
THE EMERGENCE OF CSR AND SUSTAINABILITY INDICES

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ABSTRACT

The aim of sustainability performance indices is to provide a benchmark for financial products and to measure the financial performance of companies that lead their industry in terms of sustainability. This paper examines sustainability performance indices on global financial markets and determines the extent of Australian representation within these global indices.

The paper outlines the emergence of nine major market indices designed to track the performance of a variety of listed companies that are seen to have desirable sustainability practices. These indices include: ARESE Sustainable Performance Indices; Dow Jones Sustainability Index; FTSE4Good Indices; Calavert, Domini Social Index; E. Capital Partners Ethical Index; Ethibel Sustainability Index; Humanix Ethical Index; and Jantzi Social Index.

Following a brief description of each of these indices, this paper catalogues each index according to: (a) their launch date; (b) the markets they cover; and (c) their Australian weighting. This section concludes by identifying that Australian listed companies are not well represented among these major indices.

THE EMERGENCE OF SUSTAINABILITY INDICES

In response to an increasing investor appetite for socially responsible and ethical investments (McKinsey & Company, 2000; Greene, 2003), and in an attempt to develop a performance rating for sustainability, a number of stock market indices have emerged on the global financial markets.

These sustainability indices are designed to benchmark the performance of global Socially Responsible Investments (SRI) and to help investors identify listed companies that employ sustainable business practices that incorporate a desire or practice to be socially responsible. These are companies that are focused on not just delivering sound financial performance but are equally focused on delivering performance around a number of sustainability issues.

Table 1 below lists the nine major stock market indices designed to track the performance of listed companies that are seen to have desirable sustainability practices.

The nine major sustainability indices mentioned above are briefly described in the following section.

Table 1: Australian weightings of major sustainability indices

| Index | Launched | Markets Covered | Australian Weighting |
|---------------------------------------|----------|-----------------|----------------------|
| ARESE Sustainable Performance Indices | 2001 | Europe | - |
| Dow Jones Sustainability Index | 1999 | Global | 2.63% |
| FTSE4Good Indices | 2001 | Global | 1.46% |
| Calavert | 2000 | USA | - |
| Domini Social Index | 1990 | USA | - |

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|-----------------------------------|------|--------|-------|
| E. Capital Partners Ethical Index | 2000 | Global | 1.60% |
| Ethibel Sustainability Index | 2002 | Global | 1.62% |
| Humanix Ethical Index | 2001 | Global | 1.56% |
| Jantzi Social Index | 2000 | Canada | - |

ARESE SUSTAINABLE PERFORMANCE INDICES (ASPI)

The ARESE Sustainable Performance Indices (ASPI) was launched in July 2001 and tracks the financial performance of leading sustainability companies across Europe. The ASPI indices inclusion criteria has four main themes: (1) triple bottom line perspective; (2) positive screening approach; (3) risk management; and (4) a stakeholder-centered approach. The ASPI does not include any Australian companies within its composite.

DOW JONES SUSTAINABILITY INDEX

Launched in September 1999, the Dow Jones Sustainability Indices (DJSI) was the first global indices tracking the financial performance of leading sustainability-driven companies worldwide. The DJSI is constructed with a selection criteria comprising the following six elements: (1) strategy; (2) financial; (3) customer and product; (4) governance and stakeholder; (5) human; and (6) process. Of the 316 companies included in the DJSI World Index, 16 are Australian companies, which represent a total of 2.63% of the total index market capitalisation.

FTSE4GOOD INDICES

The FTSE4Good Indices measure the performance of socially responsible companies around the world. Launched in July 2001, the selection criteria cover environmental sustainability, stakeholder relationships and universal human rights. Of the 627 companies that comprise the FTSE4Good Global Index, 17 companies are Australian and together they represent only 1.46% of the indices weighting.

CALAVERT SOCIAL INDEX

Launched in April 2000, the Calvert Social Index measures the performance of US-based socially responsible companies included in the 1,000 largest companies (listed stocks on the NYSE and Nasdaq-AMEX) in the US. Companies included in the Calvert index meet the selection criteria comprising environment, workplace issues, product safety and impact, community relations and investments, military weapons contracting, international operations and human rights, and indigenous peoples' rights. The Calvert does not include any Australian companies within its composite.

