UNEP FI & ADFIAP
Environmental & Social Risk Analysis Workshop
Sustainability Risk Management
An Overview

Ben Ridley
Regional Head of Sustainability Affairs, Asia-Pacific

Manila, 27 October 2009
Sustainability Risk Management

- Types of Risk

- Reputational Risk

- Sustainability Risk
  - Issue Screening
  - Guidelines / Policies
  - Key Sectors

- Case Studies
## Types of Risk

<table>
<thead>
<tr>
<th>Management risks</th>
<th>Strategy risk</th>
<th>Outcome of strategic decisions or developments</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Reputation risk</td>
<td>Damage of our standing in the market</td>
</tr>
<tr>
<td>Chosen risks</td>
<td>Market risk</td>
<td>Changes in market factors such as prices, volatilities, correlations</td>
</tr>
<tr>
<td></td>
<td>Credit risk</td>
<td>Changes in the creditworthiness of other entities</td>
</tr>
<tr>
<td></td>
<td>Expense risk</td>
<td>Difference between operating expenses and income in a crisis</td>
</tr>
<tr>
<td>Consequential risks</td>
<td>Operational risk</td>
<td>Inadequate or failed internal processes, people and systems; or external events</td>
</tr>
<tr>
<td></td>
<td>Liquidity risk</td>
<td>Inability to fund assets or meet obligations at a reasonable price</td>
</tr>
</tbody>
</table>
Management risks

<table>
<thead>
<tr>
<th>Risk</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>Strategy risk</td>
<td>Outcome of strategic decisions or developments</td>
</tr>
<tr>
<td>Reputation risk</td>
<td>Damage of our standing in the market</td>
</tr>
</tbody>
</table>

**Nature of risk:**
- Long term
- Difficult to quantify
- Significant downside
- Difficult/Costly to minimize

**How to manage risk:**
- High on senior management agenda
- Structured process for risk management
What is Reputation?

- Reputation is a *perceived* image that you have about an organisation.

- Serious reputational damage can occur simply as a result of perceived failures, even if those perceptions are not grounded in fact.

- It is not solely about legal rights and wrongs but perceived values regarding rights and wrongs, which evolve with time and society.

- Managing reputation is tricky.

- Does reputation affect shareholder value?
Share Price Performance

The fall of Enron...

Over a 16-month period, Enron's stock price declined from a high of $90 to a low of under $1 before the giant energy-trading company declared bankruptcy.
Reputational Risk Policy

Mandatory submissions: actions / transactions that could involve...

- Controversial client and/or business activities
- Tax, accounting or regulatory implications
- Adverse environmental or sustainability implications
- Conflicts of interest
- Client suitability concerns

Other factors that could lead to a RRRP submission

“...an employee should consider how the Bank’s reputation might be damaged in hindsight, if it were associated with a particular action or transaction in the media. The Policy requires employees to be conservative when assessing potential reputational impact and, whenever in doubt, to err on the side of submitting an action or transaction to RRRP for review.”

“Reputational risk is the potential that negative publicity regarding an institution’s business practices, whether true or not, will cause a decline in the customer base, costly litigation, or revenue reductions.” (Board of Governors of the Federal Reserve System, 2004)
Reputational Risk Review Process (RRRP)

- The Reputational Risk Policy and RRRP apply globally to all Divisions of the Bank and across all regions.

- The RRRP exists to ensure global consistency in reputational risk evaluation and to decide whether or not to pursue or execute a particular action or transaction.

- Actions or transactions that are referred to the RRRP may be:
  - Declined
  - Approved with conditions, or
  - Approved with no conditions
RRRP Flow

<table>
<thead>
<tr>
<th>Responsible</th>
<th>Tasks</th>
</tr>
</thead>
</table>
| Reputational Risk Sustainability Committee (RRSC) | ▪ Representation on Executive Board  
▪ Sets policy, reviews key issues, can overrule a rejection |
| Regional CEO | ▪ Can veto an approval  
▪ (but cannot overrule a rejection) |
| Reputational risk approver (RRA) | ▪ After review, approves, rejects or modifies a submission |
| Divisional endorser (Line Management) | ▪ Business Area head or designee  
▪ Supports or rejects a submission |
| Originator (Any employee) | ▪ Initiates approval process |
Should the action/transaction be referred to RRRP?

Does the action or transaction pose an unacceptable level of risk to the firm’s reputation?

