oekom
Corporate Responsibility
Review 2011

Taking stock of sustainability performance in corporate management and capital investment

oekom research

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Welcome letter

Dr. Norbert Röttgen, German Federal Environment Minister

Companies' responsibility toward future generations: strengthening social cohesion and exploiting new markets

The famous neoliberal economic theorist Milton Friedman coined the phrase, "The social responsibility of business is to increase its profits." Who could argue with that? But is it enough? Following the events of the past few years, and particularly in the light of the global financial and economic crisis, it is increasingly evident that it is not enough. The public, consumers and players on the financial markets, are no longer merely asking how high profits are and what companies do with their profits, but above all how they make their profits. They want companies to fulfil their social responsibilities. They know that social responsibility is fundamental to the social market economy, as the social market economy lives by values which it cannot itself create. The market alone cannot create solidarity. For the founders of the social market economy, the conditions for market success lay beyond supply and demand. It was clear to them that economic success always requires social responsibility. It is the glue that holds society together.

Companies are aware of this social responsibility and are committed to fulfilling their share of it – especially the numerous small and medium-sized family firms which form the backbone of our economy. In a 2006 study, 96 per cent of German companies indicated that they were voluntarily actively socially engaged, whether through monetary donations or donations in kind, through foundations, through support for their employees' voluntary work or through direct provision of services. Respondents for four out of five companies surveyed said that social engagement was an integral part of their company's ethos. These are impressive figures, demonstrating that companies are aware of their responsibility.

The crucial factor is that they maintain their commitment to this responsibility, even in the face of tougher global competition. And I am certain that they will achieve this, as they are increasingly aware that corporate social responsibility is also a key strategic tool for ensuring their future viability. It is linked to new corporate sustainability strategies, which are becoming more and more important.

This all requires investment in sustainable structures. However, it also requires, first and foremost, investment in the new markets for efficiency-enhancing and resource-conserving technologies. Most experts agree that these markets for environmental technologies will be the greatest growth driver for the economy of the 21st century. The global market for environmental technologies has already reached a value of approximately 1.5 trillion euros. According to estimates, in ten years' time this figure will already have doubled. Germany is best placed to reap particular benefits from this growth market. Germany's share of the environmental technologies market is the largest in the world at 16 per cent, which is equivalent to 224 billion euros in terms of volume. And what is particularly important to me is that this is where the jobs of the future will be. Today, we already have 1.8 million jobs in the environmental technologies field, of which 340,000 are in the area of renewable energies alone. It is estimated that by 2020 there will be around 800,000 new jobs in "green services" and approximately 500,000 in energy efficiency. We must take full advantage of these opportunities for growth. We must do everything we can to ensure that Germany continues to build on these opportunities. Politicians will help wherever they can, and not only by providing start-up financial support for environmental technologies and enacting laws and regulations. The Federal Government has also launched a national CSR strategy and made corporate responsibility part of its national and international action plan. If we all pull together, we can strengthen the role of German companies as a model for the rest of the world, in terms of both social responsibility and sustainable management for the future. I'm counting on your support!

Yours sincerely,

Norbert Röttgen

Editorial

Robert Haßler, CEO oekom research AG

2010 marked the UN International Year of Biodiversity, a fact that unfortunately went largely unnoticed by the general public. The United Nations' aim was to raise awareness of the consequences of species extinction and the destruction of ecosystems. The dramatic nature of the possible consequences for the economy and society is impressively demonstrated by various studies which were published in the run-up to the international biodiversity summit in Nagoya, Japan, in October 2010. The United Nations Environment Programme Finance Initiative (UNEP FI) has calculated that if the world's 3,000 largest companies were charged for the damage they cause to the environment and to species, it would cost them more than 50 per cent of their profits, or a good seven per cent of their turnover. This sum is put at around 2.15 trillion euros a year. In the view of experts, the summit itself has brought substantial progress in the protection of species and ecosystems. Japan is obviously a good location for a global environmental protection treaty, even if the latest resolutions on species protection do not have quite the same significance as the Kyoto Protocol.

Nonetheless, one species has stubbornly held its ground - the black swan. The theory that the collapse of the property market and the resulting global financial and economic crisis were not foreseeable still has its proponents. The risk researcher Nassim Nicholas Taleb introduced the term "black swan" event to describe this. This refers to an event which is thought to be impossible (i.e. like black swans, before they were discovered in Australia). The economist Nouriel Roubini has refuted this "beastly" theory, pointing to cyclical crises in the market economy. According to his analysis, anyone with a clear view uninfluenced by the pursuit of short-term profits and bonuses could have seen the crisis coming.

And just as the financial crisis was not an unforeseeable event, likewise climate change and species extinction are not black swan events. Scientific studies by the Intergovernmental Panel on Climate Change, taken as a whole, provide an impressive demonstration of the dynamics and the risks of climate change. Even the contradictory views within the IPCC's scientific network which became public knowledge last year cannot alter this fact. The international climate change summit in Cancun in December 2010 was an unexpectedly successful interim step on the way toward a post-Kyoto treaty. In South Africa in 2011, the job must be completed properly.

When it comes down to it, there are no black swan events where perceptions of social responsibility at the corporate level are concerned. Any IT company having goods produced in China and any mobile phone producer procuring rare earth elements from the Congo can and must know that in those countries it will have to deal with problematical working conditions and often with human rights violations. And any company extracting crude oil at sea from a depth of several thousand meters has to know the risks and be prepared for all eventualities.

This is the third oekom Corporate Responsibility Review we have published, and there is still no shortage of subject matter: the majority of companies still fall a long way short of sustainable management. In this review, we intend to point out shortcomings and undesirable developments which could entail risks for the companies and thus also for their investors. However, we are equally keen to highlight positive examples and propose approaches to solving problems.

One aspect which we will look at in detail in the Corporate Responsibility Review is the situation as regards labour rights and human rights. We will also focus on the spread of corruption and constraints on competition, the increasing importance of sustainability criteria in the payment of salaries and bonuses, the way in which customer data is handled and the state of the forests and measures for their protection.

This year we have again been assisted by a guest author. We extend our heartfelt thanks to Eiichiro Adachi from the Japan Research Institute.

I hope you will enjoy reading this study.

Best wishes

In a nutshell: a summary of the key findings

The development of sustainable investment – facts and figures

- Overall, sustainable capital investments **continued to expand** their market share and volume during the financial and economic crisis. Worldwide, around eight trillion euros are invested taking environmental, social and governance-related criteria into account, Europe alone accounting for five trillion euros. ➔ p. 9ff.

- In the **German-speaking countries**, 354 mutual funds with a total volume of 34 billion euros had been licensed for distribution by the end of 2010. The number of funds has hit a new high, volumes have reached pre-crisis levels. ➔ p. 10

- **Mutual funds in Europe** have recorded new highs in terms of numbers as well as volume. 897 funds with a volume of 75.3 billion euros were licensed for distribution, as at 30 June 2010. France is by far the largest market for mutual funds. ➔ p. 11

- As many institutional investors reduced the proportion of equities in their portfolios due to the financial and economic crisis in favour of money market investments and bonds, the interest in factoring ESG criteria into **fixed-interest investments** has risen markedly over the past two years. Additionally, more and more private and institutional investors are also taking social and environmental criteria into account when purchasing corporate or government bonds. ➔ p. 11

- Overall, according to a study by the European industry association Eurosif, at the end of 2009, **sustainable investments in Europe** had grown by approximately 87 per cent from the 2007 year-end figure, to five trillion euros. According to Eurosif's calculations, this brings their share of the market to around 47 per cent. The bulk of this capital, however, is managed according to rather "soft" sustainability criteria. ➔ p. 12

- The principal factor behind the strong growth in the market is increased engagement on the part of **institutional investors**. One sign of the continued growth in interest by pension funds, foundations and other institutional investors is the fact that the number of signatories to the UN Principles for Responsible Investment (UN PRI) has continued to rise. Germany is still underrepresented in terms of signatories. ➔ p. 15

- An analysis carried out by the Centre for European Economic Research for the German environmental foundation Deutsche Bundesstiftung Umwelt (DBU) shows that during the crisis, sustainable investments showed no disadvantages in terms of performance compared with conventional investments. One interesting detail to emerge was that the more strictly the sustainability criteria were defined, the better the **performance** of the sustainable investment products. ➔ p. 15

- In the light of global anxiety about the credit crunch and inflation, sustainability-oriented investors are increasingly focussing not only on bonds, but also on **alternative investments**. While some areas here, such as microfinance and forestry, have long been assessed against sustainability criteria, the debate about whether and how to invest sustainably in other areas, in particular in commodities, is only just beginning. ➔ p. 16ff.

- Looking at the future development of sustainable investment, oekom research's view is that, under the motto **quality and quantity**, any further expansion of volume and market share must be accompanied by an improvement in the quality of the various SRI investment strategies. In particular, what are referred to as "broad SRI approaches", including engagement and integration, must be systematically developed in order to achieve the core objective of sustainable investment: getting companies to change course toward sustainable management. ➔ p. 19

Corporate Responsibility – status and trends

- oekom research regularly evaluates **approximately 3,100 companies** from more than 45 industries and over 50 countries. We cover international indexes such as the MSCI World, MSCI Emerging Markets and Stoxx 600 as well as important national indexes like the Austrian ATX, the Belgian BEL20, the French CAC40, the German DAX family and the Swiss SMI. ➔ p. 20

- As at 31 December 2010, a total of 550 out of the 3,100 companies, i.e. approximately one-sixth, fulfilled the requirements for being awarded **oekom Prime Status**. A further quarter of all companies evaluated did at least have the basis for a sustainable management system in place, but more than half the 3,100 companies continue to perform poorly in terms of sustainability. There are some companies in the **emerging markets** which need not fear comparison with companies from industrialised countries in terms of CSR. ➔ p. 25

- On a scale from 0 (very low sustainability performance) to 100 (very high sustainability performance), the **best performances** were from computer manufacturers, with an average score of 47.8 per cent, followed by producers of household products (45.6 per cent) and car manufacturers (42.7 per cent). ➔ p. 26

- **Bribery and corruption** are still common at the corporate level in some sectors. As in the previous year, the ignominious top spots here are occupied by the construction industry (15.3 per cent of companies in the oekom rating universe), the aviation and armaments industry and manufacturers of consumer electronics and communications technologies as well as the leisure industry (each with 12.5 per cent). ➔ p. 27f.

- The situation as regards **antitrust infringements** is even worse. Here, manufacturers of consumer electronics have set a sorry record: three-quarters of companies in this sector can be shown to have been involved in violations of competition regulations. Similarly, among producers of household products, chemicals and building materials, more than half the companies have been actively involved in such restraints on competition. ➔ p. 29

- Increasing numbers of companies are altering their **incentive structures** to focus on the long term and on sustainability. These changes include spreading the payment of variable salary components over several years and linking bonuses to the achievement of ESG targets. Sustainability ratings are often used here as a yardstick for measuring target achievement. ➔ p. 30f.

- Violations of **labour rights and human rights** are still common in some sectors. One in two manufacturers of consumer electronics and computers is in breach of recognised employment standards, either directly or through their supply chains. In the textiles sector, despite years of campaigning, more than one in three companies are still affected. The companies most heavily involved in human rights violations are those in the mining industry. **oekom research's world map of human rights violations** gives an overview of the relevant labour rights and human rights infringements. ➔ p. 31ff.

- Despite numerous warnings, customers and members of the public are still often careless in the way they manage their data. At the same time, if customers want to use a company's services, they frequently have to provide the company with extensive data. Companies therefore have a particular responsibility to treat **customer data** sensitively. There are some positive examples of this in both the sectors examined – retail as well as internet & software – but generally, companies' commitment to data protection leaves much to be desired. ➔ p. 36f.

- The world's forested area contracts by an average of over 15,000 hectares every day. **Sustainable forest management** as well as the use of legal timber are therefore of great importance. Some companies in both the media and construction industries are now using mainly or exclusively FSC-certified timber. However, these positive examples are countered by numerous companies which demonstrate no or very little commitment to the protection of forests. ➔ p. 38ff.

Socially Responsible Investment in Asia

Eiichiro Adachi, Japan Research Institute

For many Asian countries, the concept of "socially responsible investment" (SRI), though originally imported from Western countries, is now here to stay. In this article, a tour around the region reveals many of the latest SRI developments in Asia.

Japan

Japan leads the way in Asia with regard to SRI. The first environmentally-screened mutual fund was launched here twelve years ago, in 1999. The current volume of assets in the SRI market, including both retail products and institutional products, stands at more than 7 billion US-Dollar. The Japanese SRI market has characteristically depended mainly on retail products rather than on institutional products, but in recent times, the first signs of a shift from retail to institutional products have become evident.

On 16th December 2010, RENGO, the Japanese Trade Union Confederation, which has 6.75 million members and is a major supporter of the incumbent ruling party, the Democratic Party of Japan, released a set of guidelines which focuses on ESG investment, in particular on employment aspects.

It exerts a strong influence on a number of public and corporate pension funds through its union members and in recent years has been advocating a responsible investment. In 2008, after the global financial crisis, it published a paper entitled "A RENGO Perspective on the Corporate Legal Framework and Investment Fund Regulation". RENGO's aim was to strengthen the influence of the trade unions on the management of workers' capital (reserves contributed by workers), such as pension funds, and to prevent investment in funds having adverse effects on employment and society as a whole. To this end, it formulated a set of guidelines based on the United Nations Principles for Responsible Investment. As a trades union body, it previously paid little attention to the way its capital was managed, but now it is concerned that its money could be used for violations of workers' rights and might not be used to invest in green innovation and technology to regenerate growth.

Japanese public pension funds, such as the National Public Service Personnel Pension Fund and the Local Government Officials' Pension Fund, have been paying greater attention to responsible investment in recent times. And it is also understood that discussions are taking place within the Government Pension Fund of Japan, the world's largest pension plan with assets of 1.3 trillion US dollars, about responsible investment issues.

Korea

Korea ranks second in Asia in terms of SRI. According to the Korea Sustainability Investment Forum (Kosif), the total amount invested in Korean-domiciled SRI funds has risen to 3.3 billion US dollars. The National Pension Service is a major supporter of SRI, accounting for 1.1 billion US dollars of these invested assets.

On September 14, 2009, the Korea Exchange (KRX) launched its Socially Responsible Investment Index ("SRI Index"), composed of outstanding companies that demonstrate excellence in corporate sustainability assessments of their performance, including their environmental, social and corporate governance from the extra-financial perspective. The SRI Index provided by KRX is a market capitalization-weighted (free-float adjusted) index comprising 70 constituent companies demonstrating outstanding SRI performance, as of January 2, 2009.

China

For the Chinese capital market, SRI is a completely new phenomenon. There are still only a few mutual funds which take ESG criteria into account when investing in companies. However, the term "corporate social responsibility" has become widespread, promoted by the central government, which has been keen to build a harmonious society, avoiding the distortions produced by high levels of economic growth.

The Shanghai and Shenzhen stock exchanges have played an important role with regard to SRI. Firstly, in 2006, the Shenzhen stock exchange issued its CSR Guidelines for Listed Companies, which called upon listed companies to assume responsibility for social development, protect the natural environment and other resources and commit to advancing the interests of shareholders, creditors, employees, customers, consumers and others involved in their businesses. These guidelines also urged companies to evaluate their performance regularly and to issue voluntary disclosures about the results.

In May 2008, the Shanghai Exchange issued a Notice on Strengthening Listed Companies' Assumption of Social Responsibility (Shanghai CSR Notice) and the Guidelines on Listed Companies'

Environmental Information Disclosure (Shanghai Environmental Disclosure Guidelines). According to these documents, Shanghai Exchange-listed companies should fulfil their social responsibilities, address the interests of their stakeholders and commit themselves to promoting sustainable economic and social development.

In August 2009, the Shanghai Exchange and China Securities Index Company Limited officially launched the SSE Social Responsibility Index. The constituent components of the index, the base day of which is June 30, 2009, are 100 SSE-listed stocks exhibiting "good performance in the area of social responsibility".

The CSI ECPI China ESG 40 Equity Index, launched in September 2010 and comprising 40 companies in mainland China, is a collaboration between Chinese Securities Index Company, an index provider backed by the Shanghai and Shenzhen stock exchanges, and ECPI, a European ESG research and indices company.

Under these circumstances, a boom in SRI is predicted in China in the near future. And this will not be restricted to retail mutual funds. A statement by an official from the National Council for Social Security Fund indicated that this large-scale pension fund might consider SRI for its future investments. In September 2007, he said that the social security fund would promote a style of investment based on long-term value, taking corporate governance and socially responsible investment into account.

