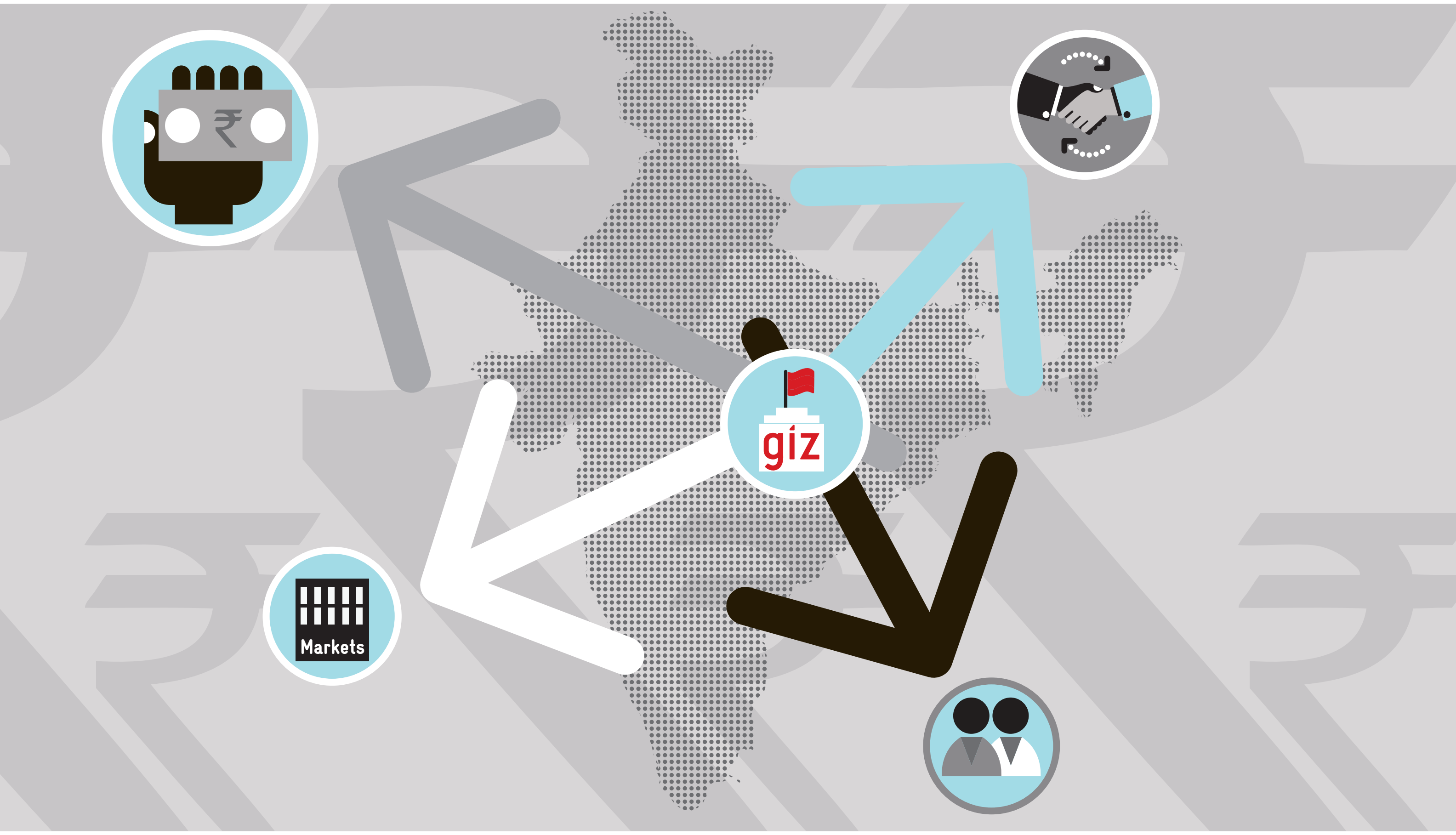

Responsible Finance – A Catalyst for Responsible Business

International and Indian Trends and Challenges in Responsible Finance

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International and Indian Trends and Challenges in Responsible Finance

Deutsche Gesellschaft für Internationale Zusammenarbeit (GIZ) GmbH

BMZ Bundesministerium für wirtschaftliche Zusammenarbeit und Entwicklung

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Abbreviations Index

ADB	Asian Development Bank
AGM	Annual General Meeting
ANBC	Adjusted Net Bank Credit
ANDE	Aspen Network of Development Entrepreneurs
ASrIA	Association for Sustainable & Responsible Investment in Asia
ASX	Australian Securities Exchange
AUM	Assets Under Management
AVPN	Asian Venture Philanthropy Network
AXENV	NYSE Arca Environmental Services Index
BEE	Bureau of Energy Efficiency
BEI	Banking Environment Initiative
BMV	Bolsa Mexicana de Valores
BOP	Bottom of the Pyramid
BSE	Bombay Stock Exchange
BSE-GREENEX	Bombay Stock Exchange Green Index
CalPERS	California Public Employees' Retirement System
CalSTRS	California State Teachers' Retirement System
CDC	Commonwealth Development Corporation
CDLI	Carbon Disclosure Leadership Index
CDP	Carbon Disclosure Project
CEE	Centre for Environmental Education
CII	Confederation of Indian Industry
CNX	CRISIL NSE Exchange/Index
CPSE	Central Public Sector Enterprise
CRISA	Code for Responsible Investing in South Africa
CRISIL	Credit Rating and Information Services of India Ltd.
CSR	Corporate Social Responsibility
CSRI	Corporate Social Responsibility Initiative
CTIUS	NYSE Arca Cleantech Index
DFI	Development Finance Institution
DFID	Department for International Development
DJSI	Dow Jones Sustainability Index
E&S	Environmental & Social
ECO	NYSE Arca WilderHill Clean Energy Index
EDFI	European Development Finance Institution
EEO	Equal Employment Opportunity
EEP	Esty Environmental Partners (USA)
EIRIS	Ethical Investment Research Service
EPFI	Equator Principles Financial Institutions
EPs	Equator Principles
ESG	Environmental, Social and Governance
ESP	Environmental and Social Policy
EU	European Union

EUR	Euro
EURO SIF	European Sustainable Investment Forum
FETA	Federation of Environmental Trade Associations
FIEG	Financial Inclusion Experts Group
FSSS	Financial Services Sector Supplement (GRI)
G 20	Group of Twenty Finance Ministers and Central Bank Governors
GBP	Abbreviation for the British pound sterling
GDP	Gross Domestic Product
GEPF	Government Employees Pension Fund (South Africa)
GHG	Greenhouse Gas
GIIN	Global Impact Investing Network
GIIRS	Global Impact Investing Rating System
GIZ	Deutsche Gesellschaft für Internationale Zusammenarbeit
GPFI	The Global Partnership for Financial Inclusion
GRI	Global Reporting Initiative
GSBI	Global Social Benefit Incubator
GSFN	Global Sustainable Finance Network
HDFC Bank	Housing Development Finance Corporation Bank
HNI	High Net Worth individual
IBA	Indian Banking Association
ICRW	International Centre for Research on Women
IDBI	Industrial Development Bank of India (IDBI)
IDFC	Infrastructure Development Finance Company
IDX	Indonesian Stock Exchange
IFC	International Finance Corporation
IFI	International Financing Institution
IGCC	Investor Group on Climate Change
IIGCC	The Institutional Investors Group on Climate Change
IIIF	India Inclusive Innovation Fund
IIM	Indian Institute of Management
IIRC	International Integrated Reporting Committee
IL&FS	Infrastructure Leasing & Financial Services Ltd.
INCR	Investor Network on Climate Risk
IRDA	Insurance Regulatory and Development Authority (India)
IREDA	Indian Renewable Energy Development Agency
IRIS	Impact Reporting & Impacting Standards
ISE	International Securities Exchange
J&K Bank	Jammu & Kashmir Bank
JICA	Japan International Cooperation Agency
KfW	Kreditanstalt für Wiederaufbau
LGT-VP	Liechtenstein Global Trust Venture Philanthropy
LIC	Life Insurance Company
MCA	Ministry of Corporate Affairs (India)

MFW	Marketing Fund for Women
MNRE	Ministry of New and Renewable Energy (India)
MoEF	Ministry of Environment and Forest (India)
MoF	Ministry of Finance (India)
MoMSME	Ministry of Micro, Small and Medium Enterprises (India)
MSCI	Morgan Stanley Capital International
MSMEs	Micro, Small and Medium Sized Enterprises
MUN	Mahila Udyam Nidhi
MVN	Mahila Vikas Nidhi
NAB	National Australia Bank
NAPCC	National Action Plan on Climate Change
NASDAQ	National Association of Securities Dealers Automated Quotations
NBIM	Norges Bank Investment Management
NGO	Non- Governmental Organization
NIC	National Innovation Council (India)
NIFTY	National Stock Exchange's Fifty
NPS	National Pension Scheme
NPV	Net Present Value
NSE	National Stock Exchange
NVG	National Voluntary Guidelines
NYSE	New York Stock Exchange
OMIGSA	Old Mutual Investment Group (SA)
OMX	Helsinki Stock Exchange
PFRDA	Pension Fund Regulatory and Development Authority (India)
PiC	Partners in Change
PIIF	The Principles for Investors in Inclusive Finance
PPF	Public Provident Fund
PRI	Principles of Responsible Investment
RBI	The Reserve Bank of India
RBS	Royal Bank of Scotland
S&P	Standard & Poor's
SAM	Sustainable Asset Management
SARCI	Saudi Arabian Responsible Competitiveness Index
SBI	The State Bank of India
SEBI	Securities and Exchange Board of India
Si2	Sustainable Investments Institute
SIDA	Swedish International Development Cooperation Agency
SIDBI	Small Industries Development Bank of India
SME	Small and Medium sized Enterprises
SPS	Safeguard Policy Statement
SRI	Socially Responsible Investment
SRISTI	Society for Research and Initiatives for Sustainable Technologies and Institutions
SSB	Standard Setting Body

SSE	Shanghai Stock Exchange
SSP	Swayam Sikshan Prayog
TCTS SA™	Teach Children to Save South Africa™
TEEB	The Economics of Ecosystems and Biodiversity
UBS	Union Bank of Switzerland
UK SIF	United Kingdom Sustainable Investment Forum
UN	United Nations
UNCTAD	United Nations Conference on Trade and Development
UNEP	United Nations Environment Programme
UNEP FI	United Nations Environment Programme Finance Initiative
UNGC	United Nations Global Compact
UN PIFF	United Nations Principles for Investors in Inclusive Finance
UNPRI	United Nations Principles of Responsible Investment
US SIF	United States Sustainable Investment Forum
USAID	United States Agency for International Development
VÖNIX	VBV-Österreichischer Nachhaltigkeitsindex
WBCSD	World Business Council for Sustainable Development
WFDFI	World Federation of Development Financing
WIF	World Investment Forum
WRI	World Resources Institute

Executive Summary

Global sustainable development challenges such as climate change or poverty cannot be addressed without Responsible Finance – finance that integrates social, environmental and governance concerns into the lending and investment decision making of financial institutions. Responsible financial systems can contribute to the goal of sustainable economic development through promoting business innovation and strengthening economic, environmental and social responsible behavior of businesses. Businesses need access to capital, credit or equity to expand and grow their businesses. By setting the right incentives through non financial lending and investment criteria, the financial sector acts as a 'multiplier' of responsible business practices and sustainable economic development. Consequently, Responsible Finance cannot be decoupled from the responsible business agenda as ultimately Responsible Finance is a means to the end of responsible business.

This study sets out a series of major Responsible Finance trends and identifies a number of key challenges and barriers for its further integration. The study is aimed at those interested in learning about the status quo, trends and drivers influencing business practices through lending and investment decisions in the financial sector internationally and in India. It is has been financed by the German Ministry of Economic Cooperation and Development (BMZ) through the Sector Project Financial Systems Development and bilateral technical cooperation in the field of Private Sector Development in India, implemented by GIZ.

It defines Responsible Finance as a broad umbrella term for a bouquet of strategies employed by financial institutions involving the integration of environmental, social and governance (ESG) criteria and metrics into financial lending and investment decision making. The three categories of Responsible Finance considered in this study are: Sustainable/Responsible Lending, Sustainable/Responsible Investment, and Impact Investing.

- **Sustainable/Responsible Lending:** Refers to the practices of retail lenders and corporate financiers' (investment banks) to apply environmental, and/or social criteria in their lending decision making, the latter specifically in their project financing decisions.

- **Sustainable/Responsible Investment:** Refers to the incorporation of environmental, social and governance (ESG criteria) into investment decision making by investors.

- **Impact investment:** Refers to an investment approach by a new breed of venture capitalists and angel investors at the start up or early stage of a business's development. In providing early stage financing impact investors aim to maximize social and environmental impacts alongside financial returns with their investments.

The trends, challenges and recommendations in this study are based on extensive stakeholder engagement and desk based research. Over 35 interviews with international and India based stakeholders from the sector were conducted in December 2011 and January 2012; in addition, the study builds on two multi-stakeholder consultation events with representatives over 240 investor and banking stakeholders undertaken by GIZ earlier in 2011 in Mumbai, India. The report concludes with recommendations for GIZ's future engagement on this agenda.

The key findings are outlined in the following boxes:

International Responsible Finance Trends

- Recognition of the Business Case for Responsible Finance
- International Commitment by the Financial Institutions to Responsible Finance
- Governmental and regulatory drivers of ESG management and disclosure
- Increasing Stock Exchange Listing Requirements
- Translating a Commitment into ESG Policies
- Implementing Practices to manage operational and portfolio impacts
- Disclosing Policies, Practices and Performance
- Measuring, Rating and Rewarding Performance
- Increased interest in impact investing
  - A new asset class
  - Geographic Focus on emerging markets
  - Thematic focus on a number of key sector such as health and education
  - Impact measurement and engaged investing

Responsible Finance Challenges and Barriers

- Lack of disclosure and data availability
- Data quality and comparability, standardization of metrics and impact
- Assurance of data
- Lack of researc h on business case and business case recognition by banks and investors
- Thematic blind spots of risks and opportunities
- Lack of measurement tools
- India specific challenges include:
  - Lack of awareness, understanding, commitment and capacity
  - Lack of engagement by the media and other stakeholders
  - A focus on operational impacts by banks rather than portfolio impacts
  - Non-compliance
  - Shareholding patterns and lack of engagement by domestic insurance and pension funds

Impact investing specific challenges

- Information asymmetry and lack of a pipeline
- Capacity and investment readiness
- Lack of seed funding
- Lack of local capital
- Transaction costs
- Scalability
- Defining impact and performance
- Exits

1 Introduction

In the wake of the financial crisis regulators, governments and NGOs are calling for greater responsibility and accountability by financial service providers to create *'more transparent, inclusive and equitable financial markets'* and to contribute towards the promotion of responsible business and sustainable economic development.[1]

Responsible Finance cannot be decoupled from the responsible business agenda. Whether it is accessing debt or equity all companies, both big and small, sooner or later require cash injections from the financial system to start up, grow and mature. Financial institutions have considerable influence over companies in their twin functions as financial service providers and investors. Consequently, they can play a key role in promoting responsible business by serving as 'multipliers' or 'catalysts' for improving social and environmental practices and performance of companies.[2] In doing so, responsible financial systems provide scope for increased equity and opportunity for both business and society as well as to poverty reduction and the goal of sustainable economic development.[3]

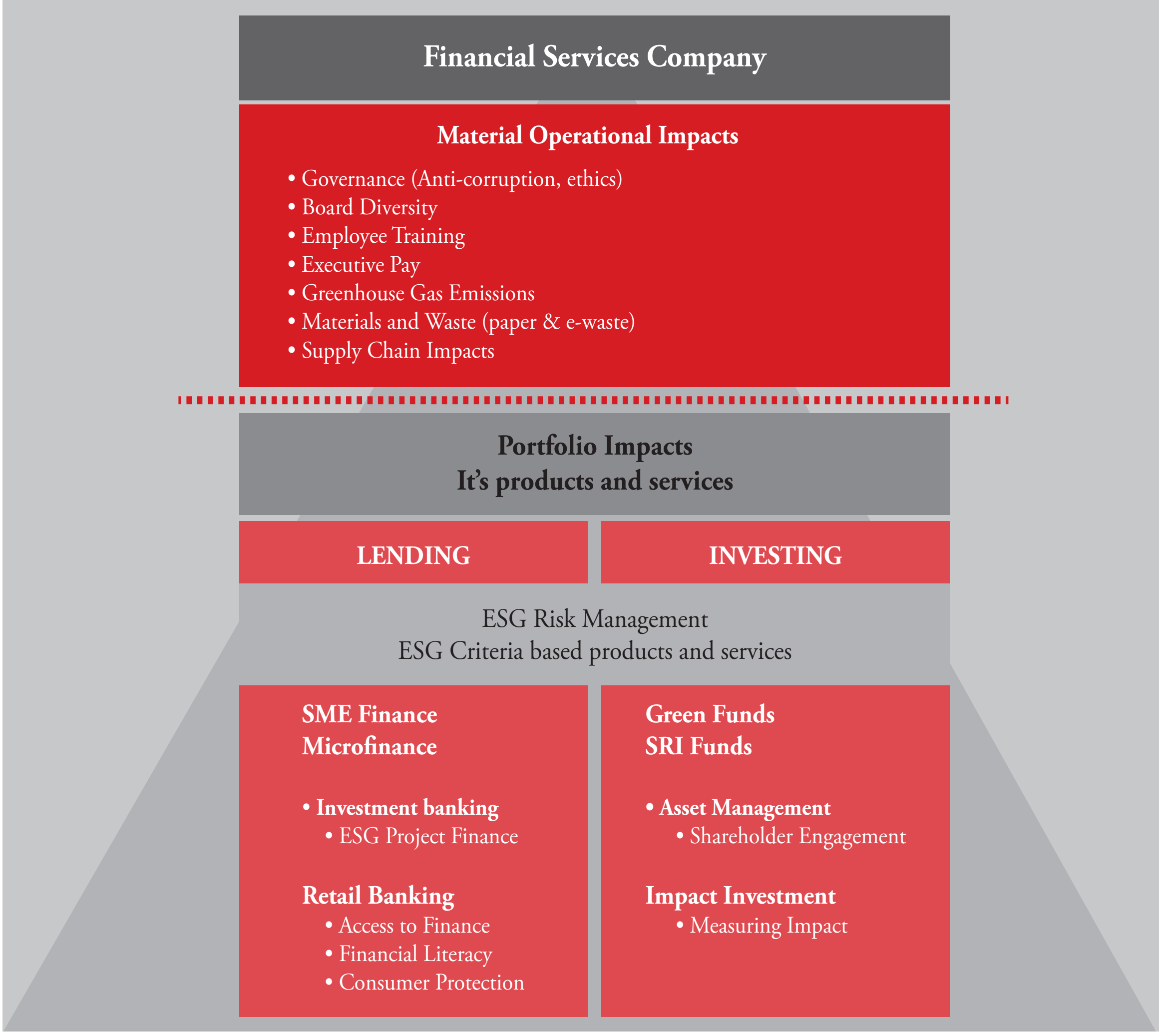
The way financial institutions exert this influence is what this paper refers to as Responsible Finance. As such, Responsible Finance is a broad umbrella term that is used to refer to a bouquet of strategies employed by financial institutions involving the integration of environmental, social and governance (ESG) criteria and metrics into financial lending and investment decision making. Both banks and investors apply ESG criteria both from a risk and opportunity perspective in recognition that these non financial factors also contribute to long term financial returns and sustainable economic development. The extent to which criteria are applied differs from institution to institution, as do expectations regarding company performance. What financial institutions identify as risks and opportunities, and the choices they make in how finance is deployed, has the scope to drive and influence the behavior of companies dependent on their finances.

As a term Responsible Finance is used by sector stakeholders to refer to the operational environmental, social and economic impacts of the financial institution and how these are effectively managed. These impacts can include sector specific risks and opportunities, such as board gender diversity, executive payment as well as environmental issues such as greenhouse gas emissions and waste generation. See figure 1 that illustrates the differential impacts of a financial services company, between its operational impacts and those it incurs in its lending and investment activities.

The trends in strategies employed in Responsible Finance are generally subcategorized by stakeholders on the basis of the different types of financing activities. The main categories of Responsible Finance include:

Sustainable/Responsible Lending: this refers to the practices of retail lenders and corporate financiers' (investment banks) to apply environmental, and/or social criteria in their **lending** decision making, the latter specifically in their project financing decisions. These criteria are set out in specific policies which may be applied across all their lending decisions. In addition, there may be additional policies or criteria for individual products or services that a client must adhere to in order to qualify for a loan.

Figure 1 To Illustrate the Differential Impacts of a Financial Services Company



Responsible lending also encompasses the financial inclusion agenda focusing on access to finance for 'priority sectors' including individuals from specific socio-economic backgrounds, microfinance, small and medium enterprises (SMEs), and financing efforts focusing on different segments such as rural communities and women entrepreneurs. It also includes physical access to finance, financial literacy, and consumer protection. In this context it focuses on how banks protect consumers, and build financial capability to ensure financial inclusion of the poor and vulnerable.

Sustainable/Responsible Investment: This refers to the incorporation of environmental, social and governance (ESG criteria) into **investment** decision making by investors. Both mainstream investors and the specialist Socially Responsible Investment (SRI) community use similar strategies, yet apply differing levels of priority on specific ESG criteria during the process when they deciding on what companies to buy shares/equity in.

The strategies employed can involve **negative screening**, which is the avoidance of investment in targeted companies, industries and countries, or **positive screening** to proactively seek to invest in companies with a commitment to responsible business practices, or that produce responsible products and/or services. Positive screening is used to select the best in class within a sector, based on specific environmental and/or social practices and performance.[4] In doing so, investors take a call on whether they think that these factors present either risks or opportunities to the company and will negatively or positively impact the share price of a company in the long term.

The term SRI also refers to activities employed by investors after an investment has been made. It includes shareholder **engagement/advocacy and voting** to promote positive change by challenging management when irresponsible practices are taking place. Essentially, engagement is the active use by investors of their rights to influence companies. This includes exercising their voting rights on stocks in the portfolio of their investment funds, which is recognized to be part of a well functioning corporate governance system. Sometimes voting is referred to as proxy voting, which is when investors use an electronic voting platform to cast their vote rather than attending the annual general meeting (AGM) in person to avoid unnecessary costs and to increase the efficiency of the voting services.[5] [6] Other approaches taken by investors to talk with companies on issues of social, environmental or governance concerns include filing, and co-filing shareholder resolutions, for example, on climate change issues, which are then, in turn, presented for a vote to all owners of a corporation.[7] The idea behind these engagement- and voting activities is to increase the long term value of the company for its shareholders and its other stakeholders.[8] Where the investor is unhappy with the continued practices of the company it is invested in, it may in turn 'divest' its shares.[9]

Impact investing: This refers to an investment approach by a new breed of venture capitalists and angel investors at the start up or early stage of a business's development. In providing early stage financing impact investors aim to maximize social and environmental impacts alongside financial returns with their investments.[10] [11] The process of impact investing is commonly referred to as the deployment of so-called 'patient capital' into social enterprises and inclusive business models that focus on wealth creators and producers at, or serving, the bottom of the pyramid (BOP).

