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COMPACT

Who Cares Wins

**Connecting Financial Markets
to a Changing World**

Recommendations by the financial industry to better integrate environmental, social and governance issues in analysis, asset management and securities brokerage

Endorsed by:

ABN Amro • Aviva • AXA Group • Banco do Brasil • Bank Sarasin • BNP Paribas • Calvert Group • CNP Assurances
Credit Suisse Group • Deutsche Bank • Goldman Sachs • Henderson Global Investors • HSBC • Innovest
ISIS Asset Management • KLP Insurance • Morgan Stanley • RCM • UBS • Westpac



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Swiss Federal Department
of Foreign Affairs



United Nations



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Endorsing institutions

The report is the result of a joint initiative
of the following companies:

ABN Amro

Aviva

AXA Group

Banco do Brasil

Bank Sarasin

BNP Paribas

Calvert Group

CNP Assurances

Credit Suisse Group

Deutsche Bank

Goldman Sachs

Henderson Global Investors

HSBC

Innovest

ISIS Asset Management

KLP Insurance

Morgan Stanley

**RCM (a member of Allianz Dresdner
Asset Management)**

UBS

Westpac

Note: Throughout this report, the pronoun “We” refers to the endorsing institutions listed above and not to the individuals that have contributed to producing this report.



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Executive summary

This report is the result of a joint initiative of financial institutions which were invited by United Nations Secretary-General Kofi Annan to develop guidelines and recommendations on how to better integrate environmental, social and corporate governance issues in asset management, securities brokerage services and associated research functions. Eighteen financial institutions from 9 countries with total assets under management of over 6 trillion USD have participated in developing this report. The initiative is supported by the chief executive officers of the endorsing institutions. The U.N. Global Compact oversaw the collaborative effort that led to this report and the Swiss Government provided the necessary funding.

The institutions endorsing this report are convinced that in a more globalised, interconnected and competitive world the way that environmental, social and corporate governance issues are managed is part of companies' overall management quality needed to compete successfully. Companies that perform better with regard to these issues can increase shareholder value by, for example, properly managing risks, anticipating regulatory action or accessing new markets, while at the same time contributing to the sustainable development of the societies in which they operate. Moreover, these issues can have a strong impact on reputation and brands, an increasingly important part of company value.

The report aims at increasing the awareness of all involved financial market actors, at triggering a broader discussion, and supporting creativity and thoughtfulness in approach, rather than being prescriptive. It also aims to enhance clarity concerning the respective roles of different market actors, including companies, regulators, stock exchanges, investors, asset managers, brokers, analysts, accountants, financial advisers and consultants. It therefore includes recommendations for different actors, striving to support improved mutual understanding, collaboration and constructive dialogue on these issues.

The endorsing institutions are committed to start a process to further deepen, specify and implement the recommendations outlined in this report by means of a series of individual and

collaborative efforts at different levels. They are also keen to start a dialogue with other stakeholders on ways to implement the recommendations because they are convinced that only if all actors contribute to the integration of environmental, social and governance issues in investment decisions, can significant improvements in this field be achieved. As an important next step, endorsing institutions plan to approach the relevant accounting standard-setting, professional and self-regulatory organizations, and investor relations associations in order to ensure that their intentions are fully understood and supported. They invite the Global Compact or one of its implementing bodies to review the state of the implementation of this report's recommendations in a year's time with the goal of assessing how market actors have responded to the call for action by this report.

Endorsing institutions are convinced that a better consideration of environmental, social and governance factors will ultimately contribute to stronger and more resilient investment markets, as well as contribute to the sustainable development of societies.

The report's recommendations can be summarized as follows:

- **Analysts** are asked to better incorporate environmental, social and governance (ESG) factors in their research where appropriate and to further develop the necessary investment know-how, models and tools in a creative and thoughtful way. Based on the existing know-how in especially exposed industries, the scope should be expanded to include other sectors and asset classes. Because of their importance for sustainable development, emerging markets should receive particular consideration and environmental, social and governance criteria should be adapted to the specific situation in these markets. Academic institutions, business schools and other research organisations are invited to support the efforts of financial analysts by contributing high-level research and thinking.
- **Financial institutions** should commit to integrating environmental, social and governance factors in a more systematic way in research and investment processes. This must be supported by a strong commitment at the Board and senior management level. The formulation of long-term goals, the introduction of organisational learning and change processes, appropriate



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training and incentive systems for analysts are crucial in achieving the goal of a better integration of these issues.

- **Companies** are asked to take a leadership role by implementing environmental, social and corporate governance principles and policies and to provide information and reports on related performance in a more consistent and standardised format. They should identify and communicate key challenges and value drivers and prioritise environmental, social and governance issues accordingly. We believe that this information is best conveyed to financial markets through normal investor relation communication channels and encourage, when relevant, an explicit mention in the annual report of companies. Concerning the outcomes of financial research in this field, companies should accept positive as well as critical results.
- **Investors** are urged to explicitly request and reward research that includes environmental, social and governance aspects and to reward well-managed companies. Asset managers are asked to integrate research on such aspects in investment decisions and to encourage brokers and companies to provide better research and information. Both investors and asset managers should develop and communicate proxy voting strategies on ESG issues as this will support analysts and fund managers in producing relevant research and services.
- **Pension fund trustees** and their **selection consultants** are encouraged to consider environmental, social and governance issues in the formulation of investment mandates and the selection of investment managers, taking into account their fiduciary obligations to participants and beneficiaries. **Governments** and **multilateral agencies** are asked to proactively consider the investment of their pension funds according to the principles of sustainable development, taking into account their fiduciary obligations to participants and beneficiaries.
- **Consultants and financial advisers** should help create a greater and more stable demand for research in this area by combining research on environmental, social and governance aspects with industry level research and sharing their experience with financial market actors and companies in order to improve their reporting on these issues.

- **Regulators** are invited to shape legal frameworks in a predictable and transparent way as this will support integration in financial analysis. Regulatory frameworks should require a minimum degree of disclosure and accountability on environmental, social and governance issues from companies, as this will support financial analysis. The formulation of specific standards should, on the other hand, rely on market-driven voluntary initiatives. We encourage **financial analysts** to participate more actively in ongoing voluntary initiatives, such as the Global Reporting Initiative, and help shape a reporting framework that responds to their needs.
- **Stock exchanges** are invited to include environmental, social and governance criteria in listing particulars for companies as this will ensure a minimum degree of disclosure across all listed companies. As a first step, stock exchanges could communicate to listed companies the growing importance of environmental, social and governance issues. Similarly, **other self-regulatory organizations** (e.g. NASD, FSA), professional credential-granting organizations (e.g. AIMR, EFFAS), **accounting standard-setting bodies** (e.g. FASB, IASB), **public accounting entities**, and **rating agencies and index providers** should all establish consistent standards and frameworks in relation to environmental, social and governance factors.
- **Non-Governmental Organisations** (NGOs) can also contribute to better transparency by providing objective information on companies to the public and the financial community.



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Graphical summary of key recommendations

Overall goals:

- Stronger and more resilient financial markets
- Contribution to sustainable development
- Awareness and mutual understanding of involved stakeholders
- Improved trust in financial institutions





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Background and scope of the report

This report is the result of a joint effort of financial institutions which were invited by United Nations Secretary-General Kofi Annan to develop guidelines and recommendations on how to better integrate environmental, social and governance issues in asset management, securities brokerage services and associated research functions. The work that led to this report took place under the auspices of the U.N. Global Compact.

The Global Compact is a corporate responsibility initiative launched by Secretary-General Kofi Annan in 2000 with the primary goal of implementing universal principles in business. By establishing the link between environmental, social and governance issues and investment decisions, this report wishes to contribute to better integration of these factors in investment decisions which will ultimately support the implementation of the Global Compact principles throughout the business world.

The need for this report has been repeatedly expressed to the U.N. Secretary-General and to the Global Compact by senior executives of financial institutions and other companies which are signatories to the Global Compact. In January 2004, Secretary-General Kofi Annan wrote to the CEOs of 55 of the world's leading financial institutions inviting them to join in the initiative that led to the development and release of this report.

Exhibit 1

Brief description of the U.N. Global Compact

Launched in July 2000 by United Nations Secretary-General Kofi Annan, the Global Compact is an international initiative bringing companies together with UN agencies, labour and civil society to support ten principles in the areas of human rights, working conditions, the environment, and anti-corruption. Through the power of collective action, the Global Compact seeks to advance responsible corporate citizenship so that business can be part of the solution to the challenges of globalisation. In this way, the private sector — in partnership with other social actors — can help realize the Secretary-General's vision: a more stable and inclusive global economy.

The Global Compact is a voluntary corporate citizenship initiative endorsed by companies from all regions of the world. It has two objectives:

1. Mainstream the ten principles in business activities around the world
2. Catalyse actions in support of UN goals

To achieve these objectives, the Global Compact offers facilitation and engagement through several mechanisms: Leadership Model, Policy Dialogues, Learning, Local Networks and Projects.

As of June 2004, more than 1,500 companies worldwide had committed to the Global Compact and its principles.



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Exhibit 2

U.N. Global Compact Principles

Human Rights

- Principle 1: Businesses should support and respect the protection of internationally proclaimed human rights within their sphere of influence; and
- Principle 2: make sure that they are not complicit in human rights abuses.

