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UNEP **Finance Initiative**
Innovative financing for sustainability

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Australasian UNEP Finance Initiative

Newsletter

'Innovative financing for sustainability'

Contents

Integrating sustainability at mecu

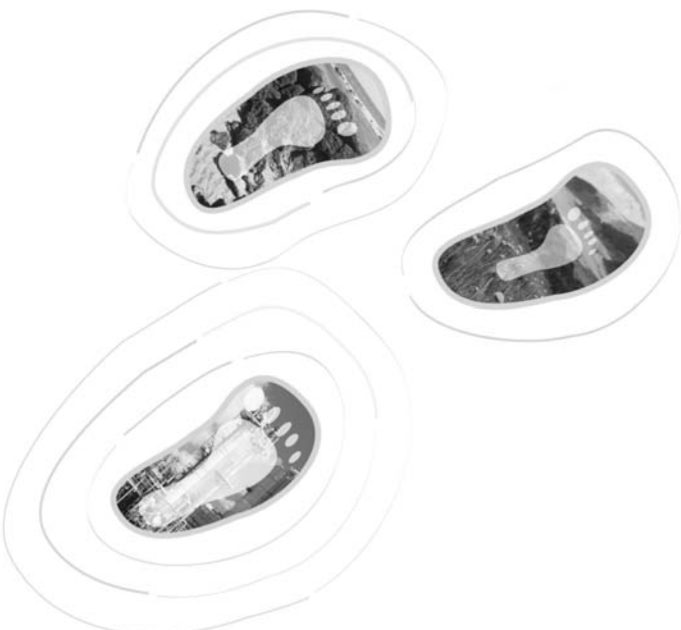
Rowan Dowland, **mecu**

mecu, Victoria's largest Credit Union, aims to become the pre-eminent socially responsible banking brand in Australia. To facilitate this goal becoming reality, **mecu**'s *Sustainable Business Strategy* is being integrated in all areas of its business.

mecu recognises the need for a broader measure of business progress and common prosperity than economic growth alone and is going about the task of integrating financial performance with human and social capital and ecological sustainability.

The **mecu** Board is charged with the responsibility of directing and monitoring implementation of the *Sustainable Business Strategy* across the organisation.

The executive team are responsible for leading **mecu**'s approach to sustainability. *Footprints*, a cross-functional staff sustainability group is responsible for identifying opportunities to innovate in a sustainable way and for engaging employees across the business in **mecu**'s *Sustainable Business Strategy*.



mecu has formalised its commitment to sustainability by signing the UNEP Statement by Financial Institutions on Sustainable Development and the Environment. **mecu** has also developed a

Sustainability Covenant, with EPA Victoria. The objectives of the Covenant, which identify some 40 sustainability initiatives in its first year are to:

- Increase the efficiency with which **mecu** uses resources to develop and deliver its products and services;
- Help to alleviate negative environmental and social impacts through **mecu**'s products and services;
- Encourage and assist **mecu** members to live more sustainable lives;
- Apply prudent financial business practices to operations, to ensure economic and financial sustainability; and
- Support developments within the finance sector that encourage others to embrace sustainability.

mecu recognises that its major environmental and social impacts are those caused by the activities it supports through its products. Accordingly **mecu** products are being redesigned so that they contribute towards a responsible and sustainable society.

Following the launch of its goGreen® Car Loan, which offers interest rate incentives to people to purchase environmentally efficient vehicles and offsets 100 per cent of the CO_2 emissions produced by the cars it finances, **mecu** continues to innovate in the area of personal banking products.

The underlying principle upon which **mecu** is developing its sustainable banking product range is that products must be mainstream. Core banking products are redesigned to include environmental and social features. So-called 'green' products are not added to the **mecu** product range as a separate product line thereby reducing potential consumer trade-off decisions in their purchase evaluation process.

The **mecu** standard home loan product was redesigned in 2004 to include the following socially and environmentally responsible features:

- Interest rate incentives for borrowers to retrofit their homes with water and energy conservation technology;
- Parental leave loan repayment pause; and
- Free loan protection insurance, which automatically pays out the loan or pays $120,000 off the outstanding balance of a loan on the death of a borrower.

mecu's VISA Credit Card is yet another example of aligning sustainability principles with mainstream banking products. The card is the only product to offer consumers a 100 per cent 'No Marketing Promise'. This feature means that **mecu** promises never to offer incentives to cardholders in an effort to increase their level of indebtedness. Nor will **mecu** ever make unsolicited pre-approved credit limit offers to cardholders. This feature is an illustration of **mecu**'s responsible lending practices and its desire to see people better manage their levels of personal debt. Furthermore the VISA Credit Card is produced from the more environmentally friendly chlorine free PETG plastic.

Sharing success with its shareholding members is a priority for **mecu**.

In 2005 **mecu** published its first Sustainability Report based on the Global Reporting Initiative's Sustainability Reporting Guidelines 2002, making it one of a very small number of Australian SMEs to publish a report.

In the year ending 30th June 2005 **mecu** reported a net profit after tax of $12.3million, representing an increase of 22.4 per cent compared to its 2004 result. Shareholding member's funds grew to $128.2million, an increase of 11.8 per cent since 2004.

Customer satisfaction levels have increased from 93 per cent in January 2003 to 95 per cent in December 2004. At the same time external research conducted amongst **mecu** staff in 2005 indicated their strong support of the Sustainable Business Strategy.

mecu believes that environment and social issues offer a set of strategic business opportunities. It believes there are benefits in aligning its business with those forces moving society in a more sustainable direction, which are also consistent with its own long held socially responsible values.