DOMINI SOCIAL INDEX

The Domini Social Index is a socially and environmentally screened index consisting of primarily large-cap US companies and is the oldest US socially responsible index and was launched in 1990. The Domini Social Index excludes companies with significant revenues from alcohol, tobacco, gambling, nuclear power and weapons contracting. It includes companies with positive

records in community involvement, the environment, employee relations and hiring practices. The Domini Social Index does not include any Australian companies within its composite.

E. CAPITAL PARTNERS ETHICAL INDEX

The E. Capital Partners Ethical Index was launched in January 2000 and is a global index combining traditional financial approaches with social and environmental criteria. The general guiding principle of the index penalises those companies that operate in sectors E.Capital assesses as being injurious to the rights and dignity of humanity. Primarily, armaments, nuclear, alcohol, tobacco and gambling, and pornography. The E.Capital includes only 1.60% of its weighting in Australian companies.

ETHIBEL SUSTAINABILITY INDEX

The Ethibel Sustainability Index commenced in June 2002 and is a global index that focuses on sustainable development and stakeholder involvement. Ethibel comprises companies that have been screened on the following core themes: internal social policy, environmental policy, external policy and economic-ethical policy. The Ethibel includes only 1.62% of its weighting in Australian companies.

HUMANIX ETHICAL INDEX

The Humanix Ethical Index was established in January 2001 and is a globally focused index. Humanix comprises companies that have passed the Humanix ethical screening process and are approved by the Humanix Ethical Council for inclusion in the index. Humanix includes only companies whose activities are not related to significant environmental risks, respect human rights, and where 97% or more of the total turnover is not derived from production and/or marketing of arms or the production of alcoholic beverages. The Humanix Ethical Index includes only 1.56% of its weighting in Australian companies.

JANTZI SOCIAL INDEX

The Jantzi Social Index (JSI) is a socially screened index containing Canadian companies that pass a set of broadly based social and environmental criteria. The index was launched in January 2000. The JSI does not include companies that have significant involvement in the production of nuclear power, the manufacture of tobacco products or weapons-related contracting. The JSI also avoids companies that have a consistently poor relationship with aboriginal communities; undertake questionable or fraudulent business practices; have a consistently poor employee relations record; have a consistently poor environmental performance record compared with industry counterparts; have experienced significant problems at their operations outside of Canada, or have operations in, or links with, Burma; or manufacture unsafe products. The JSI does not include any Australian companies within its composite.

SUMMARY OF SUSTAINABILITY INDICES

Sustainability indices first emerged on a global basis in 1999 with the Dow Jones Sustainability Index (DJSI). While the methodologies used to compile the indices differ between each index, the focus of the selection models are similar in that they screen companies based on factors such as their corporate governance, workplace practices, social impact and environmental performance.

These indices have an important role in helping to facilitate SRI and to benchmark SRI performance (McKinsey & Company, 2000). The out-performance of these indices (and the individual companies that together constitute the indices) relative to global stock market indices has also been used as evidence to support a growing argument that practicing sustainability increases the value of the firm (Bauer *et al.*, 2003; Brown & Caylor, 2004, Gompers *et al.*, 2003; Hamid & Sandford, 2002; Harrison & Freeman, 1999; Pava & Krausz, 1996; Roman *et al.*, 1999; Waddock & Groves, 1997).

Of the nine major sustainability indices, only the Dow Jones Sustainability Index (DJSI) uses a comprehensive approach to CSR and rates its constituent companies using the four key elements of CSR: (1) environmental impact; (2) corporate governance; (3) social impact; and (4) workplace practices.

CONCLUSION

Of the nine major sustainability indices, only five have a global reach and of these five, only a few Australian companies are represented. The absence of stronger Australian representation across the indices and the absence of a comparable index on the Australian bourse indicate the relative immaturity of sustainability disclosure by Australian companies. This finding is consistent with a recent Federal Government study which examines corporate sustainability from the perspective of investors and concluded, “companies are not articulating their sustainability behaviours as well as they might” (Mays, 2003, p.6).

This lax behavior regarding sustainability disclosure by the majority of Australian listed companies is likely to change with the pressure coming from: (a) an increase in Australian SRI investment; (b) new legislation targeting disclosure; and (c) the introduction of an Australian ratings agency focused on this rating typology.

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