Brexit... prepare for the worst and hope for the best

TAM Asset Management provides an overview.

Since the early 80’s regulation has become an integral part of working in the financial sector, with legislation and guidance abundantly introduced and reinforced. Regulation by stringent and diligent authorities on the one hand shows customers that they are treated fairly, and trading operates within important market rules. European regulatory development can also add a strain to existing business relationships. Brexit is not the only significant change. MiFID II was rolled out to further protect trading practices and client’s interests and increase the scope of transparency. This is the set of guidelines European regulators are using to govern companies through regulatory change. Little interest has been taken by the regulators to check implementation yet. This will follow and should not be underestimated. MiFID has some interesting nuances and opens new areas in which advisers can delve (ESG for one) and professionalises the market further. Brexit could on the other hand turn out to be a nasty wake up call for those thinking “equivalency” is nailed on. Recently we hear of bank accounts in the UK for UK expats in Europe being withdrawn… that’s drastic and smacks of preparing for the worst and hoping for the best!

If there is indeed a hard Brexit it creates the very real need for UK-based investment funds (Oeics, trusts) would immediately have two sorts of consequences, if there is no understanding in place between regulators, Brexit is not the only significant change. MiFID II was rolled out to further protect trading practices and client’s interests and increase the scope of transparency. This is the set of guidelines European regulators are using to govern companies through regulatory change. Little interest has been taken by the regulators to check implementation yet. This will follow and should not be underestimated. MiFID has some interesting nuances and opens new areas in which advisers can delve (ESG for one) and professionalises the market further. Brexit could on the other hand turn out to be a nasty wake up call for those thinking “equivalency” is nailed on. Recently we hear of bank accounts in the UK for UK expats in Europe being withdrawn... that’s drastic and smacks of preparing for the worst and hoping for the best!

Confidence in a solution that allows equivalency to the problems impact is still not obvious; however, the financial landscape is changing. MIFID II is here potentially thousands (or hundreds of thousands) of variables can be accounted for. It’s no wonder, therefore, that there is an absence of an ‘‘ideal solution’’ and a degree of uncertainty as to the best path to follow.

Kevin’s initial thoughts are:

Entering into the world of ESG is like opening Pandora’s box. Any newcomer, or indeed seasoned professional, is confronted by a plethora of standards purporting to be effective measures of E, S or G – or all three. At the same time, one is left knowing that none of these standards actually provides the answers to the specific circumstances one is dealing with. This is not entirely surprising given the potentially endless list of variables that can have a bearing on any company’s ESG rating. The 17 UN SDGs, for example, have some 197 variables that may be accounted for. This pales into insignificance, however, when one takes a ‘big data’ approach: here potentially thousands (or hundreds of thousands) of variables can be accounted for. It’s no wonder, therefore, that there is an absence of an agreed ‘standard’ and a degree of uncertainty as to the best path to follow.

Companies offering to provide ESG ratings to customers are yet nascent. The bigger companies appear to be going down the road of big data – and using AI to analyse the data and draw conclusions. There are some potential advantages to his approach (its comprehensive screening of vast amounts of data) but there are also some serious limitations – two main ones being the absence of causality in correlational analysis and the sheer complexity of understanding the outputs. It may well be that these issues are overcome in time, as companies become more proficient in these matters, in the meantime, however, we are largely utilising assessments of ESG that are based on a more limited range of criteria. Indeed, this may well prove to be the future of ESG related assessments as the needs of different industries vary considerably. One size, it seems, does not fit all.

Is the search for a universal measure of ESG futile? Can big data (however sophisticated the analysis becomes) really produce meaningful real-world output? Are the UN’s SDGs an effective measure of ESG across many different sectors? Should we, instead, agree on a single measure for E, S and G (for example, E could be carbon emissions and G could be an effective independent Board of Governors)? This approach, at least, would be cheap and easy to understand. It is unlikely, however, to satisfy.

Whatever approach emerges as the one most favoured, we are still confronted with a significant problem. We may, in time, come to some agreement as to what should be measured but the next big question is how do we measure all of these things? But, it is not just a matter of how do we measure these things, it is how do we measure them economically, efficiently and effectively? Then how do we analyse these things (being reasonably confident about causality) and produce output that really understands.

We are a long way from providing good answers to these questions. For the moment, the important thing is that we are on a journey, individually and collectively, towards answering these questions.

The admission of Sustainable Capital plc to the NASDAQ Sustainable Bond Network is part of BRC’s ESG compliant investment platform. As market leaders in our field we are developing a growing competence and confidence in our approach which will include ESG traffic light system for future issuances to assist advisers in understanding and providing a clear path for their clients’ investment objectives. If you would like to talk to us about our approach please contact Kevin.haines@bedfordrowcapital.com For more information on Sustainable Capital PLC, email ir@sustainablecapitalplc.com or Global Head of Business Development Chris Kruecken (chris@bedfordrowcapital.com)