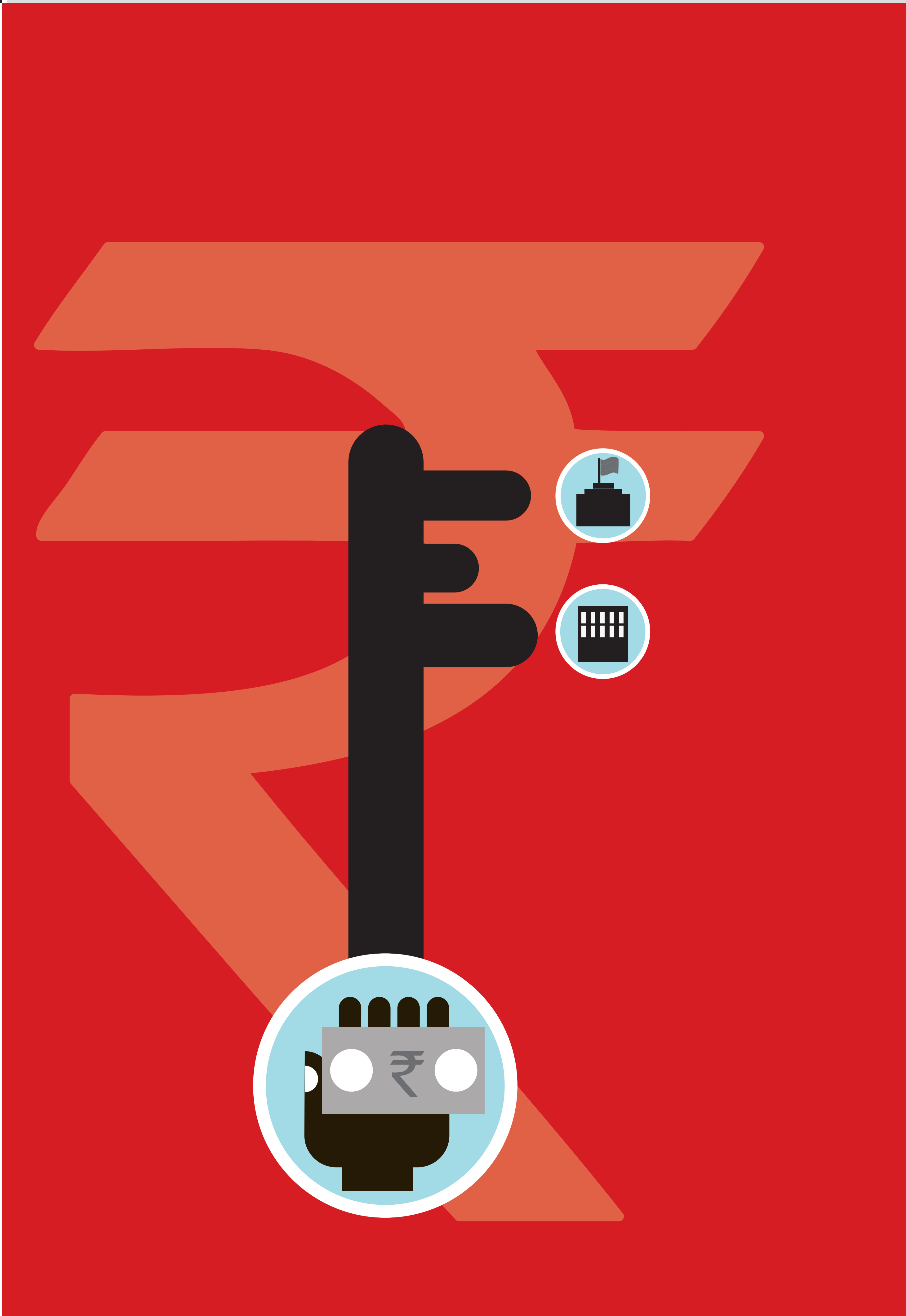
Some refer to it as an investment approach that has a greater tolerance for risk than traditional investment; as well as having longer time horizons for the return of capital. The extent to which this category of investor focuses on impact first or returns can differ, as do the criteria applied.

As part of its ongoing commitment to private sector development, GIZ has undertaken this research to understand the key international trends and Indian context for Responsible Finance. In addition, to establish the trends in the current practices of banks and investors in India to integrate ESG concerns into their lending and investment decision making. This study is based on the premise that a sustainable approach to financing not only promotes responsible business, and sustainable development, but that it is also a strategic value creator. It aims to not only understand the landscape within India but also the role GIZ could play in encouraging improved ESG integration by the sector in India.

This publication is based on desk based research and a stakeholder consultation with 35 individuals representing a range of different stakeholder groups with an interest in Responsible Finance based in India and internationally. Furthermore, it builds on two previous multi-stakeholder consultations undertaken by GIZ involving over 230 stakeholders. The first dialogue was held on the theme of Responsible Investment in partnership with the Global Reporting Initiative (GRI) in Mumbai on 19 January 2011 and subsequently, a high-level conference in partnership with the Small Industries Development Bank (SIDBI) for Indian banks and banks active in India on Non-Financial Reporting and Risk Management took place in Mumbai on June 6, 2011. Enriched by this research, this study seeks to complement and build on existing research in the field from an Indian perspective to build awareness and support the global business case for Responsible Finance.

Footnotes

1 Responsible Finance Forum, 2011
2 Responsible Finance Forum, 2011
3 Responsible Finance Forum, 2011
4 *http://ussif.org/resources/sriguide/srifacts.cfm*
5 *http://www.robeco.com/eng/about_robeco/responsible_investing/voting/voting_by_proxy.jsp*
6 *http://www.robeco.com/eng/about_robeco/responsible_investing/voting/index.jsp*
7 *http://ussif.org/resources/sriguide/srifacts.cfm*
8 *http://www.robeco.com/eng/about_robeco/responsible_investing/engagement/index.jsp*
9 Business for Social Responsibility, 2008
10 Acumen Fund,2011
11 JP Morgan & GIIN,2011



2 Key Stakeholders in Responsible Finance

There are a broad range of financial and non financial stakeholders that are active in the field of Responsible Finance each of them having their own interests in its promotion and implementation depending on their role in this complex system. As background information for those new to the theme of Responsible Finance, this chapter briefly summarizes the interests of each key type of stakeholder, as well as highlights key organizations within these categories, operating internationally and/or in India. The information detailed about the different categories or stakeholders and their interests, as well as the organizations listed in the reference table in the appendix, primarily result from the stakeholder engagement process, complemented by desk research.

The key categories of stakeholders include:

Academics

Academic institutions are focused on conducting research on the topic of Responsible Finance and business. Research is often from either a corporate or development perspective and can explore issues such as inclusive financing and business models, sustainability investor strategies and the business case for sustainability.

Examples include: Initiative for Responsible Investment, The Hauser Centre for Non Profits, at Harvard Business School, USA.

Asset Owners and Asset Managers

Asset owners are the owners of capital to invest. These can be institutional investors, which include pension funds, foundations and insurance companies, or retail investors. All of these types of investors are interested in Responsible Finance from the perspective of managing the ESG risks that may erode their assets if not effectively managed. This is particularly relevant to insurance and pension funds with extended investment horizons and may be exposed to the longer term risks of climate change and water scarcity. In addition, these investors consider ESG opportunities as a way to get better returns for their capital.[12]

Asset managers act as intermediaries on behalf of the asset owner and seek to ensure that the value of capital is maintained. With the increasing recognition of impact of ESG factors on financial performance, asset owners may mandate asset managers to consider non financial criteria in their decision making process. In addition, there are specialist asset managers often referred to as SRI investors that specialize in responsible investment.[13]

Examples include: Sustainable Asset Management (SAM), Switzerland & Pax World, USA, Government Pension Fund Global, Norway, Life Insurance Company (LIC) India.

Banks

Retail and investment banks accept deposits from clients, and channel those deposits into lending activities, either directly or through capital markets. They are generally subject to minimum capital requirements which are based on an international set of capital standards, known as the Basel Accords. Within India, there are a number of categories of banks: Public sector- these are listed in the stock exchanges NSE and BSE but the government of India holds majority stake in these banks; private sector banks; and foreign banks.[14] These different types of banks are interested in Responsible Finance in their lending decision making to manage their environmental, social and governance risks, as well as focusing on their operational non financial impacts, such as the GHG emissions from their branches.

Examples include: Small Industries Development Bank (SIDBI), India and HSBC, UK.

Bilateral Agencies and Development Finance Institutions

Bilateral agencies are government departments or agencies that work on behalf of the government that provide development assistance to partner countries, selected on the basis of the needs of the recipient country and a combination of development priorities and national interests of the donor country. Areas of work include private sector development, strengthening of capital markets, or small- and medium-size enterprise development. Some donors and implementing agencies are increasingly devoting efforts to promoting responsible business practices and Responsible Finance, such as in the case of GIZ on behalf of the German Federal Ministry of Economic Cooperation and Development (BMZ).[15] [16] Some bilateral donors have Development Finance Institutions such as CDC, which is wholly owned by the UK Government's Department for International Development (DFID).[17]

Examples include: BMZ/GIZ, Germany and DFID, UK.

Business Consultants

Consultants advise clients on a broad range of issues including on non financial risks and opportunities and Responsible Finance strategies such as the creation of ESG policies. Mainstream business advisory as well as boutique sustainability agencies and risk consultants are all active in this field.

Examples include: Ernst & Young, and Mercer.

Governments

Government refers to the political institutions and ministries that formulate and enforce the national policy related to Responsible Finance and create the policies for the regulators of the financial markets in a country to implement. They are active in creating voluntary or mandatory requirements related to Responsible Finance and business more broadly or on thematic risks or opportunities such as related to energy and carbon.

Examples include: Ministry of Corporate Affairs, Government of India.

Impact Investors

Impact investors are investors intending to create positive impact beyond financial return. As such, they require the management of social and environmental performance (for which early industry standards are gaining attraction among pioneering impact investors) in addition to financial risk and return. They focus on start up or early stage financing to enterprises that are not publicly traded on a stock exchange. Impact investors are part of the private equity industry and the investments provide working capital to a company to grow its business.

Examples include: The Acumen Fund, Aavishkaar, India Unlimited

Multilateral Agencies

Multilateral agencies such as the United Nations represent groups of governments but enjoy an independent legal and operational status.[18] As they work to promote international collaboration on sustainable development, Responsible Finance and business are cross cutting themes that are addressed in their public statements, policies, and programmes.

Examples Include: UN Principles for Responsible Investment, UNEP Finance Initiative, World Bank and IFC.

NGOs

Responsible Finance is on the agenda of a number of non-governmental organizations (NGOs). These organizations actively work with civil society to promote issues related to sustainable development, inclusive business models and sustainable private sector development. Some NGOs work on corporate transparency and accountability issues and are actively engaging on issues related to Responsible Finance.

Examples include: The Global Reporting Initiative (GRI), Carbon Disclosure Project (CDP).

Regulators

A regulatory agency (also regulatory authority, regulatory body or regulator) is a public authority or government agency responsible for exercising autonomous authority over some area of activity in a regulatory or supervisory capacity. They may include Responsible Finance or disclosure as a mandate over those companies that they supervise.

Examples include: Reserve Bank of India, the Insurance Regulatory Development Authority (IRDA), the Pension Fund Regulatory Development Authority (PFRDA) and the Securities and Exchange Bureau of India (SEBI).

Research and Data Providers

This group broadly encompasses a range of supporting institutions that provide monitoring services, market information and quantitative and qualitative research on the ESG practices and performance of companies. This may involve gathering media coverage of any controversies or other sources of data to inform the investment and lending decisions by asset managers and owners regarding the investment portfolios they manage or own. In some instances, these organizations also provide a third party ranking or rating of performances based on their own methodology or criteria provided by the client. These rankings are often in the form of ESG indexes, of which each has its own calculation methodology based on a range of financial and non financial parameters. Typically, these indexes rank the responsible business practices of a range of companies within a specific geography and/or sector on a broad range of sustainability parameters and/or single themes such as carbon management. These types of organizations can be NGOs, private companies or in some instances academic institutions.[19]

Examples include: Bloomberg, cKinetics, Dow Jones Sustainability Index

Business Associations

Networks of financial services providers, either banks or investors, focused on advancing the interests of their members, discuss issues related to Responsible Finance to set industry standards to inform and influence the agenda. There are groups of investors or banks in the industry that have formed to collaborate on responsible investment or banking themes, further research on the topic and advocate for increased awareness and change.

Examples include: Indian Banking Association (IBA), Confederation of Indian Industry (CII).

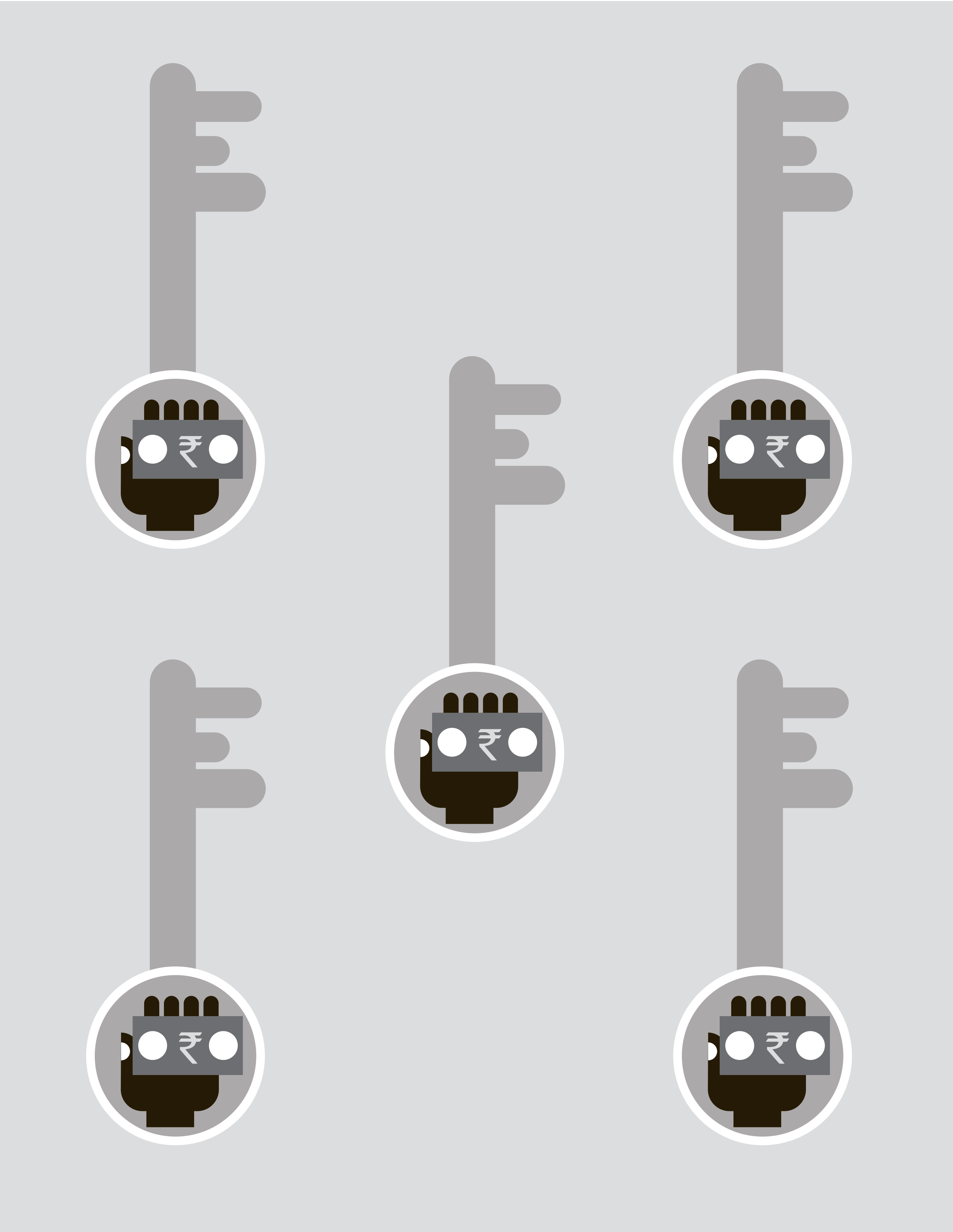
Stock Exchanges

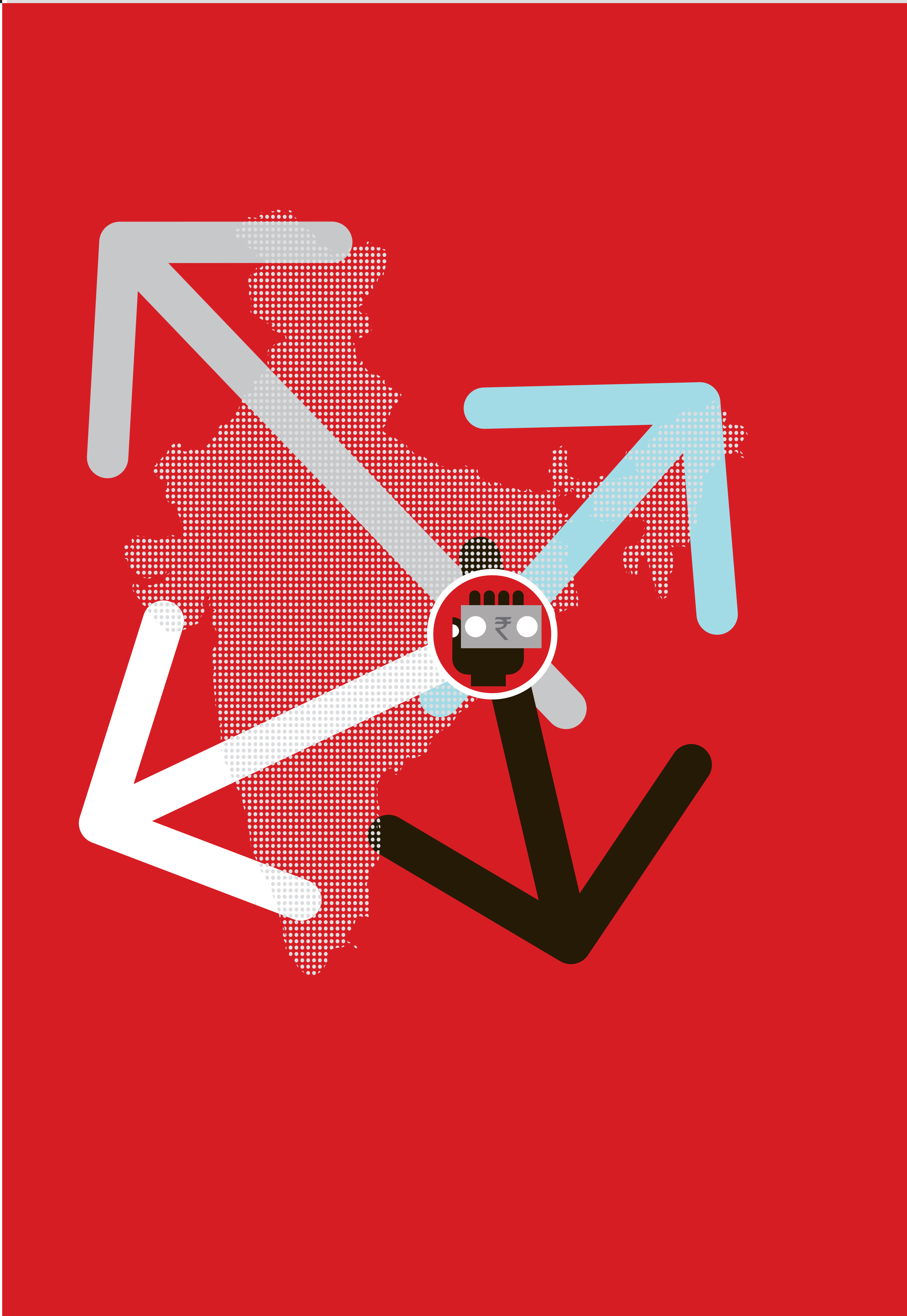
Stock exchanges are the market place of a financial system, where securities (bonds, notes, shares) are bought and sold at prices governed by the forces of demand and supply.[20] Stock exchanges can influence the corporate practice of the companies that use these exchanges to access capital by imposing listing requirements.[21]

Examples include: Bombay Stock Exchange (BSE), and BM&F BOVESPA, Brazil.

Footnotes

12 IFC, 2011
13 IFC, 2011
14 RBI, 1999
15 *www.responsible-business.in*
16 *http://www.wbcsd.org/web/projects/sl/type.htm#2*
17 *http://www.cdcgroup.com/who-we-are.aspx*
18 *http://www.wbcsd.org/web/projects/sl/type.htm*
19 IFC, 2011
20 *http://www.businessdictionary.com/definition/stock-exchange.html*
21 Responsible Research, 2010





3 International and Indian Trends

Financial factors are no longer widely regarded as the exclusive drivers of sustainable business growth and wider economic development. Instead, many companies and investors recognize the interdependency of financial performance and Environmental, Social and Governance (ESG) or sustainability performance.[22] [23] [24] [25] The management of external environmental and social risk factors, such as the guarantee of a sustainable energy supply, or a skilled and motivated workforce, is now acknowledged as important to achieve long term success and contribute towards business goals. In turn, companies have demonstrated that if these non financial factors and their impacts are managed effectively, they can confer clear benefits in terms of risk management, cost and efficiency savings, brand management and innovation opportunities.[26]

Emerging research highlights the economic value of sustainability, specifically the economic consequences of climate change, and biodiversity loss for business and society, as well as the value of other types of natural capital.[27] [28] [29] For example, even though financial institutions are not directly dependent on ecosystem services, they are exposed to Biodiversity Ecosystem Services risks through the loans, investments and insurance cover they provide to companies and projects. The financial services industry is starting to ask questions about biodiversity and ecosystems both from a risk and an opportunity perspective. Strategies employed include 'redlining' investments (redlining is the practice of arbitrarily denying or limiting financial services to specific neighborhoods) in areas of high biodiversity; developing sector guidelines for environmentally sensitive sectors; refraining from financing sectors in which a bank lacks specialist knowledge, and working with borrowers to improve their environmental performance and to mitigate harm.[30]

With this recognition of the business case for Responsible Finance , this chapter further strengthens the business case as it sets out a number of key trends and drivers for Responsible Finance both internationally and in India. The following trends were identified through stakeholder consultation and desk research.

> "The costs of acting to counter climate change, by stabilizing emissions of carbon dioxide in the atmosphere, might be about 1 per cent of annual global GDP by 2050. But the cost of doing nothing would be far greater – risking up to 20 per cent of the world's wealth.
>
> **Stern Review 2009**

> "The economic value of avoiding GHG emissions by conserving forests: US$ 3.7 trillion (NPV) and the economic value of species diversity specifically the contribution of insect pollinators to agricultural output is estimated to be ~ US$ 190 billion/year
>
> TEEB Report 2010

International Commitment by Financial Institutions to Responsible Finance

International

A notable trend is the significant increase in recent years in the number of signatories to a plethora of international commitments and declarations related to Responsible Finance. These commitments emphasize the recognition by their signatories of the link between environmental, social and governance factors and financial performance.

The UN backed Principles for Responsible Investment (see table 1) is recognized by stakeholders, as one of the main drivers of Responsible Finance agenda. It is a voluntary framework for investors committed to incorporate ESG criteria into their decision-making and ownership practices. The number of signatories has gone from 50 in 2006 to over 979 in 2010, which represents assets of over US$ 22 trillion.[31] Consulted stakeholders noted the UNPRI as a leading stakeholder in the field of Responsible Finance with 'strong brand value'.

The United Nations Environment Programme (UNEP) Statement of Commitment by Financial Institutions (FI) on Sustainable Development is of broader application to the sector with a total of 206 UNEP FI signatories representing banks, investment managers and insurance companies. It provides a focus for the financial sector to make a public commitment to sustainable development, and work collectively toward common sustainability goals, through sustainability management and public awareness and communication.[32]

Of significance to those banks involved in project finance are the **Equator Principles** (EPs). This is a credit risk management framework for determining, assessing and managing environmental and social risk in project finance transactions. These principles are based on the IFC Performance Standards[33] and are adopted by institutions voluntarily where total project capital costs exceed US$10 million.[34] Since its establishment with 16 Signatories in 2003, the EPs have seen adoption of the Principles rise to 73 in 2011.[35]

Table 1 Breakdown PRI Signatories by Type of Institution

Category	Number of signatories
Asset owners	246
Investment managers	572
Professional service partners	161
Total	979

Table 2 UNEP FI Signatories by Region

Region	Number of signatories
Africa	14
Asia Pacific	57
Europe	87
Latin America	22
Middle East	1
North America	25

The **Equator Principles (EPs)** are a credit risk management framework for determining, assessing and managing environmental and social risk in project finance transactions. Project finance is often used to fund the development and construction of major infrastructure and industrial projects. The EPs are adopted voluntarily by financial institutions and are applied where total project capital costs exceed US$10 million. They are primarily intended to provide a minimum standard for due diligence to support responsible risk decision-making.

