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Sustainable Investing in Emerging Market

What Are Reasons for Vietnamese Fund Companies to Take Part in Sustainable Investing?

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The goal of this study is to identify factors driving Vietnamese fund companies to engage in sustainable investing, as well as how ESG is integrated and measured. This research paper is written in the context of climate change issues, raising the importance of sustainability and the demand for sustainable investing practices as a way to reduce the worst effects.

The study used a qualitative research method in which data is primarily collected from secondary sources: business journals, newspapers, and articles. PwC's readiness survey was examined to identify factors driving responsible investors. Two Vietnamese ESG funds were also studied for a benchmark review and conclusion.

A net zero transition is underway, which has caused emerging countries like Vietnam to adopt ESG in recent years. Due to new ESG regulations, strong demand from investors, and favorable macro conditions, Vietnam represents an appealing market internationally and privately. These are some of the reasons why Vietnam receives private and international investments in its economy. Additionally, these two Vietnam ESG funds may share a slightly common ESG integration approach, but ESG performance measurement is done differently. This is because each fund company may have a different investment strategy, objectives, and requirements. It appears that the industry has not yet found the universal approach regarding ESG integration and measurement.

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Contents

1 Introduction

Recent global trends like climate change are reshaping society rapidly. Sustainable investing is growing as one of the ways to prevent the worst effects of climate change. Fund companies may invest in solutions which could reduce gas emissions and accelerate the world towards a carbon neutral economy. (TradeTalk 2022.) The growth of sustainable investing is also a response to demands by investors that fund companies should act in environmentally and socially responsible ways while also maintaining high standards of corporate governance (Mobius, Carlos & Greg 2019, 7-8).

1.1 **Topic Background**

The increase of released carbon emissions into the atmosphere is one of the reasons leading to the greenhouse effect (Nunez 2019). Instead of allowing heat to escape into space, the gas absorbs solar energy and contains it in the surface of the Earth. This trapping of heat is known as the greenhouse effect. The emission of greenhouse gas trapping would not disappear in 10,000 years. (Gate 2022, 18-19.) Today, we refer to it as global warming as it not only affects the weather and climate system, but also due to rising temperatures affecting the habitats within the natural ecosystems (Nunez 2019). A small increase of 1 or 2 degree Celsius could cause big problems (Gate 2022, 20-22).
Due to the rise of the temperature, water will evaporate into the atmosphere. Then, water vapor condenses into rain, it releases a massive amount of energy which soon becomes a thunderstorm. (Gate 2022, 26-27.) Typically, powerful storms last a couple of days; however, its effects can result in hurricanes and floods that demolish years' worth of construction work on roads, buildings, and electricity lines. (Gate 2022, 26-27.)

The world's current annual total gas emissions is 52 billion tons per year. It would cost $5.2 trillion per year to solve the climate problem as long as we produce emissions. (Gate 2022, 63-64.) Perhaps, direct access to the global pool of capital would be needed to tackle climate change risks (Karadima 2021).

An investment portfolio, no matter the size, can play a role to mitigate those risks. Fund companies can invest in firms that are researching cutting edge solutions that help the environment, and also help out other companies in reducing carbon footprint. (Trager 2022.) Fund companies may also invest in companies that invest in flood-resistant buildings that can better prevent damage from flooding, severe wind and storms (Trager 2022). This kind of investing approach can be called sustainable investing which invests for a sustainable world (NN Investment Partners 2022).

1.2 **Research Questions**

- What are the key reasons for Vietnam fund companies to take part in sustainable investing?
- How do Vietnamese fund companies integrate sustainable investing into the current investing processes?
- How do Vietnamese fund companies evaluate impact investments?

1.3 **Definition of key concepts**

Fund companies are private fund companies that pool the money from multiple investors. Each investor purchases an interest in the fund entity as an investment to the fund. Then, the fund uses that money to invest on behalf of the partners. Typically, the fund companies invest in businesses in return for equity and focus on particular industries or in firms at a certain stage. (SEC 2022.)

Sustainable investing or ESG investing is an investing strategy which considers environmental, social, and governance factors into the investment process (Mobius et al. 2019, 1-2). E (for environment) is based on a company’s or government’s contribution towards carbon emissions causing climate change, energy efficiency and waste management (Robeco 2022). S (for social) stands for the concerns of human rights, labor codes, child labor, and workplace health and safety. G (for governance) is concerned with how companies manage external stakeholders, including competitors, suppliers, shareholders and governments. (Deutsche Bank 2022.) Embedding environmental, social, and governance factors into current investment strategies enable investors to conduct more thorough evaluations and make better investment decisions. (Stobierski 2022.) In fact, companies with more sustainable and ethical business practices may outperform those without in terms of managing long term risks and improving return (Hurley 2019).

ESG measurement is an assessment that demonstrates how a firm performs against ESG values (Environmental, Social, and Governance) (Altvia 2022).

Emerging markets are countries with low to middle per capita income which have become a significant player in the global economy (Rousseau 2015).

Internal Rate of Return is an indicator which can be used to forecast how profitable a potential investment might be for a company (Stobierski 2020).

Financial Statements are written documents that indicate a company's transactions and financial health (Stobierski 2020).

Gross Profit Margin is a profitable metric that indicates what percentage of turnover remains after deducting the cost of goods sold (GOGS). The cost of products sold is the direct cost of production and excludes all operational expenditures, interest, and taxes. (Stobierski 2020.)