Malaysia

Malaysia is another country where many investors are paying attention to ESG issues. Bursa Malaysia, the stock exchange in Malaysia, began publishing CSR guidance for companies in September 2006. Since that time, Bursa Malaysia has been closely monitoring and evaluating the quality of CSR reporting in Malaysia.

The exchange has also worked closely with Malaysia's regulators and policy-makers to initiate a carefully-paced transition toward mandatory CSR reporting by listed companies. Malaysian companies are now required to include in their annual reports a description of their CSR activities and practices or, if there are none, a statement to this effect. This requirement is also incorporated into Bursa Malaysia's listing rules.

Singapore

As a member of the Commonwealth of Nations, Singapore has a comparatively long history of involvement in SRI. Furthermore, in recent times, the Singapore Exchange (SGX) has recognized that more and more investors are paying attention to environmental, social and governance (ESG) issues and on August 28, 2010, it released a "Proposed Policy Statement and Guide to Sustainability Reporting for Listed Companies". SGX's policy proposal was under public review until October 29, 2010. Though the jury is still out on this, SGX might well become the first securities exchange in Asia to require listed companies to introduce sustainability reporting.

Indonesia

On June 8, 2009, Indonesia Stock Exchange (IDX), in collaboration with Yayasan Keanekaragaman Hayati Indonesia (the Indonesian Biodiversity Foundation – KEHATI), launched a new index, the SRI-KEHATI Index, based on sustainable and responsible investment (SRI) practices. The new index is expected to enhance the exposure of listed companies that have met their environmental and social responsibilities as well as showing good corporate governance. The SRI-KEHATI Index consists of 25 stocks.

Thailand

The Stock Exchange of Thailand (SET) has taken a different approach to raising CSR awareness and standards. In 2007, SET established the Corporate Social Responsibility Institute (CSRI), which encourages listed companies to become more involved with ESG issues and to promote CSR concepts and practices. SET organises annual CSR awards to reward listed companies for exceptional contributions to society. Substantive measures have also been taken to raise corporate governance standards.

Hong Kong

On July 7, 2010, Hang Seng Indexes Company Limited announced the launch of the Hang Seng Corporate Sustainability Index Series, the first index series to focus exclusively on Hong Kong and the Chinese mainland.

The Hang Seng Corporate Sustainability Index and the Hang Seng (China A) Corporate Sustainability Index include 30 Hong-Kong-listed and 15 mainland-listed corporate sustainability leaders, respectively. The Hang Seng (Mainland and HK) Corporate Sustainability Index is a cross-market index combining the constituent stocks of the other two indexes, in which the number of constituent companies represented will vary but at launch will be 39.

Taiwan

Finally, in Taiwan, Fubon Financial Holding began using corporate social responsibility as an investment standard for funds in March 2009. Similarly, Taiwan's labour retirement pension fund has integrated corporate social responsibility and ethics into the operational principles of its fund investments.

In February 2010, the Taiwan Stock Exchange (TSE) and GreTai Securities Market (GTSM) announced CSR Guidelines for listed companies as "soft law" to encourage companies to make forward progress in this area. The Guidelines, drafted by BCSD-Taiwan and CSR Taiwan, are regarded as a milestone in the linking of CSR to the capital market. They are also seen as the new driving force in both CSR performance disclosure and responsible investment, providing guidance to assist listed companies in implementing CSR in the environmental, social and corporate governance (ESG) field.

Without doubt, Asia remains the most economically dynamic region on earth. However, this does not necessarily mean that Asia focuses solely on development through economic growth. Asian companies are subject to constant external pressure, both domestically and internationally. Choosing the path of sustainable development will automatically lead to the emergence of SRI in Asia. This will also generate opportunities of great benefit to global investors.

Eiichiro Adachi is the head of the ESG research centre at the Japan Research Institute Limited (JRI) in Tokio, which is a wholly-owned subsidiary of Sumitomo Mitsui Financial Group, Inc. He received his bachelor's degree in economics from Hitotsubashi University in Japan in 1986. He is currently engaged in the CSR screening of listed Japanese companies for Sumitomo Trust and Banking Co. Ltd, STB Asset Management Co. Ltd, Daiwa Asset Management Co. Ltd and others. He is also the project manager for research studies on environmental finance and CSR commissioned by a number of ministries. He is the author of "The Introduction to Corporate Environmental Management" (2009, Nikkei Publishing Inc.), "Social Finance" (2006, Kinzai) and the co-author of several books, such as "Corporate Social Responsibility Management and Socially Responsible Investment" (2004, Kinzai). He has been a working group member of the Committee for the Promotion of CSR Management at KEIZAI DOYUKAI (Japan Association of Corporate Executives), a member of the CSR study group set up by the Ministry of Health, Labour and Welfare, and, until May 2009, was one of the experts in the Japanese delegation to the ISO / Social Responsibility Standards (ISO26000) Working Group. JRI's research covers approximately 2,000 companies in 33 sectors of the economy in Japan. JRI currently has 7 ESG analysts, including 3 analysts covering Asia. JRI plans to expand its research coverage of Asian countries.

1. The development of sustainable investment – facts and figures

According to a study by Eurosif, the European industry association for sustainable investment, the volume of investments in Europe that took environmental, social and governance-related (ESG) criteria into consideration stood at five trillion euros at the 2009 year-end. During the crisis years 2008 and 2009, the volume thus rose by 87 per cent. New highs were also reached in terms of numbers and volumes of sustainable mutual funds in Europe. Here, the focus has increasingly been on bonds, which in the public debate about sustainable investment had long been overshadowed by shares. At the same time, there has been a tangible increase in interest among sustainable investors in alternative investments, such as forestry and commodities. These and other interesting trends in sustainable investment will be described in the following pages.

1.1 Current market trends in various markets

1.1.1 German-speaking countries

Interest in sustainable investments has continued to grow among both private and institutional investors, as is shown by a range of studies published in 2010. For example, 32 per cent of the 500 financial decision-makers in German households who were surveyed by Union Investment, a German asset management firm, find sustainable investments an attractive option. According to Union Investment, sustainable investments resonate most with young investors aged between 20 and 29. A study by DZ Bank reports that the proportion of private investors who are already investing their money according to environmental sustainability criteria is up from 22 per cent in 2009 to 29 per cent in 2010. 1,100 investors in Germany took part in the survey. In a spring 2010 Union Investment study of 242 major German investors, such as insurance companies, pension funds and church investors, with combined portfolios worth 920 billion euros, a good two-thirds (68 per cent) said they had investments in environmentally, socially or ethically oriented investment products. The previous year, the figure had been 64 per cent. On a five-year horizon, the majority of large investors (55 per cent) anticipate positive trends in the market for sustainable investment products.

Sustainable mutual funds in Germany

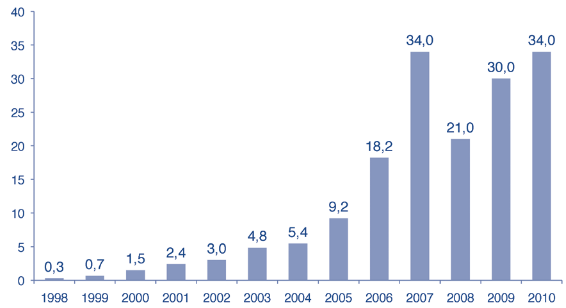
The growing interest among private investors evident from the surveys cited above is also reflected in the trends in the number and volume of sustainable mutual funds. According to a study by the news service ECOreporter, the volume of mutual funds licensed for distribution in Germany reached a record high in 2010. As at 31 December 2010, a total of 32.42 billion euros were invested in such funds. One year previously, the volume had stood at just 30.08 billion euros. Investors can now choose between 304 funds licensed in Germany in the areas of sustainability, ethics and renewable energies. At the end of 2009, there had been only 279 such funds. The funds include share funds, bond funds, mixed and umbrella funds, microfinance funds and exchange-traded funds (ETFs).

Of these, share funds performed best, registering annual growth of 38.2 per cent. The ECOreporter survey documents a further 161 sustainable share funds which performed well in 2010. Only six of the share funds lost value, and there, the loss was at most of 2.3 per cent. The top-performing sustainable mixed fund showed growth of 26.3 per cent, and the top-performing sustainable bond fund grew by 18.5 per cent. The poorest performer was a renewable energy fund which lost 29.4 per cent.

Sustainable mutual funds in the German-speaking countries

According to data from the Sustainable Business Institute (SBI), a total of 354 sustainable mutual funds were licensed for marketing in Germany, Austria and Switzerland, as at 31 December 2010. The rise in the number of sustainable mutual funds thus continued in 2010: the SBI recorded only 313 funds at the end of 2009. As at 31 December 2010, approximately 34 billion euros were invested in these 354 funds, i.e. the overall volume of sustainable mutual funds has once more reached the level it was at before the financial crisis.

25 new funds were launched in 2010, with a total volume of around 700 million euros. These comprised nine share funds, eleven mixed funds, three bond funds, one microfinance fund and one exchange-traded fund (ETF). A further 34 funds, which had either already been licensed in other countries or have recently begun to factor in sustainability criteria and which account for investments totalling around 2 billion euros, have been added since the end of 2009. 18 funds have closed or have been amalgamated with other funds since the beginning of the year.



Volume of sustainable mutual funds in German speaking countries; as of 2010-12-31; in bn. euros; source: SBI (2011)

The overall market for sustainable investments in the German-speaking countries

At the end of 2009, according to a study by the Forum for Sustainable Investment (FNG), the total volume of sustainable assets under management in Germany, Austria and Switzerland stood at just under 38 billion euros. This represents a 67 per cent increase compared to the 2008 year-end. According to the FNG's calculations, volumes rose in Germany by 68 per cent to just under 13 billion euros, in Switzerland by 63 per cent to 23 billion and in Austria by 200 per cent, to approximately two billion euros. The study included both mutual funds and sustainable mandates. 40 investment companies, banks and institutional investors took part in the FNG survey.

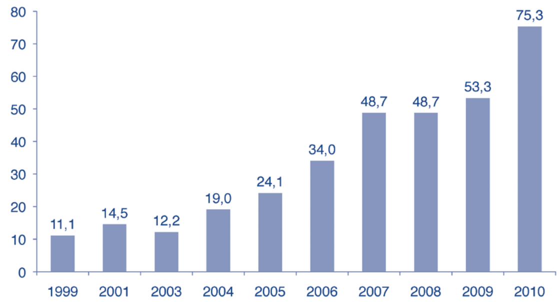
A market analysis by the consultancy firm Funds@Work threw up very different figures. In a network analysis, it identified, from a parent population of over 1,000 institutional investors in the German-speaking countries, 100 actively sustainable investors who claimed to be managing or having managed on their behalf a total of 355 billion euros taking sustainability criteria into account. This represents just over 50 per cent of their overall capital investments.

The clear difference between these two studies in the volumes calculated is due to different ways of defining which investments to include.

1.1.2 Europe

Sustainable mutual funds

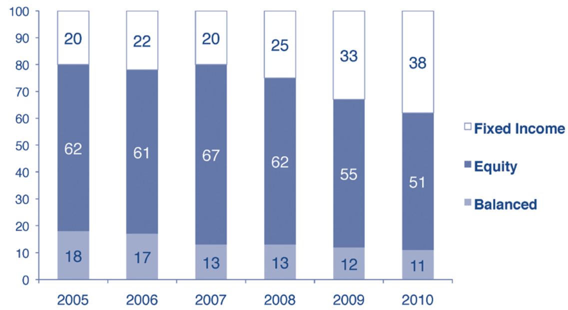
Sustainable mutual funds increased in number as well as volume in Europe as a whole. According to data from Vigeo Italia, 897 such funds were licensed for distribution as at 30 June 2010, and their total volume stood at 75.3 billion euros. This corresponds to growth of over 40 per cent compared to end of June 2009.



Volume of sustainable mutual funds in Europe; as of 2010-06-30; in bn. euros; source: Vigeo Italia (2010)

These figures represent new highs in terms of both the number and the volume of sustainable mutual funds. Belgium (227), France (215), the United Kingdom (98) and Switzerland (91) together account for 72 per cent of all funds included in the study. Compared to the previous year, France showed the greatest growth in terms of volume, with capital invested in funds increasing by 92 per cent representing 26.5 billion euros. This makes France, ahead of the UK, by far the largest market for sustainable mutual funds in Europe.

The proportion of assets invested in bond and money-market funds has continued to grow, despite the recovery on the stock markets in 2010. The proportion of sustainable bond and money-market funds stood at 38 per cent in 2010, whereas in 2009 it had been 33 per cent. A little over half the capital (51 per cent) was invested in share funds, while mixed funds continued to lose ground. Bond and money-market funds had the highest average volumes, at 211 million euros, while share funds had an average volume of 83 million euros and mixed funds 63 million euros.



SRI mutual funds licensed in Europe, distribution in asset classes; as of 2010-06-30; in %; source: Vigeo Italia (2010)

Quality label? Go-ahead!

In 2010, the debate about whether there should be appropriate labelling systems to assist private investors in their search for suitable sustainability funds was reignited due to the growing numbers of this type of product. Three initiatives, albeit very different ones, already exist - Eurosif‘s transparency logo, the Austrian eco-label and the French SRI organisation Novethic’s SRI label. Eurosif’s logo is awarded to funds which meet certain requirements with regard to the transparency of the investment process and the criteria applied. However, it is still up to the individual investor to evaluate the content of the concept. The Novethic logo goes one step further as it also specifies requirements for the funds in terms of content. Funds must fulfil four criteria in order to gain the award: consideration of ESG factors in the investment process, extra-financial reporting, transparency regarding the SRI investment strategy and full disclosure of all portfolio holdings. The logo is currently awarded only to funds licensed in France. Funds which bear the Austrian eco-label must meet transparency and quality criteria and demonstrate that they apply certain positive and exclusionary criteria.

oekom research supports the development of labels for sustainable investment products. The more varied and heterogeneous the range of products are and the more investors, new in matters related to the issue of sustainability, are interested, the greater the need for guidance. In this context, a logo should transcend mere transparency criteria and should also give investors an idea of the quality of the product in terms of content. The main emphasis here should be on giving investors sound information on the scope and “strictness” of the sustainability criteria used, as well as on the quality of the research processes underlying them. The final decision on whether a product matches their own ideas about sustainability cannot be taken away from investors.

The overall market for sustainable investment in Europe

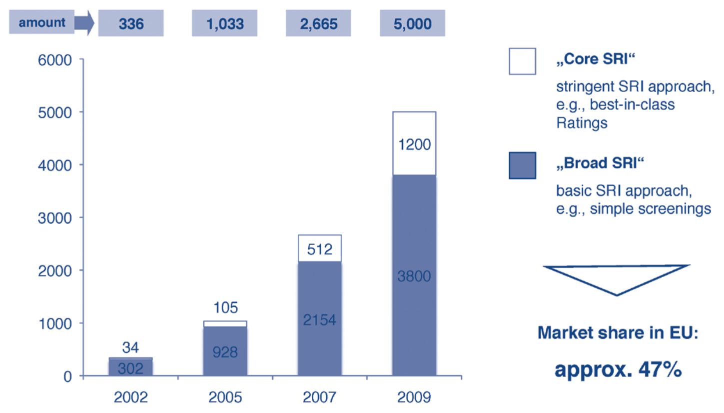
There was great interest in the publication of the data that Eurosif collects every two years on the market as a whole. People were eager to see how sustainable investment had fared during the crisis years 2008 and 2009. When the figures were published, on 13 October 2010, it became clear that it had fared extremely well.

Eurosif recorded a rise of 87 per cent compared with the end of 2007 for the 2009 year-end. At that point in time, a total of five trillion euros were invested taking ESG criteria into account.

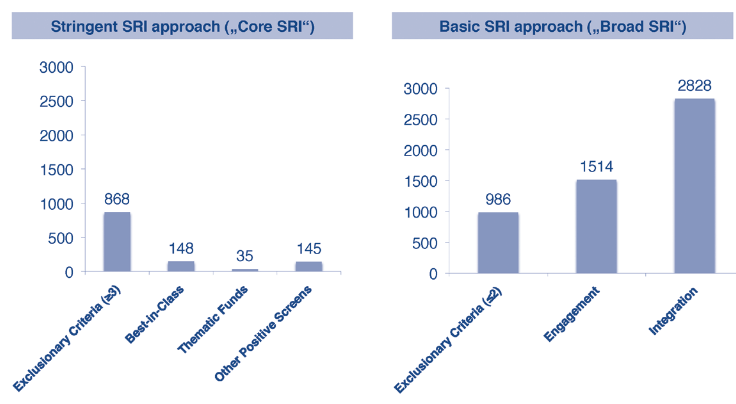
Taking the data from the Eurosif study as a basis, the market share of sustainable investments stood at around 47 per cent, up from approximately 17 per cent at the end of 2007.

