

Guide to Sustainability Analysis Organisations

Published, in its first version, in October 2001 and updated in December 2007, the "Guide to Sustainability Analysis Organisations", provides an overview of all organisations with activities that consist of, or include, analysis and rating of the sustainability performance of companies.

A wide range of actors, companies and investors, in France and abroad, have recognized the usefulness of this guide, published in French and English.

The latest update to the Guide responds to a perceived need to take account of market evolution with respect to the primary concerns expressed by investors and fund managers, as well as companies and other stakeholders. The aim of the guide to sustainability analysis

organisations is to support attempts to identify all the rating players and help companies and investors select organisations by providing them with full information concerning their methodology and structure. New sections have been included relating to governance practice and the transparency of organisations.

Given the rapid evolution of such organisations (restructuring, disappearance and offers of new services), ORSE and ADEME have decided to launch an electronic version of the Guide, accessible on the Internet, in order to facilitate periodical updating.

The Guide and individual presentations of rating agencies may be downloaded at: www.orse.org

Evolutionary trends in social and environmental rating

Since 2001, there have been significant developments in the social and environmental analysis and rating market.

- **The analysis and rating market has continued its growth.**

New market players have been identified, especially in the United Kingdom and Asia (South Korea), organisations that have been restructured and players that have widened their financial competency to include sustainability analysis and rating.

Thus, in 2007, we recorded 30 sustainability analysis organisations and 12 groups of socially responsible stock indexes at the national, regional and global levels.

- **The funding model initially adopted by organisations in the 1980s and 1990s has evolved.**

When this market emerged, sustainability analysis organisations only satisfied requests for information from investors integrating sustainability criteria in their investment decision-making process.

These organisations are currently developing services for major listed and unlisted companies, small and medium enterprises, and other organisations such as local authorities, thus ensuring the diversification of their sources of revenue by widening the range of services they offer.

- **Diversity of approaches and methodology persists.**

A study of the approaches to, and methodology of, sustainability analysis organisations clearly shows the enduring diversity of both the objectives of sustainability analysis and rating, and the research and rating methodology adopted.

- **The regional specialization of such organisations has been confirmed.**

Most sustainability rating organisations only have regional coverage. These organisations offer their clients national and international coverage limited to a single region: Europe, Asia or North America. In response to the need to widen their coverage and offer ratings for a global universe, they have set up a system of international networks and partnerships.

- **Currently, initiatives are developing with the aim of professionalizing the sustainability analysis and rating market.**

Such initiatives have multiplied since 2001, in order to professionalize the market.

In August 2004, sixteen sustainability analysis organisations joined together to form the AICSRR (Association for Independent CSR Research), to "develop, promote and maintain high professional standards, expertise and professional conduct codes for the CSR research sector".

ORSE began participating in this push for the professionalization of relations between parties in 2001, when it drew up a "draft Charter of reciprocal commitment". This project, which grew out of discussions with a range of stakeholders, is more of a declaration of intention than a contractual document, the objective of which is to improve dialogue between companies and organisations.

Country	Organisation	Country	Organisation
Germany	IMUG	France	Vigeo*
Germany	OEKOM Research	Italy	Vigeo Italia**
Germany	Scoris	Italy	E Capital Partners
Australia	Caer	Japan	The Good Bankers
Australia	Siris	Holland	DSR
Belgium	Deminor Ratings	United Kingdom	Eiris
Belgium	Forum Ethibel	United Kingdom	Ethical Screening
Canada	Jantzi Research Inc.	United Kingdom	Trucost
South Korea	Eco Frontier Co	Sweden	GES Investment Services
Spain	FED	Switzerland	Centre Info
United States	Calvert	Switzerland	SiRi Company
United States	Innovest	Switzerland	Covalence
United States	KLD	Switzerland	Inrate
France	BMJ Ratings	Switzerland	SAM Research
France	Ethifinance (ODE)		

* On 16 June 2005, Vigeo and Ethibel agreed in principle to a merger of the two bodies, giving birth to the "Vigeo group"

** In december 2006 Avanzi SRI Research integrates Vigeo Group.

Financial rating: the market that established the principle of corporate rating

The financial rating market grew out of the need to inform investors of the quality of management of the companies in which they invest.

The business of financial rating agencies is, fundamentally, to evaluate, or "rate" the financial instruments issued or exchanged on financial markets.

Financial rating really began in the United States at the beginning of the 20th Century, through the development of public issue markets.

The market has since gone far beyond United States borders.

Three players currently dominate the world market for external financial rating:

- Standard & Poor's
- Moody's Investors Service, and
- Fitch Investors Service

In 1975, the American regulatory body, the SEC (Securities Exchange Commission), granted official status to these three agencies by awarding them the NRSRO label.

