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Study Identifies Large Differences in Global Sustainability Governance

The extent to which large cap global companies are regulating themselves with regard to ethics, climate change, other environmental concerns, and labor and human rights varies significantly by nationality and industry sector. These findings emerge from RiskMetrics Group's year-long pilot project assessing more than 1,700 global companies—including the S&P 500, the Toronto Stock Exchange 300 and the Morgan Stanley EAFE index excluding Japan—on more than 200 policy and performance indicators.

EAFE companies clearly outperform S&P500 firms on both climate change and other environmental issues, but U.S. firms have the edge on ethics policies. For labor and human rights, overall performance between EAFE and S&P500 did not differ substantially. Canadian firms (the TSX300), overall, lagged companies in the other two indices, but did best on labor and human rights.

In addition, while some individual companies stand out as clear leaders, overall average performance by sector and industry stood at less than 50 percent of the ideal defined in the research model.

Assessment by Sector

RiskMetrics analyzed its sustainability research results using the Global Industry Classification Standard (GICS) developed by Morgan Stanley and Standard & Poor's, which has 10

The Assessment Model

The RiskMetrics model examines four pillars of sustainability—climate change, other environmental factors, labor and human rights, and ethics—with additional oversight and reporting indicators that touch on all these areas. Performance is measured using a governance risk lens, taking into consideration board oversight, management policy and execution, public disclosure, accounting methods and strategic planning.

A small sampling of the indicators in each area includes:

Climate change

- Does the company conduct an annual inventory of greenhouse gas emissions and publicly report results?
- Has the company set a target for managing its GHG emissions?

Other environmental concerns

- Is there a senior management official responsible for environmental issues?
- Does the company submit to environmental third party audits?
- Does the company provide numerical data on energy, hazardous waste, toxic emissions, toxic spills, water use and/or recycling? Does it set any targets to stabilize or reduce its impact in these areas?

Labor and human rights

- Is there a senior company executive in charge of overseeing labor and human rights policies and programs?
- Which of the seven core International Labor Organization standards are included in the company's policies?
- Does the company disclose numerical data on its work-related accidents and illnesses?

Ethics

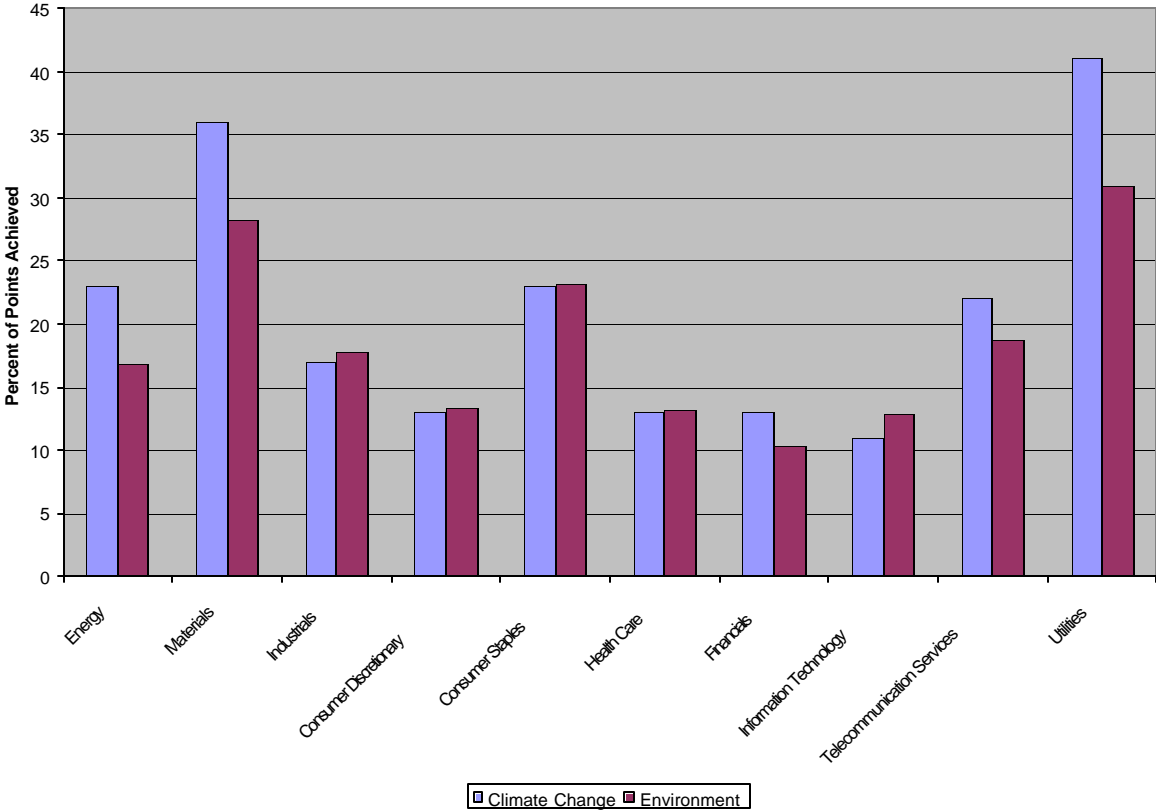
- Is there a committee of the board charged with oversight of ethics?
- How does the company facilitate reporting on violations of its ethics policy?
- Does the company engage in dialogue with local communities to assess and manage the impact of its operations?

