

DEFINITIONS AND TERMINOLOGY

The following document provides definitions and explanations of terminology that is used in the *Worldwide Investments in Cluster Munitions; a shared responsibility report*

1. FINANCIAL ACTIVITIES

Investments

Forms of investments include:

- loans and other forms of credit
- underwriting or issuing of shares and bonds
- investment in shares and bonds
- other financial services

Commercial Banking (loans)

Commercial banking includes offering or participating in loans to cluster munitions producers via general corporate finance or project finance.

Most of the time if big companies are securing loans, these loans are not offered by one single bank, but by a banking syndicate made up of a number of banks. The involvement of a banking syndicate is mostly due to the loan being very large. In such a banking syndicate a number of banks will arrange the loan and will negotiate with the company on all the conditions and characteristics of the loan, and will look for other banks in the market to complete the needed amount of money for the loan.

A loan is a very close and conscious link between a bank and a company. Before a loan contract is secured, the bank and the company will have negotiated several times about the conditions of the loan.

Traditionally, weapon producers finance their cluster munition facilities from their general corporate capital. General corporate loans can play an important role in financing.

Investment banking (arranging/issuing shares/bonds)

Investment banking services include helping cluster munition producers to sell shares and bonds to investors (asset managers, insurance companies, etc.), regardless of the use of the proceeds (most of the time general corporate services) as well as financial advisory services.

The issuing of shares and bonds is usually delegated to one or some banks, again after negotiations between company and arrangers are complete. These latter banks arrange the issue and then look for other investors to form a banking syndicate. All members of the banking syndicate underwrite the issue for a certain amount. This means that on the day of issue, all underwriting investors will buy the companies' shares or bonds for their respectively negotiated amount. Once the issue contract is signed the company is able to sell all the issued shares or bonds to the underwriting investors. The underwriters will often then try to sell the bonds or shares to other investors in the capital market.

Asset Management

Asset management means holding or managing stocks (= shares) or debt securities (=bonds) of cluster munition producers, either on the investors behalf, or on behalf of third parties (which includes the development and/or sale of investment funds containing stocks or debt securities from CM producers).

Most of the time holding or managing stocks or debt securities of a company does not imply a close relationship between the investor and the company. Investors on the market change their asset management portfolio on a day-by-day basis by selling and buying stocks and debt securities on the market.

However, some investors do have close relationships with companies as they are substantial and/or stable shareholders of the company. Holding a substantial amount of shares in a company usually gives an investor more voting power in the annual shareholders meeting and in some cases a strong influence on the policy of a company, sometimes even a seat on the Board of Directors.

Asset management can result in direct and indirect involvement of financial institutions in cluster munition producers.

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

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

Asset managers buy and sell 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 can result in clear and updated black lists of companies which is a perfect solution to this 'problem'.

2. FINANCIAL INSTITUTIONS

Examples of financial institutions are major banks, insurance companies, pension funds, sovereign wealth funds and asset managers.

Bank

A bank is a financial institution licensed by the government. Its primary activities include borrowing and lending money however many other financial activities have been allowed over time. For example, banks are important players in financial markets and offer financial services such as investment funds. Most banks offer investment banking services, commercial banking services and asset management.

Ethical Banks

Ethical banks are usually small banks, founded with the aim to serve as a source of capital for sustainable projects and companies. Sustainable energy, organic food and

cultural activities are examples of specific sectors in which these banks invest. These banks tend not to get involved in arms production. In addition, they have detailed procedures to avoid investing in 'unethical industries', like arms production, gambling etc.

Discretionary Mandate

A discretionary mandate gives asset managers the authority to manage the assets on behalf of a client in compliance with a pre-defined set of rules. This mandate is limited and specific to a single investor.

Funds following an indexⁱ

A fund following an index is a type of mutual fund; its portfolio is designed to track the components of a market index. A market index is an imaginary portfolio of securities representing a particular market or a portion of it. The fund follows a chosen index and invests in the companies on that index.

Fiduciary Dutyⁱⁱ

The person looking after the assets on the other's behalf is expected to act in the best interests of the person whose assets they are in charge of. This is known as "fiduciary duty".

Insurance Companyⁱⁱⁱ

An insurance company provides financial protection or compensates individuals or entities against losses. The company pools client risks to make payments more affordable for the insured. The company reinvests the premiums clients pay to obtain the money for compensation.

Investments are loans and other forms of credits, underwriting or issuing of shares and bonds, investment in shares and bonds, and other financial services.

Mutual Fund^{iv}

An investment vehicle that is made up of a pool of funds collected from many investors for the purpose of investing in securities such as stocks, bonds, money market instruments and similar assets. Mutual funds are operated by money managers, who invest the fund's capital and attempt to produce capital gains and income for the fund's investors. A mutual fund's portfolio is structured and maintained to match the investment objectives stated in its prospectus.

Pension Fund

A pension fund is a pool of assets forming an independent legal entity. Pension fund contributions have the exclusive purpose of financing the pension plan benefits to which they give a right.

Public Pension Fund

A public pension fund is regulated under public sector law. A private pension fund is regulated under private sector law. In some countries the distinction between public or government pension funds and private pension funds may be difficult to assess.

Retail Fund^v

A retail fund refers to the market and clients of the fund. A retail fund is a fund that individuals can invest in directly or through a financial adviser. Institutional funds, on the other hand are available to large investors, such as pension funds and not-for-profit organizations with substantial amounts to invest.

Sovereign Wealth Fund^{vi}

A Sovereign Wealth Fund (SWF) is a state-owned investment fund composed of financial assets such as stocks, bonds, real estate, or other financial instruments funded by foreign exchange assets. SWFs can be structured as a fund, pool, or corporation. Some funds also invest indirectly in domestic, state owned enterprises. In addition, they tend to prefer returns over liquidity, thus they have a higher risk tolerance than traditional foreign exchange reserves.

3. VARIA

Important to know is that numbers are written differently in Anglophone countries than in others. Moreover, points and commas are differently used.

For example three thousand four hundred fifty dollar point forty five:

Anglophone countries: US\$3,450.45

Other countries: US\$3.450,45

ⁱ Definition taken from Investopedia (www.investopedia.com), viewed 25 March 2011.

ⁱⁱ Definition taken from Investopedia (www.investopedia.com), viewed 12 April 2012.

ⁱⁱⁱ Definition taken from Investopedia (www.investopedia.com), viewed 25 March 2011.

^{iv} Definition taken from Investopedia (www.investopedia.com), viewed 25 March 2011.

^v Definition taken from Investopedia (www.investopedia.com), viewed 25 March 2011.

^{vi} For the definition see the Sovereign Wealth Funds Institute (www.sfwainstitute.org), viewed 25 March 2011.