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Bendigo Bank to offset carbon emissions

Leigh Watkins, Bendigo Bank

Bendigo Bank will offset its vehicle fleet greenhouse gas emissions through an innovative program to restore native vegetation in central Victorian water catchments.

In November 2005, the Bank announced it had signed an historic agreement with Greenhouse Balanced, a Central Victorian company offering services in reforestation and carbon sequestration.

The agreement focuses on the provision of 1700 tonnes of carbon dioxide equivalent in a newly established native vegetation plantation, with carbon sequestered (absorbed) by the plantation to help to offset the emissions from the Bank's 300-strong national vehicle fleet.

But rather than a typical monoculture approach (such as pines or bluegum), the Greenhouse Balanced plantation is designed to replicate as closely as possibly the vegetation that would have existed pre-1750. This will provide salinity, water quality, biodiversity and habitat benefits.

Bendigo Bank and Greenhouse Balanced have developed this approach to establish an 'ecological credit' as an alternative to the commonly traded carbon credits that only address carbon emissions.

In consultation with the North Central Catchment Authority, the first plantation has been established on privately owned land at Lockwood, just south of Bendigo.

The partnership with Greenhouse Balanced reflected the bank's environmental strategy and would provide benefits for the regional community.

Bendigo Bank is focusing over the next 10 years on minimising its impact on the environment and this has been demonstrated in the low energy new head office building soon to be built in Bendigo, in its energy efficiency programs across the Bendigo Group, and in its Green Loans offering incentives for sustainable housing.

Bendigo Bank believes purchasing carbon offsets is a natural next step as it demonstrates the bank's willingness to take responsibility for its emissions. This plantation will also provide many additional environmental benefits and will allow the bank to pioneer the development of a market for carbon credits in central Victoria.

Greenhouse Balanced has facilitated the project and will oversee the transaction of carbon to the Bendigo Bank. There is potential for more deals of this kind for the region.

Greenhouse Balanced is a company seeking to help companies such as Bendigo Bank in offsetting their emissions and projects like this one have great flow-on benefits for the environment and for the protection of agricultural lands in the region.

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For more information on Greenhouse Balanced, please go to:
www.greenhousebalanced.com

Encouraging solar hot water at Savings & Loans Credit Union

Lisa Kristan, Savings & Loans Credit Union

When Savings & Loans made the commitment to take a leadership stance on environmental issues, it wanted to offer practical solutions and not just rhetoric.

This led to the development of the *Breathe Easy* range of products, a collection of loans with lower interest rates available for members who make environmentally responsible purchases.

The latest product in the range is the *Breathe Easy Solar Hot Water Loan*, which provides discounts to encourage people to purchase solar hot water systems.

Savings & Loans provides a low interest rate loan with flexible repayment options for the purchase of a solar hot water unit with the South Australian Government offering a rebate on the installation of the system.

An additional feature of the *Breathe Easy Solar Loan* is that members can only make electronic repayments – the most environmentally friendly method.

Using a solar hot water system can save up to 80 per cent of a household's total water heating costs and reduce the emissions of carbon dioxide by approximately three tonnes per year, the equivalent to taking a small car off the road.

Savings & Loans Chief Executive Officer, Greg Connor, said the *Breathe Easy* product range encourages people to give real consideration to environmentally friendly selections.

“Combining the enormous environmental benefits with the substantial financial savings provides a real win-win,” he said.

“Savings & Loans is committed to environmental, social and economic sustainability – the *Breathe Easy Solar Hot Water Loan* allows us to encourage others to help themselves and the environment.

“If we all do our bit, from government to big business to the individual, collectively we make a positive difference to our lives and to the future of our planet.”

The first of the *Breathe Easy* products was the *Breathe Easy Car Loan*, which recently passed $2 million in sales, a significant achievement for one of Australia's first 'green loans'.

The loan offers a reduced interest rate for the purchase of any new or demo car models (less than 1000km) that use seven litres or less of fuel per 100km, or any LPG-run new cars or demo models.

“As an organisation, we want to do everything we can to ensure we are creating a balance between the needs of our business and the needs of the environment,” CEO Greg Connor said.

“The *Breathe Easy Car Loan* isn't our highest selling product, but this milestone demonstrates an evolving mindset in the community about environmental issues. We are extremely pleased to be leading this change.

“The unique feature of this loan is we not only encourage people to make environmentally friendly vehicle choices, but we reward them for doing so by offering a reduced interest rate,” he said.

“The feedback from members who have taken a *Breathe Easy* loan has been very positive. They are delighted we can offer them an opportunity to make a product selection that benefits the environment and saves them money at the same time.”

In addition to the *Breathe Easy* product range, Savings & Loans has implemented other initiatives to demonstrate its environmental commitment.

These include joining the Carbon Neutral Program (CNP), which offsets the carbon emissions of its vehicle fleet by planting almost 900 trees in environmentally degraded areas of Australia. The trees will be maintained for 30 years in order to correctly balance the emissions of the vehicle fleet.

Additionally, Savings & Loans became the first South Australian based organisation to participate in the United Nations Environment Program Finance Initiative (UNEP FI).

