



Explosive Investments
Financial Institutions and Cluster Munitions
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Executive summary

Although 98% of cluster munition victims are civilians, cluster munition producers don't have any problems attracting capital from financial markets. Financial institutions all over the world seem to have no objections financing companies producing cluster munitions. Expensive and well known concepts like corporate social responsibility and socially responsible investment seem to have little impact on investment decisions. Financial institutions generally don't even consider disinvesting from morbid civilian-killers like cluster munitions.

In this paper you can find the results of research into the financing of six cluster munition producers. Sixty-eight financial institutions have been found to play a role in the financing of these companies. Financial flows have reached these companies from all over the world. The research contains information on financial institutions from Australia, Belgium, Canada, France, Germany, Italy, Japan, The Netherlands, Saudi Arabia, Spain, Switzerland, UK and USA.

Together they secured credit facilities for these six cluster munition producers worth a total amount of US\$ 12.6 billion (€ 10 billion) during 2004-2007. Investment banking services have also arranged bond issues for two companies worth a total amount of US\$ 1.3 billion (€ 1 billion) during the same period. Several financial institutions have also been found to hold significant shareholdings in four cluster munition producers. And this is only the top of the iceberg. We have restricted our research to the recent and most important investments in these six companies, and there are of course far more than six cluster munition producers in the world.

Civil society and affected communities are increasingly realising that the blind allocation of capital resources to this kind of company lends legitimacy to these companies and their continuing production of cluster munitions. A strong signal by the financial community that investing in cluster munitions is no longer meeting their ethical standards, would make a big difference.

Ambitious daydreaming? Maybe, but fortunately some financial institutions have already cleared the path for these developments. Recently not only ethical banks but also some mainstream financial institutions have decided to reject any investment in companies involved in cluster munitions.

Of course governments can play a big role in reallocating capital resources away from cluster munitions. Firstly they can give the good example by excluding cluster munition investments from government funds, secondly they can vote laws banning investments in these weapon systems. Recent steps have been taken by the European Parliament, and the Belgian and Norwegian Parliaments. Now that Norway has taken the initiative to work on an international treaty to ban cluster munitions, including a ban on investments in the treaty could make a major shift.

1. Investing in cluster munition producers: an ethical problem

1.1. *Financial institutions' power and responsibility*

A wide range of financial institutions (FIs) operate in our globalised world. These include private-owned companies and state-owned institutions. Banks, insurance companies, investment funds, investment banks, pension funds, export credit agencies, multilateral financial institutions, government funds and many others play a crucial role in allocating financial resources. As a large majority of companies and governments in the world are dependent on the financial markets and these financial institutions to find the capital needed to operate, these FIs play a key role in every segment of human activity. Simply by choosing the companies and projects they will finance and invest in, financial institutions are fostering certain (business) evolutions. A clear example can be seen in the energy sector. By shifting their investments from carbon-based energy towards renewable energy, such as solar energy, wind energy, small-scale hydropower, banks could foster an important change in the fight against environmental destruction and global warming.

Unfortunately FIs are generally taking investment decisions based solely on profit maximising criteria. Most of the time the impact of these investments on human rights, armed conflict or environmental destruction are not taken into account. Of course there are exceptions, but a big majority of banking groups and other FIs are blindly investing in any profit-gaining activity and are totally neglecting – and even ignoring – the impact of their decisions on human lives. This attitude has resulted in FIs irresponsibly channelling financial flows in ways that are too often harmful to the environment, human rights and social equity.

This combination of a huge leverage power and a lack of social responsibility is a dangerous cocktail posing a serious threat to the sustainable development of our planet.

More and more affected communities and organisations fighting against injustice are recognising the power of FIs working behind the screens of companies and projects. Civil society is increasingly questioning the financial sector's accountability and responsibility. The Collevocchio Declaration on Financial Institutions and Sustainability, is a strong call by civil society organisations on financial institutions to embrace a commitment to sustainability, 'do no harm', responsibility, accountability and transparency.¹

1.2. *Fostering cluster munition production: an ethical minefield*

Several reports and studies have confirmed and documented the general knowledge that bank groups are investing heavily in the arms industry. With growing military budgets around the world, and especially the so called 'war on terror' since the end of 2001, the arms industry has remained or become an interesting profit making industry for investors. It seems that even in this risky business FIs are blindly investing in any project or company offering lucrative prospects. Nonetheless it is common knowledge that arms embargoes and arms export controls are breached on a continuous basis, fuelling numerous conflicts and supporting repressive regimes. Moreover the defence industry is known for its low sustainability standards, tendency towards corruption and lack of transparency. Consequently any FI providing financial services to the defence sector takes serious risks of becoming involved in dubious transactions.

In this briefing paper the focus lies on investments by FIs in cluster munition producers. In the next chapter you can find a whole range of examples of FIs investing in or offering financial services to cluster munition producers. These investments pose serious ethical concerns to these financial institutions. These concerns rise from two arguments: the controversial character of cluster munitions and the complicity of the investor.

