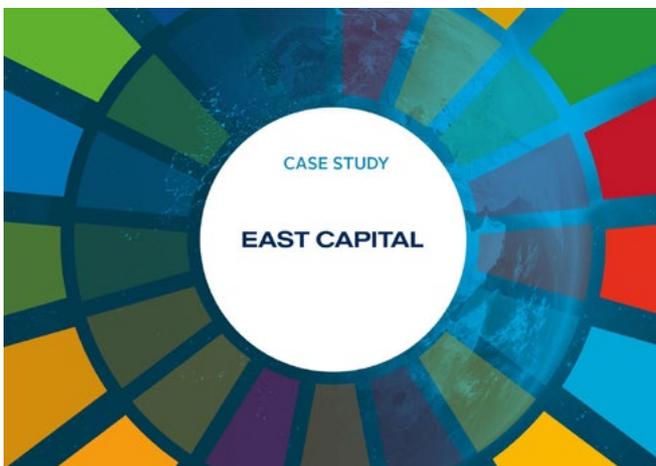




East Capital's approach to SDG outcomes



East Capital's investment philosophy is to build portfolios around reasonably valued companies with strong structural growth exposure and management of material ESG risks and opportunities. In their sustainable global emerging markets (GEMS) fund, they also use the Sustainable Development Goals (SDGs) to identify structural growth themes.

Since 2016, East Capital analysts and portfolio managers have been using a proprietary ESG scorecard.

"We find that external ESG data providers don't add much value to our investment processes, given their coverage of emerging and frontier markets is often sporadic and employs a tick-the-box approach focused on the availability of policies. We believe this hinders emerging markets companies, which are often at an early stage of their ESG journey. Our internal research leverages our local knowledge, understanding, network and track record of constructive engagement."

A key part of their ESG scorecard is a section on SDG revenue alignment, but this focus has some limitations, because:

- › it is relatively subjective for all but the most obvious companies (e.g. pharmaceutical or healthcare-related companies may immediately be deemed to contribute to the SDGs while companies producing electrical components may be overlooked without further analysis)
- › it does not necessarily represent the true SDG impact the company has (positive or negative) across its value chain
- › it pushes investors towards a narrow selection of solutions providers that are often trading at stretched valuations

Consequently, East Capital were keen to expand their ESG analysis to ensure that their investment team incorporated the analysis of SDGs more broadly.

Through bottom-up research, East Capital find many examples of attractively priced companies whose activities drive genuine and measurable SDG outcomes – from India's largest cinema chain, which has completely removed plastics in its food and beverage offering, saving up to 100k tons of plastic annually, to a Polish e-commerce company that will switch its server farms to fully renewable power by 2023.

Nonetheless, given the huge variety of companies and sectors analysed, it's difficult to incorporate our SDGs analysis in a systematic way.

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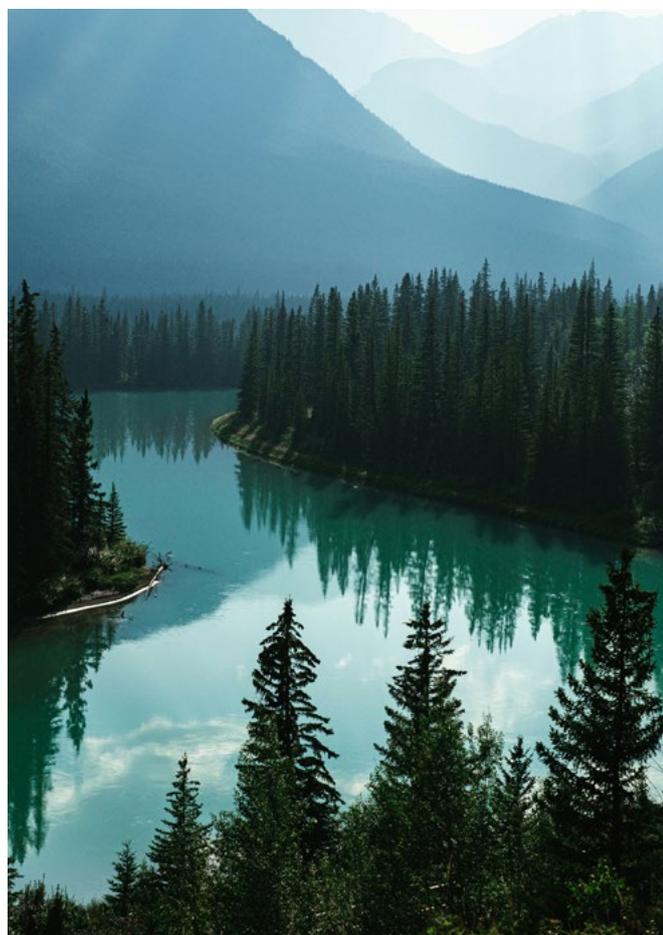
East Capital's SDG value chain analysis tool