RiskMetrics gathered the answers to these and other indicators largely from the information companies disclosed during 2006 and 2007 in their corporate sustainability reports, securities filings and websites.

economic sectors, 24 industry groups, 67 industries and 147 sub-industries. The system assigns an eight-digit code to each company in the world, allowing peer comparisons across indices. Morgan Stanley notes the system “is the result of numerous discussions with asset owners, portfolio managers and investment analysts around the world and is designed to respond to the global financial community’s need for an accurate, complete and standard industry definition.” Sectors are defined by the first two digits, industry groups by the second two-digit set, and so on. The RiskMetrics project identified substantial differences in sustainability reporting and performance among industries within each sector.

Climate change and environment: Utilities are the most likely to have detailed policies and governance systems in place to deal with climate change—no surprise given their significant regulatory risk exposure. Yet even this sector attains an average of just over 40 percent of the points available in the RiskMetrics assessment model. Information Technology firms are the lowest average performers, achieving just over 10 percent of the possible points available on climate, with slightly better results for other environmental indicators. Performance on climate-related metrics tracks with non-climate environmental indicators for the most part, with eight out of ten sectors coming out at or better on climate than on other environmental factors. This may be further evidence that climate change is a tipping point issue for corporations that aim to position themselves best for the regulatory and physical risks of a carbon constrained economy. (See Chart 1.)

Chart 1: Climate Change and Environment Sector Averages



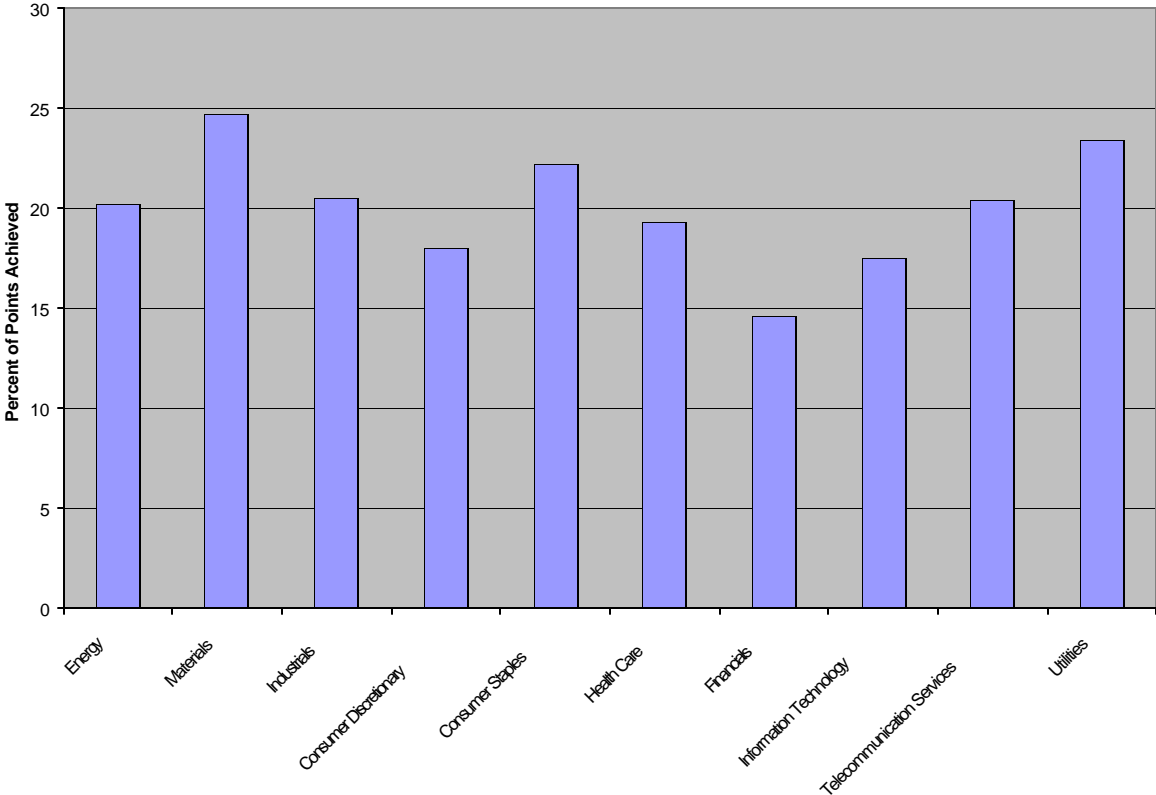
In addition to the variations *between* sectors, there were some notable variations *within* each sector. On climate change, the bottom scoring industries in four sectors—Consumer Discretionary, Information Technology, Health Care and Industrials—received no points at all, since their public communication on climate was absent. These industries were, respectively, Diversified Consumer Services, Internet Software & Services, Health Care Technology and Marine. The biggest variance between average scores by industry was within the Consumer Discretionary sector, where Automobiles scored highest, despite achieving on average only 22 percent of possible points, and Diversified Consumer Services lowest, with no points. The difference between the highest and lowest scoring Telecommunications industries was the least (10

