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Opalesque Exclusive: EM Capital seizes opportunities and challenges in ESG investing in emerging markets with new fund

Benedicte Gravrand, Opalesque London:

Environmental, socially responsible and governance (ESG) investing in BRIC (Brazil, Russia, India and China) and emerging market (EM) countries is important, according to Seth Freeman, CEO and CIO at EM Capital Management, a California-headquartered fund manager that specialises in emerging and frontier markets. He was speaking at the [Jetfin](#) conference "BRIC 2010" in Geneva on 13th April.

"We are really at the tip of the iceberg in terms of EM development," he said.

BRIC economies are projected to account for approximately 50% of global GDP by 2050. Indeed, a Goldman Sachs' report called "Dreaming with the BRICs: The path to 2050", noted that "the key assumption underlying our projections is that the BRICs maintain policies and develop institutions that are supportive of growth."

As for ESG investing, Standard and Poor's reported that "corporate governance remains one of the most important factors constraining the BRICs' attractiveness to foreign capital providers and, in particular, potential long-term shareholders." On the plus side, recent studies debunk belief that ESG investments implicitly provide lower returns than conventional analysis.

Opportunities can be found in the many EM sustainable and "green" funds but there are still few integrated ESG products.

Opportunities in ESG BRIC/EM investing are exploited by institutionals, endowments, foundations and HNWIs that are establishing specific SRI/ESG allocation policies. As the largest EM markets, BRICs are the natural recipients of the largest ESG allocations and engagement. As a result, many of the largest BRIC companies are now sensitive to the needs of domestic and foreign institutional investors and funds. So there is opportunity for long-term BRIC/EM investors to influence corporate and institutional development.

The challenges in BRIC/EM ESG investing include:

- Lack of independent ESG research and data providers;

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- BRIC countries (with exception of Brazil) under-report;
- Bad corporate ESG practices can be viewed as a competitive advantage;
- ESG policies and practices in BRIC/EMs need to be evaluated in the context of the specific market;
- "E" and "G" are more readily quantifiable while "S" requires subjective analysis;
- China and Russia are particularly weak in policies and practices;
- Investment managers are required to have robust in-house ESG research and analysis capacity;
- ESG managers should require access to CEO/CFO, Investor Relations, Management;
- And the investable universe is constrained by the challenges.

"The quality of reporting is generally very weak, so that's a major challenge," Freeman noted. "But good reporting is key; it counteracts many risks including reputational risks, scandals, etc."

EM Capital launching first ESG EM fund

[EM Capital](#) will soon launch its first ESG EM fund, which will have no lock-up and will issue daily NAV. It will be biased towards BRICs due to market-cap weightings. The architecture of the fund will include a team for fund research and outside consultants. The fund will have three structures: US mutual fund (long); UCITS-III (long); and Private Fund (Long/Short).

"Our approach is inclusionary," Freeman said at the Jetfin conference, "which requires access to senior management. But the challenge is having a large enough universe."

Freeman told Opalesque yesterday that the Private Fund's U.S. version will be domiciled in Delaware, and an offshore version (domiciled in the Caymans) will be launched concurrently, in late June. The mutual fund and the UCITS fund will be launched after that, pending regulatory approval.

The fund will invest in 22 countries. "It will be one of the first ESG broad EM products in the U.S.," he said.

EM Capital is still talking to accredited investors, and is well aware that investors generally only allocate a small portion of their portfolio to EMs or ESG. Moreover, socially responsible investing, while being accepted in Europe, is still not quite well recognised in the U.S.

EM Capital Management is a signatory of the UN PRI and UN GLOBAL COMPACT and a member of the Social Investment Forum.

Monday through Friday from 9 AM to 5 PM GMT).

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