

# Seeking Alpha<sup>α</sup>

## Aftermath Of An Epidemic: Does China Belong In Ethical Portfolios?

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With investors increasingly looking to invest in companies that align with their personal values, "ESG" funds ("ESG" stands for Environmental, Social and corporate Governance) have gathered assets at an impressive clip. After failing to seriously grow their assets following their arrival on the scene a little more than a decade ago, 2019 was the breakout year for ESG funds that industry analysts had been predicting for some time already, with AUM in these funds nearly quadrupling.

Life + Liberty Indexes founder Perth Tolle has tread a different path on the road to offering investors ethical alternatives in the emerging markets space. Rather than focus on the "ESG" side of the equation, Perth has pioneered an approach that focuses on the three key freedoms she sees as underpinning democratic societies: civil freedom, political freedom and economic freedom. The result is a fund that would make both John Locke and Thomas Jefferson proud, the Freedom 100 Emerging Markets ETF (FRDM).

Splitting her youth between China, where she spent the first decade of her life, and the United States which she relocated to with her parents, Perth had a first-hand view of the differences between democratic and undemocratic societies. Spending a year in Hong Kong straight out of college - including time visiting the mainland - she became consciously aware of the essential differences in personal and economic liberty between the U.S. and China and the wide set of opportunities and choices individuals had in free and democratic societies that simply didn't exist in autocratic countries.

The index underlying FRDM follows a methodology which ranks 26 different emerging market countries based on their adherence to more than 75 principles of personal, political and economic freedom - things ranging from freedom of the press and assembly to independent courts, women's and minority rights and labor law (a more expansive list is available here). The data underlying the index is taken from three renowned think tanks - the Fraser Institute, Cato Institute, and Friedrich Naumann Foundation for Freedom - and aggregated by Perth and her team to provide country level scoring. Countries falling below a certain score are then excluded from FRDM while the top scoring countries are overweighted within the index.

Unlike typical emerging market funds like (VWO) and (IEMG) which allocate as much as 40% of their portfolios to China, FRDM excludes China, Russia and Saudi Arabia completely. As Perth explains, "We don't go by the news, we go by the scores. It's an objective system which determines what goes into the index and what gets excluded which takes personal bias out of the

process. We are constantly re-evaluating what the data shows... if a country improves in these key areas, it will be included in the index [on the next rebalance]."

FRDM's underlying investing thesis is straightforward: Over time, democratic societies will produce better returns than undemocratic ones for a variety of reasons including better transparency, participation of a larger segment of society in innovation, and the ability to challenge existing hierarchies, to name a few.

In this episode, we ask tough questions about the Chinese government's role in covering up the effects of the virus when it first emerged in Wuhan - and about its failure to warn the global community about just how dangerous a threat COVID-19 posed. According to Perth, the difference this time isn't so much that the Chinese government has changed its behavior for the worse but rather that the global community has started to take note of just how bad an actor it has been all along. If FRDM's winning of the 2019 ETF.com award for Best New International/Global Equity ETF is any indication, her unique approach to indexing freedom is really starting to resonate with the investing public.

#### **Show Notes:**

- 4:00 - The growing bi-partisan consensus on China
- 5:00 - Issues with Zoom (ZM) blocking Chinese dissidents: Ideas for a future index?
- 7:30 - Methodology of indexing freedom: Who is in, who is out?
- 10:45 - FRDM's top holdings, method of selection, approach to weightings
- 13:15 - How many people actually died from COVID-19 in Wuhan?
- 20:00 - Was China hiding information about the early stages of the outbreak?
- 26:00 - How much misinformation is being put out by the Chinese government and how much do the Chinese people believe the official state narrative?
- 35:00 - The case of Luckin Coffee (LK): How concerned with corporate fraud should investors in Chinese companies be?
- 47:30 - The best of the Freedom 100: Polish gaming company The CD Projekt (OTC:OTGLF)