

ESG and the new era of economic uncertainty

The changing emphasis within ESG investing for charities

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Introduction



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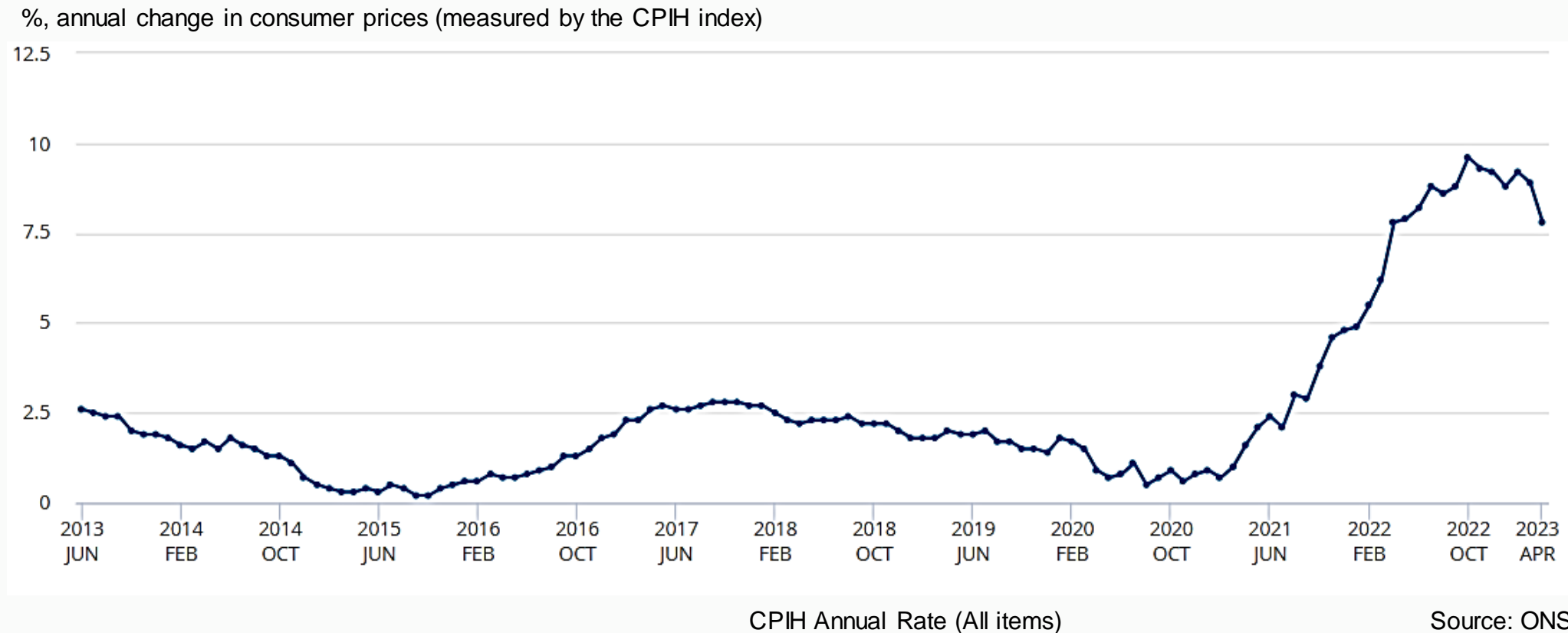
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Setting the scene:
An uncertain economic
environment...