Net Profit Margin is a profitable metric that indicates what percentage of turnover and other income remain after deducting all expenses for business (Stobierski 2020).

Working Capital is an indicator that measures available liquidity of business for day-to-day activities (Stobierski 2020).

Debt to Equity Ratio is solvency metric that calculates how much a firm finance itself with equity against debt. This metric indicates the firm’s solvency by demonstrating the ability of shareholder equity to pay all debt in case of a firm in difficult times. (Stobierski 2020.)

Return on Equity (ROE) is a profitable metric calculated by dividing net profit by equity. It reflects how successfully the company can use equity capital to generate profits for investors. (Stobierski 2020.)

Operating Cash Flow is an indicator of the total of cash a company has as a result of its activities (Stobierski 2020). This indicator might be positive, indicating that cash is available to expand operations, or negative, indicating that extra finance is necessary to continue present operations. The operating cash flow is often included on the cash flow statement and can be computed in two ways: direct or indirect. (Stobierski 2020.)

1.4 **Thesis structure**

So far, I have covered the topic background, research questions and key definitions. Next, I will explain the research method which is used for this thesis paper. Then, factors driving sustainable investing, ESG integration, and ESG measurement will be looked at in the literature review.

1.5 **Research Method**

A qualitative research method is used in this thesis paper. The data is mainly collected from secondary sources: business journals, articles, newspapers, and research papers. This thesis is divided into two sections: theoretical and empirical. The theoretical section begins with an overview of sustainable investing. This allows readers gain basic knowledge about the subject. Then, the empirical section will start with PwC’s readiness survey to identify factors driving responsible investors in Vietnam. Then, two Vietnamese fund companies are examined for a benchmark review and conclusion.

2 Literature Review

Alongside the rising concern of negative impacts on society and environment, there are other factors that may drive fund managers toward sustainability. Four key factors are examined: global macro trends: technology and political preference; stakeholder relationship, financial return, and government.

2.1 Global Macro Trends

Macro variables accelerate the transition to a sustainable future. As net zero transition is underway, it results in a massive reallocation of resources, inevitably affecting portfolios. (BlackRock2022.) The net zero transition is the transformation process through which the world will reach net zero carbon emissions by 2050 (BlackRock 2022). The main drivers that may speed up the transition are the development of technology and political preferences.
First, technological development may reduce the world’s gas emissions (United Nations Climate Change 2022). According to research performed by Accenture, in partnership with the World Economic Forum, if digital technologies expanded throughout sectors, it could deliver over 20% of the 2050 reduction required to achieve the International Energy Agency net-zero trajectories in the energy, materials, and mobility sectors (George, Regan & Holst 2022). By immediately embracing digital technology, these industries may already lower emissions by 4-10% (George et al. 2022). Energy, materials, and mobility are the three most polluting sectors, accounting for 34%, 21%, and 19% of total 2020 emissions, respectively. They also reflect industries with the greatest potential to minimize emissions from digital technology. (George et al. 2022.) In energy, digital technology could help reduce 8% of greenhouse gas (GHG) by 2050. This would be accomplished by increasing efficiency in gas emissions activity through artificial intelligence driven by cloud computing and highly networked facilities with 5G. (George et al. 2022.) Artificial Information can be used to forecast peak power consumption needs and peak solar and wind power energy production based on weather conditions (Royal Society 2021). Digital technology in materials can generate up to 7% of GHG cuts by 2050. This

might help enhance mining and upstream output by leveraging core technologies such as big data analytics and cloud/edge computing. (George et al. 2022.) Using blockchain may improve process efficiency and facilitate circular loops. Digital technology in transportation might reduce GHG emissions by up to 5% by 2050. (George et al. 2022.) This requires using sensing technologies such as IoT, imagery, and geo-location to collect real-time data to support decision-making. It would eventually provide route optimization and reduce emissions in both rail and road transportation. (George et al. 2022.) Enabling virtual simulations of transportation can help public authorities and fleet operators enhance commuting flows (Royal Society 2021). Along with their advantages, digital technologies also have their own carbon footprint. Gas emissions can be from ICT production and waste (ICT's carbon footprint) which covers consumer devices such as phones, PCs, and wifi routers, all fixed and mobile network components, and data centers. (Lövehagen 2020.) Digital technologies may accelerate net zero by reducing global emission, but it is vital to mitigate their carbon footprint and make sure they have net beneficial effects for environment and society (George et al. 2022).

Countries around the world may reduce its dependence on Russian energy due to the Russian invasion of Ukraine. It seems obvious that the war in Ukraine may disrupt the transition's path in the short run. (Samandari, Pinner, Bowcott & White 2022.) However, the benefits of energy independence and energy security may accelerate net-zero transition efforts in the long run (Samandari et al 2022). The EU is working to achieve net zero as soon as possible. This can be seen by the European Commission’s proposed RePowerEU plan. (Black Rock 2022.) By 2030, the RePowerEu plan is to increase European biomethane production and green hydrogen capacity: 510 gigawatts of wind and 600 gigawatts of solar energy will be built over the next 8 years (Samandari et al. 2022). This plan could be expedited further by the fact that, despite increasing input fossil costs, the installation of new solar and wind capacity will continue more rapidly and more affordable than fossil fuels (Samandari et al. 2022). Due to the war in Ukraine, affordability may drive societal preferences towards favoring actions that raise emissions, such as the temporary usage of coal power plants in the short run. In the long term, persistently high prices act as a sort of carbon tax on consumers. Carbon intensive types of energy and high electricity prices make sustainable energy more competitive and encourage deployment of energy efficiency, electric automobiles and renewable hydrogen. (Black Rock 2022.) It is needed to embrace renewable-energy rather than fossil fuels and enhance energy-efficiency processes. These actions may drive net-zero technologies down to optimal cost and pave the road for rapid decarbonization in other geographies (Samandari et al. 2022).