What is East Capital's SDG value chain analysis tool?

East Capital developed an SDG value chain analysis (VCA) tool. It incorporates Sustainability Accounting Standards Board (SASB) metrics that have been mapped to the SDGs by the Value Reporting Foundation (see SASB reporting standards and sustainability outcomes below).

Example of the metrics mapped to the food retail sector:

SDG	Metric (based on SASB)
1.2	(1) Average hourly wage and (2) percentage of in-store and distribution center employees earning minimum wage, by region.
1.2	Revenue from products third-party-certified to environmental or social sustainability sourcing standards
2.1	Revenue from products labeled and/or marketed to promote health and nutrition attributes
2.2	High-risk food safety violation rate
7.2	(1) Operational energy consumed, (2) percentage grid electricity, (3) percentage renewable
8.4	Gross global Scope 1 emissions from refrigerants
8.4	Fleet fuel consumed, percentage renewable
12.3	Amount of food waste generated, percentage diverted from the waste stream



The VCA tool uses these metrics as inputs, combined with SDG revenue alignment analysis across the value chain, as described in this process:

1. Use a combination of revenue alignment and SASB materiality mapping and metrics to identify the two most important SDGs for a company.
2. Assess how the company's activities (including its value chain) have impacted these SDGs over the last one to three years and how we expect them to do so in the next three to five years. The latter often requires dialogue with companies as guidance on non-financial metrics/target setting is fairly limited in general and even more so within emerging markets.
3. Based on the assessment, apply a simple five-point rating system: strong positive impact, weak positive impact, neutral impact, weak negative impact, strong negative impact. Use the four principles identified below to determine the impact a company has on the SDGs identified and assign a rating – activities meeting one or two of these principles would be given a weak positive impact rating whereas those meeting three or four would get a strong positive impact rating.
4. As part of SFDR Article 9 obligations, East Capital also look at whether the company's activities are significantly misaligned with any of the SDGs.
5. The company is then given an overall score, based on a simple weighted average of the four impact assessments – 100 is given for strong positive impact and 50 for weak positive impact.

Impact assessment criteria: the four principles

Principle	Question
Materiality	Are the impact categories material to the company's business?
Intentionality	Does the company intend to have a positive impact through its products or services?
Additionality	Does the service/product offer a tangible sustainability benefit that would not have otherwise occurred, i.e. does the company go beyond industry norms?
Criticality	Is the product or service critical to accomplishing a particular sustainability aim?

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Embedding the VCA tool into the investment process



Embedding the VCA tool into the investment process

East Capital have started embedding the VCA tool into their investment process and have already used it to make portfolio decisions. They have divested two companies in the GEMS fund because their scores were too low and have added exposure to one company because it received a high score, and they found the valuation and fundamentals sufficiently attractive.

They have also used the tool to identify engagement opportunities, especially highlighting to companies the importance of setting clear and metric-based sustainability-related targets that should filter through to management KPIs.

In the coming months, East Capital plans to fine-tune a more formal system, where company impact scores will directly feed into portfolio construction, based on a minimum threshold. They already employ such an approach with their ESG scorecard – companies usually require a score of 70 to enter the GEMS fund.

