

Research Flash

Investment Ideas

Invest in companies with a good sustainability rating in a zero yield environment

Private Banking

In a zero yield environment, invest in sustainable firms

After nine months of volatility, global share prices are broadly back where they started in 2010. But with yields at or near historic lows (Figure 1), the risk of a deflationary scenario low, and interest rates likely to stay low well into 2011, the case for reducing cash holdings and increasing equity exposure is becoming increasingly compelling, in our view. In this context, we believe the current environment offers opportunities to build positions in companies that are attractively valued, have good growth potential and are better positioned than their peers to manage risks stemming from social and environmental issues. Our responsible investment strategy integrates an analysis of environmental, social and governance (ESG) issues into our traditional investment process, with the goal of identifying companies likely to outperform peers in the long term.

Why ESG factors are becoming increasingly important

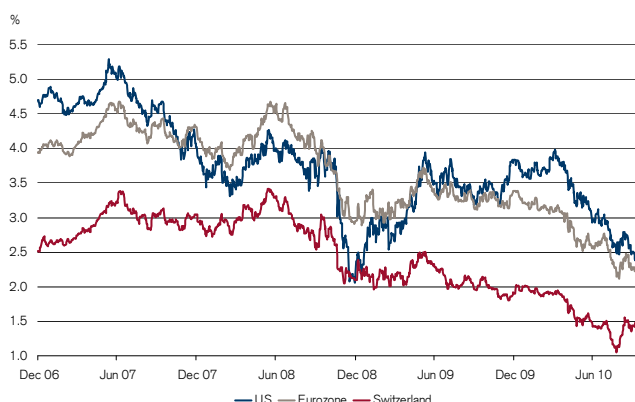
In a rapidly changing business world, the way companies manage environmental, social and corporate governance (ESG) issues is likely to become increasingly relevant to their future competitiveness. Business practices and their impact on society are also increasingly being monitored by the public, a process which has accelerated due to unprecedented levels of

Highlights

- The ability for companies to manage environmental, social and corporate governance (ESG) issues is likely to become increasingly vital to their long-term competitiveness, financial performance and long-term sustainable growth potential at a lower business risk.
- Equity valuations are attractive against bonds, with bond yields at or near historic lows. This leaves an asymmetric risk to the upside for equities, in our view.
- We recommend that investors profit from the attractive valuation environment of equities and build up exposure in companies that have an AAA- sustainability rating and are attractively priced.

Figure 1

Bond yields are at or near historical lows



Source: Bloomberg, Credit Suisse

Top investment ideas

Vodafone (BUY)

Vodafone has a well-rounded ESG strategy and is a leader in its sector. Moreover, the firm offers an attractive dividend yield of 5.4%.

BASF (BUY)

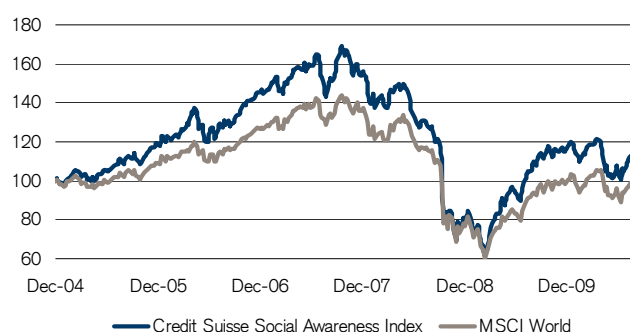
A global leader in the chemicals industry, BASF has an AAA sustainability rating and continues to secure new emerging market revenue streams. Dividend yield amounts to 4.4%.

SWISS RE (BUY)

Leader in the reinsurance sector based on research and policy engagement risk; dividend yield of 4.1%; AAA sustainability rating.