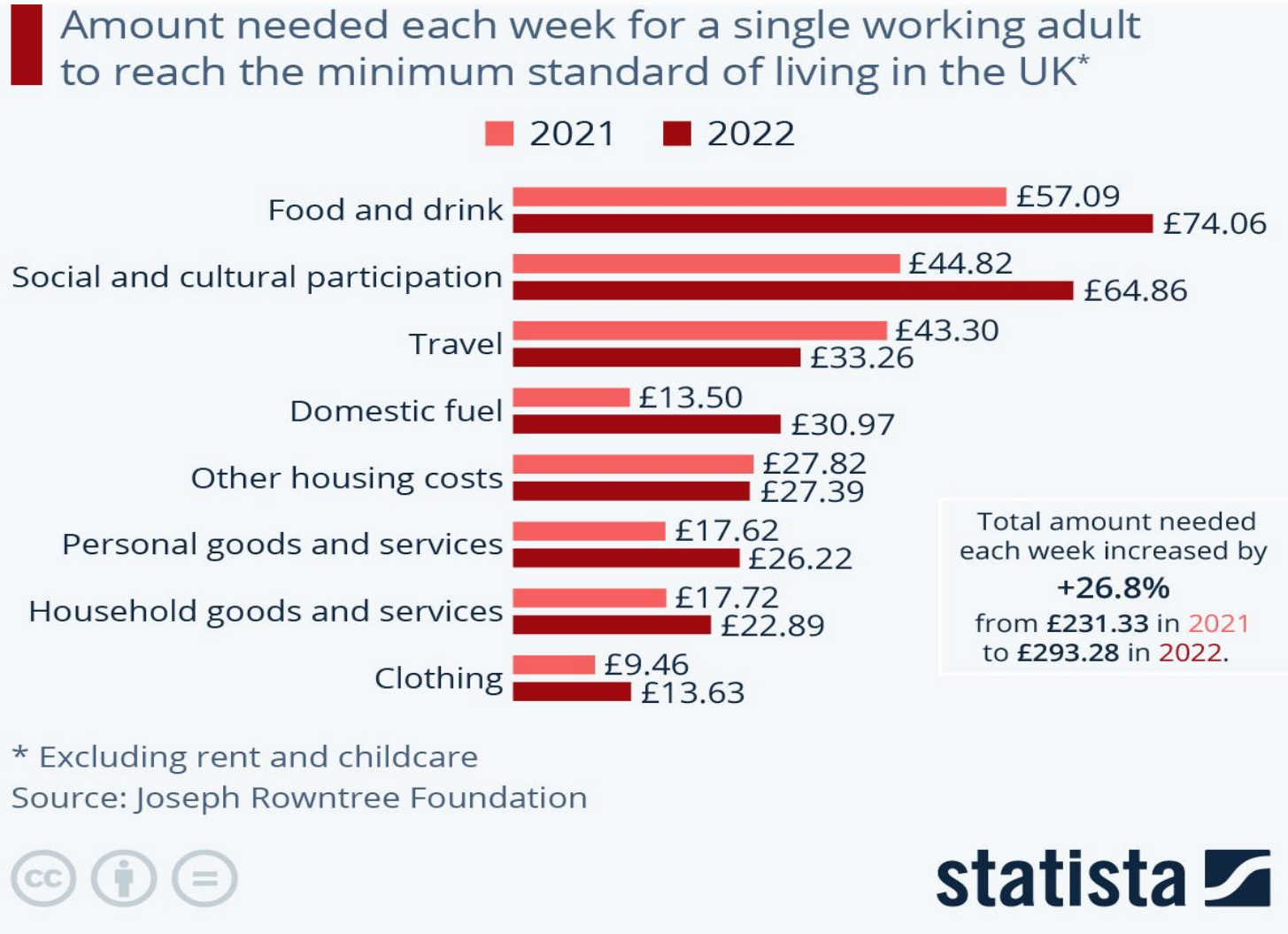


UK inflation remains high, even if it is now declining