The study differentiates between a stringent ("Core SRI") and a basic ("Broad SRI") approach to sustainability. Detailed analysis shows that approximately three-quarters of the sustainable investments can be viewed as following a broad SRI approach, with the lion's share of these following an integration strategy. This involves factoring ESG criteria into a conventional financial analysis.

The study gives no information about the type and scope of the relevant criteria used here. However, in oekom research's experience, the range extends from taking individual criteria, e.g. on climate change, into account on an ad hoc basis at one extreme to the systematic integration of entire lists of ESG criteria at the other. This investment strategy alone accounts for more than half (56.6 per cent) of all sustainable capital investments in Europe.



Volume of capital invested according to sustainability criteria in Europe; as of 31.12.; in bn. euros; source: Eurosif (2010)



SRI investment approaches; as of 2009-12-31; in bn. euros; source: Eurosif (2010)

By volume, the use of exclusionary criteria is the second most popular and active engagement the third most popular SRI investment strategy, while the best-in-class approach achieves a relatively modest three per cent market share.

There are, however, interesting national differences with regard to the distribution of core and broad SRI strategies. In the German-speaking countries, the core approaches dominate, with market shares of around 95 per cent (DE) and 100 per cent (AT, CH) respectively, while in the UK, Italy, France and Spain, for example, broad approaches make up over 90 per cent of the market.

The "quality and quantity" outlook (section 1.3) also looks at how the results of the Eurosif study can be interpreted.

Novethic: different ESG strategies within Europe

69 per cent of European asset owners integrate ESG criteria into the management of their assets. The motives as well as the methods employed however vary widely between individual countries. This is one of the findings of the recent study „ESG Perceptions and Integration Practices“ conducted by the French SRI organisation Novethic, which surveyed 251 asset owners (banks, insurance companies, pension funds, trusts and public financial institutions) in nine European countries.

For 59 per cent of French and 68 per cent of German asset owners, the prime motivation for taking ESG criteria into account is to make a contribution bringing about a more sustainable development model. However, only a minority of Danish and British investors (21 per cent and 17 per cent respectively) share this view. Protecting one’s own reputation is the most important incentive in Finland and Denmark (over 40 per cent in each case) whereas in France (11 per cent) this motive is less of a concern and in the UK was not even mentioned by investors. The management of long-term risks is cited as a motive by one-third of French and Dutch investors, but fewer than 15 per cent of German, Spanish and Finnish investors see it as playing a role.

The practices thtat are applied differ widely from country to country. The screening of ESG criteria is by far the most important approach in France (81 per cent), while shareholder engagement is favoured in the UK. In Denmark, the most favoured approaches are engagement and norm-based exclusions (more than 40 per cent each). In Germany, ESG screening is favoured, although it is closely followed by other approaches.

1.1.3 Sustainable investment worldwide

Outside Europe, growth in sustainable investments has also continued, as can be seen from some of the latest market studies:

US

According to the Social Investment Forum (SIF)‘s “Report on Socially Responsible Investing Trends in the United States”, the sustainable investment market in the US has now grown to 3.07 trillion US dollars. This represents an increase of 13 per cent on the 2007 level. With 2.3 trillion US dollars in assets invested according to SRI strategies, institutional investors dominate the SRI market. There are a total of 250 sustainable mutual funds, with an investment volume of 316 billion US dollars.

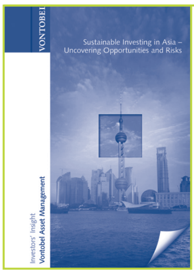
Source: www.socialinvest.org

Australia

As the “Responsible Investment 2010” report by the Responsible Investment Association Australasia (RIAA) shows, the sustainable investment market in Australia has also grown. The “Core SRI” segment of the market, which applies strict SRI criteria, has grown by 13 per cent, from 15.4 billion US dollars in 2009 to 17.7 billion US dollars. The more wide-ranging “Broad SRI” approach (integration of ESG criteria, corporate engagement, shareholder activism) can even point to a rise of 25 per cent, bringing it up to 72.6 billion US dollars.

Source: www.responsibleinvestment.org

Asia



Source: Bankhaus Vontobel

The guest contribution by Eiichiro Adachi from the Japan Research Institute (see page 6) provides a comprehensive picture of developments in Asia. In its study "Sustainable Investing in Asia – Uncovering Opportunities and Risks", Vontobel bank anticipates strong growth in sustainable investments in Asia (ex-Japan) and considers it possible that volumes will multiply, from their current level of 20 billion US dollars to as much as 4,000 billion US dollars by 2015.

Emerging Markets

There is currently no up-to-date and comprehensive market analysis available for emerging markets (ex-Asia). However, it is noticeable that the number of sustainability indexes in these countries has risen markedly. Among such indexes the following have already been launched:

- Brazil: Índice de Sustentabilidade Empresarial (ISE)
- Mexico: Bolsa Mexicana de Valores (BMV) Sustainability Index
- Turkey: Istanbul Stock Exchange Sustainability Index (ISESI)

The growing number of sustainability indexes can be interpreted as proof of increasing interest in this asset class on the part of investors. At the same time, the emergence of sustainability indexes and more stringent listing requirements by the stock exchanges mean that companies in these countries must make greater efforts to address the challenges of sustainable company management. Nowadays, pioneering sustainability-oriented companies from the emerging markets can already hold their own against the leading companies in the industrialised nations (see section 2.2.1).

Global

Based on the studies mentioned above, the global volume of sustainable investments totals approximately eight billion euros. Over 62 per cent of this sum is invested in Europe, while the US is the world's second-largest SRI market. Asia – measured against its economic performance – still has a lot of catching up to do in this area.
When interpreting the data, it should be noted that definitions and interpretations of which capital investments are counted as sustainable investments vary between the individual studies and surveys. In looking at the "integration" approach, the Eurosif study cited here has selected a particularly broad approach. In oekom research's view, transferring this approach to other markets would result in total volumes of sustainable capital investment significantly above the just under eight billion euros calculated here.

Region	As of	Volume
EU	2009	5,000 bn.
US	2010	2,310 bn.
Canada	2008	386 bn.
Australia	2010	68 bn.
Asia	2007	21 bn.
Global		**ca. 7,785 bn.**

Volume of capital invested according to sustainability criteria in different regions; in euros; sources: ASrIA, Bank Vontobel, Eurosif, Japan Research Institute, Social Investment Forum, Social Investment Organisation, Responsible Investment Association Australasia

Record number of signatories to the UN Principles for Responsible Investment

The number of signatories to the UN Principles for Responsible Investment (PRI) has grown by over 30 per cent in the last year – a sign that institutional investors are increasingly aware of the importance of factoring ESG issues into their investment decision-making. Since July 2009, 268 new signatories have pledged themselves to support the UN PRI. This brings the total number to over 800, with combined investment volumes standing at 22 trillion US dollars, which equates to over ten per cent of the estimated volume of the global capital market.

The signatories include institutional investors from 45 countries. They commit, among other things, to take ESG criteria into account in their investment decisions and to work together to disseminate awareness of the Principles.

1.1.4 Performance of sustainable investment

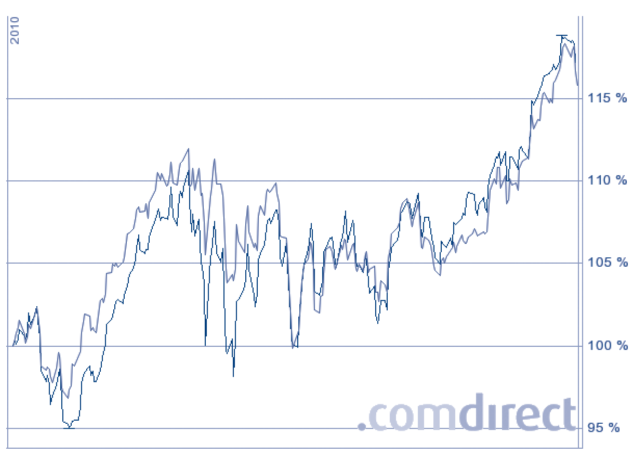
The competitiveness of sustainable investments in terms of yield and risk is still questioned by some – and that despite the fact that there are now a considerable number of studies and statistical analyses demonstrating the competitiveness of sustainable investments. The key message of these studies is summed up by Michael Dittrich of the German environmental foundation Deutsche Bundesstiftung Umwelt (DBU), in his summary of an analysis carried out for the DBU in 2010 by the Centre for European Economic Research (Zentrum für Europäische Wirtschaftsforschung, ZEW): "There is really no longer any reason not to address sustainability issues when making capital investments. Not-for-profit organisations can thus accommodate their charitable aims when making investments without that meaning that they will achieve lower yields."

The ZEW study shows that even during the financial crisis from 2007 to 2009, sustainable investments across the market achieved results no worse than those of conventional investments. One interesting detail to emerge was that the stricter the sustainability criteria applied when selecting securities, the better the performance of the investment product.

This view is reflected, for example, in the development of the Global Challenges Index, which specifies particularly stringent requirements for the companies listed.

> *„Indeed, the greater the proportion of sustainable securities selected, the better the comparative results."*
>
> Dr. Michael Schröder, Centre for European Economic Research

Example: Global Challenges Index



Performance of the GCX (dark blue) vs. MSCI World (light blue), 2010-01-01 to 2010-12-31; source: www.comdirect.de

On its third birthday, at the beginning of September 2010, the Global Challenges Index (GCX) was able to announce positive results overall. Although – or precisely because – the securities are included in the index purely on the basis of very strict social and environmental criteria, since its launch the GCX has performed better than comparable conventional share indexes. In 2010, it again outperformed other indexes including the MSCI World. (➔ www.gc-index.com)

1.2 Sustainability and alternative investments

In the light of global anxiety about the credit crunch and inflation, sustainability-oriented investors are focussing increasingly on bonds and also paying greater attention to alternative investments. While some areas, such as microfinance and forestry, have long been assessed against sustainability criteria, the debate about whether and how to invest sustainably in other areas, in particular in commodities, is only beginning.

1.2.1 Commodities

Over the past year, investors' interest in investments in commodities has increased significantly, not least due to the gold boom – the gold price attained an historic high in autumn 2010, at over 1,420 US dollars a troy ounce. Sustainability-oriented investors are also looking more closely at the question of whether it is possible to invest in commodities while taking social and environmental criteria into account. Whereas it is possible to refer to sustainability ratings when making decisions about buying shares in commodity companies, the situation as regards investments which relate directly to commodities is more complex.

In oekom research's view, a fundamental distinction must be made here between two aspects: firstly, the social and environmental "quality" of the commodities to be invested in, and secondly the impact of speculation on trends in commodity prices, in particular on the level and volatility of prices.

The social and environmental **quality of the commodities** is determined here by the conditions under which the commodities are cultivated or extracted and processed. These depend firstly on the environmental and social standards prevailing in the country where the commodity is obtained and secondly on the quality of the sustainability management system of the company obtaining the commodity. Standards for the cultivation and/or extraction of commodities are of particular significance here.

If the origin and producers of commodities are known, such aspects can be factored into investment decisions. It is then possible to invest selectively, on the basis of specialised country/company ratings, in commodities which are extracted or produced under adequate social and environmental conditions. In the case of so-called standardised products such as cocoa or oil, where tracing of production directly to individual producers is not yet possible, it will be necessary to develop further the kind of traceability concepts that are found in the timber sector or in the Kimberley Process for diamonds. In oekom research's view, sustainability-oriented investors should also consider very carefully whether or not to invest in commodities whose cultivation and/or extraction is known to be linked to severe social and environmental problems. As an alternative to abstaining completing from this type of investment, it is possible to adopt a policy of engagement where commodity investments are concerned, in order to exert a positive influence on the conditions under which the commodity is obtained. Such engagement can be targeted at both companies and countries.

The significance of this second aspect, speculation in commodities, lies in its **effect on commodity prices** (level and volatility). Prices which are not in line with the market and misleading market signals associated with these can lead to negative social and environmental impacts for producers and consumers alike. These include, for example, the switching of agricultural production based on a perceived rise in demand for certain products (for example energy crops), the opening of new mines, with all the associated social and environmental impacts, and the threat to the food supply of poorer sections of the population due to rising food prices. In the view of oekom research, speculative commodity investments which give rise to or exacerbate negative social and environmental impacts do not constitute sustainable investments.

For investments in commodities, here are the essential options:

- purchasing shares in companies active in the commodities sector, e.g. in the areas of metals and mining, oil & gas and agriculture.
- purchasing commodity funds and other commodity derivatives, e.g. certificates, futures and options as well as ETFs on commodity indexes.
- purchasing physical commodities which are then stored by the investor. This practice, common in the case of precious metals, is also increasingly being applied by commodity investors to other commodities. The most famous example here was the purchase and storage in 2010 of a large part of the global cocoa harvest by the hedge-fund investor Anthony "Choc Finger" Ward.

Food-based derivatives which do not reflect the underlying real economy – i.e. used for the hedging of buying and selling prices by farmers or food producers – should be viewed in a particularly critical light, as the direct and indirect impacts on producers and consumers, especially in emerging and developing economies, can scarcely be fully anticipated or evaluated.

The outlook for financial investments in commodities is a “Fair Trade2” situation, with clear social and environmental rules governing the extraction of, trade in, and speculation of relevant commodities. Much research still needs to be done here with regard to analysing the social and environmental impacts of commodity investments and developing methods for rating the ESG quality of such investments.

„Particularly problematic are investments in physical commodities, where the investor interferes directly with the price mechanism, hoarding scarce resources and thus removing them from the economy. Sustainability-oriented investors should campaign for a breakthrough in global standards and traceability initiatives for the production of commodities, with the aim of ensuring that these will in future be applied to commodity investments.“

Ivo Knoepfel, Managing Director onValues Ltd.; author of the study “Responsible investment in commodities” (2011)

1.2.2 Emission permits

Carbon credit funds or CO_2 funds were originally intended to cover the demand for emission permits from countries and companies with reduction obligations. The fund operates by purchasing emission permits, principally from Clean Development Mechanism (CDM) and Joint Implementation (JI) projects, with the capital it has amassed and passing these on to investors as required. This type of fund is attractive both to countries and to companies with emissions trading obligations, which use the certificates to fulfil their obligations under the Kyoto Protocol or the EU Emissions Trading System (EU ETS).

In parallel with this, carbon credit funds have also established themselves as financial assets in recent years. Here, against the background of a shortage of emission permits, investors speculate on rising CO_2 prices and price differentials in international emissions trading.

For example, they purchase emission permits from the project developers of CDM projects and sell them to companies and countries with reduction obligations, which can then use them under the EU ETS or similar cap & trade systems. The general rule here is that the earlier a purchase agreement is reached regarding the development of CDM or JI projects, the lower the purchase price for certificates from such projects are. Such agreements are therefore sometimes reached even before the projects have been officially approved by the relevant bodies at the United Nations Framework on Climate Change (UNFCCC). There are, however, risks inherent in this procedure, for example that the project may be rejected by the UNFCCC.

While there are, as yet, very few relevant investment products available to private investors, say in the form of Delta 1 certificates (investment certificates that are directly linked to an underlying asset) on EUA futures or limited-partnership shares in primary market funds, a number of vehicles have already been set up for institutional investors. These are dominated by funds, the object of whose business is the procurement and distribution of emission permits for companies subject to emissions trading obligations. For a long time, the comparatively low correlation between CO_2 investments and traditional investments was seen as an advantage. However, recent experience has shown that there is a clear correlation with the general macro-economic conditions which also influence movements in the share and bond markets.

oe-quote

„The large numbers of emissions permits issued within the EU ETS have led to extremely low CO_2 prices and thus also given out misleading signals to the market. It is therefore essential that the EU takes positive action to remedy existing shortcomings as quickly as possible in order for significant emissions reductions to be achieved in the third trading period, from 2013 onward.“

Kristina Rüter, Research Director at oekom research

The oekom Position Paper Emissions Trading provides information about the background to the European and international trade in emissions certificates and the way this functions.

1.2.3 Microfinance

In autumn 2010, there was a whole series of horrifying reports about suicides in India which were linked to the overindebtedness of microborrowers and aggressive debt collection methods by the microfinance institutions (MFIs). Overall, it is clear that microfinancing can no longer be rated positively per se, and that questions about the business models of MFIs and the specific social and environmental effects of microfinancing in the target countries are becoming increasingly important. Nonetheless, there is still a huge demand for capital in the microfinance sector. The Grameen Foundation puts this at 400 billion US dollars worldwide.