Source: http://www.equator-principles.com/ Source: http://www.equator-principles.com/

UN Principles for Responsible Investment (UNPRI)

1. We will incorporate ESG issues into investment analysis and decision-making processes.
2. We will be active owners and incorporate ESG issues into our ownership policies and practices.
3. We will seek appropriate disclosure on ESG issues by the entities in which we invest.
4. We will promote acceptance and implementation of the Principles within the investment industry.
5. We will work together to enhance our effectiveness in implementing the Principles.
6. We will each report on our activities and progress towards implementing the Principles.

Source: http://www.unpri.org/principles/

Furthermore, there are thematic initiatives representing the commitment to manage environmental and social risks and opportunities. The **Carbon Disclosure Project (CDP)** is an NGO that requests information on greenhouse gas emissions, energy use and the risks and opportunities from climate change from thousands of the world's largest companies. Banks, pension funds, asset managers, insurance companies and foundations endorse the annual CDP climate change and water questionnaires used to gather relevant information from large corporations around the world.[36] In turn, this CDP data is used by investment managers and advisors, asset owners, data and index providers, banks and brokers among others, and is available through providers including Bloomberg, EIRIS, MSCI, Sustainalytics, Thompson Reuters and Trucost.[37] In 2011, 551 financial institutions with assets of US$71 trillion were signatories to the CDP.[38] Since then this number has increased and the CDP is now backed by more than 655 institutional investors representing in excess of US$78 trillion in assets.[39]

In addition, sector specific initiatives on climate change include the **Climate Principles**, which are adopted by financial institutions committed to actively managing climate change. This includes developing products and services that enable customers to manage climate change related risks and business opportunities. These Principles have also seen a significant interest from the sector, demonstrating their commitment to the issue with 29 climate principles signatories from the financial sector, globally.[40]

A similar thematic initiative has emerged on the theme of financial inclusion. **The Principles for Investors in Inclusive Finance** (PIIF) were launched in partnership with the UN backed Principles for Responsible Investment (PRI), in January 2011. More than 50 investors have signed up to these principles signalling their commitment to inclusive finance in their own investments, and supporting the actions taken by others in their value chains.[41 42] On a similar theme the banking industry has come together globally on the topic of financial inclusion for women in a group called the Global Banking Alliance for Women. This is a group of financial institutions working together to promote access to finance for women entrepreneurs, and publicly demonstrate their commitment on the theme.[43]

The most recent commitment by the financial sector is the launch of **The Natural Capital Declaration** with 3 initial signatories, demonstrating their commitment in the lead up to the Rio+ 20 Earth Summit to work towards integrating Natural Capital criteria into its financial products and services.[44 45]

Some of these thematic sector commitments are restricted to one geographic region. **The Institutional Investors Group on Climate Change (IIGCC)** is a forum for collaboration on climate change for European investors. The network brings investors together to use their significant collective influence to engage in dialogues with policymakers, investors and companies to accelerate the shift to a low carbon economy. There are currently over 75 members, including some of the largest pension funds and asset managers in Europe, representing around €7.5 trillion.[46] In North America there is a similar network, the **Investor Network on Climate Risk (INCR)** which represents 100 institutional investor members managing nearly $10 trillion in assets.[47] While in Australia and New Zealand another group called **The Investor Group on Climate Change (IGCC)** focuses on the impact that climate change has on the financial value of investments. This group has funds under management of approximately $700 billion.[48] Collaborating together these three groups came together with UNEP-FI and PRI to issue a **Global Investor Statement on Climate Change in 2011** which was supported by 285 investors that represent assets of more than US$20 trillion.[49]

New networks related to these themes are being created such as the **Global Sustainable Finance Network (GSFN)** is a voluntary membership based global initiative of the World Federation of Development Financing Institutions (WFDFI) that brings together financial institutions and other stakeholders committed to the advancement of sustainable finance.[50]

The Banking Environment Initiative (BEI) is a voluntary bank-client partnership organized by the University of Cambridge in the UK, which is working to 'identify ways in which banks can collectively redirect capital away from environmentally damaging activities towards sustainable, low carbon growth'. It has committed to 'develop a best practice methodology for integrating a carbon price into valuation models'.[51]

An analysis of the top 50 financial services companies by market capitalization indicates that 68 % of them have international commitments in the form of signatories to varied Principles. The most widely adopted are the CDP, with 31 signatories from the top 50; the Equator Principles with 26 signatories from the top 50, while the PRI has 4 signatories. What is notable is that they highlight a commitment by these financial sector institutions towards implementing policies, practices and disclosure to promote performance on a range of environmental and social risks and opportunities. The drivers for this trend can be said to be the recognition by financial institutions that there is a relationship between financial and non financial performance. In addition, in the wake of the financial crisis there has been pressure on financial institutions to proactively commit to a more responsible form of financing—one that is characterized more by accountability and transparency. For example, the European Commission has publicly called for asset managers and asset owners, especially pension funds, to sign up to the UN Principles for Responsible Investment.[52]

India

The trend of financial institutions publicly committing to the integration of ESG into investment and lending decision making does not extend to India. There are only two PRI signatories from India to date, IDFC and Solaron Sustainability Solutions and only two Indian UNEP – FI signatories, Yes Bank and IL&FS.[53] [54] The CDP is the most popular commitment by financial institutions in India with 8 signatories in 2011 including HDFC Bank Ltd, IDBI Bank Ltd, IndusIand Bank Limited, Infrastructure Development Finance Company, Reliance Capital Ltd, State Bank of India, Tata Capital Limited, and Yes Bank.[55]

There are no Indian signatories to either the Climate Principles or the Equators Principles as yet. However, international banks operating in India, like Standard Chartered, Deutsche Bank among others are signatories to UNEP-FI and Deutsche Bank, HSBC, Goldman Sachs, Standard Chartered and J.P. Morgan are signatories to the Climate Principles. In addition, Yes Bank has formulated its own Environmental and Social Policy (ESP) based on the Equator Principles.[56]

The Natural Capital Declaration

A declaration by the financial sector demonstrating its commitment at the Rio+ 20 Earth Summit to work towards integrating Natural Capital criteria into financial products and services for the 21st century.

It states "we the endorsing Financial Institutions wish to demonstrate leadership by undertaking to collaborate globally through working groups and engagement with our customers, investee companies, suppliers, civil society, and other stakeholders as appropriate to:

1. Build an understanding of the impacts and dependencies of Natural Capital relevant to our operations, risk profiles, customer portfolios, supply chains and business opportunities;

2. Support the development of methodologies that can integrate Natural Capital criteria into the decision making process of all financial products and services – including loans, investment and insurance. We recognize that given the diversity of the financial sector, embedding Natural Capital considerations will differ across asset classes and types of financial institutions. We therefore aim to build on work undertaken through other initiatives, such as the UN Principles for Responsible Investment, the Equator Principles, the UNEP FI Principles for Sustainable Insurance, and The Economics of Ecosystems and Biodiversity (TEEB), so that we can develop methodologies to:

   a. Apply a holistic approach to evaluating bonds and equities through the integration of Natural Capital criteria in environmental, social and governance (ESG) risk analysis in short, medium and long-term growth forecasts of investee companies;
   b. Systematically consider and value Natural Capital in credit policies for specific sectors and commodities that may have a major impact on Natural Capital either directly or through the supply chain;

3. Systematically consider and value Natural Capital in core insurance business strategies and operations including riskmanagement, risk underwriting, product and service development, claims management, sales and marketing, and investment management;

Source: The Natural Capital Declaration http://www.naturalcapitaldeclaration.org/

This lack of signatories in India is not consistent with the situation in other emerging markets. For example, by comparing the Indian situation to Brazil, one can see that the numbers of signatories there is considerably higher. In Brazil the UNEP-FI has 6 signatories and the PRI has 54 signatories, the latter of which is coordinated as a local network through the PRI Brazilian focal point.[57] Additionally, in South Africa there are 30 PRI signatories active in a locally based network.[58] The higher number of signatories in these emerging markets as opposed to India could roughly relate to the amount of sustainable assets under managements, as those countries with higher number of signatories also seem to have a larger number of estimated total AUM related to sustainability (see figure 2 below).

However, a closer look reveals that there are cases where financial institutions do publicly state a commitment to some of the practices detailed within these statements without endorsing such international frameworks. In addition, as will be illustrated later in this chapter, practices do exist even if financial institutions do not promote their tacit commitment.

Stakeholders indicated that there are a variety of reasons for Indian financial institutions reluctance to sign up to the Equator Principles. For example, there is a perception these institutions would be unable to adhere to these commitments due to the competition in the Indian market, which may have detrimental brand impacts. One view to explain this is the significant mandated borrowing in India: To meet the mandatory lending requirements to micro, small and medium sized enterprises (MSMEs) and other priority sectors, banks have to lend to businesses that are not necessarily environmental and social compliant. Nevertheless, there is a well established need to increase awareness of MSMEs in India of the benefits of compliance and managing ESG risks and opportunities. This is to increase the export potential of Indian MSMEs and involvement in the supply chains of multinational companies, where sustainability can confer a competitive advantage.[59] This tension and trade off between economic, environmental and social development is not unique to India and is a challenge faced by investors and bankers globally. [60]

Figure 2 Global Sustainable Investment Market Estimates

Market	Period	Estimated total AUM related to sustainability (US$)	% of total estimated AUM
European Union	2010	$7.26 trillion	47
United States of America	2010	$ 3.07 trillion	12
Canada	2010	$531 billion	19
Sub Saharan Africa	2010	$125 billion	20
Australia and New Zealand	2010	$115 billion	13
Brazil	2009	$70 billion	12
Middle East and North Africa	2010	$54 billion	2
China	2009	$4 billion	1
South Korea	2009	$2 billion	1
India	2009	$1 billion	1

Questions for Discussion

1. Will there continue to be a proliferation of voluntary commitment statements related to aspects of responsible finance or will there be a consolidation?
2. Will the number of signatories increase for the recently launched Natural Capital Declaration as investors are influenced by the external debates around pricing natural assets and other externalities?
3. Will the Indian finance industry become signatories to global statements such as the CDP?
4. What will be the new themes of relevance that investors promote in their networks?

Governmental and Regulatory Drivers of ESG Management and Disclosure

International

Governments around the world are increasingly adopting a combination of voluntary and regulatory approaches to encourage companies to manage and disclose their sustainability performance, in general or on specific sustainability parameters. This is driven by the recognition by governments of the importance of disclosure in the promotion of accountability and trust, through the facilitation of stakeholder engagement and the identification of material sustainability risks and opportunities for companies.[61] As part of this, financial institutions are required to integrate non financial factors into financial decision making. Noted trends include the State taking a stronger stance on ensuring a minimum level of disclosure and risk mitigation by companies.

In 2011, the European Commission published a renewed EU strategy 2011-14 for Corporate Social Responsibility (CSR) to 'ensure a more responsible and transparent financial system'. As part of this the European Commission has committed to support capacity-building for investors on how to integrate non-financial information into investment decisions.[62] It has also drawn attention to the responsibility of public authorities to promote sustainability or CSR in enterprises which they own or in which they invest. While it is yet to create a legal precedent it has committed to *'consider a requirement on all investment funds and financial institutions to inform all their clients (citizens, enterprises, public authorities etc.) about any ethical or responsible investment criteria they apply or any standards and codes to which they adhere'.* [63]

Some European Member States have introduced non-financial disclosure requirements. For example, Sweden's Ministry of Enterprise, Energy and Communications issued its guidelineson external reporting by state-owned companies in 2007.[64] These guidelines, which took effect in 2008, mandate state-owned companies to publish sustainability reports in accordance with the Global Reporting Initiative's (GRI) Guidelines, an international framework for sustainability reporting. The reports also need to be independently assured.[65]

In Denmark there is a similar requirement. The Danish Financial Statements Act has mandated disclosure on corporate social responsibility for the 1100 largest Danish companies, investors and state- owned companies in their annual reports since 2009.[66] In line with this law, companies need to provide information on their CSR policies or socially responsible investments (SRIs), on how such policies are implemented in practice, what results have been obtained so far and management expectations for the future with regard to CSR and SRI. If a company has no policy, it must explicitly provide information and explanations on the above.

On a thematic basis, regulatory guidance also exists in the US. For example, companies are required to make disclosures to the US Equal Employment Opportunity Commission on the racial and gender profiles of their employees, in line with EEO-1 disclosure requirements.[67]

In emerging markets, there is a trend towards a policy focus on the theme of responsible investing. For example, in South Africa the Code for Responsible Investing in South Africa (CRISA) was launched by the Institute of Directors in July 2011. It sets out a series of 5 principles based on the UN backed PRI including that institutional investors *'should incorporate sustainability considerations, including ESG, into its investment analysis and investment activities as part of the delivery of superior risk-adjusted returns to the ultimate beneficiaries.'* [68]

Formed on an 'apply or explain' basis, the new code effective from the 1 February 2012 requires institutional investors to fully and publicly disclose to stakeholders at least once a year on the extent to which the Code has been applied, providing the reason for not fully applying the Code.[69]

These trends can also be placed in the wider context of international dialogue and consensus regarding the need to pursue sustainable economic development and the role of Responsible Finance to support this trajectory, as well as promote financial inclusion as a means towards this goal.

Financial inclusion has formed a focus of the international multilateral policy making agenda. In 2009 the G-20 created the Financial Inclusion Experts Group (FIEG), which was tasked with: supporting innovative modes of financial service delivery capable of reaching the poor; and scaling up models of small and medium enterprise (SME) financing.[70] Further to this, in 2010 at the G20 Summit in Seoul, a financial inclusion action plan was endorsed and this resulted in the creation of 'The Global Partnership for Financial Inclusion' (GPFI) to institutionalize and continue the work began by the FIEG.[71] The GPFI has three sub-groups (SME Finance; G20 principles and Standard Setting Bodies (SSBs); and financial inclusion data and target setting) whose work is set out in an annual work plan. Of relevance to GIZ is that Germany is a co-chair of the sub-group on

SME Finance whose current three priorities include: promoting access to finance for women entrepreneurs; improving SME access to finance in the poorest countries; and improving access to finance for agricultural SMEs.[72]

In June 2012 the international community will convene to reaffirm its broader commitment to sustainable economic development at the United Nations Conference on Sustainable Development, Rio+20, to be held in Rio de Janeiro.[73] During this gathering world leaders and policy makers will work to discuss a new declaration that sets ambitious new goals for achieving sustainable development.

NGO representatives have already drawn attention to the fact that the declaration will require large amounts of financing to implement, and are asking questions about where this financing comes from, how it is used, and the role International Financing Institutions (IFIs) can play?[74] International NGOs such as the Global Reporting Initiative (GRI) advocate that the Declaration commits to develop a global policy framework requiring all listed and large private companies to consider sustainability issues and to integrate material sustainability information within the reporting cycle, in their Annual Report and Accounts – or explain why if they do not.[75] This is also supported by the Corporate Sustainability Reporting Coalition (CSRC) which represents financial institutions, professional bodies, NGOs and investors with assets under management amounting to a Global AUM of US$2 trillion.[76] This call is already been recognized in the Zero Draft Version of the Rio Outcome Document entitled 'The Future We Want'.[77]

These issues are on the radar of high level policy makers and their advisors. In a report issued by the UN Secretary General's High Level Panel on Global Sustainability, as input to the event, the panel recommends that 'Governments should promote and incentivize the inclusion of long-term sustainable development criteria in investment and transactions conducted by companies, including financial transactions'. Furthermore, they draw attention to the fact that 'most goods and services sold today fail to bear the full environmental and social cost of production and consumption'. To address this, the panel calls for consensus and methodologies to price environmental externalities. In addition, they advocate for the international community to 'measure development beyond gross domestic product (GDP) and develop a new sustainable development index or set of indicators'.[78]

India

The trend in governmental action encouraging voluntary action by financial institutions and companies to manage their sustainability risks and opportunities and disclose on their practices and performance extends to India. This broader trend is widely recognized by Indian stakeholders as a key driver encouraging companies and financial institutions attention towards Responsible Finance. The key departments that are involved in promoting Responsible Finance and business practice in India include the Ministry of Finance, Ministry of Corporate Affairs, and the Ministry of Environment and Forestry.

Priority Sector Lending

Of specific relevance to the financial sector in India is the 'priority sector' lending requirements for banks. In 2011, the Reserve Bank of India issued a Master Circular on Priority Sector Lending, which incorporates and consolidates the multiple sources of guidance on the topic dating back to the 1960s.[79] Priority sector lending targets and sub-targets are applicable to various bank groups, for example domestic banks have to make priority sector advances that are 40 percent of Adjusted Net Bank Credit (ANBC) or credit equivalent amount of Off-Balance Sheet Exposure, whichever is higher. For foreign banks it is 32 percent.[80] Failing to meet these targets results in penalties set out in section II of the Guidance. For example, foreign banks having shortfall are required 'to contribute to Funds to be set up with Small Industries Development Bank of India (SIDBI) or with other Financial Institutions, for such other purpose as may be stipulated by Reserve Bank of India from time to time'.[81]

National Voluntary Guidelines on Social, Environmental and Economic Responsibilities of Business

The Government has released the Draft National Voluntary Guidelines on the Social, Economic, and Environmental Responsibilities of Business in order to encourage the mainstreaming of responsible business practices by Indian companies. The NVGs were issued by the Ministry of Corporate Affairs in July 2011. These guidelines encourage companies to demonstrate their adoption of the National Voluntary Principles to their stakeholders through credible reporting and disclosures on an 'Apply-or-Explain' principle. Three options are provided for reporting. The guidelines encourage companies that are already reporting to provide details of the framework under which their reports were prepared, for example, the Global Reporting Initiative's framework. Those companies that are not yet reporting are encouraged to publish at minimum a simple communication to their stakeholders, indicating their commitment to adopt these guidelines in full or in part, and the basic details of the activities undertaken by them in line with the guidelines. In addition, another option is to use a reporting framework suggested in the National Voluntary Guidelines, which identify certain basic parameters on which businesses can disclose their performance to demonstrate their adoption of these guidelines.

In 2007, the Reserve Bank of India (RBI) drew attention to the *Role of Banks and Corporate Social Responsibility, Sustainable Development and Non-Financial Reporting* in a circular which advised banks to take note of the issue and 'to put in place a suitable and appropriate plan of action (…) with the approval of their Boards'. They also stressed the importance of banks keeping 'abreast of the developments on an on-going basis and dovetail/modify their strategies/plans, etc. in the light of such developments' and that 'the progress made there under could be placed in the public domain along with the annual accounts of banks.' As part of the latter recommendation, the RBI pointed to the GRI Guidelines as a way for banks to disclose their sustainability performance.[82]

Guidelines of Corporate Social Responsibility and Mandatory CSR spending for Central Public Sector Enterprises (CPSEs)

CSR expenditure is now mandatory for Public Sector Undertakings (PSUs) in line with the 'Guidelines on Corporate Social Responsibility for Central Public Sector Enterprises' issued by the Ministry of Heavy Industries and Public Enterprises in March 2010.[83] The exact amount to be spent is prescribed depending on the Net Profit After Tax (PAT) in the previous Financial Year and ranges from 0.5% - 5% of PAT. The Guidelines also require PSUs to create a Corporate Social Responsibility Action Plan, undertake a baseline survey to enable their impact to be quantified with reference to base line data, and in addition the projects should be evaluated by an independent external agency.[84]

The Company's Bill (Tabled December 2011)

The current Company's Bill (forthcoming) is anticipated to contain new legislation related to sustainability of companies and illustrates the trend towards an increasing policy focus on sustainability and disclosure of the Indian private sector. The Bill proposes that companies disclose their CSR activities online or in a report, and that they create a formal CSR policy.[85] (See Appendix for the relevant text extract). In the view of stakeholders, this focus on sustainability disclosure by the government is raising awareness among financial institutions and companies and the potential benefits of managing and measuring sustainability performance.

Environmental and Social Policy and Regulation & Compliance

India has developed a National Action Plan on Climate Change (NAPCC)[86] which outlines a number of steps to simultaneously advance India's development and climate change adaptation and mitigation objectives. Finance is a key element of the National Action Plan on Climate Change, outlined in the plan's National Missions. In addition, the Ministry of Environment and The Ministry of Finance offers range of tax subsidies and benefits for Environmental Projects and Technology.[87]

Incidents in Tirapur such as the controversy over the Sumangali scheme, and absence of effluent treatment plants has drawn the attention of the regulatory authorities to the need for greater policy guidance, regulation and monitoring or compliance on social and environmental policies and schemes.[88] [89] According to stakeholders, these types of incidents have acted as a driver for the government to respond to these issues through voluntary or mandatory responses includes pressure from the international community.

Furthermore, in 2011 the Ministry of Environment and Forests tightened its implementation of environmental regulations and clearances. In particular, monitoring of adherence to environmental clearances was stepped up for infrastructure and mining projects, and in a number of high profile incidents clearances were revoked.[90 91 92 93] In principle, without these clearances projects are not legally allowed to start, even so stakeholders indicated it was widely known that in the past many companies did not adhere to the conditions of their clearance. Since monitoring is now tighter, the general view of the finance industry, as perceived by stakeholders consulted, is that there is now a stronger business case for investors to ask for environmental clearances and check adherence to the conditions of the clearances, particularly for projects involving land. According to stakeholders this is because the risk of projects being delayed or halted is now too high.

This stricter monitoring of adherence to environmental clearances by the Ministry, and also by financing institutions and investors, has been noted as 'a very good' by consulted stakeholders. From the perspective of the financial institutions it is these regulations and the fear of legal or regulatory recourse that are seen as the main driver for a change in practices by the banks and investors. Nevertheless, the overall stakeholder perception is that regardless of the government's priority on the responsible business agenda , there remains a significant gap between policy and practice on the ground at the level of environmental and social compliance.

Questions for Discussion

1. Will the declaration and goals resulting from the Rio +20 conference focus on mandatory corporate transparency and disclosure on environmental and social impacts?
2. Will there be a transition towards regulatory rather than voluntary corporate disclosure in some markets?
3. Even if there are regulations for disclosure in India, will they be followed and will the penalties for non compliance be sufficient to incentivize adherence?
4. Will there be mandatory disclosure requirements placed on investors regarding their investment approach and integration of ESG criteria into decision making?
5. What pilot methodologies will emerge post Rio +20 to price environmental externalities and how will the responsible finance community receive the results of these efforts?
6. What G20 policy themes will emerge as priorities related to financial inclusion and responsible finance post Rio +20?
7. What implications will the Rio+20 policy outcomes related to Responsible Finance and corporate disclosure on ESG impacts have for new financing priorities by bilateral and multilateral donors?

Increasing Stock Exchange Listing Requirements

International

There is a trend towards stock exchanges requiring disclosure on sustainability performance as a listing requirement to enhance corporate sustainability reporting of listed companies.[94] A 2010 study of the top 30 global stock exchanges shows that there is a preference among exchanges for voluntary initiatives over mandatory requirements hence issuing guidelines for voluntary adoption of ESG practices and reporting. In addition, it highlighted the need for 'greater education and consistent outreach to sovereign, retail and institutional investors…to eradicate the worst of the market's short-term mentality', as well as the need for investors, regulators and exchanges to support the movement for integrated financial and non-financial reporting, and the development of products such as sustainable investment indexes to promote responsible investment.[95]

In Australia, the Corporate Governance Council of the Australian Securities Exchange (ASX) recently amended its Corporate Governance Principles and Recommendations to incorporate sustainability issues. For example, gender performance-related disclosure is mandated as part of this. Its listing rules require companies to disclose the extent to which they have followed these recommendations on an 'if not, why' basis.