Labour

- Principle 3: Businesses should uphold the freedom of association and the effective recognition of the right to collective bargaining;
- Principle 4: the elimination of all forms of forced and compulsory labour;
- Principle 5: the effective abolition of child labour; and
- Principle 6: eliminate discrimination in respect of employment and occupation.

Environment

- Principle 7: Businesses should support a precautionary approach to environmental challenges;
- Principle 8: undertake initiatives to promote greater environmental responsibility; and
- Principle 9: encourage the development and diffusion of environmentally friendly technologies.

Anti-Corruption

- Principle 10: Businesses should work against corruption in all its forms, including extortion and bribery.*

** The Secretary-General introduced this principle at the Global Compact Leaders Summit on 24 June 2004.*

Working group and partner organisations

A working group including representatives of endorsing institutions was in charge of developing this report in the period between early March 2004 and the end of May 2004. It was facilitated by Ivo Knoepfel, on behalf of the Global Compact Office, represented by Gavin Power. The Swiss Government provided funding to facilitate the process and produce this report.

In addition to the Global Compact Office, The Conference Board, Columbia Business School and the UNEP Finance Initiative supported the work leading to this report. Their input and the support of many individuals involved is greatly appreciated.



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Exhibit 3

Members of the working group

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Exhibit 4

Acknowledgements

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Exhibit 5

Partner organisations

The Conference Board

The Conference Board creates and disseminates knowledge about management and the marketplace to help businesses strengthen their performance and better serve society. Working as a global, independent membership organization in the public interest, it conducts research, convenes conferences, makes forecasts, assesses trends, publishes information and analysis, and brings executives together to learn from one another. The Conference Board runs a total of 11 member Councils on corporate citizenship issues and a total of six Councils on corporate governance related aspects. Councils are membership groups joining executives with common responsibilities and interests to share solutions to business challenges.

Columbia Business School

Columbia Business School's Social Enterprise Program aims to inspire and prepare leaders who create social value in business, non-profit and government organizations. Situated in the world's financial capital and widely admired for its global and cutting-edge curriculum, Columbia Business School is one of the world's leading business schools. *Finance and Sustainability*, a course taught by Bruce Usher, will draw on insights from this project to prepare future leaders in finance to create social, environmental and economic value.

The UNEP Finance Initiative

The United Nations Environment Programme Finance Initiative (UNEP-FI) is a global public private partnership between the United Nations Environment Programme and 239 firms from across the global financial services sector. Its mission is to collaboratively integrate relevant environmental, social and corporate governance criteria into financial sector operations and services. The Asset Management Working Group (AMWG) of UNEP-FI includes 12 financial institutions and has actively contributed to drafting this report. Its goals are three-fold: 1. sector-specific financial analysis of ESG issues; 2. engagement with institutional investors; 3. ESG management as a risk mitigation option for emerging market investment.



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Introduction

In an increasingly complex and interconnected world, the importance of actively managing risks and opportunities related to emerging environmental and social trends, in combination with rising public expectations for better accountability and corporate governance, presents a new set of challenges with far-reaching financial consequences for corporations. This is true both at the level of companies and at the level of investment portfolios.

The financial industry has begun to acknowledge the importance of such issues and has engaged in a series of initiatives to improve their management in core business processes. Several institutions have implemented systems to manage environmental risks in their lending businesses. Other companies have engaged in initiatives aimed at improving accountability and governance or the integration of environmental and social aspects in project financing¹.

Until now, the industry has not developed a common understanding on ways to improve the integration of environmental, social and governance (ESG) aspects in asset management, securities brokerage services and the associated buy-side and sell-side research functions. This is due partly to the complexity and diversity of issues involved.

As more analysts and fund managers have begun to experiment with the integration of these issues, knowledge and awareness in the industry is increasing. Investors have also become more vocal in their demand for products and services incorporating such aspects. *We therefore believe that this is the right time to provide the industry with better guidance on ways to improve the consideration of environmental, social and governance issues in investment decisions.*

Throughout this report we have refrained from using terms such as sustainability, corporate citizenship, etc., in order to avoid

“Every corporation is under intense pressure to create ever-increasing shareholder value. Enhancing environmental and social performance are enormous business opportunities to do just that.”

Gary M. Pfeiffer
CFO, Du Pont

¹ For example, in the context of the recently released Equator Principles

misunderstandings deriving from different interpretations of these terms. We have preferred to spell out the environmental, social and governance issues which are the topic of this report.

This report focuses on issues which have or could have a material impact on investment value. It uses a broader definition of materiality than commonly used — one that includes longer time-horizons (10 years and beyond) and intangible aspects impacting company value. Using this broader definition of materiality, aspects relating to generally accepted principles and ethical guidelines (e.g. the universal principles underlying the Global Compact) can have a material impact on investment value.

Sound corporate governance and risk management systems are crucial pre-requisites to successfully implementing policies and measures to address environmental and social challenges. This is why we have chosen to use the term “environmental, social and governance issues” throughout this report, as a way of highlighting the fact that these three areas are closely inter-linked.

In particular, we believe that corporate governance systems can play a key role in implementing many of the recommendations in this report, particularly with regard to better transparency and disclosure, linking executive compensation to longer-term drivers of shareholder value and improving accountability.

Recently released recommendations on best practices in the corporate governance field, such as those released by The Conference Board Commission on Public Trust and Private Enterprise², lay out a corporate governance framework which in our view is crucial in order to successfully implement the recommendations outlined in this report.



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² *Conference Board Commission on Public Trust and Private Enterprise: Findings and Recommendations, 2004*



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Rationale and recommendations

1. General considerations

Ultimately, successful investment depends on a vibrant economy, which depends on a healthy civil society, which is ultimately dependent on a sustainable planet. In the long-term, therefore, investment markets have a clear self-interest in contributing to better management of environmental and social impacts in a way that contributes to the sustainable development of global society. A better inclusion of environmental, social and corporate governance (ESG) factors in investment decisions will ultimately contribute to more stable and predictable markets, which is in the interest of all market actors.

To some extent, financial markets are already factoring in environmental and social issues, but often only if they are seen as being material to value creation and risk in the short-term. In addition, we believe that markets do not yet fully recognise the importance of new emerging trends, such as the growing pressure on companies to improve corporate governance, transparency and accountability and the increasing importance of reputation risks related to ESG issues.

The integration of these aspects in investment decisions is increasingly viewed as falling within the scope of the fiduciary duty of trustees, financial advisers, asset managers and intermediary institutions. It therefore needs to be addressed effectively by all involved market actors.

We recognise that a series of barriers have in the past hindered a better integration of ESG factors. CEOs and CFOs recently interviewed by the World Economic Forum³, for example, stressed that intangible aspects related to ESG issues play an increasingly important role in value creation but that analysts' short-term focus

“Creating long-term value for our shareholders while concurrently ensuring the enduring viability of our human and natural resources is an important part of our business philosophy”.

Dr. Josef Ackermann
Chairman of the Group
Executive Committee
Deutsche Bank AG

hinders them in recognising this trend. Challenges cited by the WEF survey include:

- Problems of definition of ESG issues
- Problems of making and measuring the business case
- Problems with quality and quantity of information
 - Problems of skills and competence
 - Problems of differing time horizons

“Environmental and social issues count. (...) In an increasingly complex world we believe such issues are part of the relative quality of overall management performance needed to compete successfully.”

Goldman Sachs Global Investment Research

Additional challenges which have been mentioned by analysts and fund managers in past surveys related to the long-term nature of many ESG issues and the uncertainty about future regulation in this area.

Throughout this report we will address these obstacles and show how they could be overcome. Obstacles related to time horizons and regulation are addressed in chapter 1, obstacles related to defining and measuring the business case in chapter 2, obstacles related to skills and competences in chapters 4 and 6, and obstacles related to information in chapter 5.



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Recommendations:

- a. ***We are convinced that it is in the interest of investors, asset managers and securities brokerage houses alike to improve the integration of ESG factors in financial analysis. This will contribute to better investment markets as well as to the sustainable development of the planet.***

- b. ***We invite all financial market actors, including investors, asset managers, analysts, financial advisers and consultants to improve their understanding and consideration of these trends and related potential impacts. This will not be possible without adequate disclosure on these matters by companies.***

- c. ***The use of longer time horizons in investment is an important condition to better capture value creation mechanisms linked to ESG factors. We therefore invite investors and other market actors to include longer time horizons in investment mandates and to request research supporting this development.***

- d. ***We urge regulators to be transparent with regard to the nature and timing of new regulations concerning ESG issues relevant to investment. This will make regulatory changes more predictable and quantifiable for financial markets and will support integration in financial analysis.***

Exhibit 6

A selection of ESG issues impacting company and investment value

ESG issues relevant to investment decisions differ across regions and sectors. The following are examples of issues with a broad range of impacts on companies:

Environmental issues:

- Climate change and related risks
- The need to reduce toxic releases and waste
- New regulation expanding the boundaries of environmental liability with regard to products and services
- Increasing pressure by civil society to improve performance, transparency and accountability, leading to reputational risks if not managed properly
- Emerging markets for environmental services and environment-friendly products

Social issues:

- Workplace health and safety
- Community relations
- Human rights issues at company and suppliers' /contractors' premises
- Government and community relations in the context of operations in developing countries
- Increasing pressure by civil society to improve performance, transparency and accountability, leading to reputational risks if not managed properly

Corporate governance issues:

- Board structure and accountability
- Accounting and disclosure practices
- Audit committee structure and independence of auditors
- Executive compensation
- Management of corruption and bribery issues



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Exhibit 7

World Economic Forum Initiatives

Survey of CEOs and CFOs on communication with the financial community

In January 2004, the World Economic Forum's Corporate Citizenship Initiative released results of a survey of CEOs and CFOs of member companies focusing on the communication of corporate citizenship to investors and financial institutions ⁴.