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Shorts

Canada Pension Plan – Policy for Responsible Investment

The Canada Pension Plan (CPP) is one of the largest institutional investors in Canada with assets of C$92 billion expected to grow to C$190 billion in the next decade. It serves the retirement interests of approximately 16 million contributors and beneficiaries. In October 2005, it published its updated Policy for Responsible Investment (PRI), in which it reiterates its commitment to encouraging companies to adopt policies and practices that enhance long-term corporate financial performance. The Policy also outlines its strong belief that responsible corporate behaviour, with respect to environmental, social and governance factors, can generally have a positive influence on long-term financial performance.

To view the CPP's Policy for Responsible Investment, go to:
www.cppib.ca/how/social/index.html

Goldman Sachs Environmental Policy

Goldman Sachs, the leading global investment banking, securities and investment management firm, released its first environmental policy in November 2005. Commitments in the policy include working to ensure that its people, capital and ideas are used to help find effective market-based solutions to address climate change, ecosystem degradation and other critical environmental issues, and to seek to create new business opportunities that benefit the environment. This incorporates making up to $1 billion available to invest in renewable energy and energy efficiency projects.

The company will also work to making environmental, social and governance criteria a part of best-in-class investment research.

To download Goldman Sachs' environmental policy, go to:
www.gs.com/our_firm/our_culture/social_responsibility/environmental_policy_framework/index.html

Allianz Group sustainability research

Following research undertaken with WWF, Allianz, the German headquartered financial services provider, has commissioned a group-wide task force to systematically examine climate change related risks and opportunities in its business operations across all business lines. The task force will act as a 'Centre of Competence' for the Board of Management and the business lines, and will cover all possible issues such as assessing the insurability of wind energy producers and introducing risk assessment tools like flood zoning and natural catastrophe modelling.

To view the study undertaken by Allianz and WWF as well as other Allianz sustainability research reports, go to:
www.allianz.com/azcom/dp/cda/0,,917559-44,00.html

New Sustainability Reports

A number of UNEP FI signatory organisations have released reports in 2005 that outline their sustainability performance over the last year. The following details those that have done so, the title of the report and where each report can be found on the Internet.

(Reports marked * are Annual Reports that include substantial discussion of sustainability issues)

In Australia:

ANZ Banking Group – Corporate Responsibility Report 2005, *When people are inspired*
www.anz.com/aus/promo/CorporateResponsibility/default.asp

Insurance Australia Group – Sustainability Report 2005, *It's just good business*
www.iag.com.au/pub/iag/sustainability/publications/report/2005/index.shtml

mecu – 2005 Sustainability Report
www.mecu.com.au

National Australia Bank – Corporate Social Responsibility Report 2005, *Our principles in practice*
www.nabgroup.com/0,,76539,00.html

*Savings & Loans Credit Union – Annual Report 2005
www.savingsloans.com.au/library/2005_AR.pdf

VicSuper – Sustainability Report 2005, *Building a sustainable super fund*.
www.vicsuper.com.au/resources/documents/Sustainability_Report_20051.pdf

Westpac 2005 Stakeholder Impact Report, *Sustainable Value...*
www.westpac.com.au/internet/publish.nsf/Content/WICROR+2005+Stakeholder+Impact+Report

Internationally:

ABN Amro
www.abnamro.com/com/about/sd/sd.jsp

Aviva
www.aviva.com/csr05/index.asp

AXA
www.axa.com/lib/en/uploads/acr/group/AXA_Activity_Report_2004.pdf

Bank Sarasin
www.sarasin.ch/sarasin/show/main/public/1,1015,1000301-0-1,FF.html

Bank of Tokyo-Mitsubishi
www.bk.mufg.jp/english/society/reporting.html

Barclays
www.newsroom.barclays.co.uk/imagelibrary/detail.asp?MediaDetailsID=4418

Co-operative Financial Services
www.cfs.co.uk/sustainability2004

Development Bank of Japan
www.dbj.go.jp/english/environment/index_2005.html

FMO (The Netherlands Development Finance Company)
www.fmo.nl/downloadPub.php?taal=en&bestandsnaam=FMOSustainabiltyReport-2004

HSBC
www.investis.com/reports/hsbc_csrr_2004_en/report.php?type=1&page=1

Japan Bank for International Cooperation
www.jbic.go.jp/english/environ/report/2005/index.php

Sompo Japan Insurance
www.sompo-japan.co.jp/english/engl091.html

Standard Chartered
www.standardchartered.com/corporateresponsibility/site/index.htm

The Co-operative Group
www.co-op.co.uk/csr2004

The Royal Bank of Scotland Group
www.rbs.com/crreports

WestLB
www.westlb.de/cms/sitecontent/westlb/ui/en/Sustainability/at/bericht.-bin.acq/qual-SingleAttachment.Single.AttachmentAttachmentFile/Sustainability_Report.pdf

The Carbon Disclosure Project: CDP4 expands in Australia and New Zealand

Joanne Saleeba, Investor Group on Climate Change Australia/New Zealand

The Carbon Disclosure Project (CDP) is a global initiative seeking investment related information from companies worldwide. The 2005 information request, was made by the CDP secretariat on behalf of 155 institutional investors, with more than $21 trillion in assets under management, who are concerned with the shareholder value implications of climate change.

This third request by the CDP (known as CDP3) was for a range of information from FT500 companies, including the companies' approach to climate change, the quantity and intensity of their emissions and any emissions reduction programs in place.