The Johannesburg Stock Exchange in South Africa has a listing requirement of compliance with the King Code of Governance for South Africa (King III), 2009, which was issued by the Institute of Directors in Southern Africa. The King III Code requires sustainability reporting from companies in an integrated reporting format, as well as disclosure of 'material matters' including sustainability risks, in a timely fashion. Similar trends are noted in other emerging markets. For example, in China, the Shenzhen Stock Exchange has issued guidelines on social responsibility to listed companies, and in 2008, the Shanghai's stock exchanges issued their guidelines on environmental information disclosure by companies listed on the Shanghai Stock Exchange.[96] Both of these encourage listed companies to disclose environmental information in a CSR report, for example, on energy consumption, and also provide details of the key points that should be included and disclosed in social responsibility reports. Most recently, in early 2012 in Brazil the stock exchange, BM&FBOVESPA, issued guidance recommending that its listed companies either publish sustainability reports or explain why they do not.[97] [98]

This engagement by stock exchanges has been driven by responsible investors themselves, as they recognize the role that they can play to influence the corporate practice of the companies that use exchanges to access capital. [99] It is also being pushed by major Asset Managers and coalitions of investors and funds who are encouraging exchanges to include sustainability criteria in their listing requirements.[100] This can be backed up with the fact that in January 2011, investors that are signatories to the UNPRI, representing $1.6 trillion in assets under management, sent a letter to the top 30 stock exchanges calling on them to *'encourage better internal corporate governance within companies, such as improving structure, independence and quality of boards of directors and disclosing how sustainability issues are addressed at the Board level' as well as to 'consult with firms on how to integrate sustainability into long-term strategic decision-making and to encourage firms to adopt integrated reporting'.*[101]

Furthermore, there is increasingly dialogue on the theme of responsible investment among stock exchanges, investors and others, such as UNCTAD World Investment Forum (WIF), a biennial, multi-stakeholder gathering on the world's key emerging investment-related challenges. Themes include how investment can foster sustainable development, and how pro-poor investment strategies can foster sustainable economic growth, development and poverty reduction and form a new investment class.[102] [103]

India

The trend of stock exchanges and regulators actively encouraging listed companies to adopt certain levels of sustainability performance and disclose ESG information extends to India. On 24 November 2011 the Securities Exchange Bureau of India (SEBI) passed a board resolution which mandates listed companies to report on their Environmental, Social and Governance (ESG) initiatives through a Business Responsibility (BR) report which would form part of a company's annual reports/filings. Companies should describe measures they have taken related to the key principles of the 'National Voluntary Guidelines on Social, Environmental and Economic Responsibilities of Business' issued by the Ministry of Corporate Affairs (MCA). This resolution states that the SEBI directive will be immediately applicable to the top 100 listed companies (by market capitalization) and remaining companies will come under its ambit in 'a phased manner'.[104] While this is a promising development, according to stakeholders, there are still questions about this new requirement. These relate to the penalty for non disclosure and who is covered by the mandate since those in the top 100 by market capitalization fluctuates over time. The driver of this development is recognized by stakeholders as being pressure from the Ministry of Corporate Affairs to promote a voluntary approach to responsible business in India rather than having to revert to regulation.

Questions for Discussion

1. Will the trend for stock exchanges to mandate sustainability disclosure in general continue or will the focus be to mandate specific thematic disclose by listed companies?
2. Will the penalties from stock exchanges for non compliance by listed entities for disclosure be sufficient to incentivize adherence to the requirement?
3. To what extent will stock exchanges continue to collaborate with other entities to develop sustainability indexes in order to benchmark company performance?

Translating a Commitment into ESG Policies

Internationally

Investors

Based on international commitments mainstream institutional investors are increasingly incorporating ESG criteria into their investment decision making particularly in North America and Europe. This is in part as a result of international stakeholder expectations that investors use strategies such as positive and negative screening, and actively engage with their clients that do not follow the ESG policies.[105] But the main reason they are doing so is that they want to take advantage of the opportunities resulting from companies that are successfully managing their sustainability impacts, and mitigating the risk of investing in those that are not sufficiently considering their non financial impacts. To do so they apply both positive and negative screenings, the former focusing on leading companies, and the latter on avoiding investing in companies whose practices have a negative impact on the environment and/or the society. In the US alone, responsible investment now encompasses an estimated $3.07 trillion out of $25.2 trillion in the U.S. investment market place.[106]

Specialist SRI Investors lead the trend. An early adopter of such criteria was Pax World, a US based SRI investor that has a family of actively-managed mutual funds.[107] As part of its investment decision making Pax considers a range of ESG factors and sets out its investment position on these topics in a series of publicly available issue briefs. For example, on the topic of Human Rights, they consider if a company transparently communicates whether it has operations in places where repressive regimes are in power. Consequently they choose not to invest in companies with operations in Sudan or Myanmar. In addition, Pax favors companies that have in place policies that prohibit human (labor and sex) trafficking and programs to educate employees and consumers about related risks.[108]

But it is also mainstream investors such as Aviva Investors, which has £236 billion funds under management that is also integrating such criteria. For example, Aviva considers a company's disclosure to the Carbon Disclosure Project (CDP), along with the annual report and financial accounts, in its investment decision making. It uses this information to ascertain the quality of the company's carbon management and the extent to which the company is managing the key risks and opportunities associated with climate change. As an investor, Aviva also engages directly with companies requesting them to respond to CDP and publicly disclose their responses.[109]

The big push is now coming from long term investors such as pension funds. For example, the Norwegian Government Pension Fund applies these criteria in its decision making.[110] On behalf of the Ministry of Finance, Norges Bank Investment Management (NBIM) manages the fund set up to manage Norway's petroleum revenue. The Ministry of Finance has a detailed set of guidelines publicly available which sets out the criteria and a list of excluded companies including those involved in the production of tobacco or those that have committed 'severe environmental damage'.[111] The ethical guidelines are applied through exercising ownership rights, which is the responsibility of NBIM and excluding and observing companies which is the responsibility of the Ministry of Finance.[112]

In May 2011, the $153 billion California State Teachers' Retirement System (CalSTRS) announced that all performance-related discussions with external investment managers would include a review of ESG criteria in their investment strategies. CalSTRS has developed a series of procedures to follow when faced with any major geopolitical and social issue as identified by 21 risk factors. Factors include respect for human rights, worker rights, environmental responsibility, monetary transparency, refraining from investing in war weapons.[113] In the same State, the $236 billion California Public Employees' Retirement System (CalPERS) has also announced that it is fully integrating ESG factors into all of its investment decisions. While on the opposite coast line the New York State Comptroller, who oversees Albany the $133.8 billion New York State Common Retirement Fund, has called for money managers and investment consultants to include more ESG criteria in their investment process.[114]

It is not just pension funds that are strong actors and drivers in this field. International development finance institutions such as the World Bank and the IFC have detailed expectations about the policies and standards that govern their investments. One lesser cited example is CDC, the UK's development finance institution, which has an investment code to support its investments in emerging markets. This Code is compatible with the 2006 IFC Performance Standards and the 2007 agreement for common environmental and social standards among the European Development Finance Institutions (the EDFI Rome Consensus).[115]

CDC uses a tool kit for fund managers, which includes a 6 stage ESG management system in order to support the implementation of their policies. This sets out guidance at each phase in the process of initial screening, due diligence, investment decision, investment agreement, investment monitoring and exit.[116] Furthermore, they provide specific climate change policy guidance for their fund managers.[117]

It should be noted that at an international level while there is an overriding trend in the application of policies in investment decision making, there are interregional differences. For example, in a series of roundtables in 2011 the IFC and Association for Sustainable and Responsible Investment in Asia (ASrIA) found that an increasing number of regional financial institutions are alert to sustainable investment issues and even integrating aspects into their wider investment policies. Yet there is variation in the level of adoption of ESG factors in the region with it being 'early days of adoption' throughout most of the region but 'promising'.[118] Similarly, another report in 2011 by the IFC highlights that there is variation within Africa, with sustainable investment is anchored in South Africa. However, it forecasts that over the next five years Kenya, and Nigeria will also see a growth of this practice, and that the Government Employees Pension Fund (GEPF) in South Africa will emerge as a key player as it already has a responsible investment policy and is the world's 6th largest pension fund.[119]

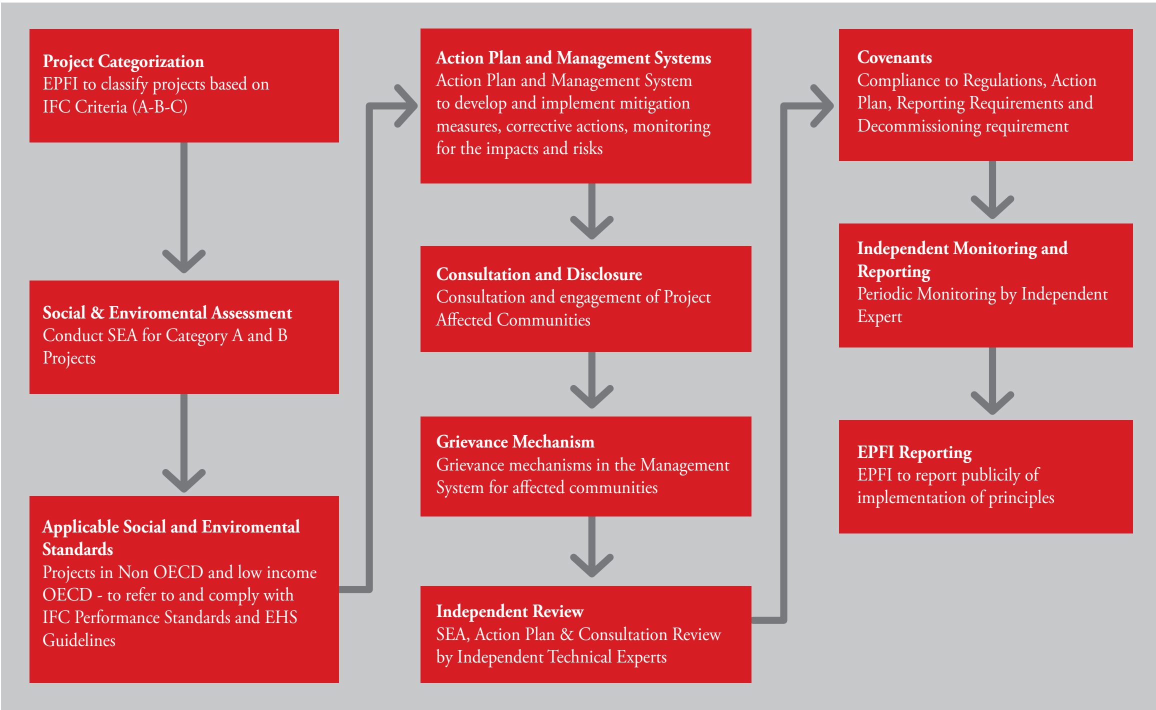
Banks

It is not just investors but also banks that have increasingly been applying ESG criteria in their **lending decision-making** both on the investment and retail banking side. Even though this has become a standard expectation of multiple stakeholders, stakeholder consultation confirms that the drive has also been coming from internally within banks rather than just a response to stakeholder pressure.[120]

HSBC is recognized as a sector leader in both Dow Jones Sustainability Index and FTSE4Good in 2011. The bank has sector-wise policies that set out internationally accepted standards to be followed while lending or investing in companies or projects operating in sensitive sectors. The policies specify areas where an involvement is prohibited or restricted. Sector-wise policies for lending/ investing in the following sectors: Chemicals Industry; Defence Equipment; Energy; Forest Land and Forest Products; Freshwater Infrastructure; and Mining and Metals. HSBC is also a signatory to the equator principles and publicly reports on the number of clients complying with its sector policies, and by value of the loan, as well as the number of transactions that were vetted by the bank in line with category A, B or C of the equator principles.[121] Category A refers to projects with potentially significant adverse social and environmental impacts that are diverse, irreversible, or unprecedented; category B refers to projects with limited adverse social and environmental impacts that are few in number, generally site specific, largely reversible, and readily addressed through mitigation measures.[122]

The typical equator principles work flow is detailed in the following diagram:

Figure 3 **Equator Principles work flow**



Similarly Itau Unibanco, named Sustainable Bank of the Year in the 2011 Sustainable Finance Awards, used its own Social and Environmental Risk Policy for Corporate Credit. This policy outlines criteria and establishes tools that integrate social and environmental issues with the process of granting corporate credit and was developed based on internationally recognized policies and principles such as the Equator Principles. On its launch in 2007, it was submitted to the bank's stakeholders for external consultation, with the international standard AA 1000 as a reference.[123]

As the risks of sustainability impacts become clearer, specific themes and sectors have gained recognition in banks policies. For example, 32% of large banks have developed sector specific guidelines for clients and projects in the forestry sector such as JPMorgan Chase which sets deadlines for verifying the legal origin of wood sourced by clients from countries with a reputation for illegal logging (FSC 2005).[124]

Stakeholder pressure can also shape a bank's policies. In 2011 Amnesty International and the Cluster Munitions Coalition ran a successful targeted campaign against the Royal Bank of Scotland (RBS) in the UK, who were found to be lending money to cluster munitions manufacturers. This campaign was backed by public sentiment as a poll commissioned by Amnesty International found that 78 per cent of people in Britain do not believe institutes should be permitted to offer loans to firms who manufacture cluster munitions. As a consequence of the campaign, the RBS Group publicly declaring its intention to stop lending money to cluster munitions manufacturers or support any application for funding or financial services that would lead to contravention of the Oslo Convention on cluster munitions.[125]

India

Investors

In India, the key institutions active in implementing these policies differ from the international trend. Primarily it is development financing institutions (DFI's) that apply ESG criteria in their investment decision making within the country. Widely recognised by stakeholders is the policies applied by the International Finance Corporation (IFC), the private sector lending arm of the World Bank Group. The IFC requires its clients to follow its Performance Standards as a requirement for receiving and retaining IFC investment. These Performance Standards define the clients' roles and responsibilities for managing their projects.[126 127] The World Bank also applies lending which is primarily provided to governments but in India has included private sector recipients such as IF&FS.[128]

Other development banks active in India such as KfW from Germany, are recognised as applying the same criteria to inform their own decision making. Similarly, the Asian Development Bank applies Safeguard Policy Statements (SPS) to their investments to govern the environmental and social safeguards of ADB's operations. As a consequence of these requirements, recipients of such investments have been driven to apply environmental and social criteria in their lending decisions for example, IDFC, IL&FS and SIDBI, which illustrates how investor requirements influence the practices of banks and other companies.[129]

Banks

The only private sector bank to have instigated such policies without being required to receive international financing is Yes Bank, which strategically positions itself in the 'sustainable banking and investment space'. The bank has created an Environmental and Social Policy (ESP) integrated with its Credit Risk policy, which is based on the Equator Principles even though Yes Bank is not a signatory. This is used to evaluate and assess projects the bank finances to ensure that they are socially and environmentally sustainable; respect the rights of staff and local communities; and are designed and operated in compliance with applicable regulatory requirements and good international practice.[130] Yes Bank has been recognized as having an advanced exclusion list and does not invest in defense and tobacco.[131]

The Small Industries Bank of India (SIDBI) is the Principal Financial Institution for the promotion, financing and development of the Micro, Small and Medium Enterprise (MSME) sector and for coordination of the functions of the institutions engaged in similar activities. In this role, SIDBI has developed a series of innovative products, tools and mechanisms addressing the needs of MSME and has introduced innovations in the field of promotion of sustainability finance. SIDBI adheres to a number of Environmental and Social Policies to inform its lending decision making in line with the World Bank and other international donor requirements for its international lines of credit. As a re-finance institution, it plays an important role to introduce environmental and social concerns in the banking sector and its lending practices. Furthermore, it has an exclusion list and incorporates some ESG factors into its standard loan policy.[132] Stakeholders widely perceive that the application of these criteria by these local financing institutions has been driven by the conditionality of the international financing rather than by internal factors.

Questions for Discussion

1. Will international financing from multilateral and bilateral agencies in India and other markets continue for international lines of credit? And if it doesn't continue, will interest reduce in the integration of ESG policies into lending and investment decision making by investors and banks in emerging markets?
2. What are the emerging areas of environmental and social concern from civil society and how are these going to influence the lending and investment policies of banks and investors?
3. Are there new countries that will be on lending or investment exclusion lists in the near future or will countries be removed from these exclusion lists? For example, will there be democratic reforms in countries such as Myanmar which will lead to the relaxation of existing policies, and if so, how will this change in policies be managed and publicly perceived?
4. Will there be new themes that emerge that require investors to develop new policies outlining their approach to managing the issue?

Implementing Practices to Manage Operational and Portfolio Impacts

Internationally

Investors

From an investment perspective Responsible Finance can involve a financial institution taking an active stance as a shareholder in other stocks to influence the practices of other organizations in its investment portfolio. This active engagement is a noted trend for investors internationally particularly among SRI investors but increasingly among mainstream investors.

Examples of engaged investors include the Cooperative Financial Services in the UK which co-filed investor resolutions at two major multinational oil and gas company's AGMs in 2010, calling for the companies to disclose information on the social and environmental risks of their tar sands developments.[133] The investor also monitors, measures and discloses the total number of interactions and resolutions voted on.

The Dutch based Asset Manager Robeco, which owns Sustainable Asset Management (SAM) behind the Dow Jones Sustainability Index, also integrates environmental, social and governance factors into its investment analysis and decision-making processes.[134] Robeco has used engagement and voting to encourage the companies they invest in to act responsibly. They engage these companies in an active dialogue on corporate governance and responsibility.[135]

In addition, since 2009 Itaú Asset Management has had a voting policy where it has proactively taken into account sustainability issues of the companies it has shares in when exercising the right to vote. In turn, they publicly disclose the voting policy on sustainability issues, as well as the number of votes cast. For example, in 2010, Itaú Asset Management voted in 47 meetings complying with the guidelines of this policy.

Banks

Internationally banks have begun to recognize that their environmental and social impacts go beyond focusing on their operational impacts but also extend to the footprint of their portfolio. Nevertheless, there is a perception among stakeholders that many banks still focus primarily on their operational impacts.

Similarly, the expectation by stakeholders internationally is that banks manage their social and environmental risks in their product and services portfolios as well as their operational impacts. These expectations regarding practices are set out in international commitments such as the Equator Principles and also in international reporting guidelines such as the GRI Financial Services Sector Supplement. These include implementing procedures for assessing and screening environmental and social risks in line with the bank's policies; monitoring and auditing clients implementation of and compliance with environmental and social policies and procedures; interacting with clients/investees/business partners regarding environmental and social risks and opportunities; and mitigate environmental and social impacts of the bank's products and services.[136]

Turning first to the operational impacts of banks, there is a trend among banks to address their operational impacts, in line with stakeholders' expectations. These include addressing sector specific material issues such as the lack of board gender diversity, access to finance both in terms of physical access to banking facilities, as well as ensure that the financing is inclusive, and promoting financial literacy.[137]

For example, National Australia Bank (NAB) has created targets to achieve a gender balance in its workforce, and create enough women in the lower ranks of the organization to progress into senior roles. In turn they regularly monitor these targets and reports progress to the board. In addition, the bank has drawn up a set Diversity and Inclusion Service Provider Principles which all external recruitment suppliers are required to demonstrate their compliance to.[138]

In terms of portfolio impacts, in order to ensure that its social and environmental risk policy is correctly applied, Itau Unibanco has implemented an e-learning program on the policy. Initially it was developed for staff in the commercial and credit analysis department but it has since been rolled out to all new employees.[139] Credit Suisse is an example of a bank that undertakes internal audits related to the implementation of policies in the area of sustainability and sustainability risk management on a regular basis. In addition, HSBC has developed products that integrate ESG criteria and minimize the environmental impact of its products and services. For example, in partnership with Allianz, it has developed green building insurance.[140]

India

Investors

Stakeholders indicate that the trend in India for investors and banks is to look for more stricter levels of environmental and social compliance from companies they are investing in or lending to than previously. A driver for this trend is the number of high profile incidents regarding non compliance or irresponsible environmental practices by companies that have received considerable public attention. Consequently, mainstream investors and researchers have started looking at these non financial factors with increased interest. Nevertheless, public information on how investors are applying these criteria is not publicly available.

One area where investors are publicly disclosing information about their practices in India is within the new and growing field of 'impact investing'. These trends will be considered separately in chapter 5.

Banks

A key Indian trend among banks is the focus on mitigating their operational environmental impacts. It is notable that the majority of banks do not yet consider the environmental and social impacts of their products and services, with notable exception to the issue of financial inclusion driven in part by regulatory obligations. Consequently, products that promote financial inclusion were perceived by many stakeholders as 'Responsible Finance products' in the Indian market.

A study of a sample of the top 30 Indian banks by market capitalization backs this up, as it indicates that 25 of the 30 banks publicly disclose information about their products and services to encourage financial inclusion.[141]

One such initiative is HDFC's Urban Financial Inclusion program in partnership with the mobile phone operator Vodafone launched in November 2011. This collaboration between HDFC Bank Mobile Bank

Account with Vodafone M-PESA is an effort to promote financial inclusion by leveraging deep penetration of mobile phones. The concept is that customers perform basic banking transactions on the mobile phone including depositing and withdrawing cash, at appointed Vodafone M-PESA TM outlets, without having to go to bank branches.[142]

MSMEs fall within the scope of priority sector lending, and in addition to the Small Industries Development Bank (SIDBI), Syndicate Bank, and Allahabad Bank are active in lending to MSMEs. Recognizing the lack of financial inclusion of women in general and specifically access to finance for women entrepreneurs, SIDBI has a specific product targeting women entrepreneurs called the SIDBI Marketing Fund for Women (MFW), as well as two schemes for women under its indirect financing (refinance). Mahila Udyam Nidhi (MUN) is an exclusive scheme for providing equity to women entrepreneurs, and Mahila Vikas Nidhi (MVN), which offers development assistance to women for pursuit of income generating activities.[143 145 146] In addition, Canara Bank provides certain special benefits to women entrepreneurs in the MSME sector for loans up to 5 lacs, such as no processing charges or upfront fees, in order to encourage more women to undertake entrepreneurial activities. In terms of efforts among Indian banks to minimize the environmental impacts of their operations, one such example is Indusind Bank's Green Banking Initiatives. These include using bagasse based Eco-friendly Paper, adopting so-called Thin Computing, and retrofitting ATMs to work on solar power.

There are some limited activities by Indian banks to manage their environmental risks through their lending activities. Nevertheless, the findings of this stakeholder consultation and research support the findings of an earlier study, which found that social and environmental risk assessment is not integrated fully into Indian bank's strategies.[147]

At SIDBI Credit Officer use an E+S Questionnaire and categorization mainly based on environmental considerations, to implement their ESG lending policies and support this with site visits to potential clients to identify site-specific risk issues. It also supports the implementation of its policies through conducting capacity building measures for MSMEs on environmental and social risk management procedures, and staff training to raise awareness on the policies and how to implement them.

Some products are emerging that go beyond the integration of social criteria into the lending decision making, and incentives and environmental criteria and incentives are also being integrated by banks into their financial products. SIDBI has pioneered lending for green and energy efficient technologies in MSME sector in India and other banks are set to follow. For example, SIDBI promotes investment in clean production and energy efficient technologies / production process using concessional lending under bilateral Lines of credit from KfW, Germany and JICA, Japan.[148]

Other examples in India exist. The ICICI Bank Vehicle Finance offers car loans with a 50% waiver on the processing fee for car models that use alternate mode of energy.[149] Similarly, J&K Bank does not provide consumer finance for refrigerators, air conditioners, tube lights and transformers which are not labeled as energy efficient by the Bureau of Energy Efficiency (BEE).