- Cluster munitions: threat to civilians

Cluster munitions pose a serious threat to civilian populations during and after a conflict.

1. Cluster munitions are designed to cover a large area where one or more targets are located. Spreading the munitions over this area results in a large chance of civilian casualties during the attack.
2. But these weapons also cause civilian casualties after the end of the armed conflict. The sub-munitions contained in cluster bombs or rockets have a certain rate of failure (dud rate). Following a cluster attack there will be many unexploded submunitions left behind over a large area. A mine field is created, with a great risk for civilians, for years after the conflict.

At this moment cluster munitions have been used in 23 countries or areas. Recent use has been documented in amongst others former Yugoslavia, Afghanistan, Iraq and Lebanon. In the first world-wide research on cluster munition victims, Handicap International revealed² that nearly all recorded cluster munition casualties are civilians, putting the figure at 98 percent. Twenty seven percent of these are children.

Using cluster munitions is a serious breach of International Humanitarian Law as it is impossible to distinguish between civilian and military targets, and causes disproportionate long-term civilian harm. Therefore cluster munitions stand out as the weapon category most in need of stronger national and international regulation.

- Investing as a complicity

Some financial institutions are trying to argue that financing or investing is a completely neutral activity. They claim to be neutral, not to be choosing sides. This is of course a total denial of reality.

Investing in a company is clearly an active and supportive effort to raise the capital that is needed to fulfil the plans this company has made. Any financial service delivered to a company by a FI is in fact an approval and a belief in the plans this company is making. Moreover it is a crucial, important and necessary support to the company and its projects and plans.

In some cases a financial institution such as a bank will refuse to offer credit or another financial service to a company because the bank doesn't believe in the company's plan. Amongst other things the argument can be that the FI doesn't believe in the profitability of the company, doesn't believe in the future evolution of the company, or thinks the risks involved in the plans are too high. This clearly shows that financing and investing are active choices, based on a clear assessment of the company and its plans.

In their Report dated November 2003 the Norwegian Government Commission on Ethical Guidelines for the Government Petroleum Fund stated: "Even though the issue of complicity raises difficult questions, the Committee considers, in principle, that owning shares or bonds in a company that can be expected to commit gross unethical actions may be regarded as complicity in these actions. The reason for this is that such investments are directly intended to achieve returns from the company, that a permanent connection is thus established between the Petroleum Fund and the company, and that the question of whether or not to invest in a company is a matter of free choice."

Investing in a cluster munition producer therefore is a choice to support the production of these civilian-killers, and is clearly choosing sides. On the other hand refusing to invest in cluster munition producers is also a clear choice. FIs that develop a policy to no longer invest in these companies are not willing to take responsibility for these kind of weapons and their use. They do not want to bear any complicity in the killing of innocent civilians.

Investors in cluster munition production can be considered as being complicit in the unnecessary killing and maiming of innocent civilians by cluster munitions during and after a conflict.

It's getting closer to home

There is still another dimension to this investment connection. Most of the time banks are using their clients' money to make their investments. Banks have a redistributing function. They collect money from their clients (you and I) in amongst others savings accounts and investment funds. This money is in return used to finance projects and to invest in companies.

This way the story becomes still more frightening. If you are a client of a bank without a restricted investment policy regarding weapons generally or cluster munitions specifically, this means your money could be used to invest in cluster munitions. Most of the time you don't realise it, but still you are earning interest or profit on your account that is partially coming from arms production or cluster munition production.

2. How financial institutions get involved in cluster munition producers

Banks and other financial institutions provide various types of financial services to cluster munition producers. The most important are commercial banking, investment banking and asset management.

In this section we describe concrete financial services delivered by a wide range of international financial groups to six cluster munition producers. These producers are:

- GenCorp (USA): Aerojet, a fully-owned subsidiary of Gencorp, produces the cluster munitions for the ATACMS-missile of Lockheed Martin. Aerojet also produces the solid propellant rocket motor for this rocket. At least until 2004, Aerojet assembled BLU-97 submunitions and integrated them into the AGM-154 A Joint Standoff Weapon (JSOW-A).³
- Lockheed Martin (USA) produces various missiles which can be categorised as cluster munitions, including the MLRS M26 surface-to-surface missile containing 644 M77 submunitions, and the MLRS XM30 rocket containing 404 DPICM submunitions. The M26 rockets have been used by the US Army in Iraq (2003) and by the Israeli Army in Lebanon (2006).⁴
- Raytheon (USA) produces the AGM154 Joint Standoff weapon (JSOW), an air-delivered bomb with some cluster munition variants. For example the AGM154A, the standard version, contains 145 BLU-97/B sub munitions. Also the Tomahawk cruise missile has amongst its variants a submunition warhead.⁵
- Textron (USA), produces the CBU-105 Sensor Fused Weapon, an air-to-surface cluster bomb. This weapon was used by the US Army during the latest Iraq War.⁶
- Thales (France): TDA, a wholly-owned subsidiary of Thales, is a European producer of missiles, amongst others some cluster munitions. TDA admitted to the Norwegian Central Bank that it produces a PR Cargo bomb containing 16 dual effect submunitions. In 2006 Forges De Zeebrugge, a fully-owned subsidiary of TDA, admitted that it is working on a 70mm FZ101 rocket containing eight submunitions for the Tiger Helicopter program of the German army.⁷
- EADS (The Netherlands): Until the end of 2005 TDA was a joint venture by Thales (50%) and EADS (50%). Investment information in this report dates before EADS sold its shareholdings in TDA to Thales.⁸

