

Assessing and Unlocking the Value of Emerging Markets Sustainability Indices



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About Esty Environmental Partners (EEP)

Esty Environmental Partners is a management consulting firm that helps companies build business advantage through strategic response to environmental and sustainability challenges. Founded by Dan Esty, a global thought leader on the business-environment interface, and author of *Green to Gold: How Smart Companies Use Environmental Strategy to Innovate, Create Value, and Build Competitive Advantage*, EEP provides clients with a systematic and comprehensive approach to capitalizing on the sustainability imperative. Working at the frontier of environmental management, with leaders in a range of industries, EEP continually refines best-practice frameworks and insights into how to successfully embed sustainability into the global enterprise. The firm's ongoing research projects and dynamic network of clients, affiliates, and staff enable it to counsel clients on the most effective immediate and long-term strategies to reduce risk and costs, innovate, build brand, and grow revenue. EEP has offices in Boston, MA, Washington, D.C., and Sydney, Australia. For more information, visit www.estyep.com.

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Foreword

The last few years have seen a proliferation of initiatives to create sustainability indices in a number of emerging markets. IFC has supported many, including the Corporate Sustainability Index in Brazil, the S&P ESG index in India, and S&P/Hawkamah Pan Arab ESG index. Such indices can be a cost-effective way for investors to identify best in class companies in sustainability. By making clear the link between sustainability and financial returns, they also help prove the business case for sustainable investing.

Despite their increase in number, several challenges have so far kept sustainability indices from attracting significant investor interest. As investors become more sophisticated, many have moved away from passive strategies associated with index investing, preferring instead to conduct their own environmental, social, and governance analysis. A lack of transparency about how sustainability indices are constructed has also created confusion, keeping investors away.

The result is that sustainability indices stand at a critical juncture. Although they hold significant potential to elevate the importance of environmental, social, and governance issues in emerging markets, their business model is under pressure.

Assessing and Unlocking the Value of Emerging Markets Sustainability Indices, based on extensive research, is the first study of its kind to assess the state of emerging sustainable indices and to examine the drivers of and obstacles to growth. It looks at 17 current emerging market sustainability indices, comparing and contrasting business models, sustainability objectives, and construction methodologies, and identifying obstacles in establishing a viable business model.

The study is part of IFC's efforts to help mobilize more institutional capital into sustainable and inclusive equity investment funds and indices. Our work includes supporting market efforts to reward companies that embrace a sustainable and inclusive strategy and assisting investors in recognizing and valuing these practices.

Assessing and Unlocking the Value of Emerging Markets Sustainability Indices finds that sustainability indices can play a key role by helping investors to recognize non-financial value and enabling markets to reward sustainable corporate performance. But these benefits will only accrue if indices have an appropriate business model and structure. The study provides a concrete set of recommendations to unlock this potential.

It is IFC's hope that our research will trigger meaningful dialogue among investors and service providers on sustainable investing, analytical approaches, data collection, and corporate disclosure, with the goal of setting a stronger and more durable business model for emerging markets sustainability indices.

IFC is indebted to the index providers, the data providers, the investors, the stock exchanges, and the non-governmental organizations that assisted in the preparation of this report and shared valuable insight. This research would also not have been possible without the generous support of the Swedish International Development Cooperation Agency.



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I. Executive Summary

This research paper explores the rapid expansion of emerging markets sustainability indices and the potential for these indices to support the scale up of sustainable investing efforts. Specifically, this report examines three related questions:

1. Why are emerging markets sustainability indices being launched?
2. What role can these indices play in adding value for investors and other stakeholders?
3. How can index providers and other market players enhance the potential for emerging markets sustainability indices to add value to investors and other stakeholders?

Esty Environmental Partners has made a number of observations that help answer these questions, which are supported by our research and analysis, as well as by the sustainable investment literature, including:

- Interest in sustainable investing is increasing, and the market is evolving from largely values-oriented investors and now includes new segments with a growing emphasis on investors seeking value.
- Emerging markets sustainability indices have proliferated in recent years building upon the experience of developed market indices, yet emerging markets indices vary in their intents and remain at an early stage of market development.
- Despite current limitations, emerging markets sustainability indices can play an important role in supporting and driving broader sustainability efforts.
- However, emerging markets sustainability indices, like those in developed markets, face a set of fundamental challenges that need to be addressed to ensure that indices deliver value to investors and are positioned to promote corporate sustainability.
- Index providers and other stakeholders need to address these challenges to enable better alignment between the needs of various types of sustainability investors and the potential of indices to meet these varied needs.
- Looking ahead in the near-term, emerging markets sustainability indices can benefit by adopting a collaborative model when developing, launching, managing, and evolving indices. In the longer-term, indices can help demonstrate the materiality of corporate sustainability by focusing on indicators of the business upside from the successful execution of sustainability strategies, as well as the value derived from downside risk management.

These observations are summarized below and detailed in the following report.



Interest in sustainable investing is increasing, and the market is evolving from largely values-oriented investors and now includes new segments with a growing emphasis on investors seeking value.

Over the past decade, sustainability has become an important issue in the investment landscape, driven by a variety of factors including: climate change challenges; growing natural resource scarcities; rapid industrialization in emerging economies; global concerns about business practices; and the growing demand for transparency stemming, in part, from the recent financial crisis.

In parallel, sustainability as an investment concept has also evolved. Historically, sustainability-focused investors were driven by “values” and focused on “screening out” sectors or companies that were viewed as having a negative social or environmental impact. In recent years, investors have begun to realize that companies can benefit financially from their sustainability programs by reducing risks, cutting costs (through eco-efficiency), driving growth, and building brands. Increasingly, investors see the potential for companies that meet high sustainability standards to produce risk-adjusted returns that are in line with – or better than – the market.

While the tools and approaches to integrate sustainability into investment strategies are in early stages and will continue to evolve, mainstream investors have begun to explore the potential for sustainable investing to contribute to enhanced returns or decreased volatility, and interest in sustainable investing has significantly increased.

In addition, recent reports suggest that investors are beginning to realize the importance of analyzing sustainability issues in emerging markets, where future rapid growth could be constrained by human and natural resource issues. These dynamics have created a potentially positive environment for emerging markets sustainability indices.

Emerging markets sustainability indices have proliferated in recent years building upon the experience of developed market indices, yet these indices vary in their intents and remain at an early stage of market development.

In recent years, private financial service companies and stock exchanges have launched emerging markets sustainability indices. Seventeen emerging markets sustainability indices have been launched since 2004, with twelve of these indices launched since 2009 and two more indices in development.

In launching these indices, index providers’ intents vary from helping investors identify companies with better sustainability disclosure and performance in a given market to encouraging better corporate sustainability performance among market participants.

While the supply of these indices is growing, the market is not mature. Sustainable indices in developed markets have existed for a longer period of time, thus they are further along in several areas important for attracting investors, including establishing a track record, the availability of investable products, and brand recognition.

Given that most emerging markets sustainability indices have been launched in the last two to three years, to date many of these indices have had limited success in attracting a large investor base. Stakeholder feedback indicated that several important issues appear to contribute to lagging investor demand, including:

- Investors are placing more emphasis on active sustainable investing strategies, such as integrating ESG analysis into investment processes, versus adopting passive strategies associated with sustainable index investing;
- Investors increasingly want to generate a market return – or better – with their sustainable investments and may not understand how or if an index can achieve this performance;
- Given the complexity or lack of communication about indices’ sustainability analysis in some instances, investors may not be clear about how an index’s sustainability analysis identifies sustainability leaders and laggards in a reliable and meaningful way;
- Global investors want to have regional exposure in emerging markets, as opposed to investing in a single country;
- Investors may have separate portfolio allocations for emerging markets and sustainability investments; and
- Investors may be challenged by general emerging markets investing issues, such as concentration and liquidity of companies.

However based on our research, there is evidence of potential investor interest in these indices from:

- Local investors interested in investing in companies with higher sustainability performance in their home markets, and
- Investors using index constituent lists as a source of investment ideas.

These may be areas for further research.

Despite current limitations, emerging markets sustainability indices can play an important role in supporting and driving broader sustainability efforts.

Beyond serving as a cost-effective way for investors to identify companies with higher sustainability performance and / or disclosure in a market, sustainability indices can – and are starting to – play an important role in supporting and driving broader corporate sustainability efforts in a number of ways.

Index providers can encourage companies to improve sustainability performance and disclosure by directly engaging with them and educating them about Environmental, Social, and Governance (ESG) criteria and index membership. The recognition afforded by index membership can provide an incentive for companies to disclose more detailed information about their corporate responsibility efforts as well as improve their sustainability programs. The branding that comes from being included in an index allows a company to demonstrate its commitment to sustainable business practices to investors and other stakeholders.

These indices can also highlight sustainability issues specific to a market (such as water, human rights, etc.) by emphasizing them in their ESG analysis.

Private company index providers can earn revenue not only by licensing their index products, but they may also benefit by capitalizing on their index brand to sell ESG data.

In addition, because indices identify a set of companies that meet higher sustainability standards and can track the performance of these companies against a market benchmark over time, they may be able to help demonstrate the link between better sustainability performance and investment outcomes. Indices also have the potential to encourage longer-term thinking that contributes to improved financial stability and reduces volatility.

Despite the broader role sustainability indices can play encouraging corporate sustainability efforts, it is important to note that sustainability indices – and sustainable investing in general – are only part of the solution to improve corporate sustainability performance. Financial incentives, disclosure standards and requirements, stakeholder engagement, and government regulation will continue to play a significant role in promoting sustainability, especially in the absence of broadly accepted positive linkages between sustainability performance and financial results.

However, emerging markets sustainability indices, like those in developed markets, face a set of fundamental challenges that need to be addressed to ensure that indices deliver value to investors and are positioned to promote corporate sustainability.

Based on research and stakeholder consultation, EEP identified four critical market challenges. While these challenges are important in emerging markets, they also broadly apply to developed market indices as well as sustainability investing in general.

- 1. Investor Intent and Index Communication** – Evolving concepts of sustainable investing have brought new investor segments to the sustainable investing market. These new investor segments seek risk-adjusted returns that are in line with, or are better than, the market. Index providers need to understand these different investor segments and clearly communicate how the index intent, construction, and approach to sustainability analysis help these varied sustainability investors meet their investment goals.
- 2. Index Sustainability Framework and Metrics** – The sustainability frameworks and metrics being used by indices to assess company sustainability performance are still evolving, and most do not adequately link sustainability performance to financial results. Indices are especially challenged to assess how well a company is positioned to generate a performance premium from sustainable products and practices.
- 3. Data Analysis** – Index and ESG data providers are faced with the challenge of using sustainability data to effectively assess a company's sustainability performance and compare performance within and across sectors. Given the differences among companies, sustainability analysis needs to address varying company scales, product mixes, and value chain models (e.g., outsourced versus owned manufacturing).
- 4. Data Sourcing** – While corporate sustainability reporting is improving and some emerging markets companies have better sustainability reporting than others, ESG data and index providers continue to require meaningful and consistent sustainability data. In addition, many companies' sustainability reporting efforts do not emphasize the financial impacts of their sustainability programs, particularly as it applies to how sustainability efforts contribute to revenues.

Index providers and other stakeholders need to address these challenges to enable better alignment between the needs of various types of sustainability investors and the potential of indices to meet these varied needs.

Index providers that launch emerging markets sustainability indices face the challenge of operationalizing sustainability. These index providers – as well as other stakeholders – should be recognized for their efforts to promote sustainable investing and corporate sustainability.

Yet, as outlined above, there are a number of market challenges to overcome. To address these challenges, we recommend the following steps:

- Improve transparency and communications about the intent of the index, how the index is constructed, how it analyzes a company's sustainability performance, and how its approach impacts index performance;
- Develop sustainability frameworks and metrics to meet investor needs and assess the most material aspects of a company's sustainability performance;
- Continue to support research and analysis to understand how a company's sustainability efforts impact its financial performance and investment outcomes;
- Continue to improve analytical methods to ensure rigorous and consistent assessments and comparisons of companies' sustainability performance; and
- Support efforts to encourage better corporate sustainability reporting by focusing on materiality and engaging companies and stakeholders involved in multilateral reporting efforts.

Looking ahead in the near-term, emerging markets sustainability indices can benefit by adopting a collaborative model when developing, launching, managing, and evolving indices. In the longer-term, indices can help demonstrate the materiality of corporate sustainability by focusing on indicators of the business upside from the successful execution of sustainability strategies, as well as the value derived from downside risk management.

This report explores the current state of emerging markets sustainability indices and identifies a set of recommendations to strengthen their underlying business models. While recognizing that conditions and issues vary considerably in different emerging markets, index providers who have a well-defined intent and an index construction and sustainability analysis that are clearly communicated and aligned with investor needs will be best positioned to succeed. Partnering with key investors, leading companies, and committed stakeholders when designing and developing and later operating and evolving a sustainability index can result in a more robust index approach. Employing a collaborative model can help move indices down the path toward financial viability and growth.

Looking ahead, sustainability indices can help build the case for sustainable investing by providing evidence linking execution of companies' sustainability strategies to their financial performance. However, work is required to shift the view of sustainability from an emphasis on how well a company manages risks and avoids costs (downside risks) to a broader definition of sustainability that provides better indicators of how well a company develops and takes advantage of sustainability-driven innovation in product, service, brand and other intangibles (upside opportunities). Given the projected growth of emerging markets as well as the associated challenges from climate change, population growth and resource contention, emerging markets sustainability indices may be especially well positioned to identify approaches to analyze companies' abilities to both manage downside risks *and* benefit from upside opportunities.

In so doing, these indices will help demonstrate the materiality of corporate sustainability strategies and more fully harness the transformational power of sustainable investing.

II. Introduction and Overview

A. Study Goal

In 2010, the International Finance Corporation (IFC), the private arm of the World Bank, engaged Esty Environmental Partners (EEP), an environmental strategy consulting firm with substantial expertise in sustainability performance measurement and the construction of environment and sustainability-related investment “screens,” to research the rapid expansion of emerging markets sustainability indices and the potential for these indices to support the scale up of sustainable investing efforts.

Specifically, this report examines three related questions:

1. Why are emerging markets sustainability indices being launched?
2. What role can these indices play in adding value for investors and other stakeholders?
3. How can index providers and other market players enhance the potential for emerging markets sustainability indices to add value to investors and other stakeholders?

B. Project Approach

To analyze the emerging markets sustainability index market, EEP adopted a multi-phase approach which included:

- Using publicly available information to research emerging markets sustainability indices in order to outline the broad sustainability index market dynamics and understand how indices are constructed;
- Interviewing 10 index providers and ESG data providers to gather perspectives on index construction and sustainability analysis;
- Interviewing 15 investors to gauge investor interest in using sustainability indices with a particular focus on investors with strong sustainability or emerging markets focus areas; and
- Engaging a set of investors, index providers, ESG data providers, and consultants to gather feedback on EEP’s initial findings, recommendations, and next steps.

C. Report Structure

This report presents the findings of this research, identifies sustainability index market challenges, and outlines a draft set of recommendations that can put more market muscle behind the push for corporate sustainability.

Within the **Emerging Markets Sustainability Indices Findings** (Chapter III):

Section A. *Evolving Concepts of Sustainable Investing* examines evolving investor interest in sustainability-related investments, specifically in emerging markets.

Section B. *Emerging Markets Sustainability Index Overview* explores the rapid growth of emerging markets sustainability indices, index intents, and reasons for current limited investor demand.

Section C. *Broader Value of Indices* provides an overview of the potential role that sustainability indices can play in driving broader corporate sustainability efforts.

Section D. *Critical Market Challenges* highlights four market challenges that must be addressed to unlock the potential of sustainability indices to better meet investor needs and support corporate sustainability efforts.

Section E. *Recommendations* describes in detail a set of recommendations that address the challenges outlined in Section D.

Section F. *Considerations for Developing and Launching an Emerging Markets Sustainability Index* provides a summary checklist of considerations for index providers launching or managing an index.

Section G. *A Look Ahead* provides a high-level summary of EEP’s perspective on the potential future for emerging markets sustainability indices.

