



BSR Conference 2010
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Sustainable Investment in Emerging Markets

Breakout Session Summary

Wednesday, November 3, 2010 | 11:30 a.m.-12:30 p.m.

Speakers

- » **Seiji Kawazoe**, Associate General Manager, Sumitomo Trust & Banking Co.
- » **Ian Zhu**, Principal, Tsing Capital
- » **Jeremy Prepscius**, Managing Director, Asia, BSR (moderator)

Highlights

- » Sumitomo Trust launched a Chinese responsible investment equity product in March 2010. The fund has been outperforming the Shanghai 300 index.
- » Tsing Capital is a private equity company investing in Chinese clean-tech companies; it sits on these companies' boards and helps them improve their sustainability practices.
- » While Kawazoe advocated opportunities for higher returns on investments as a reason for pursuing responsible investments, Zhu emphasized risk management as a key motive.

Memorable Quotes

"We have learned that responsible investment is a great way to measure the maturity of management. It tells us that the management team is capable." —Ian Zhu, Tsing Capital

"We invest in companies that are able to put money into sustainable business practices ... and presumably that means they have better margins and higher growth." —Seiji Kawazoe, Sumitomo Trust & Banking Co.

"When there are [environmental] problems, this means there are opportunities for companies to address these problems, and we invest in these companies because we can benefit." —Seiji Kawazoe, Sumitomo Trust & Banking Co.

Overview

Prepscius kicked off the session by introducing the topic—responsible investment and managing ESG risks in emerging markets—as well as the two panelists. Kawazoe is a senior fund manager for institutional accounts at Sumitomo Trust & Banking Co. He is the head of global business development and socially responsible investing (SRI). In March 2010, Sumitomo Trust launched a responsible investment equity product focused on the Chinese market. The fund is benchmarked against the Shanghai 300 and has been outperforming the index.

Kawazoe explained that Sumitomo launched the product because the Trust is very active in the field of SRI with a broad range of products focusing on ESG factors. Also, there is growing interest in responsible investing in Japan and internationally, and companies that adopt sustainability practices will presumably have better margins and higher growth.

He then described the investment process undertaken to select the companies in Sumitomo's portfolio. A survey is made of 2,000 companies in the original universe. The survey includes 70 questions pertaining to ESG factors and a qualitative ranking is then produced through an in-house developed model. The research focuses on whether the company has policies addressing ESG issues and whether these policies are effective.



Kawazoe then exposed some of the challenges that he has faced. First, the survey must be communicated effectively and carefully, in order to be a positive driver for companies. Then the fund must perform well and beat the index. Lastly, sufficient resources must be dedicated to run the portfolio effectively.

Tsing Capital is a private equity and venture capital firm, investing in clean-tech companies in China. When introducing his firm, Zhu first underlined the long-term aspects of investing and how much has changed since the first investments were made in 2001. The fund invests in clean-tech businesses, including renewable energy, environmental protection, energy efficiency, sustainable agriculture, transportation, new materials, and carbon ventures (such as carbon capture and storage, and carbon trading).

When describing the fund's investment process, Zhu said exclusionary criteria were applied. Companies in the portfolio must deliver products that benefit the environment and that do not harm society. An extensive evaluation process is undertaken, including training as well as annual audits. Zhu engages with BSR to help portfolio companies enhance their sustainability practices. From a risk management perspective, Zhu believes that having a strong sustainability practice is a good indicator to gauge the strength of a company's management practices as a whole.

Prepscius asked how Zhu convinces his portfolio companies to adopt more sustainable practices, since Tsing Capital remains a minority investor. Zhu explained that he can have a lot of leverage in these companies because he sits on their boards. Also, ESG requirements are integrated in transactional documents when investments are first made.

A question from the audience asked Zhu if he could provide examples of companies that have turned risks into business opportunities. Zhu talked about a Chinese company that has developed an innovative biotech solution, which can turn restaurant waste—a big issue in Chinese cities—into organic fertilizer on an industrial scale.

Another question from the floor asked both speakers how they verify what the companies tell them with the reality of what is happening on the ground. Kawazoe said his firm asks organizations like BSR to inform them on the practices of companies. Zhu added that a lot of data can be found in financial statements.

Prepscius inquired about the trend of increased demand for ESG disclosure and how this affects the speakers. Zhu welcomes initiatives from U.S., European, and Chinese governments to demand more disclosure for companies, but standards should be relevant for all companies and should not be burdensome on smaller companies. For example, carbon footprinting is not relevant for all companies.

Closing remarks focused on the performance of the funds. While Sumitomo's fund overperformed the market index, Zhu said some of Tsing's funds have returned three times their original investments.

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