sustainable
autumn 2009
AMP CAPITAL NEWSLETTER

How much carbon is in SALT?

It is difficult to pick up a newspaper today and not read some discussion on the impact of the proposed emissions trading scheme or the impact of climate change on Australian business – some saying it will be the end of business in Australia, while others say it provides great opportunities. As investors, whether or not these views are proven correct will have some important implications.

The AMP Capital Investors Sustainable Alpha Team (SALT) has been considering the issues of climate change for over 8 years. In 2001 we surveyed the ASX100 companies and those in energy intensive industries about how they managed their climate change risk. We are now participants in the Investor Group on Climate Change (www.igcc.org.au) and the investor-led Carbon Disclosure Project (www.cdproject.net).

The AMP Capital Investors Sustainable Fund ("The Fund") aims to provide competitive total returns (capital growth and income) after costs and before tax relative to the Fund's performance benchmark on a rolling 3 year basis, being the S & P/ASX200 Accumulation Index. The same principle lies behind our approach to climate change; we aim to outperform the Fund Benchmark on both an environmental and investment perspective over the 5 – 7 year timeframe.

From an environmental perspective, we assess the exposure of the investments in the Fund by considering the kilotonnes of CO_2-e emitted per $100 million dollars of each investment. This applies the company emissions (both direct and indirect) per $100 million dollars of market capitalisation and the company weighting in the fund (versus the ASX200) to come up with an overall exposure for the fund (relative to the ASX200).

No single metric can provide the whole environmental perspective, as it does not factor in the positive contribution from investment in companies involved in greenhouse gas reductions. For example, the Fund also had a significant position in the renewable energy company, Babcock Brown Wind Partners Group.

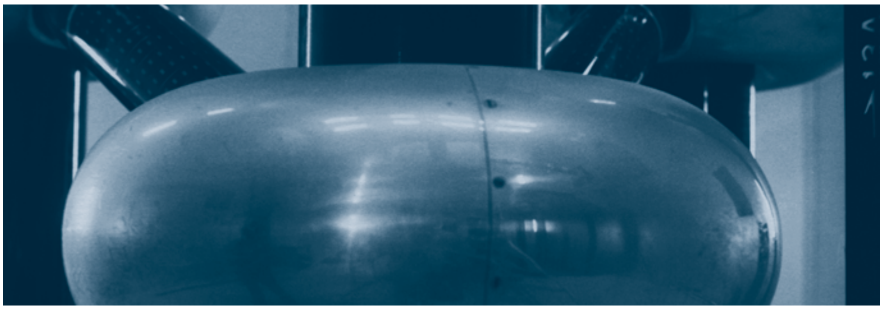
The **investment** exposure of the Fund to climate change is different to its **environmental** exposure for a number of reasons. For example, some ASX200 companies operate in developing countries where there is no proposed emissions trading scheme, so there are environmental implications but not investment implications. In contrast, emissions in developed countries proposing such schemes e.g. Australia, the EU and New Zealand, are likely to have an environmental and investment implication.

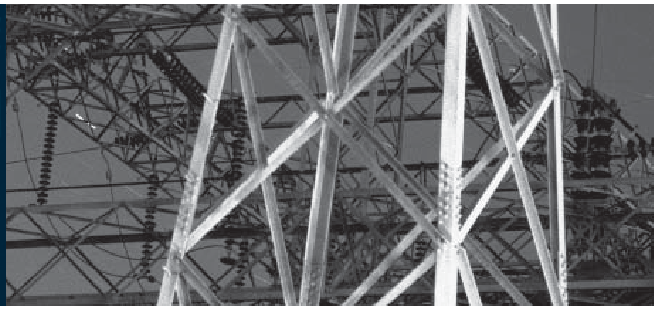
Also, some companies will be able to pass most of the costs of a trading scheme on to their customers and therefore the investment risk to them is significantly less than indicated by their emissions. The Funds portfolio relative to the ASX200, at 2 February 2009 had an exposure nearly a third less than that of the ASX200 portfolio and was underweight the greenhouse gas intensive materials sector.

Our investigation of individual companies uses more detailed analysis which makes it challenging to capture in a single metric to compare the climate change exposure of the companies in the Fund versus the companies in the Fund benchmark. Our company analysis considers such factors as: the likely assistance to companies under the proposed Australia trading scheme, cost of abatement options available to the company, ability to pass through costs, potential impacts as a result of exposure of customer or supplier to a trading scheme, and the physical impacts of climate change.

With the Australian emissions trading proposed to start in late 2010, it is important that all investors are looking at the exposure of their portfolios to climate change. SALT will continue to analyse the impact of climate change at a company and portfolio level.

