

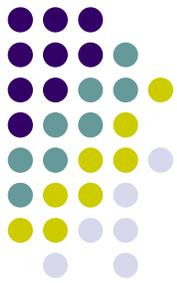
An Elephant on Wall Street

A Case Study in Successful Public-Private Sector Dialogue on Corporate Performance

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US EPA
Office of International Affairs

Meeting the Future: A Research Agenda for Sustainability

Ronald Reagan Building and International Trade Center
Washington DC
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“In times of great change, the learners inherit the earth, while the learned find themselves beautifully equipped to deal with a world that no longer exists.”

Eric Hoffer.

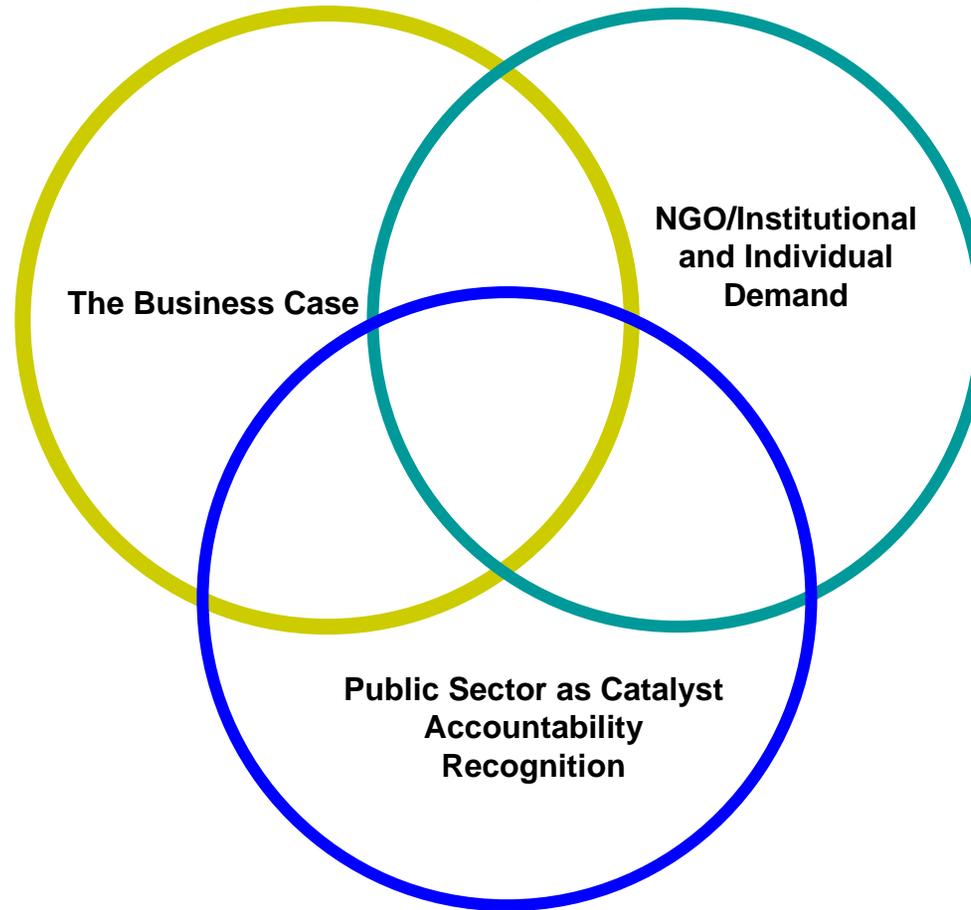


Today

- Drivers of Corporate Sustainability
- Wall Street and *The Elephant in the Room*
- Energy Star/Wall Street Engagement
- Lessons Learned



There are three major forces driving increased investment in strategic corporate sustainability.



The first major driver of corporate sustainable is the financial business case.



The Business Case



Project

Project-specific IRRs

Quantifiable productivity gains

Demand for “Green” design

Direct cost savings effects on bottom line: sustainable practices often increase cash flows, GM, NM, EPS, and SP

Organization

Enhanced reputation gains (DJSI, others)

Increased shareholder value (Innovest);

Reduced investment risk (lower beta)

The second major driver is institutional and individual demand for greater corporate social responsibility and accountability.



