
Event Report

2008 Social Enterprise Conference Panel: “Private Equity in Emerging Markets: Looking Beyond the Internal Rate of Return”

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On October 24, 2008, Columbia Business School’s Social Enterprise and International Development Clubs hosted its seventh annual Social Enterprise Conference. This year’s conference included the panel “Private Equity in Emerging Markets: Looking Beyond the Internal Rate of Return.” The panel discussion was moderated by Paul E. Tierney, Jr., adjunct professor and general partner at Aperture Venture Partners, LLC, and featured the following panelists: Thomas R. Gibian, founding partner, CEO and managing partner of Emerging Capital Partners (ECP); Teresa C. Barger, cofounder and CEO/CIO of Cartica Capital LLC; Cynthia Hostetler, vice president, investment funds, at Overseas Private Investment Corporation (OPIC); and Brian Trelstad, chief investment officer of Acumen Fund.

Since 2005, private equity firms have invested more than US\$108 billion in companies in emerging markets.* In countries with underdeveloped financial markets, private equity is an especially critical source of capital for companies in various stages of growth, ranging from small entrepreneurial businesses to more mature companies seeking expansion capital. While private equity in emerging markets has seen tremendous growth recently, the long-term economic and social impact of these investments is not yet widely understood. This panel explored many topics, including the evolution of the private equity industry globally, the role of the public sector in encouraging private investment and the impact of the recent financial crisis.

* Source: Emerging Markets Private Equity Association (EMPEA).

As head of OPIC’s private equity group, Cynthia Hostetler has invested more than \$5 billion in 65 emerging market funds. Her mission is catalyzing development in emerging markets where it is important to U.S. strategic interests. Interestingly, OPIC is not only one of the largest investors in emerging-markets private equity in the world but also one of only two U.S. government agencies that make a profit (the other is the Securities and Exchange Commission, which generates revenue through fines). Ms. Hostetler pointed out that private equity in emerging markets is considered a legitimate asset class in its own right for three reasons. First, the quality of fund managers has improved, and managers now have an established track record in these markets. Second, the talent level of executive management in portfolio companies has increased, as nationals educated abroad at elite universities return home to take on CEO, CFO and COO roles. Third, sophisticated blue-chip investors, such as Yale University’s Endowment, have invested in emerging markets private equity funds.

The panelists also discussed the double bottom line of their businesses—that is, the ways in which private equity investments can both generate financial returns and have a social impact by encouraging development in emerging markets. The panelists noted that a multiplier effect exists, so that one dollar invested has an impact of seven to eight times that amount in terms of overall wealth creation. Thomas Gibian of Emerging Capital Partners measures impact through job creation and the degree to which companies improve transparency and corporate governance. He also argued that in Africa, as new businesses bring efficiency to the marketplace, people’s expectations rise, which can eventually translate into a demand for more accountable political leadership. Brian Trelstad from the Acumen Fund looks to make investments with a potential for a positive and “outsized social impact” on the poor in the critical areas of health, water, housing, energy and agriculture. He measures success in terms of creating a development model that can be replicated, such as LifeSpring Hospitals, which began in Hyderabad, India, and is expanding to other parts of the country. Once these models are replicated, private-sector approaches to solving the problems of poverty will be more widely recognized as beneficial and complementary to traditional development assistance.

The panelists noted that countries’ political leaders have increasingly recognized the need for reforms to attract private equity capital. Teresa Barger, CEO/CIO of Cartica Capital, stated that governments of emerging-market countries understand that they are competing with one another to create a favorable regulatory environment for investors. She cited the example of President Alvaro Uribe of Colombia, who sought to lower the number of days needed to enforce a commercial contract in his country. He had read about Colombia’s poor ranking on that

measure in the World Bank’s *Doing Business* report. Mr. Gibian believes that leaders of many African nations—such as Uganda, Angola and Nigeria—have embraced the notion that the private sector has to be the engine of growth in the economy. Deregulatory reforms across industries are being adopted in order to encourage private investment. Paul Tierney cautioned that, despite this overall trend, investors should carefully assess the risks of investing in developing nations, particularly the risk that assets could be nationalized.

One pressing question discussed was whether the global financial crisis would act as a deterrent to investment in emerging markets. Mr. Gibian noted that it is extremely difficult, if not impossible to begin fund-raising for emerging-market investments in this environment. Ms. Hostetler added that institutional investors in particular will be reluctant to make new commitments. Ms. Barger optimistically contended that private equity investing in emerging markets will remain attractive given growth projections and relative value. The 2009 forecast for growth in emerging markets is approximately 5 percent, compared to 0.5 percent in the developed world. Furthermore, she noted that emerging-market equity is relatively cheap, trading at half the price-to-earnings ratio of stocks in the S&P 500. While the industry now faces unprecedented challenges, the panelists generally agreed that private equity investment in emerging markets would continue to remain an attractive asset class.

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