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Emerging stronger: building an economically and environmentally resilient AC world
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While lockdown measures have been necessary for public health, they have imposed enormous economic costs and exposed the vast inequalities in South Africa.

The COVID-19 crisis has highlighted the imperative to create an improved local and global economy that is better able to cope with any future catastrophes. Efforts to address the immense social and environmental challenges we currently face will be of prime importance in both the public and private sectors.

How might we use this current crisis to catalyse collective action to build more resilient economies - and how is the role of responsible investors being redefined for an after-coronavirus (AC) world? Tarryn Sankar, Head of Listed Credit at Futuregrowth Asset Management, shares her thoughts on how COVID-19 might be used as an opportunity to build economic and environmental resilience.

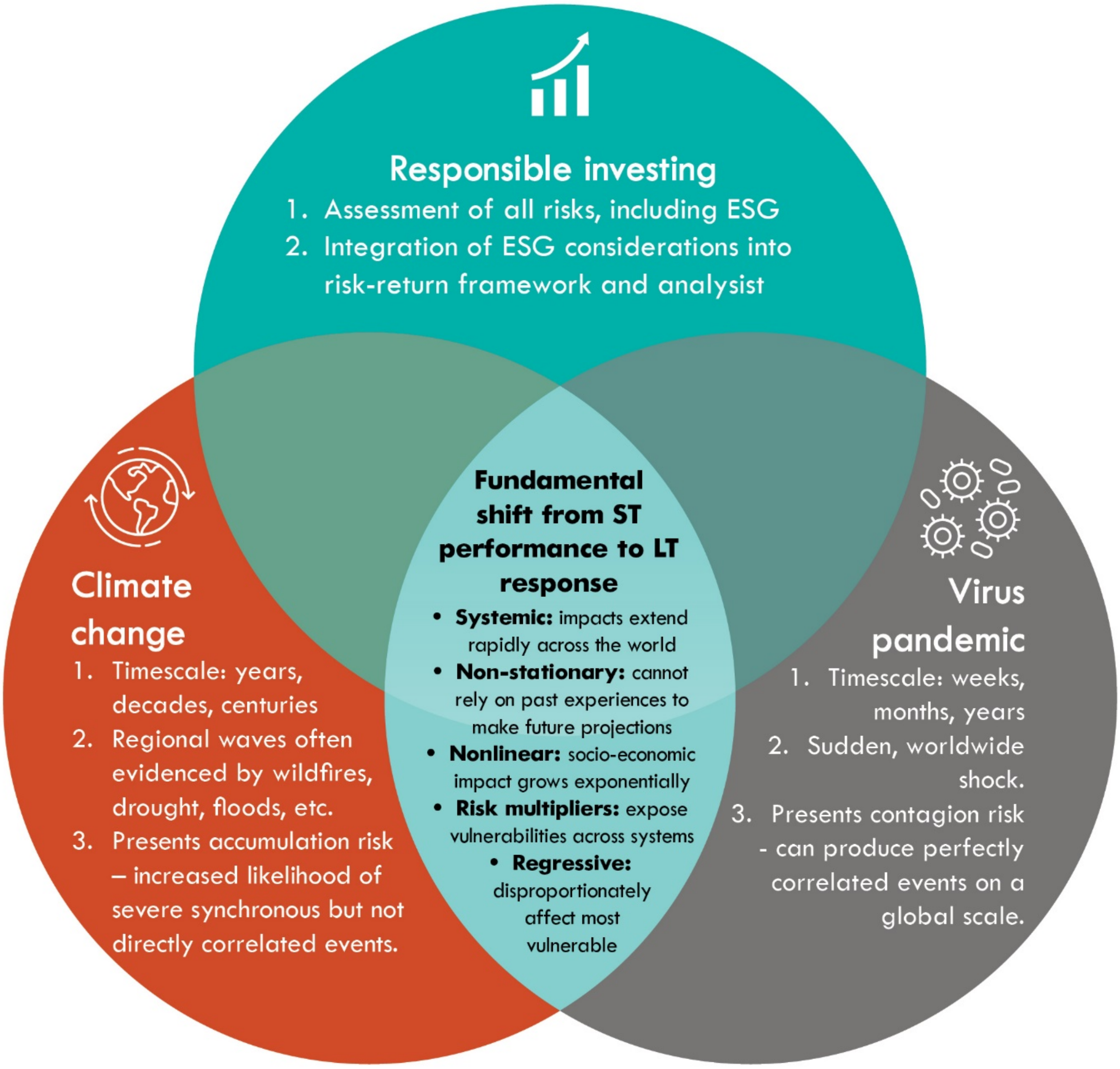
Crises don't create, they reveal
While the exact origin of the COVID-19 virus is yet to be scientifically established, the World Economic Forum estimates that 60% of infectious diseases originate from animals, and 70% of emerging infectious diseases originate from wildlife. Scientists have found that between two and four new viruses emerge annually as a result of human infringement on the natural world and the vast illegal wildlife trade.