A Few Examples

Investor Network on Climate Risk (INCR)

Coalition on Environmentally Responsible Economies (CERES)

Global Reporting Initiative (GRI)

Business for Social Responsibility (BSR)

Global Environmental Management Initiative (GEMI)

The Pew Center

The Conference Board

The Business Roundtable

Investor Responsibility Research Center

Pew Center

World Business Council on Sustainable Development (WBCSD)

**NGO/Institutional
and Individual
Demand**



The third major driver is public sector recognition for long-term investment in corporate sustainability.



Over 150 Federal voluntary programs on corporate sustainability and 'beyond compliance.'

Sarbanes-Oxley

Awards and Recognition

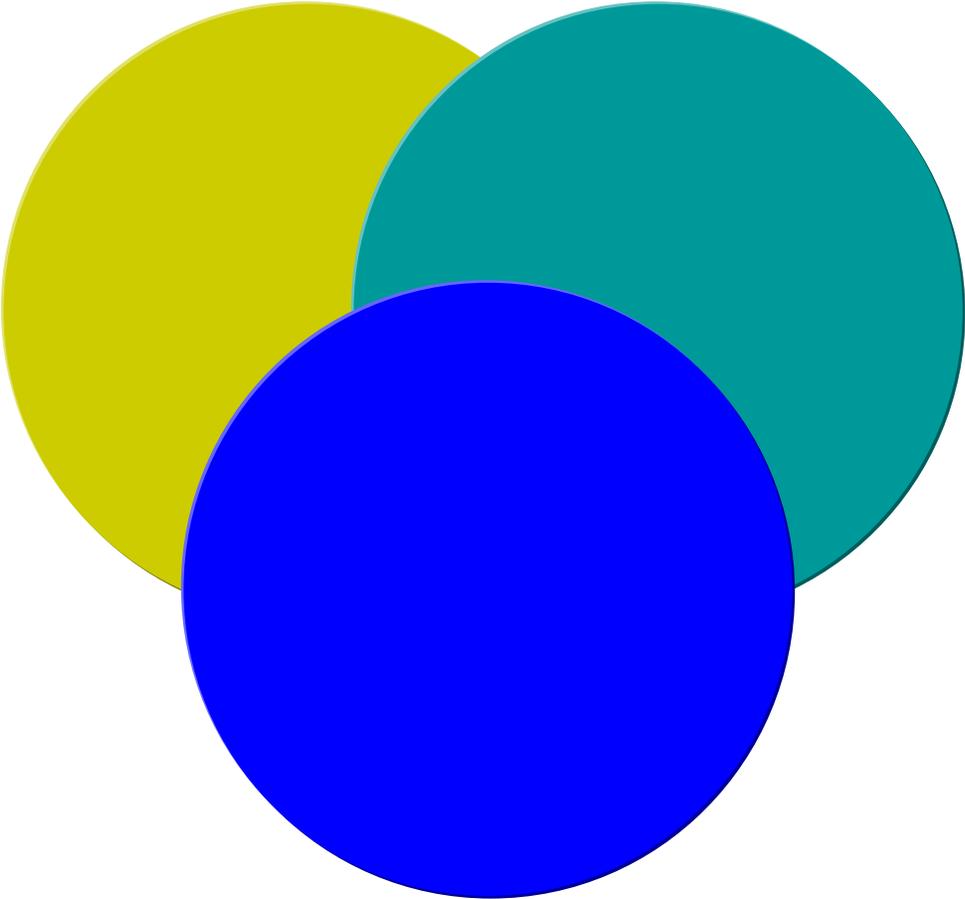
States?

Municipalities?

**Public Sector as Catalyst
Accountability Recognition**



I don't know about you. But, I hear a wake-up call for wholesale corporate re-engineering on sustainability.



**So, is there an elephant in the room?
If so, who let it in?**



**Yes.
And, we did.**





***“Whoever Controls the Language
Controls the Debate.”***



To get top management support on environmental issues, speak to them about what they care about.



- Shareholder value
- Competitive strategy
- Risk
- Corporate governance
- Reputation
- Long-term profitability/shareholder value

What we sought to accomplish on Wall Street?