They also want to use the tool to generate clear and insightful data on the SDG outcomes of investments. This is challenging, however, due to the industry-wide lack of data and the wide variety of positive and negative SDG outcomes.

While they already report on some portfolio-wide metrics, including carbon intensity, gender diversity at board and senior management level and – where the data allows – water usage, others are less broadly applicable. For example, for food retailers, careful management and control of food waste is one of the most material metrics we would look for (SDG12 – Responsible consumption and production), though this is not something they would expect companies in other sectors to report on.

SASB reporting standards and sustainability outcomes

The [SASB reporting standards](#) identify 12–14 material and largely outcome-based sustainability metrics per sector. The Value Reporting Foundation has broken these into 77 sub-sectors, making them highly specific and relevant. They provide our analysts and portfolio managers with a ready-made list of the outcomes to look for when assessing a company's broader SDG alignment.

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SDG VCA analysis example

Example: Assessing an Indian telecoms company using VCA

A significant part of Airtel's revenue comes from providing mobile phone coverage to rural areas of India, including reasonably priced 4G services, India has the lowest data costs in the world at US\$0.09 per GB of data.

As we have seen first-hand when travelling in emerging markets, phone and internet access can have a transformational impact on people's lives, providing access to work and educational opportunities as well as the formal financial system.

Airtel's activities are clearly supportive of SDG 9 – Industry, innovation and infrastructure, particularly 9.1: *“Develop quality, reliable, sustainable and resilient infrastructure, with a focus on affordable and equitable access for all.”* However, this is primarily because Airtel is a telecoms company, rather than having a specific focus on generating a positive impact. Consequently, East Capital gave them a weak positive impact ranking both for their current activities and outlook, as they do not expect this to change in the future.

Given Airtel is primarily a network operator, East Capital identified SDG 12 – Responsible consumption and production – as most material, given it includes many metrics regarding energy use.

Airtel has made significant strides in this area, largely through network upgrades, with a 97% reduction in network emissions intensity from 2015 to 2020. It is targeting net-zero emissions by 2050 and – more importantly – targeting eradicating diesel consumption by 2030.

Given these intentional steps, East Capital gave Airtel a strong positive impact ranking for the next three to five years.

The overall score is based on a simple weighted average of these four impact assessments, where 100 is given for strong positive impact and 50 for weak positive impact. Airtel, a holding in our GEMS fund, scored 63.

Assessing Bharti Airtel using the SASB-based VCA tool¹

		
<p>How have the company's activities (including its value chain) impacted this SDG in the last one to three years?</p>	<p>Weak positive impact:</p> <ul style="list-style-type: none"> • Key provider of mobile phone access to rural areas in India: 169 million rural customers in 2020 vs. 127 million in 2017. • Instrumental in rolling out 4G in India - reaching 95.4% coverage of India's population in 2020. • Key provider of home broadband (111 cities), which enables critical connectivity, especially during the COVID-19 pandemic (working from home, home schooling). 	<p>Weak positive impact:</p> <ul style="list-style-type: none"> • Through improving technology, the company has achieved a 97% reduction in network emissions intensity from 2015 to 2020: 8.4tCO₂e/terabyte in 2015, 0.99CO₂e/terabyte in 2018, 0.217CO₂e/terabyte in 2020.
<p>How do you expect the company's activities (including value chain) to positively impact this SDG in the next three to five years?</p>	<p>Weak positive impact:</p> <ul style="list-style-type: none"> • Roll-out of 5G services across India in the coming five years. • Reduce annual customer churn rate by 20% by 2023 (2019 as a baseline, which was 7.1%). 	<p>Strong positive impact:</p> <ul style="list-style-type: none"> • Achieve net-zero carbon emissions by 2050. • Eradicate diesel consumption from operations by 2030 (16.3 million litres consumed in 2021, up from 15.0 million in 2019).
<p>Is the company's activities or value chain misaligned with any of the SDGs?</p>	No	
<p>Overall impact score</p>	63	

1. Source: East Capital

Additional resources: [Assessing SDG outcomes across the value chain \(Chinese translation\)](#)