Questions for Discussion

1. Will India investors' interest in ensuring that projects have adequate environmental clearances be sustained once these issues have faded from media attention?
2. Will investors in India start to put in place steps to ensure that the companies they invest in continue to comply with their environmental clearance conditions after the initial clearances have been approved?
3. Will Indian investors start to disclose publicly how they are integrating ESG concerns into their investment decisions?

Questions for Discussion

4 What environmental or social themes will new innovative banking products address and what behaviors will they incentivize?

5 Which stakeholders will be targeted by the next wave of innovations in banking products? Will these products be tailored to meet the needs of rural communities or for example women entrepreneurs?

Disclosing Policies, Practices and Performance

International

The disclosure of non financial information is a key international trend by financial institutions, particularly banks but is also true of the wider corporate sector. This is driven by investors and banks increasingly requiring information on ESG policies, practices and performance of companies to support their investment and lending decision making.

The EU estimates that about 2,500 European companies publish CSR or sustainability reports. In 2010, over 1800 companies produced a sustainability report in line with the Global Reporting Initiative's Guidelines, the world's most widely used framework for sustainability reporting.[150] Specifically, the Financial Services Sector represents the largest sustainability reporting sector globally as in 2010, 192 of these reports were from the sector and 129 declared their use of GRI's sector specific sustainability reporting guidance, the Financial Services Sector Supplement. (FSSS)

An analysis of the world's top 50 identified financial institutions based on market capitalization indicates that 41 out of 50 communicate on non-financial performance metrics in some form of public disclosure, 35 out of 41 sustainability reporters use the GRI framework with 30 of them using the GRI Financial Services Sector Supplement. From these 40 % get their sustainability reports assured by the third parties, and 32 % reporting in line with GRI declare their reports at a level of A+.[151] [152]

This trend is not restricted to Europe or North America. Brazil is the third largest GRI reporting country after the USA and Spain, with 7% of the world's sustainability reporters in 2010 and has been recognized by third parties as the leading emerging market when it comes to ESG disclosure. [153] [154] This has been attributed to the national sustainability index along with increased pressure from investors, who are demanding improved ESG disclosure and research.[155] The Emerging Markets Disclosure project coordinated by US SIF, on behalf of PRI, is credited for pushing for disclosure in the emerging markets, as is the Global Reporting Initiative (GRI).[156]

The drivers for disclosure may differ by country; however, one driver recognised by international stakeholders is the pressure for disclosure by international investors that are increasingly interested in investing in these markets on behalf of their clients, as well as the desire by transparent companies to attract international financing. Internationally, momentum is gathering to bring together non financing and financial reports in so called integrated reports. This is a new approach to corporate reporting that demonstrates the linkages between an organization's strategy, governance and financial performance and the social, environmental and economic context within which it operates. The International Integrated Reporting Committee (IIRC) is leading the development of a global framework for Integrated Reporting.[157] These developments relate to a stated need by stakeholders for more research on how to price externalities and natural assets and in turn how to report on how companies use these natural assets such as water and biodiversity, and carbon.

India

While the number of sustainability reports and the level of ESG disclosure in India have increased in recent years, there is still a trend of limited disclosure both in general and relative to other emerging economies.[158] Some stakeholders describe the level of sustainability reporting in India as in its infancy, and this is supported by the findings of a detailed study on Sustainability Reporting Practices and Trends in India published in early 2012.[159] Despite this, there is increasing recognition of the benefits of non financial reporting. For example, Dr K.C. Chakrabarty, Deputy Governor of the RBI, spoke of the advantages and benefits of such reporting in his speech at the a National Conference on Non Financial Reporting and Risk Management for Financial Institutions in India in June 2011.[160] In addition, according to those consulted access to international capital is one of the key drivers for this trend towards disclosure and companies that are listed outside India are more likely to disclose of ESG information in sustainability reports.

In 2010, there were 24 GRI based reports published in India; however, estimates put the total of over 50 sustainability reporters in the country overall.[161] A number of international banks with subsidiaries in India are among existing GRI FSSS reporters. But while good practices exist in India, an analysis identified that only one Indian bank was among the financial services sector reports in 2010. This is despite the previously cited RBI notification on 20 December 2007, which drew attention to the Role of Banks and Corporate Social Responsibility, Sustainable Development and Non-Financial Reporting.[162]

In light of the recent publication of the National Voluntary Guidelines (NVG) on Social, Environmental and Economic Responsibilities of Business by the Ministry of Corporate Affairs the time has come for the financial services sector to consider adopting international best practices and take a closer look at the business case for integrating ESG factors into decision making.

There are a few banks that do report on their sustainability practices on their website or in their annual reports. However, the majority of banks have not yet started publishing a separate sustainability report. In 2010, SIDBI became the first Indian bank to publish a sustainability report as per the GRI G3 Guidelines, including the GRI Financial Services Sector Supplement. Since then Punjab National Bank has produced two reports, although not in line with the GRI Guidelines.[163] Forthcoming are reports from IDFC, Yes Bank and the State Bank of India.

Questions for Discussion

1. At what speed will the discussions related to integrated reporting develop and what level of consensus will be able to be achieved regarding the format of these disclosures?
2. Will there be consolidation in corporate disclosure frameworks related to specific issues e.g. energy or water?
3. Will there be increased disclosure in India by companies as a consequence of the SEBI mandate and the release of the National Voluntary Guidelines?
4. Will the RBI issue an updated circular on non financial reporting based on the developments with sustainability reporting since its earlier circular in 2007?

Measuring, Rating and Rewarding Performance

International

There is an international trend towards the development of sustainability indices to track publicly disclosed sustainability performance. Various international indices, initiatives and awards track, rate and recognise performance on non-financial metrics much like the 'market capitalisation' and 'share price index', for financial performance.

Out of the world's top 50 financial services companies by market capitalization, the majority of companies are featured on the Dow Jones Sustainability Index (DJSI) and the Financial Times Stock Exchange FTSE4Good Index.[164] The Dow Jones Sustainability Index tracks the financial performance of the leading sustainability-driven companies worldwide, in cooperation with Sustainable Asset Management (SAM) to provide asset managers with reliable and objective benchmarks to manage sustainability portfolios.[165] Companies are tracked on the basis of parameters including practices and performance on Occupational Health and Safety, Stakeholder Engagement, Climate Strategy, Product Stewardship, Biodiversity, and Corporate Governance. Financial sector leaders within the index as of the end of 2011 were HSBC Holdings in the DJS World & World Enlarged Index and Allianz in the DJS World 80 and DJS World 80 ex US.

Much like the DJSI, the FTSE4Good Index has been designed to measure the performance of companies that meet globally recognised sustainability standards in order to support asset owners, fund managers, investment banks, stock exchanges and brokers assess or create responsible investment products.[166] In addition to its broad based sustainability index, FTSE4Good has developed thematic indexes such as the FTSE CDP Carbon Strategy Index Series using data from the Carbon Disclosure Project to support investors in incorporating climate change risks into their investment strategy.[167]

Until recently the number of markets for these indexes has been limited but now momentum is building outside Europe and North America within emerging markets. A 2011 publication by the IFC noted that there has been an increase in the number of sustainability indices in emerging market countries with 12 alone being launched since 2009.[168] The perception of stakeholders and a trend reflected in research is that this increase in interest is driven by value-oriented investors and mainstream investors, who see it as an opportunity to enhance their returns, particularly in the emerging markets where they see the potential for natural resource scarcity or human resources issue to be a barrier for growth in the future.[169]

Examples include the Indonesian Stock Exchange (IDX), which has developed the SRI-KEHATI Index in cooperation with the Indonesian Biodiversity Foundation (KEHATI).[170] This index tracks the sustainability performance of Indonesian companies listed on the IDX and provides investors with useful insights to support their investment decision making. In Malaysia, the Bursa Malaysia has also begun to focus on sustainability and reporting and launched a CSR framework with a view to also create a similar index.[171] A full list of these indexes is listed in the appendix.

To date there has been perceived limited success in general of these indices in attracting a large investor base, in part attribute to lack of communications and education of investors to support their understanding of how the index provides them with meaningful and reliable information about sustainability leaders and laggards.[172]

In addition to these indices, there are a range of support services that provide customised company benchmarks, and research services primarily to asset owners, as well as sustainability data. For example, to support this demand for sustainability information by investors, in 2009, Bloomberg launched a service that provides publicly available ESG data on companies for clients hooked up to its data terminals.[173]

The support services market is fragmented and there has been a recent trend of consolidation in the market as indicated in the figure below, which outlines some of the firms that have merged in the last couple of years.

Figure 4 **Indicating Market Consolidation of Data Providers and Research Agencies**

Thomas Reuters
- Acquired **Asset4** (ESG & Economics firm) in 2009
- Acquired **Point Carbon** (Carbon Data & Analysis) in 2010

Governance Metrics International
- **The Corporate Library** (Global governance research) and **Governance Metrics International** (U.S. corporate governance advisory) merged in 2010

Jantzi Sustainanalytics
- **Jantzi Research** (North American ESG Research) and **Sustainanalytics**(European Responsible Investment) merged in 2010

MSCI
- In the early 2000s, MSCI and Barra Aegis merged
- Through the 2000s, **Risk Metrics** took over Ennovent, ISS, CFRA and KLD
- In 2010, MSCI took over Risk Metrics

India

In India there is growing interest in benchmarking listed company's sustainability performance in indices. The S&P ESG India Index established in January 2008 was the first such investable index in India. It was launched by Standard & Poor's, CRISIL and KLD Research & Analytics and sponsored by the International Finance Corporation (IFC), a member of the World Bank group. The Index comprises 50 Indian companies that meet certain ESG criteria and have been drawn from the largest 500 companies listed on the National Stock Exchange of India through a two-stage screening process. The S&P ESG India Index is maintained by India Index Services Ltd., a joint venture between CRISIL and the National Stock Exchange of India, which also manages the flagship S&P CNX NIFTY index of India's largest and most liquid companies.[174]

The Carbon Disclosure Leadership Index (CDLI) is a 5 year old non investable index based on carbon management and performance of companies in India. In 2011 on behalf of its signatories the Carbon Disclosure Project (CDP) sent its annual information request to the top 200 of India's companies by market capitalisation asking them to measure and report what climate change means for their business. From this sample, 28.5% (57) of companies responded, compared to 51 companies in 2010 and a financial institution, Yes Bank, was ranked third in the Carbon Disclosure Leadership Index (CDLI).[175 176]

More recently, in February 2012, BSE launched the first live carbon index, the BSE-GREENEX, in collaboration with gTrade (supported by GIZ promoted by Federal Republic of Germany, Observer Research Foundation and IIM Ahmedabad). This index takes the BSE listed companies as a baseline and recognises companies in line with existing metrics related to the Kyoto Protocol on their carbon emissions performance. It is based on the BSE form 20 data which includes information on energy consumption and from that it is possible to calculate the carbon emissions, as well as Free Float Market capitalisation & Turnover.[177 178 179]

Questions for Discussion

1 Will more thematic indexes emerge in the future e.g. on corporate performance on water efficiency and consumption?

2 Will these indexes result in new market driven investment products? Will participation from companies who wish to receive recognition of their performance be sustained and continue to increase?

3 Even if there is more disclosure by companies in India and internationally will the increased performance data available result in the mainstreaming of integration of ESG criteria into lending and investment decision making?

4 How can economic values be ascribed to environmental and social externalities and what role will investors play in developing the methodologies for calculating these values?

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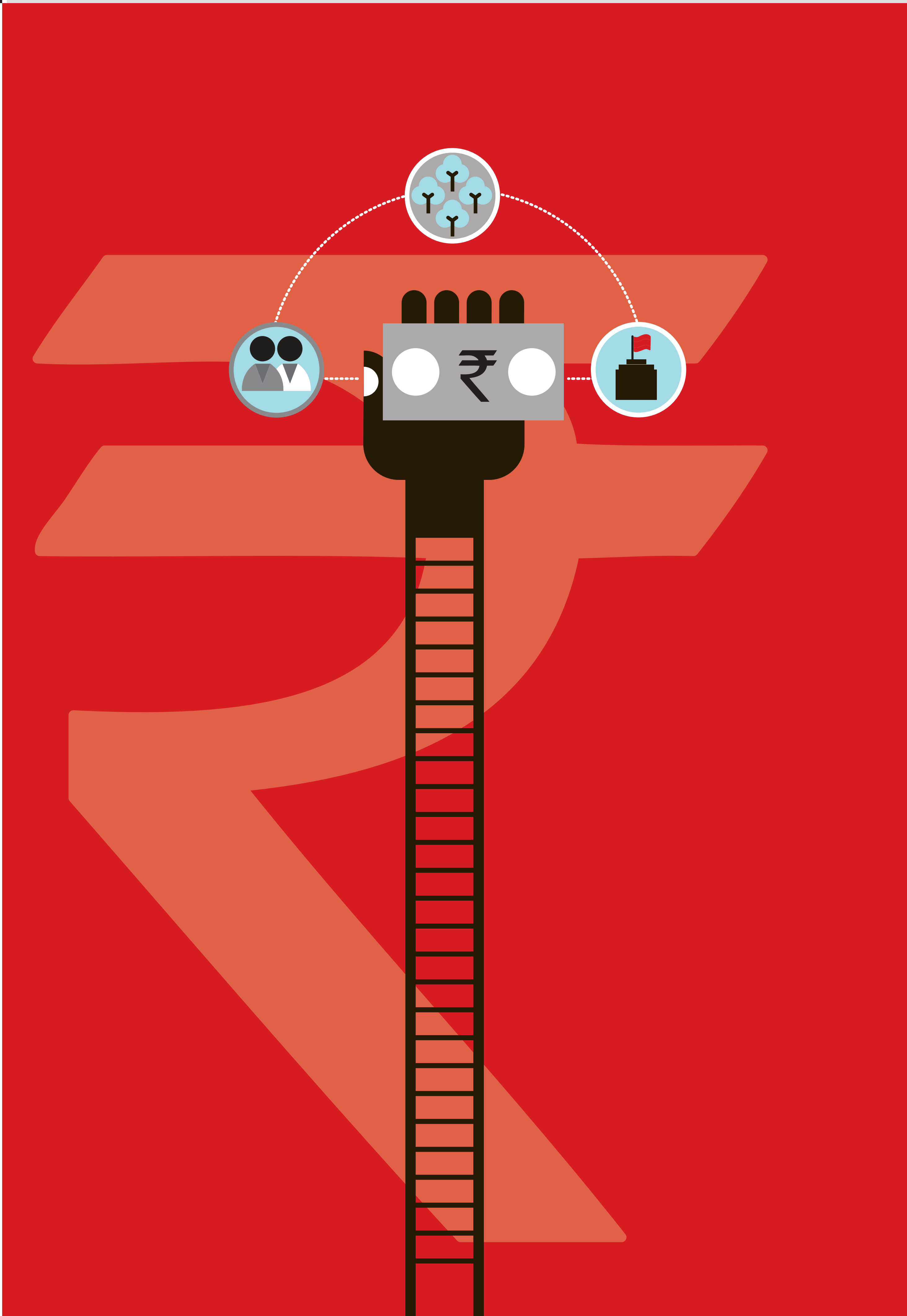

4 Lessons Learnt in International ESG Integration and Responsible Finance

The integration of environmental, social and governance factors into lending and investment decision making by banks and investors is a growing trend. Nevertheless, stakeholders perceive the routine consideration of a broad range of these non financial risks and opportunities as not yet mainstreamed. For the upward trend to continue, they cite a number of challenges that must be overcome to achieve the widespread adoption of Responsible Finance. This chapter outlines the challenges and barriers identified through an extensive series of stakeholder consultations and it highlights the similarities and differences between the challenges internationally and in the Indian context.

International Including India

Lack of Disclosure and Data Availability

Information and data on companies' environmental, social and governance policies, practices and performance is a prerequisite for Responsible Finance. It is required to formulate an accurate picture of the extent to which a company has taken steps to mitigate its non financial risks and positioned itself effectively to take advantage of emerging opportunities. Without this information, investors and other stakeholders are unable to make informed decisions and implement Responsible Finance strategies.

"Even though globally the level of disclosure is increasing the lack of transparency and data on corporate practices and performance remains a challenge. This has been identified by both Indian and international stakeholders as key barriers for implementing Responsible Finance and is also supported by literature on the theme."[180]

To address these challenges, there were a variety of views expressed on whether disclosure should be voluntary or made mandatory. However, there were strong views that in India voluntary disclosure will not be sufficient and regulatory intervention may be needed to ensure adequate data availability.

Data Quality and Comparability, Standardization of Metrics and Impact

Disclosure and transparency is only the first step towards corporate accountability. It is imperative that consistent sustainability metrics are used to enable a fair comparison. Only then can the data be used to compare performance of companies within and between sectors, as well as how a company has improved over time on these non financial parameters.

'Companies may have beautiful reports but getting real information from them is a big challenge', according to those consulted. They recognized the important role of standardized global reporting systems such as the Global Reporting Initiative (GRI). Nevertheless, while GRI is used by many companies to report on their non financial performance, there is a perception that there remains a lack of consistency in reporting on existing GRI parameters. Furthermore, there is still a need for standardized metrics on specific issues. There are calls both among international and Indian stakeholders to 'count things in the same way'. Furthermore, greater emphasis needs to be made on performance and impact focused reporting, rather than simply on a company's management approach on an issue. It is not enough to know that a company has a policy on corruption. It is also important to receive clear answers to questions such as: To what extent have employees been educated on the policy, what systems are in place to monitor it, and what impact has this made on incidents of corruption?

Assurance of Data

Despite increasing levels of disclosure, much of the data and information disclosed is still not assured and therefore questionable, according to stakeholders consulted. Moreover, where data is assured there is inconsistency in the assurance approach taken. There is a perception both internationally and certainly in India that the information disclosed may be inaccurate, even in cases where third parties have assured the data. As such a barrier to the further integration of Responsible Finance practices is the assurance of sustainability data by third parties to ensure that the information used for decision making is reliable and accurate.

Evidence and Recognition of the Business Case

Even though there are multiple studies that provide evidence that there are better risk adjusted returns from investing in companies with improved sustainability performance, there is still a need to convince key stakeholders internationally and in India, according to the majority of stakeholders consulted. This corresponds to literature on the theme which also emphasizes the need to 'build a more robust business case for the financial services providers'[181] and the need 'to further demonstrate the materiality of non financial issue to financial performance'.[182]

Lack of Capacity Among Investors

A challenge indicated by stakeholders both international and from India is the lack of capacity and training on sustainability risks that prevents mainstream investors from integrating ESG into their investment decision making. In addition, finance specialists 'don't seem to fully understand the language of environmental and social impacts'. This is supported by other studies on the theme.[183] [184] Hence, there is a perceived need to increase the capacity of mainstream investment organizations in order to fully integrate ESG criteria and help finance specialists to understand the language of environmental and social impacts.

Lack of Measurement Tools

Frameworks such as the Global Reporting Initiative (GRI) do exist for supporting disclosure but stakeholders both in India and internationally expressed a concern for a lack of simple tools to measure specific aspects of non-financial performance.

India

A Lack of Awareness, Understanding, Commitment and Capacity

The level of awareness and understanding of the relationship between non financial and financial performance remains 'abysmally low' among investors and financial institutions. There is a belief that this awareness needs to be built before Indian institutional investors are to take active ownership in questioning management on ESG performance, and that domestic asset owners need to be encouraged to subscribe to the principles of responsible investment.[185]

From the perspective of the companies whose behavior will be stimulated to change through Responsible Finance, there is a perceived need for a development of their awareness of environmental and social risks. Many stakeholders consulted cited the lack of awareness specifically among SMEs who often 'cut corners' when it comes to environmental and social compliance. Smaller companies in India are believed to assume that managing these risks will be a cost. Many use the fact that they are small as an excuse, but there is a belief by many stakeholders that 'being small doesn't mean that they don't have to comply with environmental and social regulations'.

While some see ignorance as a challenge, other stakeholders maintain the view that there is just a lack of will and commitment. They argue that there is awareness on the business case of non-financial reporting and risk management but there are perceived cost barriers, which make banks and investors reluctant to follow these practices. Furthermore, promoters are focused on the short terms and so routinely ignore environmental and social risks.

Ultimately, these challenges indicate the strong need for capacity development by financial institutions as well as for companies on the business case for sustainability and the integration of non financial risks and opportunities into business and financing decision making.

Lack of Engagement by the Media and Other Stakeholders

In other markets the media or NGOs have targeted financial Institutions to withdraw funding from or investments in companies that they believe are engaging in irresponsible environmental or social practices. In India, however, while stakeholders have campaigned against companies directly there is no history of them targeting the sources of financing. In addition, the media in particular has allowed companies to showcase their philanthropic efforts regardless of their social and environmental impacts on local communities, workers and suppliers, which indicate a lack of understanding by the media on the topic.

A Focus on Operational Impacts by Banks and Not Portfolio Impacts

While internationally banks are increasingly focusing on the ESG impacts of their lending activities, the stakeholder perception and evidence suggests that Indian banks are focused primarily on their operational impacts. In instances where there is evidence of banks integrating for example energy efficiency requirements in their lending, it is perceived to be driven by external international finance requirements rather than driven from within the organization. A challenge that stakeholders have indicated needs to be overcome is the buy in from top management to understand that there are environmental and social risks that are faced through lending activities. In turn, only by understanding the strategic value of managing portfolio impacts in addition to operational impacts, will the shift take place.

Non Compliance

There is a perception of weak environmental and social compliance that some stakeholders perceive as a ‘culture of non-compliance’. Furthermore, despite a recent trend towards the revoking of environmental certificates, there is a lack of monitoring of compliance. Clearance conditions are adhered to only while getting the clearance certificate. In the Indian context, there remains the challenge of balancing basic adherence to laws and E&S norms and meeting the regulatory requirements regarding financial inclusion, for example, of MSMEs. Furthermore, competition among banks is cited as a reason why such compliance is not checked during financing decisions.

In order to ensure that SMEs achieve environmental and social compliance, there is a view that there needs to be a simplified environmental and social appraisal process to conduct due diligence on SMEs during the lending process. Based on the amount that SMEs are borrowing the costs of a more extensive E&S due diligence process might be too high.

Some stakeholders believe that banks should be continuously monitoring environmental and social compliance after a loan has been granted and not just at the financing decision making stage. Until Responsible Finance conditions are applied throughout the financing cycle, the challenge of non compliance will continue to exist. In addition, there is a view that banks should make greater use of their powers to revoke their funding if environmental or social compliance is not adhered to.

Shareholding Patterns and Lack of Engagement by Domestic Insurance and Pension Funds

In India shareholding patterns are very different from other countries in the world where Responsible Finance is more common place. The government owned insurance company, Life Insurance Corporation (LIC), or pension funds are the main shareholders of most large companies, with the balance of shares being held by a small number of very rich individuals, and relatively fewer floating shares. This means that investors generally have a lower voice and less influence over the companies that they invest in as they only hold a relatively small number of shares. Hence, some of the active engagement strategies used by investors in companies within other markets can be difficult to apply to the Indian market. If domestic insurance and pension funds were to engage on the topic of Responsible Finance, then companies may be forced to voluntarily adopt more responsible business practices. However, until they do so, the lack of engagement by domestic insurance and pension funds remains a barrier to the further implementation of Responsible Finance.

Questions for Discussion

1. What are the best organizations to collaborate with in terms of encouraging standardized disclosure and on what themes?
2. Which are the best organizations to collaborate with in terms of the development of standardized metrics for measuring social and environmental impacts? Should there be one organization that coordinates this globally or would different organizations be preferable to take the lead for different purposes?
3. Which measurement tools are most useful for investors to support them in their decision making?
4. What tools are useful for companies to support them with the integration of environmental and social risks and opportunities into their strategies, policies and practices?
5. How can assurance of sustainability information be improved to ensure a standardized methodology is used? Which are the best organizations to collaborate with on this purpose?
6. Will the same strategies for building the capacity of investors on the integration of ESG into investment and lending decision making be suitable universally or should country specific strategies for engagement be developed?
7. Is there scope for collaboration between banks, investors and stock exchanges in emerging markets on addressing these challenges?
8. What capacity building can be undertaken with the media to encourage them to ask the right questions and to encourage more informed reporting on corporate transparency and accountability issues?