Appendix I. *Sustainability Index Value Chain and Terminology and Definitions* defines sustainability indices and terms used in this report and outlines the value chain and market players.

Appendix II. *List of Emerging Markets Sustainability Indices* summarizes the emerging markets sustainability indices analyzed in this report.

Appendix III. *Emerging Markets Sustainability Index Profiles* provides detailed profiles of each index.

III. Emerging Markets Sustainability Indices

Findings: Trends, Challenges, and Future

A. Evolving Concepts of Sustainable Investing

Interest in sustainable investing is increasing, and the market is evolving from largely values-oriented investors and now includes new segments with a growing emphasis on investors seeking value.

Over the past decade, sustainability has become an important issue in the investment landscape, driven by a variety of factors, including:

- Potential impacts and challenges from climate change,
- Growing natural resource scarcities, including oil, water, “rare earths,” and other minerals – especially those related to rapid industrialization in emerging economies,
- Global concerns about corporate social responsibility and sustainable business practices, and
- The need for greater transparency, stemming, in part, from the recent financial crisis.

These issues are driving changes in the sustainable investment market. Historically, sustainable investors were driven by “values” and focused on “screening out” sectors or companies that were viewed as having a negative social or environmental impact.

In recent years, sustainability has become a more critical aspect of a company’s business strategy. To address changing market trends, regulations, and stakeholder and consumer expectations, companies have begun to develop and implement corporate sustainability strategies that can yield significant business benefits.¹ How well a company manages its sustainability efforts is increasingly seen by many stakeholders as a proxy for good corporate management.

As companies implement sustainability strategies that result in material business benefits, more investors are realizing the importance of including how well a company manages its sus-

tainability strategy as part of their investment decision-making process.² Increasingly, some investor segments see the potential for companies that meet high sustainability standards to produce risk-adjusted returns that are in line with – or *better than* – the market.

Over time, different sustainable investor segments have begun to emerge, with some investors seeking returns in line with overall markets from investments consistent with their social or environmental values, while other investors are exploring the potential for sustainable investing strategies to contribute to enhanced risk-adjusted returns and / or decreased volatility. *These investor segments are described in more detail in Section D of Chapter III, which summarizes the market challenges.*

As these different investor groups enter the sustainable investing market, interest in sustainable investing has grown. While the tools and approaches to integrate sustainability into investment strategies are in early stages and will continue to evolve, several indicators of increasing investor interest in sustainability include:

- **Increasing number of signatories to the UN Principles for Responsible Investing (PRI):** As of May 2011, the UN PRI signatories include over 880 asset owners, managers, and service companies, representing over US\$25 trillion of assets under management (AUM), who are committed to incorporating ESG considerations into their decision-making and ownership practices.³
- **Growing investor interest in other “scorecard” efforts, such as the Carbon Disclosure Project (CDP):** The CDP requests greenhouse gas emissions data and climate change strategy information from companies on behalf of 551 institutional investors with US\$71 trillion of AUM.⁴ The growth of the CDP indicates increasing investor interest in how well companies manage their carbon impacts and the risks that climate change poses to their businesses. In 2010, CDP initiated a Water Disclosure Project, illustrating increasing investor focus on how companies manage water impacts. Other

1 Esty, Daniel & Winston, A., 2006. *Green to Gold: How Smart Companies Use Environmental Strategy to Innovate, Create Value, and Build Competitive Advantage*. Yale University Press, USA.

2 Gilbert, K., 2010, “Asset Managers Find New Source of Alpha – Responsible Investing.”

3 UN PRI, available at: www.unpri.org accessed May 2011. AUM as of May 2011.

4 Carbon Disclosure Project, available at: www.cdproject.net, accessed May 2011.



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scorecard efforts include Climate Counts and Newsweek Green Rankings.^{5,6}

- ***Increasing evidence suggesting that investing in companies with better sustainability performance can result in better risk-adjusted returns:*** As companies begin to realize business benefits from their sustainability programs, investors also realize that a company's management of its sustainability programs is material to its financial and competitive performance.⁷ While conclusions vary among studies, a number of studies suggest that adopting a sustainable investment strategy can yield better risk-adjusted returns.

For example, a 2011 World Economic Forum paper cited two Mercer meta-studies that analyzed the returns of responsible investments, finding that the majority of studies Mercer analyzed demonstrated a positive relationship between financial performance and ESG factors.⁸

While conclusions vary among studies, a number of studies suggest that adopting a sustainable investment strategy can yield better risk-adjusted returns.

5 Climate Counts, available at: www.climatecounts.org

6 Newsweek Green Rankings, available at: www.newsweek.com

7 Lubin, David & Esty, Daniel, May 2010. "The Sustainability Imperative," Harvard Business Review.

8 World Economic Forum. 2011. "Accelerating the Transition towards Sustainable Investing: Strategic Options for Investors, Corporations and other Key Stakeholders."

Similarly, in *Sustainable Investing: The Art of Long-Term Performance*, Cary Krosinsky makes the case that sustainable investments can result in better performance. By distinguishing between sustainable investments and socially responsible or ethical investments, he found that sustainable investments have outperformed ethical peers as well as mainstream indices.⁹

Despite these studies, more research is required to further document the positive relationship between a company's sustainability performance and financial outcomes. More research in this area is especially required in emerging markets.

- ***Increasing sustainable investing market and assets under management:*** One indication of increasing investor interest in sustainability is the assets under management (AUM) identified as sustainable. Recent reports suggest significant growth in AUM associated with sustainability, even though there is ongoing discussion about how investors are identifying assets as "sustainable."¹⁰ The 2010 Social Investment Forum (SIF) report on SRI investing trends identifies US\$3 trillion in AUM in the United States that use SRI strategies and indicates that U.S. SRI AUM have grown 380% since 1995.¹¹ The European Sustainable Investment Forum (EUROSIF) estimates AUM of €5 trillion (US\$7 trillion) in sustainable and responsible investments in Europe at the end of 2009.¹² In Europe, estimates suggest that the SRI investing market almost doubled between 2008 and 2010.¹³

In addition to general recognition of the potential for sustainable investing, recent reports highlight that investors are beginning to realize the importance of analyzing sustainability issues

in emerging markets.¹⁴ According to the IMF, emerging economies are expected to grow at a much faster rate than developed economies in the near future,¹⁵ and emerging markets investments are expected to parallel that trend.

While emerging markets provide a growth opportunity for investors, there are many factors in these markets that should drive investors to consider sustainability issues. For example, rapid population growth and improving living standards will increase consumption and put added strain on available natural resources, which could, in turn, constrain market growth or business performance.¹⁶ With so much new spending on building capacity to deliver products and services and pressure from sustainability factors, emerging markets firms have the potential to lead the world in implementing sustainable practices and business models. As such, sustainability challenges represent both a risk and an opportunity.

In addition, some emerging markets economies have had a history of limited transparency in corporate governance and other sustainability issues that could mask investor risks. While ESG disclosure in emerging markets is improving, only a small portion of companies use standard reporting frameworks or guidelines (e.g. GRI).¹⁷

As evidence of investor interest in emerging markets sustainable investing, a 2009 global survey of asset managers, conducted by IFC and Mercer, found that sustainability investing in emerging markets was over US\$300 billion.¹⁸ However, it is important to note that the majority of these assets are associated with active management.

Interest in sustainable investing in general, and in emerging markets specifically, has created a potentially positive dynamic for emerging markets sustainability indices. However, as outlined in the report below, index providers and other stakeholders must address a number of challenges in order to generate market traction.

9 Krosinsky, C. and N. Robins (eds). 2008. "Sustainable Investing: The Art of Long-Term Performance." Earthscan, UK and USA

10 It is relevant to note that assets identified as "sustainable" or "SRI" can range from traditional negative screening (e.g., eliminating certain sectors) to active ESG integration to engagement strategies.

11 Social Investment Forum Foundation. 2010. "Report on Socially Responsible Investing Trends in the United States."

12 EUROSIF. 2010. "European SRI Study 2010."

13 World Economic Forum. 2011. "Accelerating the Transition towards Sustainable Investing: Strategic Options for Investors, Corporations and other Key Stakeholders."

14 Responsible Investor, March 2010 Conference Report. "Sustainable Emerging Markets: Investing for the long-term in developing countries."

15 IMF. 2010. "World Economic Outlook: Recovery, Risk, and Rebalancing."

16 EUROSIF. 2010. "Emerging Markets Theme Report: Emerging Economies – Big Powerhouses with Large Potential."

17 Ibid.

18 IFC and Mercer. 2009. "Gaining Ground – Integrating Environmental, Social and Governance factors into Investment Processes in Emerging Markets."

B. Overview of Emerging Markets Sustainability Indices and Investor Demand

Emerging markets sustainability indices have proliferated in recent years building upon the experience of developed market indices, yet these indices vary in their intents and remain at an early stage of market development.

GROWING SUPPLY OF EMERGING MARKETS SUSTAINABILITY INDICES

Developed markets and global sustainability indices have existed for some time. For example, the Domini 400 Social Index was launched in May, 1990. Emerging markets sustainability indices, however, are relatively new.

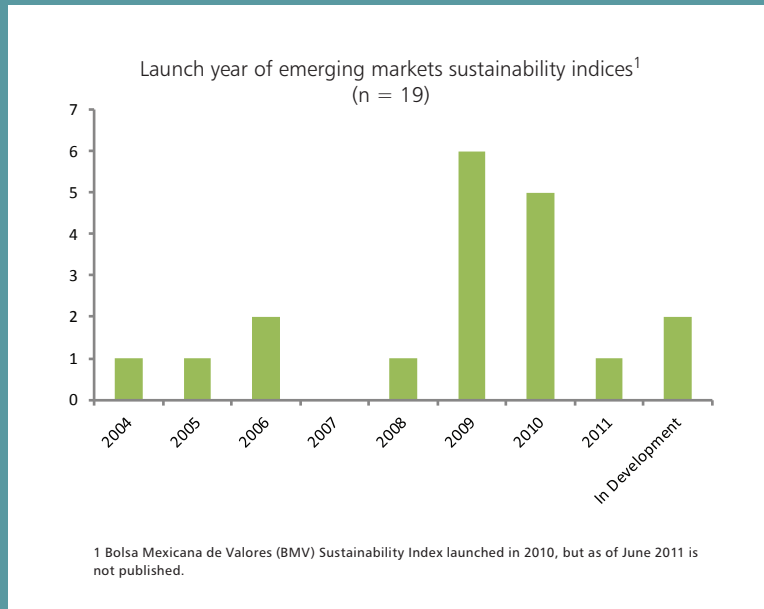
The number of emerging markets sustainability indices has grown significantly in recent years. In the course of this project, EEP identified seventeen indices that have launched since 2004.¹⁹ Twelve of these indices were launched since 2009. In addition, two indices are in development for launch in 2011 and 2012.²⁰

Figure 1 outlines the launch dates of the seventeen sustainability indices tracked in this report and highlights the two indices in development. The recent launch dates of the majority of emerging markets sustainability indices reinforces that this is a relatively new and evolving market.

¹⁹ Index information is based on EEP research and publicly available information accessed from September 2010 to March 2011.

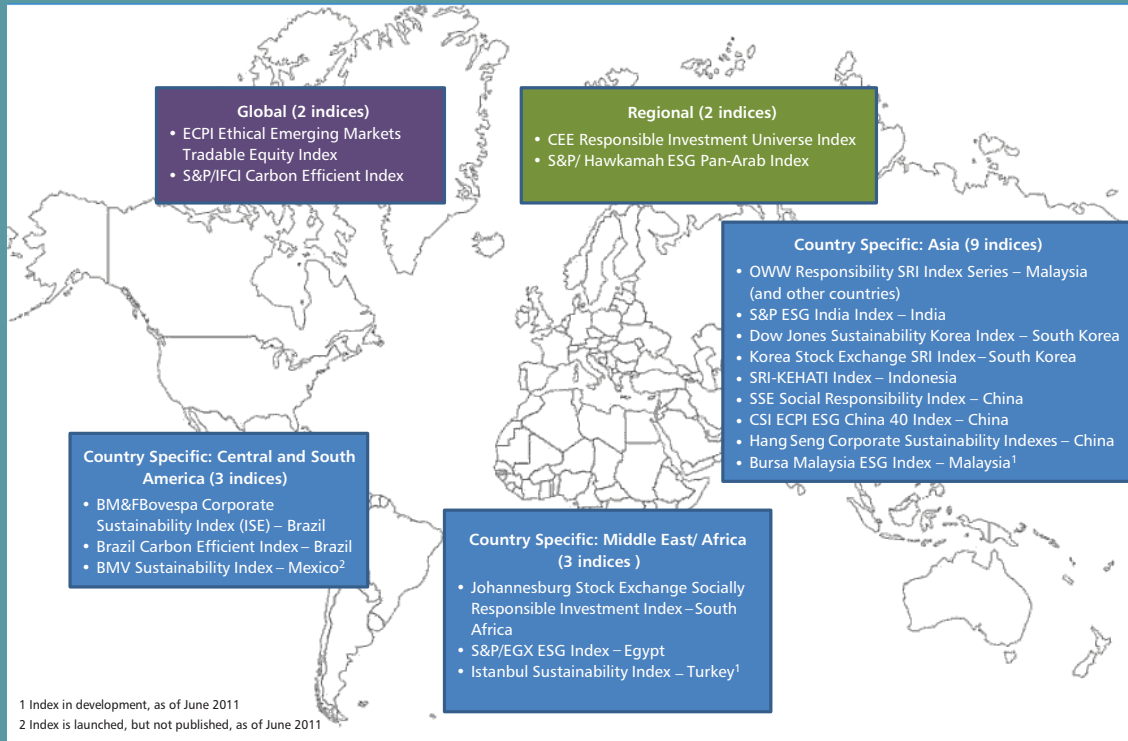
²⁰ In 2010, the Istanbul Stock Exchange in Turkey announced that they were developing a sustainability index that will be launched in the last quarter of 2011, and Bursa Malaysia, the Malaysian Stock Exchange, announced that it will be launching an ESG index in 2012.

FIGURE 1: EMERGING MARKETS SUSTAINABILITY INDICES LAUNCHES



Source: Esty Environmental Partners' Research

FIGURE 2: GEOGRAPHIC COVERAGE OF EMERGING MARKETS SUSTAINABILITY INDICES



For detailed Emerging Markets Index Profiles, see Appendix III

Source: Esty Environmental Partners' Research

The emerging markets sustainability indices that have been launched are primarily country-specific versus regional or global. Of the seventeen²¹ emerging markets indices launched, thirteen indices (as well as the two in development) are country-specific, two indices are regional, covering multiple countries,²² and two indices cover emerging markets globally.²³

21 The OWW Malaysia Index is one of a series of indices that OWW has launched covering Asia, the Middle East and North America. Only OWW Malaysia has been included in the index count as these indices are very similar. The OWW SRI Asia Index Series combines OWW country indices into an Asia regional index.

22 The CEERIUS Index covers Eastern Europe and the S&P/Hawkamah ESG Pan-Arab Index covers Middle East/North Africa (MENA).

23 The ECPI Ethical Emerging Markets Index and the S&P/IFCI Carbon Efficient Index.

While single country emerging markets indices may appeal to the local market they are designed to serve, they are less likely to appeal to investors that want regional or global emerging markets exposure. We describe this dynamic in more detail below.

Sustainability indices are being launched by a range of market participants, most notably stock exchanges and private financial services companies. Stock exchanges, such as the Johannesburg Stock Exchange and BM&FBOVESPA, have launched eight of the emerging markets indices, and private companies, such as S&P, Dow Jones, and ECPI, have launched eight other indices. One index has been launched by a consortium led by an NGO.

INDEX INTENT

Clarifying the index intent is important because it drives how the index is constructed and how the sustainability analysis is structured to meet investor needs. In addition, the index intent provides the foundation for the index business model. Based on EEP's research, index intent can vary among indices.

Private financial services companies tend to focus on how indices provide investment solutions to their clients, including attracting assets under management. These index providers see sustainability indices as a potential growth area and are interested in attracting investors and ensuring that the index is commercially viable.

