BARINGS EMERGING EMEA OPPORTUNITIES PLC

Emerging EMEA and the race to net zero

Matthias Siller, Head of EMEA Equities at Barings, explains why companies across the emerging EMEA region have an important contribution to make toward global action on climate change—from supplying essential metals for renewable energy infrastructure to manufacturing the next-generation of electric vehicles.

The global movement to transition away from fossil fuels may not—at first view—look like welcome news for the oil-rich or often coal-dependent economies of Emerging Europe, the Middle East and Africa. But as elsewhere in the world, the race to address climate change is presenting compelling investment opportunities for a range of sectors and companies across this diverse region. At Barings Emerging EMEA Opportunities, we continue to find exciting opportunities in companies that are exposed to the seismic shift to net zero globally.

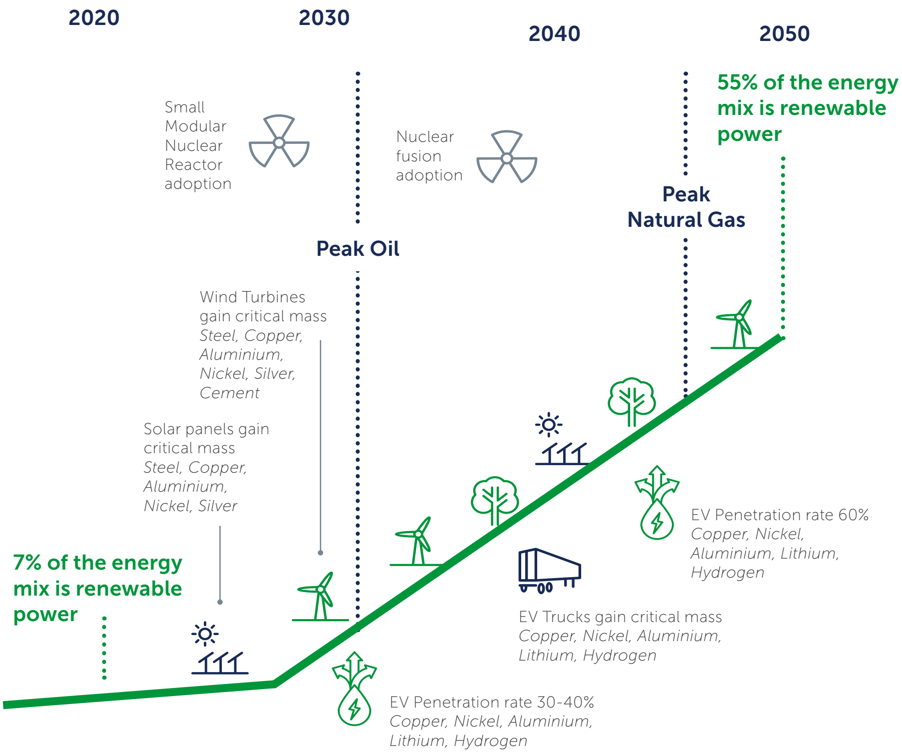
Perhaps the example that comes to mind for the EMEA region is access to natural resources. There is no denying that many of the traditional sectors, such as thermal coal and oil, are carbon intensive. However, what people might not realise is that there are a number of base metals and commodities that have a pivotal role to play in [bridging the gap] to a greener and more sustainable future.

The need for steel and its raw materials

Renewable energy needs steel—and lots of it. Producing one megawatt of solar energy in Europe requires 35 to 45 tonnes of steel. For onshore wind, it's 84 tonnes, and for offshore wind, 212 tonnes. Indeed, the amount of steel required for an offshore wind farm is roughly four to five times greater than that required by an onshore facility with the same gigawatt generation capacity. It's estimated that a full displacement of coal, oil and gas with renewables by 2030 would add around 3% to global steel demand.

It's estimated that the supply of copper, which is essential to solar panels, and zinc, a big component of wind power and EVs, will need to double between 2019 and 2050.

FIGURE 1: The energy transition is a long one, and critical to its success is the supply of resources



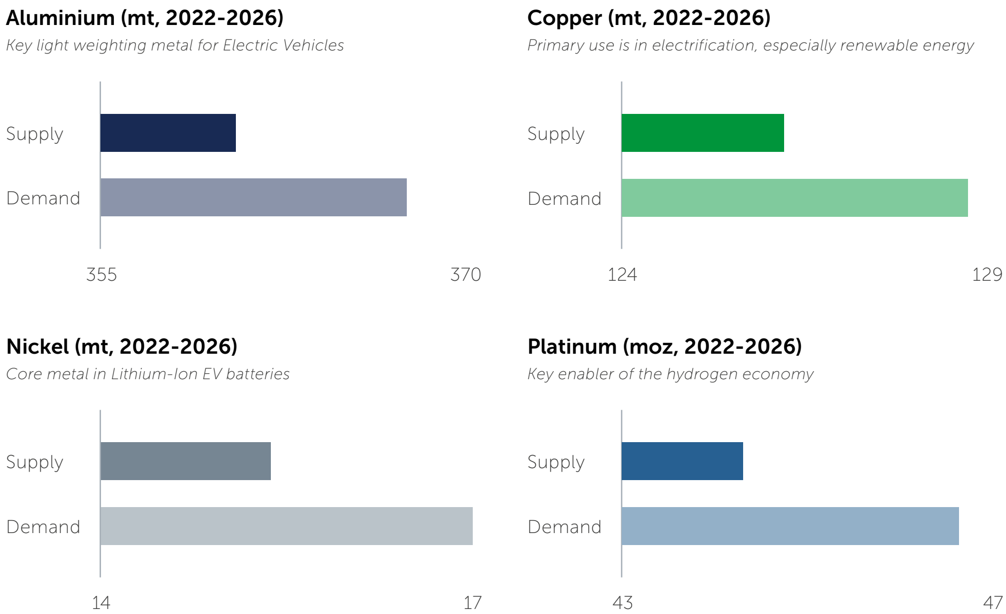
Source: Barings, February 2022, based on a Safety4Sea diagram.

