ESG: quantifying impact, and avoiding greenwashing

Mergence Investment Managers commissions research to calculate the social return on impact of affordable-housing projects

By Tshepiso Appie *

Impact investing – that is, investing for social as well as financial returns – has gone mainstream in the past few years. Today, environmental, social and governance (ESG) reporting is a basic requirement for companies, and, for fund managers, a principle that guides investment decisions.

Still, fund trustees will be well aware of the growing backlash against ESG reporting, which really gained traction in the US in 2022.

There were many reasons for this backlash. These include the difficulty of obtaining data to quantify impact, and the insidious practice of "greenwashing", when companies falsely claim to be more environmentally friendly or socially responsible than they are.

And yet, it's clear that ESG reporting isn't going away anytime soon.

A report at the World Economic Forum in Davos last year, titled *"Here's why we must not lose sight of the importance of ESG despite the recent backlash"*, firmly argues the case for ESG and impact investing. It argued that considering extra-financial information, if done properly, enables better decisions and leads to sustainable economic growth.

The WEF argued that, from an investment perspective, incorporating an ESG analysis alongside traditional financial factors adds to our holistic understanding of risk, opportunity and long-term value outcomes.

Of course, the data that underpins our understanding of ESG investments is being constantly refined and standardised. Organisations such as the Global Reporting Initiative (GRI), the Sustainability Accounting Standards Board (SASB), and the Task Force on Climate-related Financial Disclosures (TCFD) are trying to harmonise ESG reporting frameworks.

This is a valuable step forward for the industry, which will hopefully enhance transparency.

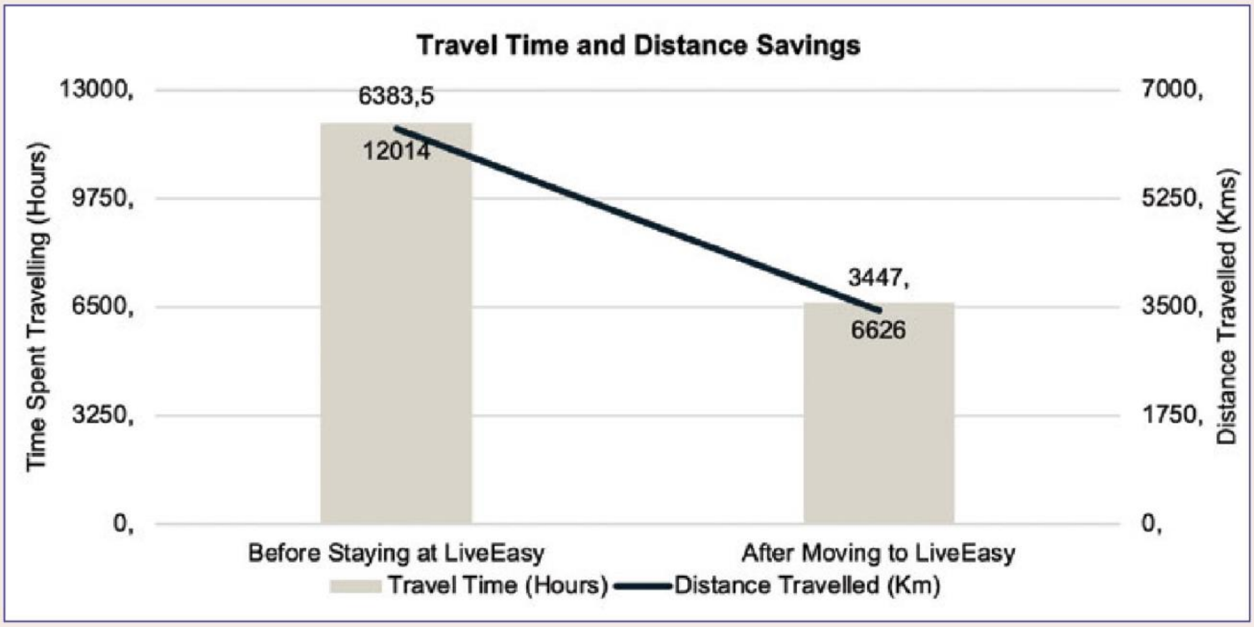
Assessing impact empirically

It's within this context that Mergence Investment Managers, which has 15 years of experience in impact investing, engaged EBS Advisory (now called EY SaTs) to look at ways of enhancing its investment process with a quantitative ESG underpin.

EY examined one particular company in Mergence's Infrastructure and Development Equity Fund I, called Live Easy. The aim of this groundbreaking research was to calculate the social return on impact (SROI) of Live Easy's affordable-housing projects, which aim to provide safe and secure accommodation to tenants.

It was the first research of its kind locally, and will be used as a baseline against which to assess further growth in the portfolio.

Live Easy was founded 12 years ago by entrepreneurs James Huff and Jeffrey Froom,



who wanted to fill the gap in the market between social housing and privately owned homes, a gap highlighted in the government's National Development Plan.