- Encourage institutional investors to consider corporate energy performance and look for ENERGY STAR® in order to drive more participation.
- Encourage Investor Relations (IR) professionals at ENERGY STAR® Partners to communicate energy performance to financial constituents.

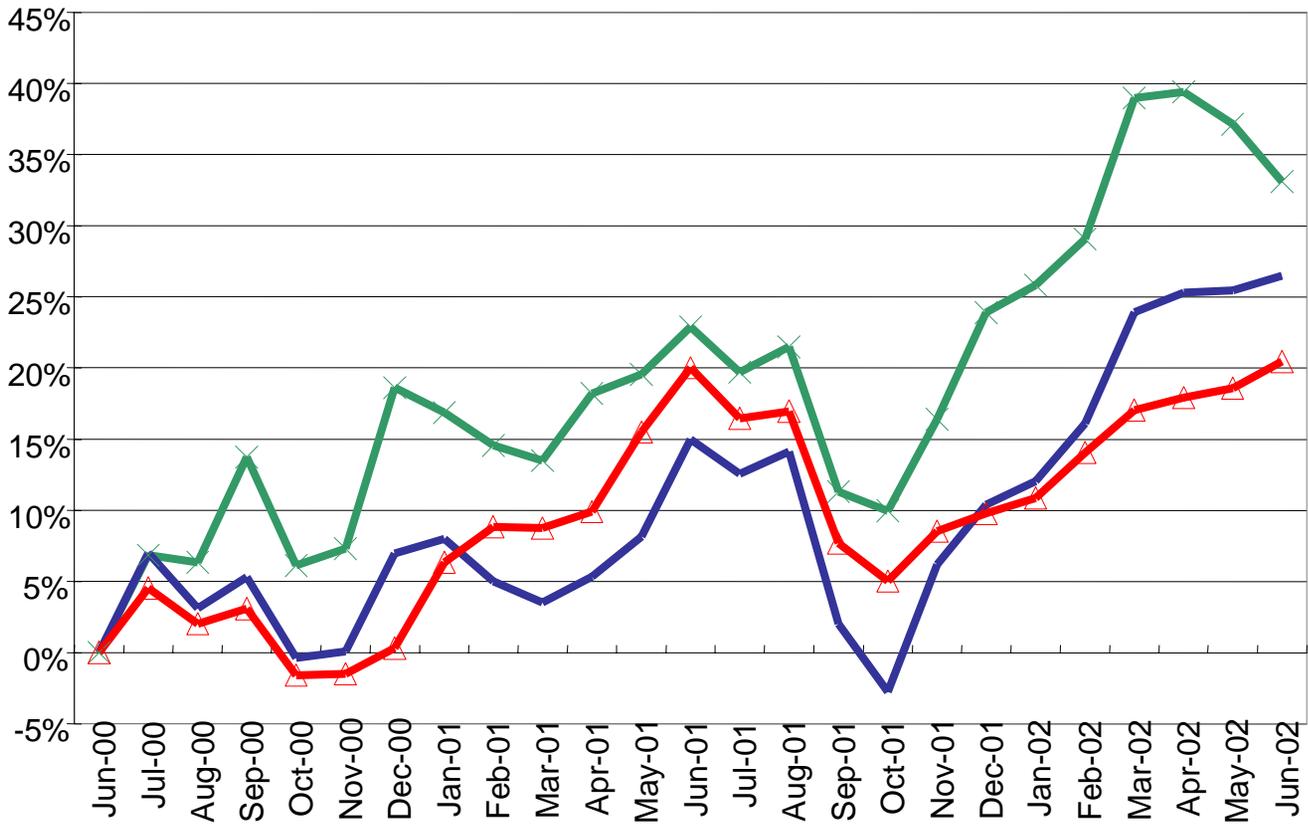
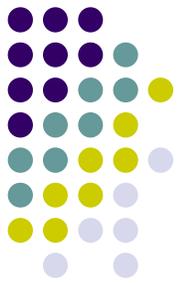
Our priorities were simple.



- Develop models to evaluate corporate energy performance.
- Analyze correlation between ENERGY STAR®, energy performance, and financial performance.
- Develop methods for comparing companies on corporate energy performance.
- Communicate these comparisons to Wall Street as a form of recognition for good performers.