2.1. Commercial banking

Commercial banking includes all types of corporate loans and credits, i.e. investment loans, working capital facilities, trade credits, et cetera. Banks sometimes dispute the applicability of their anti cluster munitions policy to these services by stating that “a working capital facility is not intended to finance the cluster munitions production itself”. But in concrete none of the corporate loans mentioned in this report include any clause preventing the companies from using the money to support cluster munitions production. And even if such a clause would be included, preventing a company from (legally) reshuffling capital within the group is hardly enforceable.

What follows are some examples of commercial banking services to six cluster munition producers during the last years.

- In December 2004 GenCorp secured a new US\$ 180 million credit facility from a banking syndicate. The facility was split into three tranches: a US\$ 80 million five year revolving credit facility, a US\$ 25 million six year term loan facility and a US\$ 75 million letter of credit facility. The proceedings can be used to repay existing debts and for general corporate purposes. The facility was arranged by **Wachovia Bank** (USA) and **Bank of Nova Scotia** (Canada). Apart from the arrangers two others banks participated in this banking syndicate: **JPMorgan Chase** (USA) and **Bank of New York** (USA). The facility has been amended several times. In June 2006 the facility was amended for the last time. On that occasion the amount of the facility was raised to US\$ 235 million (€ 187.4 million).⁹
- In July 2005 Lockheed Martin renewed a US\$ 1.5 billion (€ 1.24 billion) five year revolving credit facility until July 2010. The banking syndicate for this last facility was arranged by **JPMorgan Chase** (USA) and **Bank of America** (USA). Other banks participating to this syndicate were **Citigroup** (USA), **Mizuho Bank** (Japan) and **US Bank** (USA). The facility can be used for general corporate purposes and to repay existing debts. The revolving credit facility is not used by Lockheed Martin at present, but is intended as an emergency facility which the company can use to pay unexpected expenses and react swiftly to investment or acquisition opportunities.¹⁰
- In March 2005 Raytheon secured a US\$ 2.2 billion (€ 1.7 billion) five year revolving credit facility from an international banking syndicate. The proceedings can be used to refinance existing debts and for general corporate purposes. The facility was arranged by **Bank of America** (USA) and **JPMorgan Chase** (USA). Thirty banks participated in this syndicate.¹¹

ANZ Bank	Australia	US\$ 35 million
BBVA	Spain	US\$ 25 million
Bank of America	USA	US\$ 170 million
Bank of New York	USA	US\$ 35 million
Bank of Nova Scotia	Canada	US\$ 70 million
Bank of Tokyo-Mitsubishi, now part of Bank of Tokyo-Mitsubishi UFJ	Japan	US\$ 100 million
Barclays	UK	US\$ 100 million
Bayerische Landesbank	Germany	US\$ 50 million
BNP Paribas	France	US\$ 100 million
Calyon	France	US\$ 70 million
Citigroup	USA	US\$ 140 million
Commerzbank	Germany	US\$ 50 million
CIC	France	US\$ 25 million
Credit Suisse First Boston	Switzerland	US\$ 140 million
Fifth Third Bank	USA	US\$ 25 million
JPMorgan Chase	USA	US\$ 180 million
KeyBank	USA	US\$ 25 million
Lloyds TSB Bank	UK	US\$ 50 million
Mellon Bank	USA	US\$ 50 million
Mizuho Bank	Japan	US\$ 70 million
Morgan Stanley	USA	US\$ 115 million
Société Générale	France	US\$ 100 million
Sovereign Bank	USA	US\$ 25 million
Sumitomo Mitsui	Japan	US\$ 50 million
RBS	UK	US\$ 100 million
US Bank	USA	US\$ 25 million
UBS	Switzerland	US\$ 100 million

UFJ Bank, now part of Bank of Tokyo-Mitsubishi UFJ	Japan	US\$ 25 million
Wachovia Bank	USA	US\$ 100 million
WestLB	Germany	US\$ 50 million

The revolving credit facility is not used by Raytheon at present, but is intended as an emergency facility which the company can use to pay unexpected expenses and react swiftly to investment or acquisition opportunities.