In addition to attracting investors, some indices, especially those launched by stock exchanges, cite encouraging corporate sustainability performance and disclosure as a primary intent.

Based on the belief that companies will be motivated to improve their sustainability performance and disclosure in order to be included in an index, these indices can provide a test of sustainability for companies as well as lend credibility to the companies included in the index. By analyzing companies' sustainability performance, these index providers can also help improve market information and quality.

EARLY STAGE FOR EMERGING MARKETS SUSTAINABILITY INDICES

While both developed and emerging markets sustainability indices face a number of critical market challenges, developed markets indices are ahead of emerging markets indices in several key areas for attracting investors. These include building a track record, the availability of investable products, and brand recognition.

- **Building a track record:** Performance track records are important tools for investors to analyze how a fund or index performs over time and in different market conditions. Many investors want to examine several years of performance data before deciding to invest. The short tenure of many of the emerging markets sustainability indices suggests they will need more time to scale up investor commitment.

Developed markets indices have over twenty years of history. One of the first socially responsible indices was the Domini

400 Social, now called the MSCI KLD 400 Social Index.²⁴ It was launched in 1990 and covers the largest companies in the United States. It now has a track record of over two decades for investors to analyze.

The Dow Jones Sustainable Index family of indices was launched in 1999 to cover global developed markets. A decade later, the series added the DJSI Korea Index. The DJSI World Index has a track record of over a decade, while the DJSI Korea Index does not yet have two years of history. The first emerging markets sustainability index was launched by the Johannesburg Stock Exchange in 2004, and has yet to reach the ten-year mark.

- **Availability of investable products:** Passive investors do not invest directly in indices, rather they invest in products designed to track an index. These products can be a separately managed account, a mutual fund, or an ETF (Exchange Traded Fund). The longer tenure of the developed markets indices means there are more products based on those indices than those of emerging markets.

A few examples support this observation. While there are ETFs based on both developed and emerging markets sustainable indices, the first sustainable ETFs listed on the London Stock Exchange were introduced in February 2011 based on developed markets indices. iShares launched two ETFs available to UK investors indexed to DJSI – World and DJSI – Europe. These are regional or global developed markets funds based on indices that, in some form, have been around for over a decade. iShares also has two ETF listings for U.S. investors – MSCI KLD 400 Social Index and MSCI USA ESG Select Social Index. Both are relatively mature developed market indices.

- **Brand recognition:** Many of the developed markets sustainability indices are sponsored by companies with a broad and long standing reach into the global investment community via their standard index business. Dow Jones launched its first index in 1896, MSCI did so in 1969, and FTSE in 1962. With relationships throughout the investment community, these companies have a connection and credibility with investors that allow them to educate investors regarding

²⁴ The ESG data provider and sustainable index market has experienced consolidation in recent years. As an example, MSCI bought Risk Metrics Group in 2010. Risk Metrics had previously acquired KLD in 2009 and Institutional Shareholder Services (ISS) in 2007.

their offerings in the sustainability arena. Their reputations as providers of mainstream indices lend them credibility as they have expanded into the sustainability index market.

In contrast, with the exception of a few index providers, such as S&P and DJSI, many of the emerging markets sustainability indices have less global brand awareness. They have been launched by exchanges (JSE, BM&FBovespa) or by companies that specialize in sustainability (ECPI, OWW). While these are admirable organizations, they do not have the broad reach into the investment community of some of the developed markets index sponsors.

INVESTOR DEMAND

While emerging markets sustainability indices can be viewed as a cost effective way to identify companies that have higher sustainability performance, one key measure of index success over the long-term is its ability to attract investor capital. Attracting investors to companies is also important for indices to help drive corporate sustainability efforts.

Given the short track record of the majority of emerging markets sustainability indices in a market which is still evolving, these indices have had limited success in attracting a large investor base. Understanding investor dynamics will be important for index providers to build a solid market base as this market continues to evolve and grow.

Stakeholder feedback indicates that several important issues appear to contribute to current lagging investor demand, including:

- ***Investors are placing more emphasis on active sustainable investing strategies, such as integrating ESG analysis into investment processes, versus adopting passive strategies associated with sustainable index investing.*** Analyzing only a company's sustainability performance provides an incomplete picture of a company's financial outlook. While sustainability criteria can help identify companies with better performance, especially in the long term, additional information, such as financial performance, is required to support an informed investment decision. Some active managers are combining sustainability analysis with financial analysis to identify investable – and sustainable – companies. Sustainability indices generally focus only on

sustainability analysis, and most index approaches do not incorporate detailed financial analysis of the companies.

The majority of stakeholders consulted during the project confirmed that investors are more focused on active ESG integration than passive strategies. In addition, stakeholders see a focus on active investment strategies in emerging markets. One of the stakeholders consulted commented that “It seems many investors approach emerging markets actively rather than passively.”

In addition, some stakeholders see the rapidly changing sustainability landscape as requiring an active versus a passive approach. Asset managers may do this both to pursue out-performance and to meet standards such as those set by the UN PRI.

- ***Investors generally want to generate a market return – or better – with their sustainable investments, and may not understand how or if an index can achieve this performance.*** As discussed above, investors increasingly expect their sustainable investments to deliver risk-adjusted returns in line with, or better than, the market. A number of stakeholders consulted in the course of this project affirmed this point of view, commenting that even values-based investors were likely to target a market return from sustainable investments. The implication is that as investors consider investing in a sustainability index, they want to have confidence that the index will generate at least a market return.

Many of the emerging markets indices lack historical information and have a short-track record. Therefore, investors are challenged to understand the potential performance of an index. In addition, indices may not report this information in a way that helps investors understand the potential return. Thirteen of the sixteen published emerging markets sustainability indices (not including the BMV Sustainability Index, which has been announced but has not been published yet) report performance metrics in some manner, while three do not publicly communicate any performance data (e.g., daily, monthly, quarterly and year-to-date returns, or 1, 3, or 5 year annualized returns). However, only four of the thirteen emerging market indices that report performance compare the index to a broader market benchmark. This lack of reporting on comparative performance makes it difficult for investors to understand what kinds of returns to expect.

- ***Given the complexity or lack of communication about indices' sustainability analysis in some instances, investors may not be clear about how an index's sustainability analysis identifies sustainability leaders and laggards in a reliable and meaningful way.*** As discussed above, indices' intents vary, and each index has a different approach to sustainability assessment and index construction. While this proliferation of approaches may allow indices to meet different investor needs, the variety of approaches makes it difficult for investors to identify the appropriate index and understand how the index will help the investor meet their investment goals. In addition indices vary in how much information they communicate about their approach and what metrics they employ to analyze companies.

Furthermore, indices may not clearly articulate how their sustainability analysis identifies material sustainability issues for a company; therefore investors may not understand how the index links sustainability and business or financial performance.

This overall lack of clarity and the proliferation of approaches can cause confusion and impact investor interest in indices.

- ***Global investors want to have regional exposure in emerging markets, as opposed to investing in a single country.*** Given that the vast majority of indices are focused in a single country and global investors are generally more interested in regional or global emerging markets exposure than single country indices, many existing emerging markets indices may be challenged to attract these global investors. Single country indices may be more likely to appeal to local investors investing in their home markets than to global investors.
- ***Investors may have separate portfolio allocations for emerging markets and sustainability investments.*** With some exceptions, few global investors appear to combine emerging markets and sustainability approaches, although a number of investors interviewed suggested they expect this investment approach to increase in the future. Until these strategies are combined, emerging markets sustainability indices may be challenged to attract global investor capital.
- ***Investors may be challenged by general emerging markets investing issues.*** Investors may also be challenged to invest in emerging markets sustainability indices for more general

Despite lagging current investor demand, Esty Environmental Partners' research and stakeholder feedback indicate that there is evidence of potential investor interest in these indices.

reasons related to emerging markets investing. For example, the concentration of companies in emerging markets and a lack of diversification in the index can lead to increased volatility. In addition, liquidity in emerging markets can create challenges for investors. Many of the emerging markets sustainability indices include some liquidity criteria in their approaches, but some indices are more general in their description of the liquidity criteria that they employ.

Despite lagging current investor demand, our research and stakeholder feedback indicate there is evidence of *potential* investor interest in these indices.

- Local investors may be interested in investing in companies with higher sustainability performance in their home markets.
- Investors can use index constituent lists as a source of investment ideas.

For example, one large local investor in an emerging market uses the constituent list of a sustainability index to source investment ideas. Another local market investor is using an emerging markets sustainability index as a basis for a green fund.

These may be areas for indices to further explore.

C. Broader Value of Indices

Despite current limitations, emerging markets sustainability indices can play an important role in supporting and driving broader sustainability efforts.

Beyond serving as a cost-effective way for investors to identify companies with higher sustainability performance and / or disclosure in a market, sustainability indices can – and are beginning to – play an important role in supporting and driving broader corporate sustainability efforts in a number of ways.

Index providers can encourage company sustainability performance and disclosure by directly engaging with companies to educate them about ESG criteria and index membership. The recognition afforded by index membership provides an incentive for companies to disclose more detailed information about their corporate responsibility as well as to improve their sustainability programs. The branding that comes from being in an index allows a company to demonstrate its commitment to sustainable business practices to investors and other stakeholders.

A recent study of BM&FBOVESPA's Corporate Sustainability Index (ISE – Índice de Sustentabilidade Empresarial) found that ISE has had a positive impact on companies' sustainability efforts in the Brazilian market.²⁵ Companies that have been included in the index since the inception have been motivated to review their sustainability practices, a process which they believe leads to improved competitiveness and reputation.

Sustainable indices can also emphasize sustainability issues specific to a market (such as water, human rights, etc.). By including specific issues in their ESG analysis, indices encourage companies to develop policies and programs to address these issues. For example, in South Africa, the Johannesburg Stock Exchange SRI Index includes criteria that assess a company's performance on Black Economic Empowerment, a critical issue in the South African market.²⁶

Several emerging markets stock exchanges have been introducing indices. While a primary motivation is to encourage investors to participate in the index, a side benefit can be the

ability of an exchange to demonstrate that its listed companies are implementing sustainability standards, and are worthy of investment.

In contrast to the exchanges, private financial services companies that launch indices tend to focus on how indices provide investment solutions to their clients rather than how indices can impact corporate behavior. These index providers see sustainability indices as a potential area of business growth and a way to leverage existing ESG research. While private index providers can earn revenue by licensing their index products, they may also capitalize on their index brand to sell ESG data. FTSE4GOOD initiated an ESG rating product in 2011. MSCI also has ESG data that they sell in addition to their ESG indices. While demand for emerging markets ESG data may lag demand for developed markets ESG data, launching indices may be a way for index providers to build emerging markets databases and approaches.

In addition, because indices identify and track a set of companies with potentially better sustainability performance, over time they may be able to help demonstrate the link between better sustainability performance and investment outcomes. Indices also have the potential to encourage long-term investment thinking, which contributes to improved financial stability and reduces volatility.

Despite the broader role sustainability indices can play encouraging corporate sustainability efforts, it is important to note that sustainability indices and sustainable investing in general are only part of the solution to improve corporate sustainability performance. Financial incentives, disclosure standards and requirements, stakeholder engagement, and government regulation will continue to play a significant role in promoting sustainability, especially in the absence of broadly accepted positive linkages between sustainability performance and financial results.

* * *

The supply of emerging markets sustainability indices has increased rapidly. These indices have the potential to support sustainable investment and better corporate sustainability performance in emerging markets.

Index providers and other stakeholders should be given credit for their significant efforts in launching these indices; however, the market is at an early stage of market development and current investor demand appears to be lagging. To continue to support market uptake, EEP has identified several market challenges, which are laid out in the following section.

25 IFC. 2010. "BM&FBOVESPA Sustainability Index & the Responsible Practices of Brazilian Corporations."

26 Johannesburg Stock Exchange SRI Index. 2010. "Background and Selection Criteria 2010."

D. Critical Market Challenges

However, emerging markets sustainability indices, like those in developed markets, face a set of fundamental challenges that need to be addressed to ensure that indices deliver value to investors and are positioned to promote corporate sustainability.

Based on research and stakeholder consultation, EEP identified four critical market challenges along the sustainability index value chain:

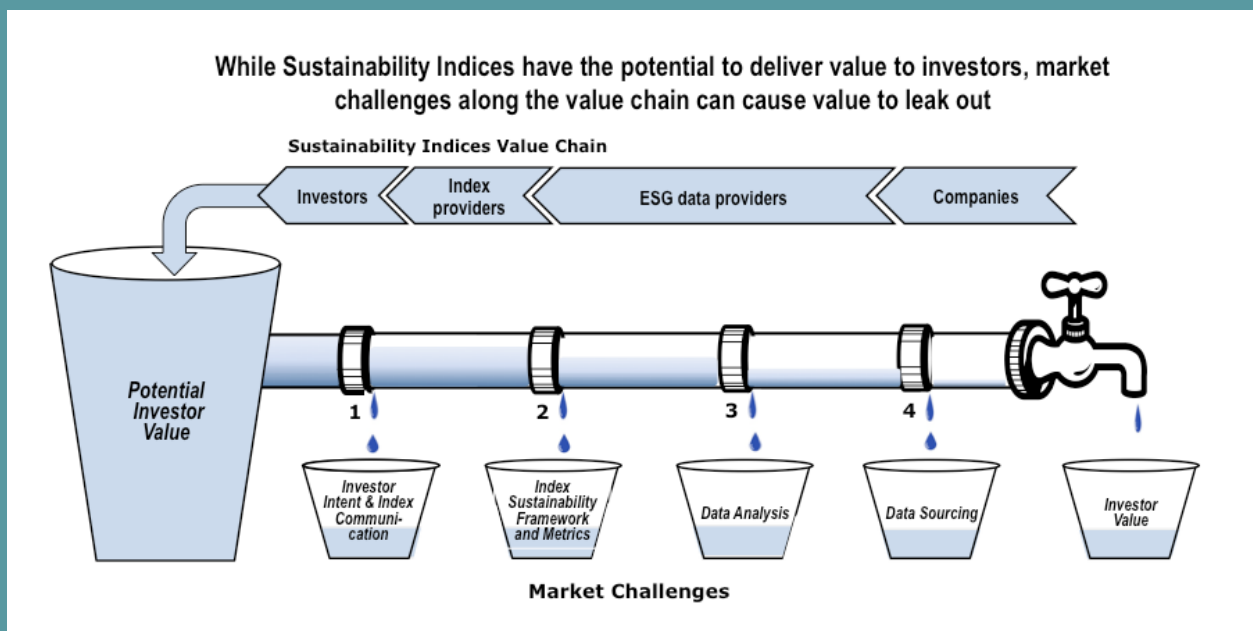
1. *Investor Intent and Index Communication,*
2. *Index Sustainability Framework and Metrics,*
3. *Data Analysis, and*
4. *Data Sourcing.*

While these challenges are particularly important in emerging markets, they also apply to developed market indices as well as the broader sustainable investing market.

To understand these challenges, it is useful to think about a “leaky pipe” as a metaphor. Investors can potentially realize value by investing in sustainable companies. ESG data providers and indices can help facilitate these investments by identifying sustainable companies. However, value flowing through the pipe can be lost at any one, or a combination, of four “leaks,” or market challenges.

Addressing these challenges will encourage alignment among market players (investors, index providers, ESG data providers, and companies) and enable the indices to meet their goals of attracting investors and encouraging corporate sustainable performance.

FIGURE 3: SUSTAINABILITY INDEX MARKET CHALLENGES: THE “LEAKY PIPE”



Source: Esty Environmental Partners' Research

Challenge 1: Investor Intent and Index Communication – *Match investors’ sustainability and investment intents and expectations to the appropriate investment vehicles.*

Historically, socially responsible investors represented a market segment that was somewhat willing to sacrifice returns as the price for value investing. Evolving concepts of sustainable investing have brought new sustainable investor segments to the market – specifically, those seeking returns that are in line with, or better than, the market.

While analysts have categorized investor groups in a variety of ways,²⁷ EEP identifies four types of investors that vary by intent and performance expectations. These investor segments are presented as four distinct investor types, though stakeholders in the research process commented that investors may straddle more than one type, and sometimes investors may not be clear about their intent or expectations. See Table 1 for a description of the four investor segments.

