

Federated Hermes Impact Opportunities

Quarterly Impact Report
Q4 2023

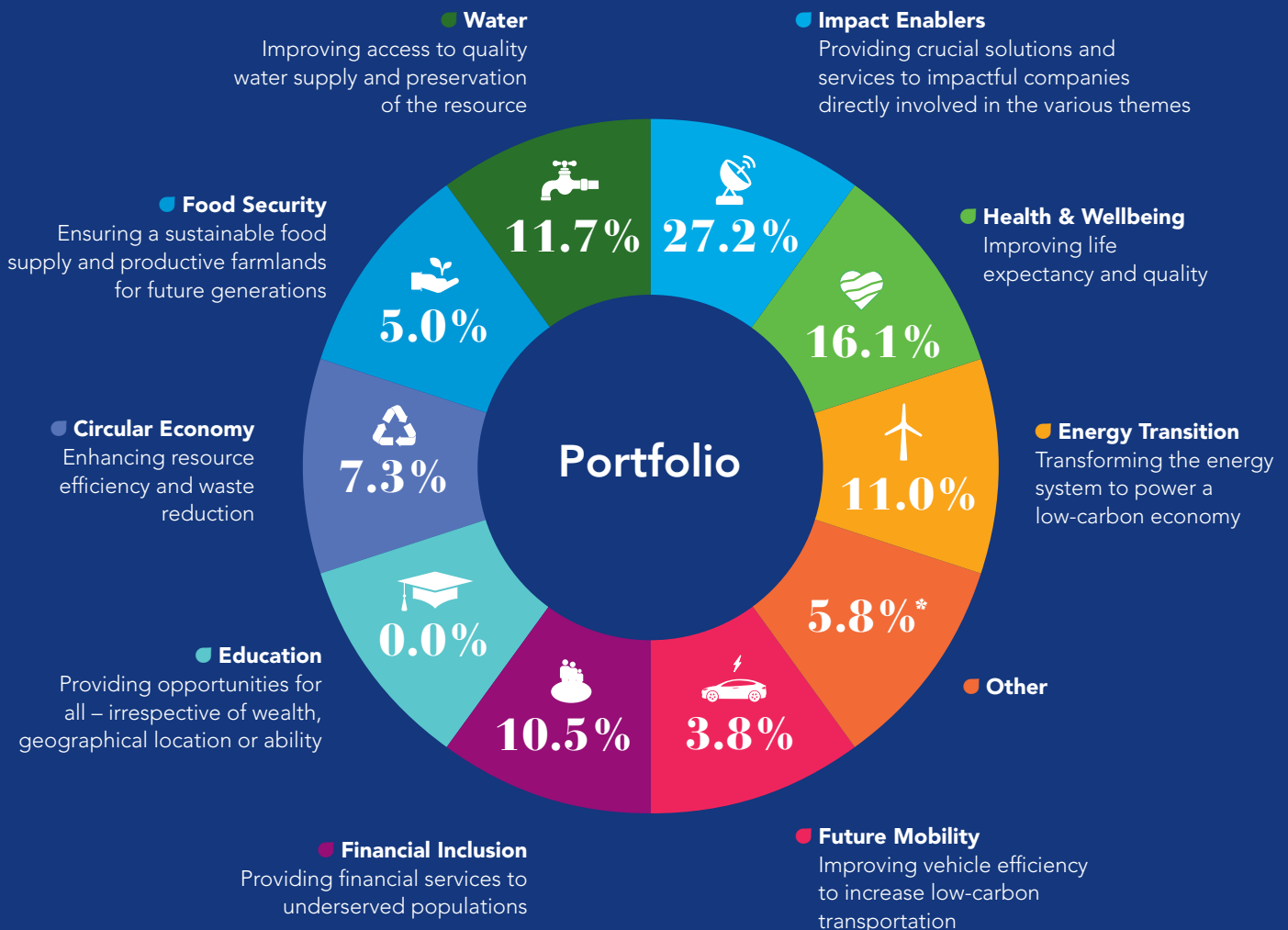
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The Federated Hermes Impact Opportunities Strategy is a high-conviction global equity strategy with a bold objective. It aims to generate long-term outperformance by investing in companies succeeding in their core purpose: to generate value by creating positive and sustainable change that addresses the underserved needs of society and the environment. In this way, it focuses on tomorrow's leading companies – today.