percent for Diversified Telecommunication Services and 5 percent for Wireless companies) of all the sectors studied; as noted above, these firms overall have low scores on climate change indicators. As such, these scores may be a proxy for the degree to which this industry believes it is exposed to climate change risk relative to other industries.

The largest variance in sustainability governance performance on the environment was also within the Consumer Discretionary sector, where Automobiles again come out with the highest average score (32 percent) and Diversified Consumer Services the worst (zero percent). There were plenty of bedfellows at the bottom, however, with industries in other sectors—Information Technology, Health Care, Industrials and Financials—barely earning any points; these included Internet Software and Services, Health Care Technology, Trading Companies & Distributors and Thrifts & Mortgage Finance firms. The Chemical industry came out with the highest average industry score—55 percent—probably illustrating the impact of close scrutiny from the public and government of these firms’ effects on the environment.

Labor and human rights: RiskMetrics studied the extent to which companies address labor and human rights for their employees and their suppliers. Materials sector firms, where historically higher rates of unionization may have boosted employee safety and benefits standards, hold the lead with nearly 45 percent of points possible. By contrast, Financial sector companies, which have received comparatively little pressure on this issue, achieve on average about one-quarter of the points possible, at the bottom of the heap. (See Chart 2)

Chart 2: Labor & Human Rights Sector Averages

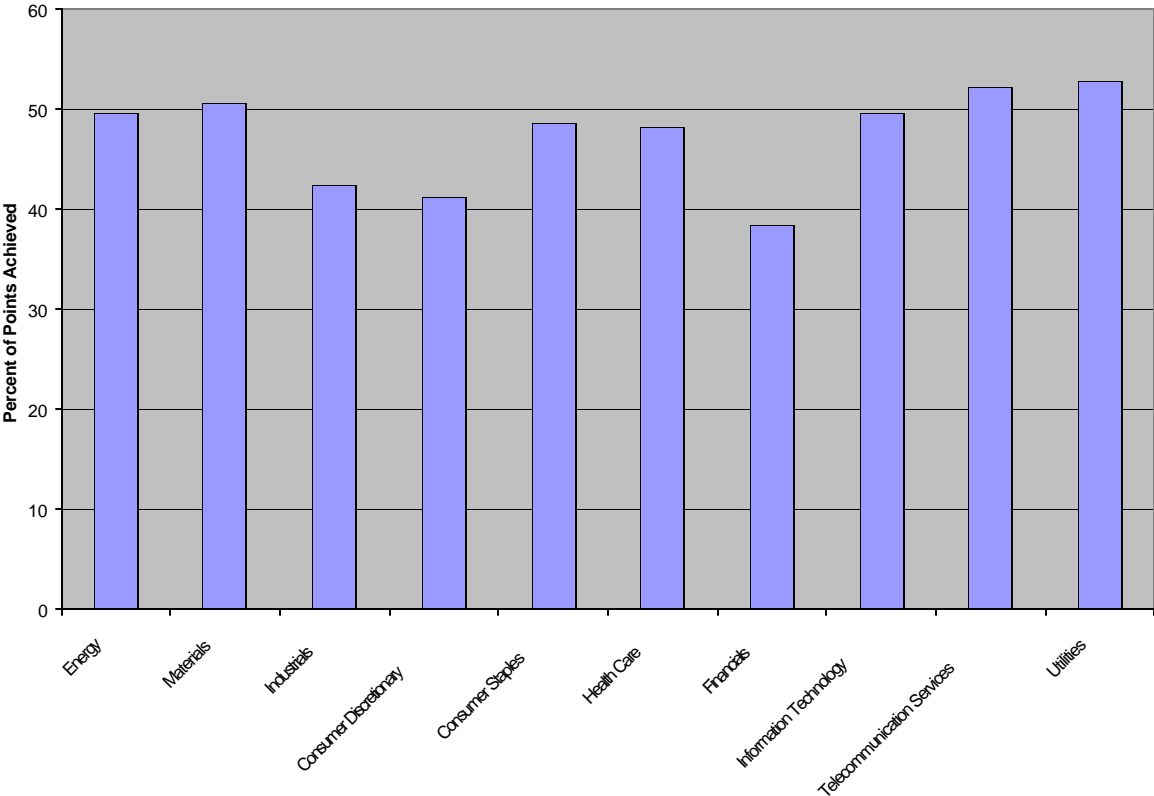


Drilling down to the industry level, policies for company employees on labor and human rights had the greatest variability in the Health Care sector, where Pharmaceuticals achieved 46 percent of available points on average and Health Care Technology firms just 10 percent. The least variability comes for the mid-range scoring Utility sector, where the top and bottom performing industries—Oil, Gas & Consumable Fuels and Energy Equipment & Services—both get about one-third of available points. Individual industries with the best performance on company labor and human rights policies are Chemicals, Household Products and Automobiles, which all had average scores between 53 and 55 percent.

Ethics: The last pillar in the RiskMetrics sustainability assessment model is ethics. In contrast to the other areas, performance on these indicators was both higher and more consistent across economic sectors. All but Financials achieved more than 40 percent of possible points, and three sectors—Utilities, Telecommunications and Materials—topped 50 percent. (See Chart 3)

Despite the better performance on ethics indicators by all sectors, variability within industries was the greatest for this pillar in the RiskMetrics model. The variance within sectors was greatest among Health Care firms, where the top scoring Life Sciences Tools & Services achieved 57 percent and the lowest performing Health Care Technology only 12 percent. The differences between top and bottom scoring industries are also substantial for Financials (56 percent for Thrifts & Mortgages and only 15 percent for Real Estate Management & Development) and Industrials (54 percent for Air Freight & Logistics and just 18 percent for Marine). Top scoring industries across the board achieve about 50 percent or more of available points, making the bottom scorers particular outliers.