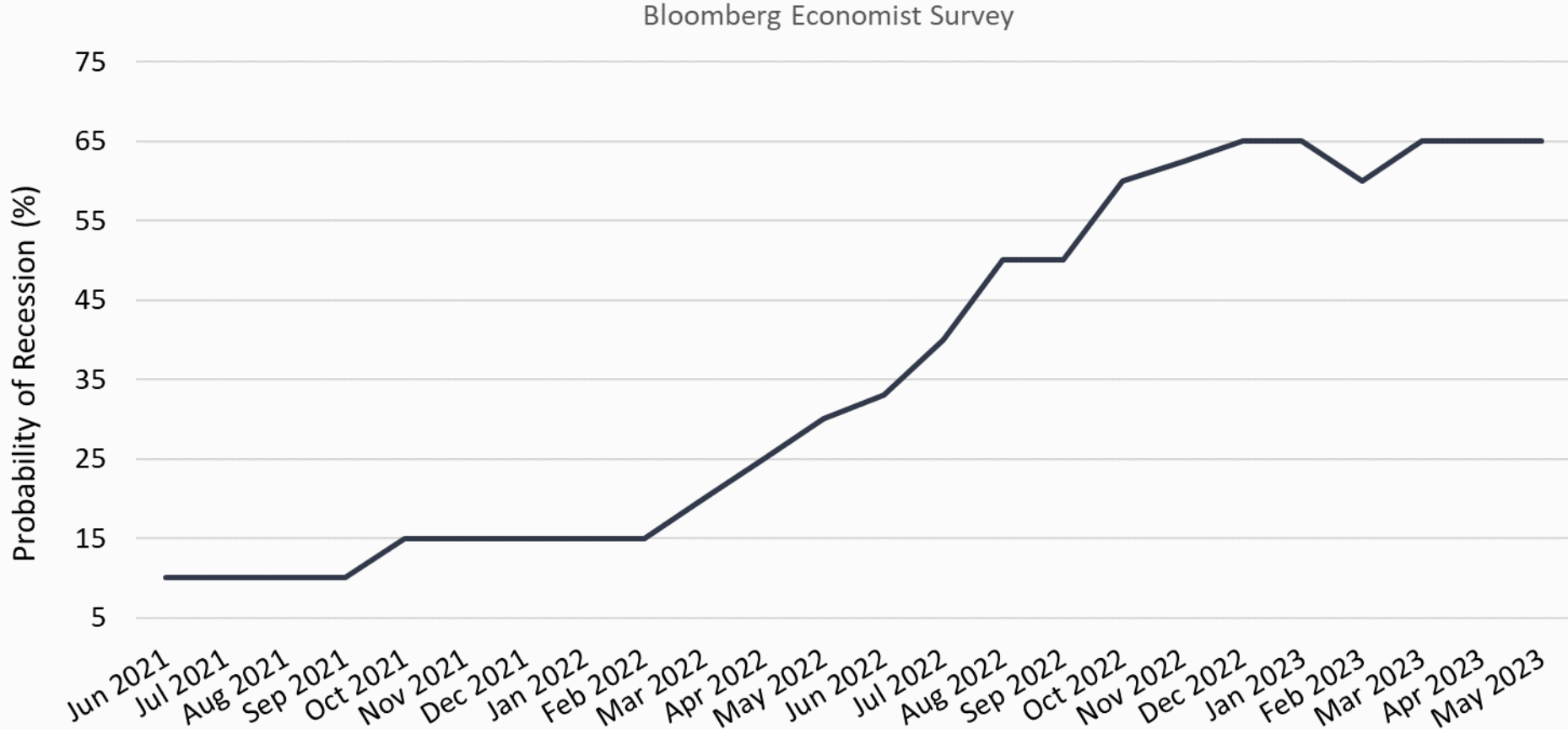
Latest headline inflation print 7.8%, down from a high of 9.8%