- Affect the firm’s External Image?
- Raise Suitability Issues for the Client?
- Pose Ownership Issues for the firm?
- Have Accounting, Regulatory or Tax Consequences?
- Meet any of the 13 Mandatory Submissions?

No submission required unless circumstances change. End determination process

File a submission
Year 2008 Rep-Risk Referrals, APAC Region

- 336 referrals to the Rep-Risk team
- 94 referrals (28%) were in the ‘Environment’ category
Reputational / Sustainability Risk Governance

**CEO**
- Highest decision-making authority
- Appoints Chair Reputation Risk - Sustainability Committee

**Reputation Risk - Sustainability Committee (RRSC)**
(4x/year) *

**Tasks:**
- High-level review of transaction approvals / rejections
- Discuss update on sustainability/regulatory issues, trends and focal topics
- Determine CSG’s strategy with respect to environmental and social issues (priorities, policies and positions) and evaluate the achievement of annual sustainability objectives
- Ensure implementation of CSG’s environmental policy and sustainability commitments (UNEP FI, UN GC, CoC)
- Endorse annual Environmental Management Review as part of ISO 14001 process

**BoD / RC**
Sustainability review

**Sustainability Affairs**
Supports RRSC through:
- Monitoring of trends/competitors
- Coordination of projects
- Internal consulting and support
- Reporting

* Members of the RRSC:
  - 4 Regional CEOs
  - 4 Regional Risk Approvers
  - Chief Risk Officer
  - General Consul
  - Chief Communication Officer
  - Head Public Policy
  - Head Sustainability Affairs
  - Optional: 3 Divisional CEOs

---

Produced by: Public Policy - Sustainability Affairs
Date: October 2009  Slide 12
Sustainability Risk Management Process

Reputational Risk Review Process

- **Transaction**
  - Type
  - Purpose
  - Location/Jurisdiction

- **Main sustainability impacts of industry**
  - Public image/controversies and sustainability track record of client

- **Pre-assessment**
  - Low/medium/high risk

- **Pre-assessment + question list to deal team**

- **Request for 3rd party report (ESIA, AP)**

Examination of documentation (ESIA, AP, answers to questions)
- Benchmark against CS Industry Guidelines/Policies + IFC Industry EHS Guidelines

- **Sustainability Affairs**
- **3rd Party Consultant**

Assessment of CS Rep Risk: low/medium/high + conditions to reduce and mitigate risks (to be covenanted/included in deal documentation)

Control of conditions

**Tools/Support**

- Specialized issue websites/newsletters
- Client website
- Innovers Intangible Value Assessment
- Ecofact Rep Risk™
- IFC Industry EHS guidelines
- NGO involvement
  - Site visits
- 3rd Party consultants
- IFC Industry EHS guidelines
- CS Industry Guidelines/Policies

**Standardized assessment template**

Proper by: Public Policy - Sustainability Affairs
Date: October 2009  Slide 13
## Key Industries / Sectors

### Internal Sustainability Policies / Guideline exist for:

<table>
<thead>
<tr>
<th>Sector</th>
<th>Forestry</th>
<th>Mining</th>
<th>Oil &amp; gas</th>
<th>Hydropower</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Issues</strong></td>
<td>Loss of high conservation value forest</td>
<td>Contamination of land and water</td>
<td>Contamination of land, water, air</td>
<td>Impact on riverine and surrounding terrestrial environments</td>
</tr>
<tr>
<td></td>
<td>Loss of biodiversity</td>
<td>Impacts on biodiversity</td>
<td>Impacts on biodiversity</td>
<td>Destruction of natural habitats</td>
</tr>
<tr>
<td></td>
<td>Illegal logging</td>
<td>Impacts on public health and safety, local cultures, community-based livelihoods</td>
<td>Impacts on public health and safety, local cultures, community-based livelihoods</td>
<td>Destruction of natural habitats</td>
</tr>
<tr>
<td></td>
<td>Monoculture (palm oil, soy)</td>
<td>Decommissioning and rehabilitation</td>
<td>Decommissioning and rehabilitation</td>
<td>Impacts on cultural heritage</td>
</tr>
<tr>
<td></td>
<td>Loss of home, shelter, subsistence for local communities</td>
<td>Poor governance/corruption</td>
<td>Poor governance/corruption</td>
<td>Displacement or resettlement of people</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th><strong>Standards</strong></th>
<th>IFC EHS Guidelines for Forest Harvesting / Pulp &amp; Paper Mills</th>
<th>IFC EHS Guideline for Mining</th>
<th>IFC EHS Guidelines for Offshore / Onshore Oil and Gas Development</th>
<th>IFC General EHS Guidelines, OP Safety of Dams</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>GRI Mining Sector Supplement</td>
<td>Extractive Industries Transparency Initiative (EITI)</td>
<td>Extractive Industries Transparency Initiative (EITI)</td>
<td>World Commission on Dams (WCD) guidelines</td>
</tr>
<tr>
<td></td>
<td>FSC</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>RSPO</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

