

Consider this

Sustainable investing: Understanding SA's water crisis on the ground

January 2024



Anthony Walker
ESG Manager at M&G Investments

As part of M&G Investments' commitment to an active and sustainable investment approach, we closely examine the environmental, social and governance (ESG) risks and other considerations associated with the companies in which we invest. We consider the longer-term requirements for a company's sustainable operations, and the impact their business has on the environment, while collaborating with them and other groups (such as outside experts) to understand their challenges and concerns when it comes to ESG issues. In the past 18 months we have engaged often on the topic of water scarcity, which is becoming one of the more prevalent challenges faced by South African companies and municipalities. There is a great need to overcome these water shortages, despite a lack of municipal funding in many areas of the country, and despite the unpredictability of climate change. All stakeholders – companies, governments, individuals, investors – need to be aware of the risks; they are becoming an increasingly serious concern that we are taking into consideration as we approach a water crisis in South Africa and southern Africa more broadly.

Water shortages are an increasing reality in South Africa

Southern Africa is expected to be particularly severely impacted by climate change in the coming years, becoming both hotter and drier than other regions and resulting in unprecedented water shortages. Since 2015 droughts have become more common and severe in South Africa – evidenced by Cape Town's "Day Zero" in early 2018 and further crises in Nelson Mandela Bay and other areas of the Eastern Cape. By contrast, KwaZulu Natal has been experiencing more erratic rainfall, and discussions with operations managers of water suppliers in this region indicate they expect this to be an ongoing trend. Meanwhile, from an operational perspective we have seen failures of water provision of significant scale in parts of KwaZulu Natal and Johannesburg of late. These failures have at times extended to weeks of non-provision, with a devastating impact.

Local and provincial governments do have plans to improve both the quantity and quality of our water supply, including rolling out more dams, tapping aquifers, improving treatment plants and introducing more desalination. However, for most of these regions, studies show that these plans are not adequate, due largely to the perpetual issue of funding shortages. Meanwhile, municipalities with significant mining operations appear to be increasingly reliant on the miners themselves in terms of water provision, generating potential dependency relationships. The current available plans for South Africa's large metropolises indicate only Cape Town is on track for adequate water supply beyond 2035. With the lead times involved in such projects, the possibility of future water shortages is a very real concern, even without the potential for climate change to exacerbate extreme weather patterns that magnify failures of infrastructure and investment.

In terms of our investment approach around water issues, much of our engagement centres on urging companies not to assume a stable water supply in the future, to be aware of systemic pressures in the municipalities in which they operate, and the levels of mitigation (and related costs) that they may need to incur. Our engagements with miners also focus on water usage, rehabilitation, licensing issues, etc. For example, we are engaging with one company on their proposed initiative to use indigenous plants and wetland areas for rehabilitation that also carry the benefits of trees for water treatment for the uptake of heavy metals from a mining operation.

Mining and chemicals are currently the sectors most in focus for the most immediate water risks. Not only is supply to the companies' operations a risk, but in some cases the supply to the mining staff and communities becomes dependent on the mine propping up supply. We are increasingly seeing public-private sector 'partnerships' to this end. We also understand there are instances where, when miners fail to help with water supply, communities end up damaging the water supply and place themselves at risk of drinking non-potable water. Management of wastewater at mines is another complex challenge, where failures, even from illegal miners, bring liabilities and risks to mining licences.

More specifically, in our interactions with our investee companies we aim to understand what approach and actual work related to water risks the company has undertaken in the following areas:

- 1. Governance, risk and accountability:** Are there genuine structures in place to monitor water risks, and are there defined roles of accountability? As a minimum requirement – has work on water at least started?
- 2. Meaningful data:** Is the entity gathering meaningful and useful data on water, or is it just gathering and reporting data? Is it gathering data at all the right points of its processes?
- 3. Milestones are more important than policies:** Is the company meaningfully progressing its water plans? We would be concerned if there are simply policies and risk processes in place without being backed by credible milestones and movement.
- 4. Mitigation plans:** Does the company have the ability to mitigate its water risks, and if so, then at what costs and on what timeline?
- 5. Municipal plans matter:** Does the entity simply trust future municipal supply plans, and has it studied these and understood them for context and reliability?

Talbot Water Roadshow 2023

One example of our water-related engagements in the past year involved the Talbot Water Roadshow. We partnered with Talbot, a large water consultancy and testing group, and participated in a nationwide roadshow focusing on the current material and increasing risks related to water availability in South Africa. The roadshow included presenting to, and having discussions with, large water users such as Sasol, as well as those with water vulnerabilities like miners in arid regions. Our key objective was for our ESG Specialist, who was a speaker, to illustrate to companies what asset managers are looking for in terms of a company's objectives around water, risk monitoring, governance structures, and data.