Exposure by impact theme

We take a thematic approach: our holdings fit into one or more of nine impact themes aligned with the Sustainable Development Goals (SDGs) of the United Nations (UN).



Federated Hermes Limited, as at 30 September 2023.

*Note: as at 30 September 2023, 5.8% of our exposure was not directly related to any of our nine impact themes, while 1.6% was held as cash.

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THEMATIC FOCUS:

Diabetes and obesity: Treating the 21st Century's silent killers

Around 537 million people worldwide have diabetes¹, while over 650 million are obese² – and numbers are rising rapidly. With both conditions linked to a wide range of other serious medical issues, countering these two silent killers is one of the key healthcare and social challenges of the 21st Century.

Fast reading:

- Diabetes is not a new problem; however, the impact of modern lifestyles has resulted in a huge surge in cases of type 2 diabetes. Given the limited impact of public health campaigns, effective treatments are vital to reduce the social and economic cost.
- Being overweight is both a major cause of type 2 diabetes and a factor in numerous other diseases, including heart attacks, strokes, osteoarthritis and cancer. As obesity becomes recognised as a public health issue, the pathway to effective treatment is opening.

In 2023, the journal *Public Health Challenges* named diabetes as one of the world's top 10 public health issues, calling it 'a serious and potentially debilitating condition with costly complications to individuals, families, healthcare systems, and national economies'.³

Meanwhile, the World Health Organization (WHO) has called rising obesity a 'public health crisis... that undermines social and economic development throughout the world and has the effect of increasing inequalities between countries and within populations'.⁴

Until recently, the focus has largely been on prevention – unfortunately with limited success. However, recent medical advances present the opportunity to manage diabetes more effectively, and to treat both type 2 diabetes and obesity with highly effective drugs.

Not to sugar-coat the facts, the rise in diabetes is largely a social issue

Two forms of diabetes account for the vast majority of cases; these are known as type 1 and type 2.

- **Type 1 diabetes:** A condition where the pancreas makes little or no insulin; it usually develops in children and currently accounts for less than 10% of all cases.⁵ The causes are unknown and there is no known cure.
- **Type 2 diabetes:** The pancreas produces insulin, but the body is unable to properly absorb it. According to the WHO, more than 95% of diabetes cases worldwide are type 2,⁶ and this percentage is likely to rise. It is strongly associated with lifestyle choices, particularly high-calorie diets, lack of exercise and associated obesity.

The International Diabetes Federation predicts the number of diabetics globally will hit 783 million by 2045, an increase of 46% on current figures.⁷ By that time, one in eight adults will be living with the disease.⁸

According to the International Diabetes Federation, by 2045 one in eight adults globally will be living with diabetes.⁹

Death rates for diabetes rose 70% between 2000 and 2019, putting it in the top 10 of causes of death worldwide.¹⁰ As well as acute complications from the disease itself, diabetes is associated with a wide range of chronic issues including heart attacks, strokes, kidney problems, nerve damage, gum disease, sight loss, sexual problems and higher risk of some cancers.

¹ Facts & figures page of the International Diabetes Federation website. Accessed 24 November 2023. <https://idf.org/about-diabetes/diabetes-facts-figures/>

² Obesity and overweight page of the World Health Organization website. Accessed 24 November 2023. <https://www.who.int/news-room/fact-sheets/detail/obesity-and-overweight>

³ 'Top 10 public health challenges to track in 2023: Shifting focus beyond a global pandemic'. Published in *Public Health Challenges*, Volume 2, Issue 2, 2 May 2023. <https://onlinelibrary.wiley.com/doi/10.1002/puh2.86>

⁴ 'WHO acceleration plan to stop obesity', p2. Published by the World Health Organization, 3 July 2023. <https://www.who.int/publications/i/item/9789240075634>

⁵ JAMA patient page, type 1 diabetes, as at September 2007.

