

RESPONSIBLE RETURN

INVESTMENT BOARD

Corruption: Bogging down sustainability assessments

ENGAGEMENT

Siemens and Telekom Austria

COMPANY OF THE MONTH

ABB

PIN IT DOWN

A firm handshake instead of backhanders



Editorial



Wolfgang Pinner is Chief Sustainability Investment Officer and heads the Responsible Investments team at Erste Asset Management.

Corruption scandals always shake our belief in the legitimacy and justice of any political or economic system. Central Europe has not been immune from scandal in recent times: e.g. the Telekom Austria and Siemens cases have triggered widespread discussion and are covered in more depth in the Engagement article (page 5). Corruption is not only morally reprehensible – in that accepting bribes or benefits in kind is based on the abuse of power – but also incredibly expensive. At the corporate level, focus is on the personal benefits for the corrupt individuals on each side of the equation, at the expense of the company's interests.

Whether dealing with politics or businesses, we need to ask the same question: Is this a one-off incident, or is the corruption systemic? It is not easy to identify the level of corruption present; in fact different sources have very different assessments of the extent of corruption within the economy.

According to a survey by Ernst & Young, 46% of managers in Austria considered bribery to be „normal“ in their country. However, there are also marked regional variations in perceived corruption levels: e.g. the figures for Germany (30%) and Switzerland (10%) were much lower than for Austria, whilst Italy (60%) and Greece (84%) scored much higher.

In contrast, if you talk directly to stock exchange-listed companies and evaluate their compliance management structures and measures to combat fraud – many of which have been tightened up recently – you might be persuaded that the economic system does not allow corruption a foothold.

In view of this discrepancy, it seems that close analysis is more than a necessity.

Sincerely

A handwritten signature in black ink, appearing to read 'Wolfgang Pinner', written in a cursive style.

Wolfgang Pinner
Head of SRI Team

Investment Board

The EAM Investment Board gives a structured form to the ongoing and responsive dialogue with and among sustainability research agencies. The Board provides the opportunity for the consultation process between own research and external research to take place. It also discusses rating details, the ESG's assessment of the IPOs of new issuers and sustainability issues in general.

Corruption: Boggling down sustainability assessments



When evaluating corporate corruption, the gravity of the offence is a key factor: Our assessments distinguish between very serious, serious, moderate and minor offences. In order to classify cases within the spectrum, consideration is given to whether an offence has been com-

Anti corruption measures improve the sustainability ranking

mitted, the financial amounts involved, frequency and whether the management was involved. In this regard, systematic malpractice is viewed in a particularly severe light.

Companies embroiled in corruption scandals can score bonus points if they take rapid and professional remedial action. The EAM Responsible Investments team especially considers whether they introduce or improve internal rules and guidelines, set up or optimise internal and external audit bodies, and take steps to ensure maximum transparency.

Corruption status:

Serious corruption offences are a criterion for exclusion from the EAM sustainability rating. Companies can get suspended for up to three years. Corruption forms part of Compliance which amounts to 10% of the ESG rating.

Corruption used to be interpreted primarily in terms of reputation risk for the company. Today, however, particularly in light of record-breaking fines, the financial ramifications have overshadowed ethical considerations. Germany's Siemens Group has had to pay fines totalling USD 1.6 billion for corruption offences committed between 1995 and 2006.

As with violations of anti-competition law, the timeline can be a problem when assessing corruption offences. Corrupt practices are often discovered with a long delay. The revelations often generate a whole host of accusations, which are then inves-

tigated, and might eventually lead to a sentence.

Years can pass between offence and investigation

Sustainability research factors in corruption scandals as soon as the details are made public. Court rulings are another criterion included in the analysis. The evaluation is further complicated by the fact that in English-speaking countries years of legal wrangling often end with a settlement, rather than any admission of guilt.



3 types

Corruption stands for the abuse of power for personal gain. The word stems from the Latin “corrumpere”: to bribe, to damage, to destroy. There are three different types of corruption: situational corruption based on a spontaneous decision, structural corruption that is the result of a plan, and systemic corruption which concern ample parts of public or private entities. Organisations like the NGO Transparency International or the OECD offer tools for tackling corruption: www.transparency.org/whatwedo/tools, www.oecd.org/corruption/

Engagement

Engagement is of great importance for EAM's sustainable investment approach. It combines own initiatives with collaboration on a national and international level. The structured engagement process is based on the „EAM Engagement Guideline“ which determines engagement issues, approach and procedures.