In January 2003, the SEC granted NRSRO status to the Canadian agency, Dominion Bond Rating Service Limited.

Compared with the initial subscription model, these agencies have developed another economic model requiring issuers to pay a percentage of the value of their bond issues.

The four agencies provide ratings for everyone making issues on capital markets world-wide (local authorities, States, companies).

The origins of the sustainability analysis: socially responsible investment

Sustainability analysis organisations play a central role in the socially responsible investment (SRI) system.

They serve the needs of institutional investors that offer socially responsible investment funds. They are veritable market intermediaries between:

- the investors that buy their ratings, and
- the companies they evaluate.

These sustainability analysis organisations provide information on the sustainability risks faced by companies and the performance of their of social responsibility policies.

SRI designates all financial placements chosen on the basis of a compromise between:

- not only the financial performance of the assets in question,
- but also account for sustainability criteria such as corporate behaviour with respect to the company's economic, social and environmental conditions.

Although the ethical considerations initiated by American religious congregations at the end of the 19th Century obviously have an important place in socially responsible investment, the concept goes far beyond this original context to integrate other considerations relevant to corporate social responsibility.

During the 1980s and 1990s, SRI made unprecedented gains.

Currently, only a minority of investors with strong ethical (religious congregations) or militant convictions are prepared to sacrifice part of their financial gains to investment choices in accordance with their values.

Most institutional investors seek concrete financial results from management of the risks and opportunities presented by corporate social responsibility.

The United States remain the principal SRI market in the world with total assets nearing 2,290 billion dollars in 2005.

In Europe, national SRI markets are smaller, the British market being the most developed (but it should be noted that comparisons between SRI sums in the United States and Europe are difficult because the calculation bases are not the same).

The French SRI market has grown continually since its emergence, now covering more than 12 billion euro of assets (end of 2006).

	French Offer		Foreign Offer		Total	
	2005	2006	2005	2006	2005	2006
Total	5691	8403	4189	4140	9880	12543

Evolution of SRI funds under management by Mutual Funds on the French Market in millions of euros at th 31/12/06
(source: letter L'indicateur Novethic)

Sustainability Analysis: definition and approaches

The definition of Sustainability Analysis

Sustainability Analysis, as developed by most organisations, provides a measure of the quality of social, environmental and corporate governance commitments, policy and performance.

By exploiting social, environmental and corporate governance information provided by the company or obtained from other stakeholders (NGOs, the media, etc.), sustainability analysis organisations evaluate:

- commitments and policies implemented,
- performance of the company relating to both its economic activities and its impact on the social, environmental and governance spheres.

The organisation establishes an overall score, or grade, which positions the company on a rating scale based on a set of relevant criteria weighted according to degree of importance.

The analysis is conducted using an evaluation framework defined by the sustainability analysis organisation. This framework varies widely depending on the stated aims of the organisation. The investor client then uses this global score to select the companies that will make up its investment portfolio, depending on its own approach and criteria.

There are three possible approaches to sustainability analysis:

- **Sustainability analysis using an "avoidance approach"** relies on exclusionary criteria defined either by the organisation itself or investors. These exclusionary criteria cover:
 - controversial business sectors such as the tobacco, arms, alcohol, pornography, and nuclear industries, etc, and
 - practices that are deemed to be irresponsible, such as child labour, animal testing, the use of pesticides, etc.

- **Sustainability analysis using a "performance approach"** is based on the definition of positive screening criteria established by the organisation or its clients. The majority of organisations applying this approach evaluate the good social and environmental performance of companies using a "best in class" comparison with other companies in the same sector.

- **Sustainability analysis based on a "risks and opportunities approach"** aims to provide managers with a complete perspective of the risks and opportunities of investing in the rated companies.

Sustainability analysis "materializes" environmental, social and governance risks and evaluates their significance for the financial performance of the company in the short, medium and long term.

The end-users of sustainability analysis

Sustainability analysis is generally produced by organisations in an investment perspective, mainly for the creation of socially responsible funds or stock market indexes.

Investors are currently the main clients of sustainability analysis organisations.

Many organisations also offer sustainability rating services directly to:

- major listed and unlisted companies,
- SMEs, and
- local authorities, etc.

The goal of such rating is to inform the company and all its stakeholders concerning implementation of their social responsibility policy, including:

- performance factors and
- progress factors.

The company or local authority can then use the sustainability rating in communication with both the financial community and its partners and employees.

In a more limited way, sustainability analysis is also used by various actors, such as international organisations, NGOs, foundations and consumers.