⁶ 'Diabetes' page of the World Health Organization website. Accessed 27 November 2023. <https://www.who.int/news-room/fact-sheets/detail/diabetes>

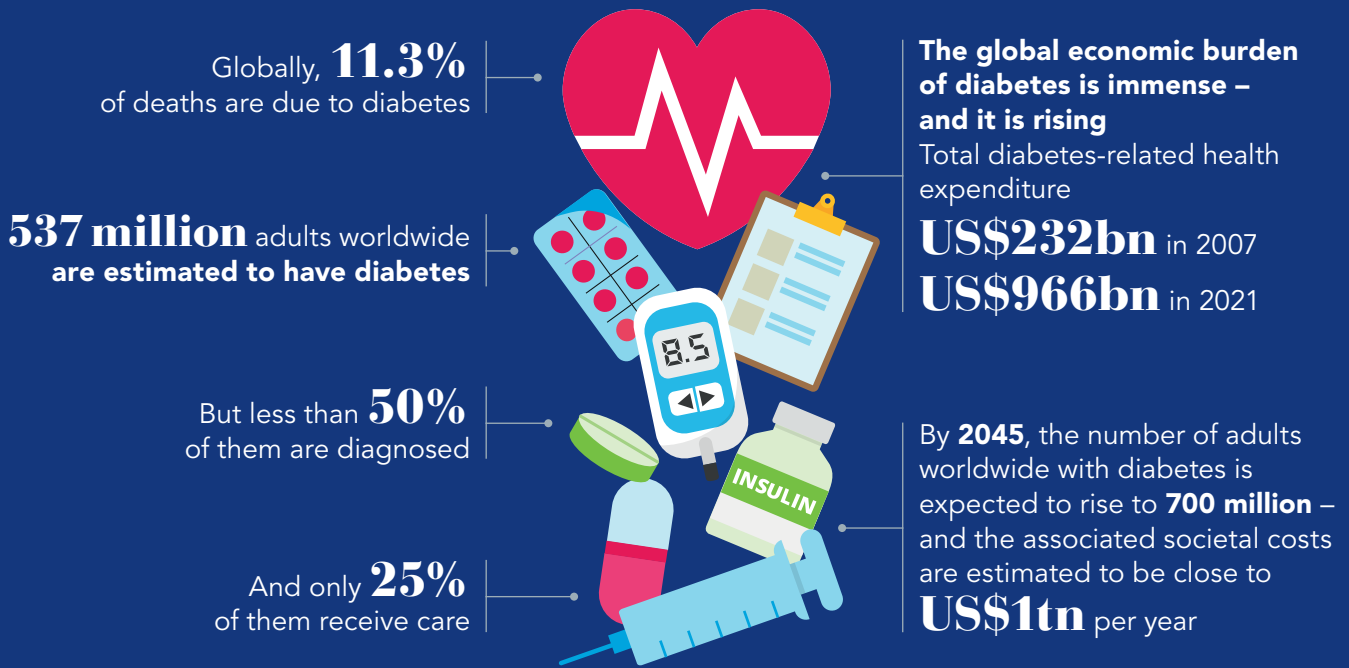
⁷ Facts & figures page of the International Diabetes Federation website. Accessed 24 November 2023. <https://idf.org/about-diabetes/diabetes-facts-figures/>

⁸ Facts & figures page of the International Diabetes Federation website. Accessed 24 November 2023. <https://idf.org/about-diabetes/diabetes-facts-figures/>

⁹ Facts & figures page of the International Diabetes Federation website. Accessed 24 November 2023. <https://idf.org/about-diabetes/diabetes-facts-figures/>

¹⁰ 'The top 10 causes of death'. Published by the World Health Organization, 9 December 2020. <https://www.who.int/news-room/fact-sheets/detail/the-top-10-causes-of-death>

Figure 1. Diabetes is one of the fastest growing health conditions globally



Source: International Diabetes Federation, December 2021

A weighty issue: obesity as a health problem

The growth in type 2 diabetes is being driven by various factors, including urbanisation, an ageing population and reduced physical exercise. However, probably the most significant factor is obesity. Both being overweight and obesity are defined by the World Health Organization as ‘abnormal or excessive fat accumulation that may impair health’.¹¹ Obesity implies that excess weight is high enough to cause a significant risk to health.