We presented at the roadshows and participated in an open-floor discussion in Johannesburg. The discussions showed that companies are increasingly concerned about water security and the ability of provincial and municipal governments to supply reliable water to their operations. We are also increasingly seeing this concern among a range of entities with diverse operations in different geographies.

Many of the companies attending were listed, and either existing or potential investee companies for M&G. Participants included Exxaro, African Rainbow Minerals, Harmony Gold, Omnia, Sasol, Oceana, AECI, Sibiya and Distell. In Johannesburg, we hosted around 80 attendees representing some 60 companies. There was lively debate among the participants, with quite a lot of transparency around mining groups needing to prop up rural municipal water supplies and sharing of common concerns. The Cape Town event had approximately 50 people in attendance, including experts such as the drafter of the Green Drop and Blue Drop national water and effluent reports, and some leading consultants and water academics. This also helped turn this event into a meet and greet for people with similar concerns, putting experts in touch with one another for collaboration on an industry level.

Glencore

Glencore was another entity we recently engaged with on water supply related to their La Guajira operations in Colombia. This has been a priority issue for the company, having conducted some remarkable work in the region in terms of the rehabilitation and use of water supplies and monitoring. As a result of its intervention, flows of a key river in the area have improved significantly, the strength of which has not been seen for several years, in turn supplying additional water to the local community and Glencore operations.

The company has been working closely with communities and local government in the La Guajira area to help source more supply and improve the distribution of water, even distributing it to some areas by rail. There is recognition that a long-term solution is critical, given that water supplies must be sustainable even after the mining operations have

ceased. This has been a complex challenge given the mix of issues (mine licensing, elections, lack of government funding and the community politics of water), and shows that public-private partnerships are becoming increasingly important in providing solutions in poverty-stricken regions in South America, just as in South Africa. Even in areas where the regulatory and political environments can be volatile, miners are increasingly committed to helping where governments cannot, and governments recognise the necessity of working together despite conflicts of interest. At M&G we are monitoring Glencore's progress and see La Guajira as a good example of what can be achieved with cooperation between all parties.

Flowing forward

Strain on water systems, both locally and globally, is expected to increase in the coming years. In fact, should the widely expected shift from La Nina to El Nino manifest this year, we could very soon see further testing of water reserves in South Africa and elsewhere.

At M&G we anticipate having more engagements with municipalities and water suppliers in 2024. Water losses in several South African metropolitan areas are becoming even more concerning as infrastructure crumbles and water is wasted even within the existing systems -- it is no help if the water supply is managed, but the resource is lost in delivery.

We are excited to see that, besides employing known solutions for coping with water scarcity, some local mining companies are exploring innovative methods around water usage and treatment involving wetlands and other ecosystems, which are also being tested overseas. Currently we are bolstering our own knowledge in this area by studying existing research to better understand the feasibility and ongoing sustainability of such projects – this will also be an area of focus for the M&G ESG team in 2024.

Working towards improved sustainability

In conclusion, when it comes to sustainable investing, investors may not have a full picture of the activities of investment managers, since much of it happens behind the scenes. The hard work of uncovering valuable ESG information is done through detailed conversations and data sharing, and requires study and experience to understand. It is seldom in the news. However, it is taking place consistently at M&G Investments, with myriad engagements to ensure we uncover all the risks associated with an investment. Even more importantly, we are working every day to help improve the sustainability of our own company, our investee companies, and the communities we impact. For more information on our activities and progress in this area, read our recently released [Sustainability Report 2022/23](#).

Disclaimer.

This document is for information purposes only and is not an offer to or solicitation for investors to invest in any of the capabilities or products offered by MandG Investment Managers (Pty) Ltd [M&G Investment Managers] (Registration no. 2013/051515/07) and MandG Investments (Namibia) (Pty) Ltd (Registration no. 1996/85) [M&G Namibia] or any of their associates, being MandG Investments Unit Trusts South Africa (RF) Ltd (Registration no 1999/005242/06) and MandG Investments Unit Trusts (Namibia) Ltd Registration no. 2007/609. M&G Investment Managers is an authorised discretionary financial services provider by the Financial Sector Conduct Authority of South Africa [FSP45199] in terms of the Financial Advisory and Intermediary Services Act, and has its registered offices at 5th Floor Protea Place, 30 Dreyer Street, Claremont, 7708. M&G Namibia is an approved person in terms of section 4 of Stock Exchanges Control Act and has its registered offices at 6 Feld Street, Windhoek, Namibia. Information given in this document has been obtained from, or based upon sources believed to be from an accurate and timely source but M&G Investment Managers and M&G Namibia make no representations or warranty, express or implied, with respect to the correctness, accuracy or completeness of the information and opinions. This information is not intended to constitute a basis for any specific investment decision. Investors are advised to familiarise themselves with the unique risks pertaining to their investment choices. Investors should seek the advice of a properly qualified financial consultant/adviser before investing. The value of an investment will fluctuate and past performance is not necessarily an indication of future returns.