Surveyed CEOs/CFOs note many positive signs with regard to an increasing interest and activity by investors, analysts and financial institutions concerning ESG matters. 70% of respondents "expect to see increased interest in ESG issues by mainstream investors in the future".

But they also highlight what they perceive as being key obstacles to mainstream investors who show more interest in how corporations address ESG risks and opportunities:

- Problems of definition of ESG issues
- Problems of making and measuring the business case
- Problems with quality and quantity of information
- Problems of skills and competence
- Problems of differing time horizons

In terms of interest from mainstream investors, just over two-thirds of the companies that participated in the survey claimed that "they are occasionally asked questions about their corporate citizenship activities, but usually only when there has been a crisis related to their industry or company, or around certain 'hot' topics such as climate change, diversity, obesity and HIV/AIDS". The head of investor relations at one company reflected the comments of many others, "These issues never come up unless there is a problem — no one cares unless there's a financial risk or short-term exposure." One CFO commented, "With a few honourable exceptions, most mainstream investors ask little or nothing about social responsibility. That might change in the event of a serious environmental/community/political incident, which raised questions about the company's performance."

⁴ *World Economic Forum: Values and Value — Communicating the strategic importance of corporate citizenship to investors, 2003 CEO Survey*

Initiative on corporate citizenship and investment

WEF's Global Corporate Citizenship Initiative, in association with AccountAbility, is also exploring how best to improve the understanding of concrete impediments to, and opportunities for, the broader integration of the social and environmental aspects of corporate citizenship in mainstream investment policies and practices. The initiative is grounded in a series of international roundtables with some of the financial sector's most important actors from pension funds, asset management companies and regulators. The initiative will offer insights into how best to impact information, competencies and incentives along the investment value chain. Results will be published in a WEF/AccountAbility report in October 2004.



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2. Investment rationale

The investment rationale for more rigorous inclusion of ESG criteria in financial analysis rests on the business case at the level of the company. Several recent studies of companies and industries have contributed to better understanding the value drivers through which good management of ESG issues contributes to shareholder value creation.

Furthermore, many studies confirm that the way a company manages ESG issues is often a good indicator of overall risk levels and general management quality — which are both strong determinants of companies' long-term success. A recent report on the oil and gas industry by Goldman Sachs, for example, concludes that companies with the best track record in terms of social responsibility and a long-term vision about a low-carbon future also dominate the market share of strategic projects, which is seen as a key determinant of business success.

Companies with better ESG performance can increase shareholder value by better managing risks related to emerging ESG issues, by anticipating regulatory changes or consumer trends, and by accessing new markets or reducing costs. Instead of focusing on single issues, successful companies have learned to manage the entire range of ESG issues relevant to their business, thereby achieving the best results in terms of value creation. Moreover, ESG issues can have a strong impact on reputation and brands, an increasingly important part of company value. It is not uncommon that intangible assets, including reputation and brands, represent over two-thirds of total market value of a listed company. It is likely that ESG issues will have an even greater impact on companies' competitiveness and financial performance in the future.

It is interesting to note that, when asked, both investors/asset managers and company representatives confirm the increasing

“Considering that a large share of company value is intangible and relates to future earnings, it is evident that risks and opportunities deriving from environmental and social trends are of great importance”.

Martin Hancock
Chief Operating Officer
Westpac, London Branch

“The Corporate Social Responsibility imperative is one which, we believe, will increase in importance over time. (...) Looking at CSR could improve stock picking ability”.

**ABN Amro
Equities Research**

importance of intangible ESG factors in shareholder value creation. In a survey by Cap Gemini Ernst & Young, for example, 81% of Global 500 executives rated environmental, health and safety issues among the top ten factors driving value in their businesses. In a survey by CSR Europe, Deloitte and Euronext, 40% of interviewed fund managers and analysts, and over 50% of investor relations officers, confirmed a significant contribution to value creation by intangible aspects.

“Even within the same industry — electric utilities — the level of financial risk exposure to regulatory responses to climate change can vary by a factor of 30”.

Matthew Kiernan
CEO, Innovest Strategic
Value Advisors



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Recommendations:

- e. ***We call on financial analysts to take an active role in testing and refining the investment rationale for ESG integration in research and investment decisions. We invite analysts not only to focus on ESG risks and risk management, but also to consider ESG issues as a potential source of competitive advantage.***

- f. ***We invite academic institutions, business schools and research think-tanks to support financial analysts' work in this field by contributing forward-thinking research on ESG risks and opportunities and the related business and investment case, of both a strategic and quantitative nature.***



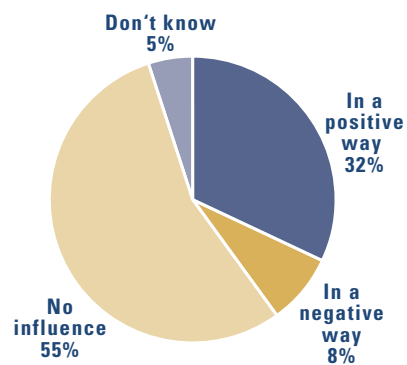
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Exhibit 8

The view of fund managers, analysts and investor relations officers

A recent survey conducted among European fund managers, analysts and investor relations officers⁵ found that in the opinion of 78% of fund managers and analysts, the management of environmental and social risk has a positive impact on a company's long-term market value. In the case of a shorter time horizon (3-12 months), only 32% of respondents believe that environmental and social risk management significantly impact market value.

A company's short-term market value



A company's long-term market value

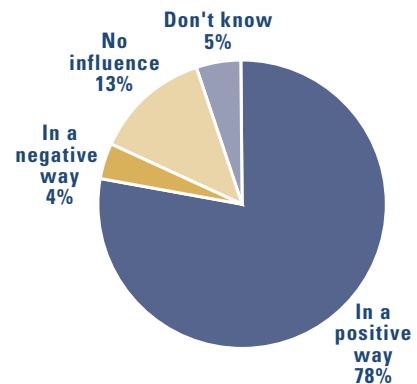


Figure 1: Results of the CSR Europe, Deloitte and Euronext survey of European fund managers, analysts and investor relations officers. Reply to the question: "Based on your experience, how does social and environmental risk management impact on a company's short-term/long-term market value?"

⁵ CSR Europe, Deloitte, Euronext, *Investing in Responsible Business. The 2003 survey of European fund managers, financial analysts and investor relations officers.*

Exhibit 9

Drivers through which good management of ESG issues can contribute to shareholder value creation:

- Early identification of emerging risks, threats, management failures
- New business opportunities
- Customer satisfaction and loyalty
- Reputation as an attractive employer
- Alliances and partnerships with business partners and stakeholders
- Enhanced reputation and brands
- Reduced regulatory intervention
- Cost savings
- Access to capital, lower cost of capital
- Better risk management, lower risk levels



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Exhibit 10

Environment, Healthy and Safety (EHS) performance as an intangible driver of market value

In February 2004, a study released by the Global Environmental Management Initiative⁶, based on earlier research by Cap Gemini Ernst & Young^{7 8}, came to the conclusion that:

- 50 to 90% of a firm's market value can be attributed to intangibles like EHS.
- 35% of institutional investors' portfolio allocation decisions are based on intangibles like EHS performance.
- 81% of Global 500 executives rate EHS issues among the top ten factors driving value in their businesses.

⁶ GEMI: *Clear Advantage: Building Shareholder Value*, February 2004.

⁷ Cap Gemini Ernst & Young: *Measures that Matter*, 1996 (a survey of 300 sell-side analysts, 275 buy-side analysts, as well as interviews with portfolio managers)

⁸ Cap Gemini Ernst & Young: *Decisions that Matter*, 1999 (a survey of financial executives at global 500 corporations).



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Exhibit 11

Goldman Sachs Energy Environmental and Social Index (A. Ling, J. Waghorn, S. Forrest, M. Lanstone, Feb. 2004)

Goldman Sachs (GS) recently released the Goldman Sachs Energy Environmental and Social (GSEES) Index for the energy sector as a response to UNEP Finance Initiative's call for better research in this field. The scope of GSEES is to identify specific environmental and social issues likely to be material for company competitiveness and reputation in the oil and gas industry and, to the extent possible, to quantify their potential impact on stock prices. 30 criteria in the following eight categories have been used, including environmental and social issues:

- Climate change
- Pollution
- Human rights
- Management diversity and incentives
- Investment in the future
- Workforce
- Safety
- Transparency and vision

Rationale

To succeed in the rapidly evolving energy industry, GS believes companies have to win, and then operate, larger, more complicated projects, often in new regions (so-called "new legacy assets"). Competition is more intense, the workforce smaller and external observers less forgiving. The analyst team that worked on the GSEES Index set out to explore a potential correlation between environmental and social management quality and the capability to succeed in winning and managing new legacy assets.

