and maternal mortality rates, have increased lifespans around the world. Between 2000 and 2019, the WHO reported that global life expectancy had increased by more than six years – from 66.8 to 73.1.¹ With people living extended lives, the prevalence of chronic conditions and diseases associated with older age, such as hearing loss, dementia and diabetes, are likely to rise in the coming years.² Technological advancements and scientific progress have improved patient outcomes by enabling better diagnosis, prevention and treatment.

Although longevity is improving, another global health challenge is surfacing. Obesity rates around the world have been escalating. Long considered to be a problem faced by high-income economies, about 70% of the world's obese people live in low- and middle-income countries as of 2020.³ Processed foods, reduced exercise and rising incomes, for

Figure 1. Percentage of adults aged 20 and older considered overweight



Source: Statista, 2024.

¹ Source: WHO <https://www.who.int/data/gho/data/themes/mortality-and-global-health-estimates/ghe-life-expectancy-and-healthy-life-expectancy>

² Source: WHO <https://www.who.int/news-room/fact-sheets/detail/ageing-and-health>

³ Source: World Bank Group <https://www.worldbank.org/en/news/press-release/2020/02/05/obesity-related-diseases-among-top-three-killers-in-most-countries-world-bank-says>

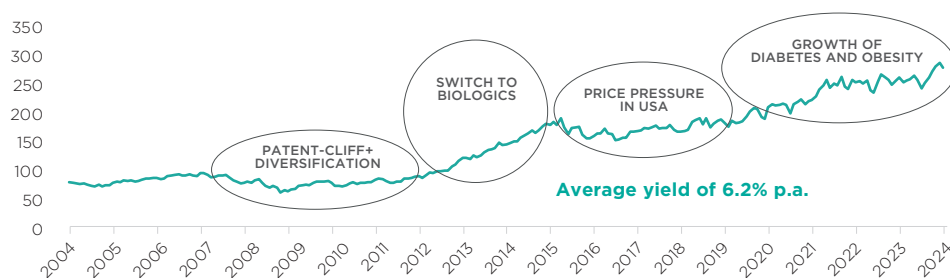
instance, have led to higher consumption rates of unhealthy foods.⁴ The American Medical Association estimates that there are around 200 obesity-related diseases, including diabetes and high blood pressure.⁵ By 2035, more than half of the world's population is expected to be affected by excessive weight levels.⁶

Longer lives and growing obesity rates are driving up health costs worldwide. In the United States, health care spending grew by 4.1% in 2022 to \$4.5 trillion, or \$13,493 per person.⁷ Health care spending currently amounts to 17.3% of the country's GDP – three times more than the 5% GDP budgeted in 1960.⁸ The picture is similar in other countries, too. In 2022, member countries of the Organisation for Economic Co-operation and Development (OECD) spent on average 9.2% of their GDP on healthcare, up from the 2013-2019 average of 8.8%.⁹

DIAGNOSING THE HEALTHCARE SECTOR: A FOCUS ON QUALITY

From an investor's perspective, the healthcare sector has long defied economic cycles because its products are considered as a vital necessity for people everywhere. In our view, ageing populations and rising obesity levels are likely to serve as long-term growth drivers for research and development (R&D) and innovation. Rising costs for healthcare systems will also likely encourage the creation of more efficient products and services.¹⁰ Given the essential nature of healthcare products and services, we believe it's unlikely that macroeconomic developments (such as interest rates, wars, pandemics) could steer these long-term growth drivers off their current course.

Figure 2. Performance of the MSCI World Index pharmaceutical sector since 2004



Past performance is not indicative of future returns. Source: Comgest / Factset. Performance expressed in EUR; as at 30-Apr-2024.

⁴ International Fund for Agricultural Development. "Addressing Overweight and Obesity in LMICs in Rural Development and Food Systems: A Country Mapping." International Fund for Agricultural Development, June 2023.

⁵ "Obesity." American Medical Association. Accessed 28-Nov-2024.

⁶ World Obesity Federation. "Economic Impact of Overweight and Obesity to Surpass \$4 Trillion by 2035." World Obesity Federation, 2-Mar-2023.

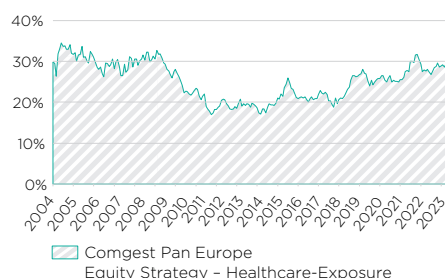
⁷ Source: National Health Expenditure Accounts (NHEA), 2024

⁸ Source: Organisation for Economic Co-operation and Development, 2024

⁹ OECD. "Health at a Glance 2023." OECD iLibrary, 7-Nov-2023.