Figure 2

Credit Suisse Social Awareness Index outperforms



Source: Bloomberg, Credit Suisse

corporate transparency, as well as by the proliferation of web-enabled participatory media such as Twitter, YouTube, Facebook, etc. Given this changing business context, we believe that companies that pay attention to ESG issues can differentiate themselves from competitors by better managing risks, but also by capitalizing on opportunities arising from the changing business context.

How can ESG factors affect business strategy?

Some examples of how paying attention to ESG factors can affect business strategy and profitability may include the following:

- Protecting brand equity or reputation: Firms with responsible ESG practices are likely to be better positioned relative to peers to operate in an environment of tightening national, regional and global regulatory requirements for non-traditional business and investment risks. In other words, firms that treat workers poorly, create products that harm consumers, or neglect the environment through their business practices are more likely to eventually face lawsuits or a backlash from consumers or regulators.
- Reducing capital costs: Constant failure to address the concerns and expectations of stakeholders could ultimately reduce investors' confidence in the firm's stock, impacting the cost of financing (weighted average cost of capital) and thus the company's profit-making opportunities.
- New revenue through new products/services: This includes technologies, such as electric cars, solar panels, wind energy, energy efficient light bulbs, etc.
- First-mover advantage: Anticipating changes in the regulatory and business environment ahead of competitors.
- Good stakeholder relationships: Securing, retaining and enhancing a "social license to do business" – particularly in emerging markets.
- Attracting, retaining and motivating top talent: ESG performance makes firms more attractive to job seekers and generally tends to improve the motivation of existing employees by developing a healthy corporate culture.

- Better operational efficiency: Reducing operating expenditures through energy efficiency and waste minimization.

Can ESG factors translate into equity outperformance?

The competitive advantages mentioned above also typically allow businesses to achieve improved profitability relative to their peers. The performance of our Credit Suisse Social Awareness Index supports this tendency of companies with good ESG ratings to outperform their peers (Figure 2). For more detailed information, please refer to our primer on responsible investments, titled "Responsible Investment: A systemic approach to investing in market leading companies," which we published in February 2010.

Our Responsible Investing Screening Approach

The premise of our Responsible Investment strategy is that, over time, the interests of shareholders will be best served by companies that maximize their financial performance by strategically managing their economic, social, environmental and ethical performance. To this end, our screening approach (Figure 3) relies on both an analysis of extra-financial or ESG factors as well as traditional financial parameters.

The methodology of our screening approach

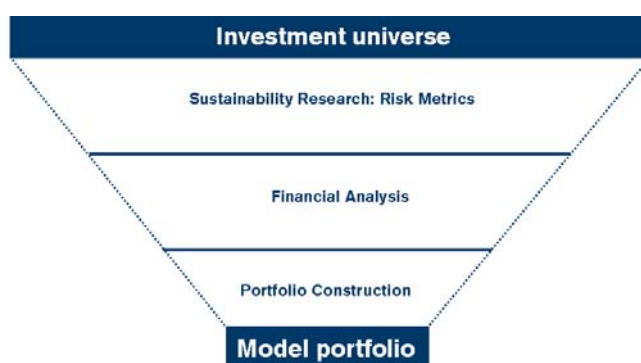
The approach can be summarized into four steps:

- 1) Highest possible ESG rating (i.e. AAA)
- 2) BUY rating
- 3) Attractive dividend yield
- 4) Undemanding valuation relative to sector based on forward price-to-earnings and price-to-book multiples

The first step of our screening approach focuses on the highest possible rating on ESG factors according to risk metrics (i.e. AAA). This rating process relies on a positive screen of over 120 ESG factors that are likely to impact the future competitiveness, profitability, and share price performance of a

Figure 3

Responsible Investment process



Source: Credit Suisse

company. For instance, we look at issues, such as: how well companies manage the risks associated with and opportunities arising from climate change; how well they attract, retain and motivate their employees; the quality of their relationships with key stakeholders, such as non-governmental organizations, governments and consumers; and how carefully companies manage their brands and reputations. An AAA rating is assigned to a company with minimal, well-identified environmental/social risks and liabilities, and a strong ability to meet any losses that could materialize.