GS notes that ultimately the industry is moving from the age of oil to the age of gas, and potentially to an even lower carbon world. To succeed in this new world, GS believes companies must be both environmentally and socially aware, in order to succeed in managing a

diverse workforce in a socially responsible and acceptable manner with a vision of the evolution of the industry towards the age of gas. An increased focus on climate change and corporate governance, together with the rise of socially responsible investment (SRI)-managed money and non-governmental organisation (NGO) activity, are additional issues that the industry needs to manage.

Main conclusions from the GSEES Index

Based on the experience of calculating the Index and on its results, GS concludes that one-off environmental and social issues have limited impact on share prices unless they have a material impact on the underlying returns of the company in question. A strong performance in social and environmental issues is no guarantee of stock market performance. That said, GS notes that social and environmental issues are having an increasing impact on companies' future project slates. GS believes that this will have an increasing impact on future returns, and therefore valuation and share price performance.

In addition, GS notes that those companies with the best track record in terms of social responsibility and a vision of a low-carbon world for the future (i.e. with the best GSEES scores) dominate the market share of new legacy projects, a strong determinant of business success. GS adds that "It stands to reason that the best-managed companies deliver the best performance with regard to social and environmental issues and their interaction with the general business community. It is not surprising that they manage these issues as well as they manage the other more traditional success factors".

Detailed results

The GSEES Index was created by scoring companies relative to each other on metrics within the defined eight categories. GS found significant differences in performance across categories, but some companies score consistently well, notably BP, RD/Shell, Statoil and ExxonMobil. BP and RD/Shell's scores are 8% higher than that of their nearest peer, ExxonMobil.



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Goldman Sachs Scenario

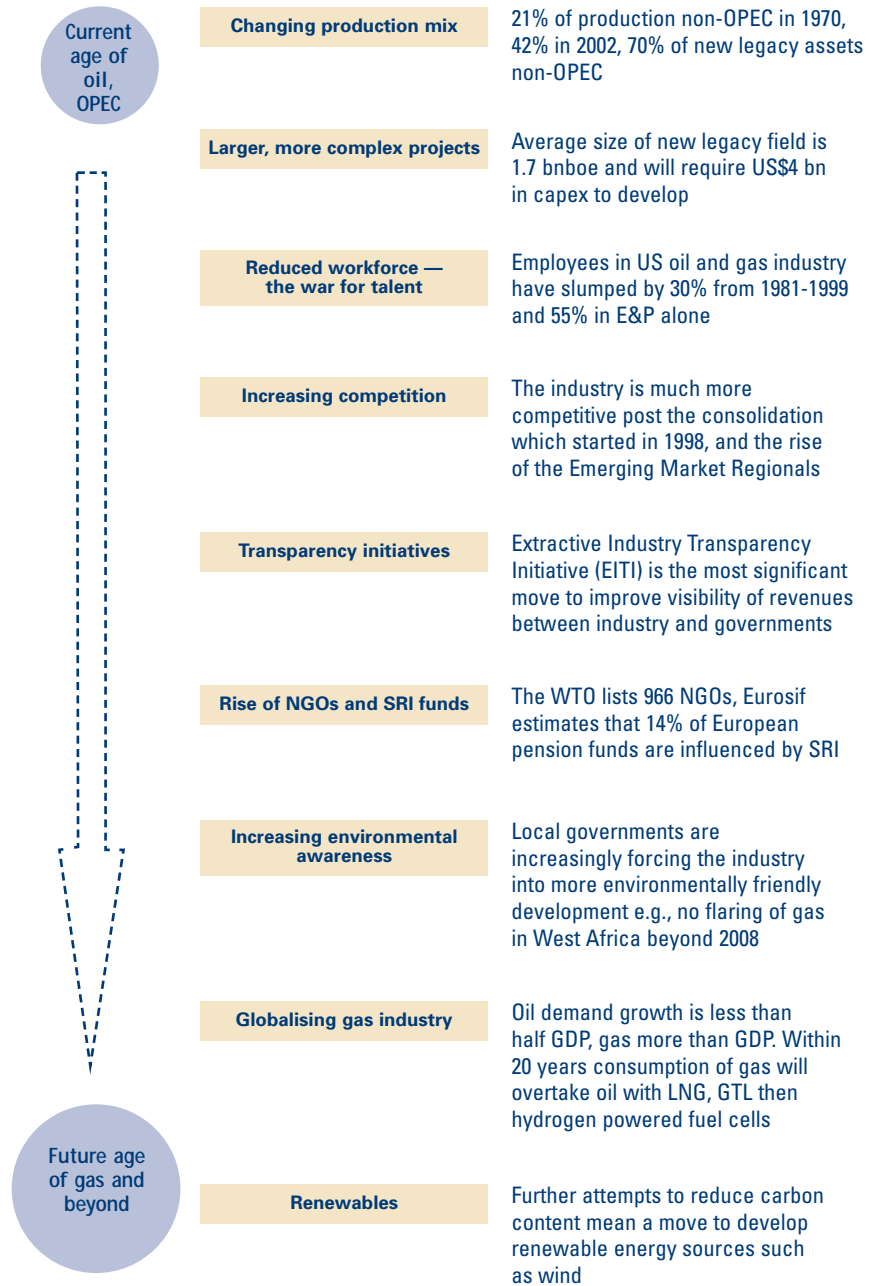


Figure 2: Evolution of the industry towards the age of gas and renewables⁹

⁹ Goldman Sachs Global Investment Research — February 24, 2004

Goldman Sachs Energy Environmental and Social Index

Company	Climate Change	Pollution	Human Rights	Management Diversity and Incentives	Investment in the Future	Workforce	Safety	Transparency and Vision
BP	23	3	11	20	6	22	21	14
RD/Shell	22	3	9	21	8	19	21	14
Statoil	18	7	11	18	5	19	18	13
ExxonMobil	13	3	8	18	8	23	23	12
Norsk Hydro	18	8	10	13	7	16	17	10
TOTAL	19	4	9	18	10	19	9	9
ChevronTexaco	14	3	10	20	8	19	13	8
BG	17	8	10	15	5	13	16	10
ENI	15	8	10	16	6	13	12	10
OMV	15	5	9	15	6	12	13	10
ConocoPhillips	12	6	9	20	7	11	8	11
Amerada Hess	14	5	10	15	2	11	11	11
Occidental	10	5	6	21	2	9	14	9
Marathon	5	3	6	20	2	15	17	7
Repsol	15	3	10	12	6	12	5	11
Petrobras	5	5	7	13	3	13	13	7
CNOOC	5	8	6	13	3	13	9	8
PetroChina	5	5	7	17	4	10	7	8
MOL	7	2	7	10	6	8	12	10
Sinopec	5	3	6	11	6	12	5	8
Yukos	7	4	7	10	2	7	5	5
Lukoil	5	4	6	12	2	8	5	4
CEPSA	5	2	5	13	2	9	5	4
Average	11.9	4.7	8.2	15.7	5.0	13.6	12.1	9.3
Maximum	25	8	12	23	10	25	25	14



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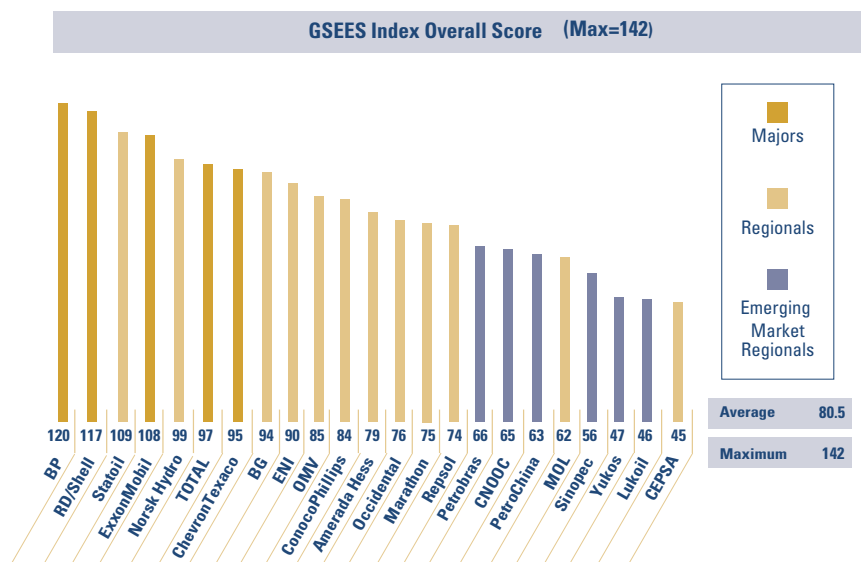


Figure 3: Company relative positioning on the Goldman Sachs Energy Environmental and Social Index¹⁰

¹⁰ Goldman Sachs Global Investment Research — February 24, 2004



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Exhibit 12

Case-study on the automobile industry

(Sustainable Asset Management and World Resources Institute, *Changing Drivers: The Impact of Climate Change on Competitiveness and Value Creation in the Automotive Industry*, October 2003.)

In a 2003 report, SAM and WRI used conventional shareholder valuation techniques to demonstrate how emerging policies to tackle climate change could alter discounted future earnings for the ten largest global auto companies.

Emerging climate policies create both financial risks and opportunities for auto manufacturers. The report used scenarios of future regulatory policies and industry commitments to identify possible cost and earnings trajectories for the auto companies over the next decade. The analysis paired data on ESG factors, such as the CO₂ emissions intensity of specific vehicle models, with conventional investment data, such as sales volumes and profit margins. The analysis also explicitly assessed the quality of management in addressing climate change issues.