¹⁰ World Economic Forum. "How Digital Healthcare Tools Cut Costs and Boost Outcomes." World Economic Forum, 4-Jan-2024.

Figure 3. Comgest Pan Europe Equity Strategy Exposure to Healthcare Sector



Source: Comgest / Factset, 30-Apr-2024.

The healthcare sector is vast and varied, encompassing everything from hearing aids to weight loss drugs and care facilities to ultrasound machines. Based on our experience, Comgest’s investment approach enables us to scan this universe of opportunities and uncover what we consider quality growth companies with durable competitive advantages. Our Comgest Pan Europe Equity Strategy has consisted of around 20%–35% healthcare companies over the past two decades (as shown in figure 3).

At Comgest, we are not thematic or sector investors. When you visit our website, you will not find an “anti-obesity fund” as part of our portfolio of products, nor will you see sector-specific job titles, like “Portfolio Manager – Healthcare”. That’s because we are generalist stock-pickers that look for company-specific drivers of growth and enduring competitive advantages – regardless of sector. In our view, this “generalist” approach ensures that our investment opportunities are diversified and that we are not blinded by one growth trend or sector at the cost of another.

Our investment approach places an emphasis on quality – not on predicting clinical trial results. In the healthcare sector, we are wary of business models that promise the next miracle drug. Pharmaceutical drug pipeline forecasts are difficult and news is quickly reflected in share prices. This makes investing in pharmaceutical manufacturers, the largest part of the healthcare sector, highly complex. In recent years, pharmaceutical companies have faced several market phases of underperformance, with an annual average return of around 6% over the past two decades.¹¹

We are aware of the fundamental challenges facing pharmaceutical companies, from price regulations to the capital-intensive nature of research and development (R&D). The timeline for developing a new drug can take years, sometimes even decades.

Pharmaceutical products undergo various preclinical and clinical test phases over several years. Of the countless products in an R&D pipeline, only a select few eventually receive authorisation for market use. Sometimes patents expire or price controls are put into place by government policymakers, as has been the case in the European Union¹² and, more recently, the United States.¹³ Investors are highly reactive to R&D developments as successes and failures are also quickly reflected in a company’s share price.

Based on our experience, R&D spending is an essential competitive advantage for a healthcare company’s long-term success, but it’s not the only one. We seek pharmaceutical companies with deep competitive moats, built on innovation and culture, to drive sustainable growth.

¹¹ Source: MSCI World Pharmaceuticals Biotechnology & Life Sciences Index, as of 30-Apr-2024

¹² Council of Europe. “[Council Directive 89/105/EEC of 21 December 1988 relating to the transparency of measures regulating the prices of medicinal products for human use and their inclusion in the scope of national health insurance systems.](#)” Council of Europe, 21-Dec-1998.

¹³ The White House. “[Fact Sheet: Biden-Harris Administration Announces New, Lower Prices for First Ten Drugs Selected for Medicare Price Negotiation to Lower Costs for Millions of Americans.](#)” The White House, 15-Aug-2024.

As bottom-up stock pickers, we believe that companies with these distinctive strengths – regardless of their sector – have the potential to achieve continuous growth over time. Rather than getting bogged down in predicting pharmaceutical trials, we stick to our time-tested investment approach of identifying high-quality companies.

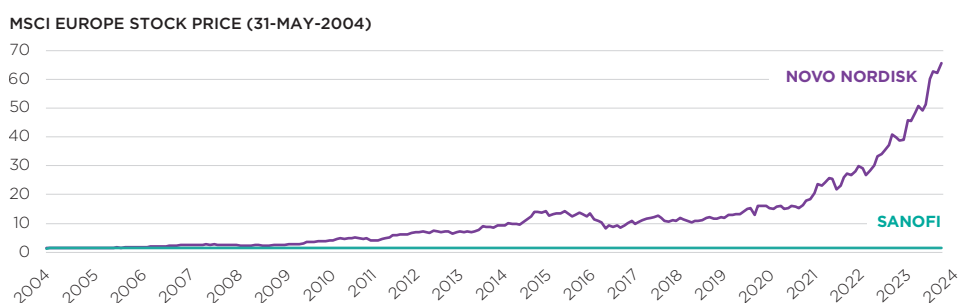
FOCUS. FOCUS. FOCUS.



