

2 March 2009

PRI Board statement on financial crisis

Responsible investment is an important part of the response

We are facing the largest financial crisis in a generation. While few predicted the extent, we, as investors, need to accept our share of responsibility, as we are the owners of the financial institutions whose practices led to the crisis, and also investors in the financial products they provided. But investors are, of course, only one group of many that share the responsibility for the crisis. There were failures by regulators, rating agencies and other financial intermediaries, asset consultants, and most importantly, the organizations that constructed the financial products that led to the collapse.

We also need to recognize that investors can, and should, be part of the response to this crisis and that responsible investment has an important role in mitigating future such market failures. There is no doubt that better regulation (both hard and soft) is also necessary, and investors should actively participate in the debates about the type and extent of the required regulatory response. However, regulation alone cannot prescribe well-functioning markets, which are based on high levels of trust, accountability and transparency among market participants. As investors, we must take responsibility for protecting our investments and ensuring our agents act in our best interests.

We believe the Principles for Responsible Investment (PRI) provides a robust framework to assist investors in responding to this crisis.

Principle 1 is about better analysis of risk. It calls for the integration of a broader range of environmental, social and governance (ESG) issues into investment processes. This crisis demonstrated a clear lack of understanding of our underlying investments, and how they may have been putting not only the companies involved at risk, but the entire economy.

Principle 2 calls for active ownership, whereby investors actively monitor companies and ensure that risks are being managed properly through active shareholder engagement and voting. Greater active ownership may have resulted in investors seeing warning signs earlier and being able to mitigate some of the inappropriate practices, including short-term and high-risk investment strategies, opaque investment vehicles, and inappropriate compensation structures. An increase in active ownership will enhance accountability, lessen the need for



one-size-fits-all regulatory responses and ensure that assets are being managed in the best interests of end beneficiaries and customers.

Principle 3 points to investors seeking comprehensive and systematic disclosure of ESG risks and opportunities from investee companies. Lack of transparency was clearly a contributor to the severity of this crisis, and this Principle, if implemented broadly, will enhance investors' understanding of their underlying investments and enable them to address risks earlier.

Principle 4 calls on investors to ensure that their agents also abide by the philosophy behind the PRI. This crisis was, in part, a failure of agents to act in the interests of their principals. Investors need to incentivise their agents to act in their long-term best interests, and this includes ensuring that fund managers have the capability to integrate ESG risks and brokers and other ESG research providers are incentivized to produce research that analyzes these issues in a systematic way.

Principle 5 calls on investors to work together. If we are to address the problems facing the economy, we must have a collaborative approach, particularly around addressing systemic issues and working together with policy makers to ensure an appropriate regulatory response that enhances the goals of the PRI.

Principle 6 is focused on investors' own transparency. Going forward, there will be increasing demands on investors to show they are well governed and indeed part of the solution to this crisis. As investors, we need to be transparent about how we are addressing the crisis, both to our members and to the broader community.

In responding to this crisis, we therefore call on institutional investors to:

- 1) See responsible investment, and the PRI framework, as an important part of the response to the current crisis and a tool to help build the structures to prevent the next one.
- 2) Invest *more* in responsible investment activities. Now is the time to enhance the capacity to research, understand and address ESG issues, in all parts of the investment chain.
- 3) Become signatories to the PRI and join a global network of peers working to address ESG risks and opportunities, both on the company and systemic levels.
- 4) Incentivize – in a concrete way – fund managers, asset consultants, brokers and research providers to ensure that they further enhance their capacity to research, understand and address ESG issues.
- 5) Invest in active ownership capability, monitor investments closely, and engage in dialogue with companies where risks are not being managed appropriately. Ensure shares are being voted in an informed and robust way.
- 6) Engage actively with governments and market authorities at a national and international level to ensure that responsible investment is seen as part of the solution, and any regulation

supports the mechanisms through which investors exercise their responsibility (such as strong shareholder rights and corporate disclosure requirements).

7) Publicly disclose their responsible investment activities, and in particular, the measures being taken to respond to the crisis.

8) Promote the view within the entire investment chain that the long-term value and success of business are inextricably linked to the integration of environmental, social and governance issues into corporate management and operations, and the corporate responsibility will help to restore the trust that is required for markets to function.

In support of this statement, the PRI Initiative will be bringing together leading PRI signatories to develop an action plan for the financial crisis and determine the role that investors can play in the solutions to the current problems.