

# NEWS STORIES ON PROMISING CORONAVIRUS TREATMENTS CAN MOVE THE EQUITY MARKET INDEXES IN BOTH DIRECTIONS

*By Nick Terhune, CFA®*

Analysts studying the healthcare industry's war on the coronavirus often have a bird's-eye view of the importance of perceived medical breakthroughs. As part of their "due diligence" these analysts speak with a myriad of professionals, including epidemiologists, scientists, doctors, caregivers, and hospital supply chain managers to provide the context needed to interpret the latest news. Commerce Trust Company Senior Investment Analyst Nick Terhune, CFA®, shares his insights on where the country is in this fight against the pandemic.

## **HOW HAS COVID-19 CHANGED YOUR INVESTMENT RESEARCH PROCESS?**

I've been a healthcare and industrial stock analyst at Commerce Trust Company for nearly a decade. My research has generally focused on individual stock opportunities, but the rapid global economic impact of COVID-19 has required the use of a wider lens when looking at these sectors recently. From an investment perspective, this situation may be best described as an economic crisis caused by a healthcare crisis. To solve the economic crisis, we must first solve the healthcare crisis. Unfortunately, the process will not be smooth, as you can see in the recent market volatility.

I see three main topics to monitor where the economy and healthcare currently intersect. First, it is increasingly apparent that a COVID-19 vaccine may be needed for the economy to safely return to full function. Treatment prospects, topic two, are a stopgap measure as the economy limps along preserving essential services. Third, although COVID-19 testing is imperfect, it will serve as our eyes and ears. COVID-19 testing can help govern the level of social distancing measures needed to balance the economic risks against the health risks given the evolving availability of treatments and vaccines.

## **COVID-19 TREATMENTS AND VACCINES HAVE BEEN DISCUSSED IN THE MEDIA FREQUENTLY. HOW ARE TREATMENTS AND VACCINES DIFFERENT IN THE CONTEXT OF COVID-19?**

Treatments help a person recover after they become ill from COVID-19. Vaccines train a person's immune system to recognize and fight the COVID-19 virus to prevent illness. I like the analogy of the immune system as a self-driving car. Treatments help repair the car after an accident due to a mistake by the self-driving system. A vaccine is an update to the self-driving system to prevent a future accident.

## **WHEN WILL A VACCINE BE AVAILABLE?**

Our best estimate is that a vaccine could be available for emergency use within the next 12 to 18 months. Vaccine development historically takes four years or longer, so the current timeline is significantly shorter in comparison.

Vaccine development is a lengthy process because it involves using a partial or weakened virus to train the immune system without causing illness or safety issues. The safety aspect of testing vaccines may carry added weight because the experimental vaccines are tested in otherwise healthy people. In addition, an adequate number of people need to try the experimental vaccine to gain confidence it is safe. Even a relatively safe new treatment given to billions of people will likely have negative side effects for some, which must be considered. It is also worth remembering that it takes time after the vaccine is given for the immune system to develop the protective benefits. At some later point, we learn whether the vaccine offered the protective benefits expected.

The question of timing naturally leads one to wonder who will “win the race” developing a vaccine. However, behind the scenes the environment is being described by insiders as more collaborative than competitive. Academic, government, and biopharma company labs are working together toward a common goal. This collaboration and recent scientific advancements are reasons to be hopeful for vaccine prospects.

### **WHEN WILL A TREATMENT FOR COVID-19 BE AVAILABLE?**

Because COVID-19 is a new virus, there are no known safe, reliable treatments specifically for COVID-19 as of this date. Existing treatments for other viruses and illnesses are being used in emergency COVID-19 care and show potential, but studies are ongoing. I would encourage readers to exercise caution using general media and social media as resources for COVID-19 treatment prospects. There are many studies attempting to understand different aspects of treatment such as timing, dosage, drug combinations, severity of illness, and demographics, among other factors. Some treatments may work in certain situations but not in others. The details of drug trials are key and the general media has the potential to unintentionally mislead readers (either positive or negative) when reporting updates. This will be important to understand during the flurry of drug trial data this spring and summer.

### **WHAT ELSE SHOULD ONE CONSIDER WHEN THINKING ABOUT AVAILABILITY OF TREATMENTS AND VACCINES?**

The science of developing COVID-19 vaccines and treatments has received most of the attention, but development is only a first step. Manufacturing and distributing billions of doses will be challenging. Until there is enough supply, thorny social issues will need to be addressed such as deciding who receives the treatment first (trade issues, strategic considerations, demographic considerations, etc.). The protective benefits come to mind first, but potential risks should be considered as well.

### **HOW SHOULD WE BE THINKING ABOUT THE COVID-19 TESTING SHORTAGES IN THE NEWS?**

Because COVID-19 is a new virus, there was initially a limited ability to test for it. In response, several companies developed tests to identify the presence of the virus. Unfortunately, new bottlenecks emerged from supply chains and raw material shortages (reagents) to complete the tests. Reagents remain a limiting factor for some testing due to the unprecedented global demand.

Luckily, it now appears a faster, simpler testing method may be available to address some aspects of the global COVID-19 response. Some newly developed methods test the immune system for signs the person has already been exposed to the virus rather than testing for the current presence of the virus itself. This type of test could help determine the safe pace social distancing measures can be eased so populations can begin resuming activities. However, it is important to keep in mind that these tests are not perfect. The error rates of false positives and negatives are meaningful, so these should be viewed as one of many tools in the decision-making process.

### **ARE THERE ANY OBVIOUS COVID-19 STOCK PICKS?**

No, and I would encourage investors to be careful here based on the unique biopharma fundamentals during pandemics. During normal times, companies typically wait to build manufacturing plants until late in the research process when it is reasonably clear the research will be a success. During the pandemic, numerous companies are

investing in manufacturing capabilities alongside unproven research in the interests of time. If the COVID-19 related research is not successful, the financial losses could be larger than typical drug development failures. In addition, most COVID-related sales opportunities will likely be temporary and at little to no profit for humanitarian reasons. The temporary opportunity to participate in higher than normal losses and lower, if any, profits leave us cautious on rumored “COVID cure stocks”.

However, there is a silver lining for pharmaceutical and biotech investors. The COVID-19 pandemic has highlighted the strategic and social need for sophisticated drug development capabilities. For their part, industry leaders have demonstrated social responsibility by donating potential treatments, investing billions of dollars toward a cure, and pledging to sell the drugs at no profit. As a result, the image and risk profile for biopharma stocks have improved from being villains in need of price regulation to one offering the ability to save lives and protect social stability. Some form of pricing regulation remains possible. However, it seems likely this regulation will be more sensitive to the health of the companies than was the case prior to the COVID-19 pandemic. This lowered risk improves future earnings potential and stock valuations broadly, supporting our positive view on the biopharma sector.

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