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MAKING ALTERNATIVE MAINSTREAM: FINANCING FOR A SUSTAINABLE FUTURE

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Futuregrowth supports efforts to increase awareness among retirement funds of the alpha-adding potential of the alternative investment space - in particular the infrastructure sector - as well as the role the retirement fund industry can play in promoting economic growth while generating risk-adjusted returns.

This is facilitated by creating an enabling environment through legislation for retirement funds to invest in infrastructure and related assets, with a 35% unlisted asset allowance and a 45% total cap on infrastructure investments for funds to invest in these possibilities under Regulation 28. Importantly, infrastructure investments must fit into an established asset allocation plan, whether in debt, equity, or property. These investments usually have a lengthy lifespan and serve as a natural asset/liability match for retirement savings. Retirement fund returns must be offered on fully commercial terms to provide investors with sound risk/return characteristics. Similarly, subsidised finance can play a role in making some transactions bankable, but only through so-called Development Finance Institutions (DFIs).

For institutional investors to access infrastructure investments, government first needs to address the infrastructure finance gap, which is expected to be approximately R1.9 trillion over the next two decades and includes a wide variety of infrastructure and development projects. The private sector (which also represents institutional investors), alongside government, can play a vital role in reducing the gap – but, ultimately, legislation can only go so far and bankable deal flow is a requirement to feed the market. It is important that funding is based on achieving commercial risk-adjusted returns and sustainable long-term outcomes for our clients.

Some success stories

The long-term viability of these deals depends on a clear and concise government policy that addresses how budgeted money is utilised across all departments of government. We are seeing some success stories emerge from the establishment of Infrastructure SA and the Infrastructure Fund under the Development Bank of SA, but more can and should be done. Another example is South Africa's successful Renewable Energy Independent Power Producer (REIPPP) programme, which has been running for the past ten years, and its planned reform of the power sector and transition to cleaner energy, which has received international recognition and significant support.

South Africa's REIPPP programme is a prime example of a successful public-private partnership, which afforded Futuregrowth the opportunity to invest in renewables, and thereby support innovative technologies that will enable a transition to clean energy. Futuregrowth's Power Debt and Infrastructure funds have more than R8 billion invested in 31 renewable energy projects that use a variety of technologies ranging from wind power, solar PV, and solar CSP to hydropower.

COP27: A call for innovative climate finance

Much hope and expectation were placed on the recent COP27 event held during November 2022 in Sharm El Sheikh, Egypt, as world leaders convened to address the critical climate challenges facing us, recognising that climate risks are pervasive, and their effects are felt across global economies and ecosystems.

Day four of the convention - labelled "Finance Day" - was a call for innovative climate finance solutions that support sustainable initiatives and promote a transition to a low-carbon economy. Each year a significant amount of investment capital is required to achieve national net-zero emissions targets. During the discussions, it was acknowledged that for emerging nations to reach their 2030 ambitions and near-term climate financing goals, there is a need to significantly accelerate capital investment into these countries. To address the funding gap, particularly in African nations, Egypt's COP27 Presidency announced a finance initiative that will enable African countries to borrow money at an affordable rate, mobilise more green funding, and draw in private capital.

A positive development in support of this was the announcement that France and Germany would contribute €600 million to South Africa to support its transition away from coal as part of a Just Energy Transition Partnership (JETP). According to Ismail Momoniat, Acting Director-General of the National Treasury, "*While South Africa still requires more support for its Just Transition path, considering the scale of the required transition in the context of the current socio-economic challenges of high unemployment, high level of poverty and inequality, this funding will assist in addressing the challenge of financing the critical adaptation and mitigation programmes and supporting a resilient, sustainable, and inclusive growth*".

Concessional loans like these will assist South Africa to reduce its escalating debt costs. Despite this injection, a 44% funding deficit will remain (equivalent to R700 billion) if South Africa is to reach its decarbonisation ambitions by 2030. There is understandable scepticism about the country's capacity to implement the JETP investment plan. Added to this is the daunting reality that the power sector in South Africa is facing an unprecedented electricity supply shortage, compounded by Eskom's declining generation due to increasingly unreliable coal plants, and soaring electricity prices - factors that are all taking a huge toll on the economy. The JETP investment plan will

require a public-private sector partnership to support innovative financing methods for project and green finance. This will provide more opportunity for retirement funds to access a variety of alternative investments.

Local impetus

Government has announced a R300 billion investment pipeline with a potential 19 green hydrogen projects for accelerated development, which is also promising. This falls under South Africa's Green Hydrogen National Programme, which is recognised as a Strategic Integrated Project for rapid development under the country's Infrastructure Development Act.

As asset managers, it is our fiduciary duty to act in a responsible manner when making investments, as allocators of capital into sustainable businesses that enable us to produce long-term, commercial returns for our clients while minimising risk. This includes assessing both financial and non-financial (i.e., climate-related) risks, as part of our investment process, and integrating such considerations into a risk: return framework. This includes supporting the transition to a low carbon economy and related infrastructure projects, in a way that will drive the significant economic and social development that our clients and stakeholders want to see, while helping combat the challenges of climate change.

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