

# The Briefing Report

ESG's impact on the fund industry

## What's it all about anyway?

What is the real goal of ESG investing? Is the prime motivation to get the best possible risk adjusted return? Or is it to make a positive difference to the world – with an important, but secondary, reason of getting a good return?

Many of its most avid proponents claim that ESG investing boosts risk-adjusted investment returns. They say that at its best ESG provides 'positive' alpha. 'Voluminous research has shown conclusively that businesses properly integrating ESG factors into their plans are typically more successful and profitable,' former US Vice President Al Gore stated in a June 2020 Wall Street Journal op-ed.

This may not be correct. But that doesn't mean that the underlying rationale for ESG investing is debunked. What experts in Modern Portfolio Theory, and the like, fail to understand is the motivation of many, if not most, ESG investors - institutional and retail.

But first, do the claims of Al Gore and many others who state that ESG provides investors with 'positive' alpha hold up?

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## The EU's ESG protectionism

The EU's proposed carbon border tax has given rise to very many angry charges of protectionism around the world. And the EU's SFDR, which prevents non-compliant third country funds being distributed in Europe, is also said to be protectionist.

The European Commission has put forward plans for the world's first carbon border tax, on imports of carbon-intensive steel, aluminium, cement, fertilisers and electricity.

This border levy will be phased in from 2026. It is designed to protect European industries from competitors abroad whose manufacturers can produce at lower cost because they are not charged for their carbon output. A transitional phase from 2023-25 will require importers to monitor and report their emissions.

Importers will have to buy digital certificates representing the tonnage of carbon dioxide emissions embedded in the goods they import. The price of the certificates will be based on the average price of permits auctioned each week in the EU carbon market.

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