* under development
Screening Tools

Credit Suisse

RepRisk Relationships
- General Information
- Financial Institutions (364)
- Other Companies (273)
- Projects (25)
- Countries (31)
- Issues (22)
- UN GC Principles (8)
- NGOs (41)
- Campaign Exposure (3)

Sector(s):
- Banks

Headquarters:
- Switzerland

Website:
- www.credit-suisse.com

Credit Suisse Group AG (Credit Suisse), formerly Credit Suisse First Boston

RepRisk Index Trend

Current RRI 25 • Peak RRI 61 in Nov 2007

Trend of the RRI over the past 24 months, based on all news.

<table>
<thead>
<tr>
<th>Date / Source</th>
<th>News</th>
<th>Abstract</th>
</tr>
</thead>
<tbody>
<tr>
<td>01.08.2009 dtc.gn Các.org (Down to Earth Indonesia)</td>
<td>NGO report addresses problems caused by companies in Indonesia</td>
<td>Companies involved with the United Nations REDD projects (Reducing Emissions from Deforestation and Forest Degradation) have come under fire as the programs have been criticized for an alleged lack of community consultation, failure to protect indigenous rights, and potential corruption, in a Down to Earth report on Indonesia. It also detailed the negative impacts of palm oil production in the country, such as the violation of indigenous rights, overuse of resources, impact on ecosystems and endangered species, and the neglect of local participation processes. It is alleged that the Roundtable on Sustainable Palm Oil has certified companies that are involved in unresolved community conflict in Indonesia.</td>
</tr>
<tr>
<td>26.08.2009 regenwacht.org</td>
<td>Semang, Interhill Shin Yang, KTS und Rimbanan Hijau accused of rainforest destruction in Malaysia (German)</td>
<td>NGO Betzoldten Regenwald is urging the public to write to the Malaysian government, demanding the recognition of land rights for the Indigenous Penan people, and an immediate stop to the threat of rainforest destruction by firms including Semang, Interhill Shin Yang, KTS, and Rimbanan Hijau. This issue is once again in the spotlight as more than 3000 Penan are currently staging protests in the forests of Borneo, claiming that the companies have destroyed their traditional hunter and gatherer, nomadic lifestyle through logging and palm oil activities. Credit Suisse is also criticized for aiding such activities, including Semang’s IPO and Golden Agri-Resource recapitalization.</td>
</tr>
</tbody>
</table>
### Screening Tools

#### Credit Suisse Group
- **Industry:** Global Banks
- **Country:** Switzerland
- **Outlook:** Steady
- **Analyst:**

<table>
<thead>
<tr>
<th>Intangible Value Assessment</th>
<th>Business Activities</th>
<th>Global Compact I</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

#### Intangible Value Assessment Four-Pillar Scores

<table>
<thead>
<tr>
<th>Company Score</th>
<th>1</th>
<th>2</th>
<th>3</th>
<th>4</th>
<th>5</th>
<th>6</th>
<th>7</th>
<th>8</th>
<th>9</th>
<th>10</th>
</tr>
</thead>
<tbody>
<tr>
<td>Strategic Governance</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>X</td>
</tr>
<tr>
<td>Human Capital</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>X</td>
</tr>
<tr>
<td>Environment</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>X</td>
</tr>
<tr>
<td>Stakeholder Capital</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>X</td>
</tr>
<tr>
<td>Industry Average</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>X</td>
</tr>
</tbody>
</table>

#### Rating Comment

The strongest driver of a bank's long-term financial performance is its ability to profitably allocate capital and accurately forecast and manage risk. In our view a bank is only as sustainable as the risks that it finances. Our analysis of banks addresses two core questions:

- What is the environmental and social (ESG) risk intensity of the companies and consumers that a bank has financed?
- Is the bank’s (ESG) risk management strategy and product portfolio commensurate with its ESG risk exposure?