From discussions with auto analysts, it appears that the mid- to long-term impacts of climate change policy are not currently “priced in” to auto company stock values. Yet, the SAM/WRI analysis shows that pricing in the impact of climate change policies could significantly affect earnings (see Figure 4). Moreover, companies are very differently positioned on this issue, indicating that climate change will be a new and additional influence on competitiveness within the industry.



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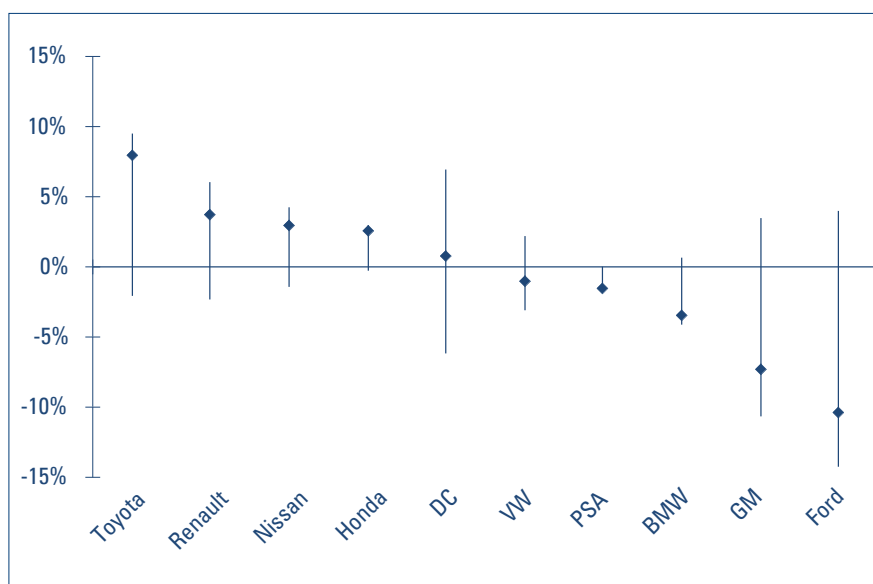


Figure 4: Potential Impact of Climate Change Policies for Earnings of Leading Auto Companies (Percentage Change in EBIT Forecasts (2003-2015) from Pricing in Climate Change Policies) Source: SAM/WRI, *Changing Drivers*, 2003. Note: Vertical lines indicate possible ranges for discounted EBIT; dots indicate “most likely” forecast EBIT.

Exhibit 13

The view of fund managers, analysts and investor relations officers

A recent survey of European fund managers, analysts and investor relations officers indicates that the link between intangible assets and shareholder value is widely acknowledged by the financial industry¹¹. The ability to innovate (65%), and corporate governance and risk management (54%) were mentioned as top-ranking issues systematically taken into account by fund managers and analysts. Environmental impact management and supply chain management were ranked highly as being integrated for some sectors or companies. This reflects the need for a sector-specific approach in terms of both the company’s communication approach and financial analysis.



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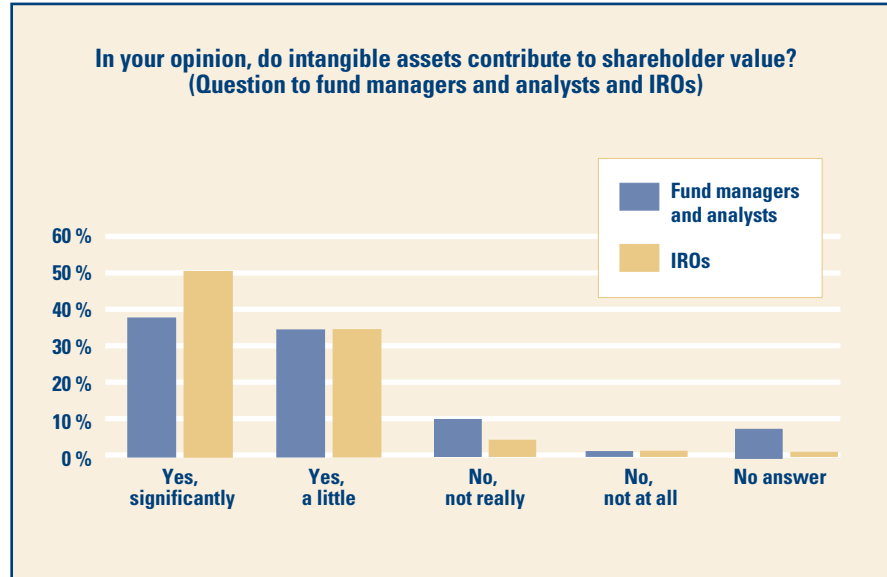


Figure 5: Results of the CSR Europe, Deloitte and Euronext survey of European fund managers, analysts and investor relations officers¹²

¹¹ CSR Europe, Deloitte, Euronext: Investing in Responsible Business. The 2003 survey of European fund managers, financial analysts and investor relations officers.

¹² CSR Europe, Deloitte, Euronext: Investing in Responsible Business. The 2003 survey of European fund managers, financial analysts and investor relations officers.



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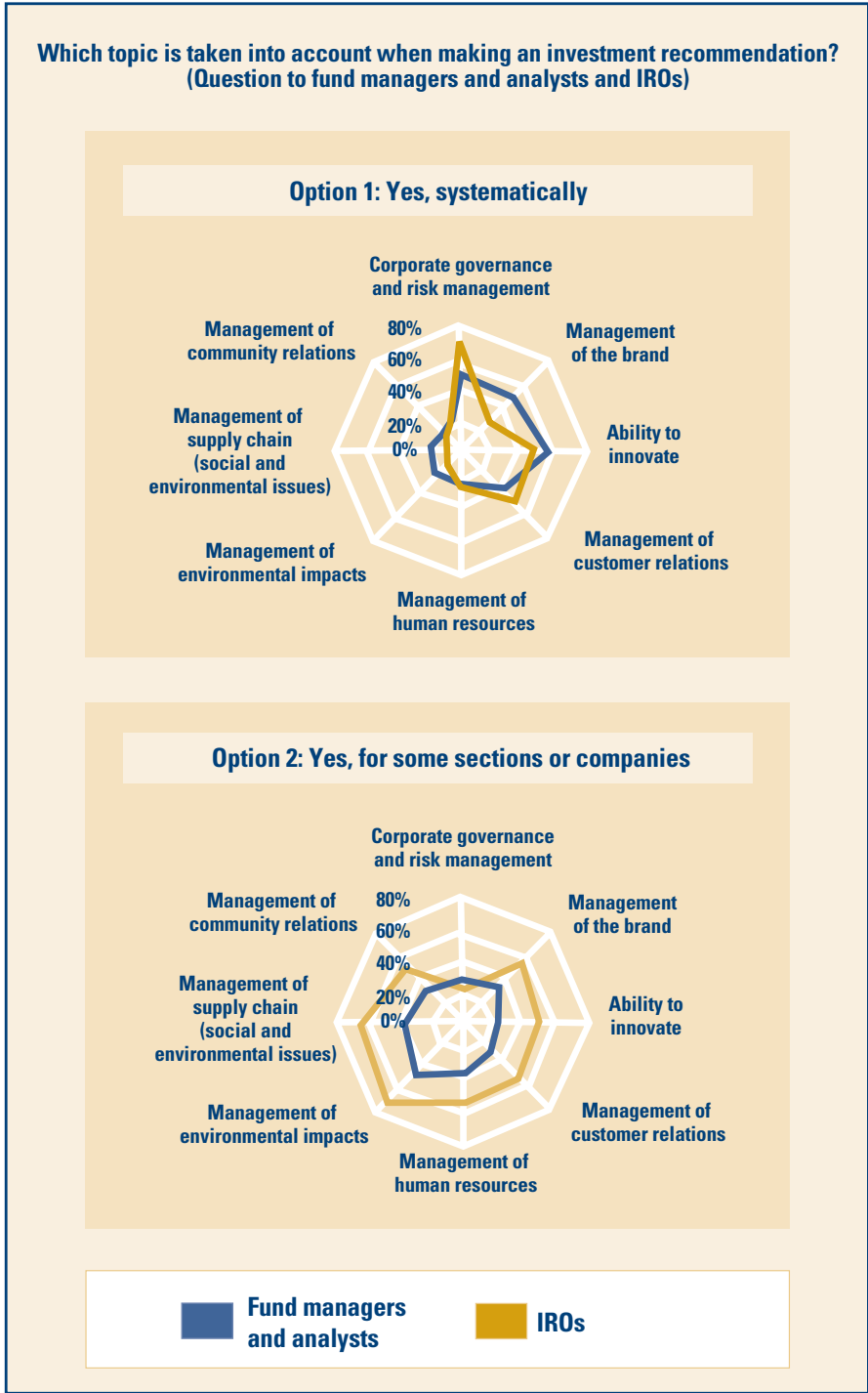


Figure 6: Results of the CSR Europe, Deloitte and Euronext survey of European fund managers, analysts and investor relations officers ¹³

¹³ CSR Europe, Deloitte, Euronext: Investing in Responsible Business. The 2003 survey of European fund managers, financial analysts and investor relations officers.