Chart 3: Ethics Sector Averages

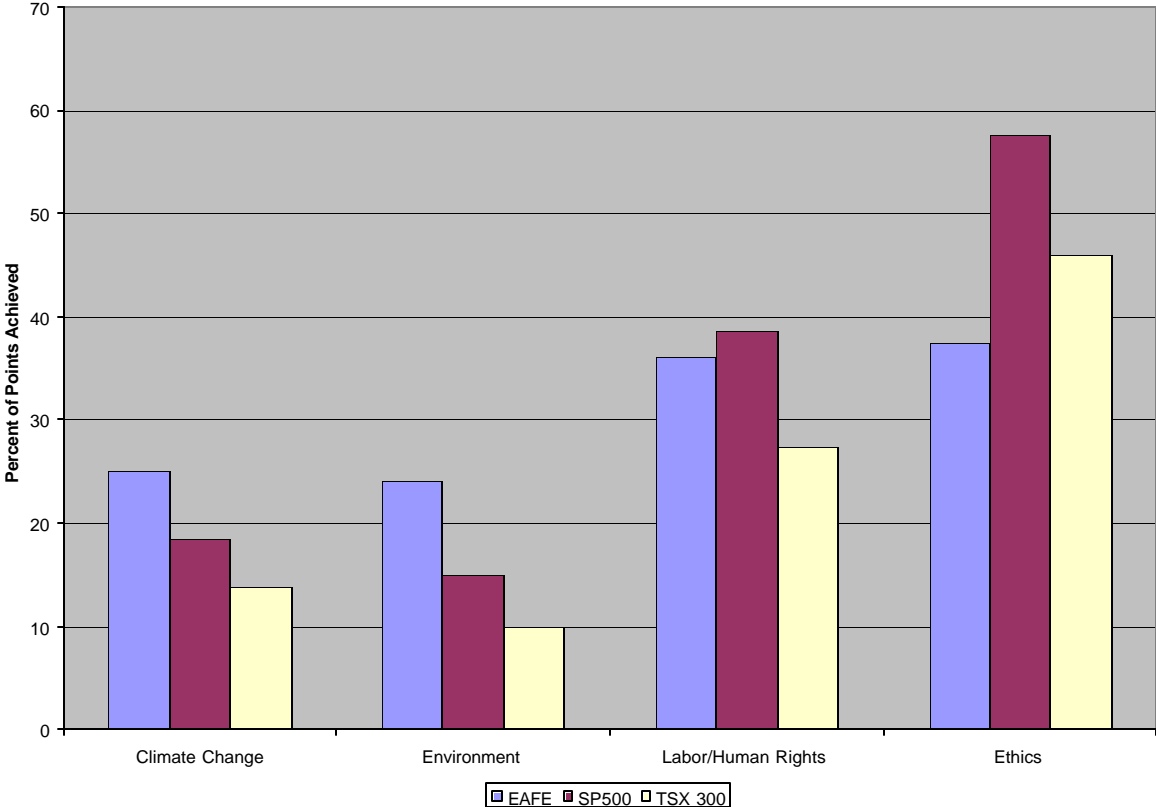


EAFE Companies Far Exceed U.S. Counterparts

Whether a company outperforms its peers on the four sustainability indicator areas in the RiskMetrics model appears to be clearly linked to its place of incorporation. On the whole, EAFE firms do better than S&P500 and Canadian companies. RiskMetrics disaggregated the sustainability data by each issue pillar and index, though, revealing substantially different results. Overall, EAFE companies appear to perform far better on climate change and the environment than their S&P500 counterparts. But their handling of ethics issues appears to be not nearly as far along as it is for U.S. firms; EAFE companies earned just 37 percent of the total points possible for ethics, compared with 58 percent for the S&P500. Much more parity shows up for labor and human rights, where there is little difference between the two. Canadian companies come out with lower scores than EAFE and S&P500 companies in every area aside from ethics, where the TSX firms do better than EAFE. (See following Chart.)

Given the smaller number of companies in the TSX, results by sector and issue pillar should be treated with some caution; for this index, there are just seven Health Care firms and only five Telecommunications Services companies. Likewise, there are only five in the latter sector for the S&P500.

Sustainability Performance by Index



Climate change: Within the climate change pillar, there is little difference between the top scoring EAFE and S&P500 Utilities companies. Both sets of companies achieve nearly half the points possible in RiskMetrics’ scoring model. Not far behind, and with similarly minimal differences, is the Materials sector. At the lower end of the scale, the scoring gap opens up, and EAFE companies in the Financials sector have average scores that exceed their S&P500 counterparts by more than three to one—21 percent versus just 6 percent.