Consider Danish pharmaceutical company **Novo Nordisk**. Since its founding over 100 years ago, the company has maintained a razor-edge focus on combatting diabetes. We believe that Novo Nordisk's specialisation in just a few product areas, including diabetes and haemophilia, has enabled it to increase production efficiency, realise R&D returns and strengthen its marketing strategies. The company's R&D spending has made it difficult for competitors to gain a foothold in the diabetes market.¹⁴ In 2023, research and development costs represented 14% of net sales – compared to 13.6% in 2022 and 12.6% in 2021.¹⁵ The company's accelerating R&D spending will likely further strengthen its already wide competitive moat in the coming years.

R&D spending has been a crucial part of Novo Nordisk's growth story. In the past decade, the company overtook French rival Sanofi to become the leader in the diabetes treatment market by introducing a new treatment known as glucagon-like peptide-1 (GLP-1). As a result, Novo Nordisk's share price has increased 70-fold over the past two decades, while Sanofi's has largely stagnated (see figure 4).

Figure 4: Diabetes Treatment – The Story of Two Pharmaceutical Companies



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Novo Nordisk's initial investment in GLP-1 paid off in more ways than one: it has also proven to be an effective anti-obesity drug.¹⁶ When GLP-1 was first introduced, investors and the scientific community were unaware of its effectiveness in countering obesity. Now marketed under

¹⁴ Johnston, Ian. "Novo Nordisk Chief Seeks More Deals to Cement Weight-Loss Lead amid 'Hype.'" *Financial Times*, 8-Mar-2024.

¹⁵ Source: *Novo Nordisk Annual Report 2023*

¹⁶ Johnston, Ian. "Novo Nordisk Readies Trial Results for Next-Generation Weight-Loss Drug." *Financial Times*, 17-Nov-2024.

the name Wegovy, the drug is a leader in the growing obesity market alongside Eli Lilly's Zepbound.¹⁷ In our view, companies that share Novo Nordisk's fundamentals – namely a strong reinvestment rate, healthy balance sheet, longevity and visible track record of growth – are better positioned to innovate and deliver long-term returns.

BEYOND THE BENCHMARK

By operating independently of a benchmark, we believe that Comgest is well placed to invest in areas of the healthcare sector beyond pharmaceuticals. For example, our Pan Europe portfolio includes biopharmaceutical manufacturing suppliers, such as **Sartorius Stedim**, a German laboratory equipment supplier and **Icon**, an Irish healthcare company. These companies supply equipment and render services required for biopharmaceutical R&D and production, including microbial tests and technology solutions.

Our Pan Europe portfolio also features medical device retailers, such as the Italian hearing aid company **Amplifon** and the Swiss dental implant manufacturer **Straumann Group**. These companies are likely to benefit from the growth trends linked to an ageing population, as people will likely need hearing and dental solutions as they age. In our view, longer lifespans will create more demand for health care products and services as people seek to maintain health and vitality throughout their lives.

All of these businesses possess significant competitive advantages and prioritise end-user markets. From diabetes to myopia and dentures to gastrointestinal issues, Comgest invests in a wide variety of healthcare companies that target specific markets with bespoke and diversified growth models. By sticking to our quality growth approach, we can diversify our research and investments across various medical sectors, thereby minimising R&D pipeline risks associated with large pharmaceutical manufacturers that dominate the sector.

STOCKPICKING WITH A TAILWIND OF SCALE AND LONGEVITY

At Comgest, we are less concerned with sectors or themes when it comes to investing. For nearly 40 years, we have concentrated on quality growth stock picking. We are firmly convinced that active investors can identify attractively valued healthcare companies by focusing on company fundamentals and durable competitive advantages. Our Comgest Pan Europe Equity strategy benefits from long-term growth drivers such as an ageing population and the rising demand for weight loss solutions. By applying our bottom-up, quality growth investment approach, we aim to identify healthcare businesses that can weather policy shifts and macroeconomic disruptions, while delivering consistent, long-term returns that compound to benefit our clients.

¹⁷ Nelson, Eshe, and Charlotte De La Fuente. ["It Introduced Ozempic to the World. Now It Must Remake Itself."](#) *The New York Times*, 20-Apr-2024.

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Wolfgang Fickus joined Comgest in September 2012 and is a Product Specialist as well as an Investor Relations Manager. Wolfgang began his career in 1995 at Paribas Asset Management Paris as a European-equity fund manager. In 2000, he moved to WestLB where he worked as an analyst for European technology stocks before becoming the Head of Mid- and Small Cap Research in 2005. Wolfgang Fickus is a graduate of the University of Cologne (Germany) with a degree in business administration (Diplom-Kaufmann) and studied at the London Business School. He also holds a CEMS Master's in international management and is a CFA® charterholder.

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