Our second screening step is to select only BUY-rated stocks, based on our Private Banking analysts' recommendations. Our third step focuses on identifying companies with positive dividend yields, which is especially attractive when the dividend yields alone often exceed the currently low bond yields (Figure 1). And in a fourth and final step, to further refine the screen, we select companies that are currently trading at attractive forward price-to-earnings and price-to-book valuation levels relative to their sector peers. The results of our screening approach can be seen in Table 1.

Conclusion

Looking ahead, we believe the ability for companies to manage environmental and social issues is likely to become increasingly vital to their long-term competitiveness and financial performance – and perhaps even to their survival. In this context, we believe sustainability is likely to become one of the most critical drivers of business over the next decade as companies realize that their survival hinges on how well they respond to ESG issues. And, especially in an environment in which bond yields are at or close to historical lows, investing in stocks with long-term, sustainable growth potential is likely to become increasingly attractive. In this context, we believe our Responsible Investment strategy is a way to identify attractively valued companies with good management and a long-term strategy for success.

Table 1: Top 20 results of the Responsible Investment stock screen

Company	Ticker	Sector	Country	Curr.	Rating	Sustain rating	Market cap (bn USD)	Div. yield FY 1 (%)	P/E FY1	P/B FY0	Target upside (%)
IBERDROLA	IBE SM	Utilities	Spain	EUR	BUY	AAA	43.26	5.7	11.2	1.17	13.84
VODAFONE	VOD LN	Telecom	UK	GBP	BUY	AAA	136	5.4	10.33	0.94	13.51
LAFARGE S.A.	LG FP	Materials	France	EUR	BUY	AAA	16.2	5.0	12.32	0.78	9.66
LEND LEASE CORP.	LLC AU	Financials	Australia	AUD	BUY	AAA	4.22	4.5	12.21	1.28	24.01
SWISS RE	RUKN VX	Financials	Switzerland	CHF	BUY	AAA	17.69	4.4	9.52	0.69	24.24
BASF	BAS GR	Materials	Germany	EUR	BUY	AAA	62.04	4.1	11.03	2.55	7.26
NTT DOCOMO	9437 JP	Telecom	Japan	JPY	BUY	AAA	68.88	3.9	11.28	1.21	18.08
ERICSSON	ERICB SS	IT	Sweden	SEK	BUY	AAA	34.39	2.9	13.88	1.64	32.13
DANONE	BN FP	Consumer	France	EUR	BUY	AAA	37.16	2.9	16.1	2.04	15.02
ENCANA	ECA CN	Energy	Canada	CAD	BUY	AAA	22.35	2.6	24.88	1.35	55.54
WPP	WPP LN	Consumer Discre.	UK	GBP	BUY	AAA	13.91	2.4	12.7	1.48	9.79
BAXTER INT.	BAX US	Health Care	USA	USD	BUY	AAA	28.83	2.3	12.54	4.01	9.42
SAB MILLER	SAB LN	Consumer Staples	UK	GBP	BUY	AAA	51.15	2.3	18.02	2.57	7.84
EAST JAPAN RAIL	9020 JP	Industrials	Japan	JPY	BUY	AAA	24.46	2.2	12.46	1.11	48.22
AEON	8267 JP	Consumer Staples	Japan	JPY	BUY	AAA	9.08	1.8	24.78	0.88	13.29
HONDA MOTOR	7267 JP	Consumer Discre.	Japan	JPY	BUY	AAA	64	1.8	10.48	1.21	19.45
BMW	BMW GR	Consumer Discre.	Germany	EUR	BUY	AAA	45.79	1.7	13.07	1.65	19.52
SAP	SAP GR	IT	Germany	EUR	BUY	AAA	61.74	1.5	16.64	5.23	7.3
ASML	ASML NA	IT	Netherland	EUR	BUY	AAA	13.34	1.2	10.54	5.4	35.81
PANASONIC	6752 JP	Consumer Discre.	Japan	JPY	BUY	AAA	29.75	1.1	26.48	0.92	53.06