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3. Meeting clients' needs

Recently, institutional investors have launched a series of joint initiatives calling on companies to improve disclosure and on investors and asset managers to improve their consideration of ESG aspects in investment decisions and in engaging with companies. A wide range of issues and sectors has been touched upon by these initiatives, including climate change, corporate governance, issues relating to the pharmaceutical industry, the disclosure of payments to governments and the management of corruption and bribery cases.

We welcome these initiatives because they support better disclosure and transparency by companies and the efforts of financial market actors to better integrate these issues in the investment value-chain. Clearly, it is client demand that will most effectively trigger change in the financial industry. That said, we believe that in addition to requesting better integration of ESG factors, clients must also be prepared to explicitly demand and reward better research and investment services taking into account ESG aspects.

Given the importance of pension funds in the world of asset management, trustees and their consultants can play a pivotal role in requesting better coverage of ESG issues in investment mandates and the underlying research. Consultants and financial advisers also have an important role to play in creating greater and more stable demand for ESG research.

Sell-side analysts have in the past demonstrated their preparedness in effectively responding to an explicit request by clients. A recent example was the call by the members of the UNEP Finance Initiative Asset Management Working Group requesting

“There is a growing body of empirical evidence that companies which manage environmental, social and governance risks most effectively tend to deliver better risk-adjusted financial performance than their industry peers”.

Jean Frijns
Chief Investment Officer
ABP

“The consideration of material social and environmental issues should be part of every financial analyst’s normal work. Not only does this make sense from an investment risk perspective; institutional clients are increasingly asking for better integration in fund management”.

Thomas Albrecht
Director of Research
Credit Suisse Asset
Management

ESG research from financial research organisations. Within a period of only 8 months, research organisations produced a total of 11 reports on a wide range of industries and issues.



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Recommendations:

- g. We encourage pension fund trustees and their selection consultants to consider integrating ESG issues into the formulation of investment mandates and the selection of investment managers, taking into account their fiduciary obligations to participants and beneficiaries. We believe that governments and multilateral agencies should proactively consider the investment of their pension funds according to the principles of sustainable development, taking into account their fiduciary obligations to participants and beneficiaries.***
- h. Consultants and financial advisers should support the integration of ESG criteria by combining ESG research with industry level research and sharing their experience with financial actors and companies in order to improve ESG reporting.***
- i. We urge investors to explicitly request and reward research that includes environmental, social and governance aspects and to reward well-managed companies. Asset managers should integrate research on such aspects in investment decisions and encourage brokers and companies to provide better research and information.***
- j. We encourage brokers and asset managers to more actively forge partnerships with institutional clients with a stated or potential interest in ESG research***



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and raise the awareness of clients on the relevance of ESG issues to their investments.

- k. We invite investors to develop proxy voting guidelines clarifying their position on ESG issues. This will support asset managers and analysts in producing relevant research and implementing proxy voting strategies.***

Exhibit 14

Recent initiatives by institutional investors on ESG issues:

- The Carbon Disclosure Project, calling on companies to provide investment-relevant information relating to greenhouse gas mitigation
- The Institutional Shareholders Committee Principles, issued by a group of large institutional investors, calling on fund managers to take a more active approach in relation to their engagement with companies, which should include ESG issues
- The Pharmaceutical Shareowners Group's call for better disclosure in the pharmaceutical industry
- The Investor's Statement on Transparency in the Extractives Sector, aimed at increasing the transparency of payments made by extractive sector companies to governments and government-linked entities
- The U.S. Investor Network on Climate Risk, a group of US State and City Treasurers and Trustees with fiduciary responsibility for some of America's largest and most influential pension and labour funds, which recently called for greater investor focus on climate change risks and opportunities
- The UK Institutional Investors Group on Climate Change, with similar goals as the U.S. Investor Network on Climate Risk
- To be noted is also a 15% increase in U.S. shareholder resolutions relating to ESG issues from January 2001 to June 2003.

Exhibit 15

Investor networks on climate change

In November 2003, the United Nations convened a summit of institutional investors in the US controlling more than \$1 trillion in assets, including several state and city treasurers, to discuss climate change risks. This group set up an Investor Network on Climate Risk and issued a 10-point call for action, including¹⁴:

- The SEC to enforce corporate disclosure of climate change risks
- Companies in major greenhouse gas-producing sectors (e.g. autos, power utilities) to report to shareholders on the financial implications of climate change — including regulation and competition
- Investment managers to include climate change in their analyses.

Speaking at the summit, California State Treasurer Phil Angelides commented, “In global warming, we are facing an enormous risk to the US economy and to retirement funds that Wall Street has so far chosen to ignore. The corporate scandals over the last couple of years have made it clear that investors need to pay more attention to corporate practices that affect long-term value. As fiduciaries, we must take it upon ourselves to identify the emerging environmental challenges facing the companies in which we are shareholders, to demand more information, and to spur needed actions to respond to those challenges.”

In the UK, the Institutional Investors Group on Climate Change brings together 19 funds with assets totalling £450 billion to focus on investment risks and opportunities in this area. It has produced reports on aviation and power generation, analysing the investment issues from a move to a low-carbon economy. In both cases, the analysis concluded that the sectors would be significantly affected, and that the impacts would vary significantly from company to company, with clear implications for sector weightings and stock selection.¹⁵

¹⁴ Association of British Insurers, *Risk Returns and Responsibility*, Author: Roger Cowe, Feb. 2004

¹⁵ Association of British Insurers, *Risk Returns and Responsibility*, Author: Roger Cowe, Feb. 2004



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Exhibit 16

Financial research organisations respond to buy-side call for more ESG research

The Asset Management Working Group (AMWG) of the UNEP Finance Initiative, comprising 12 financial institutions managing total assets of about 1.6 trillion USD, recently invited leading financial research institutions from around the world to produce sector-specific reports that would:

1. Identify the specific environmental and social issues that are likely to be material for company competitiveness and reputation in that particular industry
2. Identify and to the extent possible quantify their potential impact on stock price

The outcomes in terms of sector specific reports and insights with regard to the relevance of ESG issues will be summarised in a separate report and presented at the U.N. Global Compact Leader Summit in June 2004. Pending approval from the AMWG members, a second invitation will be launched in Q3 2004. A wide range of financial research institutions has responded to this call. The contributing institutions and the titles of their reports are noted below:

1. Deutsche Bank Global Equity Research: Beyond the Numbers — Corporate Governance: Implication for Investors
2. Deutsche Securities South African Equity Research: No Evidence to Link Share Ratings with Good Corporate Citizenship...Yet
3. NikkoCitigroup Japan Equity Strategy: Environmental Technologies Fuelling Zones of Growth
4. Goldman Sachs Global Energy: Introducing the Goldman Sachs Energy Environmental and Social Index
5. ABN AMRO Equities United Kingdom: Pharmaceuticals
6. West LB Equity Markets Pan-European Equities: Insurance and Sustainability: Playing with Fire
7. Nomura Japanese Equity Markets: Corporate social responsibility (CSR) in the nonlife insurance sector
8. HSBC: European Utilities
9. UBS Global Equity Research: European Emissions Trading Scheme — Bonanza or Bust
10. Dresdner Kleinwort Wasserstein Europe / Equity: Utilities — Emission trading — Carbon Derby Part II: And they're off
11. Dresdner Kleinwort Wasserstein UK / Europe / Equity : Transport — Aviation emissions: Another cost to bear

Exhibit 17

Increasing integration of ESG factors in UK pension funds' management

According to a recent study by the Association of British Insurers¹⁶, the knowledge of and interest in ESG aspects among pension trustees is constantly increasing. The study cites a recent survey of 70 UK pension funds by the research organisation EIRIS. The picture that emerges is of trustees concerned about ESG criteria, but relying largely on fund managers to take the initiative.

Following an amendment to the Pensions Act which came into effect in 2000, trustees are now required to include in their Statement of Investment Principles (SIP) comment on the extent to which (if at all) their investment decisions take account of social, environmental and ethical issues. Research has shown that many trustees have responded positively to this requirement. Almost £90 billion of pension funds' UK equity holdings are now subject to some form of socially responsible investment policy, equivalent to almost a quarter of the sector's total UK holdings. This figure is based on SIP statements. In practical terms, in many cases this has not led to substantial change in investment practice.

Of the 70 responses to the EIRIS poll (mostly from the private sector), 90% said their investment strategy did take account of Social, Environmental and Ethical (SEE)¹⁷ factors. The survey also highlighted the increasing activity of pension funds in integrating SEE aspects in their management of funds:

- 59% of funds said they consider SRI experience and performance when appointing or reappointing investment managers
- 54% of the funds' pensions managers/trustees have received training on incorporating SEE issues into investment strategy
- 59% said they have asked their investment managers to consider the financial implications of SEE factors when assessing the risk and returns of each company
- 11% undertake some form of screening and/or preference weighting in relation to SEE issues
- 87% say they exercise voting rights on SEE grounds.

¹⁶ Association of British Insurers, *Risk Returns and Responsibility*, Author: Roger Cowe, Feb. 2004

¹⁷ Social, Environmental and Ethical (SEE)



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4. Integration in financial analysis

Until now, efforts to integrate ESG aspects in financial analysis have focused on specific sectors, such as the energy, extractive, automobile, utilities, pharmaceutical and chemical industries, which are perceived as being more exposed to these aspects. Analysts in these sectors have started to collect information, and to deepen their understanding and analytical skills with regard to ESG issues. Their experience is invaluable in expanding the scope to other industries.