As in the past, development work and microfinance institutions continue to be financed principally through funds from public donors and (supra-) national organisations like the World Bank and the German bank KfW. In addition, for a number of years, efforts have been made to divert funds from private and institutional investors toward microfinancing. One of the pioneers in this area is the cooperative Oikocredit.

In the recent past, the range of relevant funds for institutional and private investors has risen markedly. With the money they raise from institutional and private investors, these funds can extend loans to microfinance institutions. The increasing involvement of institutional investors, in particular, is supported by public institutions, which often fulfil a facilitating function, for example by providing guarantees or investing public funds in a "first-loss tranche". Such tranches are the first to be called upon in an emergency, in order to cushion possible losses. The creditworthiness of MFIs, as recipients of capital from the funds, is checked by specialised rating agencies such as Microrate, Microfinanzas or M-CRIL. This process involves evaluating the MFIs' strategies, their ownership and corporate governance structures, the quality of their credit portfolios and their market positions.

Experts state that there are currently more than 90 microfinance investment vehicles, i.e. investment funds or structured products, with an overall volume of just under six billion euros. By 2015, the World Bank is anticipating revenue from private sources amounting to 15 billion euros. One advantage of microfinance products is seen as being their low correlation with other asset classes, i.e. their independence from the market fluctuations of other investments.

In Europe, Luxembourg and Switzerland are home to numerous microfinance funds aimed at private investors. In Germany, the law on investment was changed at the end of 2007 to facilitate the establishment and marketing of this type of fund. In autumn 2010, KfW, the world's largest financier of microfinance, issued its first microfinance bond. The resources raised, 250 million euros in total, will be used to support the global expansion of the microfinance sector. KfW is thus adding a new variant to supplement the existing themed bonds from the World Bank ("Green Bond") and the Asian Development Bank ("Water Bond").

> *"It is in the interest of investors and providers of microfinance investment products that there be voluntary and statutory regulations to protect customers and ensure transparency in the microfinance market."*
>
> Steffen Ulrich, German Catholic Bishops' Organisation for Development Cooperation Misereor e. V.

Further information on this topic can be found in the oekom Position Paper Microfinance

1.3 Outlook: quantity and quality

Sustainable investments have a 47 per cent market share of the European capital market: this figure comes as a pleasant surprise, but also gives rise to a certain degree of scepticism. With volumes at this level, should the issue not be far more prominent in the public's perception? Should the bank advisors not be promoting relevant products more actively? And above all, should the effects on companies not be more obvious, if one in every two euros invested in Europe is being invested taking ESG criteria into account?

As important as the growth in the SRI market is, in order to prove that sustainable investments represent an independent, viable and attractive form of investment, it is also important to have a differentiated analysis of the volumes invested and the various strategies employed. The starting point here is the question of the extent to which a strategy - be it the best-in-class approach, active engagement or the integration of ESG criteria into conventional financial analyses - makes a contribution to getting companies (or countries) to change course toward greater consideration of sustainability issues. In principle, each of the strategies mentioned can make a contribution here, it is just a question of the way in which it does so and of the extent to which the relevant criteria are taken into account. This is especially true in the case of the integration of social and environmental criteria into financial analysis. For many years, this was a sort of "Holy Grail" for sustainable investment. The mantra went that, when conventional analysts first started applying this type of criteria, then the goal would have been reached in terms of sustainability.
According to data from the Eurosif study, the integration strategy is used in more than 50 per cent of sustainability-oriented investments in Europe, totalling more than 2.8 trillion euros. Unfortunately, the study does not comment on the quality of the integration. However, it can be assumed that this ranges from the consideration of individual criteria, such as climate strategy, to the consideration of comprehensive lists of criteria, as is called for in the UN PRI Principles. However, only the systematic consideration of relevant criteria over the entire spectrum of sustainability will bring about the desired effect on companies and countries. The same is true of engagement: here, only a comprehensive and systematic approach, a continuous dialogue with companies, will bring about change. Moreover, engagement is ineffective without the option of disinvestment, i.e. selling shares or bonds, so it is essential that this be an integral part of the strategy.

The best-in-class approach, too, must be evaluated against this background. Following the events surrounding the "Deepwater Horizon" oil rig and given the listing of BP in numerous sustainability indexes and funds, in 2010 there was much debate, some of it very critical, about this strategy, which is intensively pursued in Europe, particularly in the German-speaking countries. However, it seems a little extreme to base the appropriateness (or lack of it) of the approach on one individual case. At the same time, the debate shows the ongoing uncertainty over the effectiveness of a strategy which is restricted to labelling the best companies in an industry without first defining specific minimum standards. oekom research sees the consideration of absolute minimum requirements in terms of sustainability performance – what is known as the absolute best-in-class approach – in combination with the application of the criteria in practice and the traceable evaluation of these criteria as a way of further increasing the acceptability of this strategy.

From the point of view of oekom research, it is now time, under the slogan **quantity and quality**, to herald a second phase of sustainable investment. The anticipated further quantitative growth of the SRI market – here, drivers identified by the Eurosif study include the increasing demand from institutional and private investors and external pressure from NGOs and the media – must be accompanied by qualitative improvement in the implementation of the strategies. This will entail, depending on the strategy, a more systematic approach, more criteria and more direct influence on companies. However, it will also require more evidence of the actual impact on the companies. Only in this way can one of the key concerns of sustainable investment be achieved – getting companies to change course toward sustainable management, or as Eurosif's slogan so succinctly puts it: "Sustainability Through (European) Financial Markets".

2. Corporate Responsibility – status and trends

In 2010, corporate social responsibility was brought to the public's attention due to numerous scandals, first and foremost the "Deepwater Horizon" disaster in the Gulf of Mexico. However, the debates about data protection in connection with the publication of images on Google Street View or the suicides at the Taiwanese electronics supplier Foxconn, which produces goods for Apple and Hewlett-Packard, among others, are also still fresh in the memory. Are these isolated cases, or is the economic upturn which is taking place in at least some national economies accompanied by a disregard for social and environmental standards?

These and other issues concerning corporate social and environmental engagement lie at the heart of the oekom Corporate Responsibility Review 2011. oekom research now has an even broader basis for its analyses, with the oekom universe currently comprising over 3,100 companies. The review's analyses focus firstly on general developments in companies and industries. Secondly, we take a closer look at a few issues which have been the subject of intense public debate or which have particularly caught our attention. This year, these include the way companies handle sensitive customer data, the increasing linking of management remuneration to sustainability criteria and the global situation with regard to labour rights and human rights. The outlook this time focuses on the relationship between sustainability rating agencies and companies.

2.1 Basis for the analyses: the oekom Universe

As a sustainability rating agency, oekom research specialises in evaluating companies and countries according to social and environmental criteria. We currently have 28 analysts who collect relevant data from companies and from independent sources and evaluate this using industry-specific rating methods. Our ratings are used by more than 70 clients from eight countries in the management of their capital investments and for designing appropriate investment products, e.g. sustainable mutual or special funds.

oekom research regularly evaluates approximately 3,100 companies from more than 45 industries and over 50 countries. We cover international indexes such as the MSCI World, MSCI Emerging Markets and Stoxx 600 as well as important national indexes like the Austrian ATX, the Belgian BEL20, the French CAC40, the German DAX family and the Swiss SMI.

In a two-stage process, the securities from a parent population which meet the requirements of sustainability-oriented investors are identified, i.e. those which perform well in terms of sustainability and/or do not exhibit controversial business practices or activities defined as exclusionary criteria by the investors.

oekom two-step model; as of 2010-12-31; source: oekom research AG (2011)

As a first step, the **oekom Corporate Scouting** process identifies those companies which can demonstrate that they meet minimum requirements in terms of social and environmental measures and of transparency about these. Companies which do not meet these requirements are pooled together in the oekom Scouting Universe. These currently make up approximately 2,000 of the 3,100 companies evaluated in total. oekom research's analysts carry out an indicative rating of these companies. The Scouting is updated annually.

Companies which clear this first hurdle are accepted into the **oekom Rating Universe**. These issuers of shares and bonds, currently numbering around 1,100, are comprehensively evaluated in a second step, the oekom Corporate Rating (see next section).

The oekom Rating Universe can be divided into three sub-universes:

1. Large listed companies from conventional industries, currently around 800 securities;
2. Small and medium-sized listed companies with a focus on sustainability, currently over 200 companies;
3. Non-listed bond issuers, currently over 100 issuers.

Please note:

The following analyses relate to different parent populations. Please refer to the relevant notes in the respective analyses.

The terms "corporate responsibility (CR)" and "sustainability", as well as "CR management" and "sustainability management", are used synonymously in the study.

oekom Corporate Rating

oekom's Corporate Rating provides a comprehensive evaluation of a company's social and environmental performance. To accomplish this, depending on the sector analysed, oekom research uses approximately 100 individual indicators from six categories which are drawn up on a sector-specific basis in order to cater for the particular social and environmental challenges faced by each sector.

oekom research employs an absolute best-in-class approach. Under this approach, the only companies which qualify for investment are those which have achieved a minimum rating stipulated by oekom, on its rating scale which ranges from A+ (highest score) to D-. In this context, oekom research uses the term "Prime Threshold", which is determined separately for each industry. The greater the industry's negative impact on the environment, employees and society, the higher the threshold. Companies whose performance exceeds the threshold are awarded oekom Prime Status by oekom research.

The lists of criteria are regularly updated in order to take into account new technical, social, legal and other developments.

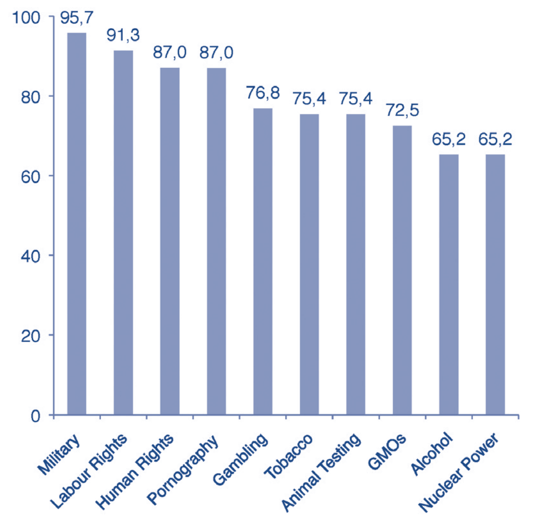
Areas of assessment in the oekom Corporate Rating; source: oekom research AG (2011)

Exclusionary criteria

The Eurosif study clearly stressed the importance of the use of exclusionary criteria in sustainable development (cf. section 1.1.2). These are employed in more than one-third (37.1 per cent) of all sustainable capital investments in Europe. This process excludes from investment those companies which either

- are active in controversial areas of business, i.e. for example producing alcohol, nuclear power, armaments, genetically-modified seed or tobacco products, or
- display controversial business behaviour that violates recognised standards, e.g. the labour standards of the International Labour Organization (ILO) or the human rights defined in the UN Declaration of Human Rights.

For all the companies in the oekom Rating Universe, oekom research carries out a comprehensive analysis in respect of potential breaches of a total of 18 exclusionary criteria. The diagram shows the ten exclusionary criteria most frequently used by oekom research's clients. It is clear that the "sin stocks" traditionally spurned by church investors – i.e. alcohol, gambling, pornography, armaments and tobacco – are still considered significant today. Another aspect that is particularly important to customers, however, is the exclusionary of issuers which are involved in violations of labour rights and human rights (cf. also section 2.3.3).



Top 10 of the exclusionary criteria used by oekom research's clients; as of 2010-12-31; in %; source: oekom research AG (2011)

Case study: BP – how credible is the best-in-class approach?

The oil disaster in the Gulf of Mexico was caused by serious management failings, according to the official National Commission inquiry. A summary of the inquiry report published in January 2011 states that safety was not a priority for the managers of the companies involved in the accident, BP, Halliburton and Transocean.

Following the report on the accident, a number of critical comments have been made about the listing of BP in various sustainability indexes and funds and, linked with this, about the pros and cons of the best-in-class approach. oekom research's stance on this matter is as follows:

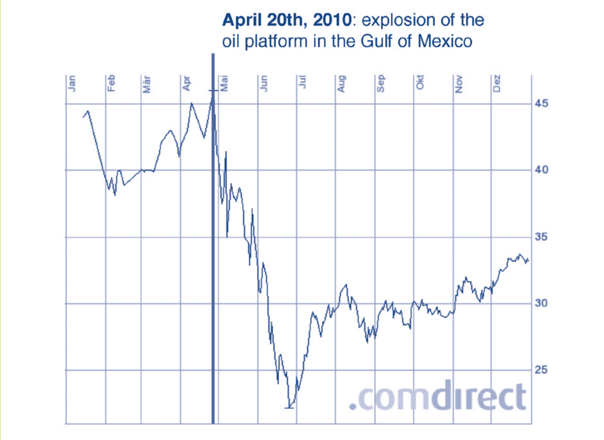
1. The aim of the best-in-class approach is to initiate competition among companies in individual sectors of industry to produce the best sustainability performance. The more capital is invested taking social and environmental criteria into account, and thus the greater the incentive is for companies to make themselves an attractive proposition for such investors, the better this lever functions.
2. Here, oekom research favours an absolute best-in-class approach, where best-in-class status is awarded only to those companies which not only are relatively among the best companies in a sector, but also meet absolute requirements in terms of sustainability performance. For all sectors, oekom research has therefore defined strict minimum requirements for companies' social and environmental performance. Only companies which meet these requirements are awarded oekom Prime Status.
3. Comprehensive best-in-class ratings such as the oekom Corporate Rating provide investors with information on numerous individual issues and thus enable a detailed analysis of the opportunities and risks. By contrast, concentrating on individual key performance indicators (KPIs) can only deliver an incomplete picture of a company. Thus in the oil & gas industry, greenhouse gas emissions are often used as a key indicator. Here, BP performs well compared with its competitors, e.g. Shell and Exxon. Investors who had made their investment decision on the basis of this criterion were not aware of the company's poor environmental and safety standards.

4. oekom research also regards a combination of a best-in-class approach with the use of exclusionary criteria as a sensible option. This ensures that companies with relevant breaches in relation to the environment and also labour rights, human rights and corporate governance can be excluded from the investment universe, irrespective of their performance rating.

In oekom research's ratings, BP has regularly failed to achieve Prime Status in recent years. The reasons for this included shortcomings in the areas of environmental protection and plant safety. For example, on the grounds of cost, necessary investments have been put off, the modernisation e.g. of refineries has been neglected and pipelines have not been maintained, despite numerous clear warning signs, such as critical condition/damage reports, leaks and accidents, as well as fines. Very serious accidents have occurred as a consequence of this, for example an explosion in 2005 at a refinery in Texas which caused a large number of deaths.

In the environmental sphere, too, the company has a long history of violations. For example, for years, large quantities of carcinogenic benzene were being released untreated into the atmosphere from BP's refinery in Whiting (US). In Alaska, inadequate maintenance on the pipeline system led to repeated major leaks, for which BP was fined 20 million US dollars in 2007. In January 2011, the pipeline had to be closed temporarily because of a renewed leak.

Customers who base their investments on oekom Prime Status will therefore not have invested in BP securities. As a result, they have been able to avoid both the economic losses associated with the fall in the share price as well as any loss of reputation following the public debate.



Market trend of BP shares, 2010-01-01 to 2010-12-31; source: www.comdirect.de

2.2 Corporate responsibility: overall performance

84 per cent of Germans want companies to increase their commitment to CSR. At the same time, according to a study by the consultancy firm Icon Added Value, 52 per cent think that large corporations, irrespective of sector or origin, do not act responsibly. So, high expectations combined with a high degree of scepticism are definitely – not an easy point of departure for companies seeking to position themselves as socially responsible players. This can only be done by the systematic implementation of appropriate measures. As we live in an information society, PR spin or even "greenwashing" will easily be detected and penalised. How serious are companies' efforts? We hope that the evaluations and interpretations below, which are based on oekom research's rating results, will help to answer this question.

2.2.1 Companies with oekom Prime Status

The following tables each show five companies from selected indexes which in 2010 demonstrated a particularly high degree of engagement in the integration of social and environmental criteria into their management structures, processes and products. Possible exclusionary criteria have not been taken into account here.

In the **DAX 30**, SAP achieved the highest rating, with a score of 67.01 on a scale from 0 to 100. The company, which has jumped from ninth into first place, stands out in particular for comprehensive measures on increasing the energy efficiency of its data centres and numerous measures for promoting digital integration of e.g. poorer segments of the population and minorities. As in the previous year, Henkel, BMW and Deutsche Telekom were among the top 5 companies.