- In March 2005 Textron Inc. secured a US\$ 1.25 billion (€ 1 billion) five year revolving credit facility from an international banking syndicate. This facility replaces a US\$ 1 billion facility scheduled to expire in April 2007 and a US\$ 250 million 364 day facility expiring in March 2005 and can be used to support issues of commercial paper. The facility was arranged by **Citigroup** (USA) and **JPMorgan Chase** (USA).¹² In April 2006 this credit facility was amended extending the maturity date from March 2010 to April 2011. There was also a shift in the constitution of the syndicate. Nineteen banks are now participating in this syndicate.¹³

Bank of America	USA	US\$ 90 million
Bank of Montreal	Canada	US\$ 45 million
Bank of New York	USA	US\$ 20 million
Bank of Nova Scotia	Canada	US\$ 45 million
Bank of Tokyo-Mitsubishi UFJ	Japan	US\$ 60 million
Barclays	UK	US\$ 90 million
BNP Paribas	France	US\$ 60 million
Citigroup	USA	US\$ 120 million
Credit Suisse First Boston	Switzerland	US\$ 60 million
Deutsche Bank	Germany	US\$ 90 million
HSBC	UK	US\$ 60 million
JPMorgan Chase	USA	US\$ 120 million
Mellon Bank	USA	US\$ 20 million
Merrill Lynch	USA	US\$ 60 million
Morgan Stanley	USA	US\$ 60 million
Société Générale	France	US\$ 40 million
UBS	Switzerland	US\$ 90 million
Wachovia Bank	USA	US\$ 60 million
William Street Commitment Corporation	USA	US\$ 60 million

- In April 2006 Textron Financial Corporation, a wholly owned subsidiary of Textron Inc., secured a US\$ 1.75 billion (€ 1.4 billion) five year credit agreement expiring in April 2011. This credit agreement is used to refinance existing debts. It is an amendment to an earlier US\$ 1 billion five year credit agreement expiring in July 2010. At the same time it replaces a US\$ 500 million 364 day credit agreement expiring in July 2006. **JPMorgan Chase** (USA) arranged this facility.¹⁴
- In January 2005 Thales secured a five-year € 1,5 billion (US\$ 2 billion) loan from an international banking syndicate arranged by **BNP Paribas** (France), **Calyon** (France), **Deutsche Bank** (Germany) and **JPMorgan Chase** (USA). € 60 million will mature in 2009, € 120 million in 2010 and € 1.32 billion in 2011. The loan is used to refinance its August 2001 five-year loan and is supporting Thales's EMTN programme. Under this EMTN programme the company is able to issue bonds with a tenor of three to five years on a regular basis and without too many regulatory requirements. Twenty-eight banks are participating in this new syndicate.¹⁵

ABN Amro Bank	The Netherlands
ANZ	Australia
Bank of Tokyo-Mitsubishi UFJ	Japan
Barclays	UK
BBVA	Spain
BECM, part of Crédit Mutuel	France
BNP Paribas	France
BRED	France
Calyon	France
Citigroup	USA
Crédit du Nord	France
Commerzbank	Germany
Deutsche Bank	Germany
Dresdner Kleinwort Wasserstein	Germany
Fortis Bank	The Netherlands/Belgium
HSBC	UK
HVB, part of Unicredit	Italy
ING Bank	The Netherlands
IXIS, part of Natixis	France
JPMorgan Chase	USA
Lloyds TBS	UK
Mediobanca	Italy
Natixis	France
RBS	UK
Riyad Bank	Saudi Arabia
Sumitomo Mitsui	Japan
Société Générale	France
UBS	Switzerland

- In July 2005 EADS renewed a € 3 billion (US\$ 3.65 billion) seven year revolving credit facility from an international banking syndicate. This facility enables EADS to swiftly borrow money when confronted with unexpected expenses or sudden investment opportunities. The facility is also backing up the EMTN program that allows EADS to issue bonds. The facility was arranged by **ABN Amro Bank** (The Netherlands), **Calyon** (France), **Citigroup** (USA), **RBS** (UK), **BBVA** (Spain), **Bank of America** (USA), **Dresdner Kleinwort Wasserstein** (Germany) and **Société Générale** (France). Thirty-six banks are participating in this syndicate:¹⁶

ABN Amro Bank	The Netherlands	€ 145 million
ANZ	Australia	€ 45 million
Banco Santander Central Hispano	Spain	€ 45 million
Bank of America	USA	€ 120 million
Bank of Tokyo-Mitsubishi UFJ	Japan	€ 85 million
Barclays	UK	€ 85 million
Bayerische Landesbank	Germany	€ 85 million
BBVA	Spain	€ 120 million
BNP Paribas	France	€ 85 million
Calyon	France	€ 145 million
CDC IXIS	France	€ 85 million
Citigroup	USA	€ 145 million
CM-CIC	France	€ 85 million
Commerzbank	Germany	€ 85 million
Commonwealth Bank of Australia	Australia	€ 45 million
Deutsche Bank	Germany	€ 85 million

Dresdner Kleinwort Wasserstein	Germany	€ 120 million
Fortis Bank	Belgium/ The Netherlands	€ 45 million
Helaba	Germany	€ 45 million
HSBC	UK	€ 85 million
HVB, part of Unicredit	Italy	€ 85 million
ING Bank	The Netherlands	€ 85 million
JPMorgan Chase	USA	€ 85 million
KfW	Germany	€ 85 million
Landesbank Baden-Württemberg	Germany	€ 85 million
Mizuho Bank Bank	Japan	€ 85 million
Morgan Stanley	USA	€ 45 miljoen
Natexis Banques Populaires	France	€ 85 miljoen
Royal Bank of Canada	Canada	€ 45 miljoen
RBS	UK	€ 145 miljoen
Société Générale	France	€ 120 miljoen
Sumitomo Mitsui	Japan	€ 45 miljoen
Toronto Dominion	Canada	€ 45 miljoen
UBS	Switzerland	€ 85 miljoen
WestLB	Germany	€ 45 miljoen
WestPac	Australia	€ 45 miljoen

2.2. Investment banking

Investment banking services include helping clients to sell shares and bonds to investors (asset managers, insurance companies, et cetera), as well as financial advisory services.

