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INVESTMENT MANAGEMENT

WE DON'T USE ESG TO SAVE THE WORLD

Author: Conway Williams – Head of Credit – Prescient Investment Management

Renowned finance professor Aswath Damodaran, from Stern School of Business wrote an opinion piece for the Financial Times late last year, where he asserted: "*Born in sanctimony, nurtured with hypocrisy and sold with sophistry, ESG grew unchallenged for a decade, but it is now facing a mountain of troubles, almost all of them of its own making*."

Damodaran added his voice to several others who have been critical about the airtime given to Environmental, Social and Governance (ESG) themed investing and in all honesty, his points carry serious merit.

Prescient Investment Management recently released its latest Responsible Investing Report where it unpacks the relationship between ESG, responsible investing and sustainability – terms that are often used interchangeably or as synonyms for "investing for good".

At Prescient Investment Management, we have long been sceptical of the way that ESG was being positioned in the market and for us it was critical that we built our own methodologies, specifically to address the issue of quantifying what are largely qualitative risks, rather than simply buying off-the-shelf commoditised offerings. And, so we did.

This ground-breaking, evidence-based systematic approach to ESG analysis allows us to continually adapt and enhance our investment process to capture, assess and mitigate the many risks we face in financial markets and the world at large as we consider investment opportunities across our portfolios.

We have firmly embedded our internally-developed ESG scorecard into our investment process. It has proven to be an invaluable tool in evaluating prospective and existing investments based on ESG risks and opportunities, and to a large extent, it allows us to understand and monitor material long-term sustainability risks for a company. Simply put – the evidence suggests that ESG risks do have an impact on a company's long-term sustainability, and the consideration (or lack thereof) in a business's strategy will eventually impact cash-flows.

Today, we are a leading systematic investment house in SA, based on a dual data-driven approach that incorporates both quantitative and qualitative analysis. This allows us to process over 120 million data points daily, analyse meticulously, and maintain vigour and efficiency in our analysis. A key distinction here is that this process is highly systematic, allowing the data to lead the way, rather than for us to be swayed by perceptions of "doing good" or "delivering impact", or to be driven by natural human biases.

Importantly, this intellectual property has not been limited to theoretical scenarios – we actively use this for risk management across portfolios, and also for the selection and management of securities across our investment universe. Two prime examples of the latter include: The Prescient Clean Energy and Infrastructure Debt Fund (CEIDF) and the Prescient Infrastructure Debt Strategy (PIMIDF).

The CEIDF invests in initiatives that facilitate infrastructural, environmental, and socio-economic impact and development in Southern Africa. To date this fund has deployed over R4bn in 30 renewable energy projects and infrastructure opportunities. Launched in 2015 the fund is currently invested in 28 projects, many of which are operational and located across South Africa. The Fund has contributed to the addition of 2.2 GW of clean energy to the grid, which equates to the usage of approximately one million average South African homes. At last count, these projects currently employ 2 125 individuals.

The PIMIDF, launched in September 2021, currently manages R1.6bn in assets. The offering follows a broad infrastructure mandate, giving investors access to generally inaccessible infrastructure assets which offer returns uncorrelated to traditional South African equity and capital markets.

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Our meticulous approach involves a thorough consideration of both risk and return, with a particular emphasis on ESG factors, recognizing their essential role in the risk management framework. Our proven track record with these funds underscores our adept utilization of ESG as a crucial risk management tool, enabling us to deliver superior risk-adjusted returns for our clients. Furthermore, this strategy ensures our compliance with Regulation 28 requirements, encompassing both "qualitative" and "quantitative" aspects within our investment methodology.

ESG is not about saving the world – it is also not beyond redemption. Rather it needs to follow a data-driven approach where clear returns on investment can be demonstrated and value created.

Furthermore, for ESG to enact meaningful change, however, the industry must make a collective effort — there should be a common assessment methodology: a framework that ensures ESG is rigorously evaluated and implemented across the investment spectrum in a standardised and consistent manner for all stakeholders. In this spirit, we are actively seeking collaboration and engagement with the industry to drive this vision forward.

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