2.2 **Stakeholder Relationship**

The shift to low-carbon economies has already had a significant impact on a variety of stakeholders, which has led to economic restructuring in a variety of key industries (Finance for Tomorrow 2022). Sustainable companies are those that positively affect all stakeholder groups. However, it is not always obvious how companies may benefit all stakeholders or how to increase their positive influence. (Szekely & Dossa 2015, 2-3.) In fact, companies often give priority to some stakeholder groups while completely neglecting others. Companies are sustainable only if they engage with their stakeholders to understand and respond to their demands. (Szekely et al. 2015, 2-3.)

According to Szekely & Dossa (2015), stakeholders are divided into two groups: primary stakeholders and secondary stakeholders. Those who have a direct connection to a company through financial transactions such as shareholders, managers, employees, clients, and suppliers are considered primary stakeholders. (Szekely et al. 2015, 2-3.)
Secondary stakeholders, on the other hand, are individuals who have a less direct connection to or influence with a firm. They are the environment, society at large, and local communities. According to the authors, most organizations pay more attention to primary stakeholders over secondary stakeholders. (Szekely et al. 2015, 2-3.)

A firm’s first responsibility in engaging stakeholders is to pay attention to all of them equally. In other words, there should not be any prioritization between primary stakeholders and secondary stakeholders. (Szekely et al. 2015, 2-3.)

Although secondary stakeholders might not share direct financial ties, they are also as important as primary stakeholders in the company. Therefore, if all stakeholders are treated equally, a company's financial objectives will not be fulfilled at the expense of a firm's social and environmental objectives. (Szekely et al. 2015, 2-3.)

Directors play a critical role in exercising the company's oversight. They oversee relevant risks and opportunities in diversity, equity, and inclusion as well as climate change. (King, Gerber, Atkins & Skadden 2021.) In addition, they develop metrics for measuring a firm's performance and oversee operational execution to achieve long-term goals. Then, they need to disclose to the public how those goals align with accomplishing long-term sustainable value and how their organizations are doing in pursuing their goals (King et al. 2021). Sustainability disclosure may help investors better understand the risks they perceive and to more efficiently allocate investment towards the firms that may potentially be better able to thrive in a low-carbon environment (OECD 2022).

The largest cloud service providers such as Amazon.com Inc, Microsoft Corp, Alphabet Inc, and Alibaba Group Holding Ltd. are under pressure to reduce the upstream value chain's emissions in response to demand from the board members. These four companies represent one-third of the cloud market. (MSCI 2021.) If these companies were to decarbonize their direct and energy-use emissions, they would reduce the upstream value chain's emissions across the economy, equivalent to 0.5% of total global emissions (MSCI 2021). Forward-looking companies take ESG issues because they see the connection to the company's long-term success (PwC 2022).

2.3 **Government**

The actions governments take now could accelerate the sustainable transition that balances environmental, economic and social outcomes.
Governments can announce detailed action plans with clear responsibility. Through cooperation amongst local authorities, it could be accomplished by setting out specific policy measures, initiatives, goals, timelines and necessary resources (Atalla, Mills & McQueen 2022).

In other words, the implementation of a green action plan requires the full commitment of government agencies, including those in charge of infrastructure, housing, transportation, and defense as well as those in charge of education, healthcare, and social services (Atalla et al. 2022). Government involvement will also be key to reducing the carbon footprint by providing incentives and penalties which help them achieve the transition (Atalla et al. 2022).

The authorities can offer various incentives and grants for business, scientists, and researchers to make net zero solutions more feasible (Atalla et al. 2022). In Germany, the government made the decision to stop relying on coal by May 2029 at the latest (Federal Ministry for Economic Affairs and Climate Action 2022). They will assist energy companies in making the shift away from coal by 2025 by providing incentives for investments to get rid of coal. One of the examples is giving incentives for using electric automobiles and developing a charging infrastructure. (Federal Ministry for Economic Affairs and Climate Action 2022.)

The government's explicit commitment to invest in infrastructure and key investment projects would help increase funding opportunities and offer institutional investors and insurers long-term stability (Atalla et al. 2022). Since the Fukushima tragedy in 2011, the Japanese Government has funded renewable energy sources in an effort to reduce its dependence on fossil fuel imports and move away from nuclear power (Atalla et al. 2022).

A 2019 bill demonstrates a commitment to wind energy by enabling wind farms to operate in Japanese waters for up to 30 years (Atalla et al. 2022). Businesses need authorities to initiate and align their ambition towards the problems. This will provide businesses with the clarity and confidence they need to invest. (Howard 2022.)

2.4 Financial Return

Sustainable investing has drawn attention from investors across the world. Over 75% of impact investors who participated in the Global Impact Investing Network (GIIN)'s most recent Annual Impact Investor Survey said that private equity was the most often used instrument in impact investing. (Mudaliar & Bass 2017, 4-5.) In a recent study, Cambridge Associates (CA) and the Global Impact Investing Network (GIIN) examined a sample of 71 private equity impact funds that seek market rates and social impact goals (Mudaliar et al. 2017, 4-5).

