NewNet Investor Profile, Salvador Escobedo, Ecos Sustainable Equity Fund

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Salvador Escobedo

Salvador Escobedo discusses investing in Latin American cleantech, the debate surrounding biofuels and the need for forward-thinking policy.

Ecos Sustainable Equity Fund is a private equity/venture capital investment fund, targeting SMEs active in providing tools for a more sustainable development, specifically cleantech and sustainable forestry operations. Founded by Swiss partners, the firm focuses primarily on South America from a central office in Panama.

Salvador Escobedo is Mexican and French national with a background in international business and marketing operations. Previously, he was international marketing director residing in New York City for a group of 21 Mexican agroindustrial companies.

What is the background of the firm and its activities in the sector?

'We are a family office of Swiss origin with main offices in Panama. We invest in cleantech (defined as environmental engineering and renewable energy) and sustainable forestry operations throughout Latin America. We also have a couple of portfolio companies in Europe and the US.

We believe that the sectors we target have enormous potential - specifically cleantech and renewable energy – it represents what I like to call "future energy, today". In the region that we focus on, energy demand is currently barely met and is projected to continue growing as economic development continues.

With the current global economic slowdown there will be a reconfiguration of the sector that will provide great opportunities for private equity investors, especially as credit conditions toughen and companies look to generate synergies to squeeze everything they can to maintain margins. The world is still running out of oil, pollution remains a big issue, carbon will continue to be priced on the market and the technologies deployed for renewable energy produce steady flows of cash.

Responsible energy production and management has gone from an ideal, to a business opportunity, to an industrial reality. Just last year approximately $150bn was invested in the cleantech sector. This year that number will likely be surpassed, some mention the $200bn mark (even after the financial crisis). It is widely accepted that investment in cleantech is poised to surpass $500bn by 2020. It an area of tremendous growth.'

What is your specific focus?

'Our focus is based on three pillars: energy generation, biofuels and efficiency. On energy generation we look at solar and wind energy, hydropower, biomass/biogas energy and geothermal energy, which we feel has been overlooked to date, but has massive potential. In this sub-sector you could be looking at technology developers, technology deployers and services companies. We look more at technology deployers and services. We believe that the US and Europe have access to outstanding and experienced technology investors to look at the technology development side.

In the biofuels sector, we are very cautious, and are closely following the food versus fuel debate. This has obviously been causing quite a bit of turmoil in the market as growing food to burn as fuel has been shown to have an effect on worldwide food distribution and prices. The UN, the World Bank the IMF and other important multilateral institutions and NGOs have publicly accepted that food-based biofuels do have a significant impact. Ultimately we want to be a part of the solution and not the problem, and this is the main reason why we are staying away from such activity. However, we do accept that the current biofuel economy is paving the way for newer and more efficient technologies for the future. This is where we feel the real solutions may lie.'

Why are biofuels of particular interest?

'The world needs fuel and we are running out of oil. Within biofuels we are particularly interested in second generation fuels. First generation biofuels utilise soy, corn, wheat, sugar and other edibles to transform them into bioethanol and biodiesel. With second generation biofuels we are seeing non-edible materials being used, such as switch grasses, straw, wood waste and even municipal solid waste, turned to highly efficient and clean burning fuels. We believe that this kind of approach has a lot more potential than the first generation products.

Recently however, we are also seeing a group of third generation biofuels such as micro-algae and cyanobacteria gaining ground. These last two have enormous potential. Putting this into perspective, a large biodiesel plant needs hundreds of thousands of hectares of soy crops to keep it going, with certain micro-algae, you would only need a couple thousand hectares at most. This is obviously a very attractive proposition.

First generation biofuels are of no interest for us. The technology has been in place for decades and we think that there is sufficient need, experience, capital, creativity and technological base to start looking at genuinely sustainable means to produce alternative fuels, rather than relying on the old methods, especially at a time when there are six billion people on the planet that need to be fed.'

Which other areas do you look at?

‘Another area interest is energy efficiency, as this is where we believe the most robust investment volume will take place in the future in order to really have a truly sustainable and positive impact.

We are looking at smart grid applications, using technology to direct energy in a more efficient way. There are enormous losses in industrial transmission and distribution of energy, so this is a very immediate application and a clear first step in the right direction to responsible energy management. We are seeing some very creative and interesting business models being developed at the moment.

We are also looking at more niche technologies, such as those that can be installed at home but that are affordable and deployable for Latin America’s infrastructure.’

Why do you focus mainly on Latin America?

‘We think that Latin America is a market that has been largely overlooked for too long. Countries have relatively high energy costs which translate to strong potential for clean energy generation and energy efficiency.’