As at 2 February 2009, the Fund portfolio had a greenhouse gas exposure 30% lower than the companies in the Fund Benchmark and the portfolio was underweight greenhouse intensive sectors, such as utilities, energy, metals and mining and materials.





AMP Capital corporate governance

Remuneration

Much has already been written about the current global financial crisis. Economists such as AMP Capital's Shane Oliver linked the freezing of lending and the disrupted credit flows to a combination of the following four factors – 'financial deregulation', 'the shift from high inflation to low inflation', 'financial innovation' and 'the US housing boom'[1]. On the other hand, the International Corporate Governance Network (ICGN) cited 'corporate governance failings' as another significant contributor to the current woes, claiming that problems have emerged above all because boards failed to understand and manage risk and tolerated perverse incentives"[2].

Various newspapers have opined on the role played by 'perverse incentives', for example stating that: "Through nearly two decades of tinkering, each new twist in executive pay has proved flawed. Incentives meant to reward good management have done just the opposite, and efforts to reform the system have in some respects made matters worse. From the bursting of the dot-com bubble to the collapse of companies like Enron and WorldCom, from the rampant backdating of stock options to the current meltdown of the global financial system, the so called pay-for-performance movement has led to colossal windfalls, reckless risk-taking and fraud"[3].

For many years AMP Capital has focused, voted, engaged and reported on issues of executive remuneration. We see the nature of remuneration structures, along with the composition of boards, as the most important governance issue. In turn we have actively encouraged companies to structure overall remuneration to be fair and reasonable and aligned with shareholder interests.

In 2008, falling share-prices and company profits have highlighted the unintended consequences and shortfalls of many current remuneration structures, including:

- Increasing complexity
- Significant, and often unjustified, increases in fixed pay
- Poor alignment with shareholder interests
- Generous arrangements for termination payments
- The practice of revising or re-testing performance hurdles, when previous hurdles were not met
- Unjustified, substantial sign-on payments
- Significant increases in, or poorly structured, non-executive remuneration

It has been AMP Capital's long-held view that alignment between the interests of shareholders and management is key.

As such, it is vital that appropriate performance hurdles be set. Incentives should ideally be designed to reward future superior performance with a clear link to appropriate relative benchmarks which are challenging and the achievement of which genuinely reflects an improved competitiveness of the company. Long-term incentive plans for senior executives should also clearly state their objectives, reflect the responsibilities of the executives, be reasonable when compared to the market and be transparent. They should also be of sufficient duration to retain key executives beyond the short-term and should not allow for automatic and full vesting on change of control where poor structure may potentially lead to conflicts of interest. Finally, to maintain their independence, non-executive directors should be ineligible to participate.

The March 2009 AMP Capital Investors Corporate Governance Report provides more detail on remuneration in Australia and internationally, and the AMP Capital Investors proxy voting report.

(http://www.ampcapital.com.au/institutions/governance.asp).

1. Oliver, S. 'Lessons learned from the global financial crisis' Oliver's Insights: (December 12, 2008)
2. International Corporate Governance Network (ICGN): Statement on the Global Financial Crisis (November 10, 2008)
3. Hilzenrath, D.S. 'Executive Pay' Washington Post (December 21, 2008)

profile

Michael Murray

BCom, MSc, CFA

Senior Portfolio Manager, Sustainable Funds

Michael joined the AMP Capital Investors Sustainable Alpha Team shortly after its inception in 2000. Since that time his primary responsibility has been to identify stocks that represent attractive investments within the ESG framework under which the team operates. On a day to day basis this involves meeting with companies from sectors as diverse as healthcare and steel manufacturing.

Whilst keenly focused on potential investment return, Michael often draws upon the expertise of the team's in-house ESG researchers to highlight a broader range of issues when meeting with company management. With responsibility for several heavy manufacturing and mining companies, occupational health and safety, environmental and local community issues often come to the fore.

Prior to working with AMP Capital Investors, Michael spent time working in organisational change and management consulting as well as completing a Master of Science examining tensions between economic and social issues. He has developed these interests during travels on the Indian subcontinent where he spent time researching the provision of microfinance by organisations such as Grameen Bank. He is the current secretary of the Responsible Investment Association Australasia and holds a board position on the Vincent Fairfax Leadership in Ethics Foundation.

stock story

Fisher and Paykel Healthcare

The Fund invests in shares in Fisher and Paykel Healthcare Corporation Limited (FPH), a medical devices company which designs, manufactures and markets products and systems for use in respiratory care, acute care, and the treatment of obstructive sleep apnea. FPH range include neonatal care products designed to help maintain normal body temperature for newborn babies, infant resuscitators and continuous positive airway pressure (CPAP) systems designed to improve infant respiratory function.