Source: Bloomberg, HOLT, Credit Suisse

Abbreviations frequently used in reports

Abb.	Description	Abb.	Description	Abb.	Description
CAGR	Compound annual growth rate	EPS	Earnings per share	P/B	Price-to-book value
CFO	Cash from operations	EV	Enterprise value	P/E	Price-earnings ratio
CFROI	Cash flow return on investment	FCF	Free cash flow	PEG	P/E ratio divided by growth in EPS
DCF	Discounted cash flow	FFO	Funds from operations	ROE	Return on equity
EBITDA	Earnings before interest, taxes, depreciation and amortization	IBD	Interest-bearing debt	ROIC	Return on invested capital

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Equity rating history as of 13/10/2010

Company	Rating	Date
AEON (8267 JP)	BUY	since 08/07/2010
	HOLD	since 15/04/2010
	HOLD	since 08/01/2010
	HOLD	since 07/10/2009
ASML (ASML NA)	BUY	since 13/10/2010
	BUY	since 16/07/2010
	BUY	since 14/07/2010
	BUY	since 20/04/2010
	BUY	since 14/04/2010
	BUY	since 22/01/2010
	BUY	since 20/01/2010
	BUY	since 15/10/2009
	BUY	since 14/10/2009
	BUY	since 10/09/2009
BASF (BAS GY)	BUY	since 02/08/2010
	BUY	since 29/07/2010
	BUY	since 03/05/2010
	BUY	since 29/04/2010
	BUY	since 01/03/2010
	HOLD	since 25/02/2010
	HOLD	since 30/10/2009
	HOLD	since 29/10/2009
	HOLD	since 20/10/2009
	HOLD	since 14/10/2009
BAXTER INTERNATIONAL (BAX US)	HOLD	since 26/08/2009
	BUY	since 23/07/2010
	HOLD	since 26/04/2010
	HOLD	since 23/04/2010

BMW (BMW GY)	HOLD	since 29/01/2010
	HOLD	since 28/01/2010
	HOLD	since 19/10/2009
	HOLD	since 16/10/2009
	HOLD	since 17/07/2009
	BUY	since 04/10/2010
	BUY	since 03/08/2010
	BUY	since 13/07/2010
	BUY	since 06/05/2010
	BUY	since 18/03/2010
DANONE (BN FP)	BUY	since 15/03/2010
	BUY	since 01/02/2010
	BUY	since 03/11/2009
	BUY	since 25/09/2009
	BUY	since 27/07/2010
	BUY	since 15/04/2010
	BUY	since 12/02/2010
	BUY	since 11/02/2010
	BUY	since 23/10/2009
	BUY	since 28/07/2009
EAST JAPAN RAILWAY (9020 JP)	BUY	since 30/09/2010
	BUY	since 28/04/2010
	BUY	since 29/10/2009
	BUY	since 28/07/2009
ENCANA (ECA CN)	BUY	since 21/07/2010
	BUY	since 09/06/2010
	BUY	since 26/04/2010
	BUY	since 12/02/2010
	HOLD	since 09/12/2009
	HOLD	since 16/11/2009
ERICSSON (ERIC SS)	HOLD	since 23/07/2009
	BUY	since 10/09/2010
	HOLD	since 28/07/2010
	BUY	since 23/07/2010
	BUY	since 28/04/2010
	BUY	since 23/04/2010
	BUY	since 25/01/2010
	BUY	since 14/01/2010
	SELL	since 22/10/2009
	SELL	since 28/07/2009
HONDA MOTOR (7267 JP)	BUY	since 29/09/2010
	BUY	since 02/08/2010
	BUY	since 21/06/2010
	BUY	since 28/10/2009
	HOLD	since 30/07/2009
	HOLD	since 24/02/2010
IBERDROLA (IBE SM)	BUY	since 21/07/2010
	HOLD	since 29/04/2010
	HOLD	since 24/02/2010
	BUY	since 23/10/2009
LAFARGE S.A. (LG FP)	BUY	since 23/07/2009
	BUY	since 31/08/2010
	BUY	since 02/08/2010
	BUY	since 30/07/2010