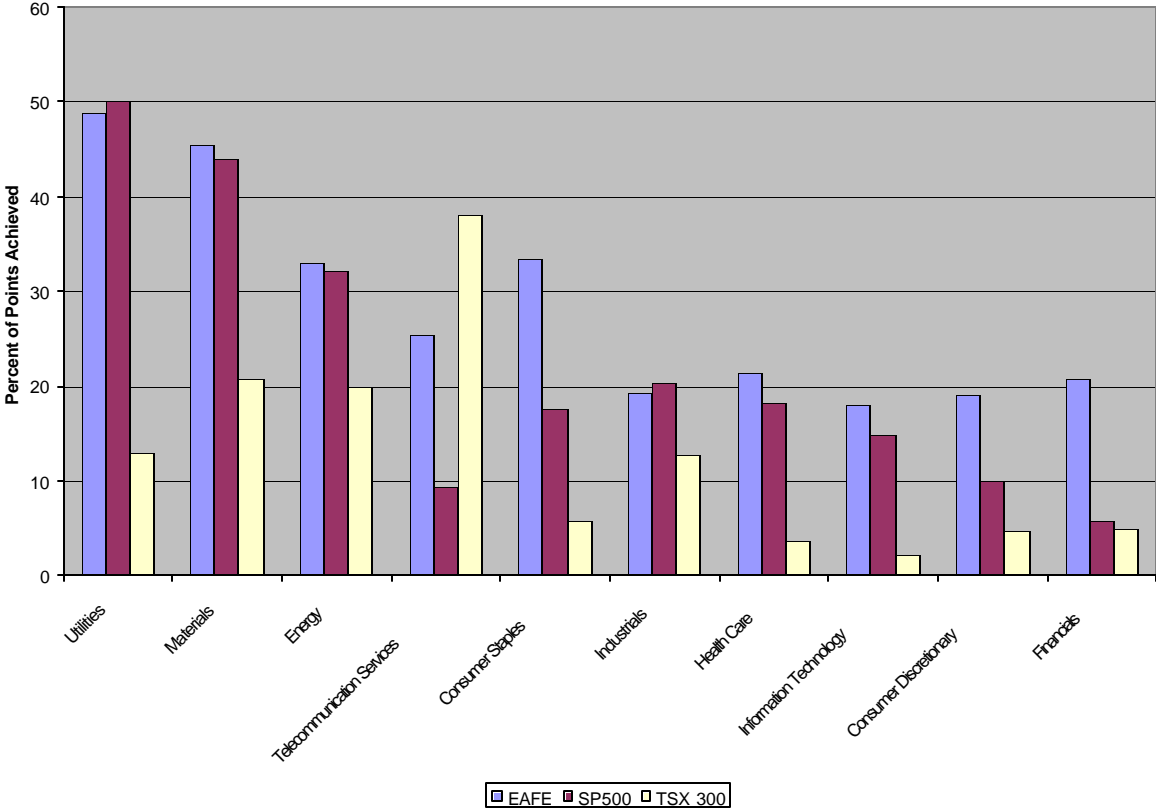
Environment: The Utilities and Materials sectors occupy the high end of the scale for non-climate environmental indicators, although EAFE scores are one-quarter and one-third higher than those for S&P500 counterparts, respectively. The difference between scores at the low end of the scale is more pronounced, however. EAFE Financials firms earned scores that are more than four times those of their sector peers in the S&P500. U.S. Financials seem barely to have environmental issues on their radar, earning only 3 percent of possible points, compared with 16 percent for EAFE counterparts. The trend of EAFE members scoring better than U.S. firms comes through for all sectors. The most dramatic differences show up in Telecommunications Services, although the small samples noted above may skew this result and the finding that Canadian companies in this sector do much better than both U.S. and EAFE peers.

Labor and human rights: For labor and human rights indicators on company policies—excluding supplier standards—S&P500 companies have a slight overall edge (39 percent versus 36 percent of possible points), with EAFE companies slightly ahead among the top scoring sectors and slightly below on the other end of the scale. Companies in the top-ranked Materials sector still earn less than 30 percent of