Financial institutions have recently begun to consider ESG factors in a more systematic way across all industries and across different asset classes. Even though ESG aspects are particularly important for equity analysis, the importance for other asset classes such as fixed-income, private equity and real estate investments also needs to be considered.

Because of their importance to global growth, emerging markets should receive particular consideration and ESG criteria will need to be adapted to the specific situation in these markets. Emerging countries will become increasingly important in terms of delivering sustained economic growth, of enabling investors to diversify their portfolios and in terms of their role in the context of sustainable development.

In order to improve the inclusion of ESG factors in financial analysis it will often be necessary to adapt current analytical models and tools. In particular, including qualitative information on competitive advantages of well-managed companies or on the impact of emerging risks must be improved.

We believe systematic evaluation of corporate governance, environmental and social responsibility through “extra-financial” analysis provides a better view of investment risks and opportunities.

Philippe Lespinard
Chief Investment Officer
BNP Paribas Asset
Management

“Environmental and related social issues in transactions are becoming an integral part of our risk analysis”

David Bushnell
Head of Risk Management
Citigroup Global Corporate
and Investment Bank

Recommendations:

- l. Building on the existing awareness for ESG factors in exposed industries, financial analysts should expand their understanding and analysis of these factors to other industries.***

- m. While supporting a thoughtful and creative process led by the analysts, we encourage financial institutions to explore ways to more systematically integrate ESG issues in research. We encourage analysts to prioritise ESG issues on the basis of their potential impact on financial value and on a sector-by-sector basis. In each case the time scale over which issues might become relevant should be analysed. Financial institutions should support the work of analysts with the necessary training, resources and tools.***

- n. Financial analysts should improve their understanding and integration of ESG issues in emerging markets research. They should take into account that criteria and methodologies must be adapted to the specific situation in emerging countries.***

- o. We invite financial institutions to expand the scope of ESG integration in research to other asset classes impacted by ESG factors, beyond equity.***

- p. We encourage analysts to further advance the development of valuation methodologies to better deal with qualitative information and uncertain impacts related to ESG issues. Specific techniques such as scenario models, options pricing, etc., might prove useful in this context.***



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Exhibit 18

Examples of traditional and emerging ESG issues in different sectors¹⁸

Sector	Traditional issue	Emerging issue
Oil and gas	<ul style="list-style-type: none">• Oil spills• CO2 emissions	<ul style="list-style-type: none">• Socio-economic impacts• Government relations and revenue sharing
Food industry	<ul style="list-style-type: none">• Food safety• Brand and reputation risk	<ul style="list-style-type: none">• “Functional food” regulation• Nutritional value, especially in low-income diets
Pharmaceuticals	<ul style="list-style-type: none">• Bio-safety• Animal welfare	<ul style="list-style-type: none">• Role re. national healthcare systems• Patent rights• Environmental effects of compounds
Automotive	<ul style="list-style-type: none">• Safety requirements• CO2 emissions	<ul style="list-style-type: none">• Mobility and socio-economic impacts• Low emission regulations

¹⁸ Arthur D. Little and *Business in the Community, Speaking the Same Language*, 2003

Exhibit 19

Taking into account the specific situation of emerging countries

ESG issues are as important, and perhaps more important, in emerging market investment analysis in terms of financial materiality, reputation management and good corporate citizenship as compared to developed market analysis. This is because:

- Regulation and enforcement are typically weak
- Many of the world's most economically important non-renewable and renewable resources are located in developing countries
- Developing countries are also where the world's most pressing environmental and social problems are caused and/or felt
- Companies are in general more involved in shaping markets and more exposed to government and societal expectations.

In this context it will be important to support capacity building for better management of ESG issues by local companies and financial markets, bearing in mind that this process will take time and will need to take into account local cultural and economic realities. U.N. or investor-led initiatives could play an important role in this field. An example of such an initiative is the Hong-Kong based Association for Sustainable & Responsible Investment in Asia (ASRIA).



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5. Transparency and disclosure

Efforts by financial markets to improve the integration of ESG factors in financial analysis and investment will not be successful without adequate disclosure on these matters by companies. Transparency and disclosure are therefore crucial elements of better functioning markets in this field.

The quantity and quality of companies' reporting on ESG issues has increased rapidly in recent years. In its international survey of corporate sustainability reporting, KPMG concludes that reporting in this area is becoming mainstream with 45% of global Fortune 250 companies regularly disclosing related information compared to 35% in 1999¹⁹.

Fund managers and analysts, on the other hand, when asked if they are satisfied with the information they receive from companies answer "No" by a wide majority of over 55%²⁰. Something is clearly not working in the communication between companies and financial markets on these issues. Analysts confirm that a lot of information is available, but that it is not presented in a consistent and meaningful way and its relevance for the core business of the company is not explained. That said, it is also true that analysts often do not show much interest in this type of information.

This situation must be unlocked. We welcome the recommendations by the U.N. Global Compact which cover four areas of "good communications practice" with investors:

- Communicate a leadership commitment toward values-based management
- Emphasise the social contribution of the core business

"These issues are raised more often and in an increasingly knowledgeable and professional manner at investor meetings".

Anthony Trahar
CEO
Anglo American Plc.

¹⁹ KPMG International Survey of Corporate Sustainability Reporting 2002, The Netherlands, 2002.

²⁰ CSR Europe, Deloitte, Euronext: Investing in Responsible Business. The 2003 survey of European fund managers, financial analysts and investor relations officers.

- Develop a credible and measurable business case for corporate citizenship
- Communicate change in a consistent and coherent manner

We also believe that regulatory frameworks requiring a minimum degree of disclosure and accountability on ESG issues would improve the availability and comparability of data, and therefore support integration in financial analysis. Stock exchanges, for instance, could include ESG criteria in listing particulars for companies. Both voluntary and market-friendly regulatory approaches are needed to improve disclosure. Both should be flexible enough to allow for diversity of approaches and providers, rather than relying on rigid prescriptions.

We are also convinced that international and national accounting bodies and rating agencies are key players in developing better standards and achieving a better quality and availability of useful ESG information. Non-governmental organisations (NGOs) can also contribute to better transparency by providing objective ESG information on companies to the public and the financial community.



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Recommendations:

- q. ***We invite companies to take a leadership role by implementing ESG principles and policies and to provide information and reports on ESG issues in a more consistent and standardised format, and to explain their relevance to value creation. Companies are invited to identify and communicate key challenges and drivers and prioritise ESG issues accordingly. We believe that this information is best conveyed to financial markets through normal Investor Relation communications channels. We also encourage, when relevant, an explicit mention in the Annual Report of companies.***
- r. ***Companies are encouraged to facilitate a constructive dialogue with asset managers and analysts and***



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accept both positive and more critical outcomes of ESG analyses.

- s. Analysts should improve their understanding of the link between ESG performance and value creation and more actively communicate with companies on these issues.***
- t. We believe that regulatory frameworks should require a minimum degree of disclosure and accountability on ESG issues, but rely on market-driven voluntary initiatives to formulate detailed standards.***
- u. We encourage financial analysts to participate more actively in ongoing voluntary initiatives, such as the Global Reporting Initiative, and help shape a reporting framework that responds to their needs. We also encourage the Global Reporting Initiative to closely cooperate with national and international financial analysts associations.***
- v. We encourage stock exchanges to include ESG criteria in listing particulars for companies, because this will ensure a minimum degree of disclosure across all listed companies. As a first step, stock exchanges could communicate to listed companies the growing importance of ESG issues. Similarly, other self-regulatory organizations (e.g. NASD, FSA), professional organizations (e.g. AIMR, EFFAS), accounting standard-setting bodies (e.g. FASB, IASB), public accounting entities, rating agencies and index providers should all establish consistent ESG standards and frameworks.***

Exhibit 20

Investor initiatives for better disclosure in the pharmaceutical and extractive industries²¹

In March 2003, 12 institutional investors issued a framework for pharmaceutical companies to improve disclosure in annual/social reports in the context of “the public health crisis in emerging markets”, with a focus on issues relating to access to patented medicines. The investors involved in the initiative believe that “the sector’s response to the crisis could impact shareholder value in the long term and therefore want to enhance their understanding of how companies are addressing this issue.”

In May 2003, a group of institutional investors representing US\$ 7 trillion issued a statement in support of the Extractive Industries Transparency Initiative (EITI). Launched in September 2002 by United Kingdom Prime Minister Tony Blair, with the support of leading mining and energy companies, as well as NGOs, the EITI aims to increase transparency of payments made by extractive sector companies to governments and government-linked entities. The statement supports a wider use of EITI and commends the efforts made by companies and governments already engaged in the initiative, and calls on the engagement of new companies, as well as inviting other investors to join the statement.

²¹ *World Economic Forum: Values and Value — Communicating the strategic importance of corporate citizenship to investors, 2003 CEO Survey*



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Exhibit 21

Case-study on disclosure in the US pulp and paper industry

One key barrier to the integration of ESG issues into mainstream financial analysis continues to be the poor quality and limited quantity of financially relevant environmental information disclosed by companies.

