"For just as the body is one and has many members, and all the members of the body, though many, are one body, so it is with Christ."

"If one member suffers, all suffer together with it; if one member is honoured, all rejoice together with it."

1 Cor 12.12 & 16

THE CHURCH OF ENGLAND

Ethical Investment Advisory Group

Annual Review 2012/13

GS Misc 1047

Chair's Letter

It is now more than five years since the onset of the financial crisis in 2007. In the UK and the rest of Europe the vital signs of the economy are weak. We can be thankful that we remain one of the world's wealthiest and safest nations. However, our government is still over-indebted and struggling with a huge budget deficit, our economy is sluggish, and many in our communities are suffering as a result of unemployment or reduced real wages and benefits. Our pre-crisis economic model did not live up to its promises.

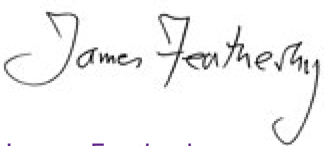
I have argued for some time that the crisis represents a once in a lifetime opportunity to examine our financial system, and to change the way we think about it so that it can better serve the real economy - remembering that the real economy is just a term of art used to describe the economic welfare of all of us.

There are signs that thinking and policy are changing, even if the changes are as yet modest. The Kay Review, commissioned by the Department for Business Innovation and Skills, has shone a light on the way in which institutional investors can unfortunately encourage companies to pursue a short-term approach. The Financial Reporting Council's Stewardship Code has highlighted the importance of investors taking responsibility for the health of the companies they own. A UN initiative, the Principles for Responsible Investment, continues to make a powerful case for the integration of environmental, social and governance factors into investors' decision-making.

Institutional investors do not always find scrutiny of this kind easy. Sometimes they prefer to keep their focus on the immediate job of simply generating financial returns for beneficiaries.

However, it is becoming clear that where historic assumptions and practices stand in the way of good principles, it is not the good principles that should give way. We are learning that aligning good investment practice with the long-term health of economies and societies is in the collective best interests of beneficiaries because everything is connected. Such an alignment creates the possibility not only of more sustainable financial returns but also of a better quality of life for beneficiaries. As we note on the cover, we are one body – and the EIAG's work in detecting and addressing unhealthy economic practice is one way to prevent people suffering.

This is a vital and exciting moment for reflection on the ethical conduct of investment. The EIAG is fortunate to have a new Archbishop of Canterbury for whom issues of financial ethics are as much a priority as they were for his predecessor. We are grateful also for the strong support of the Church of England National Investing Bodies who have committed extra resources to the EIAG in the past year for both the generation of advice and support for its implementation. This review details our activities on both counts.



James Featherby
Chair, Ethical Investment Advisory Group

Barclays

In June 2012 it was announced that Barclays Bank had been fined approximately £290m for seeking to manipulate Libor, the London inter-bank lending rate, which underpins trillions of pounds of loans and financial contracts.

This was the latest in a series of scandals associated with the bank, which, like many of its peers, had lost sight of its fundamental role in society and its wider obligations.

We have engaged intensively with Barclays since last June, including at Board level. We have been encouraged by the determination of the bank's new leadership to turn a corner and to foster a more ethical culture.

However, ethical conduct cannot simply be enforced. We will know that Barclays has truly transformed when it inspires its staff to make sustainable profits through serving its customers and fulfilling its fundamental role in society.

We were delighted that the new Chief Executive of Barclays, Antony Jenkins, shared a platform at St Paul's Cathedral on 12 June with the Archbishop of Canterbury to discuss 'Good Banks'.

EIAG lunchtime Synod fringe, Monday 8 July 2013

General Synod is a touchstone for the EIAG for views in the Church of England on ethical investment. We seek active dialogue with Synod members and hold a fringe meeting at every York Synod. This year's takes place at 1pm on Monday 8 July in Room T006 in the Exhibition Centre. Synod members are warmly invited to attend.

Engagement

Between April 2012 and March 2013 the EIAG and its staff conducted engagement with 50 companies in face-to-face meetings or by video- or tele-conference.