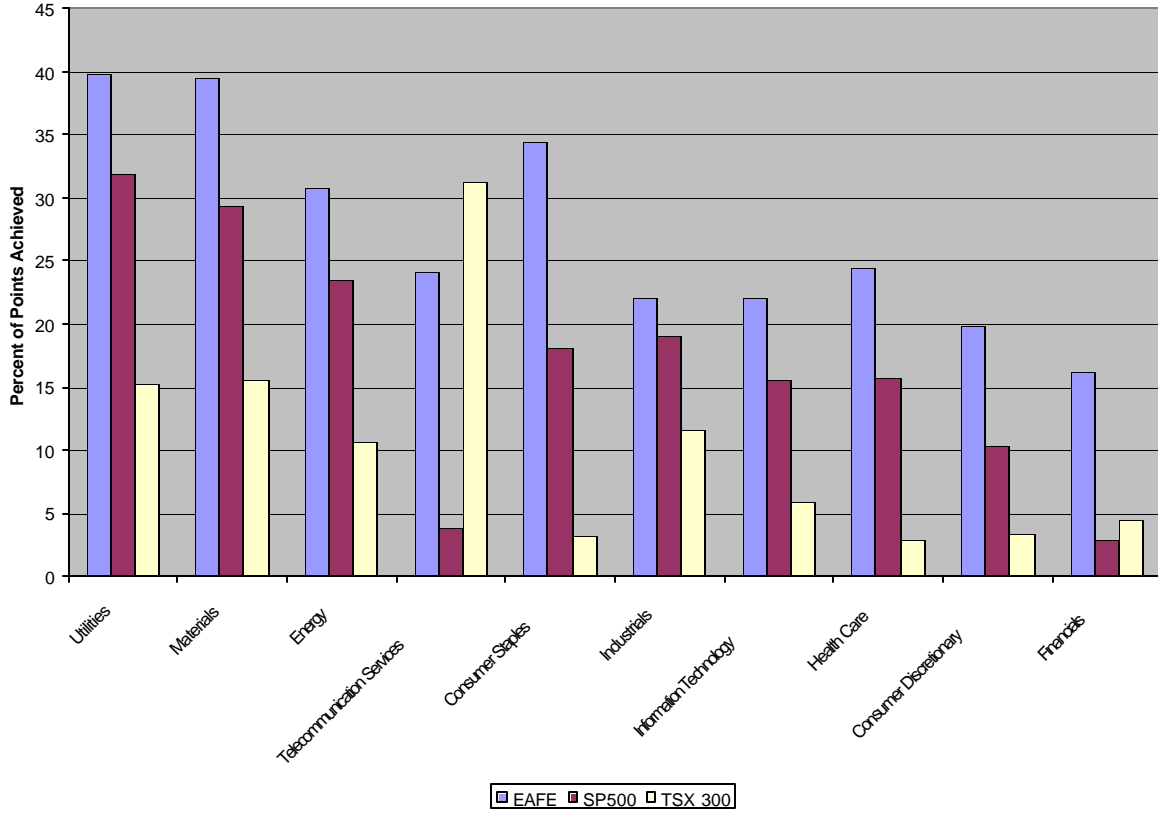
possible points, on average, however. Financials again come out at the bottom, for all the indices. The highest scoring Canadian sector is Telecommunications and the lowest is Consumer Staples.

Ethics: Results for ethics indicators buck the trend of better sustainability performance by EAFE companies overall and in the other three issue pillars. Five U.S. sectors—Telecommunications, Materials, Utilities, Consumer Staples and Industrials come out with more than 60 percent of the available points. No EAFE sectors come close, although the top scoring EAFE sectors—Telecommunications Services, Materials, Utilities and Energy—all get close to half the available points. TSX companies do better than EAFE in most sectors. EAFE Financials come in at the bottom, just edging past 30 percent of available points, on average.