Engagement focus on corruption



Although their respective countries of origin, Germany and Austria, hold relatively good rankings in the global corruption indices, Siemens and Telekom Austria in recent years have been in-volved in high-profile corruption scandals that managed to attract both national and international attention.

Corruption is best fought with transparency and compliance

Siemens has become a model pupil for compliance in response to the massive pressure of the media. Once the problems had been revealed, the priority was to prevent corruption and incorporate compliance structures into daily operations. The new Siemens system encompasses prevention, investigation and response measures. Telekom Austria's new compliance management system is fairly similar. The system is built around strategic

issues, ranging from management integrity to communication to auditing and a highly commendable external certification process.

As an international plant construction company, Siemens is constantly exposed to political pressures, which the company feels are overrated. Large-scale projects tend to involve long-term contracts including maintenance agreements. From Siemens' perspective, strict compliance rules can put the company at a disadvantage when competing with corrupt rivals, but can also be work in its favour, since the company can build a reputation as a transparent and reliable partner. Siemens is also involved in a number of external corruption prevention programmes.

Telekom Austria was involved in a number of cases of political party financing, which is a form of lobbying that has been successfully eliminated by other companies partially government owned. As in the case of Siemens,

most of the major corruption offences have now been investigated, but it is not yet clear whether all the details have emerged.

Proving maximum transparency and implementing state-of-the-art compliance management structures both at home and in high-risk regions seem to be the way forward for both companies. They will also need to ensure that joint ventures and investors do not circumvent the compliance processes.

Status of Siemens and Telekom Austria:

Siemens has sold its holdings in the armaments and nuclear power industry and rejoined the EAM sustainability universe, now that the corruption issues have been eliminated. One research partner still has doubts about Telekom Austria at present.

Company of the month: ABB

The Company of the Month is selected due to recent developments and in connection with the **topic of corruption**. The EAM Responsible Investments team analyses the strengths and weaknesses of the selected company in terms of ESG.

Zurich-based ABB specialises in power and automation technologies. The company was formed in 1988 through the merger of the Swedish ASEA and the Swiss BBC. Turnkey systems and services for power stations, power transmission and distribution make up the main product ranges.

Corruption.

When it comes to corruption and unfair competition, ABB has a lot of past sins to atone for. The company has been fined heavily in recent years. In September 2010, ABB paid out EUR 58.3 million under a settlement deal with the US Justice Department. The settlement pertained to bribes paid in several countries between 1997 and 2004. The deal included a commitment to investing in an internal business integrity programme. The new anti-corruption guidelines also apply to subsidiaries and suppliers. The guidelines include an anonymous whistleblower programme and internal audits. ABB's anti-corruption standards are currently slightly ahead of the industry average.

In 2012, ABB reported consolidated revenue of USD 39.34 billion, with a workforce of around 145,000. ABB has five divisions: Power Products, Power Systems, Discrete Automation & Motion, Low Voltage Products and Process Automation. Around one-third of ABB's orders come from Europe, another third from North & South America, one quarter from Asia, and the remainder from Africa and the Middle East.



Picture: ABB

Infringements of competition law.

Over the past four years, ABB has been fined by competition authorities in Germany, the European Union and Brazil for distorting competition in relation to substations, underwater cabling and transformers.

Energy consumption.

ABB promotes itself as a specialist in the field of energy efficiency. In fact, more than half of all research & development expenditures is channelled into this area. (The Swiss-based engineering group currently employs a workforce of more than 8,000 in seven R&D centres around the world).


Around 60 % of ABB's revenues are generated from energy efficiency products and services. The company's product range includes its own solution sets for a wide variety of applications.

Health and safety.

ABB's health and safety management system based on ILO standards and OHSAS 18001 has been rated positively. Compared to its peers, the company employs a large proportion of its workforce at European locations. However, there is still scope for improving the requirements for suppliers and subcontractors. The special health and safety standards in ABB's construction activities are even regarded as poor.