LEND LEASE CORPORATION LIMITED (LLC AT)	BUY	since 25/02/2010
	BUY	since 19/02/2010
	BUY	since 06/11/2009
	BUY	since 13/10/2009
	BUY	since 29/07/2009
	BUY	since 17/08/2010
	BUY	since 14/07/2010
	HOLD	since 04/03/2010
	HOLD	since 22/12/2009
	HOLD	since 07/12/2009
NTT DOCOMO (9437 JP)	HOLD	since 21/08/2009
	BUY	since 04/10/2010
	BUY	since 29/06/2010
	BUY	since 01/02/2010
PANASONIC (6752 JP)	BUY	since 05/11/2009
	BUY	since 14/08/2009
	BUY	since 04/10/2010
	BUY	since 30/07/2010
	BUY	since 11/05/2010
	BUY	since 08/02/2010
	BUY	since 26/01/2010
	HOLD	since 10/11/2009
SAB MILLER (SAB LN)	HOLD	since 06/08/2009
	BUY	since 28/05/2010
	HOLD	since 19/11/2009
	HOLD	since 15/10/2009
SAP (SAP GR)	HOLD	since 09/09/2009
	BUY	since 30/07/2010
	BUY	since 27/07/2010
	BUY	since 17/05/2010
	BUY	since 14/05/2010
	BUY	since 29/04/2010
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	BUY	since 08/02/2010
	BUY	since 05/02/2010
	BUY	since 27/01/2010
	BUY	since 14/01/2010
	BUY	since 03/11/2009
	HOLD	since 28/10/2009
SWISS RE (RUKN VX)	HOLD	since 30/07/2009
	BUY	since 10/08/2010
	BUY	since 05/08/2010
	BUY	since 12/05/2010
	BUY	since 06/05/2010
	BUY	since 19/02/2010
	HOLD	since 19/01/2010
	HOLD	since 04/11/2009
	HOLD	since 03/11/2009
	HOLD	since 04/09/2009
VODAFONE (VOD LN)	BUY	since 10/09/2010
	BUY	since 08/09/2010
	BUY	since 27/07/2010
	BUY	since 23/07/2010
	BUY	since 18/05/2010
	BUY	since 05/02/2010
	BUY	since 04/02/2010
	BUY	since 10/11/2009
	BUY	since 16/09/2009
WPP (WPP LN)	BUY	since 01/04/2010
	BUY	since 27/08/2009

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Guide to analysis

Equity rating allocation as of 13/10/2010		
	Overall	Investment banking interests only
BUY	46.26%	47.06%
HOLD	49.19%	48.62%
SELL	2.64%	2.25%
RESTRICTED	1.91%	2.08%

Relative stock performance

At the stock level, the selection takes into account the relative attractiveness of individual shares versus the sector, market position, growth prospects, balance-sheet structure and valuation. The sector and country recommendations are "overweight," "neutral," and "underweight" and are assigned according to relative performance against the respective regional and global benchmark indices.

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The stock recommendations are BUY, HOLD and SELL and are dependent on the expected absolute performance of the individual stocks, generally on a 6-12 months horizon based on the following criteria:

BUY:	10% or greater increase in absolute share price
HOLD:	variation between -10% and +10% in absolute share price
SELL:	10% or more decrease in absolute share price
RESTRICTED:	In certain circumstances, internal and external regulations exclude certain types of communications, including e.g. an investment recommendation during the course of Credit Suisse engagement in an investment banking transaction.
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HOLD:	Expectation that the bond issue will perform in line with the specified benchmark
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