Though disclosure is generally improving, there are important gaps in the information that companies make available to financial analysts. A review of 13 leading, publicly listed companies in the US pulp and paper industry found that while impending ESG issues could materially affect capital expenditures and future earnings, few companies adequately disclosed the financial risks or competitive implications of these ESG issues to their shareholders²². Similarly, in 2002, of 16 leading oil and gas companies analyzed by the World Resources Institute, 11 failed to mention climate change as a business risk in their annual reports. This, despite the fact that climate change is widely recognized by oil and gas managers as being a critical issue for the industry.

Not merely an inconvenience, this lack of disclosure makes it impossible for investors to value companies accurately. Indeed, failure to disclose financially material environmental information may constitute a breach of securities law.

²² *World Resources Institute, Pure Profit: The Financial Implications of Environmental Performance, March 2000*

Exhibit 22

Stock exchanges convene to discuss corporate citizenship

On 15 March 2004, the Global Compact convened a meeting with senior representatives of the world's exchanges and principal federations at United Nations Headquarters in New York. The meeting, requested by Secretary-General Kofi Annan, invited the exchanges to explore potential partnership and collaboration with the Global Compact.

Many participants recognized that advancing the Global Compact and the concept of responsible corporate citizenship based on universally accepted principles can help in building trust in societies, which was also considered a key priority of the exchanges' work.

At the meeting, Leanne Parsons, Chief Operating Officer of the JSE Securities Exchange, described JSE's approach to corporate responsibility, or "the triple bottom line." She outlined JSE's listing and corporate governance policies and emphasized its integrated approach to socially responsible investing, which links social, environmental and economic factors. Mrs. Parsons also discussed the launch of the JSE's Social Responsibility Index (SRI), the first of its kind in an emerging market, and the first such index sponsored by an exchange.

Following the 15 March meeting, Bovespa, the Brazilian stock exchange in Sao Paulo, and the Jakarta Stock Exchange announced decisions to join the Global Compact and commit to its principles. Other exchanges are actively sharing information on the Global Compact with listed companies.



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6. Implementing change

Because of the strategic nature of ESG issues, involving relations with clients, regulators and additional stakeholders, the work of analysts and fund managers must be supported by a strong commitment at the Board and senior management level of financial institutions. The formulation of long-term goals, the introduction of organisational learning and change processes, appropriate training and incentive systems for analysts and fund managers are crucial in achieving the goal of a better integration of ESG issues.

Every institution should choose its own path, based on its structure and culture — there is no single optimal solution. Such paths can include very diverse strategies, such as buying external research, supporting financial analysts and fund managers with specialist ESG teams, training analysts and managers and adapting performance measurement and incentive systems to achieve better integration of ESG aspects in core processes.

Change will happen if all market actors join in the effort to better understand and integrate ESG factors in investment. Financial analysis and the way it is used in investment decisions is to a great extent the result of what all market actors perceive as being the relevant issues, time-frames and values. That said, financial analysts and investment professionals should take a leading role because they are the specialists best placed to show how ESG issues impact company and investment value.

Recommendations:

- w. *Financial institutions should define their own path towards organisational learning and change in this field and specify long-term goals and organisational learning and change processes.*
- x. *Financial institutions should integrate materially relevant ESG factors in performance measurement and incentive systems for analysts and fund managers.*
- y. *Senior management and Board members of financial institutions should make clear their leadership and commitment with respect to ESG issues.*



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Exhibit 23

A possible organisational path leading from separate specialist teams to full integration of ESG issues

On their path from a research and investment process not including ESG factors to full integration of ESG issues, many organisations go through different stages often involving the use of specialist Socially Responsible Investment (SRI) functions and teams. It is interesting to note that full integration usually leads back to the initial organisational structure, in which specialist ESG know-how and teams are re-integrated and fully embedded into normal research and fund management functions. See Figure 7.



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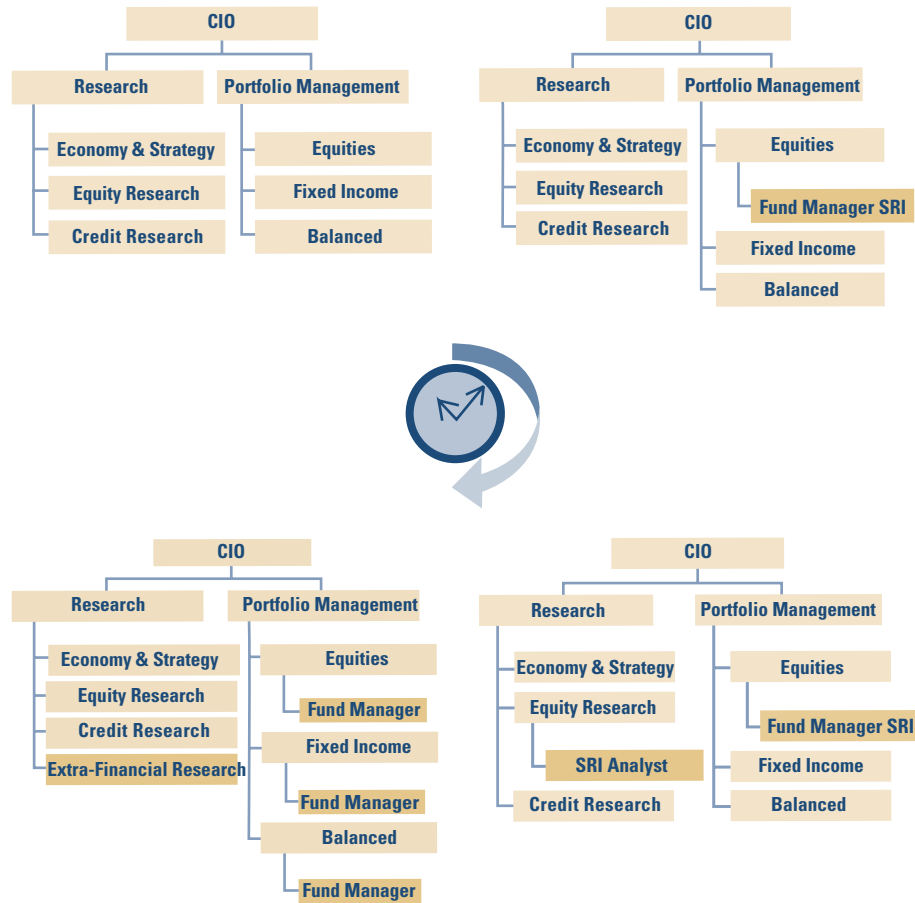


Figure 7: One (of many) possible organisational paths leading from mainstream (upper left), to first generation screening (upper and lower right), to partial ESG integration in different asset classes (lower left), to full ESG integration (upper left) in research and portfolio management processes²³

²³ Eric Borremans, BNP Paribas Asset Management, Presentation at the meeting of the Financial Sector High-Level Initiative on "Best-Practices in Financial Analysis", Zurich, 4 March 2004.

Conclusions and outlook

The institutions that have produced this report are committed to start a process to further deepen, specify and implement the recommendations outlined in this report. This will happen at different levels and will include both individual and collaborative efforts.

As an important next step, we plan to approach the relevant accounting standard-setting bodies (FASB, IASB, etc.), professional and self-regulatory organizations (AIMR, EFFAS, NYSE, NASDAQ, FSA, etc.) and investor relations associations (NIRI, DIRK, etc.) in order to ensure that our intentions are fully understood and supported.

We also plan to use platforms provided by initiatives such as the UNEP Finance Initiative, The Conference Board, the World Economic Forum and others to start an in-depth dialogue with the key stakeholders mentioned in this report, including investors, companies, regulators, stock exchanges, accountants, consultants, and NGOs. We are keen to learn their views and are interested in starting a process of communication and mutual learning in implementing the recommendations.

We will approach our clients and assess their interest and needs with regard to research that includes ESG aspects. We are committed to improving the coverage of ESG issues in the research and investment services we provide to our clients.

We will encourage our analysts to engage in both individual and collaborative efforts to improve the know-how and tools needed to integrate ESG factors in financial analysis. Our goal is to trigger creativity, diversity of approaches and innovation in the field. We are committed to support analysts with the necessary resources and training.

We invite the Global Compact or one of its implementing bodies to review the state of the implementation of this report's recommendations in a year's time, with the goal of assessing how our institutions and other market actors have responded to the call



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for action by this report. The review should also describe how concepts to better include ESG issues in financial analysis, asset management and securities brokerage have evolved over time and update the recommendations if necessary.

Exhibit 24

A proposal for reviewing implementation

UNEP-FI has expressed its preparedness in tracking global progress on the recommendations of this report. Its Asset Management Working Group has proposed a preliminary list of ten indicators that could be used for the planned review process. They include:

Investors:

1. Investors specifying their proxy voting guidelines on ESG matters
2. Trustees and their selection consultants consider integrating ESG issues into the formulation of investment mandates and the selection of investment managers, taking into account their fiduciary obligations to participants and beneficiaries
3. Government and multilateral agency pension funds start considering the principles of sustainable development in their investments

Asset Managers:

4. Senior management and Boards taking a leadership role
5. Asset managers explicitly requesting and rewarding research on ESG criteria
6. Buy-side, sell-side and emerging market investment research teams being appropriately equipped to integrate ESG issues into fundamental company analysis
7. Analyst performance and incentive systems rewarding ESG research

Capital Markets:

8. Stock exchange inclusion of ESG criteria in their listing particulars for companies and/or communication of the importance of ESG
9. Accounting bodies and rating agencies integration of ESG into their frameworks
10. Global Reporting Initiative interactions with local and international financial analysis associations