Brazilians Still Lead the Way

by Staff Reporters

Brazil continues to set the standard for corporate governance and sustainability. With more money going to sustainable funds, companies are increasing their reporting.

Brazilian corporates won the highest marks for corporate social responsibility (CSR) and corporate governance (CG), risk, and overall sustainability, according to a *LatinFinance* study in association with Madrid-based consultancy Management & Excellence (M&E). The region's largest economy again shines in relation to the rest of LatAm in the second-ever assessment of the region's largest power, energy and oil and gas entities by market capitalization.

"Sustainability has matured with a need to look beyond mere compliance," says William Cox, managing director at M&E. This year's rankings incorporate quantifiable sustainability performance and risk-to-compliance in order to determine whether companies are successfully implementing sustainability and not just paying lip service to it, he explains.

Petrobras tops the overall scores, led not only by high compliance but by achieving a much higher mark in the performance category (which measures implementation) than peers. On the energy side, CPFL and Cemig's scores tell a similar story. Companies like Argentina's YPF and Chile's Enersis fall short in performance, while OGX's inconsistency in implementation sees it get the lowest rating. Both power and oil and gas saw a wide distribution of scores. Scores tabulated for the Mining and Telecoms sectors will be released later this year.

Cox says CPFL and Petrobras score well compared to the global leaders in their sectors. He points out that CPFL's equity price jumped by 108% between March 2009 and March 2011, while Enersis came in last in the sector, with a 34.3% rise. The two also both publish annual sustainability reports.

Globally, more companies should begin to be rated according to sustainability performance, Cox says, as investors pay more attention to these measures. He also sees more investment in sustainable assets and increased shareholder pressure on executives to justify returns from sustainability investments.

Brazilian companies still rank highest in CSR

"Investors have been looking to sustainability to tell them more about the DNA of a company," Cox says. For example, a good ethics program can reduce operating expenses by 5%, he says. M&E has found that broad employee training programs can impact productivity and revenues by between 30% and more than 800% according to studies M&E has carried out with large LatAm companies.

Robeco Bank and Booz Allen predict that asset managers will be moving roughly $15 trillion into sustainably managed funds by 2015, which will raise demand for better data on sustainability, Cox says.

M&E's method for this year's report involves a total of nearly 200 attributes in sustainability compliance, quantifiable sustainability performance and sustainability risk. The compliance metric takes into account sustainable management practices, corporate social responsibility and corporate governance. In the previous year's survey, these three measures were combined for an overall governance score.

This year two other dimensions have been added. Performance measures how well companies have improved in 24 different areas, such as environmental and financial practices and social

responsibility. The risk metric measures the level of volatility in the performance category over the last three years. Together, the compliance, performance and risk measurements yield an overall sustainability score.

The new method has meant that companies with poor performance and high risk scores such as Endesa and OGX, lost points this year. Cemig, the longest-standing Brazilian company in the Dow Jones Sustainability Index (DJSI), saw an improvement. The DJSI gained 8.1% this year through April 1, versus a 5.4% rise in the MSCI world index.

As with last year, only five regional companies in both sectors provided enough data to be included in the survey. Cox says that many companies talk about having policies to promote sustainability, corporate governance and transparency, but keeping a record is another matter. Weaker companies are not necessarily poorly managed, but rather suffer from deficiencies in transparency. LatAm companies' compliance scores tend to be higher than their performance scores, Cox explains, a sign that implementation still trails planning.

"Latin companies are hardly rated in sustainability, but investor interest will drive this trend," Cox says. "Laggards may see the advantage of better voluntary transparency and attempt to improve."

Ex-Brazil LatAm companies tend to perform poorly. In the DJSI, only Brazil has any significant representation with seven companies. Even Brazil is not among the top nine countries represented in the index. The top regions are the US, Europe, Japan and Australia.

Though M&E does not collect data on other emerging markets, Cox points out that other large developing economies such as Russia are "in the dark ages" in terms of management quality, and that LatAm compares favorably. There are also signs of ex-Brazil improvement.

"Pemex and Endesa, if you look at . . . the data they've released, you'll see that the sophistication in terms of financial data, risk analysis and transparency is improving year-on-year," Cox says.

Endesa, along with Eletrobras, Enersis and particularly YPF, are still developing viable sustainability programs, Cox explains, which normally takes 5-10 years to successfully implement.

Brazil is also further along in monitoring sustainability, with standards in the other LatAm countries remaining low, Cox says. Brazil's Bovespa index runs several sustainability indices, he says, including ISE and "Nivel 1 & 2". In addition, the country has developed a broad array of monitoring agencies, such as the Brazilian Governance Association (IBGC), which publish tough standards. There are regular competitions and rankings for the most transparent companies. Itaú, for example, is the world leader in the banking sector within the DJSI.

Cox also points out that seven of the 10 companies have ADRs listed on the NYSE, including all the power companies. This fact does not necessarily entail high scores, but US listing standards do guarantee a certain minimal transparency, and tend to result in more even performance across the areas measured. YPF, for example, is rated only CC-, but does not significantly lag in any individual area. The spread between its compliance and performance scores is only two points, Cox says.

At the same time, Cox says a high risk score (25.13%) suggests that the company is not yet implementing sustainability thoroughly or successfully. He points out that its greenhouse gas and other harmful emissions have shown high volatility in the last three years.

"And try getting a response from YPF's PR or IR departments," he adds.

"All these are definite signs for uneven—if not outright poor—management," Cox says. "Investors need to consider the risks of companies with weak management and insist on either higher dividend streams or expect a capital gain proportionately above that of less risky counterparts, such as Petrobras or even Pemex." **LF**

Sustainability Ratings of Large LatAm Energy Corporations 2011
Brazil leads the pack

	CPFL	Cemig	Endesa	Eletrobrás	Enersis
	Brazil	Brazil	Chile	Brazil	Chile
Compliance Percentage	92.00%	80.00%	61.00%	65.00%	37.00%
Peformance Percentage	68.00%	75.00%	40.00%	42.00%	18.00%
Risk Score Percentage	22.58%	18.80%	12.10%	23.30%	8.70%
M&E Final Score & Rating Percentage	82.80%	82.50%	66.50%	64.50%	47.85%

** Unaudited by M&E. Rating relies on data provided by company.*
Source: Management & Excellence

Sustainability Ratings of LatAm Large Oil/Gas Corporations 2011
Petrobras still the one to beat

	Petrobras	Pemex	Ecopetrol	YPF	OGX PET
	Brazil	Mexico	Colombia	Argentina	Brazil
Compliance Percentage	86.62%	86.00%	59.00%	47.77%	39.00%
Performance Percentage	77.00%	32.00%	36.00%	46.00%	9.00%
Risk Score Percentage	21.15%	11.00%	20.80%	25.13%	64.70%
M&E Final Score & Rating Percentage	84.47%	72.90%	60.90%	58.60%	-9.00%

** Unaudited by M&E. Rating relies on data provided by company.*
***Not rated because total score was negative*
Source: Management & Excellence