



Good'n' Plenty

You can get good returns on an investment portfolio in sync with your personal values. *By Ann Monroe*

FOR A GROWING NUMBER of investors, creating a portfolio that performs well is only half the battle. Sure, they want their money to do well, but they want it to do good, too. They want their investments to march hand in hand with their principles, not work against them. ♦ Until recently, the common wisdom was that—noble though it may be—such an investment philosophy was fiscally foolish. Anytime you narrow the universe of investable options, the argument went, you

cut your potential returns. Certainly the performance of some of the well-known socially responsible mutual funds didn't do much to disprove that argument. A November 1997 report by Morningstar Mutual Funds ranked these funds in the bottom third of most of their categories, based largely on the dismal performance of several offerings from Calvert Group, one of the oldest socially responsible investing (SRI) companies.

But that attitude is changing—fast. The eight-year-old Domini Social Index of 400 companies has outperformed the Standard & Poor's 500 index over the past one-, three-, and five-year periods. A growing body of academic research indicates that screening for social responsibility, by itself, has no effect on performance. And a handful of social funds are beating not only the S&P 500 but most of their non-SRI rivals as well.

Social-investing advocates insist that's only to be expected. "Social research is a very in-depth form of qualitative research," says Sophia Collier, chairwoman of Citizens Funds, whose Citizens Index Fund recently got five stars from Morningstar—the first social fund to get that accolade. (For an article by Collier on reviewing companies' human-rights records, see *Voices*, December 1997.)

Other factors, too, make social investing more attractive now. For one thing, more and more talented managers are being drawn to the discipline as more and more investors put their money where their consciences are. According to the Social Investment Forum, a social-investing trade group, assets in screened portfolios rose 227 percent from the beginning of 1995 to the end of 1996. (For the same period, investment as a whole grew 84 percent, the forum says.)

Those figures have piqued the interest of mainstream firms. Merrill Lynch, for instance, recently launched a socially responsible unit-investment trust. At least two brokerage firms, Salomon Smith Barney and Prudential Securities, offer social-investing services. The field even has venture-capital funds and an angel network. In another sign of the mainstreaming of social investing, Calvert, eager to repair its reputation,

hired a new president from Alliance Capital in April 1997 and has introduced an SRI-enhanced index fund tied to the Russell 1000. With all these choices, social investors no longer have to settle: If performance sags at one fund, they can take their money elsewhere.

The universe of stocks suitable for the socially conscious has also grown in the past decade, notes Steve Schueth, president of the Social Investment Forum. "Think back to Earth Day of 1990," he says. "The environment became top of mind for many companies. The changes may not have been as big as their ads suggest, but relative to past practices and behavior, they were very dramatic." Socially correct portfolios need no longer be limited to Ben & Jerry's, the Body Shop, and a handful of solar-power companies; the Citizens Index includes some 200 of the S&P 500.

This plethora of choices has a downside, though. With so many social-investing options, how do you begin?

You begin, say money managers, by figuring out just why you're interested in social investing. Are you passionate about a single issue, like animal rights or abortion? Or do you have a broad vision in which various issues jockey for top place?

The point is to develop your own personal social screen. It could be a negative one—avoiding, for instance, the so-called sin stocks: alcohol, tobacco, and gambling. Or it could weigh pros against cons. "There's no such thing as a perfect company," says Peter Kinder, president of Kinder, Lydenberg, Domini, the money-management firm that devised the Domini Index and runs its associated fund, the Domini Social Equity fund. "Good social investors tend to acknowledge grays."

Here's an example: RJR Nabisco, one of the premier sin stocks, also turns up on at least one list of companies with family-friendly workplaces. "If investors are screening for more than one issue, they are going to have to figure out which takes dominance," says Suzanne Harvey, director of Prudential Securities' social-investment research service.

One approach is to ask where the company has the biggest impact. For RJR, you might decide that its cigarette sales, which affect all its customers, weigh more heavily than its good treatment of a much smaller number of employees.

Another approach is the "best-of-industry" policy. That's the tack many investors take toward the energy and pharmaceutical stocks. Both industries are harmful to the environment, but some companies work harder than others to minimize the damage. By that criterion, you might decide that RJR shows more social conscience than any other tobacco company and invest in it.

You also need to decide how willing you are to compromise. The universe of socially aware companies is big enough that most investors can assemble an ethically

satisfactory portfolio without sacrificing performance. But even fervent social-investing advocates advise against excessive rigidity. Military contracts, for example, are so common that if you eliminate every company holding one, you will jeopardize your returns, warns John Guerard, author of a seminal 1997 social-investing study in the *Journal of Investing*. Patrick McVeigh, a senior vice president at SRI adviser Franklin Research & Development, tells of a client so ardent about animal rights that he wouldn't even buy airline stocks, since airlines serve meat to passengers. "We ran some scenarios to give him an idea of what would happen when he eliminated 50 percent of the S&P 500," McVeigh says ruefully. "He ended up keeping his money in cash investments."

Once you've set your social priorities, how do you match them to investments? If you want someone else to make the choices for you, you can leave the specifics to either a mutual fund or a money manager. Both are easy to find (see box for Web sites that will give you leads on these as well as other social-investing info). You'll need to make sure the fund's screens match your own reasonably well; many funds describe their screens on the Internet, and all put them in their marketing material. Given the returns racked up by offerings like Citizens Index, Domini Social Equity, and Dreyfus Third Century (all better than 20 percent over the past three years), it

The universe of socially responsible stocks has grown in the past decade

Social In-Sites

The Internet is one of the best places to begin exploring the world of social investing. Here are some helpful Web sites.

