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The Newest “New Normal”: The World in the Wake of COVID-19



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Introduction

Franklin Templeton and Green Templeton College, University of Oxford, recently launched a three-part series of virtual academic sessions and investor panels focusing on “The Way Forward: Navigating the COVID Challenge.” Academics from Green Templeton College will be sharing and debating their latest research with Franklin Templeton investment professionals, with the hope of delivering actionable insights. Here are some of the key takeaways from the first session held on February 9, 2021.

Key takeaways

- The pandemic pulled the curtain back on an already-high level of global fragmentation and economic inequality, accelerating the impact of these challenges.
- Governments ought to establish measures and policies to enhance their countries’ resilience to any future health care emergency. Our hope is the world takes a more collaborative approach to pandemic management in terms of sharing research and data.
- The logarithmic speed with which pandemics like COVID-19 induce structural and economic change is underappreciated. Companies and governments that best adapt to this rapid pace of change are better positioned for growth going forward.
- The pandemic has revealed exciting investment opportunities in areas related to sustainability and ESG (Environmental, Social, and Corporate Governance), health care, and “green” infrastructure. At the company level, it highlights the virtues of strong business models with robust balance sheets, strong information systems to enable scenario planning and diversified supply chains.
- From an investment perspective, asset owners and managers must review their readiness for shocks. Ultimately, portfolios need to be tested for sustainability and resilience, to guard against a failure of investment returns.

In the first session, “Framing the COVID Challenge,” panelists met virtually to discuss the social, economic, and environmental challenges posed by the pandemic. Subsequent sessions will focus on “Key Lessons for Recovery Strategies” and “Measuring Progress towards a Better World.” This summary comes from the Franklin Templeton Investment Institute.

“Deconstruction” has led to a fragmented world

Relative to the 2008 global financial crisis (GFC), the world looks extremely fragmented today. During the GFC, governments reacted very quickly and launched concerted efforts to coordinate policy. This time around, while the central bankers continue to talk and coordinate, the governments have not. This has clearly been suboptimal for the world, resulting in uneven policy direction and confrontations over the supply of protective equipment, ventilators and vaccines. This is surprising, given the global nature of the pandemic and more than 2.5 million dead as of mid-February 2021.¹

It is also understandable, following four years of “deconstruction” of multilateral organizations like the World Health Organization (WHO), the United Nations (UN), and the World Trade Organization (WTO).

COVID-19 is widening global inequality

Pre-pandemic, the world was riding an unsustainable economic growth phase because of the inexorable rise of inequality and environmental degradation, resulting in waves of localized rejection of austerity policies and the rise of global populism.

COVID-19 proved to be an accelerator of these pre-existing trends, as it was clearly not an equal-opportunity pandemic.

The extent of global inequality ballooned in 2020, as the gulf between asset owners and low-income citizens widened rapidly. For the wealthy, the pandemic has been very good from a financial standpoint. Many individuals saved money by not travelling and buying large ticket items such as cars and boats, while their investment portfolios rose in value. For low-income workers, including service workers

at restaurants and bars, it's been a disaster. The “lucky ones” were furloughed—meaning they received a payout from the state. However, these payouts may be less than 50% of their regular wages—not to mention loss of tips and gratuities—forcing people to run down their modest savings. For the economy, the return of the “big spenders” may be relatively quick with obvious prejudice to the services and consumer sector, but for the bulk of the population it will be a long time. And, it is quite possible that some industries may never return.

The danger of the “silver bullet” mentality

Rising discontent and citizens' natural desire to evaluate their governments' effectiveness at combating the pandemic has led to a veritable tsunami of conflicting information and disinformation, ratcheting up pressure on governments. This would seem to imply continued open-handedness from governments who can afford it, postponing the inevitable tax hikes for as long as possible. For countries that cannot afford it, it means slightly faster economic decline and increase in social instability, as trust in government slides.

For now, it appears that most governments are placing excessive hopes in the “silver bullet” of a successful vaccination campaign. It may, or may not pay off, but the interesting aspect is that it appears indicative of a generalized shortening of horizons, both in the political classes and in the voting population. This is likely to worsen the outlook for orthodox policy formulation; if politicians believe they are likely to be elected for only a single term, they will have no appetite for long-term policy formation. This will become a problem, sooner or later.