Footnotes

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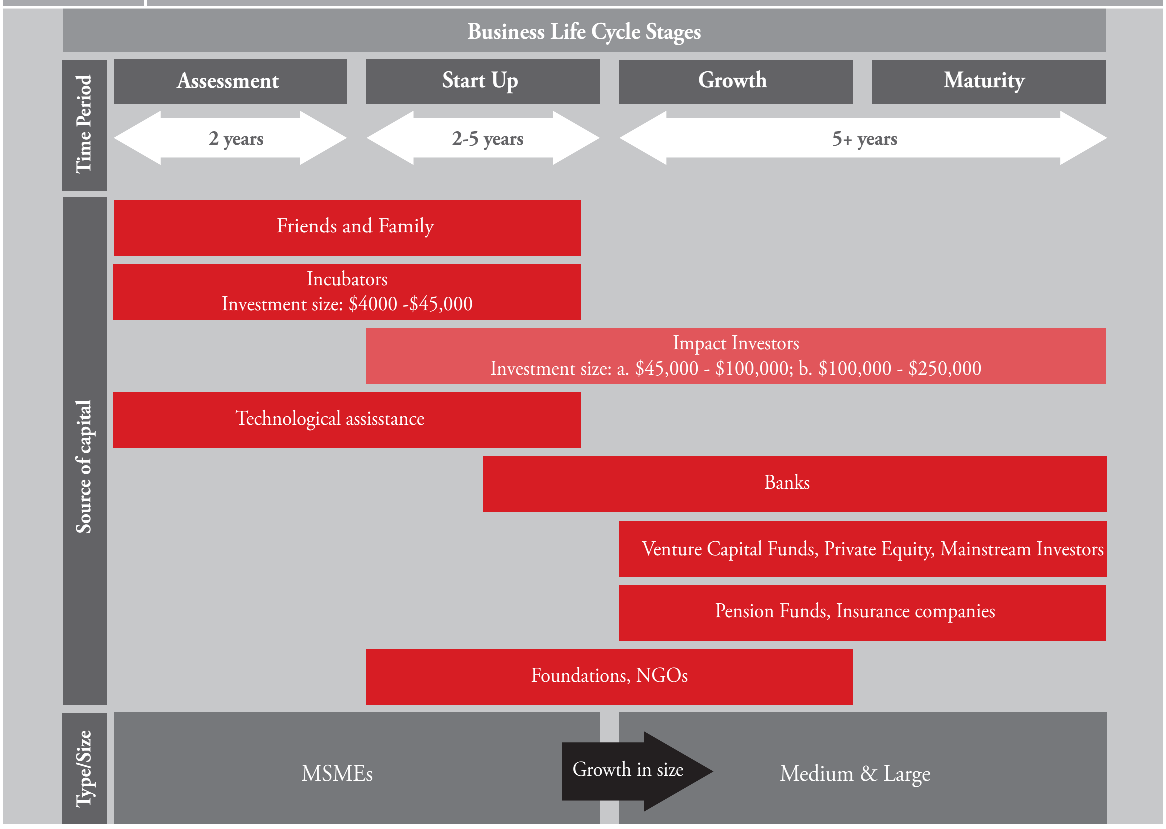
5 Impact Investing

A key international and Indian trend in Responsible Finance is the emergence of 'Impact Investments' which is widely regarded as a new asset class.[186] Throughout a business life cycle companies require different types of financing and sources of capital. Impact investments focus on the start up or early stage of a business's development by providing early stage financing to primarily inclusive businesses usually in the form of private equity. Inclusive business models are 'ones which seeks to contribute towards poverty alleviation by including lower-income communities within its value chain while not losing sight of the ultimate goal of business, which is to generate profits.' According to a recent impact investment market study, investors see this as a market 'in its infancy and growing' with almost USD 4 billion planned for investment in 2012.[187] The Monitor Institute estimates that over the next 5-10 years impact investments will grow to 1% of global assets under management.[188]

This chapter briefly summarises the trends for impact investing which emerged as an important theme of relevance for India. In addition, it highlights the specific barriers and challenges related to this type of responsible investment for the Indian context.

Figure 5 Diagram to Indicate Different Sources of Financing for SMEs during the Business Lifecycle



A Brief Introduction to Impact Investing

Impact investors aim to maximize social and environmental impacts alongside financial returns with their investments by applying social and environmental criteria in their investment decision making process. They focus on investing in businesses exhibiting transformative innovation, where an enterprise is creating new markets and transforming existing markets by introducing not only a new product or service, but also new and often inclusive business models. Inclusive businesses are focused on addressing the needs of the four billion people living at the bottom of the pyramid. These people currently in absolute terms often pay more for inferior products, a so-called 'BOP penalty'.[189] Nevertheless, stakeholders repeatedly emphasized that inclusive businesses are 'about more than just providing mini versions of what the west thinks people at the bottom of the pyramid want'.

Some people refer to the types of businesses supported by impact investors as social enterprises, although the definition of this type of business is subject to much debate. Importantly, these businesses have a large environmental, economic and/or social impact.[190] [191] Ultimately, impact investments are designed to address social or environmental challenges while generating some level of financial profit. The level of financial returns that investors find acceptable will depend on their investment philosophy and the rates of financial return they perceive acceptable. Hence, they make decisions on the sectors and businesses to invest in based on these values and criteria, and what may be seen as having a positive social and environmental impact by one investor may be perceived differently by another. Regardless, these businesses ultimately create 'new opportunities for innovation, growth, and competitiveness.'[192]

Under The Mango Tree Naturals and Organics Private Limited is a social enterprise and an example of a recipient of impact investments in India. It brings to the market a variety of gourmet honey and related products to support rural livelihoods. The business is currently active in districts of Gujarat, Maharashtra and Madhya Pradesh in India and the business creates direct, fair-trade and sustainable market access from farmers to consumers. It works together with its' not for profit arm which trains farmers to add beekeeping with the Apis cerana indica on their farms. This improves farmers' incomes due to increased bee pollination and better agricultural productivity for crops, as well as a new stream of income from honey and beeswax. Among other impacts, to date it has trained 1,432 farmers in beekeeping including women, thereby increasing their income by Rs 10,000 -12,000/ annually and provided 1,500 small beekeepers direct market access for their sustainably harvested honey and increasing their annual income by 25%.

Source: http://utmt.in

It should be noted that the debate around impact investing is closely related to the discourse about inclusive business models, MSME financing and development, innovation and entrepreneurship, financial inclusion and impact.

There are a range of stakeholders active in the field of impact investment both internationally and in India. Broadly speaking, these stakeholders can be classified as asset owners; asset managers/intermediaries; incubators; technical consultants; and finally the business owners themselves. (See diagram of the impact investing system in the Indian context).

Asset owners want to invest in line with their values and are willing to compromise on financial returns for some form of impact. Asset owners range from foundations, such as the Gates Foundation, to traditional mainstream private equity funds. Multilaterals, such as the IFC, bilateral agencies, for example DFID, and national governments, like the Indian government are also actors in this field. These governmental stakeholders are playing an increasing role in establishing challenge and innovation funds and in the provision of technical assistance to support these types of investments.[193]

Figure 6 Innovations in MSMEs and their Impacts

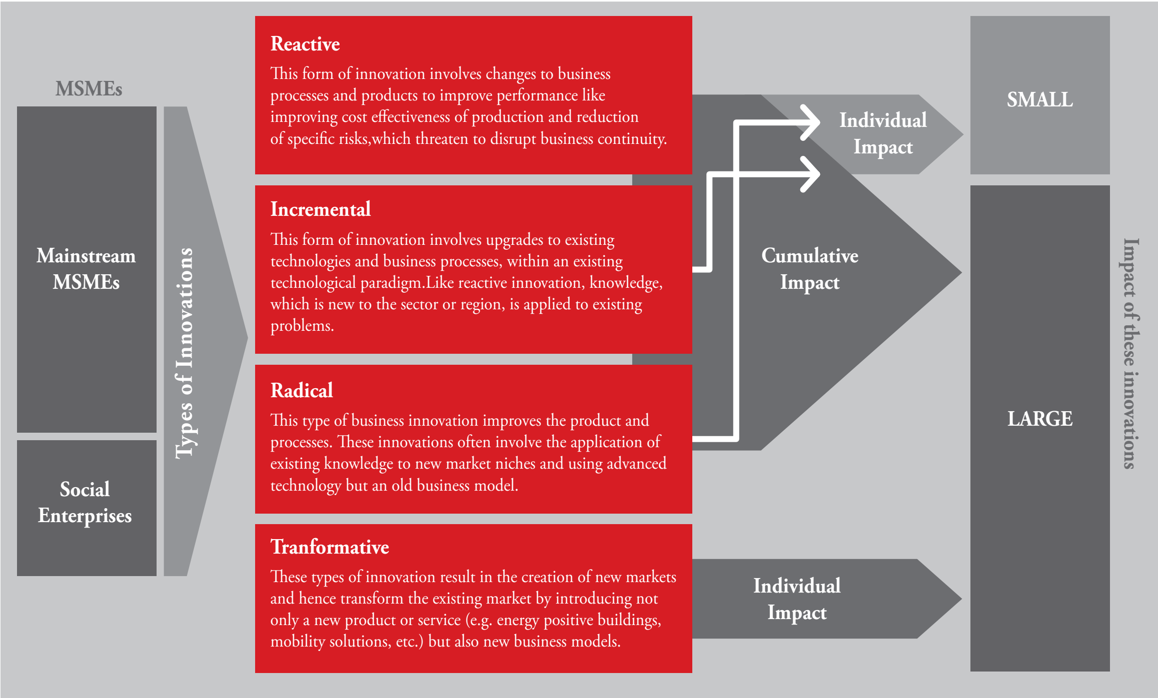
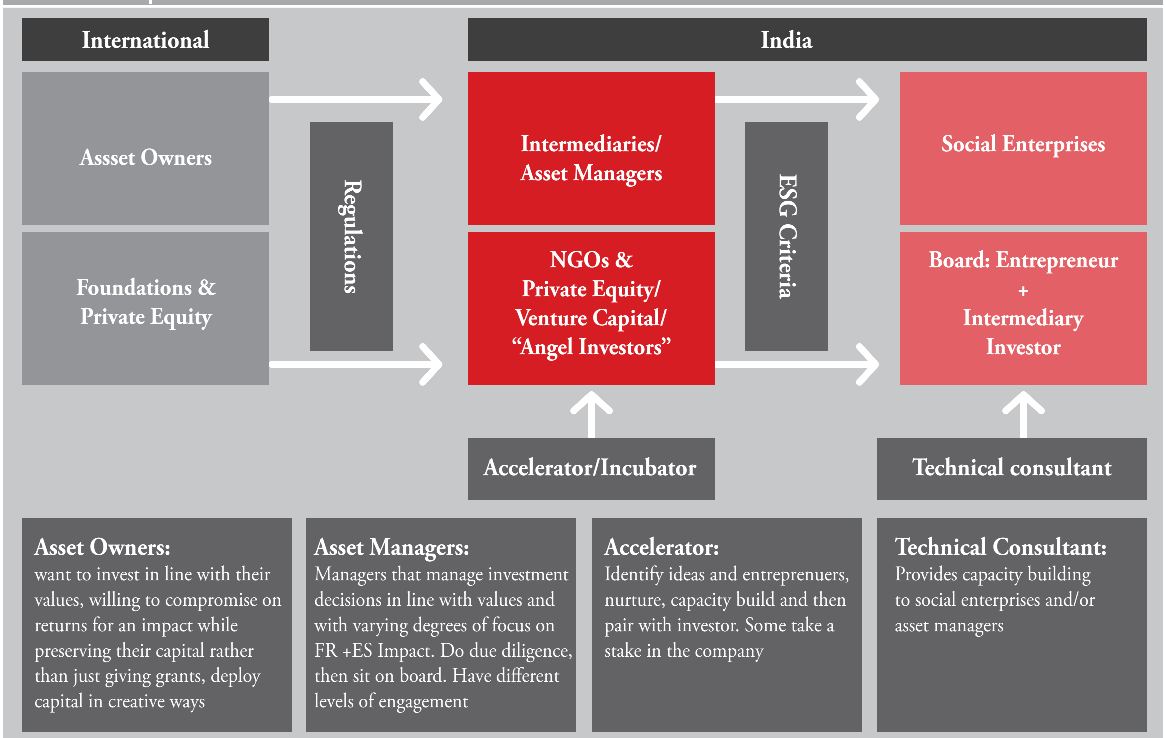


Figure 7 Diagram Indicating the Impact Investing System in India



The UK Government has recently established the Big Society Capital Group, a financial institution that aims to develop a market for investment made on the basis of positive social impact as well as financial returns.[194] Furthermore, in India the UK government's development arm DFID is setting up an impact investment fund valued at 35 million GBP to be managed through SIDBI Venture Capital. This fund is intended to focus on impact investments in the country's three lowest income states.

The Government of India's National Innovation Council (NIC) has also set up the India Inclusive Innovation Fund (IIIF) at a value of 500 crore to give out seed funds and grants in the country.[195 196] Examples of other initiatives at the multilateral level include the SME Finance Challenge by the G-20 group of nations to find and scale sustainable solutions for financing small enterprises globally, and the current G20 and IFC Challenge on Inclusive Business Innovation, a global search for businesses with innovative, scalable, and commercially viable ways of working with low-income people in developing countries.[198]

Accelerator/ Incubators and Technical Consultants are involved in the assessment and the start up phase of the enterprise development. They support entrepreneurs through capacity building, and preparation of the start up and pair them up with investors. Some do financially invest in the company at the start up phase through grants, loans and equity but others act as consultants to the businesses and recoup their consultancy fee from the enterprise once they reach a particular level of profitability on a 'success fee model'. Accelerators and incubators are usually hybrid models of NGOs and consultancy companies, such as Start Up! and India Unlimited.

One of the most frequently quoted examples in India by stakeholders consulted is Dasra, a strategic philanthropy foundation that provides support to social entrepreneurs and 'brings together knowledge, funding and people as a catalyst for social change'.[199] In partnership with Intellecap, Dasra runs the Sankalp Forum, which facilitates the collaboration between established and budding entrepreneurs, investors and recognizes the best social enterprise models through the Sankalp Awards. This initiative connects social enterprises with investors and funders and over the past three years more than 24 of these enterprises have received investments, and over 160 others have been made investment ready through mentoring and capacity building programs.[200]

Asset managers are usually not the owners of the capital, but act as impact investment intermediaries who manage investment decisions in line with their values and those of their client. They undertake due diligence on the potential investment target and then post deal represent their clients on the board of the investee company. One example is the Acumen Fund which supports entrepreneurs focused on offering critical services – water, health, housing, and energy – at affordable prices to people earning less than four dollars a day. The Acumen Fund has $73 million worth of approved investments in 65 enterprises to serve the poor.[201]

Asset managers involved in impact investing apply a range of environmental or social criteria in their decision making. However, the willingness of investors and their intermediaries to prioritize social over financial returns does vary and is a subject of much debate. Some operate on an impact first model, whereas others do so on a 'financial returns first' basis.

Each organization follows its own due diligence process to ensure that the potential client meets its environmental and social policies and is anticipated to be creating a positive impact before the investment is approved. This due diligence process could vary from 6 weeks to 6 months and can involve field visits, impact assessments, reference checking on both the business and where appropriate the promoters, and speaking with beneficiaries of the business. Post investment these organizations define metrics to monitor ongoing performance.

Other types of organizations active in this space include network based NGOs or membership organizations. Examples include Aspen Network of Development Entrepreneurs (ANDE), a global network of more than 110 organizations that works to advance entrepreneurship in the developing world, and Global Impact Investing Network (GIIN), a not for- profit organization dedicated to increasing the effectiveness of impact investing.

Key Trends

Impact investment is a trend within the broader Responsible Finance field, yet it merits special consideration as a distinct subsector. This is because there are a number of specific trends and challenges unique to this industry that were identified through stakeholder discussions. In addition, it appears to be a flourishing area of responsible investment within the Indian context.

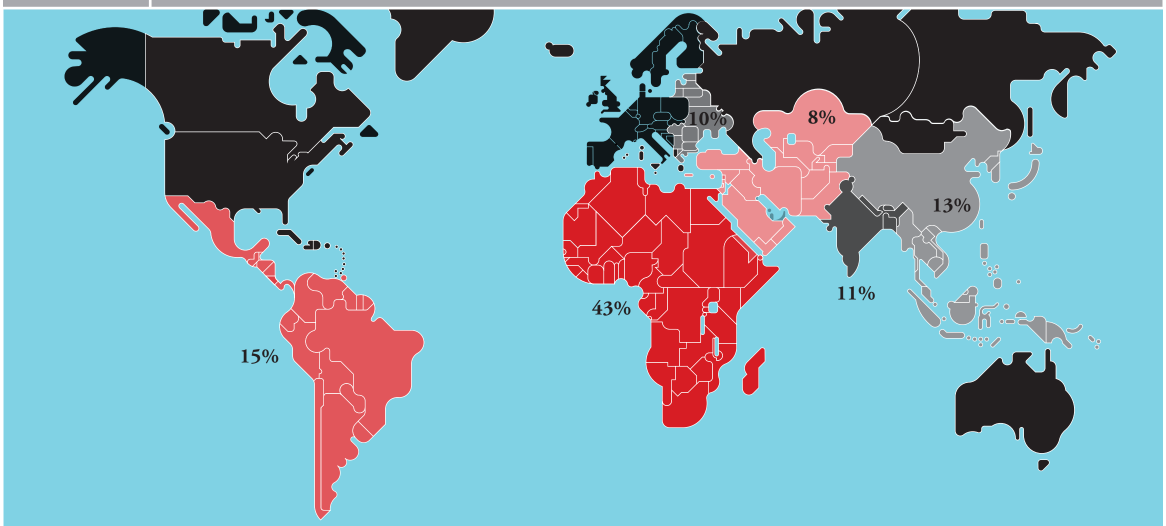
A New Asset Class

The mainstreaming of impact investing as a new asset class is emerging as a trend according to stakeholders consulted. They say that there is a 'huge growth of interest' among investors and new types of investors such as infrastructure investors, and bilateral agencies, which is seen as 'encouraging'. This finding is supported by research by GIIN, who has also noted the interest among High Net Worth individuals.[202] One of the key drivers behind the trend of impact investing is that slow down of growth in the industrialized economies and a new focus on emerging markets where approximately 70% of the world's economic growth over the next few years.[203] Another driver for this, according to stakeholders consulted is that grant making trusts are seeking capital preservation during the economic slowdown and this is an approach to ensure that 'foundation money doesn't run dry'. Nevertheless, there are concerns voiced among sector experts in India that a bubble is forming and perhaps there is 'more talk about investments than those investing' and that when 'the anticipated double digit growth doesn't materialize interest in impact investing may reduce'.

Geographic Focus on Emerging Markets

There is an industry trend in the geographic locations of investments. In addition to Brazil and Sub-Saharan Africa, India is a large market for impact investments according to both international and India based stakeholders in the field, as well as literature on the theme. A 2011 study found that within Asia, Africa and the Middle East, there was a concentration of activity by impact investors in India and Africa.[204] Figures from 2009 value the Indian impact investing industry at US $50 billion and South Asia, as a region represented 11% of impact investments between 2008-10.[205] However, while the investment base is primarily in the emerging markets and Sub Saharan Africa, most of the investments are according to those consulted 'capitalized by international rather than local money'.

Figure 8 Geographic Spread of Funds Investment Regions



Africa
Latin America
Middle East
South and South East Asia
Central and Eastern Europe
East Asia

Note: N=217, does not include 3 funds with unknown investment regions.
9 funds investing in multiple regions are counted once for each region.
Data includes funds launched and publicly known to be fundraising between 2008-2010
Source: Dalberg analysis (2001-1H2010)

Source: *ANDE 2011*

Thematic Focus

There is a global trend for impact investors to focus on a number of main themes which can be broadly categorized in terms of basic needs, such as agriculture, water, and housing, and basic services, such as education, health, energy, and financial services.[206 207 208] This corresponds to the feedback received by stakeholders during the consultation for this publication. In addition, stakeholders indicated that there is a growing interest specifically in women entrepreneurs, which aligns with the focus of multilaterals and governments at an international policy level. For example, Start Up India has worked with the ICRW and the Cherie Blair Foundation in India exploring technology and women entrepreneurs. In addition, at an international policy level the G20 is focusing on the same segment as part of its ongoing efforts to increasing access to finance for women entrepreneurs.[209]

It should be noted that stakeholders recognize an emerging trend that there are different funding requirements between sectors as well as expected returns, and this is becoming clearer as the industry is maturing. Furthermore, there is a sense among stakeholders that some sectors will be better suited to impact investments and certain types of financing than others.

Impact Measurement and Engaged Investing

The nature of impact investors is that positive social, economic or environmental change is an anticipated consequence of the investment. This has led the sector to currently be focused on measuring impact and defining performance metrics, according to those consulted. However, there is the view that 'not everyone understands how to measure impact', which is a trend that has also been noted in the literature.[210]

This relates to how impact is defined, which is also subject to much discussion within the sector. For example, some consider building basic infrastructure such as roads or schools as 'impact investment' as the products themselves are inherently serving an environmental or social purpose. Yet, others would disagree as they argue it is not just what you are building but how you go about it is also important. In the same way as when considering community investment, it is not just how much you give but on how you made the money in the first place? [211]

Impact investors are engaging with their clients and increasingly discussing the non financial performance of their clients after the investment and support them in capacity building efforts. A related trend is the development of metrics and tools to measuring the extent of impact. For example, PULSE, developed by the Acumen Fund in collaboration with Google, helps organizations track and benchmark financial, operational, environmental, and social data. As a tool it uses the Service Cloud feature of Salesforce.com, an open source software application.[212] In addition, a tool called Impact Reporting and Impacting Standards (IRIS) is being applied by investors as a tool and common taxonomy to measure ESG with a simple, universal rating by star.[213] Furthermore, there is a credit rating tool that has been developed by GIIN called Global Impact Investing Rating System (GIIRS), which generates company and fund impact ratings for comparative use.[214] GIIN has an online database of impact funds called Impact Base and in February 2012 they published a guide called 'Assessing Impact Strategy' to support investors' converse with fund managers about impact objectives.[215]

Questions for Discussion

1. Which inclusive business models are going to emerge as those most suitable for impact investing?
2. Which new geographies will emerge as leaders in impact investing? Why are some countries yet to receive impact investments? Is it that there are regulatory barriers for this asset class, or are they simply geographic blind spots?

Barriers and Challenges

The stakeholder consultation for this paper identified a number of key challenges facing the impact investing sector in the Indian context, many of which are recognised challenges more broadly in the sector. The challenges noted for India include:

Information Asymmetry and Lack of a Pipeline

In India there is more impact investment capital available than deals and investment opportunities in the pipeline – something that is referred to as information asymmetry, according to those consulted. As a consequence, concern was raised by some Indian based stakeholders that investors end up investing in the same small selection of companies. The explanation provided for this was that many enterprises are not investment ready; hence, investment readiness is a related challenge. In addition, the venture capital market itself is still described as being in a 'nascent stage' and underdeveloped.

Capacity and Investment Readiness

Sourcing good talent is one of the primary challenges for impact investors in India, according to those consulted. While there is no perceived shortage of brilliant ideas, there is a feeling that there are not enough adequately skilled entrepreneurs to implement these ideas. Capacity development is required in terms of financial management, market research, and technology access as well as business plan development. This challenge is backed by literature on the theme.[216] This issue is being addressed through initiatives by Acumen with its Fellowship Program and also India Unlimited which is rolling out a capacity building program in Mumbai.[217]

Lack of Seed Funding

Early stage financing during the initial couple of years of a business may be increasing in India but there remains a dearth of organizations that invest at the US$100,000 and below level, according to sector experts. The perception is that investing at this stage is high risk however without providing capital at this stage of a business' development it will be difficult to ensure an adequate pipeline of start up enterprises moving on to the next level of growth.

