

# GLP-1: The Weight of Speculation

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Obesity is one of the most prevalent health crises, with almost a quarter of the global population expected to be classified as obese by 2035, up from 14% in 2020.<sup>1</sup> Beyond the mental and physical impacts that obesity poses to the individual, it has far-reaching implications for the global economy: the negative macroeconomic impact is estimated to be 3.6% of U.S. gross domestic product with a potential \$1.24 trillion in indirect costs from lost productivity.<sup>2</sup>

GLP-1 (glucagon-like peptide 1) drugs have been heralded as game changers in tackling obesity, with certain drug manufacturers building out capacity following recent U.S. Food and Drug Administration (FDA) approvals.<sup>3</sup>

GLP-1 is a natural hormone released to the gut and brain in response to food, helping to regulate blood sugar by stimulating insulin-producing cells in the pancreas when blood sugar levels get too high. GLP-1 analogues have been around since 2010, largely as a treatment for Type 2 diabetes. What's new? Previously, when injected, GLP-1 did not last long enough to reach the pancreas. The new drugs on the market have managed to solve this problem. This is a significant leap forwards in tackling obesity; studies show that they can reduce body weight by 10% to 20%, may reduce consumption volume by up to 50%, and may cause patients to avoid more processed foods and snacks when taking GLP-1. Beyond this, patients have anecdotally reported a reduction in consumption of alcohol, drugs and tobacco, as GLP-1 drugs can weaken the brain's association between stimulus and feelings associated with pleasure.

<sup>1</sup> Source: Redburn Atlantic and World Obesity Atlas 2023.

<sup>2</sup> Source: Morgan Stanley Thoughts on the Market podcast, "Anti-Obesity Meds Could Bite Into Food Sales", 30 November 2023.

<sup>3</sup> Source: Eli Lilly "FDA Approves Lilly's Zepbound™ (tirzepatide) for Chronic Weight Management, a Powerful New Option for the Treatment of Obesity or Overweight with Weight-Related Medical Problems" press release, 8 November 2023.



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This has led to interesting reading on the potential impact of widespread use of this medication across multiple industries, e.g., airlines saving on fuel given lighter passengers.<sup>4</sup> The market has recently rewarded the GLP-1 drug manufacturers as immediate beneficiaries and medtech and U.S. food and beverage stocks as losers. As long-term investors conducting bottom-up, in-depth research, we believe that the medium- to long-term impact on our portfolios is minimal, but that is not to understate the broader effect. Today less than 1% of the U.S. population is on GLP-1 drugs for weight loss, while approximately 30% of the U.S. population is clinically obese. In the interest of keeping things simple, we hypothesise that approximately 10% of the U.S. population may be on the drug come 2034.

## Consumer Staples

Some analysts estimate that GLP-1 drugs could reduce calorie intake by 15% to 20%. Extrapolating this figure and projecting that 25 million to 50 million Americans may be taking the drug by 2030 could see the nation's calorie intake reduce by 1% to 3%.<sup>5</sup> Whilst the evidence of GLP-1 drugs negatively affecting consumption in these categories remains unproven, the advent of these new drugs may significantly challenge the U.S. food/beverage industry's ability to compound at mid-single-digit rates going forwards. The market has made its judgement, with the U.S. food, beverage and tobacco sub-sector down 9.9% year-to-date, trading at a price-to-earnings discount of over 10% relative to the U.S. market.<sup>6</sup>

In terms of the impact on our portfolio, we do not own food manufacturers as we consider them low-growth, low-return businesses with limited pricing power. An American multinational soft beverage manufacturer we own may, at first glance, appear to be an example of a company at risk; but an assessment of the business model suggests otherwise. Almost 70% of its product mix comes from no- or low-calorie drinks—categories that are less likely to be affected—while around 80% of sales come from outside the U.S.,<sup>7</sup> where the uptake of the drugs may well be slower. While there is a tail risk around tobacco and alcohol, the evidence of the GLP-1 drugs negatively impacting consumption in those categories is yet to be proven.

## Health Care

In health care, the immediate winners have been the companies that manufacture GLP-1 drugs, with one of the

two main providers now worth more the entire Danish domestic economy.<sup>8</sup> We don't hold these companies in our global portfolios as pharmaceutical companies typically don't meet our high quality criteria; whilst they can generate significant profits on a patented drug—GLP-1 analogues are a case in point—these revenues are reliant on patent protection. Once this patent expires, sales and profits may be decimated by generic competition. This issue is exaggerated further when a company is dependent on a small number of drugs to fuel its success.

The potential impact on life science and health care equipment providers is more relevant for our portfolios. We believe that the negative share price reaction for at least some diabetes-related products may have been overdone; ultimately, patients with diabetes will still need to monitor blood sugar levels and administer their medication. A medical devices and health care company we own recently reported that those patients who used their glucose monitors alongside taking GLP-1 medication had higher therapy compliance. Meanwhile a clinical trial provider that we hold has benefited from its involvement in GLP-1 drug trials and may also continue to benefit throughout the lifecycle of the drugs should the manufacturers wish to monitor “real-world” evidence, i.e., monitoring usage patterns and side effects. Another of our holdings—an American supplier of technology, pharmaceutical and biotechnology services—may benefit from providing the sterile injectables for GLP-1 drugs, with potential second-degree benefits in its laboratory equipment business and sale of bioscience reagents if there is reinvestment in research and development as a result of increased revenues flowing to the health care sector.

## The weight of speculation

While the hype around GLP-1 analogues continues, the long-term side effects of the drugs are not yet known. Some initial studies have suggested an association between GLP-1 drugs and gastrointestinal side effects and/or loss of muscle mass, and the FDA has committed to a review after accounts of depression from some users. Drug manufacturers are already working on improvements to address these issues. From a practical viewpoint, production capacity and insurance reimbursement factors may restrict the extent of penetration, not to mention the time it can take to reach peak penetration—it took 20

<sup>4</sup> Source: Barron's "Why the weight-loss drug hype looks overdone", 2 October 2023.

<sup>5</sup> Source: Barron's "Weight-loss drugs are threatening food stocks. The fears are exaggerated", 6 October 2023.

<sup>6</sup> Source: FactSet. As of 31 October 2023.

<sup>7</sup> Source: MSIM International Equity Team research and Company Annual Report 2022.

<sup>8</sup> Source: Bloomberg News "Novo's value surpasses Denmark GDP after obesity drug boost", 9 August 2023.

<sup>9</sup> Statins are a medication used for treating elevated cholesterol.

years in the case of statins.<sup>9</sup> U.S. insurance companies will have a key part to play, as take-up will be underpinned by their willingness to cover prescriptions. Outside the U.S., uptake will also rely on health care systems agreeing to provide coverage, and on local regulatory approvals.

The emergence of GLP-1 drugs has caused waves across industries, but we remain sanguine about its effect on our portfolios and will continue to monitor developments. Long term, what will matter is the companies' fundamentals, their future earnings' potential and the sustainability of their long-term returns.

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## DEFINITIONS

**Gross Domestic Product (GDP)** is the monetary value of all the finished goods and services produced within a country's borders in a specific time period. It includes all private and public consumption, government outlays, investments and net exports.

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