27 As an example, based on Peter Kinder’s “Socially Responsible Investing: An Evolving Concept in a Changing World” by Nelson Capital Analysis, Lloyd Kurtz of Nelson Capital identifies four types of investors: Values-based, Values Seeking, Governance, and Change. Kurtz, L. SRI in the Rockies Conference Presentation, November 2010.

TABLE 1. SUSTAINABILITY INDEX INVESTORS				
	Traditional SRI Investors	ESG Tilt Investors	Sustainability Premium Investors	Environmental Opportunity Investors
Intent	Are highly motivated to invest in line with values and select indices emphasizing social or environmental values	Seek market parity, with reduced volatility, but with a defined sustainability tilt to their portfolio	Seek better than market performance based on a belief that companies with better sustainability performance should see better long-term financial performance	Seek investment opportunities that emphasize specific environmental sectors or technologies based on a belief that these sectors offer above average returns
Performance Expectation	Primary focus is on values, even at some potential cost to investment performance; however, not all SRI investors are willing to sacrifice performance and may look for returns at least in line with the market	Performance that closely tracks a benchmark with a sustainability focus	Outperformance that is based on investing in companies with high ESG ratings or recognized sustainability leadership	Outperformance based on companies’ ability to benefit from participation in specific sectors or by taking advantage of new technologies
Potential Index Investment Sought	Indices with ESG screening methodologies that align with their values, including negative industry screens or excluding individual companies that do not meet sustainability thresholds	Indices designed to correspond to the market via similar sector weightings or other characteristics through the selection of companies that meet sustainability criteria	Indices that offer investors potential “alpha” or outperformance based on a company’s sustainability efforts, but this segment may be more likely to pursue active ESG integration versus invest in an index to achieve outperformance	Indices that offer investors potential “alpha” or outperformance based on a company’s sustainability efforts

Source: Esty Environmental Partners’ Research

All four of these investor segments have legitimate investment intents and performance expectations. Index construction may appropriately vary to meet these different investor needs.

These investor segments need to understand how indices are constructed to know if they meet their individual intents and expectations. Investors will want to understand how indices determine which companies are included in the index, what aspects of sustainability are considered, and how these “sustainable” companies perform relative to other investments or a benchmark.

As discussed above, indices provide varying levels of information about their construction and sustainability analysis, and in many instances, they are not clear about how these help investors meet their investment goals. In addition, a number of indices do not report performance, and many do not cite a benchmark.

How well indices understand the varied intents of sustainable investor segments and how indices address these intents in the index construction and communications are critical to matching investor needs with indices.

In addition, as we have noted, some indices place greater emphasis on encouraging corporate sustainability performance and disclosure than on attracting investors. These indices may serve more as a sustainability ranking of companies in a market. Yet even for these indices, it is important to clearly communicate their intent and how their index construction supports this intent.

Challenge 2: Index Sustainability Framework and Metrics – *Ensure that sustainability frameworks and metrics assess a company’s sustainability performance in a meaningful way, and focus on the most material aspects of corporate sustainability.*

Based on EEP’s research, the ability of an index to link a company’s sustainability performance to its financial results continues to evolve. One issue is that many companies may experience a time lag between implementing sustainability programs and generating value for the company. It is also especially difficult for analysts to assess how sustainability can drive better risk-adjusted returns or capture how well a company is positioned to generate a performance premium from sustainable products and practices.

As one ESG data provider said, “the lack of useful data for deciding which companies are best positioned across environmental risk and opportunity remains a key barrier.”

Challenge 3: Data Analysis – *Ensure the quality, consistency, timeliness, proper normalization, and methodological rigor of ESG data.*

Index and ESG data providers are challenged to use sustainability data from companies and other sources to effectively assess a company’s sustainability performance and compare performance within and across sectors. Given the differences among companies, sustainability analysis also needs to address varying company scales, product mixes, and value chain models (e.g., outsourced versus owned manufacturing).

Stakeholders identified data analysis as an important challenge, particularly the ability for indices to normalize data and use objective indicators, though they recognize that indices and ESG data providers are actively addressing this challenge.

Index providers that launch emerging markets sustainability indices face the challenge of operationalizing sustainability.

Challenge 4: Data Sourcing – *Obtain meaningful and consistent sustainability data from companies and other sources to conduct accurate ESG analysis.*

Corporate sustainability reporting is improving. While some emerging markets countries and companies have better sustainability reporting than others, ESG and index providers remain challenged to access meaningful and consistent sustainability data from companies and other sources. In addition, stakeholders in the process also commented that verifying information, especially from smaller emerging markets companies, is a challenge.

Various efforts are underway to improve sustainability reporting and to increase comparability and the number of companies reporting. The goals of these efforts are to make sustainability reporting more systematic by promoting frameworks and engaging companies.

Several significant efforts worth noting include:

- The Global Reporting Initiative (GRI) is a global effort to establish sustainability reporting frameworks and is arguably the most widely adopted reporting standard. In 2010, over 1800 organizations reported using GRI.²⁸
- International Integrated Reporting Committee (IIRC) is an international, multi-stakeholder initiative co-led by GRI and the Prince's Accounting for Sustainability Project (A4S). The IIRC seeks to “create a globally accepted integrated reporting framework which brings together financial, ESG information in a clear, concise, consistent and comparable format.”

28 Global Reporting Initiative, available at: www.globalreporting.org

- The Emerging Markets Disclosure Project (EMDP) focuses on the specific issues associated with emerging markets companies. Through its project work streams, EMDP highlights disclosure trends, demonstrates investor support for increased disclosure and engages with companies in specific markets to encourage disclosure.
- The European Federation of Financial Analysts Societies (EFFAS) works to facilitate the integration of ESG into investment processes. In 2010, EFFAS, along with the Society of Investment Professionals in Germany (DVFA), released a set of sector-based key performance indicators that can be integrated into traditional financial analysis.
- The Impact Reporting and Investing Standards (IRIS) aims “to create a common framework for defining and reporting the performance of impact capital.”²⁹
- Exchange disclosure requirements also encourage company sustainability reporting. For example, the Johannesburg Stock Exchange uses the King Code of Governance (King III) as a basis for its listing requirements, and requires integrated reporting from companies.³⁰

While these efforts aim to improve corporate sustainability disclosure, more work is required for companies to understand and communicate about the financial impacts of their sustainability programs. This is particularly true for reporting about the contribution of sustainability efforts to revenues and earnings, both in the short and longer-term. While stakeholders are working toward this goal, the bulk of this challenge is in front of us.

29 Impact Reporting and Investment Standards, available at: www.iris.thegiin.org/history

30 Integrated Reporting Committee of South Africa. January 2011. “Framework For Integrated Reporting and the Integrated Report – Discussion Paper.”



E. Recommendations

Index providers and other stakeholders need to address these challenges to enable better alignment between the needs of various types of sustainability investors and the potential of indices to meet these varied needs.

Index providers that launch emerging markets sustainability indices face the challenge of operationalizing sustainability. These index providers – as well as other stakeholders – should be recognized for their efforts to promote sustainable investing and corporate sustainability.

Yet, as outlined above, there are a number of market challenges to overcome. To address these challenges, we recommend the following steps:

1. Improve transparency and communications about the intent of the index, how the index is constructed, how it analyzes a company's sustainability performance, and how its approach impacts index performance.
2. Develop sustainability frameworks and metrics to meet investor needs and assess the most material aspects of a company's sustainability performance.
3. Continue to support research and analysis to understand how a company's sustainability efforts impact its financial performance and investment outcomes.
4. Continue to improve analytical methods to ensure rigorous and consistent assessments and comparisons of companies' sustainability performance.
5. Support efforts to encourage better corporate sustainability reporting by focusing on materiality and engaging companies and stakeholders involved in multilateral reporting efforts.

Recommendation 1: Improve transparency and communications about the intent of the index, how the index is constructed, how it analyzes a company's sustainability performance, and how its approach impacts index performance.

Key Points:

Sustainability index providers can help investors match sustainability index investments with their intent by providing investors with more information about:

- The intent of the index and the sustainability framework that the index uses to drive its analysis;
- What ESG categories and metrics are analyzed, and how they are aggregated and weighted in the ESG analysis;
- Where and how company ESG information is sourced; and
- How the index compares to the broader market with regard to sector weights, market capitalization, and other factors that affect stock market risk and return.

To facilitate investor demand for sustainability indices, it is critical for investors to be able to identify and select indices that align with the investment and sustainability goals that they seek. At the most basic level, index providers need to clearly communicate to investors the intent of the index, how the index assesses a company's sustainability performance, and what it means for their investment. While there is some transparency in the market today, index providers have an opportunity to more clearly communicate about their sustainability framework and the ESG categories, metrics, and indicators being used.

Communicating how the index analyzes sustainability in more detail will help investors and other stakeholders to understand what aspects of sustainability are emphasized and how the index providers relate sustainability analysis to company performance. Such transparency would make it possible for investors to be more sophisticated in how they use the data provided, honing in on the factors that they consider most important.

Along with communicating how the index assesses sustainability, the index provider should communicate not only the performance (which many indices communicate today), but also how the index compares to a broad market index regarding sector weights, market capitalization, and other systematic factors that affect stock market risk and return.

For many indices, sector, market capitalization, and other fundamental information is provided for the sustainability index without reference to a broad market benchmark. Such information would be more useful to investors if the implications for risk and return relative to the broad market were also provided.

Stakeholders interviewed by EEP commented that better communication can help “clarify the needs of the (investors) ... and the characteristics of the ... products in the market, in order to facilitate the contact between demand and supply.”

Stakeholders in the research process also provided feedback that identifying financing and funding of emerging markets sustainability indices remains challenging. Being able to define the index business model upfront is a priority – and understanding investors’ interests and needs will help index providers to assess the viability of their business models.

Indices can work directly with investors to align the index intent and construction with investor needs – even after an index is launched. For example, the JSE SRI Index has focused its post-launch strategy on engaging investors to demonstrate the value of the index, especially how the index can serve as a basis for additional research and engagement with companies.

The JSE SRI Index engages investors in several ways:

- Collaborating with the Government Employees Pension Fund of South Africa (GEPF), South Africa’s largest institutional investor. GEPF provides input into “how the index can serve the investment community best, and [how investors can] use the index research to help guide their engagement and responsible investment policies.”
- Working with EIRIS, the ESG data provider, to promote distribution of the credible and standardized ESG analysis for investor use
- Facilitating communications between companies and investors, allowing companies to present their sustainability strategies to the investor community
- Sharing knowledge with the investment and stakeholder community, including the local integrated reporting committee, CRISA (Code for Responsible Investment by Institutional Investors in South Africa), the UN PRI, the World Federation of Exchanges, etc., to offer learnings and leadership as well as to benefit from the broader knowledge base within these organizations.

Recommendation 2: Develop sustainability frameworks and metrics to meet investor needs and assess the most material aspects of a company’s sustainability performance.

Key Points:

- Given that mainstream investors are increasingly looking for sustainability indices with risk-adjusted returns that are in line with, or outperform, the market, indices should seek to address investor needs in the design and construction of the index.
- While approaches to assessing sustainability vary, the goal is to more comprehensively assess what is material about a company’s sustainability performance. The sustainability framework needs to assess not only risks and costs, but also how well a company can obtain upside benefits from its sustainability efforts (e.g., revenues from new “sustainable” products and services or brand value).
- ESG data providers need to continue to work to define and aggregate a set of metrics and indicators that represent their sustainability framework.

The index provider’s sustainability framework drives the ESG metrics and indicators that are used in the analysis. Given that investors are increasingly looking for risk-adjusted returns that are in line with or outperform the market, indices need to consider investors’ needs and expectations when they design and construct their indices. Index construction, the choice of metrics and indicators, and the weighting of metrics should take into account the most material aspects of a company’s sustainability performance. In addition, indices need to determine how best to weight companies within the index.

Based on EEP’s research and interviews, several ESG data providers make the connection from a company’s sustainability performance to its business performance in a general way, but few of them appear to conduct detailed research and analysis to support how their sustainability framework and the underlying metrics represent a company’s most material sustainability efforts. ESG data providers may measure the relationship between ESG categories or metrics and a company’s financial performance after the fact, but the goal should be to design a

sustainability framework that is based on indicators that capture the most material aspects of a company's sustainability efforts and how a company benefits from its sustainability efforts.

Index and ESG data providers' sustainability frameworks and the underlying metrics employed will vary depending on what has been identified as most material. As one stakeholder commented with regard to sustainability approaches, "There is not a one-size-fits-all solution. Diversity is important."

The overall goal is to encourage more comprehensive and meaningful analysis. One way this can be undertaken is to assess how well a company manages its sustainability risks and benefits from its sustainability efforts.

Many sustainability indices analyze how well a company addresses risks (e.g., looking at how a company addresses specific environmental or social issues), which is a first step toward determining which companies will perform better than a broad universe of companies. Investors have cited that identifying a company that manages risks well means not "owning" a company that is severely impacted by an adverse environmental or social incident.

However, managing risk is only one component of a company's sustainability efforts. The ability of a company to minimize sustainability-related costs (and promote eco-efficiency) should also be analyzed. An even more sophisticated assessment of sustainability would also account for how well a company benefits from the upside potential of its sustainability efforts – expanding revenues with sustainability-based goods and services, better connecting with sustainability-minded customers, and building a company's corporate reputation and brand.

An example of a simplified framework that is a more comprehensive approach to thinking about sustainability efforts is articulated in the article, "The Sustainability Imperative," by David Lubin and Dan Esty, published in the Harvard Business Review in May 2010.³¹ The model suggests that companies begin by focusing on defensive strategies, primarily those connected to risk and cost reduction. Once these initiatives are in motion, companies may be positioned to adopt offensive strategies that drive revenues and build value through new products and services.

ESG data providers and indices can leverage this framework by thinking about how sustainability indicators can capture the four opportunity areas of risk, cost, growth, and brand.

Once a sound sustainability index framework is identified, the next step is to define a set of metrics to reflect this framework. For example, within the environmental area, a data provider may define the metrics to analyze how well a company manages its climate change risks and costs, as well as how it manages its water footprint, biodiversity and land use impacts, waste, and raw material inputs, etc.

Defining the metrics drives the indicators that are used. A climate change performance metric may capture a company's exposure to regulatory risk, carbon efficiency, and potential for a company's products to benefit from a carbon-constrained world. Constructing the climate change metric requires layers of indicators. For example, an ESG data provider analyzing the climate change metrics may gather data on: if a company has established a climate change policy, the company's absolute Scope 1, 2, and 3 greenhouse gas (GHG) emissions, the company's emissions intensity, the company's reduction goals and targets, and the revenue from climate change related products, etc. The ESG data provider will need to determine how these indicators are aggregated, weighted and combined to form the climate change metric.

The challenge of gathering the indicators and creating metrics is further complicated by the fact that companies may not report data in the same way, may not report certain indicators, or may have different approaches to what is included in the indicator. To encourage reporting consistency and have access to meaningful indicators and data, index and ESG data providers need to actively engage companies on sustainability reporting. *See Recommendation 5 for more detail about engaging with companies on sustainability reporting.*

³¹ Lubin, David. & Daniel Esty, May 2010. "The Sustainability Imperative," Harvard Business Review.

Recommendation 3: Continue to support research and analysis to understand how a company's sustainability efforts impact its financial performance and investment outcomes

Key Points:

- To identify the most material ESG metrics, market players should support research that analyzes the link between a company's sustainability and financial performance.

As discussed above, increasing evidence suggests that there is a link between companies with better sustainability performance and better investment performance. Analysis of the performance of sustainable investments will help support the case for sustainable investing strategies. More granular analysis will also help identify what aspects of a company's sustainability program are most material.

More granular research by index providers, ESG data providers, academics, and NGOs will also help identify what aspects of a company's sustainability program are most material.

Based on EEP's research, several indices and ESG data providers are beginning to research the link between specific ESG categories or metrics and a company's financial performance. Additional research in this area is encouraged and will help identify the most material elements of a company's sustainability performance.