FPH products, and manufacturing and design processes, are certified to relevant Australian, New Zealand, US and European quality and safety standards. Its research and development pipeline which aims to expand the surgical application of humidifiers provides opportunities to increase the number of patients by expanding from the traditional intensive care ventilation market into non-invasive ventilation, oxygen therapy, humidity therapy, neonatal respiratory care and surgery. Medical devices which can assist the critical treatment of patients and improve the quality of care and of life will continue to gain support in the transition to a socially sustainable economy.

Importantly for an innovative medical devices company, FPH is a strong investor in its people and is a repeat winner of New Zealand's largest 'best employer' survey. Attraction and retention of intelligent and creative employees is essential to ensure the on-going research and product development in this sector. In addition, the company is working on other corporate responsibility initiatives including reducing its waste footprint and responding to the carbon disclosure project.

Note: AMP Capital Investors is not making any recommendation or warranty about the performance of shares in FPH.

Research and engagment

Our sustainable investment process requires an understanding of both sustainability growth drivers at an industry level, and environmental, social and governance risks at the company level. The value proposition of the AMP Capital Investors Sustainable Alpha Team (SALT) derives from a fuller understanding of company value through our process which integrates tangible financial analysis with the more intangible extra-financial research. In delivering this value proposition during the past 6 months SALT has completed industry specific research on the biotechnology and pharmaceutical, and mining sectors.

SALT has continued its constructive engagement as part of the investment process and as part of our value proposition to investors. Some engagement highlights with companies and industry were on the following topics:

Climate change: Ian Woods met with the Australian Government Treasury Department to discuss modelling the impact of emissions trading in Australia. Ian presented at the Australian Wealth Management Annual Conference on the exposure of Australian firms to climate and carbon risk. Ian also presented at the Carbon Market Expo Australasia '08 on an electricity sector analysis of carbon risk. Ian raised financial exposure under an emissions trading scheme with OneSteel Limited.

Corporate governance: Ian Woods and Karin Halliday met with the Chairmen of Westpac Bank, Commonwealth Bank and ANZ Bank to discuss best practice corporate governance. Nick Edgerton and Karin Halliday met with the Chairman on Ansell to discuss workplace and environmental risk management and the use of related KPIs. Nick Edgerton discussed best practice corporate governance with IBA Health Limited.

Corporate responsibility: Nick Edgerton visited Metcash Limited distribution centres and retail outlets to observe its business practices. Ian Woods met with BHP Limited to discuss the assessment of materiality of ESG issues. Mike Murray met with Orica Limited and discussed OHS performance and environmental management. Nick met with Australian Government Environment Department to discuss water efficiency options for business. Will Riggall and Nick discussed investing in people, and relationships with suppliers and the community with Super Cheap Auto Limited.

Social capital: Nick Edgerton raised ongoing relationships with pathology referrers with Healthscope Limited. Nick discussed investing in people and customer service with Invocare Limited. Nick discussed investing in people with Mitchell Communications Limited. Nick raised GP and Pathologist retention with Primary Health Care Limited. Nick raised organisational culture change with AWB Limited.

Sustainability reporting: Ian Woods presented at the launch of the AA1000 Assurance Statement about an investors perspective on sustainability reporting and assurance of reporting. Nick Edgerton presented a paper at the Green Cities '09 Conference entitled "What Analysts Want?"

performance

The AMP Capital Sustainable Share Fund (the "Fund") has outperformed its benchmark of the S&P/ASX200 Accumulation Index by an annualised rate of 0.80% since its inception in February 2001 to the end of February 2009. Over this period, the Fund has returned 5.21% pa compared to its benchmark return of 4.41% pa.

The Funds overweight positions in the healthcare and telecommunications sectors have been among the top contributors to performance over the last six months. Industries of the future, Cochlear Limited and Fisher and Paykel Healthcare Corporation Limited have been two of the best performers. Both companies have a defensive earnings stream by virtue of their leading market positions, and offer a robust growth outlook despite weakness in the wider economy. Overweight positions in Singapore Telecommunications Limited and Telstra Corporation Limited also aided performance. SingTel in particular has been successful in gaining market share, growing revenues for both voice and data services and successful execution of its growth strategies.

Detractors of the Fund were concentrated in companies that have difficulties with their capital structures. Access to capital, particularly debt, remains constrained and is putting the more highly leveraged companies under pressure. Included in this group were overweight positions in Transfield Services Limited, Goodman Group and HFA Holdings Limited.

Looking ahead, the Fund will continue to apply the Sustainable Alpha Process to search for investments that are offering superior returns and risk characteristics that provide a sustainable growth outlook consistent with the Fund's style.