The responses to CDP3 indicated that 86 per cent of the responding 354 companies had allocated management responsibility for climate change. A total of 80 per cent of companies had also begun to publicly disclose their emissions data. However, the responses also found that less than 50 of the FT500 companies had actually achieved a reduction in their GHG emissions. A copy of the full CDP3 report, an executive summary, analysis and the questionnaire are all publicly available.

At the Australian launch of the CDP3, in October 2005, the Investor Group on Climate Change (IGCC) announced that it had signed a Memorandum of Understanding with the CDP secretariat to expand the CDP information request within Australia and New Zealand in 2006.

Garrie Lette (Mercer Investment Consulting), Sam Mostyn (IAG), The Hon. John Thwaites (Deputy Premier and Victorian Minister for Environment), Paul Dickinson (CDP Coordinator), Bob Welsh (Chair, IGCC)

As at January 2006, the IGCC represents Australian investors, with total funds under management of over $155 billion, including

- AMP Capital Investors
- BT Financial Group
- Babcock & Brown Environmental Investments Ltd
- Catholic Superannuation Fund
- Five Oceans Asset Management
- H.E.S.T Australia
- General Property Trust
- Colonial First State Property
- VicSuper

The IGCC aims to ensure that the risks and opportunities associated with climate change are incorporated into investment decisions for the ultimate benefit of individual investors through:

- Raising awareness of the potential impacts, both positive and negative, resulting from climate change to the investment industry, corporate, government and community sectors;
- Encouraging best practices approaches to facilitate the inclusion of the impacts of climate change into investment analysis by the investment industry; and
- Providing information to assist the investment industry to understand and incorporate climate change into the investment decision.

The IGCC supports the disclosure from Australian and New Zealand listed companies of investment related information on climate change including data on emissions, reduction targets, climate change preparedness and business innovation in a carbon-constrained economy. The IGCC see the CDP information request as integral to the IGCC's overall objectives.

In February 2006 the ASX100 and NZ50 companies were asked to also complete the CDP information request. The responses will then form the basis of the Australia/New Zealand CDP4 Report.

Australian signatories to this year's CDP information request (CDP 4) include VicSuper, HESTA Super Fund, Catholic Superannuation Fund, AMP Capital Investors, BT Financial Group and Portfolio Partners.

To access the full CDP3 report please visit:
www.cdproject.net/report.asp

Further information on the IGCC can be located at:
www.igcc.org.au
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Employer of Choice and Corporate Social Responsibility at Aviva Australia

Rob Gill, CSR Manager, Aviva Australia

Being an employer of choice and offering a comprehensive corporate social (CSR) responsibility program are inextricably intertwined for a modern Australian business. To explain these terms simply, corporate social responsibility can be viewed as the external reporting of an organisation's operations that address its responsible policies and practices.

An employer of choice program is the internal policies and practices that the organisation employs to manage corporate responsibility.

An employer of choice program is essentially the 'cause', while being corporately and socially responsible is the 'effect'.

Aviva Australia has intensified its focus on addressing the link between employer of choice and CSR. Throughout 2005, Aviva continued its dedicated measurement and reporting on environmental, social, community and financial performance. The results were not only communicated to external stakeholders via media releases and reports, but also were directed internally for staff appraisal through information sessions, internal newsletters, all-staff emails and the intranet. Staff were encouraged to provide feedback, comments and voluntarily become part of the ongoing development of Aviva's CSR program through staff surveys, briefing sessions and regular e-communication.

Staff are the key to Aviva's business operations. Aviva strongly believes that developing its employer of choice program in parallel with its CSR program enables people to share in ownership for corporate responsibility. So far, the feedback from Aviva's team regarding its CSR initiatives and employee opportunities has been very positive. This is reflected in its employee opinion survey, where 71 per cent rated Aviva as a good, or above, employer.

Aviva Australia is aware of the strong relationship between an effective community and sustainability program and a committed internal employer of choice program. Without support and enthusiasm from its staff, the practices and programs devoted to ensuring the company complies with CSR excellence would not be as effective. Aviva worked hard throughout 2005 on creating an open and transparent program of CSR strategies for and with its staff.

A new initiative implemented in 2005 was documenting and recording employee program results, including Aviva's: staff volunteering program, payroll-charity deductions, modes of travel to work, and participation rates at staff events and competitions.

Keeping records enables a comparison over time and quantifies results, making Aviva more accountable to one of the key stakeholders its staff.

Many of Aviva's staff align its corporate social responsibility with their own values relating to sustainability and community involvement. Staff say that they are more comfortable with their employer when its operations reflect their own values towards a sustainable and socially-just world.

Aviva will strive to develop further its employer of choice program throughout 2006 and beyond.

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Alternative financial models for remote communities

David Edwards, Australian Conservation Foundation

Mr Ian Gill and Ms Leah George-Wilson of Ecotrust Canada were in Australia recently to talk about environmentally sustainable economic development strategies that prove that 'healthy social, ecological and financial returns can coexist on the balance sheet'.

Mr Gill and Ms George-Wilson were guests of the first Kimberley Appropriate Economies Roundtable, co-hosted by the Australian Conservation Foundation at Fitzroy Crossing, Western Australia, in October 2005.

As part of the visit they also spoke at briefing sessions hosted by ACF in Cairns, Broome and Melbourne to discuss the Ecotrust Canada model and its applicability to Northern Australia.