... and this has led to a major squeeze on incomes

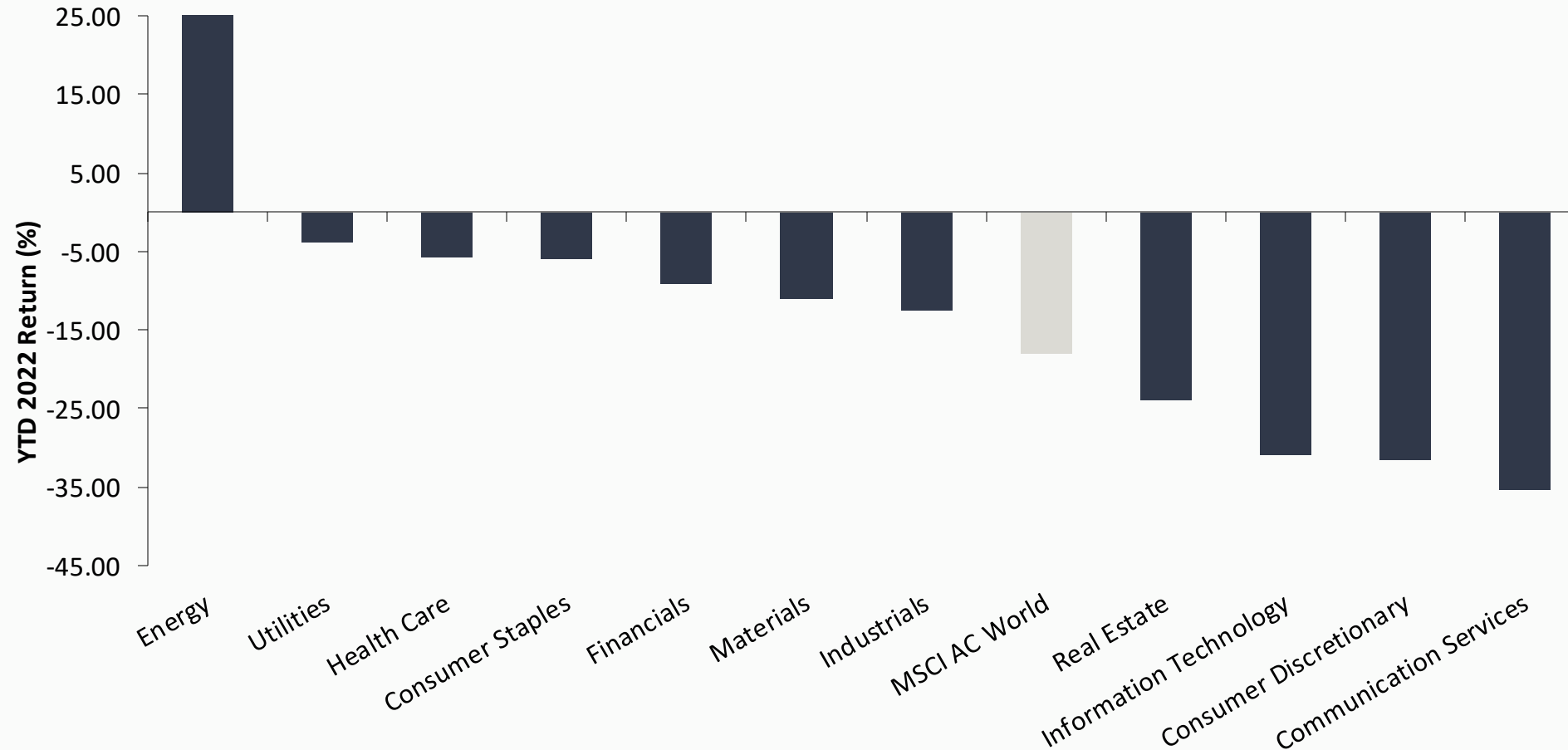


US recession probability remains elevated



Source: Investec, Bloomberg
Data as at June 2023
Investec 2023

2022 bifurcation in markets – Energy and the rest



MSCI All-Country World Index Sector Return USD Jan 2022 – Dec 2022
Source: Investec, FactSet
Investec 2023



The macro challenges facing charities in the UK



Cost of Living Crisis – A perfect storm consisting of the cost-of-living crisis, a massive increase in demand and a reduction in funding streams



Energy Crisis – The increased costs are being felt by both charities and the beneficiaries they serve



Climate Crisis – The war in Ukraine has disrupted global supply chains for energy, which has changed the conversation on climate change

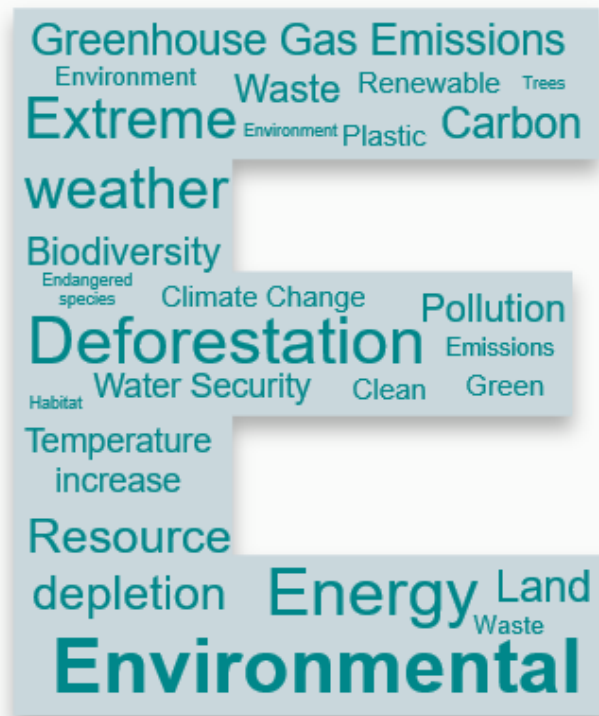


Setting the scene: ESG and the debate facing charities



ESG issues cover a wide range of topics

Navigating your way through complex and wide-ranging issues relating to ESG can be challenging for charities