Key figures for ABB


Sector	construction and engineering
ISIN	CH0012221716
Share price (15.05.2013)	21.60 EUR
Estimated PE (15.05.2013)	19.25
Dividend yield	3.15



pin it down

Closing words by
Wolfgang Pinner

A firm handshake instead of backhanders



The perfect market in a fair environment with participants that play to their strengths – that is the textbook utopia, explains Wolfgang Pinner

As always, reality unfortunately looks slightly different. Fairness in the sense of eliminating corruption remains a lofty goal yet to be attained. The long litany of wrongdoing could provide material for a whole raft of inflammatory publications .

If you want to avoid nasty surprises, you might do well to invest in known „black sheep“. Statistically speaking, it is best to fly with an airline that has recently had a plane crash, essentially because the company will have stepped up safety precautions to the maximum. In the same way, companies that have recently been involved in minor or full-blown scandals – and duly hauled over the coals – are the most likely to have put their house in order. They might even have introduced state-of-the-art compliance management systems.

The political context is another facet of the problem. What happens to the official code of conduct when faced with a corrupt politician asking for a bribe? Countries that do not have a mature democratic and legal system can be a murky and bottomless pit for companies seeking to expand. Despite all this doom-mongering, efforts are clearly being made to stamp out corruption, particularly in the business sector. They give hope and should be supported by international rules and agreements. If the private sector and institutions close ranks to combat corruption, then we really will be able to move towards more fairness, greater integrity and rising enterprise values.

For more than 10 years **Wolfgang Pinner** has been active in the field of sustainable investments. He has written two books on this topic and represents Austria at the industry association „Forum Nachhaltige Geldanlagen“.

Wolfgang Pinner is Chief Sustainability Investment Officer at the Erste Asset Management and leads the Responsible Investments at the ERSTE-SPARINVEST.

Changes in the Responsible Investment Universe

The definition of our investment universe is the corner stone in building our funds.

+ INCLUDED

MAY 2013

Daimler AG Ltd (“Automobile Manufacturers” sector)

is a global manufacturer of cars and commercial vehicles. The company produces small cars, luxury cars, vans and heavy goods vehicles (HGVs). It also provides car finance service

- ⊗ The exclusion criterion of activities in the military sector no longer applies due to the sale of all relevant investments to EADS in April 2013.
- ⊗ All production sites have ISO 14001 environmental management systems. The energy management systems in over ten sites, including large plants, are ISO 50001 certified.
- ⊗ Strict requirements for suppliers in terms of environmental management systems, material standards, banned substances and the ability to recycle components.
- ⊗ No information is available as to whether HGVs produced for military use are fitted with weapons systems.

TFS Corporation Ltd (“Forest Products” sector)

manages sandalwood plantations in Australia. The company is involved in plantation management and also manufactures sandalwood oil and other sandalwood products for use in medical and cosmetic products.

- ⊗ The company’s sandalwood oil distillery runs on bluegum plantation waste
- ⊗ Plantations are only created on land previously used for agriculture or market gardening
- ⊗ Multi-award-winning water management system
- ⊗ No biotechnology
- ⊗ Environmental management system is ISO 14001 certified



60%

Due to water recycling and rainwater capture, the Australian company TFS was able to reduce its water consumption by 60% within four years.

Picture: Two R&D employees standing in front of TFS' wastewater treatment plant.

Quellen: TFS

- EXCLUDED

Microsoft Corp (“Systems Software” sector)

is a multinational software and hardware manufacturer. The company produces operating systems, applications and hardware, including joysticks, keyboards and games consoles.

- ⊗ Violation of the labour rights exclusion criterion: In February 2013, SACOM, a Chinese labour rights NGO, reported that working conditions were very poor in Microsoft supplier Foxlink’s factories in the Guangdong province.
- ⊗ In recent years, the EU Commission has fined the company on several occasions for distorting competition by bundling software products with the Windows operating system. The company last received a fine of more than EUR 561 million in March 2013.

Responsible funds at a glance

Erste Asset Management recognized the importance of responsible fund management early on. Over the course of the past decade we have developed and successfully introduced a broad range of sustainable funds. The following funds are available in line with Erste Asset Management's „Responsible Investment Approach“.

Stock Funds

All funds are denominated in Euro.

