



# **Investment Solutions for a World in Jeopardy: The Financial Sector**

Robert Howell July 2010

## Overview

- International financial system, fraudulent and corrupt, does not take deposits and lends it to produce goods and services that benefit society
- Regulation not adequate to deal with ecological decay
- Need to use SANZ global drivers for risk
- 3 case studies: Portfolio21, Westpac, HSBC
- Major reform of our financial system needed



## Failure of the Dominant Financial Model

- The free market has failed both conceptually and practically
- A regulated market is not sufficient to significantly change environmental degradation
- Weak sustainability: economic, social and environmental factors are considered
- Strong sustainability: the resilience and capacity of ecological systems to support human life is necessary
- Change in values: from utilitarianism and a version of the Lockean social contract, to notions like equity and integrity that cover both human-human and human-Earth relations.



# Inadequate Reform Proposals

- The majority of international standards and benchmarks are inadequate
- The SRI model has criteria so loose that it permits unethical behaviour and investment that contributes to ecological degradation
- UN principles for climate change, and the UN PRI are based on weak sustainability. Equator principles are inadequate.  
[Norway SWF excludes Rio Tinto – severe environmental damage]



# Europe

**Core [3.4%]**

Ethical exclusion

Best in Class

Other Positive Screens

Subtotal € 511 bill 19%

**Broad [14.2%]**

Simple \*

Engagement

Integration

Sub Total € 2154 bill 81%

Total € 2.665 trill

[17.6% of European Asset Management Industry]

\*Simple = Weapons €656, Norms based €402, Tobacco €17.5



# USA

## *Social Investment Forum USA*

11% of \$27.1 trillion under professional management is SRI (2007)

Tobacco 88%,  
alcohol 75%,  
gambling 23%  
(2005 study)



## 3 – 4°C scenario (Lynas)

- *Glacier and snow-melt in the world's mountain chains depletes freshwater flows to downstream cities and agricultural land. Most affected are California, Peru, Pakistan and China.*
- *Global food production is under threat as key breadbaskets in Europe, Asia and the United States suffer drought, and heatwaves outstrip the tolerance of crops.*
- *The Gulf Stream current declines significantly. Cooling in Europe is unlikely due to global warming, but oceanic changes alter weather patterns and lead to higher than average sea level rise in the eastern US and UK.*



## 4 – 5°C scenario (Lynas)

- *Another tipping point sees massive amounts of methane - a potent greenhouse gas - released by melting Siberian permafrost, further boosting global warming.*
- *Much human habitation in southern Europe, north Africa, the Middle East and other sub-tropical areas is rendered unviable due to excessive heat and drought.*
- *The focus of civilisation moves towards the poles, where temperatures remain cool enough for crops, and rainfall - albeit with severe floods - persists.*
- *All sea ice is gone from both poles; mountain glaciers are gone from the Andes, Alps and Rockies.*



# Global Drivers - SANZ

- population growth
- climate change
- price rises in hydrocarbon (oil, coal, natural gas)
- water
- food
- air and water-borne toxins
- geopolitical shifts and disruptions
- wide swings in economic activity
- advances in technology



# Global Drivers - SANZ

- There will be complex interactions between all of these change drivers
- All are subject to uncertainty about timing and magnitude
- Changes will be outside the range of prior human experience in terms of magnitude, speed of arrival, and simultaneity





# Investment Criteria

- investing in a smaller number of companies
- taking a larger stake,
- a longer-term perspective will be taken (hence avoiding a short term requirement of regular high dividends).
- how aware management is of the major global drivers
- how they are incorporating these into their strategic plans
- companies have calculated their ecological impact
- the Daly formulae or Natural Step

# Case Studies: Portfolio21

- Portfolio21 is based in Oregon, USA
- \$322 million in assets in 105 companies
- philosophy is based on ecological economic principles (Natural Step) 😊
- risk analysis takes into account SANZ global drivers 😊
- recognise that there are no truly sustainable companies 😊
- actively engages 😊
- use of UN standards 😞
- very transparent 😊