Indices will continue to have different definitions and ways of constructing their sustainability analysis based on these metrics. As one stakeholder commented, "there won't be one answer to the question." Yet, further analysis to understand which metrics are material will benefit the overall market.

Index and ESG data providers also recognize that some ESG factors are more material than others. While E, S, and G categories are all important in assessing a company's sustainability performance, research suggests that these categories do not have equal implications for a company's financial or competitive performance. There is more extensive evidence linking better environmental and governance performance with financial performance than evidence linking better social performance with financial performance. Therefore, initial research should focus on better understanding the materiality of E and G metrics.

Recommendation 4: Continue to improve analytical methods to ensure rigorous and consistent assessments and comparisons of companies' sustainability performance.

Key Points:

- Given the challenge of sourcing meaningful and consistent sustainability information, where possible, ESG data providers and indices should use metrics that are output based, objective, and represent consistent timeframes.
- Since output metrics often only reflect part of a company's sustainability effort and much of this effort is difficult to measure, ESG data providers may use more subjective or survey-based information. When using this information, it is important to ensure that the data collection and the analytical process are rigorous and facilitate cross-company and year-over-year comparisons.
- Where appropriate, ESG data providers should normalize data to ensure effective comparisons across companies. However, some data, such as an assessment of a market position in green products, may be ranked or even left in absolute values.
- ESG data providers should apply quality control practices to the data analysis process and be transparent about how they handle missing information.

Given the diversity of companies and differences in reporting, index and ESG data providers require high quality data as well as rigor in the analytical process to assess a company's sustainability performance. Index and data providers recognize these challenges, and based on EEP's interviews, many data providers continue to work diligently to address these challenges. The two most critical and challenging areas are: (1) defining the variables, and (2) data collection and analysis methods.

DEFINING THE VARIABLES

Use output indicators – Where possible, ESG data providers should use output indicators in addition to input indicators. Output indicators help track results and reflect a company's performance on specific sustainability efforts (e.g., how much a company has reduced its hazardous waste, or has grown revenue from products or services that meet some specified sustainability

criteria). Input indicators, on the other hand, track the company's sustainability efforts, including the policies and management resources a company has devoted to a specific issue such as waste management or product design. While input indicators are helpful to capture a company's commitment, policies, and resources, they do not fully reflect actual performance and "on the ground" results. For example, in some instances a company may communicate policies to address environmental issues, but may not have demonstrated progress.

In addition, because input indicators track the capacity of the firm to address sustainability, they can favor large companies that are able to allocate more budget or resources to sustainability initiatives, creating a bias toward these companies.

To address these issues and where possible, output data should be used to assess a company's performance. However, because not all sustainability practices can yield quantifiable output data, input data can be used to develop a clearer picture of a company's sustainability commitment, practices and management. When analyzing input indicators, it is important to develop a consistent analytical approach, as these measures are often difficult to compare across companies and sectors.

Use objective indicators – Where possible, ESG data should be objective information which is easily measured and quantified, and less prone to bias and opinion. Using quantitative data allows for objectivity and better comparisons across companies. In cases where an indicator is important to capture but is not easily quantified, the bias can be reduced by identifying clear, unambiguous criteria for assigning scores.

Seek consistent timeframes – The data timeframes should be consistent across all companies in a single universe of stocks. All the indicators in a given dataset that are used to rate a company should be for the same time period to ensure that the company's current performance is accurately reflected. Ideally, the data timeframe for all companies should be consistent to enable a fair comparison, though this can be challenging since reporting timeframes vary.

Data sets should be updated regularly with the most recent information. Additionally, in order to better measure present performance, the collected data should be time-bounded to ensure that legacy issues do not influence current ratings. A company that has performed poorly in the past, but has improved performance, should not be penalized indefinitely

into the future. Clear guidelines should determine the time-frame as well as necessary remedial steps a company should take to address a sustainability issue, so that if a company has improved its performance, it is accurately reflected in the ESG ratings.

DATA COLLECTION AND ANALYSIS METHODS

Use measured, public data where possible and use data derived from surveys with caution – In the absence of standard sustainability reporting requirements, many ESG data providers depend on company surveys. While the use of surveys is helpful to verify data or fill in missing gaps, depending on them as a primary data source can lead to inconsistencies because companies have different abilities to respond to these surveys. Analysis based on surveys may benefit larger companies that are able to devote more resources to answering lengthy questionnaires and are able to provide more comprehensive answers, than smaller companies.

Augmenting survey data with measured data that is publicly available is one way to address this issue. In addition, when using survey data, the survey question and analysis methodologies should be rigorous and replicable, to allow for comparisons across companies and timeframes.

Normalize data, where appropriate – One of the biggest challenges that ESG data providers face is how to compare companies of different sizes, in different sectors, and with different levels of vertical integration in a way that reflects the compa-

There are concrete steps that index and ESG data providers can take to improve corporate sustainability disclosure.

panies' sustainability efforts. Larger companies emit more gases, are more regulated, use more resources, have more disclosure documents, and have more media hits, in part, because they are larger. Companies in some sectors naturally have more emissions, and use more resources due to the nature of their business.

To address this issue, data should be normalized to acknowledge inherent company differences, and prevent some companies from being advantaged or disadvantaged based on size or sector. Data should also be normalized to take into account the degree of a company's vertical integration and to reduce bias against companies that do not outsource production. Companies that manufacture their own goods and services will inherently have larger impacts than those that outsource their manufacturing. If this is not taken into account, the ESG rating may unfairly advantage companies that are less vertically integrated.

On the other hand, there are times when using absolute data or a ranking is more appropriate. For example, if the sustainability framework calls for assessing a company's leadership role in the market for sustainable products, ranking companies by their revenue derived from green products may be a better indicator of future market share than normalizing environmentally-related revenues by total revenues.

Apply quality controls – By ensuring the quality of the actual data analysis process, ESG data and index providers can further establish the analytical rigor of the ratings. There are various ways to minimize data collection errors. For instance, data and index providers can compare new data with previous data for large or unexpected changes, verify data collected through

third party audits, or engage the companies being rated to ensure that the data is correct. Alternatively, ESG data providers can certify their processes. For example, ECPI has obtained ISO 9001 certification for its data analysis process since 2006.³² Separately, EIRIS has participated in establishing the Corporate Sustainability and Responsibility Research Quality Standard (CSRR QS), which aims to improve the quality management processes and transparency around Corporate Social Responsibility and Socially Responsible Investment research.³³

Communicate ways to address missing information – Given the inconsistency of sustainability reporting across companies, missing data is a challenge. There are several ways that ESG data providers currently address this challenge. ESG data providers can emphasize sustainability disclosure and give zero points for unavailable data. Alternatively, analysis methods can be designed to approximate missing data. Where information is not available, data providers can use quantitative models to approximate data. To improve the estimation, ESG data providers can engage companies and ask them to give feedback on the approximation, so that they can correct errors. While there are different ways to handle missing data, it is important for ESG data providers to have a consistent and transparent approach.

32 ECPI, available at: www.ecpigroup.com

33 Corporate Sustainability and Responsibility Research, available at: www.csrr-qs.org



Recommendation 5: Support efforts to encourage better corporate sustainability reporting by focusing on materiality and engaging companies and stakeholders involved in multilateral reporting efforts.

Key Points:

To improve meaningful corporate sustainability reporting, index and ESG data providers can:

- Be more transparent with companies about how their sustainability performance is evaluated and the metrics being used in the analysis;
- Support standard sustainability reporting requirements;
- Encourage reporting initiatives to collaborate with one another and integrate their efforts; and
- Encourage companies to continue robust sustainability reporting, but also to report the business benefits and costs of their sustainability efforts.

While sustainability reporting has improved over the last several years, accessing consistent and meaningful data across companies in all markets is a challenge. To address this challenge, some index and ESG data providers have taken steps to encourage disclosure and promote corporate sustainability. For example, BM&FBOVESPA in Brazil helps companies improve their sustainability performance by being transparent about their assessment process and presenting their questionnaire to companies as a guide for best practices. As another example, OWW Consulting, the ESG data provider for the SRI-KEHATI Index, provides sustainability reporting training for constituent companies.

Focusing on data sourcing efforts is also important in that it encourages better sustainability data which will help support materiality analysis.

Going forward, index and ESG data providers can help to improve corporate sustainability disclosure by:

- Being more transparent about how companies are evaluated. By communicating how a company's sustainability performance is evaluated, ESG data providers can help companies – as well as other stakeholders – understand which data are most important. Exchanges that have created ESG indices

as a way to promote sustainability can provide specific guidance to help companies improve ESG performance and disclosure. Exchange-based indices can also create tools, such as online knowledge portals, to provide easy access to guidelines and information.

- Supporting standard sustainability reporting requirements. As discussed above, efforts are beginning to address how companies can identify and disclose the most material sustainability metrics. Indices and ESG data providers should support these multilateral efforts to ensure better sustainability data and more consistent reporting. Continued emphasis should be placed on the specific needs in emerging markets. Indices and ESG data providers can engage in projects, such as the Emerging Markets Disclosure Project, to continue to encourage the sustainability reporting standards that enable ESG analysis. Indices can also play a role in helping companies understand these reporting requirements.
- Encouraging sustainability reporting initiatives to collaborate with one another and integrate their efforts. While there is some integration and collaboration among reporting initiatives, stakeholders commented throughout the research process that the numerous efforts underway cause confusion among stakeholders, including investors, index and ESG data providers and companies. Stakeholders strongly voiced a need for the reporting standard initiatives to integrate their efforts, commenting that a key imperative is for “the varying reporting standards groups to integrate their efforts.”
- Encouraging companies to report business benefits and upside potential associated with sustainability efforts (e.g., dollars saved along with emissions reduced). While some companies may be reluctant to provide such information or may not be able to measure business benefits, encouraging the reporting of business benefits can provide ESG data providers and other stakeholders with a better understanding of how a company links their sustainability efforts to their financial performance. Integrated reporting efforts are underway, and focus on reporting the financial benefits and costs of sustainability efforts can build from existing efforts such as the IIRC. However, it is important to continue to emphasize the need for robust reporting of sustainability data, even as it is integrated with financial reporting.

F. Considerations for Developing and Launching an Emerging Markets Sustainability Index³⁴

Based on research and discussions with market stakeholders, EEP has developed a list of considerations for sustainability indices that have launched or are considering launching in emerging markets. These considerations are aimed primarily at index providers, either exchanges or private companies, who can think proactively about the steps to develop, launch and manage these indices on an ongoing basis.

PRE-LAUNCH

- Clarify the index intent – whether it is to attract investors, promote corporate sustainability, or both of these
 - Construct the index to meet these intents. If the primary intent of the index is to attract investors, identify how the index construction and sustainability analysis meet investor needs and how the index compares to a market benchmark
 - Identify the primary investor targets, including whether they are global or local investors, or if they are SRI, ESG tilt and/or sustainability premium investors
 - Engage investors to obtain feedback on index construction as part of the index development, using this ‘partnering’ strategy to attract a core set of investors who will provide investment commitment at the launch
 - Engage critical market stakeholders (e.g., regulatory authorities, business organizations, ESG data providers, etc.) to obtain input on ESG criteria and index construction
 - Define the index business model, including how the index will be financed or funded on an ongoing basis
 - Work with stakeholders, particularly ESG data providers, to develop the sustainability analysis, including the ESG criteria and weightings
- Develop a set of sustainability criteria that:
 - Balances global sustainability standards and specific market issues
 - Captures the material aspects of a company’s sustainability performance
 - Determine what indicators will be employed and how data will be sourced, e.g., survey versus research
 - Consider developing an advisory board or committee that can provide initial and ongoing feedback on index construction and sustainability analysis
 - Develop a process for how the index will address controversial events, company appeals, etc.
 - Develop a plan to communicate the sustainability approach and ESG criteria to companies – if necessary and resources permitting, develop ways to educate companies about how best to meet the index ESG criteria
 - Consider piloting or testing the index prior to launch to test the sustainability analysis and approach

POST-LAUNCH

- Conduct sustainability analysis on an ongoing basis, while continuing to focus on emerging sustainability issues that may need to be incorporated into the analysis
- Continue to engage critical stakeholders for feedback, including investors and companies
- Facilitate sustainability information flows between investors and companies
- Where appropriate, share best practices with other indices and engage stakeholders such as GRI, UN PRI, and local NGOs and regulators

³⁴ The authors would like to thank the JSE SRI Index for their input on the development of this list.

G. A Look Ahead

Looking ahead in the near-term, emerging markets sustainability indices can benefit by adopting a collaborative model when developing, launching, managing, and evolving indices. In the longer-term, indices can help demonstrate the materiality of corporate sustainability by focusing on indicators of the business upside from the successful execution of sustainability strategies, as well as the value derived from downside risk management.

There can be no doubt that investor interest in sustainability around the globe has gained momentum over the past decade. This progress is clearly reflected by the proliferation of emerging markets sustainability indices launched in recent years. These indices have contributed to raising awareness and gaining acceptance of the core concepts of sustainable investing among both companies and investors. Still, it should also be noted that many stakeholders and outside observers expect broad-based uptake of emerging markets sustainability indices to be some years down the road. While factors favoring the growth of sustainable investing such as increasing government regulation, natural resource shortages, stakeholder pressures and climate issues are considerable, further advances in sustainable index construction and methodologies will likely be required.

This report explores the current state of emerging markets sustainability indices and identifies a set of recommendations to strengthen their underlying business models. While recognizing that conditions and issues vary considerably in different emerging markets, index providers who have a well-defined intent and an index construction and sustainability analysis that are clearly communicated and aligned with investor needs will be best positioned to succeed. Partnering with key investors, leading companies, and committed stakeholders when designing and

developing and later operating a sustainability index can result in a more robust index approach. Employing a collaborative model can help move indices down the path toward financial viability and growth.

Looking ahead, sustainability indices can help build the case for sustainable investing by providing evidence linking companies' sustainability strategies to their financial performance. However, as this report also indicates, work is required to shift the view of sustainability from an emphasis on how well a company manages risks and avoids costs (downside risks) to a broader definition of sustainability that includes how well a company takes advantage of sustainability-driven innovation in product, service, brand and other intangibles (upside opportunities). This upside focus should ultimately aim to measure a company's new sustainability-related revenues and profits.

As index providers, companies, investors and other key stakeholders collaborate on developing, launching, managing, and evolving indices in the coming years, they should focus greater attention on measuring this business upside, especially new sustainability related revenues and profits. By identifying indicators that capture how companies create both short- and long-term financial value through successful execution of sustainability strategies, it will be possible to better assess and understand not only a company's risk management capabilities, but also the scale and durability of the sustainability upside.

Given the projected growth of emerging markets as well as the associated challenges from climate change, population growth and resource contention, emerging markets sustainability indices may be especially well positioned to identify approaches for analyzing companies' abilities to manage downside risks and benefit from upside opportunities.

In so doing, these indices will help demonstrate the materiality of corporate sustainability strategies and more fully harness the transformational power of sustainable investing.

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V. Appendices

Appendix I. Sustainability Index Value Chain and Terminology and Definitions

WHAT IS A SUSTAINABILITY INDEX?

A sustainability index identifies a set of companies from an underlying universe of firms based on an assessment of their sustainability performance and / or disclosure. Index providers select companies based on sustainability criteria, which may include environmental, social, and / or governance (ESG) measures, or a subset of ESG issues.

Companies selected for inclusion in a sustainability index are weighted to form a portfolio of stocks representing companies with better sustainability performance than the broad underlying market. Such a portfolio can form the basis of a passive approach to sustainability investing for investors who want a relatively efficient way of investing.

Emerging markets sustainability indices are similar to those in developed markets, such as the Dow Jones Sustainability Index or FTSE4GOOD, in that the index identifies a set of “sustainable” companies in a given market based on a sustainability assessment. Emerging markets indices can target a specific country, region, or be global.

SUSTAINABILITY INDEX VALUE CHAIN

The sustainability index market is a complex value chain of multiple players, and in some instances, firms can play more than one role.