What follows are examples of investment banking services to two cluster munition producers during the last years.

- In March 2005 Textron Inc. issued eight year bonds with a total value of € 300 million (US\$ 362 million). The proceedings were used to repay the existing € 300 million notes expiring in March 2005. The lead managers of the issuing syndicate were **Deutsche Bank** (Germany) and **JPMorgan Chase** (USA). Six banks underwrote this issue and participated for the following amounts:¹⁷

Bank of America	USA	€ 24 million
Deutsche Bank	Germany	€ 111 million
HSBC	UK	€ 15 million
JPMorgan Chase	USA	€ 111 million
Mitsubishi	Japan	€ 15 million
Société Générale	France	€ 24 million

- In December 2006 Thales issued three year bonds with a total value of € 700 million (US\$ 906 million). The proceedings can be used to repay existing debts and for general corporate purposes. The lead managers of the issuing syndicate were **BNP Paribas** (France), **Calyon** (France), **HSBC** (UK), **Natixis** (France) and **Société Générale** (France).¹⁸

2.3. Asset management

Asset management means investing in shares and bonds of companies and governments, on behalf of investment funds (which in turn are owned by many private investors), wealthy private clients and financial institutions such as pension funds and insurance companies.

Asset management can result in a direct and indirect involvement of FIs in cluster munition producers.

Indirect involvement means that the FI buys shares and bonds of a company on behalf of a third party. Most of the time this means the third party, a person or an institution, is buying one or more shares of an investment fund offered on the market by the FI. This fund is managed by asset managers of the FI following a certain investment policy. Nothing stops these FIs from avoiding the inclusion of cluster munition producers in the portfolio of their funds.

Direct involvement means that the FI is buying shares and bonds of a company on their own behalf (for their own account). This means the FI itself is becoming shareholder or bondholder of this company. Again nothing stops FIs from avoiding including cluster munition producers in their own portfolio.

Asset managers sell and buy shares and bonds of many companies and claim that they do not have the means to check quickly and cost-effectively if these companies are cluster munition producers. Closer co-operation and information sharing with NGOs and non-financial or SRI advisors resulting in clear and updated black lists of companies are a perfect solution to this 'problem'.

What follows are some examples of asset management resulting in significant shareholdings by FIs in four cluster munition producers during the last years.

- In September 2006 the following financial stakeholders were holding more than 4% of the shares of GenCorp¹⁹:

Pirate Capital	USA	9.0%
Sandell Asset Management	USA	7.0%
Gamco Investors	USA	5.6%
Sowood Capital Management	USA	5.1%
Keeley Asset Management	USA	4.4%
Barclays	UK	4.3%

- In September 2006 the following financial stakeholders were holding more than 3% of the shares of Lockheed Martin:²⁰

State Street	USA	18.88%
Barclays	UK	6.67%
Wellington Management	USA	5.44%
Marsico Capital Management	USA	4.55%
MFS Investment Management	USA	3.29%
Fidelity	USA	3.00%

- In September 2006 the following financial stakeholders were holding more than 3% of the shares of Raytheon²¹:

Barclays	UK	3.85%
Legg Mason	USA	3.77%
Capital Group	USA	3.65%
State Street	USA	3.60%
Harris Associates, part of Natixis	France	3.44%
NWQ Investment Management Company, part of Nuveen Investments)	USA	3.02%
Lord Abbett	USA	3.01%

- In September 2006 the following financial stakeholders were holding more than 3% of the shares of Textron²²:

AXA	France	7.57%
Barclays	UK	3.09%
State Street	USA	3.05%

How to find out if your bank is investing in cluster munition producers?

'Well, let's ask them', would be a quite logic first step. Unfortunately your bank will probably try to avoid the question. It is our experience as campaigners that the answers most bankers are giving to worried clients are incomprehensible, and talk around the problem. Banks seem to give clients the impression they care by for example showing general business principles. Knowing that there is a difference between business principles and business practice, general answers cannot guarantee any certainty.

The main problem is that banks have been building up a wall of what they call 'confidentiality'. The result is a total lack of transparency and accountability. In most countries the law-maker has not been a great help in resolving this problem of transparency. The financial sector is totally lagging behind when it comes to transparency.