Thirty-seven percent of funds manage over USD 100 million, 56% of funds manage between USD 10 million and USD 100 million, and 7% of funds manage USD 10 million of assets or less. Geographically, 39% of the total fund investment is in Africa, 37% is in the US, 17% is split between emerging and developed countries, and the remaining is in a mix of developed regions. (Mudaliar et al. 2017, 4-5.) According to the study's findings, the 71 funds produced overall net returns of 5.8% on average and 4.6% at the median (Mudaliar et al. 2017, 4-5).

Additionally, the Internal Rate of Return (IRR) for the top 5% of funds is at least 22.1% annually, while for the bottom 5% it is -15.4% (Mudaliar et al. 2017, 4-5). From McKinsey & Company's perspective, private equity has produced a net IRR of 13.1% (McKinsey & Company 2022). Environmental, social, and governance (ESG) indices like the MSCI World ESG Leaders Selects have produced an average annual return of 13.9% since 2016 (Shing 2021).

The selection of a portfolio manager is one of the factors that could determine a fund's return. According to Clare, Motson, Sapuric, & Todorovic (2014), outstanding performance fund managers are able to produce a positive return for funds while the mediocre fund manager cannot due to lack of necessary skills (Clare, Motson, Sapuric, & Todorovic 2014, 2). The outstanding performance managers may regularly move in the market because, in most cases, they are recruited by other fund companies taking their skill with them (Clare et al. 2014, 2). Therefore, fund management companies must come up with an incentive-based impact structure to make sure that their fund managers

are rewarded appropriately for their skill and impact investment performance (Izzo 2013).
This kind of incentive structure policy may enable outstanding fund managers to make a long term commitment at the fund (Izzo 2013). According to Izzo (2013), it is crucial to tie the compensation of fund managers to social impacts and financial returns to ensure that everyone is held genuinely accountable for delivering on all the promises for impact investing (Izzo 2013).

Full carry is a portion of funds profits that fund managers receive as private equity compensation in addition to their management fees (Inya 2015). It can be divided into two components: base carry for the financial performance and impact carry for social impact performance (Tandon 2020).

A fund manager receives full carry if both the financial return and the social impact expected by investors are achieved (Tandon 2020). The manager is only eligible for base carry if they fall short of the minimal level of expected social impact. If the fund manager does not earn the full carry, the remaining will be distributed to the limited partners or will be donated to charity. (Tandon 2020.)

Although this impact-based incentive structure is not the industry practice, several impact investment funds have implemented it. Examples include: Vox Capital, Emerging Media Opportunity Fund (MDIF), and Global Financial Inclusion Fund (GFIF). (Transform Finance Investor Network 2016, 2-3.)
Vox Capital divides carry into two parts: 10% for the financial performance and 10% for the social impact performance. The fund manager gets the full 20% carry only if both the financial return and the social impact expected by investors are achieved. Transform Finance Investor Network 2016, 2-3.) If the manager falls short of the minimal level of expected social impact level, the manager is only eligible to 10% carry. If the fund manager does not earn the full carry, the remaining will be distributed to limited partners. (Transform Finance Investor Network 2016, 2-3.)

Vox Capital is a fund company that specializes in scalable, innovative solutions for the Brazilian population in the field of employment, housing, health, education and financial services. It manages a fund's size of $84.3 million with a target net IRR of 15%. (Transform Finance Investor Network 2016, 2-3.)

Sustainable investment can generate a positive return for fund companies. However, it still depends on the size of the fund, portfolio managers, markets, investment strategies and objectives which may determine the fund’s return.

2.5 **ESG Frameworks**

ESG frameworks are guidelines for fund managers to measure sustainability and ways to report impacts (OECD 2020). Three frameworks measuring sustainability: UN Sustainable Development Goals, Principles for Responsible Investment (PRI), and Operating Principles for Impact Management (The Principles) will be covered.

2.5.1 UN Sustainable Development Goals

The United Nations established the Sustainable Development Goals (SDGs) in 2015 as a set of 17 goals for advancing human society, ecological sustainability, and quality of life (Huber, Comstock, Smith, Polk & LLP 2018). They cover a wide range of sustainability-related subjects, from ending hunger and battling climate change to promoting responsible consumption and developing more sustainable cities (Robeco 2022). At the 2017 World Economic Forum, UBS chose the UN’s 17 Sustainable Development Goals for evaluating its sustainable performance. This framework below describes how fund companies use SDGs to measure their impact performance. (Huber et al. 2018.) This framework outlines three core steps found in Table 1.

Step	Action
Step 1—Define Priority SDG Targets	Addresses the process of prioritization of impacts and the identification of SDGs for a company to act and report on, specifically by understanding the SDGs and their targets, conducting a principled prioritization of SDG targets based on senior management's vison and strategy and then defining the company's SDG-related report content.
Step 2—Measure and Analyze	Covers how to set business objectives, select appropriate disclosures, and collect and analyze data and performance.
Step 3—Report, Integrate and Implement Change	Provides tips and guidance to companies on reporting and improving ESG performance, including consideration of data users' needs.

Table 1. SDG Framework (Huber et al. 2018).

2.5.2 Principles of Responsible Investment (PRI)

The Principles for Responsible Investment (PRI) comprise an international network of investors working together to implement the six Principles for Responsible Investment into practice. Its main goal is to help companies integrate sustainability into their investments and support investment decision making. (Principles for Responsible Investment 2022.)