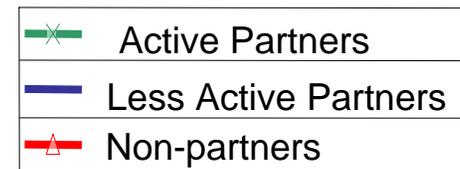


In REITs, we found a 3200 basis-point difference.

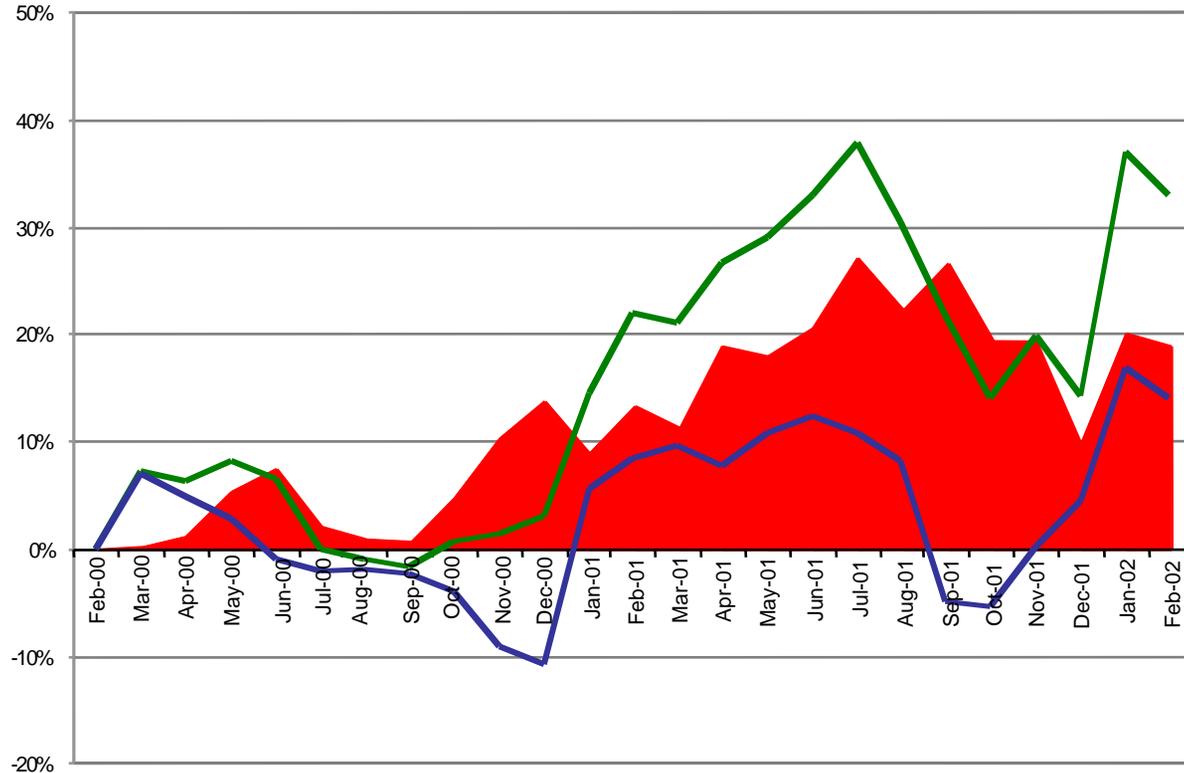
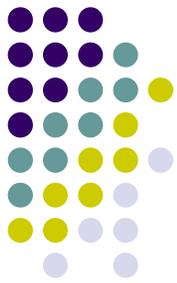