This lack of transparency plays a role on different levels:

- The policy level: what is the investment policy of my bank related to the arms industry or cluster munition producers?
- The implementation level: if there is a policy, there surely ought to be clear information about the way the bank is implementing this policy. How is my bank doing it?
- The transaction level: stakeholders should be able to find the names and details of the major transactions a bank has done. What's my bank investing in?

Consequently researching the financial links between FIs and cluster munition producers is a difficult task. You need expertise and a lot of patience to go through company yearly reports, announcements to stock market authorities, press releases, business newspapers and magazines, et cetera ... And most of the time you need access to quite expensive databases and search machines.

The following organisations are able to help you out with their experiences and expertise on this topic:

- *Netwerk Vlaanderen*, www.netwerkvlaanderen.be, *Christophe Scheire*, +32 2 201 07 70, christophe.scheire@netwerk-vlaanderen.be.
- *BankTrack*, www.banktrack.org, *Johan Frijns*, +31 30 2334343, coord@banktrack.org.
- *Profundo*, www.profundo.nl, *Jan Willem van Gelder*, +31 251 65 83 85, jw@profundo.nl

3. Financial Institutions disinvesting from cluster munitions

3.1. Low standards of responsibility

Generally spoken the financial sector is rather reluctant to disinvest from weapon producers generally or cluster munition producers specifically. This reluctance has various explanations:

- Some FIs simply don't care about cluster munitions and their impact on civilians.
- Most FIs are not recognising any responsibility for the investments they are making. Too often social, environmental or ethical criteria are not taken into account when decisions on investing or financing have to be made.
- Some FIs view ethics in terms of 'complying with the law'. As until now cluster munitions are not forbidden, they argue that they can simply go on investing in cluster munition producers. This way they are putting the responsibility on the government.
- Most of the arguments above are hiding the real reason. Most FIs don't want to lose the big clients. Cluster munitions are produced by some of the biggest arm producers in the world. Amongst others Lockheed Martin, Thales and Raytheon are 'big shots' on the market. Moreover the arms industry has been a high-return sector during the last years.
- Some FIs refer to their ethical saving and/or investment products to serve their ethical 'non-weapon loving' clients. In this way they shift the responsibility to the client. But this does not of course lessen the responsibility of the FIs themselves. Moreover not all ethical financial products offer an alternative to these clients. Recent research by Netwerk Vlaanderen on ethical financial products in the Belgian market has revealed that some ethical portfolios even contained cluster munition producers.

This general low standard of responsibility within the financial sector is regrettable. And it is even more regrettable when you realise the sector as a whole has a large potential to put pressure on companies.

Although there is a general low standard of responsibility, there are some FIs that clearly try to avoid any involvement in cluster munition producers. These can be divided in two categories: the ethical banks and mainstream FIs.

3.2. Best practice by ethical banks

Most of the time ethical banks are small banks, founded with the pronounced aim to serve as a capital source for sustainable projects and companies. Sustainable energy, organic food and cultural activities are examples of specific sectors in which these banks invest. By their nature, these banks do not most of the time get involved in arms production. Above this they have elaborated policies to avoid investments in 'unethical sectors', like arms production, gambling et cetera.

What follows are some examples of ethical banks staying out of cluster munitions.

- **ASN Bank**
In the Netherlands ASN Bank, with € 3 billion managed assets in 2005, has a total exclusion criterion for weapon producers, both for financing and asset management. Moreover ASN Bank is offering complete control tools for their ethical policies. They publish their complete investment universe on their website, with a short description for each company. The annual report of the bank includes not only the investment criteria, but also a description of the companies that are allowed, not allowed, and removed from possible investment.²³

- Co-operative Bank

The British Co-op Bank, managing £ 11.9 billion on savings accounts, does not invest in any way in companies that supply arms to 'oppressive regimes'. Co-op Bank also has some subsidiary positions regarding weapon industry, excluding investments in cluster munition or nuclear weapon producers.²⁴

- Triodos Bank

Triodos Bank is an ethical bank active in Belgium, the Netherlands, Germany, Spain and UK. At the end of 2005 Triodos had almost €2.3 billion assets under management. The bank completely excludes involvement in the weapon industry for both investments and financing. Moreover Triodos offers a complete insight into its investment universe and financing transactions on their websites.²⁵

3.3. Best practices by mainstream financial institutions (private or government)

But during the last years some mainstream financial institutions have also been reconsidering their involvement in the arms industry and in cluster munitions production. For some of them this resulted in a clear disinvestment decision concerning cluster munition producers.

- Norwegian Pension Fund

In Norway the Government Pension Fund – Global is set up to manage all the state's oil revenues. The state uses part of this money each year to balance the budget. But even more importantly, this fund is seen as an important 'savings account' for future Norwegian generations. Predictions show that Norway will not be able to keep relying on its large oil reserves in the future. In mid-2006, the fund had a market value of NOK 1,505 billion (€ 190.6 billion).²⁶

In 2004 the Norwegian Government adopted Ethical Guidelines for the Government Petroleum Fund. These guidelines included: "exclusion of companies in which there is deemed to exist an unacceptable risk of contributing to violations of fundamental humanitarian principles, gross violations of human rights, gross corruption or severe environmental degradation."²⁷ The Norwegian Parliament considers that cluster weapons are in violation of fundamental humanitarian principles by breaching the principle of distinction between military and civilian targets. Other weapon systems excluded under these ethical guidelines are anti-personnel mines, nuclear weapons, chemical and biological weapons, incendiary weapons and blinding laser weapons.

