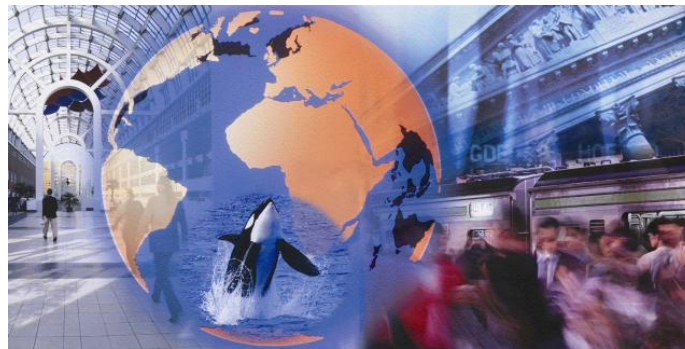


**Corporate Social Responsibility at ABP|Loyalis**  
**‘From experience and knowledge to outperformance’**



**Presentation at the  
Canadian Social Investment Conference  
June 12 – 14, Toronto**

**Hans de Ruiters  
Portfolio Manager**

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- **ABP's activities on CG**
- **ABP's activities on SRI**

## **ABP at a Glance**

- **Pension Fund for Dutch Civil Servants**
  - 2.4 million participants
  - 25% of all Dutch households
  
- **Assets under Management of € 156 billion**
  
- **Active Role regarding Corporate Governance & SRI**
  - Academic Research
  - Networking
  - Loyalis Global Sustainability Fund
  - Voting
  - Strategic Stakes

## ABP's View on CSR

### ABP's Code of Prudent Investment Policy:

- Investment are made exclusively in the interest of the participants
- ABP encourages socially responsible behavior and best-practice corporate governance principles
- ABP promotes the integration of social, ethical and environmental criteria in its investment process
- ABP makes use of its rights as a shareholder
  - to diminish risks
  - to enhance returns

## What Lies Beneath?



## Why become more active on CSR?

- **Good CSR (CG & SRI) is a prerequisite for pension funds**
- **Bad Corporate Governance**
  - Destruction of value
  - Decrease of risk/return profile
- **Good Corporate Governance**
  - Enhancement risk / return profile
  - McKinsey, Gompers: annual outperformance of up to 8%
  - Lower cost of capital for the company
- **Capturing long-term shareholders' value:**
  - By including CG and SRI in mainstream investment process
  - Research indicates a positive correlation between SRI, good governance and performance.

## What has ABP done on CG?

- **Academic Research**
  - Investigating the link between corporate governance and financial performance
- **Global (Proxy) voting**
  - We aim to vote on all our shares
  - Voting and policy on our website
- **Networking**
  - We are active in many of the major corporate governance networks
- **Other actions**

## **Academic Research**

- **The vast amount of empirical studies on the relationship between corporate governance and financial performance find a positive relationship**
- **The study by Gompers, Ishii & Metrick (2001) finds an excess return of 8.5% for well governed companies in the US**
- **Similar results are reported for other countries**
- **Message: investors care about a company's corporate governance**

## **Global (proxy) voting**

- **Through the SCGOP, a collaboration of Dutch pension funds, we regularly attend AGM's of Dutch companies**
  
- **Proxy voting**
  - Netherlands : since 1998 where possible
  - International : since 2002 via investment managers. In 2003 we implemented a structure through which we vote on all shares in our internal portfolios (ADP's ProxyEdge)
  - External investment managers are required to report on their voting behavior
  
- **We disclose our voting behavior on our website**

## Networking

- **ABP is active on several (international) corporate governance networks**
  - SCGOP
  - ICGN
  - GIGN
  - IFAS
  
- **We collaborate with other major institutional investors that are active on corporate governance**

## Other Actions

- **Other actions ABP performs on corporate governance include:**
  - Reactions to consulting papers (e.g. those of the EC)
  - Stimulate buy-side and independent research on corporate governance (e.g. GMI)
  - Monitor and manage class action positions
  - Publications and presentations

## What has ABP done on SRI?

- **Academic Research**
  - Investigating the possibility of delivering positive excess returns.
- **Networking**
  - To encourage how SRI could lead to enhancing returns
  - Endorsing initiatives like Carbon Disclosure project, Pharma
- **SRI Portfolio: Loyalis Global Sustainability Fund**
  - Sustainability screening based on 'best-in-class' approach.
  - Aiming to outperform the MSCI World Index.
  - Open to other pension funds worldwide (exchange experiences)
- **Other actions**
  - Stimulate buy-side research (Innovest, own research)
  - Publications, presentations

## Academic Research

- There is a large body of literature analysing the social-financial performance link (e.g. Hamilton, Jo and Statman, 1993; Statman, 2000; Diltz, 1995; Cohen, Fenn and Konar, 1997; Yamashita, Sen and Roberts, 1999).
- On balance all studies to date suggest:
  - That SRI-based strategies do not perform statistically significant different compared to conventional strategies
  - That (unconstrained) SRI-based strategies can have a volatile performance over time, just like any other investment style; this is partly the result of the fact...
  - ...that SRI-based strategies tend to have strong style bets (on average they are tilted to large cap/growth stocks)