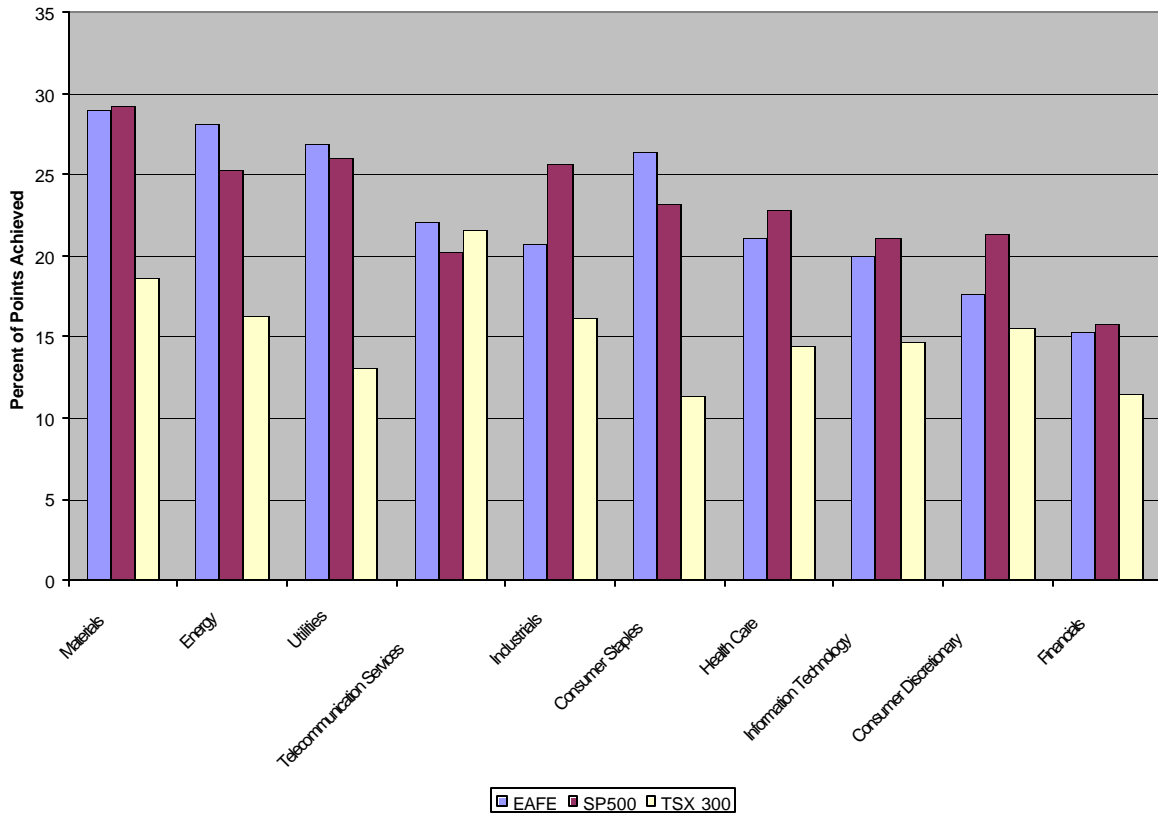
Climate Change Performance by Index



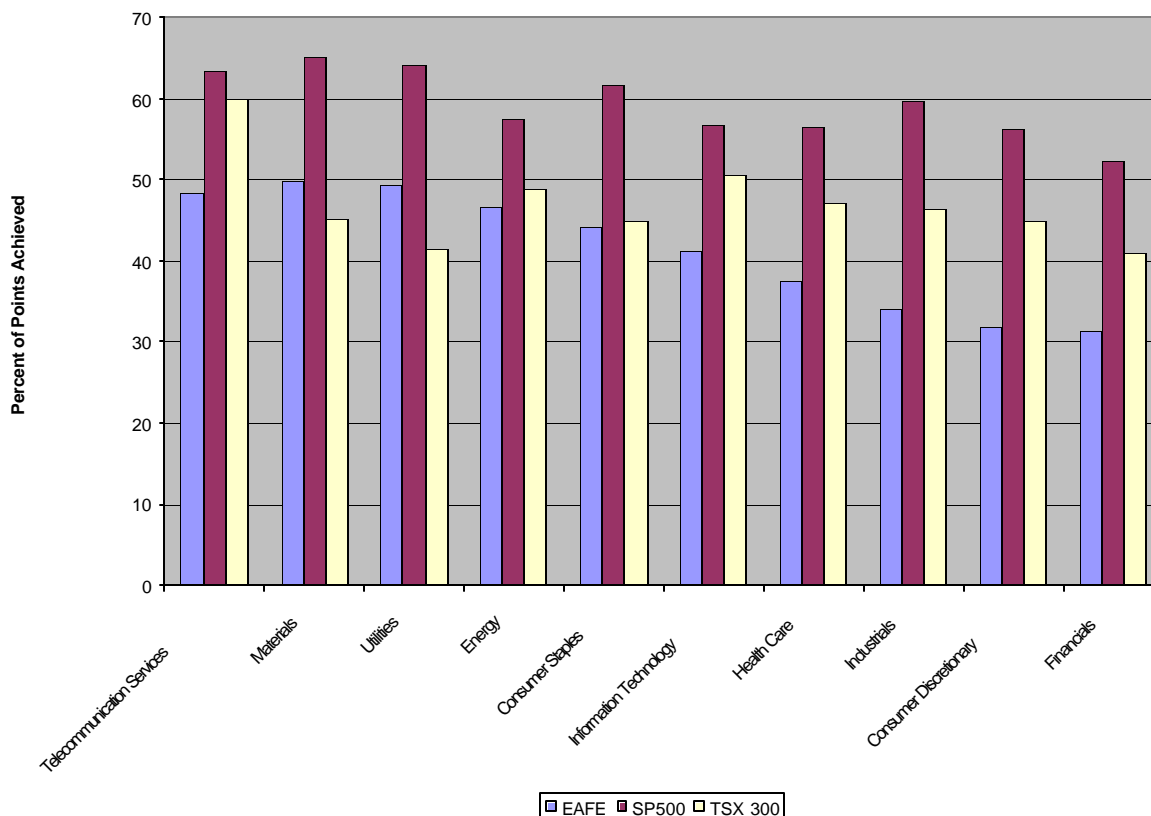
Environment Performance by Index



Labor & Human Rights by Index



Ethics by Index



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