GENERAL SITES

- ◆ www.goodmoney.com: a good all-around SRI site, with lots of links.
- ◆ www.socialinvest.org/sriguide/mfpc.htm: the Social Investment Forum's SRI fund ranking; also includes some SRI bank products.
- ◆ www.coopamerica.org/mfsc.htm: how each fund screens; a chart from Co-op America.
- ◆ www.coopamerica.org/gp/: Co-op America's searchable directory of SRI brokers and money managers; keyword: *financial consultants*.
- ◆ www.frdc.com/: general information about Franklin Research & Development,

including sample profiles and subscription information.

STOCK LISTS

- ◆ www.domini.com/400StocksA-L598.html: stocks in the Domini Index.
- ◆ www.citizensfunds.com/300_Profiles/index.htm: companies in the Citizens Trust Index, with links to their Web sites.
- ◆ www.goodmoney.com/wpубco.htm: a broad list of good-guy companies.
- ◆ www.goodmoney.com/aframer.htm: public companies owned or majority held by African Americans.
- ◆ www.workfamily.com/model.htm: Work and Family Connection's model-company profiles (including RJR Nabisco).
- ◆ www.bsr.org: Business for Social Responsibility helps firms create socially responsible policies.

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shouldn't be hard to find a fund that satisfies you both ethically and financially.

For more control than you get with a fund, choose a money manager who will create a portfolio to suit your concerns. Salomon Smith Barney runs tailored social-investing managed portfolios as small as \$50,000. Co-op America and the Social Investment Forum have lists of social-investing money managers; you can also get a referral from socially responsible financial adviser First Affirmative Financial Network.

Picking your own stocks is much harder. A lot of top-quality social-investing research is being done, but most of it is available only to professionals. An exception is Prudential, one of the few brokerage firms with a social-investing research department; it will run multiple screens to come up with stocks that fit a client's social specifications. Or you could look for a money manager interested in principled investing who's willing to share research but let you do the stock selection.

Money managers are split on whether to pick financially attractive stocks first and then screen them socially, or vice versa. Citizens Funds used to start with the finances, says Collier, but found it difficult: "Say you want a retail company. Wal-Mart has problems, so you pick Kmart. But they have union and gun problems. You end up with the most beaten-down retail name on Wall Street." It's much more satisfying, she says, to screen first, then pick the most attractive companies on the list.

If you're willing to trust others' judgment, lists of socially screened stocks are available, some of them annotated. You can also look at the companies in the Domini or Citizens index or check out what a mutual fund you like holds. (The hands-down favorite: Merck, owned by four of the six biggest social-investing funds; other popular stocks include Microsoft, Intel, Fannie Mae, and Coca-Cola.) And for as little as \$29.95 a year, Franklin Research's monthly newsletter *Insight* offers a recommended SRI portfolio, tracks previously recommended stocks, ranks mutual funds, and includes research reports on several companies

per issue. You also get e-mailed updates.

As you assemble your portfolio, remember that the social-investing universe is a bit skewed—heavy on technology, financial services, and retail and light on resource-intensive industries like energy and mining. There are exceptions, though: Pax World Fund's top 10 holdings include Enron, Bay State Gas, KeySpan Energy, and Peoples Energy. But whatever your screens, you'll wind up with a lot of intriguing companies

reflected in its stock price. It starts up—and then spins off to employees and the public—subsidiaries supposed to profit by solving social problems (see "Get Into an Incubator," December 1997). "At current prices," McVeigh says, "it's pretty attractive." Other stocks on Franklin's list: BankAmerica, Norfolk Southern, and, yes, a solar-power company, Spire. Also popular with social investors is Interface, a commercial-carpet company with a gimmick: Instead of selling its floor coverings, it leases them. Interface's position is that it's responsible for its products as long as they exist.

At the smaller end of the scale is Shaman Pharmaceuticals, an ethnobotanical-drug-discovery company. Shaman, which went public a few years ago, finds natural drugs used in nonindustrial communities and tries to replicate the active compounds commercially. So far, however, none of its products has completed clinical trials, and the company has yet to make money.

This illustrates what George Gay, president of First Affirmative, describes as the main hazard of this type of investing: falling in love with a good story. "Social investors really want these companies to succeed," Gay says. "But there are a lot of companies out there marketing social values that haven't made a dime."

Gay's lesson—that social investing has to be done with the head as well as the heart—is key. But with all the new options available to social investors, the flip side is equally true: Putting a conscience in your portfolio can be a profitable move. What's more, it can bring a new interest to the often dry job of weighing alternative investments.

"If you're an owner, you're responsible for how the business is run," notes McVeigh, who sometimes raises social issues in annual meetings on behalf of clients. "That's the fun part of the job, and we believe it makes a difference."

The related articles mentioned above are available at www.bloomberg.com.



to choose among. Here's a taste:

Coca-Cola may "sell sugar water to the Third World," concedes Collier. But it also makes its water-purification plants available to the community. "They are an economic engine in the emerging world."

One of Franklin's recommendations is AES Corp., a leader in the independent power industry. Its plants are locally run and budget funds for community projects. In Oklahoma, AES shelled out for a new school after voters refused three times to raise taxes, says McVeigh.

Franklin's largest holding is Thermo Electron. The company is so diversified that it's hard to understand, a problem