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Impact with alpha: starring emerging markets private equity

JULY 26, 2020

As [reported last week](#), impact investing is starting to make a dent in NZ with a rash of new funds coming to market this year.

But while NZ investors are, for now, looking to make a difference (and money) in their own backyard, the wider world holds a much deeper set of opportunities for problem-solving impact strategies.

According to Steven Cowan, co-founder of US-headquartered private equity firm [57 Stars](#), emerging markets, in particular, offer a unique combination of financial and impact 'alpha' that enables investors to "do good" and make attractive returns.

Aside from the superior general growth potential (that comes with higher risk) compared to the developed world, emerging markets are over-weight in global issues such as poverty, pollution and poor health.

"You get more impact bang for you buck in emerging markets," Cowan said. "If you're concerned about poverty and financial inclusion, for example, then it makes sense to invest where the most challenging and acute problems exist."

"And while the environmental challenge is a global one, it is particularly acute in the places we invest."

However, he said investors shouldn't have to give up returns in lieu of achieving impact goals.

"We're not comfortable with the concessionary approach," Cowan said. "We believe that the returns from impact strategies should be identical to our other [emerging markets private equity investments]."

Due to visit NZ just before the COVID-19 lockdown, Cowan – along with other senior 57 Stars executives Stephen O'Neill and Carl Balit – said the US\$4 billion manager started life about 15 years ago as a private equity fund-of-funds focusing on emerging markets.

More recently, the manager built its more focused impact strategy to co-invest into a pool of underlying emerging market companies that are helping solve some of the world's most intractable problems.

The 57 Stars co-investing offer, though, is not a trendy 'pivot' to the growing impact market. Cowan said the firm has "development in its blood" with many of the senior partners tracing their origins to the US Federal Government emerging markets funding agency then-known as the Overseas Private Investment Corporation (OPIC)

At OPIC (now the International Development Finance Corporation), Cowan and other 57 Stars founders helped fund a range of projects in developing countries.

"We were impact before there was a word for it," he said.

The OPIC experience also opened up Cowan et al to the commercial opportunity for investing in emerging markets at grass-roots level.

Today, the core 57 Stars private equity fund-of-funds invests through a network of about 150 specialist managers with exposure to "several thousand" underlying companies.

The impact strategy targets a list of between 35 to 50 companies best-suited to solving some of the global problems as defined by the United Nations Sustainable Development Goals (SDGs).

Specifically, 57 Stars focuses on SDG themes of poverty, healthcare and environment. While companies in the portfolio must have a strong business case (often with a technology-based theme), the manager has also developed a robust impact measurement process.

In addition to using the third-party IRIS+ set of SDG metrics, 57 Stars has built two proprietary tools to measure 'impact profile' and the 'total impact value multiple' that estimates "the potential dollar value of a company's impacts".

Cowan said as one of the few private equity players in emerging markets, 57 Stars has unique connections and insights into investment opportunities.

Even during the COVID-19 crisis many of the firm's portfolio companies are "doing better than ever", he said.



Steven Cowan: 57 Stars co-founder

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The global pandemic has also seen some offshore money exit emerging markets, possibly reducing the competition for dedicated investors.

"Historically, there has been a dearth of capital in emerging markets private equity and the crisis has reduced that further," Cowan said. "That creates opportunities for us."

Represented in Australasia by the Sydney-based private equity specialist,

Principle Advisory Services, the 57 Stars impact strategy is starting to stir interest across the Tasman. The manager has a wide range of wholesale clients including sovereign wealth funds, pension funds (such as the large US fund CalPERS) and family offices.

Cowan said the 57 Stars crew still planned to make the trip to NZ when the borders reopen, although that may be some months away.

The 57 Stars name, suggested by co-founder Stephen O'Neill's then eight year-old son, refers to the number of key stars used for celestial navigation. Actually, the list of 57 ignores the most well-known star in nautical history, which sits right on the celestial north pole.

Polaris, better-known as the North Star, stands alone because it easily fixes latitude for navigators (longitude is the tricky one) in the northern hemisphere. Down south in NZ, of course, Polaris is not such a big deal.

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