Rank	Company	Score	Rank 2009
1	SAP AG	67,01	9
2	Henkel AG & Co KGaA	65,37	1
3	Bayerische Motorenwerke AG	64,92	4
4	Deutsche Telekom AG	61,82	2
5	Siemens AG	61,30	16

Top 5 DAX 30 companies with the best oekom Corporate Rating; as of 2010-12-31; in %; source: oekom research AG (2011)

Siemens has surged from 16th to 5th place. The company, which in the past has hit the headlines following corruption scandals and its establishment of a company-friendly trade union, has made great progress, in particular in the expansion of its “green” product portfolio as well as in the provision of company-wide social and environmental data. It has also managed to improve its governance structures for preventing corruption and bribery.

The top securities from the DAX 30 also occupy the top spots in the **DJ Euro Stoxx 50**. Here, SAP has jumped from 14th to first place, followed by BMW, which has only recently joined the index, and Deutsche Telekom.

Rank	Company	Score	Rank 2009
1	SAP AG (DE)	67,01	14
2	Bayerische Motorenwerke AG (DE)	64,92	--
3	Deutsche Telekom AG (DE)	61,82	3
4	L’Oréal SA (FR)	61,66	5
5	Siemens AG (DE)	61,30	28

Top 5 DJ Euro Stoxx 50 companies with the best oekom Corporate Rating; as of 2010-12-31; in %; source: oekom research AG (2011)

Munich-based car manufacturer BMW scored points for the company-wide implementation of a climate protection strategy which takes into account sector-specific climate risks and for comprehensive measures to ensure that its major suppliers comply with standards relating to workers’ rights and health and safety at work. Deutsche Telekom is also able to point to a comprehensive climate strategy and has implemented far-reaching measures for improving the take-back of used communication equipment. The French cosmetics manufacturer L‘Oreal and the German company Siemens complete the top 5.

This year, for the first time, oekom research has rated all the companies in the **MSCI World** and the MSCI Emerging Markets. In the MSCI World, rene-

Rank	Company	Score
1	Vestas Wind Systems A/S (DK)	86,32
2	EDP Renovaveis SA (PT)	85,28
3	Gamesa Tecnologica SA (ES)	83,19
4	Iberdrola Renovables SA (ES)	78,96
5	First Solar Inc (US)	77,87

Top 5 MSCI World companies with the best oekom Corporate Rating; as of 2010-12-31; in %; source: oekom research AG (2011)

wable energy companies dominate the top rankings. Like companies from other "sustainability sectors" – such as emissions reduction, recycling and water treatment, for example – they are more likely to receive a positive rating by oekom research, as their products and services make a major contribution to sustainable development. The top four spots are occupied by European companies.

The Indian IT services provider Wipro took first place in the top 5 companies in the **MSCI Emerging Markets** index. The company has comprehensive guidelines on responsible marketing and offers a large range of environmentally-friendly products and services. The Brazilian cosmetics manufacturer Natura Cosmeticos has implemented wide-ranging measures for procuring and using sustainably produced renewable raw materials. The frontrunners from the emerging markets have nothing to fear from comparison with European, US or Japanese companies. However, the idea of CSR has yet to find broad acceptance in the economies of the emerging markets.

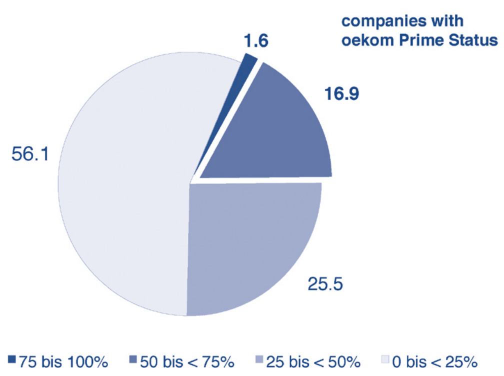
Rank	Company	Score
1	Wipro Ltd (IN)	72,30
2	Natura Cosmeticos SA (BR)	63,09
3	Tata Consultancy (IN)	62,35
4	Magyar Telekom (HU)	62,31
5	Suzlon Energy Ltd (IN)	61,38

Top 5 MSCI Emerging Markets companies witih the best oekom Corporate Rating; as of 2010-12-31; in %; source: oekom research AG (2011)

Overall, by the end of 2010 approx. one in six companies in the oekom universe had been awarded oekom Prime Status, including:

- just under 300 conventional large-scale companies,
- approximately 200 SMEs with a focus on sustainability and
- over 50 non-listed bond issuers.

One-quarter of all the 3,100 companies have already laid down a basis for the systematic development of sustainability management systems and associated sustainability communication systems, but considerably more than half the companies have not yet taken the issue into account or provide no transparency about any activities in this area.



Average rating of companies in the oekom Universe; on a scale from 0 (very poor sustainability performance) to 100 (excellent sustainability performance); in %; source: oekom research AG (2011)

2.2.2 The sector champions

The following table gives an overview of the best companies from selected sectors of the economy. The basis used here is the best-in-class rating. Possible breaches of exclusionary criteria have not been taken into account.

The top place has changed hands, compared with 2010, in eight of the 14 sectors looked at here. It is noticeable that in a good third of the sectors, the former number 2 has moved up the rankings to first place. In the engineering industry there has been a "all-Sweden" switch, with Atlas Copco supplanting its competitor Volvo. In the media and telecommunications industries, UK companies retain the leading positions. German companies head three of the sectors. Altogether, with six top places successfully defended and three companies slipping down to second place, the best companies in the various sectors show a high level of continuity in their engagement.

oekom research interprets this data as meaning that within a small, but steadily growing, group of leading companies, there is intense competition to come up with the best sustainability performance. Or, as the former German national coach Berti Vogts once put it: "It's getting crowded at the top."

Sector	Best company 2010	Country	Rank previous year	Best company 2009	Country
Automobile	Renault	FR	1	Renault	FR
Chemicals	BASF	DE	1	BASF	DE
Commercial Banks	HVB Group	DE	1	HVB Group	DE
Consumer Electronics	Electrolux	SE	4	Samsung Electronics	KR
Food & Beverages	Coca Cola Hellenic Bottling	GR	new	Danone	FR
Household Products	Henkel	DE	1	Henkel	DE
Insurance	Standard Life	UK	new	Allianz	DE
Machinery	Atlas Copco	SE	2	Volvo	SE
Media	Reed Elsevier	UK	2	ITV	UK
Metals & Mining	Norsk Hydro	NO	1	Norsk Hydro	NO
Pharmaceuticals	GlaxoSmithKline	UK	7	Sanofi-aventis	FR
Retail	Migros	CH	1	Migros	CH
Telecommunications	Vodafone	UK	2	BT Group	UK
Utilities	Terna Rete Elettrica Nazionale	IT	new	EDP	PT

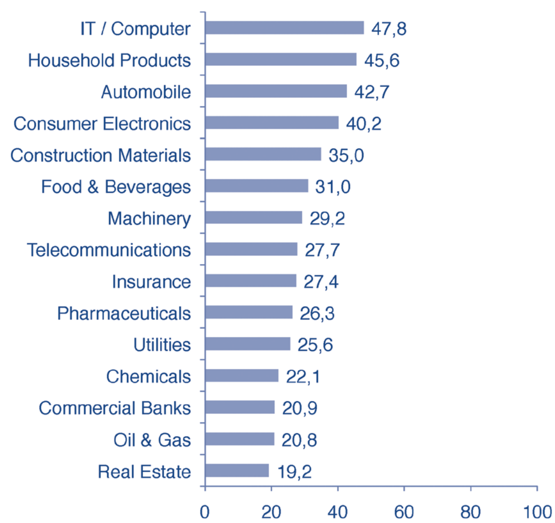
The best companies in selected sectors as of 2010-12-31; the sectors, where the leading position has changed, are marked; basis: oekom Universe; source: oekom research AG (2011)

2.2.3 Corporate responsibility in selected sectors

In none of the conventional sectors of the economy an average score of 50 per cent or more was archived. Due to the broadening of the analysis to include comparatively poorly rated companies from the oekom Scouting Universe, the results here are again worse than in the previous year, which (unfortunately) brings them rather closer to the truth. As described in section 2.1, the Scouting Universe covers those companies which demonstrate too little social and environmental engagement or are too lacking in transparency to qualify for an oekom Corporate Rating.

Once again the computer manufacturers came out on top, with an average score of 47.8 per cent. In second place were the manufacturers of household products (45.6 per cent), followed by the automotive industry (42.7 per cent).

Languishing at the bottom of the rankings were the real estate and oil & gas sectors and the commercial banks. While the real estate sector had already received the worst average rating in the previous year, the average rating for both the other sectors mentioned fell markedly, by 13.8 percentage points for oil & gas companies and by as much as 16 percentage points for the commercial banks. The underlying reason here, as with the decline in average ratings in the other sectors examined, is generally the inclusion of comparatively poorly rated companies from the oekom Scouting Universe.



Average rating of the sector's companies on a scale from 0 (very poor sustainability performance) to 100 (excellent sustainability performance); as of 2010-12-31; basis: MSCI World; in %; source: oekom research AG (2011)

No business success without sustainability

This phrase sums up the findings of a survey of CEOs on the topic of sustainability. For example, 93 per cent of the top managers surveyed anticipate that sustainability will have a substantial influence on their core business in the years to come. For the study “A New Era of Sustainability”, Accenture, commissioned by the UN Global Compact, surveyed 766 chief executives, including 439 from Europe. Fears that the struggle to deal with the consequences of the world economic crisis might be detrimental to sustainable company management have turned out to be unfounded. On the contrary: four out of five of those surveyed said that, for them, the financial crisis had further underscored the importance of sustainability. Whereas in 2007 just half the top managers surveyed stated that sustainability issues already formed part of their company strategy, the figure is now 81 per cent. However, the survey participants appear to view the long-term integration of sustainability into their core business as an immense undertaking: almost half (49 per cent) of the CEOs consider the implementation of a sustainability strategy across all parts of their companies to be the greatest challenge facing them.

2.3 Corporate responsibility with regard to selected issues

In the following sections, we will analyse developments in selected areas which were particularly significant during the last year or which in oekom research’s view will be increasingly important in the social, business and political arenas in the coming years. As in both the previous oekom Corporate Responsibility Reviews, we have examined the spread of corruption and other economic crimes as well as the situation as regards labour rights and human rights. We have also produced, for the first time, a “world map of human rights violations”, which serves to illustrate the type and extent of relevant violations by companies.

In this edition, we also analyse the link between salaries/bonuses and companies’ sustainability performance, the handling of sensitive customer data and measures to protect the forests. Finally, we pick up on some of the developments in areas which were highlighted in the 2010 edition of the oekom Corporate Responsibility Review.

2.3.1 Corruption, fraud and other white-collar crimes

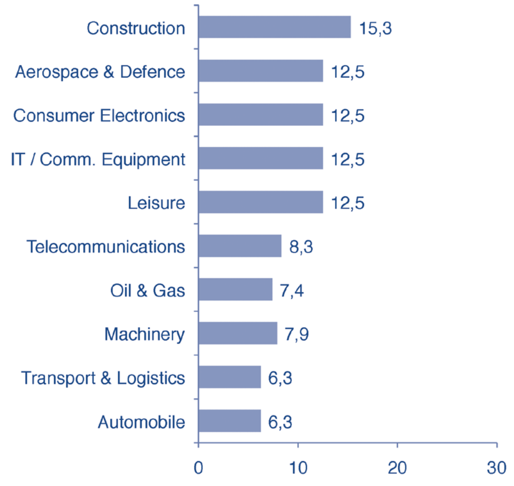
Corruption

In Germany it is called “Schmiergeld”, in Greece “Fakelaki”, in Bulgaria “rushwet”, in Brazil “propina”, in France “pot-de-vin”, in Austria “Schmattes”, in Japan “Wairo” – the staff at oekom research speak a total of 21 languages and could provide many more examples of often rather euphemistic names for what is generally known in English as a “bribe”. Bribery goes by many names, and according to the anti-corruption initiative Transparency International (TI) is on the increase worldwide. One in every four people around the world, according to the findings of TI’s 2010 Global Corruption Barometer, published in December 2010, has paid a bribe to officials or institutions over the past twelve months. Around half of those who have paid bribes stated that the reason was in order to circumvent a problem. Approximately one-quarter said that they wanted to speed up official procedures. More than 91,000 people in 86 countries and territories were surveyed.

According to TI, bribery was most widespread in sub-Saharan Africa. Here, more than half of respondents had paid bribes to corrupt officials during the last year. Next came the Middle East and North Africa, where at least one-third reported having made payments of this type. In Europe and in North America, the corresponding proportion stood at five per cent. Respondents were pessimistic about trends in corruption in Europe and North America. There, 73 per cent and 67 per cent of people respectively thought that people had become more susceptible to corruption over the last three years.

TI's analysis did not include bribery at company level, but here, too, some sectors remain particularly prone to oiling the wheels of business through bribery. As in the previous year, the ignominious 'top spots' here are occupied by the construction industry (15.3 per cent of companies in the oekom rating universe), the aviation and armaments industry and producers of consumer electronics and of communication equipment as well as the leisure sector (each with 12.5 per cent).

When interpreting the data, it should be noted that experts put the clear-up rate for corruption cases at between just five and twenty per cent.



Percentage of companies in each industry with breaches in the area corruption; as of 2010-12-31; basis: oekom Rating Universe; in %; source: oekom research AG (2011)

Case study: BAE Systems

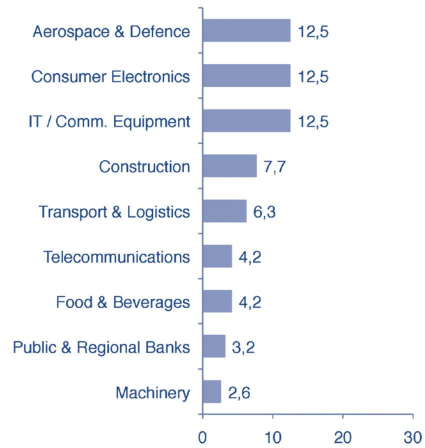
At the beginning of February 2010, BAE Systems agreed with the UK Serious Fraud Office (SFO) and the US Department of Justice to pay fines totalling around 327 million euros. This drew a line under years of investigations into allegations of corruption in Europe's largest arms manufacturer. BAE is alleged, among other things, to have paid millions of euros in bribes via subsidiaries. At the heart of the scandal was the so-called Al-Yamamah deal to supply fighter jets to Saudi Arabia, as part of which around one billion pounds were said to have been paid to Prince Bandar bin Sultan. In 2006, the case caused consternation worldwide when the British Prime Minister at the time, Tony Blair, called a temporary halt to the investigations into BAE on the grounds of an alleged threat to national security.

Fraud

Balance sheets are one of the mainstays of traditional financial analysis and therefore also key to investors' decisions on where to invest. The falsification of accounts is therefore a highly-charged topic for investors.

Although in recent years there have been no really spectacular cases like those of Enron and Parmalat, in 2010 a few companies did come under public scrutiny for suspected accounting fraud. Particularly noteworthy here are the events surrounding the acquisition of Hypo Alpe Adria by Bayerische Landesbank, but HSH Nordbank also came under suspicion of having manipulated its accounts.

However, these cases are merely the tip of the iceberg. Analysis of companies rated by oekom research shows that in some sectors, approximately one in eight companies can be shown to have committed offences of this type. As in the previous year, the aviation and armaments industry, as well as manufacturers of consumer electronics and communications technologies, are at the "top" of the rankings here.



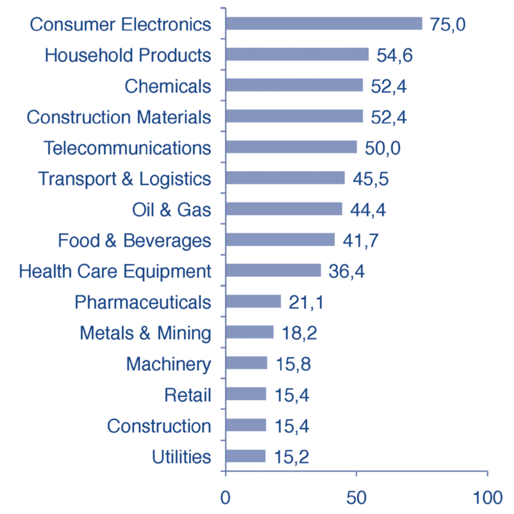
Percentage of companies in each industry with breaches in the area accounting fraud; as of 2010-12-31; basis: oekom Rating Universe; in %; source: oekom research AG (2011)

Restrictive practices

385 million euros in fines for eleven French banks, 100 million euros for seven European cement manufacturers and 115 million euros for five German and French manufacturers of ophthalmic lenses – altogether 600 million euros in fines for infringements of anti-trust law and/or anti-competitive behaviour, in particular price-fixing.