In the summer of 2005 the Fund excluded eight companies from its portfolio because they were considered to manufacture key components for cluster bombs. These companies are: Alliant Techsystems, EADS, EADS Finance, General Dynamics, L3 Communications, Lockheed Martin, Raytheon and Thales. Disinvestment from these companies totalled almost NOK 2.2 billion (€271.8 million).²⁸ In April 2006 the Ethical council recommended that the Fund no longer exclude EADS on the grounds of involvement in cluster munitions, as since the end of 2005 EADS is no longer owner of the French based cluster munition producer TDA. But the exclusion of EADS was upheld on grounds of the company's involvement in nuclear weapons.²⁹ In December 2006 the Fund excluded the South-Korean company Poongsan from its portfolio due to its involvement in the production of cluster munitions.³⁰

These decisions by the Norwegian Government are not only important because of the large amount of assets managed by the Fund. They are also an example of government best practice. There is a clear lack of consistency and double standards if a country that is opposed to the use of cluster munitions is using government managed funds to invest in cluster munition producers.

Another credit to the Norwegian Government is its full transparency on this issue. The recommendations by the Ethical Council to the Pension Fund are published and decisions by the Government are publicly announced in press releases.

- KBC

KBC is a Belgium-based bank-insurance group with € 196 billion assets under management. In 2004 they worked out a policy on investments in the weapon industry. They decided to stop any investments in anti-personnel mines, chemical weapons, uranium weapons and cluster munitions. KBC argues “these weapons have caused great suffering to innocent civilians”.

Their policy is applicable to all their activities including commercial banking, asset management and investment banking. KBC has not only worked out a clear and concrete policy, it has also implemented this policy in a strict and thorough way. In 2006 they updated their black list resulting in a publicly available list of nineteen weapon producers. KBC mentions seventeen of them as producers of cluster munitions: Aerostar, Alliant Techsystems, Aselsan, BAE Systems, EADS, Finmeccanica, Gencorp, General Dynamics, Honeywell, L-3 Communications, Lockheed Martin, Magellan Aerospace, Northrop Grumman, Poongsan, Raytheon, Rheinmetall and Thales. Singapore Technologies Engineering and Textron are excluded on the grounds of involvement in anti-personnel mines.

In response to the Belgian campaign ‘My Money. Clear conscience?’ by Netwerk Vlaanderen and some Belgian peace organisations, KBC has been the only bank to implement this restrictive policy to all their investments (including indirect investments). Moreover it has been the only bank that has delivered quasi-total transparency both on the policy and on the implementation level.

Other results of the Belgian Campaign ‘My Money. Clear Conscience?’ are the new arms investment policies adopted by the banking groups Dexia, Fortis and ING. All these policies include disinvestment from cluster munitions. But unfortunately these policies have a more limited scope. They do not apply to the indirect investments by these banking groups. In this way these groups are still offering investment funds including cluster munition producers’ shares or bonds to their clients. These are not mere details. For example, in 2004 ING managed an amount of more than € 800 billion. More than 40% (€ 330 billion) was managed through indirect investments.

Apart from this, within some banks there sometimes seems to be a serious gap between the paper promises contained in their ethical policies and the concrete implementation on the investment floor. Some banking policies include loopholes that limit the effect of ethics on their ‘freedom to invest’.

Two examples:

The weapons investment policy adopted by ING and Fortis in the spring of 2005 included some exceptions. ING makes an exception for primarily civilian companies involved in controversial weapons. Fortis makes an exception in its policies for conglomerates: “...financing is possible, herewith excluding the controversial activities.”

After some months both banking groups used these loopholes to drop ethical concerns in favour of commercial interests. In July 2005 ING and Fortis participated in a €3 billion seven year credit facility to EADS. This facility allows EADS to borrow money quickly when the company is confronted with exceptional costs or investment opportunities. Fortis contributed €45 million to this facility, ING €85 million. EADS is the second biggest European arms trader and a producer of nuclear weapons and cluster munitions. Both weapon systems are excluded in the Fortis and ING policy. Neither of these banks has been able to obtain any promise or contract clause from EADS stating that the proceeds of this facility will not be used to support cluster munitions or nuclear weapon activities.

It's clear that both banks' policies have been written to allow this kind of highly lucrative deal or important clients. Although both banking groups are seriously and adequately working on the implementation of their weapon investment policy, these kind of 'accidents' reflect a 'business as usual' mentality.

Of course we cannot afford to measure the progress banks are making in this field by good intentions or even strong policies on paper. What we are looking for is improved performance and results on the ground. In the case of cluster munitions, banking groups should be reminded that 98% of the victims are innocent civilians.