Fund name	Since 1. 1.	2012	2011	2010	2009	2008	Mgmt. fee	Volume in mn.	Average ESG- Rating	Risk notes ¹⁾
ERSTE RESPONSIBLE STOCK GLOBAL	12.13	9.51	-4.90	16.61	29.66	-37.42	1.50	223.4	C+	A, B
ERSTE RESPONSIBLE STOCK EUROPE	8.54	20.88	-23.03	9.40	27.01	-54.99	1.50	10.5	B-	A, B
ERSTE RESPONSIBLE STOCK AUSTRIA	2.92	29.19	-38.75	16.63	36.08	-56.62	1.50	7.7		A, C, D
ERSTE RESPONSIBLE STOCK EUROPE EMERGING	-0.85	24.99	-31.51	16.65	55.19	*	1.80	15.2		A, B, D
ERSTE RESPONSIBLE STOCK AMERICA	11.64 ²						1.80	41.2 ²		A, B
ERSTE WWF STOCK CLIMATE CHANGE	18.58	-7.35	-25.66	3.19	21.37	-45.82	1.50	8.9		A
ERSTE WWF STOCK UMWELT	13.90	5.63	-23.39	14.25	17.84	-48.02	1.50	45.1		A

Performance calculated according to the OeKB (Osterreichische Kontrollbank AG) method, as of 30 April 2013. The management fee is included in the performance. Subscription fees applicable at the time of purchase of up to 5.00% and other fees that may reduce returns, such as individual account and deposit fees, are not included in this presentation. Past performance is not a reliable indicator of the future performance of a fund. Please note that it is not possible to draw any conclusions on the volatility or risk of an investment from annualized averages for multi-year periods.

1) Risk notes

- A The ERSTE RESPONSIBLE STOCK GLOBAL, ERSTE RESPONSIBLE STOCK EUROPE, ERSTE RESPONSIBLE STOCK AUSTRIA, ERSTE RESPONSIBLE STOCK EUROPE EMERGING, ERSTE WWF STOCK CLIMATE CHANGE, and ERSTE WWF STOCK UMWELT funds may display increased volatility due to the composition of the portfolio. As a result, share values may be subject to significant fluctuations even over short periods of time.
- B The ERSTE RESPONSIBLE STOCK GLOBAL, ERSTE RESPONSIBLE STOCK EUROPE, and ERSTE RESPONSIBLE STOCK EUROPE EMERGING funds may invest significant amounts in derivative instruments (including swaps and other OTC derivatives) pursuant to Paragraph 73 of the InvFG 2011 (Investment Fund Act, Austria).
- C The ERSTE RESPONSIBLE STOCK AUSTRIA fund is an index fund pursuant to Paragraph 128, section 5 line 1 in conjunction with Paragraph 75 of the InvFG 2011 (Investment Fund Act, Austria). The aim of the investment strategy is to emulate the VÖNIX (VBV Austrian Sustainability Index).
- D The ERSTE RESPONSIBLE STOCK AUSTRIA and ERSTE RESPONSIBLE STOCK EUROPE EMERGING funds may invest significant amounts in sight deposits or deposits with a maturity of no more than 12 months pursuant to Paragraph 72 of the InvFG 2011 (Investment Fund Act, Austria).
- * Fund inception during the fiscal year

2) in USD

Bond funds, mixed funds

All funds are denominated in Euro.

Fund name	Since 1. 1.	2012	2011	2010	2009	2008	Mgmt. fee	Volume in mn.	Average ESG- Rating	Risk notes ³⁾
ERSTE RESPONSIBLE LIQUID	0.47	5.33	0.60	2.21	10.99	-2.91	0.24	39.9		–
ERSTE RESPONSIBLE BOND	1.69	10.57	0.94	1.72	9.07	4.51	0.60	149.7		a)
ERSTE RESPONSIBLE BOND EURO-CORPORATE	1.94	12.89	*				0.60	115.5	B–	–
ERSTE RESPONSIBLE BALANCED	3.00	*					1.20	4.1	B–	b)

Performance calculated according to the OeKB (Österreichische Kontrollbank AG) method, as of 30 April 2013. The management fee is included in the performance. Subscription fees applicable at the time of purchase of up to 3.50% and other fees that may reduce returns, such as individual account and deposit fees, are not included in this presentation. Past performance is not a reliable indicator of the future performance of a fund. Please note that it is not possible to draw any conclusions on the volatility or risk of an investment from annualized averages for multi-year periods.