Just these few examples from 2010 illustrate the economic magnitude of these infringements by companies. Those who suffer most from this are often ordinary citizens, either directly through excessively high prices, e.g. for ophthalmic lenses, or indirectly via taxes and duties, for example due to overpriced public building projects.

Manufacturers of consumer electronics have a sorry track record here: three-quarters of companies in this sector can be shown to have been involved in offences of this kind. Among the producers of household products, chemicals and building materials, too, more than half the companies have taken part in such restraints on competition, and in the telecommunications industry one in two companies is affected.



Percentage of companies in each industry involved in violations of competition regulations; as of 2010-12-31; basis: oekom Rating Universe; in %; source: oekom research AG (2011)

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“For national economies which rely on self-regulation of the market, the widespread prevalence of constraints on competition poses a serious risk to the functionality and acceptance of the economic system.“

Rolf D. Häßler, Director Product & Market Development at oekom research

Case study: Essilor

The German Federal Cartel Office reported in June 2010 that price-fixing agreements by leading manufacturers of ophthalmic lenses had virtually paralysed competition in the market since the year 2000. Following an investigation lasting almost two years, the German Cartel Office imposed a fine of 115 million euros on the five leading manufacturers, the Central Association of Optometrists (ZVA) and several individuals. The French ophthalmic lens manufacturer Essilor and its German subsidiary Rupp+Hubrach Optik have to pay 50 million euros, or almost half the total fine. According to the Federal Cartel Office, Essilor regularly met, in two separate circles, with the other manufacturers involved in the price-fixing agreements. In one group, the companies agreed their price surcharges and the discounts or bonuses they planned to offer opticians. In a second group, the manufacturers agreed their “non-binding price recommendations” with the Central Association. The Cartel Office stated that in practice, the opticians had largely stuck to these price recommendations. The price increases had generally been passed on to customers.

Summary

When the prevalence of restrictions on competition, corruption and accounting fraud becomes a measure of the state of corporate governance, there is genuine cause for concern about “good governance”.

In some sectors, fair and law-abiding behaviour is more the exception than the rule. This is particularly true where competition is concerned. The proportion of companies committing violations in this area has risen yet again compared with the previous year. In as many as five sectors, the proportion of companies committing violations already stands at 50 per cent or higher. Last year this was true of “only” two sectors. As far as corruption is concerned, the proportion of companies involved, compared with the previous year, has declined slightly, with the top four places here still “defended” by the same sectors, first and foremost the construction industry. In the area of accounting fraud, there was little overall change.

2.3.2 Remuneration structures and sustainability performance

Experts see inappropriate incentive structures, in particular the payment of high bonuses for short-term economic successes, as lying at the heart of the financial and economic crisis of the last three years. Politicians have reacted to this - albeit only in a symbolic way – by temporarily capping management salaries and taxing bonuses. At the same time, companies themselves are starting to tackle the problem. Two different approaches can be distinguished here:

Timing:
On the one hand, the payment of bonuses is increasingly stretched over a longer period of time and is only completed when the medium-term economic success of the management system as a whole and/or of individual measures and business transactions has been proven. This is intended to reduce the incentive to conclude extremely high-risk deals which yield only short-term gains.

Content:
On the other hand, ESG goals as well as financial goals are being included in managers’ target-based salary and bonus systems. These range from individual targets, such as the reduction of CO_2 emissions at a particular site or high levels of employee or customer satisfaction, to comprehensive lists of sustainability targets. The achievement of these is often measured by a listing in one of the major sustainability indexes or a good rating by a well-known sustainability rating agency. Relevant sustainability ratings thus take on additional significance for companies.

Looked at overall, the measures are still rather patchy, so it is not possible to identify the best companies in each sector here, as we have with other issues in this report. The following companies have received comparatively good (in the case of the two energy suppliers, very good) ratings from oekom research for the way in which they integrate ESG criteria into their calculation of variable salary components:

- **Coop**: The Swiss retailer Coop allows profit-sharing to account for no more than 25 per cent of managerial salaries. It is calculated from the achievement of five goals, including environmental and social targets, e.g. on carbon emissions, the number of apprentices offered permanent posts and sales of sustainable products. For example, the “sustainable own-brands” sales target makes up 20 per cent of the head of the marketing and procurement department’s variable salary component.

- **Novozymes**: Top managers at the Danish pharmaceutical company Novozymes are rewarded for good annual results with a bonus, the size of which is determined by the extent to which eleven specified sustainability targets have been achieved. These include CO_2 emissions, energy and water efficiency, supplier management, employee satisfaction, accident rates, staff turnover and performance in sustainability ratings. The bonus is calculated by multiplying the basic bonus by the target fulfilment rate determined by the supervisory board. However, the detailed composition, particularly in relation to weightings, remains unclear. The size of share options on offer, like the bonus, depends on the achievement not just of financial but also of sustainability performance indicators.

- **RWE**: In April 2010, the German energy supplier RWE decided to start linking its management remuneration to sustainability criteria. The company says that in future, 25 per cent of the bonus payment will be deferred for three years. At the end of this period, the Supervisory Board will assess the extent to which medium-term goals have been achieved and will decide on the level of bonus payments to be made on this basis. In addition, a so-called "bonus malus" factor will be applied, based on the change in value added to the company over a period of three years, the "Corporate Responsibility Index" and the Group's "Motivation Index". The company says that the Corporate Responsibility Index will count for 45 per cent, while the Motivation Index will make up 10 per cent. According to RWE, the "bonus malus" factor can range from 0 per cent to 130 per cent overall. The Motivation Index is designed to reflect employee satisfaction and motivation. The Corporate Responsibility Index evaluates the environmental and social actions of the Group and looks at ten areas for action which are laid down in the company's corporate responsibility strategy. RWE has specified goals, key performance indicators and targets for each area. These areas include climate protection, energy efficiency, security of supply, pricing, health and safety at work and environmental protection.

- **Xcel Energy**: The US energy company Xcel Energy has introduced a bonus system based on a "scorecard", which covers environmental goals as well as individual performance and corporate development. The targets are updated annually. For the year 2009, for example, the scorecard included targets specified for the implementation of projects on emissions reduction, energy efficiency and renewable energies. The percentage impact of the achievement of targets and the corresponding payout rates are shown transparently in the relevant scorecard. For projects in the field of renewable energies, for example, the payout rate varies according to the level of additionally installed capacity in the year concerned. In addition, Xcel Energy states that the level of share options is also linked to the company's environmental strategy.

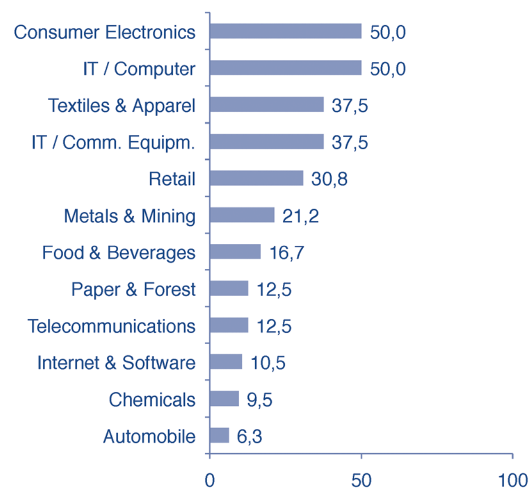
These are thus the first positive examples of integration of ESG criteria into top management target systems. It remains to be seen whether they lead to a general change in corporate strategy.

2.3.3 Labour rights and human rights

Labour rights

In 2007, a series of suicides among employees of the French car manufacturer Renault made headlines. The triggers for these acts of desperation were the poor working atmosphere at the research centre near Paris and the high pressure to achieve success. In May 2010, a series of suicides at the electronics manufacturer Foxconn in Taiwan, which produces goods for companies including Apple, Hewlett-Packard, Sony and Nokia, came to light. The company is part of the Taiwanese consumer electronics group Hon Hai Precision Industry. The suicides took place against a background of what employees say were extremely poor working conditions.

The electronics industry - with companies ranging from manufacturers of consumer electronics to computer manufacturers and producers of communications technologies – heads the list of sectors violating internationally recognised labour rights. One in two manufacturers of consumer electronics and compu-



Percentage of companies in each industry with breaches of labour rights; as of 2010-12-31; basis: oekom Rating Universe; in %; source: oekom research AG (2011) puters has committed violations in this area. Companies in the textile industry, which have relocated the majority of production to suppliers in low-wage countries in Asia, have almost by tradition had huge problems in this area.

Overall, as can be seen by the number of sectors affected and the sometimes very high number of companies involved, working conditions at suppliers in emerging markets (and in isolated cases also at "parent plants" in industrialised countries) continue to represent an enormous problem.

Case study: Gap, Marks & Spencer

Despite the fact that the retail companies Gap (US) and Marks & Spencer (UK) both have supplier monitoring systems in place, there have been further violations of employment law regulations at Viva Global and House of Pearl, two Indian companies which supply both retailers. For example, these suppliers frequently exceed the legal maximum overtime by a huge margin, as well as breaching the regulations on remuneration for overtime. In both companies, the number of overtime hours worked was up to eight per day and up to 150 per month, according to the UK daily 'The Guardian'. Workers at the factories also reported unanimously that they received only half the legally prescribed minimum wage for their overtime. Many of the employees were allegedly also procured for the supplier via a subcontractor which was responsible for their pay and was only paying them 25 pence an hour. According to the report, on this tiny income it is not possible for the workers at the suppliers mentioned to meet their basic needs and guarantee a subsistence-level income.

Marks & Spencer and Gap confirmed the allegations and provided assurances that they were taking pains to ensure an immediate improvement in conditions and to avoid repetition of such occurrences in future. Both companies announced their own investigations into the allegations and stated that the breaches had been detected in the course of their own auditing processes. Viva Global, supplying Marks & Spencer, has subsequently appointed a Human Resources Manager to tackle the grievances denounced by the workers. Gap says that it has instructed its suppliers to limit working hours to the legal maximum in future and to pay workers all overtime pay still outstanding.

Corporate activity in countries with restricted trade union freedom

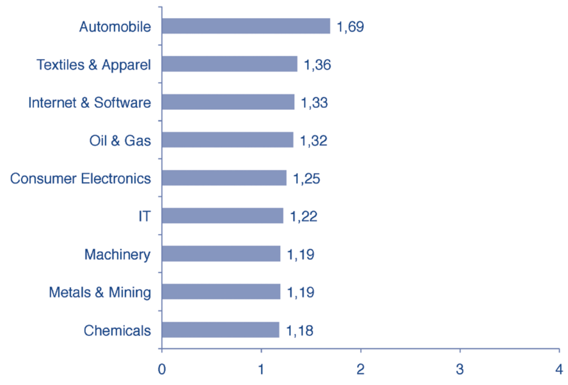
Trade union rights are generally acknowledged human rights in the workplace. These rights are defined and guaranteed by the United Nations Universal Declaration of Human Rights and by two key treaties of the International Labour Organization (ILO) (Conventions 87 and 98). According to these, nobody should be prevented from forming or joining associations and unions. In addition, employees have the right to collective bargaining and to form independent works councils and trade unions.

Many companies describe in their guidelines their international standards on granting trade union rights, but at the same time operate in countries in which these rights are partially or even totally restricted. The countries concerned include Egypt, Bangladesh and China, among others. One of the things which oekom research assesses with regard to the tensions here is the extent to which companies with their own subsidiaries in the countries concerned provide their employees with the opportunity for unionisation and co-determination and actively support this process. Factors looked at here include, for example:

- setting up works councils or working groups of managers and employees;
- greater cooperation with international trade unions and relevant NGOs;
- continuing education about labour rights;
- provision of the necessary information and resources so that employees can conduct negotiations with the company effectively and
- measures to protect from criminal prosecution employees who have taken a stand on freedom of association.

The best scores here were achieved by companies from the automotive industry, which have significantly expanded their manufacturing capacity in recent years, especially in China. The two German car manufacturers BMW and Daimler performed best in this area. Another German company, adidas, came out on top among the companies in the textiles sector, which had the second-highest average rating.

Overall, however, with a maximum average score of 1.69 on a scale ranging from 1 (very poor) to 4 (excellent), the standard of measures leaves a great deal of room for improvement.



Average rating of companies in each industry regarding implementation/promotion of co-determination in countries with restricted trade union freedom; basis: oekom Rating Universe; scale: 1 (very poor) bis 4 (excellent); as of 2010-12-31; source: oekom research (2011)

oe-quote

"Employee participation is essential in order to guarantee appropriate working conditions in factories. Responsible companies must therefore – particularly in countries in which there are no statutory requirements – create the conditions to enable such employee participation."

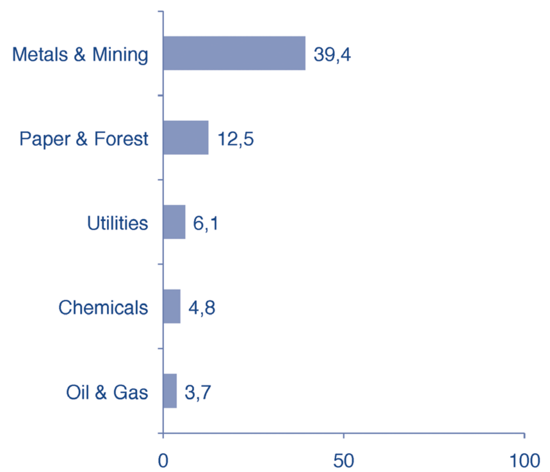
Isabelle Reinery, Senior Analyst at oekom research

Human rights

Although the events surrounding the award of the Nobel Peace Prize to Liu Xiaobo, whose chair had to remain empty during the award ceremony, received a great deal of public attention, human rights violations by companies, even during the past year, have often remained concealed from the general public. Violations in these areas are often uncovered by dedicated regional and international NGOs, which then publicise them as widely as they can. These organisations are also important partners for oekom research in researching the circumstances in such cases.

Companies in the mining industry are by far the most heavily involved in human rights violations. Almost 40 per cent of companies of this type in the oekom Rating Universe have perpetrated such a violation. These often include forced displacement of and inadequate compensation for inhabitants following the expansion of mines, disruption of the livelihoods of the local population and health problems following environmental pollution, for example the use of harmful substances such as mercury in gold mining.

oekom research has also documented individual cases of human rights violations in forestry companies, energy suppliers (see case study) and chemical and oil & gas companies. These include violations both by the companies themselves and by their suppliers.



Percentage of companies in each industry with breaches of human rights; as of 2010-12-31; basis: oekom Rating Universe; in %; source: oekom research AG (2011)

Case Study: Dong Energy, E.ON

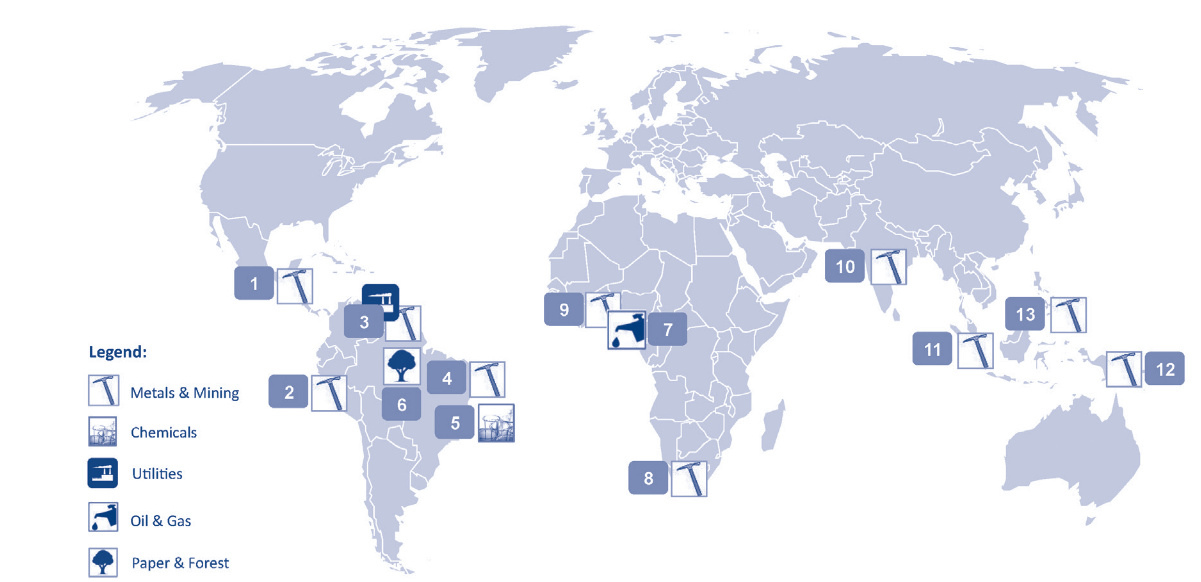
The energy suppliers Dong Energy and E.ON buy significant quantities of bituminous coal for their power plants from the controversial El Cerrejón mine in Colombia. This became known following the publication of a study by the NGO DanWatch in May 2010 on supplier relationships between El Cerrejón and electricity producers in Denmark. The El Cerrejón Coal Company operates one of the largest open-cast coal mines in the world and is owned in equal parts by the mine operators Anglo American, BHP Billiton and Xstrata. The DanWatch report confirms serious allegations of human rights violations in connection with the coal mine which human rights organisations have been raising for years and which have led to complaints being made to various international bodies. The allegations go back to 2001, when 200 people were forcibly displaced. Criticism at that time related to inadequate compensation payments, controversial negotiation tactics and threats made to inhabitants following the expansion of the mine, the destruction of the environment inhabited by the local people and health problems due to environmental pollution caused by the coal mining.