Principle 1: We will incorporate ESG issues into investment analysis and decision-making processes.

Principle 2: We will be active owners and incorporate ESG issues into our ownership policies and practices.

Principle 3: We will seek appropriate disclosure on ESG issues by the entities in which we invest.

Principle 4: We will promote acceptance and implementation of the Principles within the investment industry.

Principle 5: We will work together to enhance our effectiveness in implementing the Principles.

Principle 6: We will each report on our activities and progress towards implementing the Principles.

Figure 1. Six Principles for Responsible Investment (Principles for Responsible Investment 2022).

2.5.3 Operating Principles for Impact Management

The Operating Principles for impact management are built from the idea of an end-to-end process to design and implement an impact management system (World Bank 2022). This framework consists of nine principles which fund companies can use to manage their impact investment portfolio by monitoring and measuring impact achievements, financial return, and potential risks (CDC 2021, 7-9).

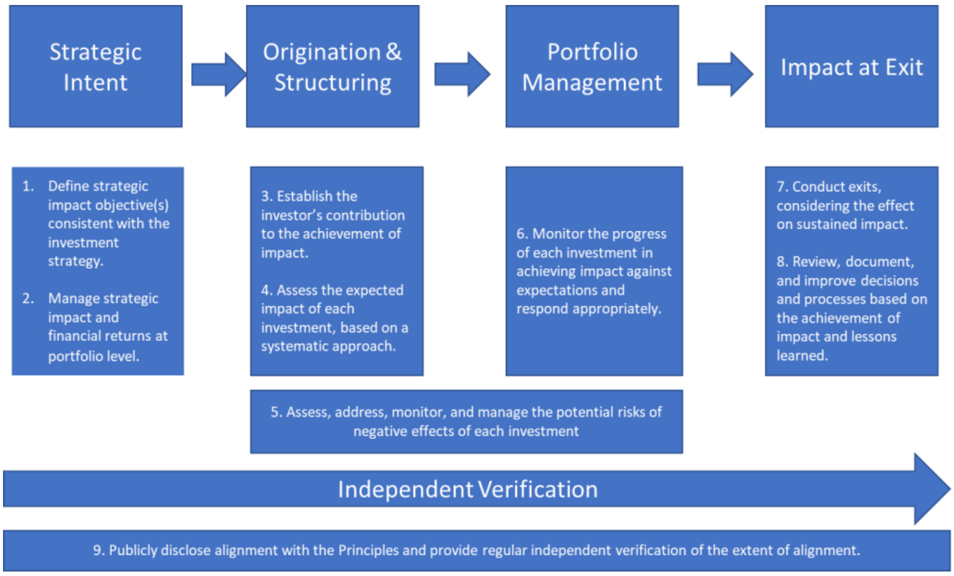

Figure 2. Operating Principles for Impact Management (World Bank 2022).

2.6 ESG Integration and Measurement

Sustainable integration is a process of integrating sustainability into investment decision making (Eurosif 2014). The sustainability integration enables fund companies to generate long-term financial return and social impacts (Black Rock 2022).

First of all, fund companies must define sustainable investment strategy. Questions can be made in order to help fund managers define the strategy and goals for their sustainable investment strategies. (Bernow, Klempner & Magnin 2017, 4-7.):

- How can a company start prioritizing ESG factors?
- What are the most important ESG factors to the fund company?
- How can a fund produce positive impacts for people and the environment?

Then, fund managers can select tools to design a responsible investment portfolio. Negative screening, positive screening, and corporate engagement are the three main techniques to design an investment portfolio. (Bernow et al. 2017, 4-7.)

Negative screening is a technique that identifies companies that perform poorly on environmental, social, and governance factors (Robeco 2022). Therefore, poor environmental or waste management records, including excessively high carbon footprints, and poor labor working conditions are typical criteria that the negative screening looks out for (Robeco 2022).

Positive screening is a technique which includes companies that perform highly on environmental, social and governance factors (Robeco 2022). When building portfolios with sustainability profiles such as good environmental records, good reputation for labor working conditions or gender equality, positive screening is frequently used (Robeco 2022).

Corporate engagement is the process of influencing management and boards to follow ESG principles. If fund managers can regularly participate in board meetings, they may use their voting rights to bring sustainable matters to the table. (Bernow et al. 2017, 6.)

It is important to do screening and due diligence to determine whether the companies may deliver both social and financial return (Graham & Anderson 2015, 17-19). Fund companies must point out the desired social impact that an investee’s companies can achieve. Clear social and environmental impact targets may help support measurement process. (Graham & Anderson 2015, 17-19.) If an investment may show substantial social and environmental gains but no financial gains, fund companies should not proceed (Graham et al. 2015, 17-19).

Once the investment is made, the financial and social performance must be measured (Graham et al. 2015, 17-19). Financial KPIs are metrics that companies use to evaluate their financial performance (Stobierski 2020).

These financial KPIs are divided into various sections, including profitability, liquidity, solvency, efficiency, and valuation. The important financial metrics are gross profit margin, net profit margin, working capital, debt to equity ratio, return on equity, and operating cash flow. (Stobierski 2020.) These financial metrics are typically found in financial statements. By understanding financial KPIs, managers and other key stakeholders can track and measure the financial performance of their companies. (Stobierski 2020.)