## Academic Research (Cont'd)

- A recent paper by Rob Bauer, head of research at ABP, and Derwall, Gunster and Koedijk (Erasmus University Rotterdam) reveals that for the US the performance of SRI-based strategies – using the SRI ratings of Innovest – can be enhanced significantly by neutralizing all major risk factors (size, value/growth, momentum, beta and industry-group)

## Academic Research (Cont'd)

- Carhart Analysis of the best in class approach (Bauer, Derwal, Gunster & Koedijk, 2004)

	$\alpha$ (0bp tc)	Rm-Rf	SMB	HML	MOM	Adj. Rsq	$\alpha$ (200bp tc)
<b>Best-in-Class Portfolio</b>	4.15 <sup>**</sup> (2.11)	0.92 <sup>***</sup> (24.15)	-0.19 <sup>***</sup> (-4.14)	0.02 (0.26)	-0.09 <sup>***</sup> (-5.31)	0.88	3.43 <sup>*</sup> (1.72)
<b>Worst-in-Class Portfolio</b>	-1.81 (-0.77)	1.03 <sup>***</sup> (27.49)	0.04 (0.93)	0.23 <sup>***</sup> (4.59)	-0.08 <sup>***</sup> (-2.86)	0.86	-2.8 (-1.20)
<i>Difference</i>	5.96 <sup>**</sup> (2.54)	-0.12 <sup>***</sup> (-3.02)	-0.23 <sup>***</sup> (-3.82)	-0.22 <sup>***</sup> (-3.52)	-0.01 (-0.20)	0.17	6.23 <sup>**</sup> (2.62)

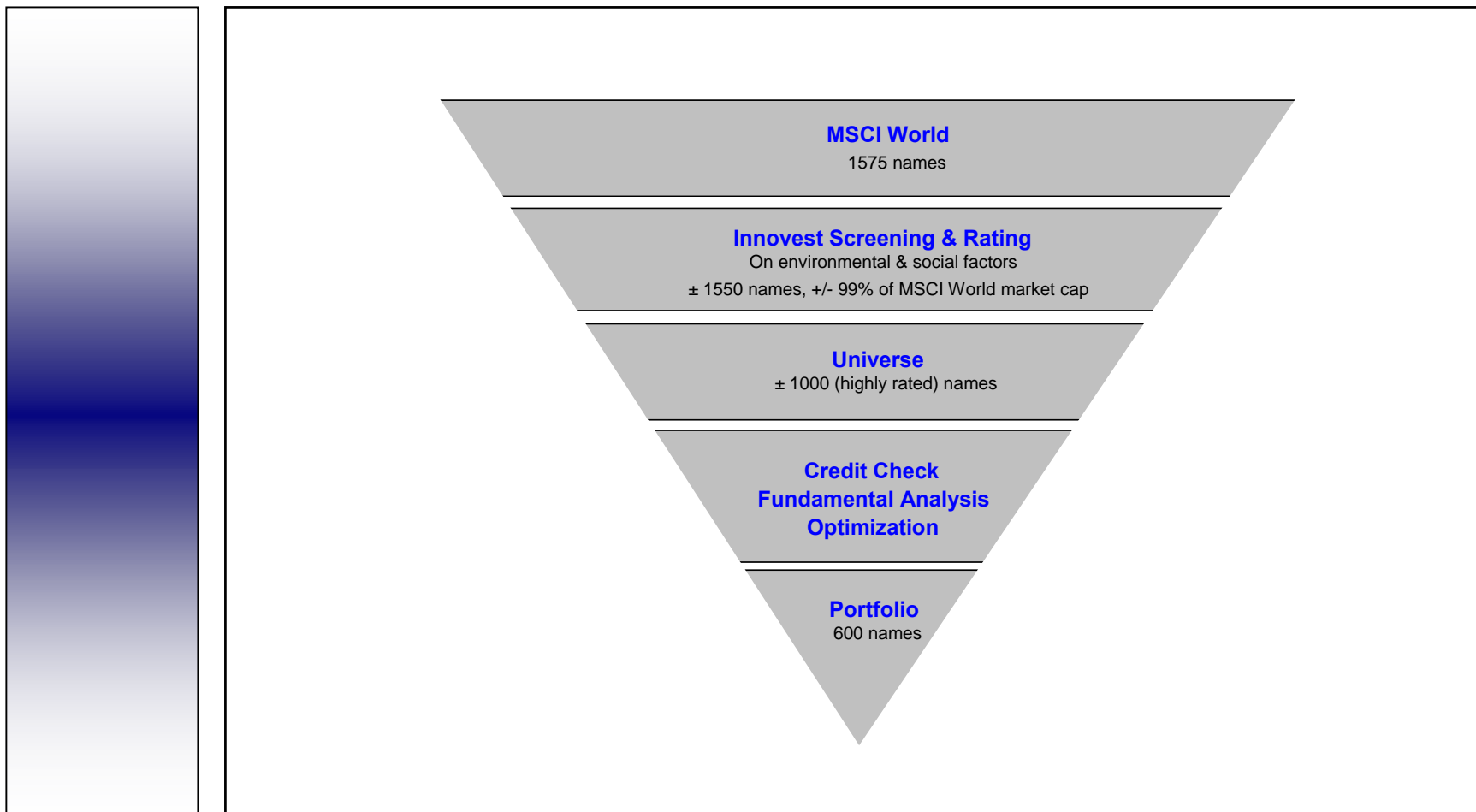
## Academic Research (Cont'd)