Summary

Measured against the standards of the International Labour Organization (ILO), the situation for employees remains catastrophic in many parts of the world. The more companies from industrialised countries shift their production to developing and emerging economies or collaborate with suppliers from these countries, the more directly they are confronted with the problems prevailing there. By no means all companies are facing up to this issue, as can be seen from the large number of companies which continue to breach recognised labour rights, either themselves or through their supply chains. As in the previous year, the electronics industry, which in recent years has shifted a huge proportion of its manufacturing to Asia, is particularly badly affected. China is a particular hotspot in respect of low labour standards. It is being said in the textile industry that production in China has already become too expensive and that companies are moving on to countries where wages – and also often social standards – are even lower. This will ensure the industry one of the “top spots” in the ranking of sectors with the highest number of labour rights violations, unless companies do some intensive work on rectifying injustices. Human rights violations, as in the previous year, are concentrated in a few sectors, the mining industry being the main culprit.

oekom's world map of human rights violations

The world map below gives an overview of human rights violations in which companies are involved recently recorded by oekom research. The map does not claim to be complete, but is intended to illustrate the possible substance and scale of relevant violations.



Selected cases of human rights violations relating to companies from the oekom Rating Universe; as of 2010-12-31; source: oekom research AG (2011)

1 **Guatemala**: inadequate compensation of the local population following relocation, as well as detrimental effect of company activities on people's livelihoods.

2 **Peru**: deaths and injuries following deployment of police and security forces during demonstrations against mining.

3 **Colombia**: threats made to inhabitants, forced relocation and inadequate compensation

4 **Brazil**: destruction of / damage to the livelihoods of indigenous peoples

5 **Brazil**: deaths and injuries among demonstrators following deployment of a security firm

6 **Brazil**: deaths following interventions by security staff

7 **Nigeria**: destruction of livelihoods through large-scale environmental pollution from oil production

8 **South Africa**: forced resettlement and inadequate compensation of local population, destruction of places of worship and graves

9 **Ghana**: use of force, threats to and intimidation of population, damage to livelihoods (arable land) coupled with inadequate compensation

10 **India**: violent clashes between pro- and anti-mining activists

11 **Indonesien**: mass intimidation and force used against the population by the military, supported/paid for by mining companies

12 **Papua New Guinea**: forced evictions and threats of violence, killings of illegal prospectors by security personnel

13 **Philippines**: mining industry profiting from intimidation and force (including killings) by military and guerrillas

2.3.4 Management of customer data

Although the protection of customer data is technically feasible, some companies are still reluctant to ensure such protection. As a result of the controversy raised about Google Street View, particularly in Germany, houses, faces and number plates have been pixelated. Similar processes are still denied to users of loyalty cards and Web 2.0. Their data can be used for personalised advertising by the service provider or sold without their knowledge to third parties.

Because on the one hand many people continue to treat their data rather carelessly, and on the other hand access to services, e.g. internet access and social platforms, is linked to the disclosure of personal data to the service provider, companies should set high standards for the collection and use of data. The following section looks at whether and to what extent this is currently being done in the retail and internet & software sectors.

Retail

The first customer loyalty card was introduced in Germany around 50 years ago in Stuttgart. Today, according to estimates by the consumer organization Stiftung Warentest, there are approximately 100 million loyalty cards in circulation in Germany alone, weighing down wallets to the tune of around 500 tonnes in total. From a purely statistical point of view, this means that every German household has over 2.5 cards, on which there is often a large amount of personal data stored. Companies give their customers loyalty cards so that they can retain them over the long term, analyse purchasing behaviour and build up customer profiles from the stored transaction data.

The highest scores in the oekom Corporate Rating went to companies which provided their customers with transparent information on what information they are collecting, why they are collecting it, whether and to whom they are passing the data on and how customers can view the data stored about them and where appropriate change it. Direct marketing based on the data collected should only be possible with the prior consent of the customer. Moreover, the company should have a person dealing with data protection issues whom customers can contact with queries. In order to prevent collected data ending up in the hands of unauthorised third parties, companies should, among other things, provide employee training on data protection and audit their respective management systems on a regular basis.

The Finnish company Kesko and the Swiss retail group Migros performed relatively well in the handling of customer data on loyalty cards. For example, Kesko enables users of its K-Plussa-Card to refuse permission for the analysis of their purchases at product level, thus preventing direct marketing. Customers can still enjoy the direct benefits of the loyalty card without data being collected when they shop. However, this means that they are no longer able to collect bonus points.

Kesko (FI)

Migros (CH)

Top companies in the management of customer data; as of 2010-12-31; source: oekom research AG (2011)

In addition, Kesko has implemented a comprehensive data protection management system intended to prevent customer data being “fished” by third parties, through a system of regular audits and employee training.

Migros gives customers the opportunity to access on the Internet all the information collected about them and where necessary to change or delete this. The M-CUMULUS bonus programme was awarded the Swiss Association for Quality and Management Systems‘ GoodPriv@cy data protection label. For example, via the CUMULUS information line, it is possible to revoke at any time consent to receive advertising mail which was given on registration.

Apart from these two positive examples, however, the overall efforts made by retail companies in this area leave a great deal of room for improvement.

oe-quote

“Using loyalty cards has become part of everyday life for many consumers. Busy collecting bonus points, they put concerns about data protection to the backs of their minds. However, the savings are generally very small, and the amount of stored data often unnecessarily large. Greater transparency toward customers and increased efforts to improve data protection are urgently required from retailers.“

Lisa Häuser, retail sector analyst at oekom research

Internet & Software

A wave of indignation swept over Google in 2010 when it became known that the company had “accidentally” not only taken photos of houses, but also, as it were in passing, collected user data, user IDs and even whole emails. Facebook has also come in for criticism for its handling of the data of its users, who now number over 500 million. The German Federal Minister for Consumer Protection, Ilse Aigner, deleted her profile from this Web 2.0 community as a protest against the company‘s practices. These are just two examples of the increasingly sensitive public reaction to the irresponsible handling of data, especially by the operators of internet sites.

In this sector, oekom research first evaluates the quality of relevant guidelines on handling personal customer data. We then examine how much data is stored and for how long, how much information customers receive about the purpose of the data storage and data processing, and whether customers are given the option of opting out, i.e. by refusing permission for their data to be passed on and used, or whether they have to opt in, i.e. grant permission for this, before their data can be used. We also analyse measures for implementing data protection guidelines, e.g. the designation of data protection managers, of physical security precautions for rooms containing data storage devices and of technical safeguards, so-called privacy-enhancing technologies (PET). Finally, we assess whether the information security management system (ISMS) is certified to a recognised standard, e.g. ISO 27001.

Generally, companies operating in the B2B segment do better here than companies with private customers such as e.g. Google and Microsoft. The Indian company Wipro and the two US companies Symantec und Unisys performed comparatively well overall.

Wipro has created an information security and compliance department to implement its strict data protection guidelines, and this department reports directly to the Chief Information Officer. In addition, Wipro’s information security management system is ISO 27001-certified throughout the company. The company conducts data protection audits both internally and at external sites to which customer data has been passed on.

Wipro (IN)

Symantec (US)

Unisys (US)

Top companies in the management of customer data; as of 2010-12-31; source: oekom research AG (2011)

Symantec publishes various versions of its data protection guidelines, each with varying levels of detail (layered privacy policy), so that customers can easily gain an overview of the most important content. To ensure compliance with its standards, Symantec has come up with extensive security precautions: physical (e.g. secure destruction of old storage media), technical (e.g. use of encoding technologies) and organisational (e.g. employee training). Unisys has also taken extensive technical security precautions for the protection of stored customer data, in order to prevent unauthorised access to customer data and to guard against its alteration or loss. The company revises its data protection guidelines at least once a year in order to adapt them to comply with the latest standards.

oe-Ton

“The bulk of internet and software companies have introduced appropriate guidelines and measures to take account of increased public interest in issues of data protection. However, there is still a need for improvement, especially in companies dealing directly with private customers, where guidelines on the scope and duration of data storage and processing are frequently incomplete or simply too lax.“

Karsten Greye, internet & software sector analyst at oekom research

2.3.5 Protecting the forests

The area of the world covered by forest is shrinking by an average of 15,000 hectares a day, primarily as a result of the conversion of forest into agricultural areas, illegal logging, which is estimated to account for 20-40 per cent of global timber production, and climate change. At the same time, demand for timber and wood products is rising in the wake of global population growth and a renaissance in the use of timber for fuel in industrialised countries.

Against this background, efforts to strengthen the protection afforded to forests and to promote the sustainable management of forests have been intensified in recent years. These include systems for certifying the sustainability of forests, such as that of the Forest Stewardship Council (FSC) and the Programme for the Endorsement of Forest Certification Schemes (PEFC). Traceability systems should also be mentioned here: they make it possible to trace the origin of timber back through the entire value chain.

It is incumbent on companies to take responsibility for the protection of forests. oekom research therefore factors in appropriate criteria when evaluating a whole range of industries, primarily in the paper and forest products sector, but also, for example, in the construction materials sector as well as in the media industry. All three sectors will be looked at below.

Further information on this topic can be found in the oekom Position Paper Forestry & Timber.

Paper & Forest

This sector comprises both companies which manage forests and/or plantations and also companies which manufacture cellulose and/or paper or cardboard products from wood. The latter group of companies generally also manage their own forests and/or plantations, thereby ensuring their access to the wood they need as a raw material. Additional wood is bought in, primarily from private or government-owned sources.

Requirements for companies in the paper and forestry industry relate principally to three areas:

- Sustainability guidelines: Companies should, among other things, commit themselves unequivocally not to use any timber (or wood products) from illegal or unknown sources. In addition, timber should not be procured from high conservation value forests and plantations should not be cultivated on areas which have been cleared of forest for this purpose. oekom research also gives a positive weighting to the exclusion of timber from genetically-modified trees, as well as to corporate strategies to increase the use of recycled timber and cellulose and to promote certification of a company's forests/plantations.
- Sustainable forest management: Measures to minimise the negative environmental and social impacts of the management of forests or plantations are rated positively. These include, for example, factoring in sustainability aspects when drawing up management plans by taking into consideration biodiversity criteria, water and soil protection and the use of pesticides. Furthermore, certification according to internationally recognised forest standards is also reflected positively in ratings. Particular value is attached here to FSC certification, which oekom research considers to be of high quality.
- Responsibility for the supply chain: In addition to guidelines on the exclusion of timber from controversial sources, oekom research takes a favourable view of companies which have implemented systems and measures for guaranteeing that timber is procured in compliance with these guidelines. These include, for example, timber traceability systems, training for employees working in purchasing and training for suppliers.

The Swedish paper manufacturers Holmen and SCA achieved good ratings for forest management. In 2009, Holmen had all its own forest areas FSC- and PEFC-certified. The company is taking extensive

Holmen (SE)

SCA (SE)

Companies with a good rating of forest management; as of 2010-12-31; source: oekom research AG (2011). The sector is currently in the update process, therefore corresponding ratings are not yet available for all companies.

sustainable forest management and biodiversity protection measures. These include, for example, leaving deadwood lying in the forest and cooperating with the relevant research institutes.

All SCA's forest areas are also FSC-certified and it too has implemented numerous measures to protect species diversity in the forests.

Both companies have taken steps with regard to the traceability of bought-in timber. Stora Enso from Finland received a very good rating here. The company has adopted comprehensive guidelines on sustainable procurement and implemented extensive systems for timber traceability and for collaboration with and monitoring of suppliers.

oe-quote

"Where the global protection of forests is concerned, the main focus of attention should be on preventing illegal overexploitation of forests and ensuring the sustainable management of forested regions worldwide."

Ellen Mayer, Senior Analyst at oekom research

Media

Although electronic newspapers and news "apps" are continuing to gain ground, printed products are still very important in the media sector. According to the Federation of German Newspaper Publishers (BDZV) in Europe alone 2,493 newspapers with a total circulation of at least 87 million copies are published every day. Worldwide, India and China are the largest newspaper markets, each with approximately 109 million copies sold daily. Even though in Germany, for example, newsprint today is manufactured from around 70 per cent recycled paper, worldwide demand in the media sector for wood for paper production remains high.

Against this background, oekom research assesses firstly whether media companies have adopted guidelines on paper procurement which specify clear rules on the provenance and environmental quality of the paper used. Secondly, we analyse what measures have been taken to ensure that suppliers implement the guidelines. These include, for example, audits of suppliers, training and the introduction of traceability systems. Finally, we assess the amount of recycled and certified paper as a proportion of the total amount of paper used.

The UK media company Pearson and the German publisher Axel Springer Verlag achieved the best scores according to these criteria. In its guidelines on paper procurement, Pearson pledges to increase the proportion of recycled paper and paper from sustainable forests and to avoid the use of paper from high conservation value forests.

Axel Springer also has sound guidelines on paper procurement and is working with its suppliers to improve traceability in the supply chain.

Pearson (UK)

Axel Springer (DE)

Top companies in the paper procurement; as of 2010-12-31; source: oekom research AG (2011)

Construction

It is estimated that the construction industry is responsible for 30 per cent of global demand for raw materials and 70 per cent of the demand for timber. The factoring of sustainability criteria into the procurement of relevant materials is therefore very important in this sector. Where the use of timber is concerned, oekom research expects companies rigorously to exclude the use of timber from primary forests. A study by the environmental NGO Friends of the Earth Netherlands showed that illegally felled timber is in evidence even in EU projects, principally of the species red maranti (Indonesia, Malaysia), ipé (Central and South America), spruce (boreal primary forests of Russia and Baltic states) and azobé (West Africa). A sustainable procurement policy should also, as far as possible, give preference to GM-free, organically farmed products.

The top scores in the oekom Corporate Rating were achieved by companies which in their internal company guidelines pledged both to refrain from procuring timber from primary forests and illegal logging and to use timber from (certified) sustainable forestry. The rating also takes account of the proportion of the timber used that comes from forests certified by the FSC or another certification body, although oekom research views FSC certification as being particularly reliable.

The two UK construction companies Taylor Wimpey and Balfour Beatty are currently the top performers in this area. Taylor Wimpey undertakes in its procurement guidelines to buy timber exclusively from legal and certified (FSC or PEFC) sources. At the same time, negative impacts of procurement on biodiversity are to be minimised. According to the company, 100 per cent of the timber used comes from sustainable sources.

Balfour Beatty, too, stresses the importance of procuring timber from sustainable sources. In 2009, according to the company's own data, 89 per cent of the timber it used came from certified sources, with 67 per cent being from FSC-certified forests. Although it has no formal guidelines in place, the construction company Hochtief showed that the timber used in its construction projects comes exclusively from FSC-certified sources.

- **Taylor Wimpey (UK)**
- **Balfour Beatty (UK)**

Top companies in the rating of procurement guidelines of timber from sustainable sources; as of 2010-12-31; source: oekom research AG (2011)

oe-quote

"Timber is a raw material fundamental to sustainable construction, as it contributes to climate protection, e.g. through long-term retention of CO_2, and has a low primary energy consumption. However, it is essential to ensure that the timber originates from sustainable forestry. Here, as in other areas of sustainable construction, the large construction companies have a considerable amount of catching up to do."