Pandemics, therefore, are often a hidden side effect of economic development and inequalities that can no longer be ignored, and illuminate the devastating ripple effects when one element in an interconnected system is destabilised. Just as carbon is not the actual cause of climate change, it is often human activity – rather than nature – that causes pandemics.

The spread of the coronavirus pandemic has emphasised the global interconnectedness of all stakeholders. Parties now have to collectively grapple with the real-time implications of how non-financial risks (in this instance, a global public health crisis caused by COVID-19) translate into significant financial risks.

The interconnectedness of climate change and virus pandemics
The recent collective experience, whether in the public or the private sector, has more often been shaped by financial shocks rather than physical shocks. The pandemic has shown just how far-reaching and cataclysmic a shock of this magnitude can be – and what we can potentially expect from future crises.

As can be seen in the Venn diagramme below, climate change and virus pandemics share several defining features.



Source: McKinsey, adapted by Futuregrowth Asset Management

Both virus pandemics and climate change require a fundamental shift in response: from optimising primarily for the shorter-term (ST) performance of systems to ensuring, equally, their longer-term (LT) resilience through investing responsibly. As a responsible investor and custodian of clients' funds, we have a responsibility to assess all risks, including non-financial risks, i.e. environmental, social and governance (ESG) risks when we make our investment decisions.

Transitioning from sustainability to resilience
While COVID-19 represents a global growth and fiscal shock, the risks are particularly pertinent in South Africa, given elevated pre-COVID-19 unemployment rates and fiscal strain. Locally, our main concern regarding the bond market remains the strong link between lacklustre economic growth and a weakening fiscal position. The impact of the recent COVID-19-related events elevates this concern considerably.

Policies that are put in place to build economic resilience should have a strong focus on predominantly environmentally friendly initiatives. The most important of these would be a systematic approach to decarbonising our energy sources, but not at the expense of a host of other social imperatives such as open markets, robust institutions, economic growth, low unemployment, education, and skills development.

In the absence of a clear virus inflection point in the near term, corporate balance sheet strength and cashflow resilience remain critical measures of credit quality across the asset classes that Futuregrowth manages. In our view, the likelihood of continued operational disruptions as our economy re-opens and the inevitable second (and third) wave of infections mean that contingency planning, scenario assessment and risk management will remain an important element of business strategy and the robustness of our credit assessments going forward.

Investment industry

To address the vast inequalities that have become painfully apparent during the crisis, we will need to redefine accountabilities. Shareholder returns at all costs will, and should, give way to basic principles, such as a company's treatment of staff, suppliers and customers. Society and investors will likely become more sensitive to the quality of a corporate's response to crises and demand more accountability in future.

The investment industry, too, will need to step up to its responsibilities as long-term holders of capital. While sustainability has at long last entered the mainstream, we are far from a world where all investors fully, meaningfully and consistently consider and appropriately price for ESG risks. This must surely change and, when we emerge from this crisis, the AC world that awaits us demands that responsible investment is the only acceptable norm.

Conclusion

During the 2008 financial crisis, sustainability shot to the top of the agenda in the investment industry. The current pandemic clearly shows that we haven't done nearly enough since then to improve the resilience of our financial systems, economy, health services and physical environment.

This crisis is going to reshape the world fundamentally and will, no doubt, have long-lasting effects on the global economy and societal behaviour. These structural shifts could leave the global economy even more vulnerable to other crises down the line; or we could choose to build a better, more resilient economy that puts us in a far stronger position to survive the next crisis we face.

By continuing to collaborate and coordinate our actions, the public sector, private sector and communities have an opportunity to reimagine a more sustainable way forward for the world. We believe responsible investing can play a crucial role in bringing this vision to life, while maintaining a long-term focus on investment decision-making. It will be critical in the weeks and months ahead that we leverage the power of collaboration to ensure that the standards of engagement on these key issues are not dropped during this crisis.

This article has been adapted for third party use. The original article can be viewed on the Futuregrowth website.

Sources

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