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Newsletter

analytics

Investing in a Cleaner Future

The global population is by no means unacquainted with the adverse effects of Covid-19. Having lived through three lockdowns (with the fourth expected to emerge just in time for our December holidays), job losses, and violent riots to name a few, South Africans are struggling to convalesce from the toll this pandemic is taking. A further unintended consequence which has more recently come to light is the detrimental effect that Covid-19 is having on the environment. Over the course of 2020 more than 52 billion disposable masks were produced around the world. Of this mammoth number, 1.6 billion masks found their way into our oceans. This equates to something in the region of 5,500 tonnes of waste. It is important also to note that the word "disposable" used to describe masks refers to their single-use nature and not to their ability to biodegrade. On the contrary, the vast majority of disposable masks are produced using a material called polypropylene, which when discarded breaks up into microplastics. These particles are estimated to take around 450 years to fully decompose while in the ocean.

A Global Environmental Initiative

The global community, now more than ever, is taking a sober look at the implications our actions are having on the environment. There is a universal drive to protect our planet and to promote long-term sustainability, both at a national and industry level. Arguably the largest, and to date the most formalised global initiative to curb the effects of climate change is that set out by the Paris Agreement, which was entered into late in 2015 and subsequently fully promulgated by November 2016. The Agreement witnessed a total of 196 countries from around the world, acting of one accord, adopt a legally binding international treaty on climate change. Essentially, this treaty serves as a call for the constituent countries involved to set out specific long-term climate strategies which will consolidate existing policies as well as planning and research across economic sectors. The ultimate and overarching goal of the Paris Agreement (of which South Africa is an auxiliary member) is to restrict a global rise in temperature to no more than 2°C of pre-industrial levels. The latest Climate Change Report issued in August by the IPCC (International Panel on Climate Change) stated that even a 2°C increase in temperature may prove too detrimental to the environment, and that a 1.5°C target should be pursued to effectively combat climate change. The consequential success of this goal will rely heavily on the world's ability to curb its greenhouse gas emissions, the majority of which is generated through the burning of fossil fuels.

South Africa's Road to Sustainability

On a comparative basis, South Africa fares rather poorly relative to our global counterparts when evaluating our carbon footprint and corresponding contribution to "Net Zero Emissions". Currently 90% of the requisite energy utilised within South Africa's borders is generated through coal power. This requires in excess of 250 million tonnes of coal to be mined and burnt in South Africa every year, a figure well ahead of the global average on a per capita basis. This was made exceedingly evident when, in a PWC 'Net Zero Index Report' published in early 2021, South Africa was ranked as the worst G20 country in terms of carbon intensity, ranking ahead even of China. This report was published on the back of our particularly negative year of carbon contribution in 2019, which saw our carbon intensity rise by 1.3% while the global average declined by 2.4%. As a member of the 2015 Paris Agreement, and as a resulting confederate in the drive to achieve no more than a 2°C global warming increase, South Africa has pledged to be a net zero nation by 2050. In support of this endeavour President Ramaphosa has put forward a goal to reduce our use of coal-powered energy to 45% by the year 2030. In order to reach our 2°C mandate set out by the Paris Agreement, we will be required to cut our emissions by between 60% and 75% over the next thirty years.

There are many factors at play which will all have a direct influence on our ability to reduce our current coal intensity and resultant carbon emissions to achieve our global warming goal. Initial estimates on the incumbent levels of investment required to reach our environmental goals calculate that we will need in excess of R10 trillion to fund our climate strategy – this coming from an economy that has already been squeezed into a vice grip from Covid-19 and unprecedented levels of unemployment (currently at a record high 34%, with expanded youth unemployment at a staggering 75%).

Currently, the coal mining industry is one of the largest employers in South Africa, providing jobs to nearly 100 000 citizens and generating close to R150 billion in revenue to the economy every year. As such, any shift away from fossil fuels to greener energy sources will require planning of a recondite nature. As a result, the government has emphasised the need for a "just energy transition" and one that has the potential to create more jobs than it culls. A further headwind faced by South Africa is the sheer lack of infrastructure relating to other, more environmentally friendly, energy sources. The output generated by solar power is 40% cheaper than that of coal plants, and the numbers are not dissimilar when comparing coal to wind and natural gas. However, South Africa has a distinct lack of alternative energy infrastructure, which has largely contributed to us falling behind the rest of the globe in our objective of achieving Net Zero.

Signing and agreeing to the terms set out by the Paris agreement was inarguably a positive step for our drive toward a "cleaner country". By doing so we will be required to report our greenhouse gas inventory to the United Nations Framework Convention on Climate Change (UNFCCC) on a biannual basis starting in 2024. This will generate a high level of accountability and will presumedly lead to positive improvements going forward.

The Environmental Impact on Investment Portfolios

In the present investment climate, environmentally-conscious investing is by no means a novel or trailblazing phenomenon. On the contrary it has now become custom at any manager feedback session or webinar for investors to be informed, often ad nauseum, of the latest ESG Fund (funds constructed using an Environmental, Social, and Governance framework) being offered to the market. Aptly termed "Sustainable Investing", these funds are constructed with the intention of promoting issues relating to Environmental, Social, and Governance factors for the long-term benefit of society. The most common and popular means by which ESG funds are constructed is by ranking all the constituent stocks within an index and systematically removing all those which employ activities which are deemed "unsustainable" (common exclusions include companies involved in the manufacture of cigarettes and firearms, companies with large carbon footprints, and companies with low levels of diversity, to name a few).

These funds have received an adulatory reception from investors, and as a result trillions of dollars have poured into these ESG investments since they first came to market. Whereas initially ESG investing was concentrated primarily in equity funds and ETF's (those investing exclusively in company stocks and holding no exposure to fixed income assets), ESG-related bonds have since become an exceedingly attractive investment option for investors looking to increase the sustainability of their fixed income holdings. The growth in popularity of these "Green Bonds" has been so exponential in nature that the Bank of America has revised its full-year forecast of issuance of these ESG Bonds from $750bn to $900bn. In June 2021, 17% of the bonds issued across the globe were labelled as social, sustainable, or green in nature. What serves to differentiate these green bonds from their regular counterparts is that the proceeds generated through the lending of money go to environmental projects, whether it be new or existing projects related to clean energy, sustainable water management etc.

Sustainable investing is not without its critics, however, and has come under unremitting scrutiny over the lack of transparency and the difficulty in measuring the degree to which ESG factors are taken into account when constructing portfolios. Opaque definitions of ESG and delusive claims regarding their environmental virtues have led to funds being accused of "Greenwashing", that is using the label of an ESG vehicle whilst not making any material moves towards greater sustainability. It is indubitably evident that greater accountability and an increase in transparency is well overdue now more than ever, as the world takes a closer, more focused view at the effects global warming and pollution are having on our planet. Currently, responsible investing in its true form covers a relatively small portion of the global financial market, however the principles espoused by underscoring a company's impact on people and the planet have the potential to make a profound impact if more widely adopted.