- **Asset Owners** – Asset owners provide capital to invest in emerging markets indices. Asset owners can be institutional investors (such as pension funds, endowments, and foundations) that have a goal or mandate to integrate sustainability into their investment strategies, or retail investors who invest via Exchange Traded Funds (ETFs) or index funds based on sustainability indices.
- **Asset Managers** – An asset owner engages an asset manager to invest funds and may require an asset manager to have a sustainability mandate. Asset managers may license an index from a sustainability index provider and then create an ETF, index fund, or separately managed portfolio that closely tracks the index.

Asset managers may also:

- Subscribe to sustainability index data to serve as a benchmark – although evidence suggests this is a relatively limited activity, or
- Source ideas from indices, using the index constituent list as potential investment targets.
- **Index Providers** – Index providers create sustainability indices by defining how the index is constructed (i.e., how stocks are selected and weighted to create the portfolio for the index) and how companies’ sustainability performance is assessed. The ESG research and analysis that is used to assess sustainability performance may be conducted in-house, or the index provider can outsource it to a third party. Index providers can be stock exchanges, private companies, or in rare instances, a NGO.
- **ESG Data Providers** – Third-party ESG data providers gather sustainability data from companies and other sources (e.g. public disclosures, media, NGO tracking, surveys, etc.), and either independently or in partnership with the index provider, develop an ESG screening methodology and analyze data to assess companies’ sustainability performances against a set of criteria. Similar to index providers, the types of companies that provide ESG data vary. ESG data providers can be private companies, academic institutions, or NGOs and may represent a single organization or a combination of organizations working together.
- **Companies** – Companies are assessed by indices and may report on their sustainability programs publicly through reports, or by responding to surveys from ESG data providers and indices. The possibility of being included in an index can provide companies with motivation to improve their sustainability performance and / or disclosure.

TERMINOLOGY AND DEFINITIONS

While the exact terminology can vary among the index and ESG data providers, defining the terminology provides clarity for the different market activities. We define the general terms as follows:

- **Index Construction** – The index construction includes the elements that factor into the creation of the index, such as how the index provider selects the underlying universe of companies, any liquidity or other criteria applied to identify the underlying universe, and how the index weights companies or sectors included in the index.
- **Sustainability Approach / Screening Methodology** – The sustainability approach (or sustainability screening methodology) is the way in which an index or ESG data provider assesses a company's performance. Within the approach, there are several layers of information.
- **Sustainability Framework** – The sustainability framework drives the aspects of sustainability that the index or ESG data provider identifies as material in their sustainability analysis, and uses them to analyze a company. Index and ESG data providers may use an established framework (such as the UN Global Compact) to inform their sustainability analysis.
- **Sustainability Assessment Methodology** – The assessment methodology is how ESG data providers analyze and score companies. The methodology can be a simple scoring system with weightings or a more complex model. The result may be a quantitative score or a rating on a scale. The assessment methodology can also include a negative screen to eliminate companies in particular sectors.
- **ESG Categories** – ESG categories are the broad components that an ESG data provider uses to analyze a company. The majority of emerging markets sustainability indices analyze all three categories (environmental, social and governance). However, variations on ESG have been created, such as including a climate change category in addition to an environmental category.
- **ESG Metrics** – ESG metrics reflect a company's performance within a category of ESG. For example, under the broad environmental category, an ESG data provider may define separate waste, water and energy management metrics.
- **ESG Indicators** – To analyze metrics, the data provider defines indicators. For example, to analyze the metric of water management, an ESG data provider may use indicators such as what water policies have been implemented, what is the company's absolute water footprint or water intensity, what is the company's water efficiency, etc.

Appendix II. List of Emerging Markets Sustainability Indices¹

Index Name	Launch date	Country/Region	Ownership Structure / Owner	Research Source	ESG Data Provider
Indices available in the market (as of March 2011)					
Johannesburg Stock Exchange Socially Responsible Investment Index	2004	South Africa	Exchange: JSE	Outsourced	EIRIS / University of Stellenbosch Business School's Unit for Corporate Governance in Africa
BM&FBOVESPA Corporate Sustainability Index (ISE)	2005	Brazil	Exchange: BM&F BOVESPA	Outsourced	Center for Sustainability Studies at Fundação Getulio Vargas (University of Sao Paulo)
ECPI Ethical Emerging Markets Tradable Equity Index	2006	Emerging Markets (global)	Company: ECPI	In-house	ECPI
OWW Responsibility SRI Index Series	2006	Malaysia (and other markets)	Company: OWW Consulting	In-house	OWW Consulting
S&P ESG India Index	2008	India	Company: S&P	In-house	CRISIL, an S&P subsidiary
CEE Responsible Investment Universe Index	2009	Eastern Europe	Exchange: Wiener Bourse	Outsourced	Mag. Friesenbichler Unternehmensberatung
Dow Jones Sustainability Korea Index	2009	South Korea	Company: DJSI	Outsourced	Sustainable Asset Management (SAM)
Korea Stock Exchange SRI Index	2009	South Korea	Exchange: Korea Stock Exchange	Outsourced	Korea Corporate Governance Service /Eco-Frontier
S&P/IFCI Carbon Efficient Index	2009	Emerging Markets (global)	Company: S&P	Outsourced	Trucost
SRI-KEHATI Index	2009	Indonesia	NGO / Company: KEHATI/OWW Consulting	Outsourced	OWW Consulting
Shanghai Stock Exchange (SSE) Social Responsibility Index	2009	China	Exchange: Shanghai Stock Exchange	Outsourced	China Securities Index Co.
Bolsa Mexicana de Valores (BMV) Sustainability Index	2010 ²	Mexico	Exchange: BMV	Outsourced	EIRIS
Brazil Carbon Efficient index	2010	Brazil	Exchange: BM&FBOVESPA	Outsourced	Trucost/BM&FBOVESPA
CSI ECPI ESG China 40 Index	2010	China	Exchange: China Securities Index Co.	Outsourced	ECPI
Hang Seng Corporate Sustainability Indexes	2010	China	Company: Hang Seng Indexes Co.	Outsourced	RepuTex
S&P/EGX ESG Index	2010	Egypt	Company: S&P	Outsourced	Egypt Institute of Directors
S&P/Hawkamah ESG Pan-Arab Index	2011	Middle East and North Africa	Company: S&P	Outsourced	Hawkamah
Indices In development/ To be launched (profiles not included)					
Bursa Malaysia ESG Index	TBD	Malaysia	Exchange: Bursa Malaysia	TBD	Bursa Malaysia
Istanbul Sustainability Index	TBD	Turkey	Exchange: Istanbul Stock Exchange	TBD	Istanbul Stock Exchange

¹ Indices are listed in order of launch year.

² BMV announced its sustainability index in 2010. The publication of the index is scheduled for late 2011.

Appendix III. Emerging Markets Sustainability Index Profiles³

Johannesburg Stock Exchange Socially Responsible Investment Index

Summary	
<ul style="list-style-type: none"> • Launched in 2004 by the Johannesburg Stock Exchange, the JSE SRI Index was the first sustainability index to be launched locally in an emerging market and also the first sustainability index to be launched by an exchange, as opposed to an index company. • As one of the older emerging market sustainability indices, the JSE SRI Index methodology has been updated and revised over the years. • The social and governance indicators measured by the JSE SRI index include not only global standards, but also track country-specific issues such as Black Economic Empowerment (BEE) and HIV/AIDS. • The exchange has been very proactive in promoting ESG disclosure, and in 2010, became the first in the world to move towards requiring integrated reporting by all listed companies. 	
General Index Characteristics	
Launch Date	2004
Geographic Markets	South Africa
Ownership Structure	Exchange: Johannesburg Stock Exchange
Key Stakeholders in Construction	N/A
Index Construction	
Index Construction	<p>The eligible universe for the SRI Index is the FTSE/JSE All Share Index, which is made up of Top 40, Mid Cap and Small Cap companies. Top 40 and Mid Cap companies are automatically assessed against the ESG criteria. Small Cap companies can choose whether they want to be evaluated for inclusion in the index.</p> <p>At each annual review, participating companies have to meet the requisite threshold as specified in the criteria to qualify for inclusion in the SRI Index.</p> <p>The index is free-float market capitalization weighted. There is no upper limit for the number of companies that can be included in the index.</p>
Publishes Index Composition	Publishes list of constituent companies on website
Historical Performance	Charts of real-time index performance are available using exchange website Daily index data available through subscription to data feed.
Benchmark Cited	No benchmark cited
Sustainability Approach / Screening Methodology	
Outsourced / In-house ESG Research	Outsourced
ESG Data Provider	EIRIS (since 2007), assisted since 2010 by University of Stellenbosch Business School's Unit for Corporate Governance in Africa
Sustainability Framework	Companies are assessed against criteria across the triple bottom line (environment, society, and economy) as well as governance and its related sustainability concerns, which are then mapped to an E,S and G categorization framework to align with UN PRI principles.
Sustainability Assessment Methodology	Companies are assessed based on policy, management/performance and reporting against more than 90 indicators across each of Environment, Society, Economy, and Governance. Social and governance criteria include indicators for issues that are important in South Africa in particular, such as Black Economic Empowerment and HIV/AIDS. Companies need to meet the defined minimum requirements on the core and desirable indicators. An advisory committee works on defining the criteria.
ESG Categories	The JSE covers E, S, and G in its criteria, and since 2010, has included a specific category for climate change.
ESG Weighting	Not disclosed publicly
Publishes Indicator Data	Yes. Criteria document published by exchange provides details for each category
Research Methodology	EIRIS uses research and publicly available information sources, and also surveys companies to collect the data
Frequency of Updates	Annual

³ All index profiles have been reviewed by the index provider and/or data provider, with the following exceptions: BMV Sustainability Index, Dow Jones Korea Sustainability Index, Korea Stock Exchange SRI Index, and Shanghai Stock Exchange Social Responsibility Index.

BM&FBOVESPA Corporate Sustainability Index (Índice de Sustentabilidade Empresarial – ISE)

Summary	
<ul style="list-style-type: none"> • Launched in 2005, Brazil's ISE Index was developed in collaboration with multiple stakeholders including IFC. • It is one of the only indices that depend on voluntary completion of surveys by companies that want to participate in the index, and use public information for qualitative analyses in its assessment of companies. • The Index is governed by a multi-stakeholder board which includes representatives of government, NGOs, and investors associations, which approve the inclusion of companies into the portfolio. 	
General Index Characteristics	
Launch Date	2005
Geographic Markets	Brazil
Ownership Structure	Exchange: BM&FBOVESPA
Key Stakeholders in Construction	<p>The index was developed by a group of stakeholders to include environmental, social responsibility and investor perspectives. These stakeholders also comprise a Board for the ISE index. Board members include:</p> <ul style="list-style-type: none"> • ABRAPP: Brazilian Association of Pension Funds • ANBIMA: Brazilian Association of Capital and Financial Markets Institutions • APIMEC: Association of Capital Markets Analysts and Investment Professionals • BM&FBOVESPA: Securities, Commodities and Future Exchange • IBGC: Brazilian Institute of Corporate Governance • IFC: International Finance Corporation • Ethos Institute of Social Responsibility • Brazilian Ministry of the Environment • UNEP: United Nations Environmental Program
Index Construction	
Index Construction	<p>To be considered in the analysis, a company needs to be among the 200 most traded listed companies in Brazil. Answering the survey is voluntary, and companies can elect whether they want to be considered the selection process of the index.</p> <p>Once the surveys are completed, statistical analysis is used to pick out up to the top 40 performing companies. Once the board approves of the selected companies, they are included in ISE Index.</p> <p>The index is constructed to be a free-float market cap weighted index. The representation of any single economic sector in the portfolio of companies is capped at 15%.</p>
Publishes Index Composition	Yes, on website.
Historical Performance	<p>ISE provides performance data, which includes the following statistics:</p> <ul style="list-style-type: none"> • Daily Price • Yearly Variation (R\$/US\$) • Monthly Volatility • Yearly Records • Average Growth Rate • Monthly Price • Market Value
Benchmark Cited	No benchmark cited
Sustainability Approach / Screening Methodology	
Outsourced / In-house ESG Research	Outsourced
ESG Data Provider	The Center for Sustainability Studies at Fundação Getulio Vargas (GVces)
Sustainability Framework	<p>ISE uses the "triple bottom line" principle for sustainability assessment, which covers environmental, social and economic criteria as foundation for its evaluation. ISE has added three additional dimensions:</p> <p>a) general criteria, which evaluate issues such as whether the company is committed to sustainable development, transparency (whether reports are published), b) product criteria, which include consideration of risks to consumer health, and c) corporate governance criteria.</p>
Sustainability Assessment Methodology	Companies fill out the survey administered by the data provider, the Center for Sustainability Studies at Fundação Getulio Vargas (GVces).
ESG Categories	E, S and G
ESG Weighting	Not disclosed publicly
Publishes Indicator Data	Yes, the questionnaire is available publicly (in Portuguese).
Research Methodology	Survey and publicly available information
Frequency of Updates	Annual

ECPI Ethical Emerging Markets Tradable Equity Index

Summary	
<ul style="list-style-type: none"> • ECPI offers a variety of sustainability indices, many of which are focused on European markets. The indices are categorized as either alpha, or beta indices. The ECPI Ethical Emerging Markets Tradable Equity Index focuses on several emerging markets, and is a beta index that has high correlation to traditional benchmarks. ECPI does not have alpha indices, which are designed to outperform traditional indices, for emerging markets. • The index is one of four emerging market indices in this study that are not focused on one country, and only one of two indices that is not region-specific (companies are drawn from countries in Asia, Eastern Europe, S. Africa, and S. America). 	
General Index Characteristics	
Launch Date	2006
Geographic Markets	Global emerging markets – Countries represented as of 12/2010 include Brazil, Hong Kong, Hungary, India, Indonesia, Mexico, New Zealand, Poland, Russian Federation, Singapore, South Africa, South Korea, Taiwan
Ownership Structure	Company: ECPI
Key Stakeholders in Construction	N/A
Index Construction	
Index Construction	<p>The index is composed of the top 50 companies by market cap, in the emerging markets, which pass the ECPI sector screening, and hold a positive ESG rating. Sectors which are screened out are those that are deemed controversial, and include “Military/Army, Pornography, Tobacco, Alcohol, Gambling, Nuclear Energy, Contraception, GMO Food production.”</p> <p>The concentration of any one country or sector is limited to 30%. To be selected for the Index, a company must also meet liquidity constraints. It should have a minimum market cap of USD 1 billion, and a 6-months average trading volume of USD 5 million.</p> <p>The Individual stocks in the index are capitalization weighted with a 10% cap on weight for any one company.</p>
Publishes Index Composition	ECPI does not publish the composition of its index on its website, but indicates that details about the constituents of its index and index performance are available through financial data vendors.
Historical Performance	<p>On its website, ECPI has charts that track the performance of its index, based on the nominal value of the index for both price and total return.</p> <p>It also provides the annualized volatility of the index.</p>
Benchmark Cited	No benchmark cited
Sustainability Approach / Screening Methodology	
Outsourced / In-house ESG Research	In-house
ESG Data Provider	ECPI
Sustainability Framework	The methodology is based on frameworks from bodies such as the United Nations Global Compact, the Global Reporting Initiative and the United Nation’s Principles for Responsible Investment (UN PRI). ECPI states that its methodology “aims to appraise and monitor a company’s long term strategic position, operational management and actual behavior towards society, the environment and markets.”
Sustainability Assessment Methodology	The ESG Rating uses indicators in the following categories: Environmental strategy and policy, Environmental management, Products, Production process, Community relations, Employees, Markets, and Corporate governance.
ESG Categories Analyzed	E, S, and G
ESG Weighting	ECPI’s ESG rating methodology does not specify the weighting of E, S and G factors in its analysis in public information.
Publishes Indicator Data	No
Research Methodology	Research on companies plus annual and sustainability reports. Information provided by qualified media sources, NGO’s statements and also direct contact with investor relations.
Frequency of Updates	Annual