This is consistent with our view that governments are generally set to become more intrusive. In an increasingly tense and fragmented world, under cover of the pandemic, it is too tempting for authoritarian leaders who understand that entrenchment means centralization of power.

This shift toward autocracy is historically inconsistent with strong investment returns, as it typically leads to stiffer political opposition, heightened social unrest and a more extreme political swing in the opposite direction when a leader moves on.

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Professor Trudie Lang

As it pertains to COVID-19 and future pandemics, it is important to remember that we cannot put all our eggs in the vaccine basket. We hope that what we have learned from the pandemic will carry on in helping to address future health emergencies globally—a need for good public health policies, an emphasis on solid health care infrastructure, better diagnostic tools, better tracking and tracing, etc. Indeed, the lack of an antiviral for COVID-19 is currently a huge gap. Has there been enough investment in research to address this concern for today? Will there be for future outbreaks? These are lessons we hope to learn going forward. There will be other pandemics. Our hope is the world takes a more collaborative approach to pandemic management in terms of sharing research and data. Perhaps governments can help smooth the way toward better industry information sharing. That is, we need to encourage team science.

The need for speed is key to success

The most underappreciated characteristic of the structural changes accelerated by COVID-19 is its speed. The logarithmic change the pandemic created has reduced the time horizons necessary to gain a different perspective. For companies and governments, the ability to be decisive, their speed of reaction to new information, of data examination and evaluation, of planning of policy and of construction of alternative strategies is key. Companies that moved fast protected earnings more effectively and enhanced their reputations with shareholders. Management teams that were quick to recognize the important role they play in protecting their employees, clients, suppliers and other stakeholders found themselves in the position of becoming trusted suppliers of practical information on

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protecting against COVID-19. This development is priceless in terms of building brand credibility and loyalty. As far as health security is concerned, the ability to move health data quickly around the globe is crucial, slowing/preventing the next global pandemic. As a point of reference, the WHO scenario planning exercise for “Disease X” had a 10% mortality rate and R2.² That is twice as destructive as COVID-19. The importance of global cooperation and coordinated action on day one cannot be overstated.

Dovetailing with ESG considerations

Concurrently with the renewed interest in health care security, a widening appetite amongst asset owners to focus on climate change has accentuated tensions between short-term reward and long-term restructuring. Nowhere is this more clearly illustrated than in oil and gas companies. BP, for example, is investing to become less of a fossil fuels company. The challenge is equally split between operational delivery on that

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Professor Rafael Ramírez

mission and bringing their investors along for the journey. The mismatch of expectations is in most cases terminal, forcing many investors to sell. This is a struggle that many more companies, not only in fossil fuels, are yet to address definitively. Even allowing for the present uncertain outlook, they will not be able to delay indefinitely.

Investment conclusions

Asset owners and investors must review their readiness for shocks. Governments ought to establish measures and policies to enhance their countries' resilience to any future healthcare emergency. This involves setting up new capacity for testing and analysis, to enhance preparedness for the next challenge. It is essential that global information flows improve and the cooperation between governments is rapidly re-established. The importance of global cooperation and coordinated action on day one of the next pandemic

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David Zahn

is impossible to overstate. At the company level, it highlights the virtues of strong business models with robust balance sheets, strong information systems to enable scenario planning and diversified supply chains.

Investors can use this experience, their new datasets, and new technology, to ensure the resilience of their portfolios. Ultimately, portfolios need to be tested for sustainability and resilience,

to guard against a failure of investment returns. Scenario planning has demonstrated its benefits in the fast-moving and testing time of COVID-19.

The pandemic has not merely accelerated the pace of change across virtually all facets of life—in the process, it has revealed exciting investment opportunities in areas related to sustainability and ESG, health care, and “green” infrastructure.

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Endnotes

1. Source: COVID-19 Dashboard by the Center for Systems Science and Engineering (CSSE) at Johns Hopkins University. As of February 16, 2021.
2. In epidemiology, the basic reproduction number, denoted R_0 , of an infection is the expected number of cases directly generated by one case in a population where all individuals are susceptible to infection. The definition assumes that no other individuals are infected or immunized (naturally or through vaccination).

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