Leah George-Wilson (Ecotrust), Don Henry (Australian Conservation Foundation), Maria Mann and Craig Phillips (Environs Kimberley), Rosemary Hill (Australian Conservation Foundation), Wayne Bergmann and Tom Birch (Kimberley Land Council), Grazia Borinni-Fayreabend (World Conservation Union), Ian Gill (Ecotrust). Photo: Justin McCaul

The sessions brought together traditional owners, academics, environment NGOs and representatives of the philanthropic, legal, banking and investment sectors. The aim was to gauge the level of interest in the Ecotrust model, consider possible challenges and decide whether to pursue a more detailed feasibility study for the Australian market.

Ecotrust Canada works to restore the health of ecosystems and increase economic opportunities for indigenous people. Its approach focuses on raising and brokering capital, building the capacity of communities and connecting conservation entrepreneurs to each other and to the marketplace, in addition to supporting other preconditions for economic success, such as recognition of indigenous land and title rights.

Ecotrust Canada's natural capital revolving loan fund was established through a government grant of C$1 million and has grown to more than C$6 million. The fund's loan portfolio finances sustainable forestry, fisheries, aquaculture, ecotourism and alternative technologies with an average loan value of C$120,000. Around one third of all loans are for projects controlled by First Nations (indigenous) people and groups. Around 70 per cent of all loans are to individuals and 30 per cent to communities.

Interestingly, Ecotrust Canada lends at market rates, although it carefully structures its loans (especially repayment schedules) to match each business's natural cycles and offers interest rate incentives where projects can deliver better mission outcomes.

All loans must satisfy strict credit analysis (which is based on standard banking lending practice) and a mission analysis of the loan and its capacity to contribute to the growth of the conservation economy.

The mission analysis utilises a number of screening processes to evaluate each investment. The environmental screening process focuses on reliance on native species, waste streams and energy usage. The social screening process focuses on fair wages, employment practices and aboriginal participation in the workplace.

Ecotrust Canada has creatively used its financial and business development experience to link up its various loan projects and achieve greater vertical integration. For example, the strong interest from indigenous communities in forestry projects lead to the development of a consultancy assisting in forest stewardship council accreditation and a cooperative buying group, helping these groups access larger and more sustainable markets.

The participants to the briefing sessions held in October strongly supported the model. ACF is currently seeking funding for a detailed Australia specific feasibility study.

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To find out more about Ecotrust Canada, please visit:
www.ecotrustcanada.com

'A Climate for Change' – IGCC's practical guide for trustees in managing the risks of climate change

Garrie Lette, Mercer Investment Consulting

There is widespread acknowledgement that there are enormous implications of global climate change. However, the precise way in which the effects of climate change will be felt through the economy, the community and through investment markets are extremely difficult to predict. As a result, formulation of specific plans to manage climate change risks can be an intimidating task.

In an effort to raise awareness, provide information and encourage best practice in relation to the management of climate change risks and opportunities, a small group of institutional investors established the Australian and New Zealand Investors Group on Climate Change (IGCC) in late 2004. Membership of IGCC has grown steadily, now encompassing ten investors, holding over $155 billion in funds the vast majority of which represents savings of Australian workers and retirees. Similar investor groups, the Institutional Investors Group on Climate Change and the Investor Network on Climate Risk already operate in the UK and US respectively.

One of IGCC's first initiatives was to prepare a guide titled *'A Climate for Change – A Trustee's Guide to Understanding and Addressing Climate Risk'*.

The guide was first prepared for The Carbon Trust and the Institutional Investors Group on Climate Change, UK, by Mercer Investment Consulting. The Carbon Trust generously made the guide available to the IGCC for adaptation to the local Australian market. This adaptation was undertaken by Mercer Investment Consulting and IGCC members during 2005.

The guide is a practical tool designed to assist trustees of superannuation funds who are key stakeholders in determining the way in which investments are managed in Australia. Some of the key messages contained in the booklet are:

- The impact of climate change will vary across and between asset classes. Virtually all assets within a diversified investment portfolio will potentially be affected, not just sectors such as insurance and transport where the effects may be most obvious.
- Climate change is very clearly a fiduciary issue. Trustees do not necessarily need to become experts on the scientific aspects of climate change. Nor do they need to exercise judgements on the way in which individual securities will be affected. They should, however, ensure that portfolios are monitored and managed with a clear focus on the risks, and possibly the opportunities, arising from climate change.
- There are reasons why other key players in investment decision-making such as stockbrokers, fund managers and investment consultants, may not devote the appropriate amount of attention to climate change. Trustees of superannuation funds have the ultimate responsibility for managing the investments of their funds' members. Accordingly, trustees must take the lead.
- The actions needed to address climate change will vary across funds depending on a range of factors such as size of assets, internal versus external management, and the resources available to dedicate to the issue. All funds can and should, however, consider the issue and take actions that are appropriate given their specific circumstances.

In the guide, a three step plan is set out. The first step involves a stocktake of the trustees' understanding of and beliefs in relation to climate change issues followed by the development of policies and processes aligned with those beliefs. The second step is to establish the extent to which processes currently being applied match those agreed under the first step. Once the preferred and actual processes are determined, the third step involves determining changes which are necessary to address any gaps between the two. For each stage, a series of questions is provided, together with possible action plans. The guide provides a practical blueprint that trustees can use to develop concrete actions to address climate change in a manner which is appropriate given the overall circumstances of their fund.

To access a copy of *'A Climate for Change – A Trustee's Guide to Understanding and Addressing Climate Risk'* please visit:
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Supply chain labour problems in China – a key risk factor for investors?

