

# **Corruption & Shareholder Value: *Why Should Investors Care?***

**Karina A. Litvack**  
**Director, Research**  
**Governance & Socially Responsible Investment**  
**Friends Ivory & Sime Plc**

**10th International Anti-Corruption Conference**  
**Prague - 9 October 2001**



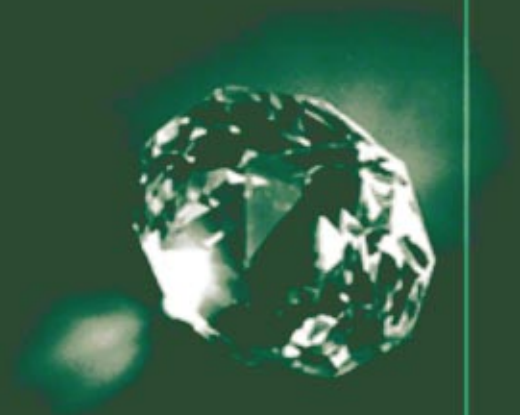
# Corruption & Shareholder Value

- Who is Friends Ivory & Sime?
- A 'Quiet Revolution' in the City
- Does Corruption Affect Shareholder Value?
- What Do Investors Want?
- Next Steps



# Friends Ivory & Sime

- □ 60 billion under management\*
- Socially Responsible Investment:
  - 1984: first SRI fund in Europe
  - 1984-2001: SRI goes global and institutional
  - 2000: Responsible Engagement Overlay®



\* 12/31/00

*Groupwide commitment to Engagement*



# The City: A Quiet Revolution

- *New Drivers of Change*
- Pensions Disclosure Regulation
- Turnbull Report
- ABI Guidelines



# Pensions Disclosure Laws

- UK Pensions Act
- France: Loi sur l'épargne salariale
- Germany: Riester Renten
- EC: CSR Green Paper



*79% of UK Pensions Funds say: I do*

# The Turnbull Committee

- Governance movement
- Risk Management
  - Environment
  - Health & Safety
  - Reputation
  - ***Business Probity***
- Materiality & Systems



***CSR Issues Embedded in Risk Management***

# ABI Guidelines on CSR Issues

- Association of British Insurers:
  - £1.1 trillion assets under management
  - £600 billion global equities
- Risk Management Focus:
  - Assess, Mitigate, Monitor & Review
- Board Oversight and Accountability



*Coming soon: Launch October 2001*

# What Are Investors Doing?





# The FIS Approach

- From avoidance to *Engagement*
- *Financial materiality* of CSR issues
- Governance & Risk Management *Systems*
- *Collaboration*:
  - Academics, Industry groups, selected NGOs
  - Fellow investors



*Understanding Best Practice*

# Corruption and Shareholder Value

- Are the risks posed by corruption *material* to shareholder value?
- What does corruption cost investors?
- What do investors expect of companies?



# Corruption and Shareholder Value

- Will profits suffer if action is taken?
- Are investors policemen?
- How can investors measure effectiveness of anti-corruption systems?



*Is Change Possible...?*

# Is Corruption a Material Risk?

- It's "just a cost of doing business"
- Poor governance = Risk premium
  - up to 20% discount
- Top down vs bottom up valuation
  - Not a deal-breaker...
  - but an indicator of management quality



*All Companies are Not Equal*

# Is Corruption a Material Risk?

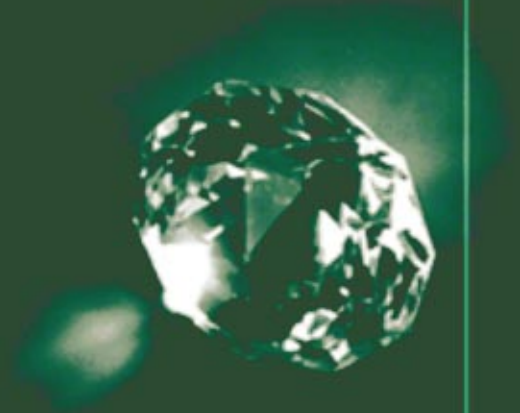
- *Risk calculus is changing*
- Risks are probably underestimated:
  - OECD Convention
  - Public opprobrium/reputation
  - Joint venture/subcontractor standards



*Superior risk analysis = profit opportunity*

# What Does Corruption Cost?

- Bribes paid: Our dividends



- Bribes received: Bad business decisions

*Obvious and hidden costs*

# What Does Corruption Cost?

- Raises costs of basic services
- Undermines ALL business activities
  - staff incentive systems
  - procurement standards
  - product quality
  - safety
  - reputation



*Obvious and hidden costs*

# What Do We Expect of Companies?

- Systems for:
  - Training
  - Performance measurement
  - Audit
  - Whistleblower protection...
- Transparency and openness
- 'Values culture' vs Compliance



# How Do We Measure Performance?

- Understand Best Practice
  - Dialogue
- Policy statements vs practical evidence
- Public commitment
- Better tools are needed



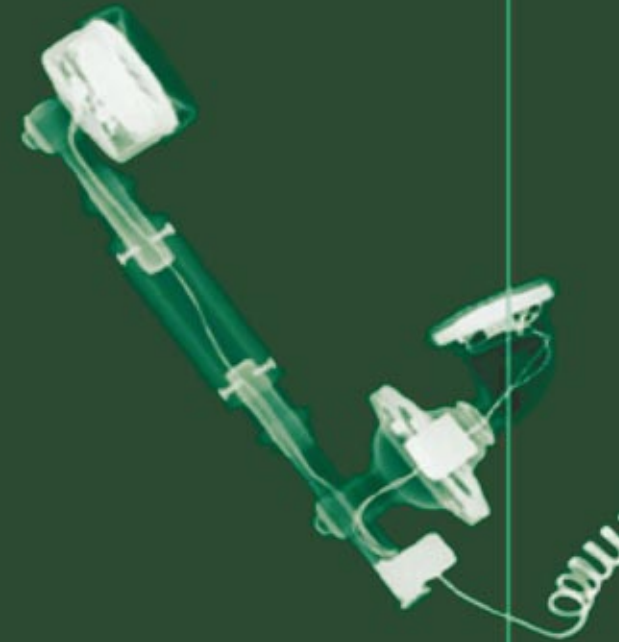
# Taking action: Will profits suffer...?

- The hero in the un-level playing field
- Are investors policemen?
- Multilateral approach
- Investors play their part



# What Next For Investors?

- Help develop effective management and reporting tools
- Promote their adoption
- Set high performance standards



# FIS Approach

- FIS Benchmarking Study
- Support of specialist efforts
- Dialogue
- Collaboration with other shareholders