- Recently, we have done a similar study as the one cited above, also using the ratings of Innovest, but now including Europe and Japan as well. Our findings corroborate the finding of the Bauer, Derwall, Gunster and Koedijk study.
- Conclusion: portfolio construction is key!

## Networking

- We frequently share information and research findings with other major investors active on SRI
- We endorse SRI-related initiatives like:
  - The Carbon Disclosure Project, aimed at enhancing the transparency of companies on their carbon emissions
  - Pharma Futures Project, aimed at making a constructive contribution to discussions about the role of the pharmaceutical industry in the healthcare value chain (the project brings together various stakeholders and enables them to do some long-term thinking)

# Loyalis Global Sustainability Fund Portfolio Construction



## Portfolio Construction (Cont'd)

- Major input for our SRI strategy are the SRI ratings of Innovest
- Innovest is an internationally recognized investment research and advisory firm. It specialises in analysing companies' performance on environmental, social, and strategic governance issues, with a particular focus on their impact on competitiveness, profitability, and share price performance.
- The ratings of Innovest are based on a best-in-class approach; this means that companies are rated on their sustainability performance relative to sector peers.

## Portfolio Construction (Cont'd)

- In our portfolio construction process we define the eligible investment universe as all stocks with a SRI-rating of BBB or higher. Furthermore, we aim to stick as close to the benchmark (MSCI World) as possible, subject to the following set of constraints:
  - No value/growth bet
  - No beta bet
  - No size bet
  - A limited industry-group bet
  - Individual stock bets are capped at 50 bp

The LGSF aims to deliver persistent returns in a risk-controlled setting

## Enhancements to the Sustainability Component

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### ➤ **Research**

- Inclusion of rating changes
- In-depth analysis of link between SRI and stock returns (e.g. what components of SRI are most correlated with company performance and stocks returns, and what are the dynamics in this relationship?)

### ➤ **Portfolio Construction**

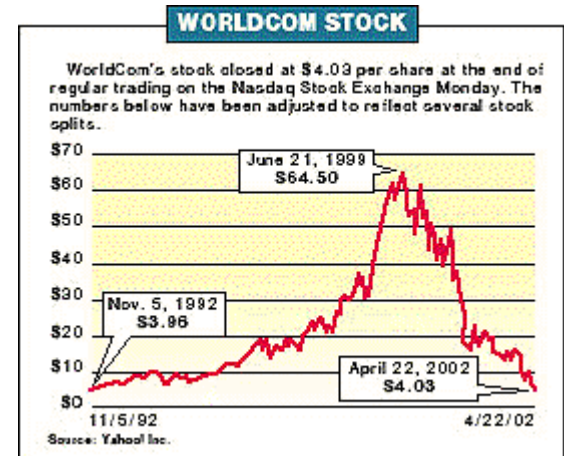
- Pure SRI return
- Neutralizing implicit region, sector, style tilts
- Alternative optimization routines

### ➤ **Relationship SRI and Corporate Governance**

- Combining SRI signal and Corporate Governance signals

## Enhancements to the sustainability component

- **Torpedo Research**
  - Systemic Risks (Long Term Oriented)
  - Credit Analysis
  - Accounting Based Research
  - Stock Watch



## Loyalis Global Sustainability Fund

### Sustainability Perspective

*'Engagement with teeth':  
stimulating companies  
to act in a sustainable way  
to develop economic growth.*

*A tool to actually implement a  
sustainable investment strategy  
as part of the long-term investor's  
policy on sustainability.*

### Investment Perspective

*A way of achieving profitable returns.*

*Diversification in investment style.*

*A well-diversified global equity portfolio.*



### Network Perspective

*A way of participating in a network of long-term investors who all have a vested  
interest in solid and sustainable business practices in the long run.*

## Other SRI-related activities

- ABP stimulates independent SRI research (Innovest)
- ABP stimulates sell side analysts to integrate SRI issues into their analyses
- ABP conducts a lot of 'in house' SRI research (part of which is published in international journals)
- ABP frequently presents its experiences with and insights on SRI at international conferences and seminars

## Loyalis Global Sustainability Fund



**'More Than Just Investing'**

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