These companies (some of whom the National Investing Bodies do not invest in, but whom we are assessing, for example under our new alcohol policy) comprised:

Aberdeen Asset Management, Aggreko, Anglo American, Arcadis, Astrazeneca (twice), Barclays (six times), Bellway, BP (three times), Chevron Corporation, Cookson Group, Diageo, Dunelm Group, ENEL (twice), ENRC, Essar Energy, G4S, General Electric Company, Glaxosmithkline, Glencore International (twice), Hargreaves Lansdown, J D Wetherspoon, Kazakhmys, Lloyds Banking Group, Lonmin, Moneysupermarket.com Group, News Corporation, Omron Corporation, Petropavlovsk, Philips, Randgold Resources, Rio Tinto, Royal Bank of Scotland Group (twice), Royal Dutch Shell (twice), SABMiller, Sainsbury's (three times), Smiths Group, Societe Generale (twice), Sompo Japan Insurance, Sony Corporation, Tate & Lyle, Taylor Wimpey, Tesco (twice), Tullow Oil, Unibail-Rodamco, Vedanta Resources (three times), Veolia Environnement, Whitbread, WM Morrison Supermarkets, WPP, Xstrata.

Themes covered in our engagement meetings included: access to medicines in developing countries, arctic drilling, banking ethics and practice, carbon emissions management and reporting, corporate governance, country-specific risks, defence sales, executive remuneration, the Groceries Code Adjudicator Bill, human rights, labour relations, oil sands, pharmaceutical ethics, relationships with communities, responsibility in the marketing and retailing of alcohol, safety/operational risk, and sustainable housing.

Responsible alcohol marketing and retailing will again be the biggest single engagement theme in 2013/14 as we continue to work on the implementation of the alcohol policy recommended by the EIAG and agreed by the National Investing Bodies in 2011. We are already seeing some indications of the kind of progress we hope to see, such as supermarkets de-listing high strength white cider.

Good progress was made with Veolia Environnement, with whom the EIAG has been engaging since 2009 about its settlement-related business activities in the Occupied Palestinian Territories. The company is in the process of withdrawing from the activities about which we have expressed concern and has confirmed to us that it does not intend to pursue new settlement-related business activities.

The EIAG's intensive engagement with News Corporation did not produce the corporate governance improvements we had sought. In August 2012 the Church Commissioners and the Church of England Pensions Board announced that they had sold their shares in the company on the advice of the EIAG. The CBF Church of England Funds did not hold News Corporation shares.

We continue to track progress at Vedanta Resources following the divestment advice from the EIAG. In April the Indian Supreme Court ruled that the decision on whether Vedanta's plans for a bauxite mine in the Niyamgiri hills of Orissa should go ahead should rest with the local indigenous communities. Given the concerns we expressed about the lack of respect for the rights of local communities at this refinery and mining project, this is welcome news indeed.

High interest rate lending

In 2011 the National Investing Bodies adopted a policy on high interest rate lending on the advice of the EIAG. We have continued to voice our concerns about exploitative lending, including at an event at St Paul's Cathedral in April 2012 co-organised by the St Paul's Institute and CCLA. We are encouraged that regulators and parliament are at last recognising the misery that can be caused by high interest rate lending. A cap on lending charges is due to be introduced under the Financial Services Act 2012.

Voting

The 2012 AGM voting season in the UK was dubbed the 'Shareholder Spring' because of some unusually high votes against company management. The most dramatic event was the resignation of a FTSE 100 Chief Executive – at insurer Aviva – after shareholders voted against his remuneration package.

Image: ©Tatiana Popova / iStockphoto

The corporate governance policy recommended by the EIAG and operated by the three National Investing Bodies has long flagged problems with executive remuneration practice in the UK. Indeed the National Investing Bodies signalled their concerns in advance of the Shareholder Spring in letters to the Daily Telegraph co-signed by church and charity investors, pension funds and asset managers with more than £1,500 billion of investments.