The tropical weather conditions in the region obviously help with generation of energy from biomass and hydro. The land is very rich, with warm weather and lots of rainfall.

There is also lots of potential for geothermal energy production in the Andean mountain range and the Central American volcanic lands.

Additionally, countries such as Chile and Mexico have some of the highest sun radiation factors in the world. In general, Latin America is a region that has lots of potential in all the fields of renewable energy.

On the other hand, we also face specific local challenges that not every investor can manage, especially trying to manage it from an office in Zurich, New York or Madrid. As an example, we have closed deals in Colombia, which has remained unattractive for a long time to European and US investors for its difficult socio-economic challenges that are mostly unique to the region. It is not an easy thing to do and you need the right partners and regional experience. Other difficulties for outside investors can also be in simply choosing the right country to invest in. Some may seem economically attractive but their history may paint a different picture. You need to know your partners very well. You also need to know where the money comes from and what implications it may have, and also what sort of deals portfolio companies are doing, and who their clients and suppliers are. It can become a very complex and risky game, but also an extremely rewarding one.’

What are the advantages of investing in clean energy?

‘Dirty energy generation contributes most to global warming. The reason we see clean energy as an attractive sector is that there is really no other way to go if we want to have a sustainable society going forward. Energy is comfort and therefore peace. Energy is freedom of thought and therefore innovation. As a society, we cannot continue polluting the way we have in the past but we need more and more energy. As economies develop throughout the world, people want more televisions, computers, air conditioning and

personal vehicles - and this is all creating an enormous demand that is not fulfilled by common technologies or resources.

It has been interesting to see that with the recent stock market collapses, one of the most solid sectors -if you can say that- has been the renewable energy sector. The laws and fiscal incentives that have been passed in countries like Germany and Spain have set the ground for long term growth and therefore, if you connect the dots, you begin to realise that the sector will gain strength; especially as investors continue trusting the available technologies which most of the time offer 25 year warranties.'

What are the challenges you face?

'The main disadvantage right now is a lack of truly long-term policy commitment from the world's largest energy consumers, such as China, India and the US. Others usually follow. The tariffs and legislation for solar or wind energy change constantly, therefore it is hard to predict cash flows looking 15 years into the future. This makes it hard to plan strategies for a successful business and makes risk assessment quite difficult in a valuation. President-elect Obama has pledged to fix this but like most of his campaign, he now has to fulfil the promise.

Internationally, the most important issue right now is having governments agree on long-term policies that enable the technologies and industries to move ahead and to be transferred.

I think public perception of cleantech is also an issue; there seems to still be too much scepticism. There needs to be a perception shift to realise that clean technologies are available and that they are fully proven to work on a commercial scale. This is beginning to happen slowly, but stronger government commitments are necessary.'

What are going to be the big sectors of tomorrow?

The hot areas would probably be the new generations of biofuels and solar energy. Decentralised energy generation technology will also be very strong. I would also definitely keep an eye on energy efficiency. We first need to reduce the amount of energy we consume, and then we need to produce it cleanly. That is where the massive investments are going take place, in my opinion.'

What is the big issue currently facing the industry?

'In my opinion, the elephant is the room is policy. We have seen good use of it in countries like Spain, Germany, Italy and Greece. Once the policy makers lay a solid foundation, you see an explosion in the sector with major creation of jobs. Spain has been receiving billions of dollars in investment in solar energy just because legislators were able to put together a package that was attractive to investors and made economic sense. It made projects financially viable for the future and the whole country has benefited. Lots of jobs were created and lots of carbon emissions were cut. All kinds of positive systemic effects begin to take place, such as a drop in respiratory diseases which lighten state expenditures in healthcare. There is no doubt that a cleaner environment, wider access to energy and job creation is good for an economy.

What is needed is a solid legal and policy foundations that allow the technology to be developed and utilised.'

How can you see things evolving?

'I think we are seeing a generally positive trend. A good example was the weight that the US Presidential campaigns gave to renewable energy – they talked about it all the time and now President-elect Obama has pledged to flash-start a new green economy based on renewable energy.

Other governments around the world are also changing. A great example would be the Saudi focus on the sector. Who would have thought that the country with most abundant and cheap oil reserves is looking to generate their power with alternative, cleaner and renewable resources such as the sun?

With the amount of venture capital investment in US cleantech, it is easy to imagine that there is quite a bit of pressure to allow the technologies being developed to be deployed in the market. The country has experience on policy-based economic growth, such as we saw with the auto industry, and this should allow the sector to move forward systematically. Policy-makers could ask their experienced European counterparts for advice and once the incentives are created, the outlook will be great for everyone.'