#### Consumer Finance

*Innovest looks for three core traits in a bank’s consumer finance operations:

- That it does not enable “prime” borrowers to live beyond their means by issuing more debt than their incomes can sustain over the long term.
- If it extends finance to low income, unbanked, or underbanked consumers that it expands due diligence accordingly and only issues debt (or trades securitized debt) on reasonable terms which is consistently repaid.
- That it proves it is achieving objectives 1 and 2 with hard data.

#### Corporate Finance

*With corporate finance Innovest takes that view that “you are what you finance.” We examine all publicly filed deals that each bank has participated in and measure the aggregate ESG risk intensity of the companies that each bank has financed.

- If a bank has a strategy of avoiding high risk companies we look to see that its deal portfolio is, in aggregate, low risk from an ESG perspective.
- If a bank’s strategy is to embrace risk then we look for statistically viable evidence that the high risk companies that it has historically financed have improved over time.
- Above all we want to see that a bank’s ESG due diligence strategy is commensurate with its risk.
Case Studies

- **Sakhalin II Oil & Gas Project**
  - World’s largest integrated oil and gas project
  - Original budget estimate USD 10bn
  - Key finance from EBRD
  - Credit Suisse appointed to advise Sakhalin Energy Investment Company in 1999

- **Trans-Amazon Highway**
  - 2,500km highway upgrade / construction mandated by governments of Brazil and Peru
  - Multi-national engineering and construction company
  - Financial guarantees provided by a regional development bank
  - Project Finance (Equator Principles cat. A) with loan repayment over 15 years
Sakhalin II Oil & Gas Project

- **Western Gray Whales**
  - Offshore platform and pipeline is close to summer feeding grounds of a threatened whale species, impact through noise of work and risk of oil spill

- **Wildlife and fisheries**
  - Construction of 800 km onshore pipeline in seismic area and crossing 1000 rivers, impacts on island wildlife and spawning of salmon and other fish

- **Aniva Bay**
  - Dredging work for LNG jetty alters seabed texture (excavation and dumping of material), impacting feeding and spawning grounds of fish

- **Indigenous peoples**
  - Disputes over sufficient prior consultation and adequate compensation
  - Impact of project work on people’s livelihood
Sakhalin II Oil & Gas Project

NGO Campaigns

Children’s drawings sent to Credit Suisse CEO
Sakhalin II Oil & Gas Project

- **Key lessons learned:**
  - Conduct environmental due diligence against broadly accepted standards
  - Use specialist consultants with industry and local knowledge
  - Integrate political factors in risk assessment
  - Include formal client commitment to risk mitigation in transaction contract
  - Regularly review project’s environmental performance (semi-annually)
  - Ensure direct access to client’s environmental affairs unit
  - Avoid exclusive reliance on deal team information
  - Engage with NGOs and client to address critical issues
Trans-Amazon Highway

Likely direct impacts (construction phase):
- Threat to protected species (flora and fauna), impact on biodiversity
- (Minor) Resettlements, potential conflicts with indigenous communities
- Potential impact on cultural heritage (archeological sites)
- Immigration of laborers in search of work during construction

Likely indirect impacts (highway operation):
- Illegal activities – logging, mining and agricultural land uses
- Impact of immigrants on indigenous peoples groups
- Emigration of local people & indigenous groups
Outcome

Turned down – too many potentially serious environmental and social impacts outside of client control

Lessons learnt

- Multilateral dev. bank guarantees financial risk and sets certain env. / social standards
- Govt. mandate for project may add some legitimacy to project – but no guarantee!
- Direct impacts may be mitigated (bank leverage with client)
- Indirect impacts very difficult to mitigate (outside of the bank’s influence), yet the bank may be held responsible for them
- Sympathy from an NGO does not protect you from rep risk

Timeline

- Multilateral Dev. Bank
- Government
- Borrower / project sponsor
- Business
- Legal
- Sustainability Affairs
- National environmental NGO
- SEA
- AP
- Consultation

Produced by: Public Policy - Sustainability Affairs
Date: October 2009  Slide 22
Sustainability Risk Management

- Thank You

www.credit-suisse.com/responsibility/en