According to the WHO, obesity rates tripled between 1975 and 2016 to include around 13% of the global population.¹² In the US, which leads the trend, prevalence among adults is over 40%.¹³ By 2030, the World Obesity Federation predicts that over one billion people worldwide will be obese.¹⁴

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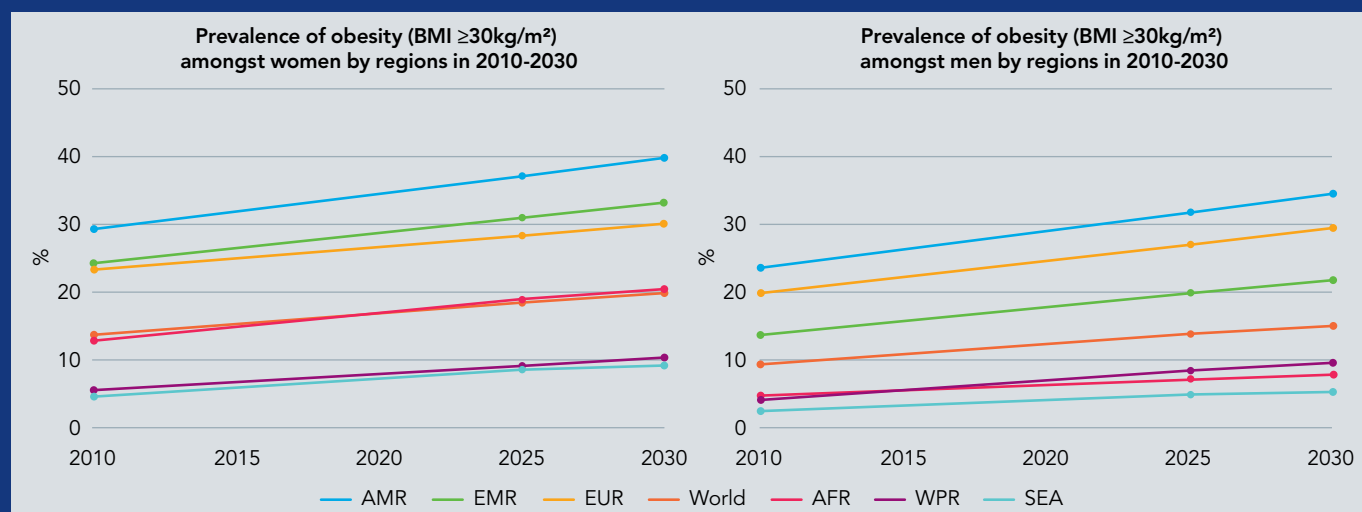
¹¹ Obesity and overweight page of the World Health Organization website. Accessed 24 November 2023. <https://www.who.int/news-room/fact-sheets/detail/obesity-and-overweight>

¹² Obesity and overweight page of the World Health Organization website. Accessed 24 November 2023. <https://www.who.int/news-room/fact-sheets/detail/obesity-and-overweight>

¹³ Adult Obesity Facts page of the Centres for Disease Control and Prevention. Accessed 24 November 2023. <https://www.cdc.gov/obesity/data/adult.html>

¹⁴ ‘World Obesity Atlas 2022’, p7. Published by the World Obesity Federation, March 2022. https://s3-eu-west-1.amazonaws.com/wof-files/World_Obesity_Atlas_2022.pdf

¹⁵ ‘World Obesity Atlas 2022’, p7. Published by the World Obesity Federation, March 2022. https://s3-eu-west-1.amazonaws.com/wof-files/World_Obesity_Atlas_2022.pdf

Figure 2. Obesity is increasing across populations globally

Source: World Obesity Atlas 2022. NCD Risk Factor Collaboration (2017) and World Obesity Federation projections.