The Study

- Real estate sector
- Over 2 years
- 36 companies
- 1,200 basis pts diff

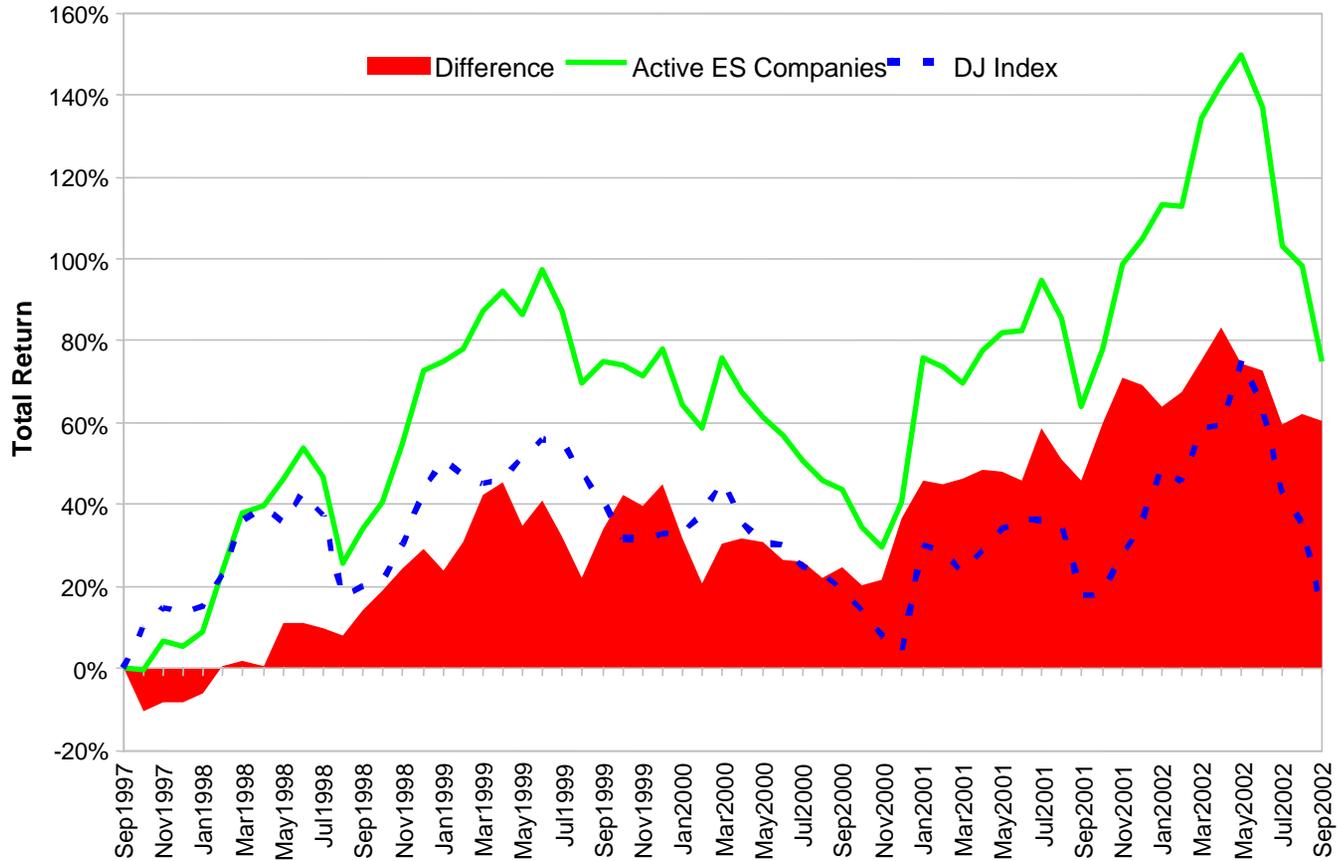


In food retail, we found a 2000 basis-point difference.



	Feb-00	Mar-00	Apr-00	May-00	Jun-00	Jul-00	Aug-00	Sep-00	Oct-00	Nov-00	Dec-00	Jan-01	Feb-01	Mar-01	Apr-01	May-01	Jun-01	Jul-01	Aug-01	Sep-01	Oct-01	Nov-01	Dec-01	Jan-02	Feb-02
■ Difference	0.0%	0.3%	1.2%	5.4%	7.5%	2.1%	0.9%	0.7%	4.7%	10.4	13.8	90%	13.5	11.4	19.0	18.1	20.6	27.2	22.3	26.8	19.4	19.5	9.9%	20.2	18.9
— Retail ENERGY STAR Partners	0.0%	7.2%	6.2%	8.2%	6.5%	0.0%	-0.9%	-1.8%	0.7%	1.3%	3.1%	14.5	21.9	21.0	26.7	28.9	33.0	38.0	30.4	21.8	14.0	19.8	14.3	37.0	32.9
— DJ BroadLine Retail Index	0.0%	6.9%	5.0%	2.7%	-1.0%	-2.1%	-1.8%	-2.5%	-4.1%	-9.1%	-10.7	5.5%	8.4%	9.6%	7.8%	10.8	12.5	10.8	8.1%	-5.0%	-5.4%	0.3%	4.4%	16.8	14.0