OWW Responsibility SRI Index Series

Summary	
<ul style="list-style-type: none"> • The first indices in the OWW Responsibility SRI Index Series were launched in 2006 and covered Malaysia and Singapore. SRI indices in other markets, such as Thailand and the Middle East, are also available to investors. • The index was the first product offered in the Malaysian market that catered to Socially Responsible Investors, by providing an assessment of the Corporate Social Responsibility (CSR) performance of Malaysian companies based on international standards, customized to the Malaysian context. 	
General Index Characteristics	
Launch Date	2006 for Malaysia, which was first in series (others were launched at a later date)
Geographic Markets	Individual indices for various markets, including Malaysia, Singapore, Thailand, Middle East, etc.
Ownership Structure	Company: OWW Consulting
Key Stakeholders in Construction	N/A
Index Construction	
Index Construction	N/A
Publishes Index Composition	N/A
Historical Performance	N/A
Benchmark Cited	N/A
Sustainability Approach / Screening Methodology	
Outsourced / In-house ESG Research	In-house
ESG Data Provider	OWW Consulting
Sustainability Framework	OWW Consulting's ESG rating methodology incorporates corporate responsibility and ESG principles, which are also part of UN PRI and Global Compact Principles.
Sustainability Assessment Methodology	The index assessment covers six domains: Environment, Labor Practices and Decent Work, Human Rights, Community, Business Behavior, and Corporate Governance. Where insufficient information is available the category is not graded. The Environmental criteria are weighted to differentiate between high, medium and low impact companies and different standards of environmental management are required in each case. A company's performance is measured by scoring its response to each question and weighting.
ESG Categories	E, S, and G
ESG Weighting	Not disclosed publicly
Publishes Indicator Data	No
Research Methodology	Survey and public information
Frequency of Updates	N/A

S&P ESG India Index

Summary	
<ul style="list-style-type: none"> The S&P ESG India Index is the first of a series of emerging market sustainability indices that S&P has launched. S&P's partnership with local data providers is a unique feature of its ESG index series. The index uses a quantitative analysis to screen the initial universe of stocks, and then uses a qualitative assessment to pick the final portfolio of stocks. All of the data used in the analyses are from public sources, and therefore the scores received reflect the extent of a company's disclosure, as well as its ESG performance. 	
General Index Characteristics	
Launch Date	2008
Geographic Markets	India
Ownership Structure	Company: S&P
Key Stakeholders in Construction	Supported by IFC, and developed by a consortium of S&P, CRISIL and KLD
Index Construction	
Index Construction	<p>The investment universe is the top 500 Indian companies based on total market capitalization, which are listed on the National Stock Exchange of India. Fifty of the best performers based on an assessment of their ESG performance are included in the index.</p> <p>The assessment process for each company assigns three scores – a quantitative, a qualitative, and a composite score.</p> <p>Liquidity is used as a secondary threshold in the selection of index constituents. After the ESG screening, stocks with the highest scores are selected provided they have traded a minimum of 20 billion rupees in the last 12 months.</p> <p>A company's weight in the index is determined by its ESG score.</p>
Publishes Index Composition	No
Historical Performance	<p>In its index fact sheet, S&P provides a brief summary of the performance of the index:</p> <ul style="list-style-type: none"> Index performance chart, with comparison to a benchmark 1 month, 3 month and YTD returns 1 year, 3 year and 5 year annualized returns 3 year and 5 year annualized standard deviations of returns
Benchmark Cited	S&P CNX Nifty
Sustainability Approach / Screening Methodology	
Outsourced / In-house ESG Research	In-house
ESG Data Provider	CRISIL, an S&P company
Sustainability Framework	The social and environmental screens are based on output from the mapping of Global Reporting Initiative, Global Compact and Millennium Development Goals.
Sustainability Assessment Methodology	<p>The assessment process for each individual company assigns three scores:</p> <ul style="list-style-type: none"> Quantitative Score: A score is assigned for the company's transparency and public disclosure on corporate governance, environment, and social governance. Qualitative Score: The 150 of the original 500 companies that have the highest quantitative scores will then be assigned a qualitative score, based on further analysis of their performance, news stories, websites, and CSR filings. Composite Score: A composite score is calculated by combining the quantitative and qualitative scores.
ESG Categories	E, S, and G
ESG Weighting	Not disclosed publicly
Publishes Indicator Data	No
Research Methodology	Research for the sustainability assessment is conducted using publicly available information, including company reports, and also news reports and other websites. Companies are given credit for their transparency and disclosure practices.
Frequency of Updates	Annual

CEE Responsible Investment Universe (CEERIUS) Index

Summary	
<ul style="list-style-type: none"> The CEERIUS Index is one of four emerging markets indices that cover multiple emerging markets countries. The ESG methodology for the index assesses companies on various criteria from the perspective of multiple stakeholders, and also includes criteria that assess the impacts of products and processes. The screening methodology uses a combination of negative screening and a quantitative model, and focuses on environmental and social concerns. 	
General Index Characteristics	
Launch Date	2009
Geographic Markets	Central, Eastern, South-Eastern Europe
Ownership Structure	Exchange: Wiener Börse AG
Key Stakeholders in Construction	N/A
Index Construction	
Index Construction	<p>Underlying stocks are selected from the CECE Extended Index and CECE Mid Cap Index</p> <p>Negative screening is used to exclude companies involved in: armaments, nuclear energy, addictive drugs (tobacco and alcohol), genetic technology, and gambling.</p> <p>Based on the sustainability assessment, the companies that achieve the four highest rating levels (A+, A, A- and B+) are included in the index. For sectors where there are fewer top-rated companies, B rated companies may be included. This prevents entire sectors which may have lower scores from being excluded.</p> <p>The index is designed to be a capitalization-weighted price index.</p>
Publishes Index Composition	The index composition is available on the exchange's website
Historical Performance	Exchange website provides quotes (15 minutes delayed) and a chart for historical performance that tracks the nominal value of the index. While summary statistics are not presented, extensive historical data is available for analysis by interested parties.
Benchmark Cited	No benchmark cited
Sustainability Approach / Screening Methodology	
Outsourced / In-house ESG Research	Outsourced
ESG Data Provider	Mag. Friesenbichler Unternehmensberatung
Sustainability Framework	The approach to sustainability includes the consideration of social and ecological risks, and the screening methodology evaluates the concerns of different stakeholder groups, and assesses the companies' products.
Sustainability Assessment Methodology	<p>Stakeholders and product criteria are based on the stakeholder model, supplemented by a value chain analysis of the products or services. The criteria are organized into a matrix with four levels of management:</p> <ul style="list-style-type: none"> • Policies & Strategies • Programs, activities & results • Management Systems • Products & Services <p>and six stakeholder groups:</p> <ul style="list-style-type: none"> • Staff • Customers • Investors • Society • Market Partner • Environment <p>Each intersection of the matrix forms a category of assessment. Overall, the sustainability model contains approximately 100 individual criteria, which are operationalized by 400 quantitative and qualitative indicators.</p> <p>The sustainability assessment assigns companies a rating on a scale of A+ to C-.</p>
ESG Categories	Covers social and environmental concerns
ESG Weighting	Not disclosed publicly
Publishes Indicator Data	No
Research Methodology	The index uses publicly available information as well as information requested from companies through surveys.
Frequency of Updates	Annual

Dow Jones Sustainability Korea Index

Summary	
<ul style="list-style-type: none"> • The Dow Jones Sustainability Index (DJSI) is one of the most developed and well known sustainability index. • All indices of the DJSI family are assessed according to the same Sustainable Asset Management (SAM) Corporate Sustainability Assessment methodology. • DJSI uses a combination of survey data and research to assess companies' performance. • General and industry-specific variables account for approximately 40% and 60% respectively of a company's score. 	
General Index Characteristics	
Launch Date	2009
Geographic Markets	South Korea
Ownership Structure	Company: Dow Jones
Key Stakeholders in Construction	N/A
Index Construction	
Index Construction	<p>The DJSI selects the top 30% of the 200 biggest companies in South Korea as listed in the Dow Jones Global Total Stock Market Index, based on sustainability analysis.</p> <ul style="list-style-type: none"> • DJSI first screens out low performing sectors from the index universe. Only those sectors where the corporate sustainability score of the highest ranked company globally has at least 1/2 of the maximum score on the assessment are eligible for the DJSI Korea. • To screen out low performing companies within the selected sectors, only companies with a corporate sustainability performance score of at least 1/2 of the sustainability score of the highest ranked companies globally in the same sector are eligible for the DJSI Korea. <p>Index components are weighted based on their free-float market capitalization.</p>
Publishes Index Composition	Composition available on DJSI's website
Historical Performance	<p>The fact sheet for the index provides a summary of the performance of the index:</p> <ul style="list-style-type: none"> • 1 month, 3 month, and YTD total return • 1 year, 3 year, 5 year, 10 year and since inception (Dec 2005) • Annualized total return
Benchmark Cited	No benchmark cited
Sustainability Approach / Screening Methodology	
Outsourced / In-house ESG Research	Outsourced
ESG Data Provider	SAM
Sustainability Framework	The index evaluates companies based on a variety of criteria including climate change strategies, energy consumption, human resources development, knowledge management, stakeholder relations and corporate governance.
Sustainability Assessment Methodology	The DJSI ranks companies within their sectors according to their corporate sustainability score.
ESG Categories	E, S, and G
ESG Weighting	Not disclosed publicly
Publishes Indicator Data	No
Research Methodology	All indices of the DJSI family are assessed according to the same SAM Corporate Sustainability Assessment. For each company, the input sources of information for the Corporate Sustainability Assessment consist of company responses to an online questionnaire, submitted documentation, policies and reports, publicly available information and SAM Research analyst's direct contact with the company.
Frequency of Updates	Annual

Korea Stock Exchange SRI Index

Summary	
<ul style="list-style-type: none"> • The Korean Stock Exchange (KRX) launched its SRI index in September 2009. • Eco-Frontier, the data provider, uses models developed by Innovest and RiskMetrics (both now MSCI), with which it has a partnership, and governance data provided by a local organization, the Korea Corporate Governance Service, to develop sustainability ratings that are specific to the local market. 	
General Index Characteristics	
Launch Date	2009
Geographic Markets	Korea
Ownership Structure	Exchange: Korean Stock Exchange
Key Stakeholders in Construction	Korea Corporate Governance Service
Index Construction	
Index Construction	<p>The underlying universe is determined based on liquidity criteria:</p> <ul style="list-style-type: none"> • Value traded: The transaction average amount for the period of the recent three months must be within the top 70% bracket among listed common stocks • Market capitalization: The transaction average market capitalization for the period of the recent three months must be within the top 50% bracket among listed common stocks • Free-float rate: More than 10% of the free-float rate of the current year <p>Inclusion in the index is based on the top scores in the SRI ratings and market capitalization (if the SRI ratings are the same). Company SRI ratings need to be above BBB for a company to be included in the index.</p> <p>The index is free-float market value-weighted index composed of 70 stocks.</p>
Publishes Index Composition	No
Historical Performance	N/A
Benchmark Cited	No benchmark cited
Sustainability Approach / Screening Methodology	
Outsourced / In-house ESG Research	Outsourced
ESG Data Provider	Korea Corporate Governance Service for Governance (G) data and local data collection, and Eco-Frontier for Environmental (E), and Social (S) data analysis
Sustainability Framework	The index is referred to as “an index for social responsibility investment,” and aims to raise awareness among companies listed on the exchange about corporate social responsibility and sustainability management.
Sustainability Assessment Methodology	Eco-Frontier uses RiskMetrics data models to assess EcoValue21™, a model for environmental ratings, and the Intangible Value Assessment Model for social assessment. Innovest, now part of MSCI, originally created these models. Korea Corporate Governance Service provides assessment for Governance.
ESG Categories	E, S, and G
ESG Weighting	Not disclosed publicly
Publishes Indicator Data	No
Research Methodology	Surveys and research
Frequency of Updates	Annual

S&P/IFCI Carbon Efficient Index

Summary	
<ul style="list-style-type: none"> • In 2009, S&P launched the IFCI Carbon Efficient Index to identify companies that have lower carbon emissions profiles. • The index is supported by the Carbon Disclosure Project. • While the index does not make claims of outperformance, it does state that the smaller the carbon footprint of the companies in the index, the lower the exposure to the rising costs of emitting carbon and the less the contribution to climate change. • The weights of companies within a single sector are adjusted based on the carbon footprint, while the sector weighting of the overall index is the same as the underlying S&P/IFCI Large Midcap Index. 	
General Index Characteristics	
Launch Date	2009
Geographic Markets	Global emerging markets, including countries from Asia, Europe, Central and South America, Africa
Ownership Structure	Company: S&P
Key Stakeholders in Construction	IFC
Index Construction	
Index Construction	<p>This index is based originally on the float-adjusted shares outstanding in the S&P/IFCI Large Midcap Index and is a modified-capitalization weighted index</p> <p>The weight of stocks within a sector is based on the company's carbon score, while the sector and country weighting of the overall index is the same as the underlying S&P/IFCI.</p>
Publishes Index Composition	Yes
Historical Performance	<p>In its index fact sheet, S&P provides a brief summary of the performance of the index.</p> <ul style="list-style-type: none"> • Index performance chart, with comparison to a benchmark • 1 month, 3 month, and YTD returns • 1 year, 3 year annualized returns • Risk as measured by the 3 year standard deviation of returns • 3 year correlation with benchmark
Benchmark Cited	S&P/IFCI Large Midcap Index
Sustainability Approach / Screening Methodology	
Outsourced / In-house ESG Research	Outsourced
ESG Data Provider	Trucost
Sustainability Framework	The index assesses companies based on their carbon intensity, which is defined as the company's annual GHG emissions, expressed as tons of CO ₂ e divided by annual revenues.
Sustainability Assessment Methodology	<p>To obtain a Carbon Score, the individual Carbon Footprint metric is used in conjunction with its benchmark weight in the parent index. The country market-sector combinations with the highest Carbon Scores are deemed to be High Potential Markets (HPM) and are targeted for potential carbon emissions reductions.</p> <p>Within each HPM, all constituents in the top half of their respective global sector rankings for carbon emissions will have their index weights reduced by 50% and redistributed on a pro rata basis to the more carbon efficient constituents within the same market sector combination. This redistribution changes the weighting of individual companies within a certain country or sector, but the weighting of the country or sector in the overall portfolio will remain the same.</p>
ESG Categories	E
ESG Weighting	100% E, with a specific focus on climate change
Publishes Indicator Data	No
Research Methodology	To calculate the carbon intensity of companies included in the S&P/IFCI Carbon Efficient Index, Trucost reviews company annual reports and filings, environmental/sustainability reports, public disclosures and corporate websites. If a company does not have a recent Carbon Footprint which can be used to calculate its carbon intensity, it is assigned a score based on its regional and sector carbon average.
Frequency of Updates	Annual

SRI-KEHATI Index

Summary	
<ul style="list-style-type: none"> • The SRI-KEHATI Index, which includes 25 companies, aims to promote environmental and social responsibility as well as good corporate governance in Indonesia. • To qualify for inclusion in this index a company must have a positive price earnings ratio. • The SRI-KEHATI index is unique because it was created to serve the particular investment needs of the Indonesian Biodiversity Foundation, and is the only NGO-owned index in this study. 	
General Index Characteristics	
Launch Date	2009
Geographic Markets	Indonesia
Ownership Structure	NGO/Company: The Indonesian Biodiversity Foundation – KEHATI, OWW Consulting
Key Stakeholders in Construction	Indonesia Stock Exchange (IDX), Yayasan Keanekaragaman Hayati Indonesia (the Indonesian Biodiversity Foundation – KEHATI)
Index Construction	
Index Construction	<p>The company must have: (1) total assets of more than 1 trillion Indonesian Rupiah, (2) positive price earnings ratio, and (3) public share ownership should be greater than or equal to 10%.</p> <p>Stocks that pass initial financial selection criteria are nominated to the Index.</p> <p>To identify the 25 stocks to include, the companies are rated based on the SRI-KEHATI sustainability criteria. The KEHATI Foundation also takes into consideration input from the Committee Board of SRI-KEHATI Index.</p>
Publishes Index Composition	Yes
Historical Performance	Daily performance data and quarterly performance statistic available online
Benchmark Cited	IDX LQ45
Sustainability Approach / Screening Methodology	
Outsourced / In-house ESG Research	Outsourced
ESG Data Provider	OWW Consulting
Sustainability Framework	OWW Consulting's ESG rating methodology incorporates corporate responsibility and ESG principles which are also part of UN PRI and Global Compact Principles.
Sustainability Assessment Methodology	<p>The index assessment covers six domains: Environment, Labor Practices and Decent Work, Human Rights, Community, Business Behavior, and Corporate Governance.</p> <p>Where insufficient information is available the category is not graded. The Environmental criteria are weighted to differentiate between high, medium and low impact companies and different standards of environmental management are required in each case. A company's performance is measured by weighting its score on its response to each question.</p>
ESG Categories	E, S, and G
ESG Weighting	Not disclosed publicly
Publishes Indicator Data	No
Research Methodology	Survey and public information
Frequency of Updates	Semi-annual

