BRIEF FEBRUARY 2022

INVEST SALONE

FAQ: The promise of environmental, social and governance (ESG) investment principles for Sierra Leone

What are ESG principles, and how important are they?

More investors every year, around the world, are applying ESG principles to their investments. The language of ESG overlaps with older principles like sustainable investing, impact investing and socially responsible investing, but puts the focus on three crucial areas: the environment, social well-being and good corporate governance. For example, a company may meet environmental criteria by using renewable energy, limiting pollution and preparing carbon and sustainability reports. It may meet social criteria by ensuring the occupational health and safety of employees and protecting communities impacted by its operations or by documenting an ethical supply chain. And it may meet governance criteria through instituting board oversight, committing to corporate transparency and ensuring diverse leadership.

Because these principles help investors fulfil their commitments and values while also mitigating concrete financial risks, ESG investing is growing incredibly fast. In the US, investments under ESG principles stood at US$17.1 trillion in 2020, having risen more than US$5 trillion in just two years. One-third of all professionally managed investments in the US are now guided by ESG principles. Commentators like Bloomberg expect this ratio to scale to the global level in the next few years.

> *Global ESG assets are on track to exceed $53 trillion by 2025, representing more than a third of the $140.5 trillion in projected total assets under management. A perfect storm created by the pandemic and the green recovery in the U.S., EU and China will likely reveal how ESG can help assess a new set of financial risks and harness capital markets.*
>
> ***– Bloomberg Intelligence, February 2021***

What did COP26 mean for ESG investment?

Climate finance is a major part of this wave of ESG investment, and the climate conference COP26, which took place in Glasgow in November 2021, undoubtedly added momentum when it set finance as one of its four overarching goals. The conference took countries to task for their unmet promise to mobilise at least US$100 billion a year in climate finance by 2020, and called on all financial institutions to “work towards unleashing the trillions in private and public sector finance required to secure global net zero” in carbon emissions.

The final Glasgow Climate Pact noted “with concern that the current provision of climate finance for adaptation remains insufficient to respond to worsening climate change impacts in developing country Parties.” The Pact therefore also called upon “multilateral development banks, other financial institutions and the private sector to enhance finance mobilization in order to deliver the scale of resources needed to achieve climate plans, particularly for adaptation”.

Is the ESG wave an opportunity for Sierra Leone?

Right now, 90% of the sustainable investment market is in North America and Europe. International investors perceive developing countries to be less transparent and riskier in ESG terms. These risks are real: Moody’s recently calculated that 60% of developing countries’ sovereign credit ratings are now negatively affected by ESG factors and risks, including climate change. This means that those who lend to developing countries now face greater risks of default due to worsening environmental, social and governance risks experienced in those developing countries. Mitigating those risks therefore ensures that investors will face better returns and more capital will flow in search of these better returns into countries that mitigate these risks.

Climate-related losses are certainly a concern in Sierra Leone, where models project an escalation in the already ever-present risks of crop failure, more intense rainfall, decline in water quality, greater infectious disease burden and damage to coastal infrastructure. These, however, are not just risks but very strong reasons to invest in adaptation now. As ESG standards continue to develop in a climate adaptation context, it is important that Sierra Leone does not get left behind. There is a significant opportunity for the country to take the lead and position itself as an ESG investment destination.

While COP26 was taking place in Glasgow, a side event in Freetown organised by Invest Salone brought the country’s finance sector together to discuss that opportunity. The roundtable welcomed a joint declaration of action on ESG guidelines from the Sierra Leone Association of Commercial Banks (SLACB) and Bank of Sierra Leone (BSL). Such guidelines would pave the way to a more competitive banking sector and support Sierra Leone’s green growth by unlocking sources of capital ringfenced for environment- and climate-related investments.

> *“Today’s investors are increasingly allocating capital based on ESG considerations. By contributing to an enabling environment for green investment and innovation, this initiative from SLACB and BSL will send an important signal to the world about our intention to deliver green and inclusive economic growth.”*
>
> ***– Aina Wright Moore, President of SLACB and Managing Director of Ecobank Sierra Leone***

How can ESG principles open up private finance?

Most finance to fill infrastructure gaps in Sierra Leone and other developing countries has come from multilateral development banks, which are increasingly raising ESG compliance criteria to the level of core requirements. This is reason enough for Sierra Leone to become a leader in ESG, but the benefits do not end with traditional development finance nor just with infrastructure. ESG also opens the door to private finance to fill gaps in financing agriculture or manufacturing, such as:

- **Impact investors**, who have specific ESG criteria related to their mandates and are willing to work with companies to ensure they can meet them.
- **Carbon offset markets**, likely through voluntary schemes at first and potentially mandatory markets in the future.
- **Insurance markets**, with the potential to link with international reinsurers and provide agricultural or catastrophe products.

The Invest Salone programme is supported by UK aid but the views expressed in this leaflet do not necessarily represent those of the UK government.

SUPPORTED BY: UKaid from the British people