Two meanings carried by ESG

“ESG has carried two meanings from birth. Regulators have never bothered disentangling them, so the whole industry speaks and behaves at cross purposes”

Source: Kirk, S. (2022) [ESG must be split in two | Financial Times](#)



The first meaning is that used by portfolio managers



The second relates to individuals trying to do the “right thing”

Risk ratings

As MSCI, one of the largest global ESG data providers put it, “*ESG ratings are designed for one purpose: to measure a company’s resilience to financially material environmental, societal and governance risks.*” (MSCI, n.d.)

They tell us nothing about the “goodness” of those companies.



Butler-Sloss Vs Charity Commission

- Charitable trustees' overarching duties are to further their charities' purposes

- This is normally achieved by maximising the financial returns on their investments at an appropriate level of risk

- Recent judgement useful in clarifying how existing legal principles should be interpreted in a modern context, but no fundamental change to the principles

- Trustees have wide discretion on how to investment on non-financial grounds. However, this needs to be balanced with any potential financial detriment and they need to evidence their decision-making

- The Charity Commission has started a process of redesigning CC14 to ensure that is easier to follow. That is expected this summer



**Different perspectives and
preconceptions:**
How our clients are responding



A client case study: Education Charity – don't do any of that ESG stuff!



A charity set up through the sale of land to provide grants and scholarships



Small trustee board that view their fund as a long-term total return endowment and the trustees want to maximize returns to support as many students as possible



Requested as few restrictions as possible with focus on maximizing returns and where initially anti-ESG

A client case study: Art's Charity – ESG all the way!



Connected to education and the arts and keen to be environmentally aware, so had substantial exclusions and screening requirements.



The trustee wanted to be at the forefront of the industry and were also keen not to displease key stakeholders such as donors, students etc. and requested a high volume of restrictions.



Last year, for example, Oil, Basic Materials, Tobacco and Aerospace & Defence were collectively up 32%.

Ethical

- Armaments
- Gambling
- Nuclear
- Pornography
- Tobacco
- Irresponsible marketing of alcohol
- High interest credit

Environment

- Companies with below average environmental management
- Coal
- Oil and Gas, Tar Sands
- Abattoirs
- Fur
- Palm Oil (manufacturers/users)

Human Rights

- Evidence of human rights abuses
- High risk to human rights
- Evidence of supply chain violations
- Product responsibility (infant nutrition, pharmaceuticals)

Is there a *right* approach to ESG investing?

The importance of understanding the views of your key stakeholders



Charity stakeholders and ESG investing

Transparency and positive communication with key stakeholders is important



Trustees, Exec and Staff



Donors



Beneficiaries

Spectrum of capital – ESG to Impact

ESG Risk Integration

Sustainable investment

Impact investment

Single Materiality.
'What is the impact of the world on the company?'

Double Materiality.
'What is the impact of the company on the world?'
Enterprise level Impact

Single Materiality.
'What is the impact of the world on the company?'

Additionality and Intent.
'Would this have happened without me?'
Investor level Impact

Double Materiality.
'What is the impact of the company on the world?'
Enterprise level Impact

Single Materiality.
'What is the impact of the world on the company?'

Ethical & Responsible Investing at Investec

ESG considerations are embedded into our investment process & monitored throughout



Membership Bodies



THE INVESTOR FORUM

Conclusion: it's all about you

- Getting it right is not easy - be guided by the charity's mission and values
- Consider all implications - NB: financial, reputational, etc.
- Ensure your Investment Policy, including ethical requirements, accurately reflects your wishes and is kept up to date
- Utilise your investment manager – they “see the market”, have substantial expertise in this area and can provide guidance
- Work out how much you can handle periods of weaker short-term performance – What is your tolerance for shorter-term periods of underperformance?
- Start talking about what you actually mean when you use the “ESG” acronym – this can help avoid confusion and division

Thank you



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