- Storebrand

Storebrand is a Norwegian financial holding with three main activities: banking, asset management and insurance. Storebrand manages assets worth NOK 209 billion (€25.8 billion). Storebrand Investments excludes producers of cluster munitions from all of their investment portfolios. This policy applies to all direct investments made by all subsidiaries of the group, but also to all investment funds managed by the group. Storebrand does not publish the list of producers it has excluded from its portfolios, but in January 2007 six companies were excluded because of their involvement in cluster munitions.³¹

4. Regulatory/ legislative initiatives and tools

Based on the research results revealed in this paper, and several campaigning and research experiences, we can conclude that self regulation by the financial sector only leads to rather patchy results. The wide majority of financial institutions around the world do not seem to take up any responsibility. Some pioneers have indeed taken the decision to disinvest from cluster munition producers. Amongst them there is still a big difference in the effectiveness of their policies.

Although investments in arms and cluster munitions have become an important topic within the social responsibility divisions of international banks, the allocation of capital resources towards cluster munition production has until now never been in danger. Stemming the capital flow towards cluster munitions will therefore need strong international regulation and legislation.

Unfortunately there doesn't seem to be a tradition of legislation placing restrictions on investment opportunities. On the contrary, economic liberalisation and the globalisation of the financial sector have dramatically loosened the grip governments have on the allocation of financial resources. Although banks often argue that governments and not banks should decide if investments in certain sectors should be forbidden or not, they don't seem very keen on restrictive legislation when MPs are intending to introduce laws on this issue.

Governments can of course deliver best practice examples themselves. The ethical guidelines given to the Norwegian Pension Fund and the investment decisions that followed it are a good example. Governments cannot afford double standards by opposing the use of cluster munitions, while their own government funds invest in cluster munition production.

Moreover a government simply cannot morally allow investments to be made by its resident financial institutions that are in total opposition to its principles or policies. Therefore any governmental effort to fight the misery connected to the use of cluster munitions should include efforts to dry up the capital flows towards cluster munition production and trade.

During the last years there have been signs that some politicians have taken up this challenge.

- In July 2005 a European Parliament Resolution “Calls on the EU and its Member States to prohibit through appropriate legislation financial institutions under their jurisdiction or control from investing directly or indirectly in companies involved in production, stockpiling or transfers of anti-personnel mines and other related controversial weapon systems such as cluster sub-munitions;”
- At the end of 2006 and after years of campaigning by Netwerk Vlaanderen, the Belgian Senate voted in favour of a law proposal forbidding any investment in cluster munition producers by Belgian financial institutions. (“Financing a Belgian or foreign company active in production, usage, repair, offer, sale, delivery, import, export or stocking of submunition in the sense of this law, is also forbidden.”) The law proposal also instructs the Belgian government to produce a list of cluster munition producers. In February 2007 the law proposal was scheduled to be discussed and voted upon by the Belgian Chamber. Adopting this law would make Belgium the first country banning investments in cluster munitions. In 2005 Belgium already became the first country to forbid investments in anti-personnel mines and in 2006 it became the first country to ban the production of cluster munitions.

As forty states are adding their weight to a Norwegian initiative for an international treaty on cluster munitions, the time is right to discuss the investment issue. The 1997 Ottawa Treaty on anti-personnel mines stated in article 1.c “Each State Party undertakes never under any circumstances to assist, encourage or induce, in any way anyone to engage in any activity prohibited to a State Party under this Convention.” Unfortunately almost no state party has ever interpreted investing in anti-personnel mines production as an 'assistance' or an 'encouragement.'

Consequently financial flows from signatory countries have sustained the production of anti-personnel mines. This double standard could be avoided in the upcoming 'Oslo Treaty' by including investment and financing in the forbidden actions concerning cluster munitions.

Stemming capital flows to cluster munition production can be a strong tool in the fight against the fatal impact this weapon has on numerous human lives around the world.

Credits

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Netwerk Vlaanderen vzw promotes an alternative approach to money. Money is an instrument that – if applied well – can promote a sustainable and honest society. For the past few years, Netwerk Vlaanderen has been running the campaign 'My Money. Clear Conscience?' to make the investment policies of the banks public, and enforce the participation of the saver and investor in the destination of their money. Netwerk Vlaanderen provides information on sustainable investment and savings products, and supports and advises organisations and companies who (wish to) have a socially and environmentally friendly approach to money.

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Netwerk Vlaanderen is a member of the Cluster Munition Coalition, a network of civil society organisations campaigning against cluster munitions.

Netwerk Vlaanderen is a member of BankTrack, an international movement for sustainability in the financial sector.

Other publications by Netwerk Vlaanderen on investments in cluster munitions:

- Explosive Portfolios – Bank Groups and Cluster Munitions, July 2006.
- Banks Disarm(ed) – An Overview of the Results of the Campaign 'My Money. Clear Conscience', April 2005.
- Cluster Bombs, Landmines, Nuclear Weapons and Depleted Uranium Weapons – A Report on the Financial Links between Banks and the Producers of Controversial Weapon Systems, April 2004.

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