(Wholesale Units) AMP Capital Sustainable Share Fund, before tax and after fees as at 28 Feb 2009

	3 months	1 year	2 years %pa	3 years %pa	4 years %pa	5 years %pa	Inception
Fund	-9.60%	-37.41%	-22.09%	-8.93%	-1.49%	4.08%	5.21%
Benchmark	-9.48%	-36.89%	-20.83%	-8.19%	-1.15%	4.37%	4.41%
Difference	-0.12%	-0.52%	-1.26%	-0.75%	-0.34%	-0.29%	0.80%

*Important Note: AMP Capital Investors Limited (ABN 59 001 777 591, AFSL 232 497) ("AMP Capital"). The above returns were available only to wholesale investors from the Fund inception on 20 March 2001 to 31 August 2008 and are before tax, after fees and costs and assume income is reinvested. Past performance is not a reliable indicator of future performance. A new class of retail units was issued in the Fund on 30 March 2007 pursuant to Product Disclosure Statement ("PDS") with higher fees and charges than those attached to the wholesale units.

To invest in the AMP Capital Sustainable Share Fund ("Fund") investors need to obtain the Fund's current PDS from AMP Capital. The PDS contains important information about investing in the Fund and it is important investors read the PDS before making any decision whether to acquire, or continue to hold, units in the Fund. AMP Capital is the responsible entity of the Fund. Neither AMP Capital, nor any other company in the AMP Group guarantees the repayment of capital or the performance of any product or any particular rate of return referred to in this newsletter.

news

There are signs that the **cocoa industry is finally moving towards improved working conditions for its suppliers**. The sector has failed to achieve its own targets of best practice conditions after many years of little action under the voluntary Harkin-Engel Protocol. The Protocol is a commitment by the global cocoa industry and the governments of Ivory Coast and Ghana, with agreed implementation in July 2001. It set an initial deadline for addressing the worst forms of child labour by July 2005, but industry was slow off the mark, and that deadline was subsequently extended to July 2008, which was also missed. In March this year Cadbury committed to achieving Fairtrade certification for key product Cadbury Dairy Milk by end of the northern summer 2009 – essentially tripling of sales of cocoa under Fairtrade terms for cocoa farmers in Ghana. It is hoped that this will kick start action from global competitors.

The Australian Government has flagged the **delay of its Carbon Pollution Reduction Scheme**, from its targeted July 2010 start date to the end of 2010. A delayed start to 2011 or 2012 is looking increasingly likely and may not significantly impact the challenge of emissions targets with business as usual emissions likely fall to with the economic downturn.

Interest is growing in soil carbon technology and practices to capture and store carbon emissions. This process involves converting agricultural and plant waste into a stable charcoal rather than allowing it to decompose. CSIRO notes its great potential, but states that there are substantial knowledge gaps which require further research to better understand its properties and benefits.

The **revised AA1000 corporate responsibility assurance standard** was launched in January. The standard focuses sustainability reporting on what is material to the company and its stakeholders, following the reporting principles of inclusiveness, materiality and responsiveness.

February saw the **launch of ESG Research Australia** (ESG RA), a new initiative from Superannuation Funds Hesta, VicSuper and UniSuper to promote a greater commitment to broker research into environmental, social and governance issues. The ESG RA is an Australian initiative which seeks to pick up where the global Enhanced Analytics Initiative left off, following its amalgamation with the UN Principles for Responsible Investment.

AMP Capital Sustainable Share Fund

The AMP Capital Sustainable Share Fund is available to Australian investors. The overall objective of the Fund is to deliver superior returns to our clients by investing in companies that contribute to, benefit from and best adapt to the shift to an environmentally sustainable and socially responsible global economy.

Further information can be found on our website:
www.ampcapital.com.au/sustainable

Important note: Investors should consider the product disclosure statement available from AMP Capital Investors Limited (ABN 59 001 777 591) for the Sustainable Share Fund before making any decision regarding the Fund. Neither AMP Capital Investors, nor any other company in the AMP Group guarantees the repayment of capital or the performance of any product or any particular rate of return referred to in this document. Past performance is not a reliable indicator of future performance. While every care has been taken in the preparation of this document, AMP Capital Investors makes no representation or warranty as to the accuracy or completeness of any statement in it including, without limitation, any forecasts. This document has been prepared for the purpose of providing general information, without taking account of any particular investor's objectives, financial situation or needs. An investor should, before making any investment decisions, consider the appropriateness of the information in this document, and seek professional advice, having regard to the investor's objectives, financial situation and needs. This document is solely for the use of the party to whom it is provided.