Sophie le Clue, Association for Sustainable & Responsible Investment in Asia (ASrIA)

Supply chain labour problems have emerged as a key risk factor for China-based and global companies that rely on Chinese suppliers. Responsible investors are becoming increasingly aware of how these risk factors can influence their investments. Not least of these factors is the issue of poor labour conditions and in particular excessive overtime.

ASrIA released the Report *'An SRI Perspective on the Impactt Overtime Project'* at the SRI in the Rockies conference in late September 2005. The report, which is the result of a collaboration with Impactt Limited (Impactt), is intended to bring the results of Impactt's well regarded work on the problem of overtime in China's supply chain, to a new and broader audience. It is based on a longer report entitled *'The Impactt Overtime Project: Tackling Supply Chain Labour Issues Through Business Practice'* and provides the key findings as well as key commentary for SRI investors.

On the one hand, investors face important moral issues associated with investing in companies which buy or produce low cost goods at the expense of workers' health, safety and welfare. On the other hand, investors have to be realistic and pragmatic in understanding the pressures that manufacturing companies in particular face in terms of keeping their business models sustainable in an extremely competitive and time-driven marketplace. Companies engaged in supply-chain related business therefore have been finding themselves caught in a seemingly irreconcilable position between remaining financially competitive on the one hand, whilst meeting increasingly stringent labour related standards as well as increasing customer requirements on the other.

The Overtime Project Report is the result of three years of hands-on practical experience by Impactt, working closely with 11 UK based brand-name purchasing companies and their local manufacturing partners in Southern China. The purpose of the project was to explore in practice the idea that if improvements in productivity can be achieved in a way that benefits workers, then it can be shown that higher labour standards can, in fact, support the goal of running a financially competitive business.

The results of the project shift the debate from a focus on applying standards to a focus on active engagement as a means to raise productivity and clearly illustrating that productivity can be improved without compromising labour standards. The strategies discussed in this report provide an alternative approach to the more traditional audit and compliance model and can provide assurance to investors that there are strategies that companies can adopt, which will enable them to balance high labour standards, high productivity and increased market competitiveness.

ASrIA is a not for profit, membership association dedicated to promoting corporate responsibility and sustainable investment practice in the Asia Pacific region. ASrIA's members include investment institutions managing over US$4 trillion in assets, however membership is open to any organisation which has an interest in sustainable investment. ASrIA's goal is to build market capacity for SRI through the publication of up to date and accessible information on the development of SRI in Asia and globally and to provide a platform for different sectors within the community to exchange information and perspectives on SRI.

English, Japanese and Chinese versions of 'An SRI Perspective on the Impactt Overtime Project' are available at:
www.asria.org/impactt

To download the full Impactt document, please go to:
www.impacttlimited.com/site/OvertimeReport.pdf

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or visit:
www.asria.org

Funding cleaner production investments – reflections on the Asian experience

Ari Huhtala, Industrial Efficiency and Pollution Control (IEPC2), Indonesia

Making the link between cleaner production (or efficient resource management) and company performance can be good business for financial institutions. A project implemented by UNEP's Division of Technology, Industry and Economics (DTIE) 1999-2003, developed instruments to demonstrate this within Asia, with its pilot activities focusing on Vietnam. Other recent initiatives in this field include those carried out by the European Commission in Liaoning Province in China, KfW of Germany in Indonesia, Landbank, Development Bank of the Philippines and some regional activities by the Asian Development Bank. Analysis of the pilot activities has shown mixed results. Essentially, despite some positive results at specific project levels, the overall concept of cleaner production still remains remote for most financial institutions in the region. So why should banks pay attention?

It has already been proven that cleaner production:

- is a loss prevention approach which often justifies extra expenditure by companies through increased productivity, increased cash flow and the business security it creates;
- has an eye on long-term profitability and reduction of risk; and
- can lead to a change of attitude and behaviour throughout the entire range of stakeholders.

Some of the lessons learned through the project include the following.

- It is helpful to bring the language between banks and companies closer (translate engineer talk to finance talk).

- Realistic input pricing by companies is essential as there is no incentive to manage heavily subsidized resources efficiently.
- Accurate cost accounting helps to highlight merits of cleaner production to company management making bank clients better aware of how much companies may actually waste in their operations processes and simultaneously alerting them to monetary savings that could be made.
- Small and medium-sized enterprises (SMEs) may require special financial instruments including technical assistance to cross the hurdle of seeking external funding.

As part of the project, UNEP/DTIE developed some training materials and checklists under a 'Profiting from Cleaner Production' series and versions are now available in English, Chinese, and Russian (for Central Asia) at www.uneptie.org, in Indonesian from office@iepc.or.id and Vietnamese from www.un.org.vn/vncpc. Dozens of experts (financial analysts, environmental engineers and accountants) have been trained by UNEP, EU and KfW consultants to apply them. This has expanded the range of services of some Cleaner Production Centres (such as those established in China, Indonesia, Sri Lanka and Vietnam as non-profit service providers to assist industries in applying cleaner production) to include the preparation of investment proposals and bankable loan applications. As well as this, dedicated credit lines with attached technical assistance and slightly below market terms have been introduced in some local financial institutions in China and Indonesia to speed up investment in industrial efficiency and pollution control. The success or failure of these activities depends mainly on macro-economic conditions, pricing of credit and health of client companies.