As well as type 2 diabetes, obesity is associated with heightened risk of a wide range of health problems, including heart disease, strokes, osteoarthritis and cancer.¹⁶ The WHO considers obesity both a social issue and a public health problem, citing its negative effect on inequalities between countries and within populations, its 'significant impacts on wellbeing and quality of life', and it being a risk factor for other serious diseases.¹⁷

Historically, public attitudes have tended to resist the categorisation of obesity as a 'disease'. However, governments, including the US, increasingly recognise it as such.¹⁸ This is important as it ensures adequate funding for treatment options.

Managing obesity

Once obesity is categorised as a public health problem, the potential to treat it medicinally becomes economically significant. Currently, the consensus view puts the market for obesity drugs at upwards of US\$60bn.¹⁹

The main clinical treatment route for obesity is through a hormone known as glucagon-like peptide 1, or GLP-1 for short. GLP-1s were first developed to treat diabetes, but the efficacy of modified, longer acting versions at aiding weight loss led to them being approved and marketed as an obesity treatment.

Novo Nordisk's Wegovy, whose semaglutide²⁰ molecule is also marketed for diabetes as Ozempic, was first to market. The drug's unprecedented popularity with both doctors and patients has caused worldwide supply shortages. This has led

to off-label prescription of Ozempic for weight loss and a problematic black market in the drug, resulting in some negative media coverage. However, the highly positive results from the huge SELECT trial of Wegovy provide ample evidence that when used under proper medical supervision, GLP-1s can not only support weight loss but also reduce the risk of potentially fatal diseases including heart attacks and strokes.

Other drug companies are now eyeing up the obesity market. Most significantly, Eli Lilly has just launched a version of its own GLP-1-based molecule, tirzepatide, as a weight loss treatment – under the name Zepbound. Second generation obesity treatments are already in the pipeline; these combine GLP-1s with other molecules which speed up the body's metabolic rate to burn calories more quickly.

Inevitably, treating symptoms rather than addressing root causes creates a potential moral hazard. We believe upstream measures to address the social issues surrounding obesity are a vital factor in improving healthcare outcomes. However, despite decades of public health messaging encouraging healthier eating, surging cases of obesity and type 2 diabetes present a significant and growing burden on healthcare systems and wider society. We therefore see a dual approach involving both prevention and cure as justified.

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¹⁶ 'World Obesity Atlas 2022', p7. Published by the World Obesity Federation, March 2022. https://s3-eu-west-1.amazonaws.com/wof-files/World_Obesity_Atlas_2022.pdf

¹⁷ 'World Obesity Atlas 2022', p7. Published by the World Obesity Federation, March 2022. https://s3-eu-west-1.amazonaws.com/wof-files/World_Obesity_Atlas_2022.pdf

¹⁸ 'The implications of defining obesity as a disease: a report from the Association for the Study of Obesity 2021 annual conference'. Published by eClinicalMedicine, part of The Lancet Discovery Science, 6 April 2023. [https://www.thelancet.com/journals/eclinm/article/PIIS2589-5370\(23\)00139-6/fulltext](https://www.thelancet.com/journals/eclinm/article/PIIS2589-5370(23)00139-6/fulltext)

¹⁹ Estimate obtained via Visible Alpha Insights.

²⁰ Semaglutide (Wegovy, Ozempic, Rybelsus) is a medicine used for weight loss in specific patients, and to lower blood sugar levels and reduce the risk of major cardiovascular events such as heart attack or stroke in type two diabetes patients. Semaglutide is a GLP-1 agonist and works by increasing insulin release, lowering the amount of glucagon released, delaying gastric emptying and reducing appetite.

