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What do environmental theme funds bring to SRI?

October 22, 2008 – Paris, France – Novethic publishes today the second edition of its survey on environmental theme funds, including an exhaustive panorama of 194 funds across Europe. The ISR research center of Novethic studied all of their environmental features and has assessed the degree to which they take SRI criteria into account. The main findings are as follows: the number of funds is growing, the themes are becoming more specific (climate, water), and environmental virtues are being reinforced. Conversely, only 29% of the sample of funds that integrates ISR criteria offer investors the guarantee that all issues related to sustainable development will be factored in—that is, over and above the environmental dimension alone.

Highly diversified set of approaches

Novethic analyzed 194 funds, breaking them down into seven categories based on their method of environmental selection: Forestry funds (2%), Renewable Energy funds (9%), Water funds (11%), Environmental Sector funds (14%), Climate Change funds (20%), Sustainable Development Thematic funds (20%) and Multi-approach Environmental funds (24%).

Conversely, the marketing terms used—of the alternative energy or climate type—do not necessarily take into account the environmental investment prism. Nearly two-thirds of all renewable energy funds invest in the water or waste management sectors. Similarly, more than half of all climate change funds can be assimilated into the multi-approach environmental funds category. Only the companies selected for the water funds are generally consistent with respect to their presentation to investors.

Turning in a good performance and also showing a certain degree of maturity, the environmental theme funds increased in number in 2007, and their aggregate assets under management exceeded 25 billion euros at the end of last year. But they did not escape the financial crisis unscathed, losing 24% of their assets between January and September 2008. However, this depreciation does not seem to be related to a massive withdrawal on the part of investors. It is more related to the counter-performances of the constituent businesses.

What role within SRI for environmental funds?

Coinciding with the Novethic survey, a number of players have expressed the desire to substitute RSI (Responsible and Sustainable Investment) for SRI, which entails putting into a single universe environmental theme funds and SRI funds that pick stocks based on ESG (Environmental, Social and Governance) criteria. In analyzing the management processes more specifically, Novethic has concluded that out of the 194 environmental theme funds examined only 29% have developed structured SRI approaches. They are grouped under the term Core SRI Thematic funds, as opposed to Broad SRI, which uses more flexible criteria.

Globally, the development of environmental theme funds has led to genuine innovations. These pertain in particular to those using SRI. One of the most interesting examples is the construction of specific environmental screens, which may target businesses operating in the fossil fuels sector (for renewable energy funds) or the use of agri-chemicals (for funds focused on the environment), or even the exclusion of industries related to overland and air transport (for some funds that focus on climate change).

The approach to stock-picking is also inventive in many cases. For environmental funds, managers adapt their usual SRI practices to the size and the activity of businesses, whose environmental strategy they are examining in greater depth.

In some cases, this can lead to a full-fledged life cycle environmental analysis (from production to products), which may be combined with special topic research to avoid major social problems.

Added value

Environmental theme funds are having an impact on traditional SRI. They are theoretically more attractive to investors because they draw the link between the issues of sustainable development and investment sectors.

Today, we find all sorts of investment vehicles linked to the environment that may integrate large businesses with good environmental management practices and smaller specialists in renewable energy undergoing rapid growth. Even though some make substantial efforts to educate, the developers of these funds, which are often complex, could improve the quality of their communications. It is also important to explain how these funds are in sync with the major issues in sustainable development, including labor law and government.

Environmental theme funds have also fallen victim to the financial crisis, but they should get back on track once the financial markets realize that they are built on solid fundamentals such as population growth, climate change and the exhaustion of natural resource!

To access the survey, click here: http://www.novethic.com/novethic/v3_uk/upload/The_new_frontiers_of_SRI_Green_Investments.pdf

About Novethic:

A subsidiary of Caisse des Dépôts, Novethic is a leading center for research, information and expertise pertaining to SRI (socially responsible investment) and CSR (corporate social and environmental responsibility). Its web site, www.novethic.com, is a comprehensive source of information for responsible economic actors.

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