3) Risk notes

- a) The ERSTE RESPONSIBLE BOND fund may invest significant amounts in derivative instruments (including swaps and other OTC derivatives) pursuant to Paragraph 73 of the InvFG 2011 (Investment Fund Act, Austria).
- b) The ERSTE RESPONSIBLE BALANCED fund may invest significant amounts in investment funds (UCITS, UCIs) pursuant to Paragraph 71 of the InvFG 2011 (Investment Fund Act, Austria).
- * Fund inception during the fiscal year

Microfinance funds

All funds are denominated in Euro.

Fund name	Since 1. 1.	2012	2011	2010	2009	2008	Mgmt. fee	Volume in mn.	Risk notes ⁴⁾
ERSTE RESPONSIBLE MICROFINANCE	0.19	3.20	2.48	0.79			1.00	24.3	x)

Performance calculated according to the OeKB (Österreichische Kontrollbank AG) method, as of 30 April 2013. The management fee is included in performance. Subscription fees applicable at the time of purchase of up to 3.00% and other fees that may reduce returns, such as individual account and deposit fees, are not included in this presentation. Past performance is not a reliable indicator of the future performance of a fund. Please note that it is not possible to draw any conclusions on the volatility or risk of an investment from annualized averages for multi-year periods.

4) Risk notes

- x) The ERSTE RESPONSIBLE MICROFINANCE fund may invest significant amounts in investment funds (UCITS, UCIs) pursuant to Paragraph 7 line 1 of the InvFG 2011 (Investment Fund Act, Austria):

Warning pursuant to the InvFG 2011 (Investment Fund Act, Austria): The ERSTE RESPONSIBLE MICROFINANCE invests entirely in assets pursuant to Paragraph 166, Section 1 line 3 of the InvFG 2011 (Alternative Investments), which represent a higher investment risk compared to traditional investments. In particular, these investments may result in a loss or even a total loss of capital invested.

New sustainable fund: ERSTE RESPONSIBLE STOCK AMERICA

On the **8th of April 2013** the ESPA STOCK AMERICA fund was **renamed** ERSTE RESPONSIBLE STOCK AMERICA. The new name was accompanied by a focus on social responsibility. Now all equities have to pass the Erste Asset Management sustainability screening before being included in the fund. With its emphasis on North American equities, the ERSTE RESPONSIBLE STOCK AMERICA broadens the range of our sustainable funds..



Glossary

Engagement

In the context of sustainable investments, Engagement means that the investor tries to convince the management of a company to take action in the fields of social responsibility, environment or transparency. On a national basis, the Erste Asset Management Responsible Investments Team carries out its engagement activities itself, on a global basis the team co-operates with the a specialised provider.

ESG

ESG is an abbreviation of Environmental, Social and Corporate Governance and refers to sustainability in business.

Exclusion criteria

The Erste Asset Management responsible funds do not invest sectors or companies that violate certain (exclusion) criteria, e. g. violation of labour regulation, nuclear energy, etc. These criteria include ethical, social and governance risk factors.

Investment Board

In this board, the Erste Asset Management Responsible Investments Team discusses topical issues and current developments, IPOs, etc. with sustainability specialists and financial experts.

Investment universe

An investment universe designates the amount of investable companies and countries. In order to become part of the Erste Asset Management Responsible Investment Universe, they need to perform above average with regards to sustainability. From this selection the fund manager picks those companies with the best prospects according to their fundamental financial data. The Erste Asset Management Responsible Investment Universe is updated on a monthly basis, which enables quick reaction to changes within the respective companies.

SRI

Socially Responsible Investments

SRI Rating agency / SRI Rating

An SRI rating agency or SRI research agency analyses and rates the activities of companies according to social, ecological and ethical criteria (e.g. A = best grade to D = worst grade). SRI ratings help investors to assess a company's exposure to environment and stakeholders. The Erste Asset Management Responsible Investments Team co-operates with several SRI-rating agencies covering different key aspects. In contrast to SRI rating agencies, finance rating agencies (e. g. Moody's, Fitch, S&P etc.) focus on companies' financial data only.

Voting

In the context of sustainable investments, voting refers to the exercise of voting rights at shareholder meetings. Possible targets are an increased transparency in management compensation or in case of nominations for the board directors. Like in its Engagement activities, the Erste Asset Management Responsible Investments Team cooperates with companies in the area of voting.





Our long-term partners in sustainability



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