Some analysis organisations also provide sectoral and thematic reports to international and national organisations. These sustainability analysis organisations have developed a social, environmental or governance expertise allowing them to work as sub-contractors for international and national organisations.

Some non-profit organisations such as foundations and NGOs also use the services of sustainability analysis organisations in order to choose their partners or corporate sponsors without taking the risk of becoming associated with companies using contradictory practices.

Originally used for the rating of major listed companies, the sustainability analysis universe has widened to cover others actors, in response to investor needs:

- SMEs,
- local authorities and States, and
- NGOs, etc.

Some sustainability analysis organisations, seek to supply this demand by adapting their sustainability analysis methodology to the specific case of each of these new actors.

Country Rating

Countries assessment is a market on which several sustainability analysis organisations angle themselves for answering the investors needs. Indeed, bonds represent a little more than 3.5 billion euros, and this market is growing. Organisations like Innovest, EIRiS Vigeo or Ethifinance have develop a specific country rating methodology. A supplement to this guide is entirely dedicated to Country rating by the Sustainability Analysis Organisations.

Rating SMEs

Although most of the risks and constraints faced by SMEs are identical to those of larger companies, SMEs are often incorporated in the sub-contracting or supply chains of major companies, and are thus subject to direct pressure from these clients.

In response to the need of asset managers, venture capitalists and bankers for evaluation and rating of SME social and environmental performance, some organisations now offer a dedicated service for SME sustainability rating.

Rating local authorities

The sustainability rating of authorities should continue to develop, still not a lot widespread, is lead up to develop because the decentralization and the development of public-private partnerships enable an evolution in the financing of authorities. Investors and authorities will have an increased need for information evaluating the financial consequences of their public policies.

In 2004, to clarify the issues and perspectives in this market, in partnership with Innovest, ADEME conducted a study assessing the feasibility of a rating of the performance of local authorities' environmental policies. Urbivalor, subsidiary of BMJRatings, proposes a social and environmental rating tool for local authorities.

"Carbon" rating

Beyond the widening universe of sustainability analysis, new fields for rating are also developing. This is the case for the issue of Greenhouse Gas emissions, which is the most easily quantifiable and financially material environmental risk.

Evaluation of reductions in CO2 emissions is a common ground for evaluation by financial and SRI analysts. Many sustainability analysis organisations integrate this new issue in their environmental analysis, some even developing a specific offer in reply to the needs of a wider investor clientele.

Profiles of Sustainability Analysis Organisations

The guide contains detailed profiles covering all the characteristics of sustainability analysis organisations:

- their activities,
- their analysis universe,
- their internal organisation and governance,
- the experience and competence of their analysis team,
- their products and services,
- their methodology, etc.

This information allows the companies replying to their questionnaires, and the investors using their analyses in the management of their specialized SRI funds, to choose between different sustainability analysis organisations.

- Concerning their activity, most sustainability analysis organisations are specialized in the processing of information on the social, environmental and governance performance of companies. However, their activities are not limited solely to corporate rating. Many of them conduct a variety of rating-related activities in order to meet the needs of their investor clients, including investment advice, sectoral and thematic studies.

- Sustainability analysis organisations distinguish two types of analysis or rating:

- **so-called "declarative" ratings** for investors, and
- **so-called "solicited" ratings**, aimed directly at actors such as companies, local authorities, NGOs, etc.

- **An organisation's success** depends largely on its ability to provide evaluations covering an entire corporate universe. Organisations generally choose to analyze the companies in a stock market index or a geographical region corresponding to their cultural and technical capacities. At the very least, most organisations present coverage of national companies.

- **The increasing professionalism of sustainability analysis organisations** also requires more transparency on their behalf concerning governance. Investors and companies expect these organisations to communicate clearly concerning their ownership structure and main shareholders as well as the composition of their board of directors, in order to prove their independence.

The majority of sustainability analysis organisations are companies whose shareholders are private or institutional investors (Vigeo, Avanzi SRI Research, Scoris). Many of them have the legal status of non-profit associations (CAER, FED, Ethibel, etc..).

- **The experience and competency** of analysts are fundamental factors in the quality of the organisation's research and analysis and, thus, of its reputation. In the second part of the Guide, each profile presents an overview of the organisation's team of analysts, their professional experience, training and previous professional experience.

As for methodology, sustainability analysis is based on a double process:

- compiling data bases from the information collected, and
- processing the information through a series of evaluation criteria.

The means of processing the information collected vary appreciably from one organisation to another, depending on the information collection methods, analysis methodology and evaluation criteria used by the organisation in its rating process.