None of the National Investing Bodies supported more than one third of the UK company remuneration reports on which they voted in 2012-13. Fuller information about the voting of the Church Commissioners and Church of England Pensions Board is disclosed in the bodies' annual reports. The voting of the CBF Church of England funds is published in full on CCLA's website.

Executive remuneration

In 2012/13 the EIAG and National Investing Bodies worked together to produce a detailed policy paper on executive remuneration, and published it in April 2013.

Building on our long-standing approach, the policy articulates key principles for executive remuneration:

- Executive directors in receipt of competitive salaries should not be awarded annual bonuses of more than 100% of base salary unless they have delivered extraordinary results
- Remuneration schemes should primarily reward long-term performance rather than short-term performance, with long-term performance assessed over five to seven years
- Companies should reward performance not just on financial issues but also performance on the ethical, social and environmental issues which drive durable value creation
- Companies should approach remuneration and reward in a holistic way for all staff and should disclose the way in which they monitor and manage internal pay differentials and trends

The voting, engagement and advocacy activities of the EIAG and the National Investing Bodies on executive remuneration are now all guided by this policy.

Policy advice

In February 2013 the EIAG published an updated and more detailed policy on genetically modified organisms following its adoption by the National Investing Bodies. The policy sets out an ethical investment approach to genetic modification in equity, agricultural land and timberland investments.

The EIAG has been reflecting on good practice in corporate taxation. Work is underway on a policy on business and engagement.

The EIAG has decided that its major piece of policy work in 2013/14 will be the development of updated and more detailed advice for the National Investing Bodies on climate change. Climate change is one of the defining challenges of our age. In a comprehensive look at the issue we shall be asking ourselves what an ethical response to the climate change problem might look like for a Christian institutional investor. This will build on our recent work on climate change, including discussions on the role of investors with the Executive Secretary of the UN Framework Convention on Climate Change, Christiana Figueres.

The policy review will be aligned well with one of the EIAG's most important engagement efforts in 2013/14 – its participation in a collaborative project led by CCLA to encourage UK-listed carbon-intensive companies to achieve the highest Carbon Disclosure Project rating for their emissions management.

The EIAG also plans to consider in 2013/14 whether its policy advice on human embryonic stem cell research should be refreshed.

Al Gore on sustainable capitalism at St Paul's Cathedral

The EIAG worked with the Church Investors Group and St Paul's Institute to organise a major event during National Ethical Investment Week in October 2012 – a speech on sustainable capitalism at St Paul's Cathedral by former US Vice-President Al Gore.

Al Gore called on investors to 'lift their heads from their Bloomberg screens', to consider where our financial and economic system is inevitably taking us, and to start to invest in a way that serves the needs of the planet and its people. An account of Vice-President Gore's remarks is published on the St Paul's Institute website.

Image: © Andrew Adams for the Church Investors Group

Partnerships

Signatory of:

The EIAG believes that excellence and impact in its work are best served through working in partnership with church investors in the UK and internationally, and with the wider responsible and sustainable investment community.

The EIAG and National Investing Bodies participate actively in the work of the Church Investors Group (CIG), and the EIAG Secretary sits on the CIG Steering Group. The CIG is continuing successfully to deepen collaboration between church investors in the UK, and between UK and international church investors, including in the US. It is organising its first two-day conference for UK and international church investors in London in June 2013.

As an extension of its role as the CIG Secretariat, CCLA undertakes engagement with a quarter of the companies in the FTSE350 about their relatively poor response to the Carbon Disclosure Project or lower quartile FTSE Environmental, Social and Governance (ESG) Ratings. These programmes are being academically assessed over the 2013-15 period, and the pilot showed a 50% improvement in company performance relative to 13% improvement within a group of companies that were not contacted by the CIG.

The EIAG Chair is a regular speaker at ethical and responsible investment events and has spoken in 2012/13 at events organised by the Christian Association of Business Executives, Tomorrow's Company and Good Deals (the UK social investment conference).

The Deputy Chair has spoken on ethical investment issues at seminaries in the wider Anglican Communion.