Monitoring and managing diabetes

While GLP-1s offer a highly effective solution to the rising tide of type 2 diabetes, they are ineffective against type 1 diabetes due to its very different pathology. With no effective treatment yet discovered, type 1 sufferers must monitor and manage their condition as the only way to limit its potentially serious and even fatal impact on their daily lives and overall health.

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Meanwhile, type 2 diabetes sufferers also need to manage their blood glucose levels or risk serious complications. While GLP-1s can help control blood sugar, they are not a direct cure for the diabetes itself. Monitoring and GLP-1 treatments are therefore both beneficial.

Traditionally, checking blood glucose levels meant taking multiple finger-prick tests on a daily basis. However, over the past 20 years, wearable devices known as continuous glucose monitors, or CGMs, have been developed. These automatically measure glucose levels every few minutes,

enabling tracking and prediction. The latest advance is the automated insulin delivery system, sometimes referred to as an 'artificial pancreas'. This combines a CGM with an insulin pump which delivers the required dose based on assessed and predicted blood glucose levels.

Inevitably, widespread treatment with GLP-1s will have the socially desirable impact of shrinking the monitoring market for type 2 diabetes over time. However, market penetration for monitoring systems is still very low, allowing considerable headroom for growth.

Conclusion

Both diabetes and obesity are significant and growing public health issues whose social and economic impact cannot be underestimated. Given the limited efficacy of public health campaigns and legislation in addressing the root causes of both type 2 diabetes and obesity, effective treatments are vital. Meanwhile, the lack of any viable treatment for type 1 diabetes makes effective monitoring and management the only means possible to improve the lives of sufferers and reduce the burden on healthcare systems. Both drug treatments for type 1 diabetes and obesity and effective monitoring and management for diabetes are therefore a major impact opportunity, which we are pursuing through multiple investments.





CASE STUDY

Novo Nordisk

Novo Nordisk is a Danish multinational healthcare company with a strong heritage in treatments for diabetes. Founded in 1923, it employs more than 59,000 people across 10 R&D centres, 16 production sites and 80 offices around the world, marketing its products in 170 countries.

Impact theme:
Health & Wellbeing

Battling Type 2 diabetes and the obesity that is a key cause

Novo Nordisk has received considerable attention recently thanks to the runaway success of its weight-loss drug Wegovy. The company has been a pioneer in the medical treatment of obesity, helping bring its treatment as an illness into the mainstream.

Wegovy's active ingredient is semaglutide, which belongs to the group of medications known as GLP-1s (see Thematic Focus section of this report) and acts as an appetite suppressant. Semaglutide is also marketed by Novo Nordisk at a slightly lower dose for the treatment of type 2 diabetes, under the brand name Ozempic.

Novo Nordisk has received considerable attention recently thanks to the massive popularity of its weight loss drug Wegovy.

The company has a strong pipeline of further treatments. These include a second-generation drug for type 2 diabetes called CagriSema, which is already in Phase 3 trials and could be on the market within two years. CagriSema combines semaglutide with a synthetic version of amylin, a hormone secreted along with insulin by the pancreas. Amylin inhibits food intake, delays gastric emptying and decreases blood glucose levels, further supporting weight loss.

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Patients treated:

36.4 million

Lives extended:

1.9 million

Note: Figures as at December 2022.

Why we're invested

Diabetes and obesity are health issues that have a severe impact on both sufferers and wider society. Addressing diabetes is proven to have broader health benefits, including reducing cardiovascular problems and kidney disease, while obesity is strongly linked to heart disease, arthritis and cancer. Novo Nordisk is one of two market leaders in medication for the former, and a trailblazer in medical treatment of the latter.

The SELECT trial, which involved 17,604 obese adults, found a 20% reduced incidence of heart attack, stroke or death from heart disease.