Impact performance can be measured based on a company's contribution to the UN SDGs framework (International Council for Small Business 2022).
As can be seen from Table 1, fund companies can establish key performance indicators (KPIs), monitor, and disclose their impacts towards the SDGs (Credit Suisse 2020, 12-14). It is necessary for fund companies to evaluate a firm's investee framework, and whether SDG KPIs and associated benchmarks are independently confirmed and based on globally accepted frameworks, for example: IRIS+5 and GRI6. Fund companies are recommended to communicate with business leaders enhancing quality reporting on these metrics. (Credit Suisse 2020, 12-14.)

Companies are encouraged to disclose more information about ESG (KPMG 2019). This is because the public wants to know how the company is contributing to gender diversity, inclusion, ethical working conditions, and the environment (Giannopoulos, Fagernes, Elmarzouky, & Hossain 2022). Fund companies may disclose their strategies, ESG performance, sustainability integration, and companies excluded from the portfolio. By disclosing ESG data, fund companies demonstrate that they respond to public demands and meet stakeholder' expectations. (Bernow et al. 2017, 8-10.)

2.7 ESG Data Collection

According to Kirby (2021), one of the main challenges in ESG data collection is data accessibility and consistency. Fund managers rely on banks and insurers on publicly available sources of ESG data as these banks and insurers have privileged access to data first than any companies. Simply, this is because banks and insurers acquire financial and non-financial data from loan businesses, mortgages and trading finance services. (Kirby 2021.)
Data accessibility affects small and big fund management companies because they depend on third-party vendors for important information such as ratings (Kirby 2021). Data may become inaccurate when it is obtained from unreliable sources (Kirby 2021). Fund management companies need to determine where that data will be sourced. It can be sourced internally, while other data can be sourced externally. (World Economic Forum 2021.)

Bigger fund management companies typically develop in-house sustainable investing teams which are able to produce their own ESG ratings and forecast them in the future (Kirby 2021). ESG rating is a measure of company performance against environmental, social and governance risks (MSCI 2022). Fund managers may use ESG ratings to improve their investing strategies and measure sustainable performance. Each rating agency may measure ESG factors differently which results in different ESG performance (Stackpole 2022). Lack of a universal approach leads to inconsistency of ESG ratings which misrepresent a firm's ESG performance (Scherpenzeel 2022). Therefore, ESG rating should be sourced from recognized firms, for example: MSCI, Moody's, and Sustainalytics (Stackpole 2022).

2.8 Tradeoffs of sustainable investing

Sustainable option incurs more costs. Swiss Re, a leading insurance company, estimates that failing to address climate change will destroy 18% of global GDP by 2050. The societal loss may directly impact business (Polman & Winston 2022). For instance, harsh weather may force factories to close. Staff members who are exposed to changing weather conditions may fall ill. Cities may become too hot to live in (European Commission 2022). Businesses can ask themselves: what is the positive return on investment to avoid these risks? It is advised to collaborate with others in the value chain, for example: NGOs, governments, and companies, to tackle the most pressing issues for the benefit of all. (Polman & Winston 2022.)

3 ESG in Vietnam

ESG has grown significantly in Vietnam in recent years. This is due to the governmental efforts to encourage ESG practices and investors’ growing need for sustainable investment. (PwC 2022, 7-9.) The government has instructed the relevant ministries and agencies to take action on ESG issues in keeping with the objective to improve the sustainable development of enterprises in Vietnam (Long, Nguyen, Hai & Quang 2022). At the United Nations Climate Change Submit (COP 26) from last year, Vietnam pledged to deliver a range of climate action commitments (Shira & Associates 2022).

Eight areas of Vietnam’s COP 26 commitment are focused on reducing greenhouse gas and moving towards a circular economy (Shira & Associates 2022). These will have a big influence on the transition to carbon neutrality and will drive Vietnam towards sustainable economy (PwC 2022, 7-9).
This is not all, however, the Vietnamese Government's efforts address all three aspects of ESG. The initiative of the Vietnamese Government to provide the relevant ESG legislations and regulations help companies play a larger role in accomplishing the national commitment related ESG objectives. (PwC 2022, 7-9.) On October 1, 2021, the Prime Minister announced Decision No. 1658/QD-TTg, which approved the National Strategy on Green Growth for the years 2021–2030 with a vision for the year 2050. This outlines the state's broad goals for achieving green growth and moving Vietnam's economy toward carbon neutrality. (Long et al. 2022.) The Vietnamese Government has also set the Labour Code, drafted Personal Data protection, Consumer Protection Law, Corporate Governance Code of Best Practices and Law on Enterprises (PwC 2022, 9-10).

The PwC's ESG readiness survey in 2022 among Vietnamese business indicates 80% have shown commitments to implement ESG soon. This is driven by the demands of consumers, staff members, and investors. The majority of respondents have ranked governance as the most essential to the ESG strategy for Vietnamese firms. (PwC 2022, 13-15.)

According to the PwC's readiness survey in 2022, 52% of respondents found ESG disclosures difficult due to the lack of transparent regulations (PwC 2022, 29-32). Several state agencies, most notably the State Securities Commission of Vietnam (SSC), as well as non-governmental organizations in Vietnam have been working to gradually implement guidelines and policies to improve the ESG practices of Vietnamese firms (Long et al. 2022).

In 2013, the SSC and the IFC worked together to create the Handbook on Sustainability Reporting, a manual primarily aimed at public and listed companies in Vietnam to help them understand, manage and disclose their ESG performance in response to the urgent need for ESG reporting guidelines (Long et al. 2022). For publicly traded and listed firms in Vietnam, the handbook was seen as one of the first steps toward achieving the SDGs. It guides Vietnamese companies to international ESG reporting standards and introduces key performance indicators for sustainability reports. (Long et al. 2022.)