The EIAG Secretary is active in the hedge funds work stream of the UN Principles for Responsible Investment (PRI), sits on the policy group of the European Institutional Investors Group on Climate Change (IIGCC) and is a member of the Leadership Committee of UK Sustainable Investment and Finance (UKSIF).

The EIAG Corporate Governance and Engagement Specialist is a member of the International Corporate Governance Network (ICGN) and a regular participant in corporate governance engagements organised by the National Association of Pension Funds (NAPF).

Feedback

We welcome feedback on this annual review as well as queries from within the Church about ethical investment. Please contact eiag@churchofengland.org.

The Ethical Investment Advisory Group of the Church of England provides ethical investment advice to:

The Church Commissioners for England who support the Church's ministry, particularly in areas of need and opportunity, and meet historic pension liabilities. They are represented on the EIAG by Gavin Oldham (non-executive member), the Rev Professor Richard Burridge (non-executive member and Deputy Chair), Andrew Brown (Secretary of the Church Commissioners), Tom Joy (Director of Investments) and Joseph Cannon (Chief Surveyor).

CCLA for the Church of England

The CBF Church of England Funds collective investment schemes managed by CCLA Investment Management Ltd in which Church of England parishes, dioceses, schools and church charitable trusts invest. CCLA is owned by its church and not-for-profit clients. The CBF Funds are represented on the EIAG by trustee director, the Rev Canon Edward Carter (non-executive member), and Michael Quicke (Chief Executive of CCLA).

The Church of England Pensions Board which provides retirement services (pensions and housing) set by the Church of England for those who have served or worked for the Church. The Board is represented on the EIAG by Pensions Board trustee Ian Clark (non-executive member) and Bernadette Kenny (Pensions Board Chief Executive).

The EIAG has representatives from other parts of the Church to provide broader expertise and insight.

The General Synod is represented by Jenny Humphreys (non-executive member).

The Mission and Public Affairs Council is represented by the Rt Rev Dr Lee Rayfield, Bishop of Swindon (non-executive member), and the Rev Dr Malcolm Brown (Director Mission and Public Affairs).

The Archbishops' Council is represented by Paul Boyd-Lee (non-executive member).

The Communications Office is represented by the Rev Arun Arora.

The EIAG has three further non-executive members. There are two co-opted non-executive members: Richard Harvey, Chairman of PZ Cussons Plc, and Elizabeth Haigh, portfolio manager at, and founder of, Rathbone Greenbank Investments. The EIAG has an independent non-executive Chair, James Featherby, a former partner of over 20 years' standing at Slaughter and May.

Only non-executive members of the EIAG may vote at EIAG meetings.

The executive Secretary to the EIAG is Edward Mason and the Corporate Governance and Engagement Specialist is Chris Anker. They can be contacted at:

e-mail:
eiag@churchofengland.org

telephone:
020 7898 1757

mail:
Investment Department,
Church House,
Great Smith Street,
London SW1P 3AZ.

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The EIAG makes recommendations on ethical investment policy. The legal responsibility for managing the Church's investments rests with the investing bodies. These bodies all have a moral and legal responsibility (known as 'fiduciary duty') to further the interests of their beneficiaries. While mindful at all times of beneficiaries' need for financial returns, the investing bodies seek to align their investment policies with the ethics of the Church by acting on the recommendations of the EIAG.

The EIAG positively recommends investment in companies with responsible employment practices, best corporate governance practice, conscientiousness with regard to human rights, sustainable environmental practice and sensitivity towards the communities in which the business operates.

The EIAG recommends against investment in any company involved in indiscriminate weaponry. It recommends against investment in companies involved in conventional weapons if their strategic military supplies exceed 10% of turnover.

The EIAG recommends against investment in any company that derives more than 3% of revenues from the production or distribution of pornography and against investment in any company, a major part of whose business activity or focus (defined as more than 25% of group revenues) is tobacco, gambling, alcoholic drinks, high interest rate lending or human embryonic cloning.

www.churchofengland.org/about-us/structure/eiag

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