## Case Studies: HSBC

- HSBC is one of the largest banking and financial services organisations in the world
- market capitalisation of US\$114 billion and assets of US\$2,527b
- HSBC has around 9,500 offices and 325,000 employees in 86 countries and territories



# Case Studies: HSBC

<a href="#"><u>HSBC Holdings</u></a>	92
<a href="#"><u>Bank of Montreal</u></a>	87
<a href="#"><u>Simon Property Group</u></a>	86
<a href="#"><u>Hammerson</u></a>	84
<a href="#"><u>Allianz</u></a>	83
<a href="#"><u>Australia and New Zealand Banking Group</u></a>	82
<a href="#"><u>National Australia Bank</u></a>	82
<a href="#"><u>Commonwealth Bank of Australia</u></a>	81
<a href="#"><u>Aviva</u></a>	80
<a href="#"><u>Lloyds Banking Group</u></a>	80
<a href="#"><u>Westpac Banking</u></a>	80
<a href="#"><u>Allstate</u></a>	79

Financials on the Carbon Disclosure Project





## Case Studies: HSBC

- setting up research teams ☺
- partnering with NGOs ☺
- committing to Climate Principles ☺ ☹?
- establishing a Climate Change Benchmark Index ☺
- mitigation now is not sufficient adaptation is required, particularly for developing countries ☺



## Case Studies: HSBC Policy

- Chemicals ☹️
- Defence 😊
- Energy ☹️
- Forest Land and Forest Products 😊
- Freshwater Infrastructure ☹️
- Mining and Metals ☹️



## Case Studies: Westpac

- Westpac is the largest bank in Australia
- second-largest bank in New Zealand
- seven South Pacific nations
- assets of \$590 billion, 34000 employees, 10 million customers
- early leader of Aussie banks 😊



## Case Studies: Westpac

- definition of sustainability = managing what matters ☹️
- risk ≠ SANZ global drivers ☹️
- no public policy (working on water) ☺️ ☹️
- some risk in credit manual ☺️ ☹️
- no climate change risks in mortgage polices ☹️
- no encouragement of clean tech investments. ☹️
- recognises that more work is needed ☺️

# Ceres survey of 40 major banks

- 16 US and 24 non-US = 60% market capitalisation
- only 14 banks have adopted risk management policies or lending procedures that address climate change in a systematic way
- only a half-dozen banks calculating carbon risk in their loan portfolios
- one of the 40 banks—Bank of America—has announced a specific target to reduce the rate of greenhouse gas emissions associated with the utility portion of its lending portfolio.
- no bank has set a policy to avoid investments in carbon-intensive projects such as coal-fired power plants.



# Banktrack: *Close the Gap*

0 = no policy; 1= voluntary; 2= vague, no commitments 3= half of essential elements  
4 = essential; 5= essential +

	<b>0s</b>	<b>1s</b>	<b>2s</b>	<b>3s</b>	<b>4s</b>
ANZ (ANZ, National, INGNZ)	5,	10,	3		
Commonwealth (ASB)	10,	8			
HSBC	2,	13,	1,	1,	1
ING	4,	9,	3,	2	
National Australia (BNZ)	9,	7,	2		
Rabobank	2,	5,	9,	2	
Westpac	6,	9			



# Implications

- Investors seek a system that identifies risk and gives fair protection and return
- We need a system that does not destroy our environment
- There is a need for principles, standards, and scoring systems that are valid, and are not just 'greenwash'.
- Bank policies do not adequately deal with ecological risks (especially Australasian banks). They are not doing enough, and they are not doing it fast enough for Earth's resilience.



# Reform Models

- Global Alliance for Banking and Values
- Started by BRAC in Bangladesh, Shorebank in the US, and Triodos Bank in the Netherlands
- Still very small in numbers and size.



# Implications

- Need to rethink banking basics: who and how we make money. Von Uexküll asks

*“Does it really make sense that our sovereign governments should have to borrow the funds needed to protect our common future from private moneylenders, who create this money themselves from fractional reserve banking, and whom we as citizens and taxpayers have just rescued from bankruptcy?” (Girardet and Mendonca, 2009).*

- If we are to move investment so that it saves rather than destroys our planet, we need to fundamentally reform our financial system.