Metals for green tech

Steel is just one commodity in the chain. It's estimated that the supply of copper, which is essential to solar panels, and zinc, a big component of wind power and electric vehicles (EVs), will need to double between 2019 and 2050 to meet targets to keep global warming within 1.5°C of pre-industrial levels. The supply of nickel (used in geothermal energy) and cobalt (used in lithium storage batteries) will almost need to quadruple.

Emerging EMEA companies will have an important role to play in meeting this demand. Barings Emerging EMEA Opportunities has a 30% allocation to South Africa[1] where holdings include diversified miner Anglo American, which we view as an important contributor toward the energy transition. The company produces a number of inputs used to make steel and is also a major producer of metals including platinum, which is used in hydrogen-powered fuel cell EVs and the production of 'green' hydrogen using electrolysis.

FIGURE 2: Key materials for the energy transition are in structural supply deficits



Source: Barings, February 2022

Emerging EMEA companies will have an important role to play in meeting the demand for the key materials needed to drive the energy transition.

Despite the wealth of minerals and commodities produced across the region, opportunities are not just confined to the availability of natural resources. There are also compelling examples of companies providing innovative solutions to help move toward a greener world, as well as businesses leading the way in addressing their own environmental footprint.

Delivering environmental solutions

There are a number of innovative companies across the Emerging EMEA region that are helping to contribute to lower carbon world. For instance, Turkish conglomerate KOC owns a significant stake in Ford Otosan, which runs one of the most efficient car production sites globally and is involved in the manufacturing of EVs. This includes Ford's highly successful Transit range of light commercial vehicles (LCVs), which, in their battery-powered form, are set to be a key to green urban e-commerce delivery.

Another example is Polish parcel delivery company InPost, who provide centralised lockers where customers can pick up their online orders. By slashing 'last mile' delivery trips, InPost estimates this is reducing CO2 emissions in urban areas in Poland by 62% compared to delivery direct to the customer's home.

[1] As at 30 June 2022.

Improving environmental activities

Companies across Emerging EMEA aren't only focused on their end products and services, but are also addressing environmental risks within their own operations. Anglo American is also doing a lot internally to improve its environmental, social and governance (ESG) practices. Its 'Smart Mine' programme includes partnering with several companies to develop the world's largest hydrogen-powered mine haul truck, with hydrogen generated on site via electrolysis. The company is also exploring this technology for the trains they use in Australia. It has clear 2030 targets to reduce greenhouse gas emissions by 30%, energy usage by 30% and water abstraction by 50% – and is currently the only global diversified miner with a 2040 net zero emissions target.

Regional dynamics

With increasing electricity demand, the need to upgrade energy grids and decarbonise electricity generation provides a common backdrop across the region. However, the specific market dynamics differ across the geography.

In the **Middle East**, utilities and government are investing in renewable energy generation, making use of the extremely favourable environment for photovoltaics (converting light into electricity) and offshore wind generation. All of the natural gas that's produced in the Gulf Cooperation Council (GCC) countries is currently sold to domestic petrochemical companies while power generation continues to burn fuels to generate the required electricity for industrial use. Reconfiguring power generation to utilise natural gas will not only reduce carbon emissions but also put the region's surplus gas production to efficient use. This will entail substantial financing needs, backed up – as we believe – by an attractive Regulated Asset Base (RAB) approach that equity investors can participate in via publicly listed companies. Currencies that are pegged to the US dollar combined with a rock-solid fiscal picture supported by high energy prices and strong economic activity will contribute to the attractiveness of the investment case.

Turkey's role as a traditional energy corridor between Central Asia and the Middle East on one side and Europe on the other is becoming more important given Europe's pivot away from Russian energy. We expect major upgrades of existing energy infrastructure that connects energy resources in Azerbaijan to Europe and the Mediterranean, which we expect to be co-financed by Turkish conglomerates. This should lead to full order books for Turkish construction companies and equipment manufacturers.

In the current energy context the stakes couldn't be higher for **Europe**. The region's dependence on Russian energy, especially for central and eastern European states, has led to significant renewed focus on the energy transition. Having set the framework in the NextGen EU and Green Deal programmes, multi-billion Euros of funding was made available to underpin the process. Given the combination of Russia's war in Ukraine and crippling energy prices, implementation plans are being sped up by regulators and policy makers, providing motivation for a separation from existing coal-based generation. This would allow emerging European utilities and energy companies unhindered investment in the renewables space, supported by EU subsidies.

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South Africa's crumbling energy infrastructure has long since been a factor holding back economic growth. A byzantine network of dependencies, state interference and price controls are the most obvious reasons for decade-long underinvestment in the electricity generation sector. The Ramaphosa's government decision to allow for and support private sector involvement in electricity generation cannot be underestimated in our view and could be a decisive step in the country's endeavour to utilise its growth potential, reduce unemployment, tackle corruption and implement structural reforms.

A growing theme

Companies across Emerging EMEA are playing an important role in the global movement to tackle climate change, and are also adopting more progressive practices aligned with shareholder and customer environmental expectations.

As a fundamental bottom-up investor, Barings Emerging EMEA Opportunities is well-positioned to identify the key beneficiaries of this global theme – one that's set to dominate investor concerns over the years to come.

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