And, in merchandise retail, we found a 6000 basis-point difference.



*Operations & sales promotion

Innovest Strategic Value Advisors, 2003

So, what to do with this information?!



The plan.

- Build an alliances with SRI and mainstream financial community.
- Provide an energy performance data infrastructure by working with independent financial information providers.
- Produce and distribute metrics that convey energy and financial performance.
- Populate metrics with actual energy performance information.
- Use these as one way to recognize leaders.



What was the premise behind the development of ratios?



- Public companies react strongly to Wall Street signals.
- Provide a basket of metrics/ratios that financial analysts use to assess:
 - Overall energy performance relative to its peers.
 - Risk associated with high energy expenditures/\$ relative to its peers.
- Mainstream corporate energy performance into *fundamental financial valuation*.



What was the premise? (cont.)

- Publicly trade companies will seek to improve their relative performance along these ratios because better values translate into higher shareholder value.



The link between energy and financial performance.



- Analysis of energy performance differentials provides source of alpha.
- Environmental performance is an excellent proxy for management quality.
- Management quality is the leading determinant of stock market performance.

Energy Performance Indices



- Energy Exposure Index
 - Energy Expenditures over Cashflow
- Energy Operating Index
 - Energy Expenditures over Operating Expenses
- Energy Sales Index
 - Energy Expenditures over Sales
- Energy Income Index
 - Energy over Net Income
- Energy Asset Index
 - Energy Expenditures over Assets



Money Isn't All You're Saving

- Facts & Figures
- Industry News
- Energy Prices
- Financial News
- Industry Links
- General Financial Links
- Market Summary
- General Economic Indicators
- Multimedia Room

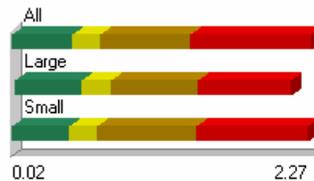


Energy Performance Indices

- VIEW PROFILE
- YOUR PERFORMANCE
- YOUR INDUSTRY
- YOUR POTENTIAL SAVINGS
- WHAT OTHER INDUSTRIES ARE DOING
- ABOUT THIS TOOL

Summary of Energy Indices for Grocery Stores

Based on 72 total observations



← Increasing Energy Efficiency

Energy Operating Index (EOI) shows the portion of expenses that go to energy by comparing energy expenditures to operating expenditures.

- Energy expenditures can be reported in several expense accounts.
- In manufacturing, energy can be part of the cost of goods sold.
- In other sectors, energy can be part of Selling, General, and Administrative (SG&A) expenses.
- Controlling expenses, including energy expenses, is always important, but is particularly critical for industries with low profit margins.
- Lower values indicate that a smaller portion of expenses is devoted to energy expenditures.
- The values in the lowest quartile range from .02 to .68.
- Energy Operating Index can be used to assess Operating Efficiency and Business Risk.

Energy Operating Index Values: Low=.02; 1st quartile=.68; Median=.95; 3rd quartile=1.28; High=2.27.