As one of South Africa's largest affordable-housing rental brands, Live Easy has 4 500 units across 10 sites and 16 buildings in Gauteng, situated close to transport and business hubs, with 1 500 units under development. The idea is to expand nationally.

The homes themselves are described as "nanos", at an average of 18m2, with a kitchenette and bathroom. The average rental is R3 500 per month – affordable to those who earn between R10 000 and R20 000 per month.

What's different is that Live Easy also provides amenities not usually available at that price: 24/7 security, biometric access, workspaces with wi-fi, lounges, chill areas, playgrounds, open spaces, retail shops, laundromats, salons, gyms and creches. It's particularly attractive to young women, who make up 60% of the tenant profile.

The research study aimed to assess, first, what impact this project has had on the environment and, second, the safety and credit risk for female tenants in five Live Easy buildings.

So, what did the study find?

On the first count, the conclusion was that living at the Live Easy apartments reduces a tenant's carbon footprint. The study measured the average tons of CO_2 reduction achieved for each of the five buildings and their tenants.

It found that tenants benefited in a number of other ways, too, including:

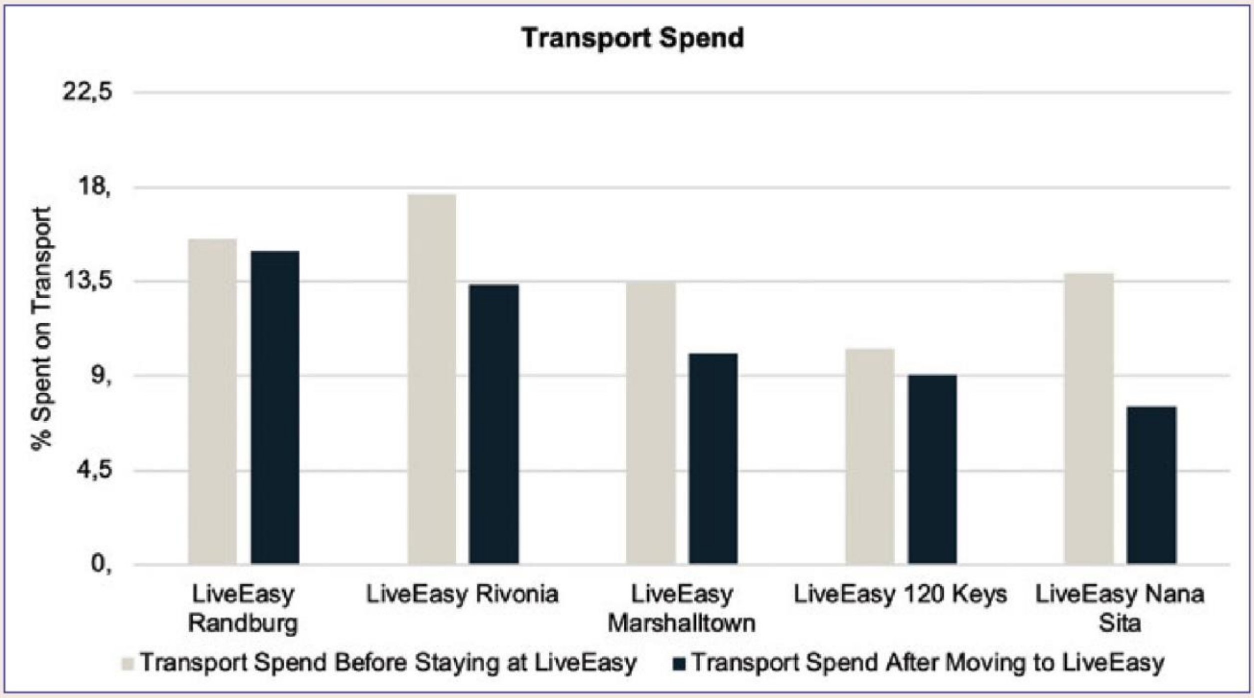
- There was an increase in disposable income, partly through energy and water savings. Their savings increased by 132% after moving in, and

Greenwashing: what trustees should look out for

For a start, trustees should be wary of firms that don't have a robust track record and experience in impact investing.

An investment firm's strategy and investment process should be underpinned by a quantitative and robust ESG appraisal methodology, to ensure that investee companies are truly making a tangible impact.

Trustees need to support firms and investment teams that have paid their dues in the impact investment space, and which are truly making a difference.



their travel spend fell by 3.1%.

- Tenants experienced, on average, a 50% drop reduction in distance travelled and time spent travelling to work or *educational* institution..

On the second count, the study found that female tenants were able to maintain good credit scores for the duration of their occupancy. On average, female tenants across all five buildings studied allocated 28% of their income to monthly rent – below the recommended maximum of 30% of gross monthly income earmarked for rent. Female tenants also reported feeling safer.

These are valuable findings in a world that is not only demanding a greater number of ESG investments, but is just as eager to know what impact these investments are having in the world. It's just this sort of study that vindicates the decision to invest – and which will hopefully spur many more projects of this sort in the future.

** Appie is an investment associate at Mergence Investment Managers*