Most drug companies are eyeing up the obesity market due to its role in other health issues. This includes key rivals Eli Lilly, who are launching their own anti-obesity drug, Zepbound, in 2024. Zepbound has even stronger efficacy data than Wegovy but, having been a lone wolf in the sector for years, Novo Nordisk has a strong first mover advantage. Its product is extremely popular with patients and practitioners alike, and the company has built up a wealth of clinical evidence to prove its efficacy, safety and broader health benefits. In trials, nearly half of adults taking Wegovy lost 10% or more weight, while 30% of people lost 20% or more.²¹ Meanwhile, the SELECT cardiovascular outcomes trial, which involved 17,604 obese adults with established cardiovascular disease in 41 countries, found a 20% reduced incidence of heart attack, stroke or death from heart disease.²²

Novo Nordisk in numbers

10 R&D sites centres in five countries around the world

16 production facilities in nine countries globally

80 offices around the world

100 years since the company was founded in Denmark in 1923

170 Number of countries with access to Novo Nordisk products

²¹ 'Weight loss with Wegovy' page on wegovy.com. Accessed 27 November 2023. <https://www.wegovy.com/about-wegovy/weight-loss-with-wegovy.html>

²² Novo Nordisk company announcement. Published 8 August 2023. <https://www.novonordisk.com/news-and-media/news-and-ir-materials/news-details.html?id=166301>



Dexcom

Founded in 1999, Dexcom, Inc. is a world leader in the development, manufacture, production and distribution of continuous glucose monitoring devices. Headquartered in San Francisco, it has manufacturing facilities in both the US and Malaysia, and offers its products in more than 50 countries.

Impact theme:
Health & Wellbeing

Improving quality of life and accuracy of treatment for diabetic patients

Dexcom specialises in innovative, easy-to-use systems that help people with diabetes proactively manage their condition and live more normal lives. Its continuous glucose monitoring (CGM) devices enable diabetes sufferers to measure, track and predict their glucose levels 24 hours a day, reducing episodes of hypo- and hyperglycaemia.

Diabetes represents a large and rapidly growing market. With the cost of care for diabetics globally already estimated at US\$760bn per year, managing the disease more effectively addresses a huge burden on society.

Dexcom has enjoyed huge growth over the past decade, increasing its sales from US\$99m in 2012 to US\$2.9bn in 2022.

Patients treated:

1.7 million

Lives extended:

67,000

Note: Figures as at December 2022.

Dexcom's existing products are designed for patients with type 1 diabetes, but they are expanding their offering to patients with type 2, who represent around 90% of all cases.²³ The company operates a razor-blade business model, with repeat purchases of sensors creating a recurring revenue stream.

Why we're invested

Dexcom is the leader in CGM, and its G7 system is the cheapest and easiest to use on the market. The company has enjoyed huge growth over the past decade, increasing its sales from US\$99m in 2012 to US\$2.9bn in 2022. Financials are strong, with EBITDA up from -US\$26.4m in 2017 to US\$391m in 2022.

The company is already providing its products to 1.7 million people. However, this is just a small fraction of the total addressable market of around 50 million, so there is significant headroom for further growth.

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Excitement around GLP-1 based treatments has had a short-term impact on Dexcom's performance. However, this is down to a lack of understanding of the company's value proposition; GLP-1 has no effect on type 1 diabetes, which is Dexcom's core market. Endocrinologists confirm CGM is complementary to GLP-1 for type 2 diabetes; in fact, data from insurance company Optum covering 2018 to 2022 indicates average CGM usage increased significantly in all type 2 populations following the use of GLP-1s.

Ultimately, Dexcom's products not only improve the lives of diabetes sufferers but also benefit society by cutting treatment costs for healthcare systems.



²³ Source: Centres for Disease Control and Prevention (CDC).

Figure 3: Dexcom is a key part of the solution for diabetic care

US\$16,750 US average annual expense per person **with diabetes**



Dexcom CGM has demonstrated:

- ↓ **35% reduction** in inpatient admission costs
 ↓ **14% reduction** in outpatient visit costs
↓ **Optimization** in type 2 diabetes medications
- ↓ **~50% reduction** in inpatient visits

Source: Federated Hermes Limited, Dexcom 2023.

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