The international literature on small and growing businesses and organizations also acknowledges this challenge. The sector seeks to overcome this through exploring innovative financing structures for these types of businesses. There are still questions about what kind of financing is needed to plug this gap. Is the answer exploring new groups of investors such as retail investors who may be interested in providing equity finance for a business they believe in? If so, to date there are no existing mechanisms enabling them to make such investments, hence these mechanisms would have to be further explored. Alternatively, does the answer lie in new innovative debt financing products tailored to the needs of social businesses? If so, what characteristics would these products have to feature to meet the needs of innovative and social enterprises, as well as ensure that they are financially viable for banks? In turn, do impact investors need to innovate around their own business models to cater to these needs or would they be addressed by banks?

The root cause of the lack of financing available at this stage of business growth is the perception of risk and the fact that the many businesses fail during this crucial start up period. Hence does the answer lie in improving mechanisms to identify the creditworthiness of SMEs? The Entrepreneurship Finance Lab Research Initiative at the Centre for International Development, Harvard Kennedy School in the USA has been exploring solutions to this challenge. They have developed of a psychometric test to determine the credit worthiness of SMEs to enable banks to be able to predict the riskiness of investing in businesses without collateral.[218]

A Lack of Local Capital and Engagement by HNW Individuals

In India all of the impact investments are capitalized by international rather than local investors, according to those interviewed. There is a ready source of High Network Individuals that could potentially invest but there is a noted tendency for them to invest in community initiatives. This India specific trend and challenge does not hold internationally where HNI, such as Bill Gates, has been behind some of the largest impact investments globally.

Transaction Costs

It takes significant efforts to create a transaction, to find the right idea and entrepreneurs and undertake the due diligence required before an impact investment. The time and effort remains the same regardless of the size of the deal, as do other transaction costs. Therefore this represents a barrier for impact investments in general and a disincentive for 'small ticket deals'. Even though there are some innovations in India to bring costs down, such as through the Artha Platform, there is a strong need to overcome this barrier in order to encourage smaller size investments. The Artha Platform is an online community and website dedicated to building relationships between impact investors and donors, and social entrepreneurs, support information sharing as part of the pre-investment due-diligence process to overcome the barrier of high transaction costs, and capacity building support organizations working on or in India.[219]

Scalability

There is a 'huge fascination with scale' right now in India, according to those consulted. Impact investors are looking to upscale their existing business models within India, driven by both profit and impact motives. Yet there are perceived challenges in scaling up enterprises once they are commercially viable. The literature has also recognized failure to scale as a problem. The IFC notes that this can mean inclusive businesses consequently fail to realize their potential for financial and development impact.[220] Hence, to overcome this challenge, it has been noted internationally that there is a need to identify the success factors and enablers for how business models can scale.[221]

Nevertheless, there are some concerns voiced by experts in the field that perhaps there is too much focus on scalability, especially given the fact that some of the entrepreneurs are reluctant to scale up. Therefore, there is scope to further explore replication of business models. Further to this, there could be room to cross pollinate successful social enterprises in other markets, by bringing viable models from Brazil and South Africa, to India and vice versa. Further to this, there is scope to explore not just what needs replication but how it can be replicated, for example, through corporate partnerships.

Defining Impact and Performance

While there is a trend to measure impact, defining environmental and social performance is recognised as 'complex' by sector stakeholders as there is no universal benchmark. There is also a tension within the sector from a philosophical perspective about what impact actually is. How to measure impact in a standardized way is a therefore recognised by international and Indian impact investor stakeholders as a real challenge. This is supported by literature on the theme, which identifies inadequate impact measurement practice as a key challenge, along with the related challenge of a lack of a common vernacular for talking about impact investing.[222] Only if this information is available, the sector will be able to understand which sectors and where money will have the biggest impact.

Exits

An 'Exit' refers to a transaction undertaken by an impact investor to recoup the initial equity investment. According to the stakeholders consulted for this research, there have only been a couple of impact investment exits in India to date. The longer investment timeframes than standard investments means that Indian based investors are raising questions as to whether impact investors can be profitable and whether there is a bubble developing in the market. Hence exit opportunities are perceived as 'a definite challenge' in India in the view of those consulted. This view corresponds to international survey findings among investors which identifies 'few exit opportunities' and 'lack of track record of successful investments' as challenges to industry growth.[223]

In addition to exits per se, the method of exit is also perceived to be a challenge in India. According to those consulted, the typical investment cycle is 5 years. After which an initial public offering (IPO) is made by the company and the equity investors receive a payout. However, Initial Public Offerings IPOs are perceived to be difficult in India and so it is perceived to be a less likely exit strategy. Instead, consulted stakeholders expect exits to have to be managed through strategic sales. This would be where a larger company, for example a multinational company, may purchase the business in its entirety as it is aligned to the parent company's core business. Consequently, some stakeholders in the industry see a need for developing a secondary market for impact investments. Until these markets develop, there is a perception that the holding periods for impact investments will continue to extend beyond the typical 5 year investment period.

Questions for Discussion

1. Is a bubble emerging in the impact investment market?
2. What kind of financing is needed to plug the gap in seed financing? Is the answer exploring new groups of investors such as retail investors who may be interested in providing equity finance for a business they believe in?
3. What mechanisms could be developed to enable retail investors make impact investments?
4. What characteristics would new innovative debt financing product require if they are to be tailored to the needs of social businesses?
5. Do impact investors need to innovate around their own business models to cater to these needs or would they be addressed by banks?

Footnotes

186 Responsible Research, 2011
187 Responsible Research, 2011
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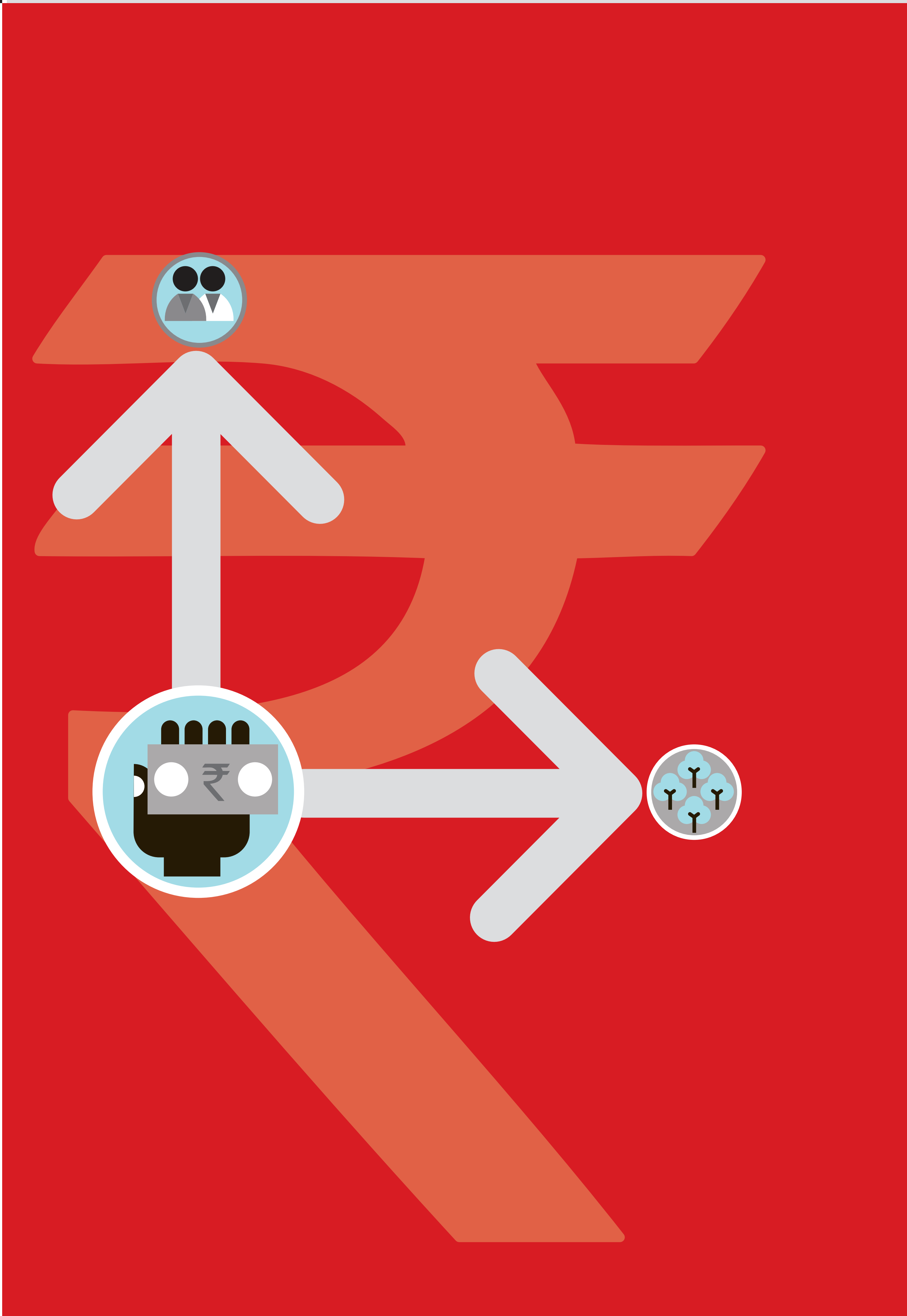


6 Recommendations and Conclusions

The financial sector is increasingly recognized as playing a catalytic role in driving responsible business as it moves away from using financial performance as the only criteria to assess business risk and opportunities. Responsible Finance is not a new international phenomenon but it is gaining significant momentum as increasing value is being placed on environmental and social assets alongside financial capital. Mainstream banks and investors, particularly those with long term investment horizons such as pension funds, are now integrating environmental and social considerations into their lending and investment decision making. In turn, their business strategies are changing as they not only consider their non financial operational risks, but also those that are presented in their lending and investment portfolio. This shift is having an impact on the broader ecosystem, which has to adjust to these changes. As these financial stakeholders demand information on companies' policies, practices and performance to inform their decision making, companies are also changing their behavior under the influence of these key stakeholders, driven by the need to secure financial resources.

This study has indicated that there are global trends showing increased supply and demand for Responsible Finance. This paper has also indicated that even though there are similarities in trends, such as the increase in ESG disclosure, and systems to analyze and rate non financial performance, there is a disparity between international and India specific trends. While there have been some welcome policy developments in India with the SEBI mandate, MCA's National Voluntary Guidelines and the expected changes outlined in the forthcoming bill emphasizing corporate disclosure on a report or explain basis, there is still a long way to go to achieve the levels of engagement and mainstreaming noted on an international scale.

Furthermore, more work is still required to promote a basic understanding of the relationship between non financial and financial performance among investors, banks and corporates. In India, the term Responsible Finance is most widely associated with responsible lending, both in terms of multilaterals promoting 'green finance' in the country, financial inclusion and literacy, and among some stakeholders the emerging area of impact investing is associated. Hence, significant capacity building and awareness raising is required to broaden this understanding.

In addition, to achieve responsible business through greater Responsible Finance some additional key challenges need to be addressed. Of high importance is addressing the need for greater transparency by corporates on their non financial policies, practices and performance. It is only through this that financial players can hold companies accountable if they have not adequately managed to mitigate and take advantage of these environmental and social risks and opportunities. While regulation is not palatable for many, it can concluded that there is a strong believe among stakeholders that 'carrots don't work in India' and, hence, regulation may have to be considered to achieve the levels of disclosure required to enable effective functioning of a Responsible Finance system in the country.

These findings highlight the compelling need to encourage both the demand and supply of Responsible Finance among investors and banks within India, to achieve anticipated market potential and to further use Responsible Finance as a driver for responsible business.

Consequently, it can be concluded that the Indian market for Responsible Finance is yet to mature and in a 'nascent stage' given characteristics of the system, and country specific challenges. This is even compared to the more mature but still niche responsible finance market internationally. In addition, in India traditional methods of active engagement by investors to influence company behavior are limited. Nevertheless, there are promising signs of change. India is a leader in terms of efforts to address the need for financial inclusion; international development financial institutions like the IFC, the World Bank and KfW are encouraging change as they require Indian financial institutions to implement such ESG policies and practices; and in addition there is an interesting area of development and significant activity in the impact investment market in India even though this is primarily being capitalized by international investors. Looking to the future, stakeholders consulted do see a market for banking and investment products in India that address the country's pressing social and environmental challenges such as the need for water and renewable energy supplies. Hence, the anticipation is that there will be an increased allocation of financing for businesses focused on addressing water scarcity and transformation to a low carbon economy, given the new business opportunities that may be opening up in these areas.

In light of the challenges, findings and conclusions of this report, there are number of recommendations that have been generated through this research about how Technical Assistance and GIZ can promote the Responsible Finance Agenda both internationally and in India and overcome the key barriers identified.

For Technical Assistance and GIZ Internationally

These findings suggest that GIZ can further promote the Responsible Finance agenda internationally by:

Advocacy and Networking

- Advocate and support policy development at the international level on Responsible Finance including forums such as the G20.
- Collaborating with other international stakeholders such as the Global Reporting Initiative and the International Integrated Reporting Committee on the standardization of sustainability and integrated reporting standards, and to advocate corporate disclosure. This would serve to promote corporate transparency and accountability and contribute to overcoming the lack of disclosure and standardization of metrics a key barrier to Responsible Finance.
- Support the UN backed Principles for Responsible Investment, UNEP FI and the UNPIFF in engaging on the topic of Responsible Finance to encourage financial institutions to publicly commit to such practices, which is the first step on the journey of integrating ESG criteria into investment and lending decision making and to financial inclusion.

Capacity Development

- Develop new partnerships and bridges between different stakeholders including investors, banks, NGOs, and stock exchanges in emerging markets like China, India and Brazil for purposes of knowledge sharing and capacity development.
- Build the capacities of investors and banks, particularly those with a focus on emerging markets, to provide them with training, tools and knowledge on the non financial risks in emerging markets, as well as how to go about managing these risks and opportunities. For example, different formats could be hosted in London, New York and Frankfurt, to update investors on the risks and realities of investing in emerging markets.
- Strengthen capacities of business sector to manage, disclose and report non-financial performance and risks in order to improve the availability and quality of data

For Technical Assistance and GIZ in India

The findings of this research and the results of the stakeholder consultations indicate that GIZ could promote the Responsible Finance agenda in India by:

Advocacy and Networking

- Supporting policy development by the Reserve Bank of India, Ministry of Corporate Affairs, Ministry of Finance among others. This can include supporting the development of responsible investment guidelines for investors and banks, and the integration of ESG risks and opportunities in sector reform agendas;
- Work with the Government to develop policies to incorporate ESG policies for its National Innovation Fund, Pension Funds, the State Banks, Insurance companies and sovereign wealth funds and Venture Capital funds;
- Collaborate with the MCA to develop sector specific reporting guidance for the National Voluntary Guidelines to support the reporting on material risks and opportunities by companies and encourage the disclosure;
- Advocate the government establishes a procurement policy where it commits to a specific spend of government contracts with SMEs and women/minority owned enterprises;
- Facilitating the development of a central repository for company sustainability data in India to improve the data collection of this information on companies, which can in turn be used by investors to support their decision making;
- Strengthen banks' capacities to integrate non-financial risks management in their MSME portfolio, e.g. through development of a simplified E&S appraisal process that banks can use for assessing SME during the financing credit process;
- Raise awareness among companies and SMEs on the responsible business case through communications campaigns and training programmes;
- Support the establishment of a UN PRI focal point in India to work to develop a responsible investor network in India, and encourage investors to become signatories to the statement;
- Collaborate with the Equator Principles on running workshops on the principles in India to encourage Indian banks to sign up to the principles;
- Partner with ANDE, GIIN, WBCSD, the Emerging Markets Disclosure Projects and others on workshops in India on topics of sustainable development, inclusive business, and Responsible Finance; and
- Collaborate with trade associations such as the Indian Banking Association and the stock exchanges, and the National Foundation for Corporate Governance on awareness building efforts in India among both banks and investors.

Capacity Development and Implementation

- Raise awareness of investors and banks on the concept of Responsible Finance and the benefits of ESG management and disclosure from both a risk and an opportunity perspective. This can be through the development of education materials and training to understand the social risks to companies for example, their human rights, labor rights and community related risks to their business.

Investors

- Work in bilateral partnerships with the IRDA, LIC, PFRDA and the state pension funds, and National Innovation Council to integrate ESG factors into their financing decision making
- Work with investors in partnerships to develop strategies for active engagement on ESG factors with companies post investment.
- Partner with German insurance companies with joint ventures in India to build awareness and encourage the India insurance industry to manage their ESG risks, as well as part to develop new systems.

Banks

- Work in bilateral partnerships with the State banks to develop policies and processes to enable them to integrate ESG factors into their decision making and for them to consider long term non financial risks;

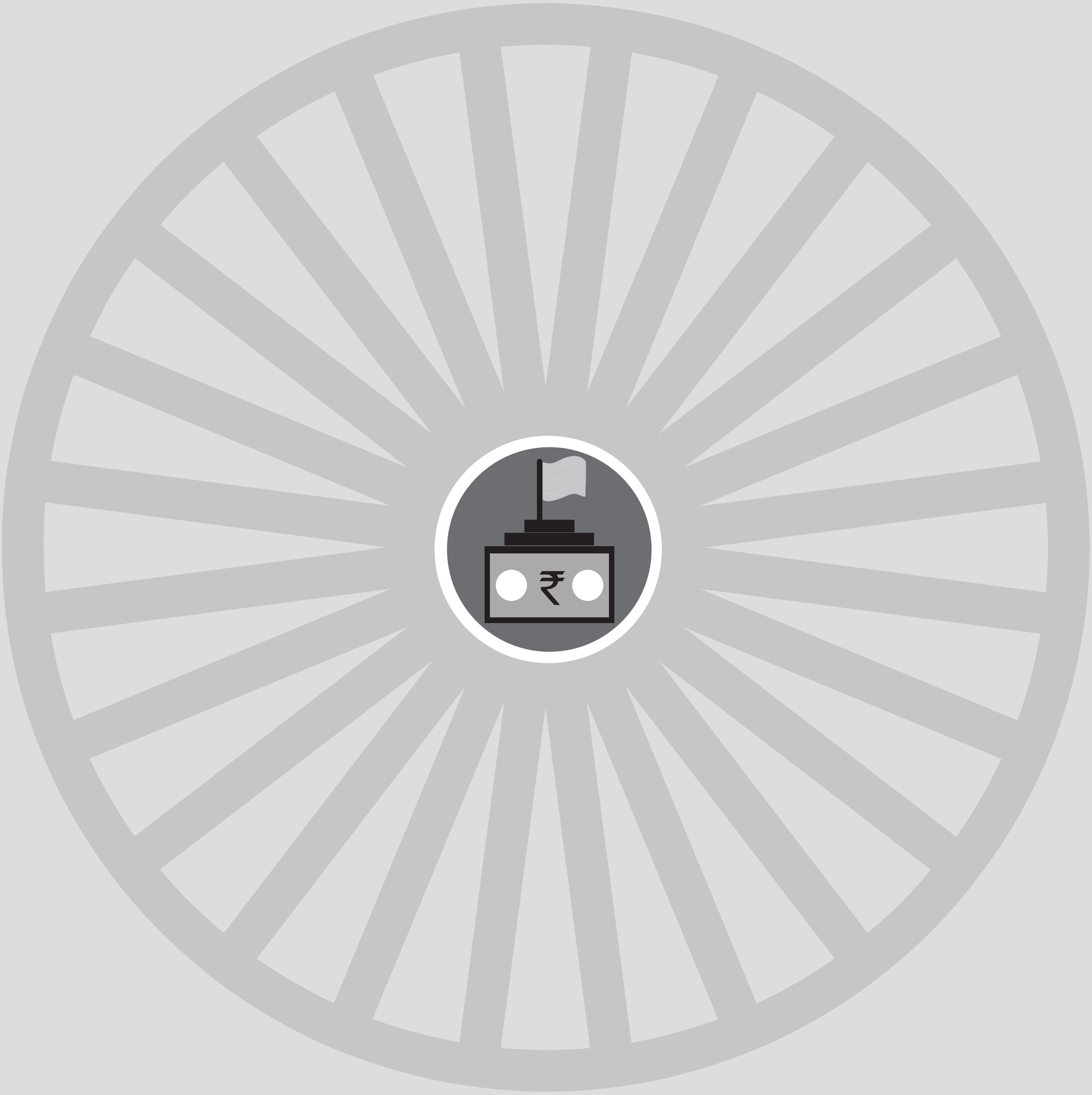
- Support banking product development with State banks on products that take into account ESG criteria e.g. on water products, or promote financial inclusion through tailoring to meet the needs of women entrepreneurs/ SME owners.

Impact Investors

- Fund an existing incubator to provide financial support to start up businesses in emerging markets;
- Set up a social enterprise incubator to increase the pipeline of enterprises for impact investing;
- Collaborate with existing incubators to provide capacity building and skills development for social enterprises in order to improve their investment readiness for impact investments;
- Run competitions or training programs for entrepreneurs to connect them to investors and funding sources; and
- Finance a CIM expert to work as a shared technical resource for multiple startups to address the financial management skills talent gaps during the early stage of business development.

Research and Knowledge Sharing

- Research and share best practice on the extent to which companies in India are implementing the newly established government CSR schemes and identifying best practice examples of where they are going beyond philanthropy to focus on social and environmental impacts of their business;
- Research the regulatory barriers that small businesses are facing and address the regulatory barriers;
- Develop a publication series detailing the material risks and impacts of key sectors. These could be used by companies to understand what risks and opportunities they should be managing and by investors to understand the material issues they should be considering in their investment decision making;
- Collaborate with academic institutions on research on inclusive financing models in India and market linkages to support rural based SMEs to get their products to market; and
- Research models and create platforms for communication and cross pollination of inclusive business models, successful factors for scalability of these enterprises and options for franchising both within India and internationally.



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Start up India, Manisha Gupta
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Trucost, Cary Krosinsky
Unlimited India, Pooja Warier
WBCSD, Caroline Twigg, Marcel Engel
World Bank, Niraj Verma
Yes Bank, Nitin Sukh

Appendices

Appendix 1: Key Sector Stakeholders

The following table sets out some of the organizations involved in Responsible Finance related to each category of stakeholder.