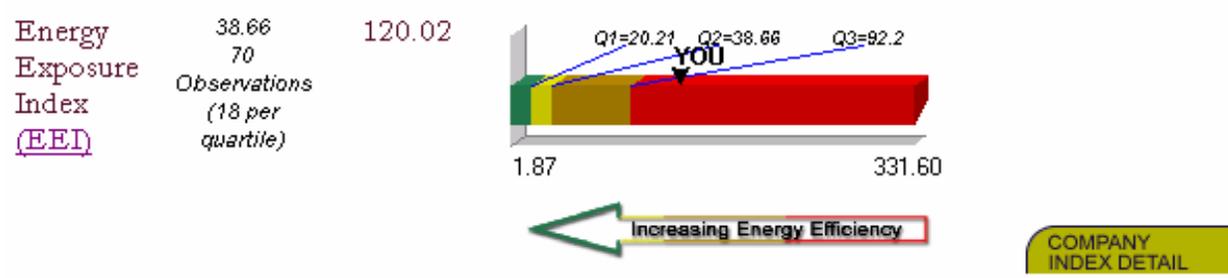
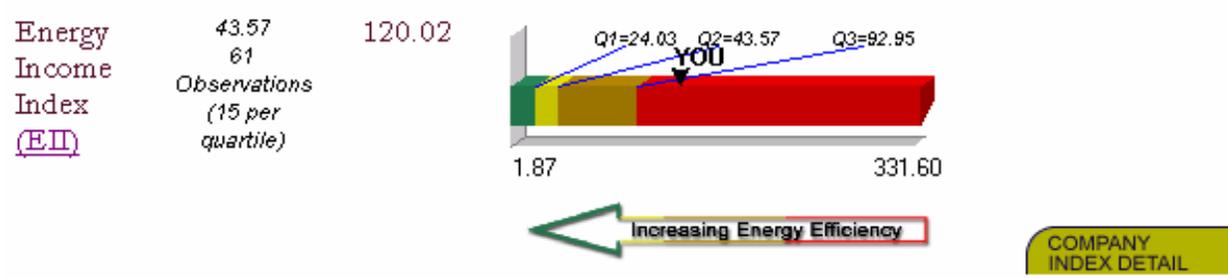
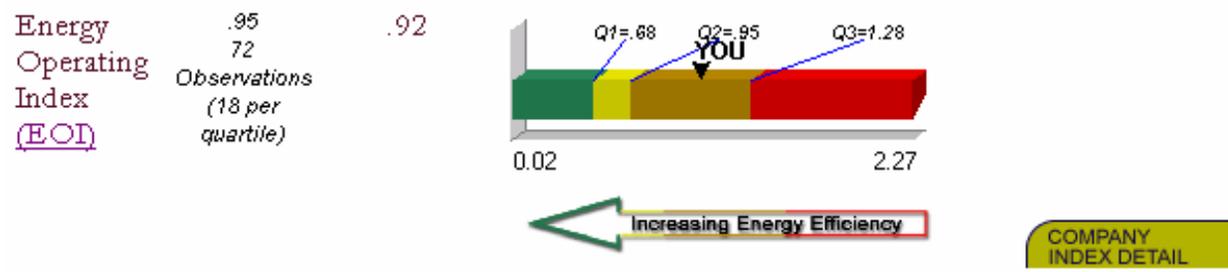
Formula: Energy Operating Index = Energy Expenditures/Operating Expenses * 100

INDUSTRY INDEX DETAIL





Index Type	(median)	REDNERS MARKETS INC	Ranking in Your Industry	Compare with another Industry
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What I learned during my (extended) summer vacation.



- *Superior environmental performance is increasingly recognized as hedge against economic downturn.*
 - Many types of risk can be prevented or mitigated through proactive environmental management
 - Investor risk (beta)
 - Cashflow
 - Goodwill/Intangible value (Tobin's Q)
- *"Show me the money."*
- *We are the ones who let the elephant in.*
- *We are the ones in a position to escort the elephant out.*
- *Do it, not because it is good. But, because it is good business.*
- *The solution to pollution is not dilution. The solution to pollution is valuation.*

But, please don't take my word for it.



“Why would sustainability practices be a proxy of good management? Because it shows that a company keeps an eye on the far horizon and long-term growth...in some instances, trying to reduce the environmental footprint creates innovation that provides more bottom line effects.”

Anne Gualtieri, VP of Investor Relations, Dupont

“Management quality is the leading determinant of stock market performance and research shows that eco-efficiency is a proxy for and predictor of superior corporate management, which generates superior financial performance and shareholder value.”

Frank Dixon, Managing Director,
Innovest Strategic Value Advisors



***“The problems of today will not be solved
by the same thinking that produced the
problems in the first place.”***

A. Einstein



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