Across the Asian region a range of banks are joining credit line schemes, supported by institutions such as KfW and the EC, that provide funding for cleaner production investments with some incentives to make the cost to the client slightly lower than market rate. Banks join these schemes:

- to benefit from technical assistance and capacity building attached to them;
- to expand their client base from consumer and trade loans to industrial investments; and
- (in Indonesia) to comply with Bank Indonesia rating regulations prioritizing environmental performance.

Such schemes are a way to kick-start the process of introducing the benefits to banks of efficient resource management and to make it easier for SMEs to communicate with the financial community. In the long run, however, cleaner production and environmental credit risk assessment should be mainstreamed into the credit application process to guide clients into considering alternatives before deciding on the type and size of their waste management and other operational facilities. There have been encouraging signs in Indonesia where some banks participating in the programme funded by KfW and executed by the Ministry of Environment are considering including some of the guidelines and checklists into all of their regular processes.

Modules for awareness raising and training are available in a number of languages, and there are experienced specialists and lessons learned from the successes and failures of recent projects, although they have so far been confined to a fairly narrow segment of the financial community. Now it is time to make good use of these resources in the region to improve the efficiency and reduce the ecological footprint of Asian businesses through more sustainable banking practices.

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UNEP FI International Update

National workshop on the roles and benefits of sustainable development for banks, 15 December 2005, Batam, Indonesia

Yuki Yasui, UNEP FI Geneva

Hosted by the Indonesian Ministry of Environment and the central bank, Bank Indonesia, the participants of this high profile event were addressed, among others, by the Minister of the Environment, the Deputy Governor of Bank Indonesia and the President Director of Bank Negara Indonesia (BNI) who signed up to the UNEP statement during the workshop to become the first UNEP FI signatory in Indonesia. The UNEP FI Secretariat participated in the forum as a speaker together with UNEP FI Asia Pacific Task Force Outreach Group members (Japan Bank for International Cooperation, Association of Development Financing Institutions in Asia and the Pacific and the Development Bank of the Philippines). The workshop was attended by over 100 senior executives from Indonesian banks and foreign banks operating in Indonesia.

Discussions focused on a regulation that was issued by Bank Indonesia in January 2005, which stipulates that productive asset assessment by banks should refer to and comply with Ministry of Environment guidelines. The regulation implies that banks need to adjust their methodologies concerning the collectibility or quality of their credit provision.

Banks are being encouraged to improve their environmental credit quality in order to protect themselves from being legally implicated in failures by customers to comply with environmental policies. Bank Negara, whose environmental risk management system includes an assessment of its customers' environmental awareness, provided an example of how this could be done.

Siti Fadjrijah, Deputy Governor of Bank Indonesia, announced that the Central Bank Indonesia and the Ministry of Environment had signed a Memorandum of Understanding aimed at improving the banking sector's role in protecting the environment.

HE. Rachmat Witoelar, Minister of the Environment, also announced the Ministry's release of a performance rating programme that assesses environmental compliance. Corporations (including commercial banks) will be rated against a set of criteria and may receive incentives or sanctions according to results.

For a full report of the event, please visit:
www.unepfi.org/regional_activities/asia_pacific/outreach/events/index.html

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Kyoto and beyond: The future of international climate policy – the financial sector perspective

Lisa Petrovic, UNEP FI, Geneva

A recent publication provided the following recommendations to governments and policymakers attending the eleventh conference of the parties to the UNFCCC (United Nations Framework Convention on Climate Change), and first meeting of the parties to the Kyoto Protocol in Montreal this past December: “Adopt a clear precautionary, long term reduction target and pathway for greenhouse gas emissions...Provide early, clear guidance on the continuation of the international climate policy regime beyond 2012." One could easily conclude that these recommendations were made by an environmental NGO or campaign group. In fact, the recommendations were put forward by a group of financial institutions – the Climate Change Working Group (CCWG) of the UNEP Finance Initiative. For some this may be a startling revelation – the business and finance communities demanding deeper regulation, and a continuation of Kyoto-style GHG reduction targets? The answer is yes, and if you examine the rationale behind the recommendations, it makes good business sense.

The latest CEO Briefing from the CCWG recognises that human-induced climate change is real, and that its negative consequences are starting to emerge. According to Munich Re, the year 2005 marks the biggest economic and insured losses from natural disasters on record. If the global community is serious about mitigating the impacts of climate change, we have to continue and enhance the reduction commitments made under the Kyoto Protocol. The CCWG calls for a long-term reduction target – essentially a continuation of Kyoto-style targets beyond 2012, when Kyoto's first commitment period ends.

Currently, the political timeframes built into the regime are not well aligned with investments, which require clarity over a 10 to 20 year timeframe, and sometimes longer. A clear, long-term framework i.e. beyond 2012, is a must if the global carbon markets established under the Protocol, such as emissions trading and the Clean Development Mechanism are to succeed in future. A liquid and efficient global carbon market is essential for achieving GHG emissions reductions at minimum cost. In addition, the creation of an international carbon market provides opportunities for companies to add value and profit from the development and commercialisation of low-carbon technologies, products and services.

So did the governments attending the Montreal talks heed some of this advice? In the run-up to the meeting there was a fear that the Kyoto-model would be consigned to oblivion. After two weeks of talks the model of mandatory fixed targets and timetables for reducing greenhouse gas emissions was kept alive to the delight of Kyoto-minded governments and environmental campaigners. This agreement, however, only covers the so-called Annex I countries, which account for one-third of global greenhouse gas emissions.