Additionally, the Vietnamese Government has made efforts to increase international economic partnership by participating in numerous free trade agreements and organizations in recent years, for example: the World Trade Organization (WTO), the Eurasian Economic Union, the European Union, and the ASEAN Economic Community (AEC) (KPMG 2021). For the past 30 years, Vietnam's GDP has grown at an annual rate of 7% on average (Vietnam Holding 2022). Vietnam's economic growth is expected to continue growing in years ahead (KPMG 2021).
The Vietnamese labor force is a key competitive advantage in attracting international investment and supporting the country's future growth. Vietnamese workers are well known for being young, hardworking, and easy to train (KPMG 2021).

Vietnam has population of 96 million and a GDP per capita of $3000 (Vietnam Holding 2022). Vietnam's labor force was 49.1 million people, accounting for 51.0% of the total population in 2019 (KPMG 2021).

To conclude, these are main reasons that Vietnam receives considerable increase of FDI year after year. Given political stability, affordable labor cost, and strong economic growth, Vietnam become an appealing market for international and private investors to invest in the economy. (KPMG 2021.)

4 Case Companies

Continuous enhancements in ESG regulations and demands driven from the investors, fund companies must adopt ESG into their investment process. Two case companies are studied on how ESG is integrated and measured in the Vietnamese market.

4.1 **Vietnam Holding**

Vietnam Holding (VNH) is a closed-fund which focuses on domestic consumption, industrialization and urbanization, and invests in high-growth businesses in Vietnam. The fund is committed to sustainability at the core of its investing strategy and it seeks to completely incorporate Environmental, Social, and Government (ESG) into the investment process and only invest in businesses that are able to achieve ESG and Financial goals. (Vietnam Holding 2022.) Dynam Capital was appointed as the investment manager in June 2018. Aligning with VNH's strategy, objectives, and requirements, Dynam Capital is in charge of overseeing the day-to-day management of VNH's investment portfolio. (Vietnam Holding 2022.) Like other funds, Vietnam Holding also implements ESG principles into the investment process. The fund has developed its own exclusion list-based guidelines of the UNPRI of which VNH is a signatory, and a user of IFC guidelines. VNH does not invest in businesses listed in their exclusion list activities. The exclusion list is a list of activities that goes against sustainable development goals, for example production or trade in weapons and ammunitions or tobacco. (Vietnam Holding 2022.) Next, ESG Management systems are created to incorporate ESG into each step of the investment process: initial screening, due diligence, investment decision, and investment measurements. Then, VNH actively engages in better governance by communicating with business leaders through face-to-face meetings (Vietnam Holding 2022). In addition to assisting the fund’s investment decisions, this also creates a positive change at investee's firms (Vietnam Holding 2022).

Vietnam is one of the five nations most vulnerable to climate change, according to the United Nations Framework Convention on Climate Change (UNFCCC) (Vietnam Holding 2022). Vietnam Holding pays special attention to managing the portfolio’s climate risks by monitoring the portfolio’s total carbon emissions, examining the transition risks of climate-sensitive sectors and encouraging VNH’s investee firms to report their carbon emissions (Vietnam Holding 2022). As a signatory to the Principles for Responsible Investment (PRI), the fund measures and discloses its carbon footprint, portfolio carbon footprint and evaluates the performance of the portfolio’s investee firms against the UN Sustainable Development Goals (Vietnam Holding 2022).

According to Vietnam Holding’s Annual Report 2022, one of the top VNH’s portfolio companies is FPT Corporation. VNH has invested and owned FPT corporation at a 0.4% stake since 2012. As a result, the investment has yielded 26.6% internal rate of return for VNH. (Vietnam Holding 2022, 15-16.)

FPT is a software company established in 1988 that offers a variety of telecom and IT services, including broadband internet. At the end of 2021, FPT shifted away from an IT service company to an end-to-end digital transformation services provider, with 178 offices and branches worldwide. Revenue from its digital transformation services hit a record of $237 million in 2021. (Vietnam Holding 2022, 15-16.) FPT has selected eight of the UN Sustainable Development Goals ("SDGs") that the company can contribute to: quality education; gender equality; affordable and clean energy; decent work and economic growth; industry, innovation, and infrastructure; responsible consumption and production; climate action and partnerships for the goals. The company applies Vietnam's action plan for implementing the 2030 Sustainable Development Goals and the GRI Sustainability Reporting Standards. (Vietnam

Holding 2022, 15-16.) In 2022, FPT announced its first ESG report for the year 2021. It shows enhancement in gender equality by increasing the number of female managers and staff members by 17.5% and 21.4%, respectively. (Vietnam Holding 2022, 15-16.)

The company was also applauded for supporting COVID 19 prevention. The launch of digital vaccination application (FPT eCovax) helped business continue to operate during the epidemic in 2021. An aid package of $2.8 million was also spent on Covid 19 prevention. FPT also established the Hope Boarding School for orphaned children who lost family during the epidemic. (Vietnam Holding 2022, 15-16.) Despite several key ESG achievements, FPT still faces challenges in measuring its total CO_2 emissions and finding ways to recruit talent in response to the industry competition (Vietnam Holding 2022, 15-16).