Shanghai Stock Exchange Social Responsibility Index

Summary	
<ul style="list-style-type: none"> • In 2009, the Shanghai Stock Exchange (SSE) introduced an index to assess how well companies are meeting the requirements for social responsibility disclosure stated in the exchange's "Notice of Improving Listed Companies' Assumption of Social Responsibilities" from May, 2008. • In this notice, a metric for "social contribution per value of share" was established, which is used to rank companies for inclusion in the index. 	
General Index Characteristics	
Launch Date	2009
Geographic Markets	China
Ownership Structure	Exchange: Shanghai Stock Exchange
Key Stakeholders in Construction	N/A
Index Construction	
Index Construction	<p>The underlying universe for the index is the SSE Corporate Governance Index. In order to determine the components of the index:</p> <ul style="list-style-type: none"> • The bottom 20% companies with the lowest average daily trading volume from the 230-company universe, based on the previous 12-month record prior to the beginning of the evaluation process are eliminated. • The top 100 companies are selected using the Social Contribution per Share (SC), which is detailed in the "Notice of Improving Listed Companies' Assumption of Social Responsibilities" issued by the SSE in May 2008. The specific criteria to assess the social contribution per share is not public. • Once the top 100 companies have been selected, they are screened to ensure that they do not have any CSR violations. • The stocks are weighted according to an adjusted market cap weighting.
Publishes Index Composition	Yes
Historical Performance	N/A
Benchmark Cited	No benchmark cited
Sustainability Approach / Screening Methodology	
Outsourced / In-house ESG Research	Outsourced
ESG Data Provider	China Securities Index Company
Sustainability Framework	Social and environmental risks and opportunities
Sustainability Assessment Methodology	The specific criteria to assess the social contribution per share is not public.
ESG Categories	E, S, and G
ESG Weighting	Not disclosed publicly
Publishes Indicator Data	No
Research Methodology	N/A
Frequency of Updates	Annual

Bolsa Mexicana de Valores (BMV) Sustainability Index

Summary	
<ul style="list-style-type: none"> • Mexico's Stock Exchange (BMV) launched a sustainability index to assess companies' sustainability, social responsibility and corporate management. • The stated goal of the index is to promote sustainable business practices. • The index will cover a diverse set of industries including beverages, construction, and mining. • The project has the support of the Financial Standards Foundation, Argentina's Financial Stability Center, Fidelis International Institute, and Mexican subsidiaries of Deloitte and HSBC. 	
General Index Characteristics	
Launch Date	December 2010 ⁴
Geographic Markets	Mexico
Ownership Structure	Exchange: BMV
Key Stakeholders in Construction	EIRIS and Ecobanca advised BMV on how to enhance corporate transparency and performance on sustainability issues among Mexican-listed companies. Anáhuac University also advised BMV on developing the index criteria and assessment methodology.
Index Construction	
Index Construction	Index has not been published
Publishes Index Composition	Index has not been published
Historical Performance	Index has not been published
Benchmark Cited	Index has not been published
Sustainability Approach / Screening Methodology ⁵	
Outsourced / In-house ESG Research	Outsourced
ESG Data Provider	EIRIS and Universidad Anahuac
Sustainability Framework	BMV defines three pillars of sustainability: Environmental Sustainability, Social Responsibility, and Corporate Governance. EIRIS based the sustainability indicators, in part, on principles established by the UN Global Compact.
Sustainability Assessment Methodology	The sustainability assessment of each company is based on their performance, impact, and positive responses to emerging issues in each of the three categories of E, S and G. Each individual question is scored on a scale from +3 to -3. The environmental assessment is normalized based on the sector in which it operates.
ESG Categories	E, S, and G
ESG Weighting	E: 50% S: 30% G: 20%
Publishes Indicator Data	Yes, BMV provides detailed category-level data.
Research Methodology	EIRIS representatives in Mexico analyze publically available information to rate a company's progress against three pillars of analysis: environmental sustainability, social responsibility, and corporate governance. EIRIS also sends surveys to companies to fill in data gaps.
Frequency of Updates	N/A

⁴ BMV announced its sustainability index in 2010. The publication of the index is scheduled for late 2011.

⁵ Information in this section is based on information that was released at the time the index was announced, but there are no index methodology documents or fact sheets available that describe the sustainability methodology.

Brazil Carbon Efficient Index

Summary	
<ul style="list-style-type: none"> • In an effort to encourage companies to assess, disclose, and monitor GHG emissions, BM&FBOVESPA and the Brazilian Development Bank (Banco Nacional de Desenvolvimento Econômico e Social/BNDES) have launched the Carbon Efficient Index (ICO₂). • The index uses an existing index, the IBrX-50, and adjusts the weighting of the components based on a carbon intensity metric, which is calculated using publicly disclosed information. 	
General Index Characteristics	
Launch Date	2010
Geographic Markets	Brazil
Ownership Structure	Exchange: BM&FBOVESPA
Key Stakeholders in Construction	BM&FBOVESPA and the Brazilian Development Bank (Banco Nacional de Desenvolvimento Econômico e Social/BNDES)
Index Construction	
Index Construction	The constituents of the IBrX-50 index are included in the index, with the weightings of the companies determined by the company's CO ₂ emission. The weight of each stock in the index takes into account: (1) Participation in the IBrX-50, in which the component stocks are free-float; and (2) The carbon intensity of the company—the "Emission/Revenue Coefficient."
Publishes Index Composition	Yes, available on website
Historical Performance	ISE provides performance data, which includes the following statistics: <ul style="list-style-type: none"> • Daily Price • Average Growth Rate • Yearly Variation (R\$/US\$) • Monthly Price • Monthly Volatility • Market Value • Yearly Records
Benchmark Cited	No benchmark cited
Sustainability Approach / Screening Methodology	
Outsourced / In-house ESG Research	Outsourced (some analysis is performed externally using information disclosed to the exchange)
ESG Data Provider	BM&FBOVESPA, with Trucost
Sustainability Framework	Assesses companies based on carbon intensity (tCO ₂ /revenue coefficient)
Sustainability Assessment Methodology	All stocks that are part of the IBrX-50 index are automatically included in the index, unless they do not report a carbon footprint.
ESG Categories	E
ESG Weighting	100% E, with a specific focus on climate change
Publishes Indicator Data	Yes, carbon emissions for included companies are available
Research Methodology	Publicly disclosed CO ₂ emissions, and publicly disclosed financial information
Frequency of Updates	Every 4 months

CSI-ECPI ESG China 40 Index

Summary	
<ul style="list-style-type: none"> • The CSI- ECPI ESG China 40 Index was announced in June 2010, and was launched in September 2010. • The data provider for the index is ECPI. • The ESG rating methodology used by the index is the same as the one for other ECPI indices. • The company that provides the index, The China Securities Index Company, is backed by a joint venture between the Shanghai Stock Exchange (SSE) and the Shenzhen Stock Exchange. 	
General Index Characteristics	
Launch Date	2010
Geographic Markets	China
Ownership Structure	Company: China Securities Index Co. (CSI)
Key Stakeholders in Construction	ECPI, China Securities Index Co.
Index Construction	
Index Construction	All the stocks in the SSE 180 Corporate Governance Index are first rated by ECPI's ESG method. Companies that rank in the top 40 are selected as index constituents. Weight of a constituent is capped at 2.5% by the equal weight factor, and therefore each company in the index is equally weighted.
Publishes Index Composition	Yes, available on website
Historical Performance	Data for the index is available on the CSI website, via charts that provide daily, monthly and yearly data about nominal value of the index, as well as trading volumes and turnover.
Benchmark Cited	No benchmark cited
Sustainability Approach / Screening Methodology	
Outsourced / In-house ESG Research	Outsourced
ESG Data Provider	ECPI
Sustainability Framework	The methodology is based on frameworks from bodies such as the United Nations Global Compact, the Global Reporting Initiative and the United Nation's Principles for Responsible Investment (UN PRI). ECPI states that its methodology "aims to appraise and monitor a company's long term strategic position, operational management and actual behavior towards society, the environment and markets."
Sustainability Assessment Methodology	The ESG Rating uses indicators in the following categories: Environmental strategy and policy, Environmental management, Products, Production process, Community relations, Employees, Markets, and Corporate governance.
ESG Categories	E, S, and G
ESG Weighting	ECPI's ESG rating methodology does not specify the weighting of E, S and G factors in its analysis in public information.
Publishes Indicator Data	No
Research Methodology	Research on companies plus annual and sustainability reports. Information provided by qualified media sources, NGO's statements and also direct contact with investor relations.
Frequency of Updates	Semi-annual

Hang Seng Corporate Sustainability Indexes

Summary	
<ul style="list-style-type: none"> The Hang Seng Corporate Sustainability Index Series includes companies with strong performance on four dimensions: Corporate Governance, Environmental Impact, Social Impact, and Workplace Practices. The Corporate Sustainability Index Series comprises three indexes. The Hang Seng Corporate Sustainability Index and the Hang Seng (China A) Corporate Sustainability Index include Hong Kong-listed companies and Mainland-listed companies respectively, while the Hang Seng (Mainland and HK) Corporate Sustainability Index is a cross-market index that combines the constituents of the other two indices. 	
General Index Characteristics	
Launch Date	2010
Geographic Markets	China
Ownership Structure	Company: Hang Seng Indexes Company Limited
Key Stakeholders in Construction	N/A
Index Construction	
Index Construction	<p>Universe comprises all stocks that have their primary listing on the Main Board of the Stock Exchange of Hong Kong ("SEHK").</p> <p>Based on a sustainability assessment, the 30 highest-scored companies on the Eligibility List of the Hang Seng Corporate Sustainability Index (HSSUS) and 15 highest-scored companies on the Eligibility List of the Hang Seng (China A) Corporate Sustainability Index (HSCASUS) are included in the HSSUS and the HSCASUS respectively.</p> <p>The index uses a free-float adjusted market cap weighted methodology with a 10% cap on each constituent weighting.</p>
Publishes Index Composition	Yes, available on company's website
Historical Performance	Daily performance data available to download from index website.
Benchmark Cited	No benchmark cited
Sustainability Approach / Screening Methodology	
Outsourced / In-house ESG Research	Outsourced
ESG Data Provider	RepuTex
Sustainability Framework	The index evaluates companies on four dimensions: Environmental Impact, Social Impact, Corporate Governance, and Workplace Practices.
Sustainability Assessment Methodology	<p>The Corporate Sustainability Rating Assessment measures the corporate sustainability performance of each eligible company against four core factors: Environmental Impact, Social Impact, Corporate Governance, and Workplace Practices.</p> <p>For each of the four categories underpinning the rating, a company receives a performance score (0-100). Each performance score is a weighted aggregation of criteria level scores (0-10). Scoring takes into account material risks that may require company action.</p> <p>A rating and score is assigned to each assessed eligible company reflecting its corporate sustainability performance.</p>
ESG Categories	E, S, and G
ESG Weighting	Not disclosed publicly
Publishes Indicator Data	Yes, Reputex provides details about its research methodology.
Research Methodology	Reputex uses publicly available information, based on company disclosure and communications, but also analyzes the performance of similar companies to establish a baseline for data to ensure that the company's claims are realistic.
Frequency of Updates	Annual

S&P/EGX ESG Index

Summary	
<ul style="list-style-type: none"> The S&P/EGX ESG Index has been developed in collaboration with the Egyptian Institute of Directors (EIoD), an organization that works under the Egyptian Ministry of Investment to spread awareness and best practices around corporate governance in the region. EIoD conducts the ESG research in the local market, which is then used by S&P to create the ESG screen and index. 	
General Index Characteristics	
Launch Date	2010
Geographic Markets	Egypt
Ownership Structure	Company: S&P
Key Stakeholders in Construction	Egyptian Institute of Directors, Egyptian Corporate Responsibility Center, Egyptian Stock Exchange
Index Construction	
Index Construction	The index is composed of the 30 top ESG performers among the top 100 listed companies in Egypt. The weighting of each company in the index is determined by its ESG score.
Publishes Index Composition	Yes, available on Egyptian Institute of Directors Website
Historical Performance	In its index fact sheet, S&P provides a brief summary of the performance of the index. Index performance chart <ul style="list-style-type: none"> 1 month, 3 month, and YTD returns 1 year and 3 year annualized returns 3 year annualized standard deviations of returns
Benchmark Cited	No benchmark cited
Sustainability Approach / Screening Methodology	
Outsourced / In-house ESG Research	Outsourced
ESG Data Provider	Egyptian Institute of Directors (under guidance of S&P and Crisil)
Sustainability Framework	The Social and Environmental screens are based on principles from Global Reporting Initiative (GRI), Global Compact (GC) and Millennium Development Goal (MDG). Standard & Poor's existing corporate governance methodology has been adapted to suit Egypt's market.
Sustainability Assessment Methodology	The stock selection methodology is identical to the one developed by S&P for its India index.
ESG Categories	E, S, and G
ESG Weighting	Not disclosed publicly
Publishes Indicator Data	No
Research Methodology	Research for the sustainability assessment is conducted using publicly available information, including company reports, and also news reports and other websites. Companies are given credit for their transparency and disclosure practices.
Frequency of Updates	Annual

S&P/Hawkamah ESG Pan Arab Index

Summary	
<ul style="list-style-type: none"> The S&P/Hawkamah ESG Pan Arab Index is similar to the other two S&P emerging market ESG indices, with the one distinction being that it covers a region of 11 countries, as opposed to one specific country market. The index also covers Egypt, which has an ESG index provided by S&P. 	
General Index Characteristics	
Launch Date	2011
Geographic Markets	Middle East and North Africa
Ownership Structure	Company: S&P
Key Stakeholders in Construction	Hawkamah (Institute for Corporate Governance in MENA region), partly funded by IFC
Index Construction	
Index Construction	The underlying universe for the index is composed of the largest (by market cap) 150 companies listed on the exchanges of Bahrain, Egypt, Jordan, Lebanon, Kuwait, Morocco, Oman, Qatar, Saudi Arabia, Tunisia, and the United Arab Emirates, subject to a liquidity screen. The index is comprised of 50 stocks that score the highest on the ESG rating, with maximum individual country representation of 15 stocks.
Publishes Index Composition	No
Historical Performance	In its index fact sheet, S&P provides a brief summary of the performance of the index. <ul style="list-style-type: none"> Index performance chart, with comparison to a benchmark 1 month, 3 month, and YTD returns 1 year and 3 year annualized returns 3 year annualized standard deviations of return 3 year Sharpe Ratio
Benchmark Cited	S&P Pan Arab Composite
Sustainability Approach / Screening Methodology	
Outsourced / In-house ESG Research	Outsourced
ESG Data Provider	Hawkamah
Sustainability Framework	The Social and Environmental screens are based on principles from Global Reporting Initiative (GRI), Global Compact (GC) and Millennium Development Goal (MDG). Standard & Poor's existing corporate governance methodology has been adapted to suit the MENA market.
Sustainability Assessment Methodology	The stock selection methodology is identical to the one developed by S&P for its India index.
ESG Categories	E, S, and G
ESG Weighting	Not disclosed publicly
Publishes Indicator Data	No
Research Methodology	Research for the sustainability assessment is conducted using publicly available information, including company reports, and also news reports and other websites. Companies are given credit for their transparency and disclosure practices.
Frequency of Updates	Annual

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