Those not party to the Kyoto Protocol, including the US and Australia, have agreed to an "open and non-binding exchange of views, information and ideas" which "will not open any negotiations leading to new commitments". These talks will focus on technology exchange and market-based opportunities, as opposed to specific reduction targets. The Asia-Pacific Partnership on Clean Development and Climate, seen as an alternative to the Kyoto Protocol, will follow a similar strategy.

It will be a major challenge to create a more inclusive framework, but it is hoped that more countries will come on board to the Kyoto process, and perhaps heed the advice of the finance community in its quest to establish vibrant, and liquid carbon markets and associated markets in renewable energy and energy efficiency.

The latest publication from the UNEP FI CCWG is available online at:
www.unepfi.org/fileadmin/documents/CEO_briefing_future_2005.pdf

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UNEP FI/VfU Roundtable: Sustainability management for financial institutions

Regina Kessler, UNEP FI, Geneva

In collaboration with UNEP FI, the VfU (German Association for Banks, Savings Banks and Insurances) has held its annual conference on sustainable finance for German, Austrian and Swiss financial institutions. The two-day conference was kindly hosted by DSGV (Association of German Savings Banks) during November 2005. Thirteen UNEP FI signatories participated in the Roundtable including Credit Suisse, Deutsche Bank, HVB Group, Munich Re, UBS and West LB. The diverse programme combined latest research from an international perspective with practical implementation aspects of sustainability in local institutions and attracted more than 80 participants.

The Roundtable commenced with a session on the UNEP FI Asset Management Working Group's Materiality Project. West LB, who had submitted its own broker's report to the project, made a presentation, which was complemented by the insights of a rating agency on its key methods of undertaking environmental, social and cultural screenings of companies.

The following session was dedicated to best practices in organisational sustainability management and was presented by Credit Suisse and Munich Re. Subsequent presentations were given on the external communication of sustainability activities highlighting the UNEP FI/GRI Financial Services Sector Supplement (Environmental and Social Performance) for extra-financial reporting in financial institutions. The day concluded with a session on internal communication where banks such as HVB and West LB presented on their internal sustainability campaigns that aim to enhance employee awareness.

On the morning of the second day, participants split up into separate workshops on sustainable banking services with focus on opportunities in climate change and socially responsible investment.

A study presented by Imug, a German sustainability research and consulting agency, provided information on sustainable investments by retail banking customers. The study gathered feedback from customers of 21 German banks on knowledge of socially responsible investment (SRI) funds. The level of familiarity of SRI products by investment advisers was generally perceived to be poor to non-existent. Proposals for campaigns to increase awareness among banking staff triggered a lively discussion as to where knowledge on sustainable retail products has to be created first – either at the bank's executive or its customer level.

In the second work stream of the morning, participants discussed the necessity of environmental management systems. Of particular interest in this session were the VfU indicators, which measure direct environmental impacts of financial institutions. The indicators were jointly developed by Allianz Group, Credit Suisse Group, Swiss Re, UBS AG and Westpac Banking Corporation and have gained high acceptance in German speaking countries and increasingly at an international level.

During the afternoon session's theme of risk management, ETH Zurich presented its studies on the integration of environmental risks into credit risk management processes. According to ETH Zurich's research, environmental risks play a role in 10 per cent of credit defaults. If environmental risks are material, banks should therefore integrate environmental risks into all phases of the credit risk management process such as rating, costing, pricing and monitoring. Banks that are signatories of the UNEP statement by banks on the environment and sustainable development were compared with banks that have not yet signed the agreement. The results show that generally, banks integrate environmental risk assessments especially into the initial rating phase. But only a few integrate them in all phases of the credit management process. Furthermore, significant differences in integrating environmental risks between UNEP and non-UNEP banks were found.

In 2006, UNEP FI and VfU will hold their joint roundtable for the German-speaking finance sector in Berlin. The event will be hosted by Deutsche Bank and will include a special CEO's meeting in order to increase awareness amongst chief executives. Due to high interest among German-speaking financial institutions of sustainability reporting, UNEP FI and VfU will also organise a workshop on the Financial Services Sector Supplement to the GRI guidelines in the first half of 2006. Other possible activities include a competition for innovative ideas in sustainable finance among organisations' apprentices and a workshop on social requirements for the finance sector.

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To access further studies of ETH Zurich, please visit the following websites:

The relationship between sustainability performance and financial performance of firms
www.vfu.de/download/roundtable%202005/GRI_Report.pdf

Incorporating sustainability criteria into credit risk management
www.vfu.de/download/roundtable%202005/Incorporating.pdf

To access the VfU Indicators on sustainability reporting, please visit:
www.vfu.de/vfu-indicators-2005.htm

To see presentations of the 2005 UNEP FI/VfU conference (in German) please visit:
www.vfu.de/roundtable2005.htm

New UNEP FI Signatories:

- Bank Negara Indonesia (Indonesia)
  www.bni.co.id/english
- The Export-Import Bank of Korea (Korea)
  www.koreaexim.go.kr/en
- Domini Social Investments (USA)
  www.domini.com
- Fundación Social (Columbia)
  www.fundacion-social.com.co/
- Henderson Global Investors (UK)
  www.henderson.com
- Hyundai Marine and Fire Insurance Co Ltd. (Korea)
  www.hi.co.kr/company/en/ceo/ceoView01.jsp
- Lombard Odier Darier Hentsch & Cie (Switzerland)
  www.lodh.com
- Trucost (UK)
  www.trucost.com

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