4.2 **VinaCapital**

VinaCapital Vietnam Opportunity Fund (“VinaCapital”) is one of the Vietnamese leading fund companies that seeks to invest in sustainably oriented firms operating in financial, real estate, materials, and supply chain industries that benefit Vietnam’s long-term growth (VinaCapital 2022). The fund is committed to integrating environmental, social, and corporate governance (ESG) into its investment process (VinaCapital 2022). The ESG integration approach used by VinaCapital for its investment assets is known as Responsible Investment Framework by Asset (VinaCapital 2022). As part of the initial assessment, the investment team will screen a target company’s activities against the exclusion list. If a target company’s activities are on an exclusion list, the investment team will stop the evaluation process. (AIC 2020.) This is because VinaCapital does not invest in businesses engaged in the activities listed on the exclusion list, which was made on international best practices (VinaCapital 2022).
A reasonable test can be used if the investment director thinks the target company's activities might have a significant positive development impact (for example, to the local community) that outweighs any risks incurred by activities on the VinaCapital Exclusion List. This will require approval from Investment Committee before further investment evaluation could take place. (AIC 2020.)

Next, VinaCapital may conduct an ESG review to evaluate the firm's compliance with the requirements. The requirements are national laws on governance, social issues, environment, and IFC performance standards. This review is measured in seven key indicators: E&S Risk Category, E&S Management Score, Corporate Governance Score, Business Integrity Alert, Potential E&S Risks and Issues, E&S Opportunities. (AIC 2020.) The E&S Risk indicator has low, medium, and high levels. Business operations that have minimal or no negative effects on the environment or society are at a low risk level. The internal team may conduct ESG evaluation. Business operations that have potentially limited negative effects on the environment or society are at a medium risk level. (AIC 2020.) The internal team or an external ESG specialist may conduct ESG evaluation. Business operations that have potentially significant negative effects on the environment or society are at a high-risk level. An external ESG specialist may conduct due diligence. (AIC 2020.)
In case compliance with the requirements cannot be met, a corrective action plan must be agreed upon with the target firm in order for the investment to move forward. The plan must outline all necessary steps to bring a target firm in compliance. (AIC 2020.) A completion date for each step must also be agreed. Prior to the investment's completion, the target firm must supply all needed information, and the transaction lead in the investment team must confirm that the target firm is going to meet the requirements (AIC 2020). A summary of the ESG evaluation, whether carried out by an internal team or an external specialist, must be examined by the Risk Management Committee and Investment Committee prior to the investment's completion (VinaCapital 2022). The Risk Management Committee may take into account all relevant risks while the investment committee may approve the investments (AIC 2020).
VinaCapital delegates oversight of all ESG matters to the board of members of investee companies, and discuss ESG issues, goals, and performance. The fund will carry out an annual review of the ESG compliance of each company in VinaCapital's portfolio. (AIC 2020.) The ESG performance will be measured by continuous compliance against requirements. This will depend on the disclosures made by the firm. Additional independent evaluation may be required if the information to complete the review is needed. (AIC 2020.) If the investee's companies violate any Vietnamese laws or exclusion activity list, VinaCapital may decide to exit the investment (VinaCapital 2022).

SkyxSolar is a member of VinaCapital, which provides top quality rooftop solar panels and distribute energy solutions to business clients in Vietnam (SkyX Solar 2022). VinaCapital and EDF Renewables intend to invest over $100 million in SkyX Solar to develop 200-Megawatt rooftop solar for commercial and industrial clients in Vietnam in the next 2-3 years (Vietnamplus 2021). The demand for sustainable energy is going to increase due to the country's growing energy demand and government's goal of reducing CO_2 emissions (SkyX Solar 2022).
At the COP 26 submit last year, Vietnam pledged to stop the construction of new coal facilities although energy demands are rising in the manufacturing powerhouse (CNA 2022). Solar energy appears to be one of solutions to decrease CO_2 emissions in Vietnam. According to SkyX Solar (2022), Vietnam's total capacity of solar energy will reach double from 2020 to 2030, reaching 137-143 GW by 2030. If SkyX Solar rooftop solar is installed in a 1 MW (about 7000 squares meters of roof space) which help rooftop owners reduce 46,000 tonnes of carbon emission while saving considerable amount of money in energy bills. (SkyX Solar 2022.)

5 Conclusion

In conclusion, climate change has accelerated the world toward net zero emissions. The Vietnamese Government has pledged to shift away from carbon-intensive energy and commit towards a carbon neutral economy. These commitments have led to the rapid growth of ESG in Vietnam recent years. In addition to new ESG regulations, Vietnam has become an attractive market for responsible investors due to demands driven by investors and favorable macro conditions: political stability, economic growth and the labor force. Vietnam Holding and VinaCapital, two top ESG Vietnamese fund companies, have invested in Vietnamese companies and projects which could both deliver financial and impact returns. They may share a partial similarity in the ESG integration approach, but the ESG measurement approach is implemented differently. Vietnam Holding chose 17 SDGs to measure its investee's company ESG performance, while VinaCapital uses legislative requirements and IFC performance standards as well as E&S risk indicator for benchmark review. Two Vietnamese fund companies may tailor them to their specific needs and requirements. It should be noticed that the industry has not yet found the universal approach to integrate ESG and measure ESG performance. Adopting ESG may result in positive returns depending on the fund's size, markets, portfolio managers and investment strategy. In an emerging market like Vietnam, sustainable investment may result in a good financial return in the long run due to responsive regulations, strong demands from investors as well as favorable macro conditions.

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