Category	India	International
Academics	IIM Ahmedabad	• Initiative for Responsible Investment, The Hauser Centre for Non Profits, at Harvard Business School, USA • Corporate Social Responsibility Initiative (CSRI) at Harvard Kennedy School, John F. Kennedy School of Government, Harvard University, USA. • Entrepreneurship Finance Lab Research Initiative at the Centre for International Development, Harvard Kennedy School, USA. • Boston University: Boston Area Sustainable Investment Consortium, USA Institute for Social Research, Stockholm University, Sweden • Socially Responsible Investment Department, Faculty of Law, at the University of Toronto, Canada • The Banking Environment Initiative (BEI), Programme for Sustainability Leadership, University of Cambridge, UK • Skoll Centre for Social Entrepreneurship, Säid Business School, University of Oxford, UK. • The Global Social Benefit Incubator (GSBI™), a program developed by Santa Clara University's Center for Science, Technology, and Society, USA.
Asset Managers and Asset owners	**Asset Managers** Re Capital TATA Asset Management Co. IL&FS IDFC Mutual Funds **Pension Funds** Employees' Pension Scheme Employees' Provident Fund	**Asset Managers** • Domini Social Investments, USA • ESG Managers Portfolio, Portsmouth, UK • Hendersons, USA • SAM, Switzerland • Calvert, USA • Pax World, USA • Robeco, Netherlands • Sustainable Asset Management (SAM), Switzerland OMIGSA, South Africa

- National Pension Scheme (NPS)
- Public Provident Fund

Insurance Companies

- Life Insurance Corporation of India (LIC)
- SBI Life Insurance Co. Ltd

Foundations

- Dhan Foundation
- Edelweiss Corporate
- Foundation
- Skoll Foundation*
- The Nadathur Group (and its Samhita Initiative)

- Generation Investment Management, USA
- Element Investment management, South Africa
- Public Investment Corporation, South Africa
- Aviva Investments,UK
- Dexia Asset Management, Belgium
- Vigeo, France

Foundation

- The Gates Foundation, USA
- Rockefeller Foundation, USA
- Schwab Foundation, Switzerland
- Shell Foundation, The Netherlands

Pension Funds

- CalPERS, USA
- CalSTRS, USA
- Connecticut State Pension Fund, USA
- Government Pension Fund Global, Norway
- Hermes, UK
- New York State Common Retirement Funds, USA
- The Government Employees Pension Fund (GEPF), South Africa

Insurance Companies

- Allianz, Germany
- Aviva, UK
- Munich Re, Germany
- Storebrand Insurance Co, Norway
- Swiss Re, Switzerland

Banks & Investment Banks

- HDFC
- HSBC*
- ICICI Bank
- IDBI
- ING Vysya
- KBSLAB
- NABARD
- RBI
- SBI
- SIDBI
- Syndicate Bank
- Yes Bank
- Standard Chartered Bank*
- IDFC
- IL&FS
- Punjab National Bank

- Banco Central do Brasil, Brazil
- Credit Suisse, Switzerland
- Deutsche Bank, Germany
- Goldman Sachs, USA
- ING, Netherlands
- Itau Banco, Brazil
- J.P. Morgan, USA
- Morgan Stanley, USA
- Royal Bank of Scotland, UK
- Shorebank International, USA
- Triodos Bank, Netherlands
- UBS, Switzerland

Bilateral Agencies and Development Banks

- GIZ, Germany
- KfW, Germany
- DFID, UK
- JICA ,Japan
- SIDA ,Sweden
- USAID, USA
- CDC,UK

Consultants

- Asian Operations of
- Mercados – Energy Markets
- International*
- Grameen Capital
- Intellecap*
- Monitor Group*
- McKinsey's*
- Mercer*
- NEXGen Financial Solutions
- Adelphi, Berlin
- Morningstar Associates llc, USA
- United Capital, USA
- CSR Asia, Hong Kong
- OWW Consulting, Malaysia
- Viridis Strategy Group (formerly Esty Environmental
- Partners (EEP)), USA.

Governments

- Ministry of Finance (MoF)
- Ministry of Corporate Affairs (MCA, IICA)
- Ministry of Environment and Forest(MoEF)
- Ministry of Micro, Small and Medium Enterprises (MoMSME)
- Ministry of New and Renewable Energy(MNRE)
- The Planning Commission.

Impact Investors

- Aavishkaar*
- Acumen Fund*
- Ashoka
- Coastal Enterprise
- Elevar Equity
- Ennovent - SocialEnterprise Fund
- First Light*
- Grayghost Ventures*
- India Unlimited
- LGT - VP
- Mumbai Angels
- Omidyar Network
- Power Finance Corporation
- Unitus Impact
- Start Up! India
- Unitus Capital
- Venture East
- Villgro Capital
- Bamboo Finance, USA
- Calvert, USA
- Grassroots Business Fund, USA
- GroFin, Africa
- New Island Capital, USA
- Pax World, USA
- Warburg Pincus, USA
- Willow Tree Impact Investors
- Actis, UK
- Bridge Ventures, UK

Multilaterals	• World Bank* • Asian Development Bank • (ADB)* • International Finance Corporation (IFC)*	• UN PRI • UNEP FI • UNGC • G20 • OECD
NGOs	• GRI* • CDP* • WBCSD* • WRI* • Aspen Network of • Development Entrepreneurs • (ANDE)* • Dasra • India Philanthropy Network Partners in Change (PiC)* • Small Business Banking • Network SANKALP Forum • Society for Research and Initiatives for Sustainable Technologies and Institutions (SRISTI) • Swayam Sikshan Prayog (SSP) • TERI • The Hub, Mumbai	• Amnesty International, USA • B-Lab, USA • Generation Impact, USA • GIIN, USA • Global Environment Fund, USA • Toniic, USA • Natural Value Initiative, USA • SNV, The Netherlands • International Seed Federation, Italy • Investor Network on Climate Risk (INCR), USA • Root Capital, USA • Social Edge (online community), USA • Village Capital, USA • Ceres, USA • Tellus Institute, USA • Interfaith Center on Corporate Responsibility, USA • Samhita,
Regulators	• IRDA • PFRDA • SEBI • RBI	
Research and Data Providers	• Bloomberg* • cKinetics • CRISIL • MSCI* • S&P* • Responsible Investment • Research Association • GTrade • S&P ESG Index	• Chevreux International, France • EIRIS, UK • Jantzi Research, Canada • Responsible Research, Singapore • Sustainable Investment Institute (Si2), USA • Sustainanalytics, The Netherlands • Trucost, UK • Dow Jones Sustainability Index, USA • FTSE4Good, UK • Jantzi Social Index, The Netherlands • NASDAQ , USA • S&P Indices, USA • BM& BOVESPA Corporate Sustainability Index, Brazil
Stock Exchanges	• National Stock Exchange • Bombay Stock Exchange	• BM&F BOVESPA, Brazil • Deutsche Börse, German • Johannesburg Stock Exchange, South Africa • London Stock Exchange, UK

		• New York Stock Exchange (NYSE), USA • Shanghai Stock Exchange, China • Shenzhen Stock Exchange, China
Trade Associations & Networks	• CII • Indian Banks' Association • IREDA	• The Federation of Environmental Trade Associations (FETA), UK • World Federation of Exchanges, France • US SIF, USA • EURO SIF, UK • Association for Sustainable and Responsible Investment in Asia (ASIA), Hong Kong UK SIF, UK • Institutional Investors Group on Climate Change • (IIGCC), Europe • The Investor Group on Climate Change (IGCC), • Australia and New Zealand • Investor Network on Climate Risk (INCR), USA • Global Impact Investor Network (GIIN), USA • Asian Venture Philanthropy Network (AVPN), Singapore • European Venture Philanthropy Association, Belgium

Note: Organizations marked with (*) are International organizations active in India

Appendix 2: Top 50 Financial Services Sector Company List[224]

Rank	Name	Country	Industry	Market Cap in dollar million (Sept, 2011)
1	Industrial & Commercial Bank of China	China	Banks	251,078
2	China Construction Bank	China	Banks	232,609
3	Berkshire Hathaway	US	Nonlife insurance	206,671
4	JP Morgan Chase	US	Banks	183,640
5	HSBC	UK	Banks	181,937
6	Wells Fargo	US	Banks	167,416
7	Bank of China	China	Banks	145,978
8	Agricultural Bank of China	China	Banks	141,363
9	Bank of America	US	Banks	134,915
10	Citigroup	US	Banks	128,704
11	Itau Unibanco	Brazil	Banks	99,720
12	Banco Santander	Spain	Banks	98,120
13	China Life Insurance	China	Life insurance	94,681
14	Royal Bank Canada	Canada	Banks	88,019
15	BNP Paribas	France	Banks	87,789
16	Commonwealth Bank of Australia	Australia	Banks	83,937
17	Sberbank of Russia	Russia	Banks	83,577
18	Goldman Sachs	US	Financial services	82,552
19	Toronto-Dominion Bank	Canada	Banks	77,950
20	Westpac Banking	Australia	Banks	75,705
21	Bradesco	Brazil	Banks	71,982
22	UBS	Switzerland	Banks	69,007
23	Bank of Nova Scotia	Canada	Banks	65,958
24	Mitsubishi UFJ Financial	Japan	Banks	65,564
25	Ping An Insurance	China	Life insurance	65,121
26	ANZ Banking	Australia	Banks	63,933
27	Allianz	Germany	Nonlife insurance	63,872
28	Lloyds Banking Group	UK	Banks	63,388
29	American International Group	US	Nonlife insurance	63,094
30	Standard Chartered	UK	Banks	60,865
31	National Australia Bank	Australia	Banks	58,001
32	Bank of Communications	China	Banks	55,027
33	Deutsche Bank	Germany	Banks	54,721
34	BBVA	Spain	Banks	54,559
35	American Express	US	Financial services	54,349
36	Barclays	UK	Banks	54,214
37	Banco Brasil	Brazil	Banks	51,965
38	US Bancorp	US	Banks	50,889
39	Credit Suisse Group	Switzerland	Banks	50,604
40	China Merchants Bank	China	Banks	48,845
41	Societe Generale	France	Banks	48,566
42	Axa	France	Nonlife insurance	48,547
		Netherlands	Life insurance	48,544

43	ING	Italy	Banks	47,772
44	Unicredit	US	Life insurance	47,197
45	Metlife	Brazil	Banks	46,257
46	Santander Brasil	Sweden	Banks	44,281
47	Nordea Bank	Japan	Banks	44,121
48	Sumitomo Mitsui Financial	US	Financial services	42,227
49	Morgan Stanley	Switzerland	Nonlife insurance	41,203
50	Zurich Financial Services			

Appendix 3: Extract from Forthcoming Companies Bill

135. (1) Every company having net worth of rupees five hundred crore or more, or turnover of rupees one thousand crore or more or a net profit of rupees five crore or more during any financial year shall constitute a Corporate Social Responsibility Committee of the Board consisting of three or more directors, out of which at least one director shall be an independent director.

(2) The Board's report under sub-section (3) of section 134 shall disclose the composition of the Corporate Social Responsibility Committee.

(3) The Corporate Social Responsibility Committee shall,—

(a) formulate and recommend to the Board, a Corporate Social Responsibility Policy which shall indicate the activities to be undertaken by the company as specified in Schedule VII;

(b) recommend the amount of expenditure to be incurred on the activities referred to in clause (a); and

(c) monitor the Corporate Social Responsibility Policy of the company from time to time.

(4) The Board of every company referred to in sub-section (1) shall,—

(a) after taking into account the recommendations made by the Corporate Social Responsibility Committee, approve the Corporate Social Responsibility Policy for the company and disclose contents of such Policy in its report and also place it on the company's website, if any, in such manner as may be prescribed; and

(b) ensure that the activities as are included in Corporate Social Responsibility Policy of the company are undertaken by the company.

(5) The Board of every company referred to in sub-section (1), shall make every endeavor to ensure that the company spends, in every financial year, at least two per cent of the average net profits of the company made during the three immediately preceding financial years, in pursuance of its Corporate Social Responsibility Policy: Provided that if the company fails to spend such amount, the Board shall, in its report made under clause (o) of sub-section (3) of section 134, specify the reasons for not spending the amount.

Appendix 4: Summary of Sustainability Indices

Exchange (or company)	Index	Launch year	Country/Region
BM&F BOVESPA	BM& BOVESPA Corporate Sustainability Index	2005	Brazil
	Brazil Carbon Efficient Index	2010	Brazil
BMV	Bolsa Mexicana de Valores Sustainability Index	2011	Mexico
Bolsas y Mercados Españoles (BME)	FTSE4Good IBEX Index	2008	Mexico
Bursa Malaysia	Bursa Malaysia Sustainability Index	To be launched soon	Malaysia
Cairo Stock Exchange Market	S&P EGX ESG Index	2010	Egypt
China Securities Index Co.	CSI ECPI ESG China 40 Index	2010	China
Deutsche Börse	DAXglobal® Alternative Energy Index	2008	Germany
	DAXglobal® Sarasin Sustainability Germany Index	2007	Germany
	DAXglobal® Sarasin Sustainability Switzerland Index	2007	Switzerland
Dow Jones Sustainability Index	Dow Jones Sustainability Korea Index	2009	South Korea
ECPI	ECPI Ethical Emerging Markets Tradable Equity Index	2006	Global
FTSE	FTSE KLD Global Climate 100 Index	2008	Global
	FTSE KLD Global Sustainability (GSI) Index Series	2008	Global
Hang Seng Indexes	Hang Seng Corporate Sustainability Indexes	2010	China
Indonesia Stock Exchange	SRI-Kehati Index (with NGO-Kehati)	2009	Indonesia
International Securities Exchange	ISE Water Index Exchange	2000	Global
	ISE-CCM Green Energy Index	2001	Global
	ISE Global Wind Energy Index	2005	Global

Istanbul SE (2009)	Istanbul Sustainability Index	To be launched soon	Turkey
Johannesburg Securities Exchange (2010)	Johannesburg Stock Exchange Socially responsible investment Index	2004	South Africa
Johannesburg Stock Exchange	King III	2009	South Africa
Korea Stock Exchange	Korea Stock Exchange SRI Index	2009	South Korea
London Stock Exchange FTSE	FTSE4Good Index Series	2001	England
	FTSE4Good Environmental Leaders Europe 40 Index	2007	England
	FTSE4Good Australia 30 Index	2008	England
	FTSE Environmental Technology Index Series	2008	England
	FTSE Environmental Opportunities Index Series	2008	England
NASDAQ OMX	OMX GES Ethical Denmark Index	2008	Denmark
	OMX GES Ethical Finland Index	2008	Finland
	NASDAQ OMX® Clean Edge® Global Wind Energy Index	2008	Global
	Wilder NASDAQ OMX Global Energy Efficient Transport Index	2008	Global
	OMX GES OMXS30 Ethical Index	2008	Global
	OMX GES Ethical Nordic Index	2008	Nordic
	OMX GES Sustainability Nordic Index	2008	Nordic
	OMX GES Ethical Norway Index	2008	Norway
	OMX GES Ethical Sweden Index	2008	Sweden
	OMX GES Sustainability Sweden Index	2008	Sweden
	NASDAQ Clean Edge US Index	2006	USA
National Stock Exchange (2009) S&P	S&P ESG India Index	2008	India
New York Stock Exchange Dow Jones	Dow Jones Sustainability Indexes	1999	USA
NYSE Euronext	NYSE Arca Environmental Services Index (AXENV)	2006	USA
	NYSE Arca WilderHill Clean Energy Index (ECO)	2008	USA
	NYSE Arca WilderHill Progressive Energy Index (WHPRO)	2006	USA

	NYSE Arca Cleantech Index (CTIUS)	1999	USA
	Low Carbon 100 Europe® Index	2008	USA
	Euronext FAS IAS® Index	2006	USA
OWW Consulting	OWW Responsibility SRI Index Series	2006	Malaysia
S&P	S&P/IFCI Carbon Efficient Index	2009	Global
	S&P Hawkamah ESG Pan-Arab Index	2011	Middle East and North Africa
Shanghai Stock Exchange (2009)	SSE Social Responsibility Index	2009	China
Singapore Stock Exchange	Voluntary Guidelines for sustainability reporting	2011	Singapore
Tadawul (TASI)	Saudi Arabian Responsible Competitiveness Index (SARCI)	2008	Saudi Arabia
Tel-Aviv Stock Exchange	Maala SRI (Socially Responsible Investing) Index	2005	Israel
TMX Group	Jantzi Social Index	2000	Canada
Wiener Bourse (the Vienna Stock Exchange)	VBV-Österreichischer Nachhaltigkeitsindex (VÖNIX)	2005	Austria
	CEE Responsible Investment Universe Index	2009	Austria

Source (1): *http://www.world-exchanges.org/sustainability/m-7-0.php*
Source (2): *http://www.responsibleresearch.com/Responsible_Research___Sustainable_Stock_Exchanges_2010.pdf*

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Bamboo Finance,*www.bamboofinance.com*
Banco Central do Brasil *www.bcb.gov.br/*
Birla Sun Life Insurance Co. Ltd, *www.birlasunlife.com/*
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BM&F BOVESPA, *www.bmfbovespa.com.br/en-us/home.aspx*
Bombay Stock Exchange,*www.bseindia.com*
Boston University: Boston Area Sustainable Investment Consortium,*www.bostonsri.org/*
Bourse de Luxembourg,*www.bourse.lu/*
CalPERS *www.calpers.ca.gov*
CalSTRS *www.calstrs.com/*
Calvert *www.calvert.com/*
Care *www.care.org*
CDC *http://www.cdcgroup.com/*
CDP India *http://cdpindia.com/*
Chevreux International *https://www.cheuvreux.com/*
CII *www.cii.in/*
cKinetics *www.ckinetics.com/*
CLSA *www.clsa.com/*
Coastal Enterprise *www.ceimaine.org/*
Connecticut State Pension Fund *http://www.state.ct.us/ott/aboutpension.htm*
Credit Suisse *www.credit-suisse.com/us/*
CRISIL *www.crisil.com/*
Dasra *www.dasra.org/*
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EIRIS *www.eiris.org/*
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HDFC *www.hdfcbank.com/*

Henderson's *www.henderson.com/home/private_capital*

Hermes *www.hermes.co.uk*

HSBC *www.hsbc.com/*

ICICI Bank *www.icicibank.com/*

IDBI *www.idbi.com*

IDFC *www.idfc.com*

IL&FS *www.ilfsindia.com/*

IMPACTS *www.impacts.org*

India Philanthropy Network *www.avpn.asia/countries/india/*

Indian Banks' Association *www.iba.org.in/*

ING *www.ifan.co.in/*

ING Vysya *www.ingvysyabank.com*

Institute for Responsible Investment *http://hausercenter.org/iri/*

Institute for Social Research, Stockholm University *http://su-se.academia.edu/Departments/Swedish_Institute_for_Social_Research*

Intellecap *http://intellecap.com/*

International Finance Corporation (IFC) *www.ifc.org/*

International Securities Exchange *www.ise.com/*

International Seed Federation *www.worldseed.org/*

Investor Network on Climate Risk (INCR) *www.ceres.org/incr/*

IRDA *www.irda.gov.in*

IREDA *www.ireda.gov.in*

Itau Banco *www.itau.com.br/*

J.P. Morgan *www.jpmorgan.com*

Jantzi Research *www.sustainalytics.com/*

Jantzi Social Index *www.sustainalytics.com/*

JICA *www.jica.go.jp/english/*

Johannesburg Stock Exchange *www.jse.co.za/*

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KBSLAB *www.kbsbankindia.com*

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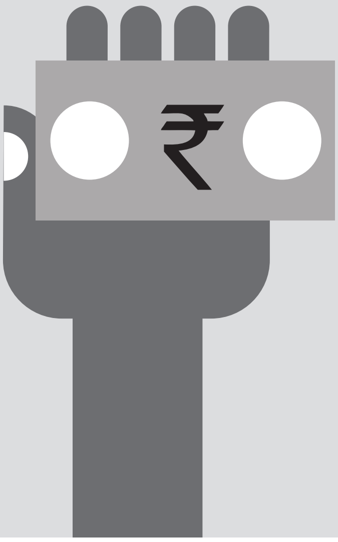
Ministry of Environment and Forest (MoEF) *http://moef.nic.in/index.php*
Ministry of Finance (MoF) *http://finmin.nic.in/*
Ministry of Micro, Small and Medium Enterprises (MoMSME) *http://msme.gov.in*
Ministry of New and Renewable Energy(MNRE) *www.mnre.gov.in*
Monitor Group *www.monitor.com*
Morgan Stanley *www.morganstanley.com*
Morningstar Associates llc *corporate.morningstar.com/us/asp/subject.aspx?xmlfile=23.xml*
MSCI *www.msci.com*
Mumbai Angel *www.mumbaiangels.com*
Munich Re *www.munichre.com*
NABARD *www.nabard.org*
NASDAQ Clean Edge US Index *http://www.nasdaq.com/newsroom/news/pr2006/ne_section06_060.stm*
NASDAQ OMX *www.nasdaqomx.com*
National Pension Scheme(NPS) *http://pfrda.org.in/*
National Stock Exchange *www.nseindia.com*
Natural Investments *http://naturalinvesting.com/*
Natural Value Initiative *www.naturalvalueinitiative.org*
New Island Capital *http://newislandcap.com/*
New Ventures *www.newventuresindia.org*
New York State Common Retirement Funds *www.osc.state.ny.us/pension/index.htm*
New York Stock Exchange *www.nyse.com*
NEXGen Financial Solutions *www.nexgenfs.com*
NYSE Arca Environmental Services Index (AXENV) *www.vaneck.com/funds/EVX.aspx*
Omidyar Network *http://www.omidyar.com/*
Partners in Change (PiC) *http://picindia.org/*
Pax World *www.paxworld.com*
PFRDA *http://pfrda.org.in/*
Power Finance Corporation *www.pfc.gov.in*
Prince of Wales' P8 Group *www.princeofwales.gov.uk/*
Public Provident Fund
RBI *www.rbi.org.in*
Re Capital *www.recapital.in*
Responsible Investment Research Association *www.ri-research.org*
Responsible Research *www.responsibleresearch.com*
Rockefeller Foundation *www.rockefellerfoundation.org*
Root Capital *www.rootcapital.org*
Royal Bank of Scotland *www.rbs.in*
S&P *www.standardandpoors.com*
S&P ESG Index *www.standardandpoors.com/indices/...esg-index/.../us/?indexId...esg-index*
S&P Indices *www.standardandpoors.com/indices*
SAM *www.sam-group.com*
Samhita *www.samhita.org*
SANKALP Forum *www.sankalpforum.com*
SBI *www.statebankofindia.com*
SBI Life Insurance Co. Ltd *www.sbilife.co.in*
Schwab Foundation *www.schwabfound.org*
SEBI *www.sebi.gov.in*
Shanghai Stock Exchange *www.sse.com.cn/en_us/ps/home.shtml*
Shell Foundation *www.shellfoundation.org*

Shorebank International *www.sbksbi.com*
SIDA *www.sida.se/English*
SIDBI *www.sidbi.com*
Skoll Foundation *www.skollfoundation.org*
Small Business Banking Network *www.sbbnetwork.org*
SNV *www.snvworld.org*
Social Edge (online community) *www.socialedge.org/features/resources/.../online-community-building*
Socially Responsible Investment Department, Faculty of Law, at the University of Toronto *http://www.law.utoronto.ca/visitors_content.asp?itemPath=5/5/3/0/0&contentId=1464*
Society for Research and Initiatives for Sustainable Technologies and Institutions (SRISTI) *www.sristi.org*
Standard Chartered Bank *www.standardchartered.co.in*
Start Up! India *www.startup-india.org*
Storebrand Insurance Co *www.storebrand.com*
Sustainable Investment Institute (Si2) *www.siinstitute.org*
Sustainanalytics *www.sustainalytics.com*
Swayam Sikshan Prayog (SSP) *www.sspindia.org*
Swiss Re *www.swissre.com*
Syndicate Bank *www.syndicatebank.com*
TATA Asset Management Co. *www.tatamutualfund.com*
Tellus Institute *www.tellus.org*
TERI *www.teriin.org*
The British Council *www.britishcouncil.org*
The Federation of Environmental Trade Associations (FETA) *www.feta.co.uk*
Toniic *www.toniic.com*
Triodos Bank *www.triodos.com*
Trucost *www.trucost.com*
UBS *www.ubs.com*
UN *www.un.org.in*
UN PRI *www.unpri.org*
Under the Mango Tree *http://utmt.in/*
UNEP FI *www.unepfi.org*
UNGC *www.unglobalcompact.org*
United Capital *www.unitedcp.com*
Unitus Capital *http://unituscapital.com/*
Unitus Impact *http://www.unitusimpact.com/*
Unltd. India *www.unltdindia.org*
USAID *www.usaid.gov/in*
Venture East *www.ventureast.net*
Village Capital *www.vilcap.com*
Villgro *http://www.villgro.org/*
Warburg Pincus *www.warburgpincus.com*
WBCSD *www.wbcsd.org*
Wiener Bourse (the Vienna Stock Exchange) *http://en.wienerborse.at/*
World Bank *www.worldbank.org.in*
World Federation of Exchanges *www.world-exchanges.org*
WRI *www.wri.org*
Yes Bank *www.yesbank.in*



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- Private Sector Development
- Social Protection
- Financial Systems Development
- HIV/AIDS-Blood Safety

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