Frauke Demuth, construction materials sector analyst at oekom research

2.3.6 Digging deeper: a follow-up on the oekom Corporate Responsibility Review 2010

In this section, we will re-examine specific developments in some of the areas we analysed in the oekom Corporate Responsibility Review 2010. This overview makes no claim to be exhaustive.

Water: UN declares clean water a human right

The United Nations (UN) has included entitlement to clean water in its Universal Declaration of Human Rights. The General Assembly of 192 member states approved by a majority a resolution to this effect. The resolution was put forward by Bolivia and supported by 33 other countries. In the resolution, the General Assembly voiced its concern about the fact that an estimated 884 million people worldwide have no access to clean drinking water. Over 2.6 billion people have no access to sanitary facilities.

However, the Declaration of Human Rights and thus also the entitlement to clean water are not binding under international law. The right to water is not enforceable even in the signatory countries, which all 192 UN members automatically become upon accession. Nonetheless, its inclusion has a high symbolic value and consequently also influences the policies of countries and of the United Nations.

Biodiversity: TEEB publishes final report

The final report of the Economics of Ecosystems and Biodiversity (TEEB) project was presented at the 10th Conference of the Parties to the UN Convention on Biological Diversity in October 2010 in Nagoya, Japan.

TEEB is to biodiversity as the Stern Report was to climate change. The study evaluates the economic benefits of ecosystem services. The study uses analyses from over 200 individual studies to demonstrate the value of natural services and how these could be factored into policy and business decision-making.

Source: www.teebweb.org

TEEB's final report, "Mainstreaming the Economics of Nature", calls for the wider recognition of nature's contribution to human livelihoods, health, security and culture by decision-makers at all levels – not only in politics, but also by businesses and ordinary citizens. The authors of the study recommend that changes in the value of natural capital and ecosystem services be recorded in national accounting systems and that external effects on the environment be documented in companies' annual reports and accounts.

Climate: 2010 – The Year of Natural Disasters

According to Munich Re, 2010 was marked out by a particularly large number of natural disasters. Overall, the German reinsurance company recorded 950 natural disasters, 90 per cent of these being weather-related and in many cases also climate-related events such as storms and floods. This made 2010 the year with the second-highest number of natural disasters since 1980. According to Munich Re's calculations, the number was also significantly higher than the average for the previous ten years of 785 events a year. The total economic losses amounted to approximately 130 billion US dollars, of which 37 billion US dollars were insured. This meant that the year was one of the six with the heaviest losses for the insurance industry since 1980. The total economic losses were somewhat above the already high average for the last ten years.

The weather-related natural disasters included two events which, based on the UN's definition, fall into the highest category of major disasters: the floods in Pakistan following extreme monsoon rainfall in summer 2010 and the heatwave in Russia and neighbouring countries between July and September 2010. The latter had the highest death toll of any natural disaster in the history of Russia, with at least 56,000 people dying from the consequences of heat and air pollution.

2.4 Outlook: Sherpas and Scouts

At the end of 2010, the German Council for Sustainable Development initiated a dialogue on drawing up a Sustainability Code for Germany, which is intended to form a binding framework for sustainability rating on the financial markets. The aim of the Code, according to the initiators, is to "strengthen business models, provide guidance, make sustainability tangible and make the requirements in terms of content transparent."

This venture can be seen as an indication that both the issue of sustainability and the sustainable capital market have increased in importance, which supports the optimistic forecasts made in the 2010 oekom Corporate Responsibility Review. The idea that the German Sustainability Code should have the same significance as the German Corporate Governance Code and that companies should have to furnish relevant reports annually is a very appealing one. With sustainability anchored in German company law in this way, the notorious sceptics would have far fewer opportunities to argue against the necessity of integrating sustainability criteria into management systems. At the same time, this is not the first initiative to achieve standardisation of sustainability criteria. The development of key performance indicators (KPI) by the Society of Investment Professionals in Germany (DVFA) and the US "Global Initiative on Sustainability Ratings" are along much the same lines.

As understandable as the desire for uniformity and standardisation is, it can either apply only to a core set of criteria or must be carried out on a highly aggregated level. In any event, it cannot be associated with any claim to a complete listing of all relevant sustainability criteria, as sustainability challenges in the various sectors differ widely and sustainability-oriented investors often have very specific views. A German Sustainability Code is therefore – like the other KPI initiatives – a valuable addition to the existing concepts, but cannot replace a comprehensive and detailed sustainability rating that is tailored to the needs of the individual investor.

It is no weakness, but rather a strength of the concept of sustainability that it invites social discourse and evolves through the participation of relevant social groups, including sustainability-oriented investors. Sustainability, interpreted in this way, can tolerate the multiplicity of initiatives and the competition between them. What is important, however, is transparency about how the individual players define sustainability for themselves and – in the case of sustainability rating agencies – measure and evaluate this. The European agencies, under the umbrella of the Association for Independent Corporate Sustainability and Responsibility Research (AI CSRR) and by defining a strict quality standard, have done their homework here.

The transparency of the criteria is also, incidentally, what makes it possible for the agencies to stimulate greater sustainability in companies, which is, of course, a fundamental aim of sustainable investment. In companies which are open to the SRI market and have experience of sustainability ratings, it has become increasingly clear that there are three main functions of sustainability rating agencies from which they benefit:

Sustainability rating agencies as sherpas

CSR departments often perceive sustainability rating agencies as "allies". External enquiries from agencies with a foot in the capital market help to promote decisions on a company's sustainability strategy and serve as catalysts for internal decision-making processes. A sustainability rating serves (often at no cost to the company) as a strengths/weaknesses analysis of the company's sustainability management system and thus forms a sound basis for its further development.

Sustainability rating agencies as scouts

The agencies' criteria reflect both the expectations of the relevant company stakeholders and new issues which could become relevant to the companies in future. Sustainability rating agencies thus function both as issue scouts and as negotiators between the companies and their stakeholders, particularly sustainable investors.

Sustainability rating agencies as motivators

Good sustainability ratings are increasingly being highlighted by companies in their external communications. Overviews of this kind can be found in a growing number of sustainability and business reports, and their mention in newspapers advertisements is no longer uncommon. Ratings thus make a positive contribution to the positioning and reputation of companies. They can improve the motivation of employees and the position of a company in the oft-quoted "war for talents". This is, incidentally, completely in keeping with the best-in-class approach, which is intended to generate continuous competition within a sector to produce the best sustainability performance.

This influence on companies brings with it responsibilities which must be reflected in high standards for the work of sustainability rating agencies. These include, in particular, the previously mentioned high degree of transparency about criteria, methods and processes plus as great a degree as possible of independence, which oekom research believes must be reflected in a clear separation of rating and advice and in a business model where the rating is paid for not by the issuer, but by the sustainability-oriented investor as the user of the information.

The relationship between companies and sustainability rating agencies – as far as oekom research is able to judge – is good. This is evident from the further increase in the already high level of participation in the rating process by companies and the intensification of contact in the form of telephone conferences and visits. However, it could be even better, given greater mutual understanding of each other's motives and circumstances.

oekom inside

oekom research AG is one of the world's leading rating agencies. Since 1993, oekom research has actively helped to shape the market for sustainable investments. Our research universe comprises the world's major companies and countries. On this basis we offer a comprehensive package of research services for the integration of ethical, social and environmental aspects in the investment management of our clients. In 2009, despite the incipient financial crisis, we were able to continue to extend our customer base to include over 70 asset managers and institutional investors from eight countries. We provide research for assets totaling more than 90 billion euros.

Key to the success of oekom research AG is the credibility of our analyses. In order to guarantee this, there are in our view two particular aspects that are of crucial importance: independence – both at agency and at analyst level – and a sophisticated quality management system. In both these areas, oekom has followed a consistent path since its founding in 1993 and has put appropriate standards in place on various levels. For example, we do not permit any companies which we evaluate, nor any financial market players, to be shareholders in oekom. We also consciously refrain from providing any form of consultancy to the companies which we evaluate.

With regard to the quality of our rating processes, the market has for years acknowledged our leading position over our competitors. Nonetheless, over the last year we have subjected our rating system to a detailed audit by external auditors of our compliance with the internationally recognised quality standard CSRR-QS 2.1 of the Association for Independent Corporate Sustainability and Responsibility Research (➔ www.csrr-qs.org).

At the moment the interdisciplinary team of oekom research consists of 39 members.

In all our activities, we try to put the basic principles of corporate responsibility into practice, especially in the way we treat our employees as an employer, and in the way we treat our clients and competitors as a market participant. We take appropriate measures to minimise the load on the environment which our business activities give rise to.

Referencen

Institutional investors:

- Deutsche Bundesstiftung Umwelt
- Diocese Linz
- Diocese Rottenburg-Stuttgart
- ERAFP
- Evangelical Lutheran Church in Bavaria
- Foundation EVZ
- MAIF
- Missionszentrale der Franziskaner
- Munich Re
- Novartis Pension Fund
- Religious Orders
- VBV Pensionskasse

Financial services companies:

- AGICAM
- Allianz Global Investors France
- AmpegaGerling Investment
- Amundi Asset Management
- Baden-Württembergische Bank
- Bank für Orden und Mission
- Bank für Sozialwirtschaft
- Bankhaus Jungholz
- Bankhaus Schelhammer & Schattera
- BankInvest Group
- Bank Vontobel
- BayernInvest
- BNP Paribas Asset Management
- BÖAG – Börsen AG Hamburg/Hannover
- CM-CIC Asset Management
- Daiwa Asset Management
- DekaBank
- Deutsche Bank
- DJE Kapital
- DZ Bank
- Erste Sparinvest
- European Investors
- Evangelische Darlehnsgenossenschaft
- GLS Gemeinschaftsbank
- Groupama Asset Management
- Hamburger Sparkasse
- HSBC Global Asset Management
- HypoVereinsbank
- Kaiser, Ritter, Partner
- KD-Bank
- Kepler Fonds
- Landesbank Baden-Württemberg
- LBBW Asset Management
- LIGA Bank
- MEAG
- Metzler
- Metzler Asset Management
- Natixis Asset Management
- NordLB Kapitalanlagegesellschaft
- ÖkoWorld Lux
- Pioneer Investments
- Proventus
- quirin bank
- Raiffeisen Capital Management
- Sal. Oppenheim
- Schwyzer Kantonalbank
- SEB Invest
- sks Vermögensverwaltung
- Sparkasse Oberösterreich
- Steyler Bank
- Umweltbank
- Unicredit
- VINIS
- VKB-Bank
- Wilhelm von Finck

Methodology

In order to be able to analyse comprehensively the diverse environmental and social challenges relating to the activities of companies, oekom research AG has developed a pool of indicators. These currently number approximately 500. For each company, an average of 100 indicators are selected from this pool on an industry-specific basis so that a targeted evaluation of the problems specific to that company can be carried out.

To build up a comprehensive picture of each company, our analysts collect the information relevant to the rating both from the companies being analysed and from independent experts. The work of oekom research's analysts is supported by a network of international experts from the fields of sustainability, human rights, employment rights and consumer protection:

- evaluation of company documentation such as annual and sustainability reports;
- interviews with company representatives;
- media screening;
- interviews with independent experts;
- assessments from independent specialists from NGOs, governmental and public institutions, business associations, research institutes, consumer protection groups etc.

The overall analysis is graded on a twelve-point scale from A+ (extraordinary performance) to D- (little engagement). oekom research awards Prime Status to those companies which according to the oekom Corporate Rating are among the leaders in their industry and which meet industry-specific minimum requirements (best-in-class approach).

Corporate Responsibility Prime
rated by oekom research

Comments to the rating

„To Cemig, the oekom's questionnaire is one of the most important tools of internal management in relation to sustainability. The advantage of oekom in relation to other questionnaires is that we receive the rating and comments in each question."

Arlindo Porto Neto, Vice-President, Cemig

"oekom research has been selected by OMV as one of the rating agencies with whom we work actively together. The reason for this is that oekom research's ratings are highly regarded in the SRI investment field and, in addition, we are impressed by the transparency and objectivity of the rating process. Its dialogue and feedback mechanisms operate very well. Last but not least, the rating also provides us with a benchmarking and issue management tool for finding out what our stakeholders expect from the group and for closing any gaps that might exist."

Simone Alaya, Stakeholder Management, OMV

„We value the opportunity to enter into dialogue. Some rating agencies won't do this so we now are very selective about who we invest our time with in the SRI rating world."

Noel Morrin, Senior Vice President Sustainability, Skanska AB

Glossary

Best-in-class approach

Under the best-in-class approach, the best companies in an industry are selected for investment, best here being defined as particularly committed to social and environmental matters. A distinction can be made between the relative and the absolute best-in-class approaches. Under the relative approach, a set percentage of the best companies in an industry are selected, irrespective of their effective sustainability performance, for example, always the top 20 per cent. Under the absolute approach a minimum threshold is also taken into account and only companies which satisfy these minimum requirements can be best-in-class.

CSR

Corporate Social Responsibility; including social and environmental aspects.

Engagement

Also: active shareholding, approach which is widespread particularly in the Anglo-American world, in which investors attempt through direct dialogue with companies to rectify grievances about the companies' social and environmental performance. This approach is now also gaining in momentum in continental Europe.

ESG

This abbreviation stands for Environmental (E), Social (S) and Governance (G) and describes three dimensions of sustainability that are routinely integrated into sustainability ratings and sustainable capital investments.

Exclusionary criteria

Approach, common among sustainability investors, whereby companies which are active in certain areas of business (e.g. relating to alcohol, pornography, military or tobacco) or which attract attention through controversial business behaviour (e.g. human rights and labour rights violations), are excluded from investment.

Materiality

The financial relevance of individual environmental and social criteria and of the sustainability concept as a whole is examined under the heading of "materiality". There continues to be the widely held preconception that sustainable investors have to make do with lower yields than conventional investors. However, numerous studies have provided evidence that sustainable investments exhibit no systematic disadvantage in terms of yield, and some studies even see a yield advantage in such investments.

SRI

Socially Responsible Investment.

UN PRI

The United Nations Principles for Responsible Investment (UN PRI) comprise six principles for sustainable investment. Signatories to the UN PRI undertake to implement these principles in their capital investment.

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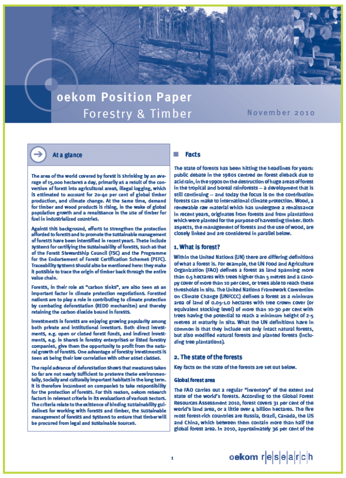
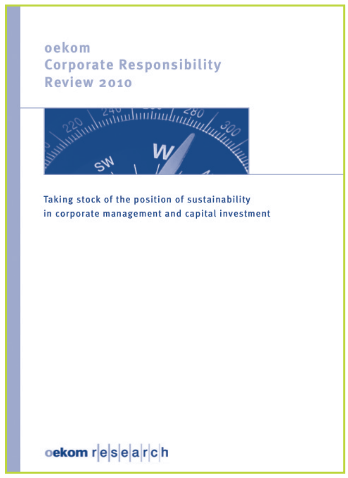
Publications

The following publications have been published by oekom research in 2010, some in cooperation with partners. All publications are available at oekom research on request.

oekom Position Paper Emission Trading (8/2010)



oekom Position Paper Forestry & Timber (11/2010)



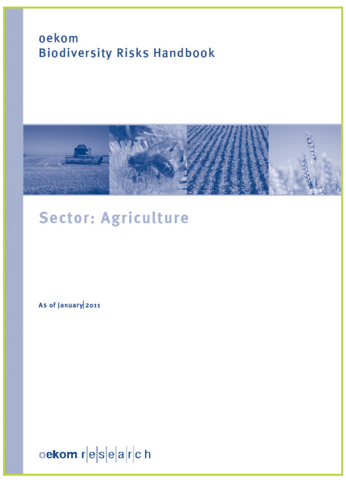
oekom Corporate Responsibility Review 2010 (3/2010)

oekom Industry Focus Insurance (7/2010)

oekom Industry Focus Metals & Mining (9/2010)

Further Industry Focus' have been published in 2010 to the following sectors:

- Automobile
- Development Banks
- Food & Beverages
- Health Care Equipment & Supplies
- Internet & Software
- Machinery
- Oil & Gas
- Public & Regional Banks
- Real Estate



oekom Biodiversity Risks Handbook (10/2010)

Video clip:
„How your money works“
at: www.bewusst-investieren.de

in cooperation with Green City Energy

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