Investing for a Better World

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INSIDE

Sold on Social Responsibility: The Sell Side Finally Buys into CSR

By Steve Lippman

For all its gains over the past twenty-five years, socially responsible investing has remained firmly entrenched on the buy side of Wall Street. Now there are welcome signs that's changing.

(With apologies to those who already know this nomenclature – mutual funds, asset managers like Trillium Asset Management and individual investors are considered the "buy side" of Wall Street, while brokerage houses that issue research on particular stocks are considered the "sell side.")

Until recently, almost all the activity around socially responsible investing centered on the buy side of the street – socially screened mutual funds proliferated, assets managed under SRI strategies accumulated, and a growing number of individuals and institutions embraced socially responsible investing. All the while, big brokerage houses typically ig-

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Battle for the Soul of Organic

By Shelley Alpern

The average American consumer is long overdue access to affordable organic foods. Yet **Wal-Mart's** pledge to squeeze the typical premium paid for organic foods from 20-30% down to 10%[1] is making a whole lot of people very nervous. Wal-Mart's modus operandi is to keep prices low by driving down costs in the production chain and keeping its own wages low; its competitors' practices are variations of the same theme, if less cutthroat. Good ol' American-style capitalism and its frequent bedfellow, inadequate regulation, now threaten to strip "organic" of everything it once stood for (and everything that has made it more expensive): small scale production, gen-

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Dear Reader

Joan Bavaria

This summer I spent an unusual amount of time hanging out in my back yard, getting to know a little family my husband Jesse named "The Flying Yellow Circus". The Circus consisted of about four male goldfinches and three females. The "kids" were typical reckless awkward juveniles, misjudging perches to swing perilously before righting themselves or squabbling over a single coveted twig as if it was the only place to land within miles. We learned that goldfinches are the only "feeder bird" that will actually turn upside-down on a perch in special goldfinch feeders filled with Audubon-recommended goldfinch food. Lucky birds, these. The Circus is on its way South now, strong and noisy, raised on human-provided food, now searching for their Southern wintering habitats in what has so far been a downright boring hurricane season.

In this quiet weather year, absent the drama of killer hurricanes, one of the cinematic surprises of the summer was an intelligent movie called "An Inconvenient Truth" based on a slide show that Al Gore has been showing around environmentalist circles for years. The movie, produced to emphasize Gore's quest and highlight the startling statistics around global climate change, stayed in theaters for weeks and became the third highest grossing documentary in the United States to date. The movie's magic is the irrefutable truth of it; Al

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From Bigger to Smaller

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By Lisa Leff

On this page in the last *Investing For a Better World*, Blaine Townsend wrote about the economic and environmental challenges of U.S. oil dependency. It's easy to get discouraged by current trends. It's perhaps even more disheartening to realize the advent of oil was only 150 years ago, and that we as a species have arguably done so much to threaten the health of the planet in so little time. Conversely, this brief history, this concentration of human activity, may provide the greatest source of hope for reversing the damage. Human beings have the capacity to create dramatic change in relatively short periods of time.

Prior to 1850, most of the energy powering economic and other human activity came from muscle power – from humans and domesticated animals. In comparison, oil as a source of energy was dramatically cheap and plentiful. According to author Richard Heinberg, "A single gallon of gasoline has about the same work potential as maybe six weeks of hard human labor. If we were to equate the two economically, either we would be paying people a fraction of a cent per hour for their labor or we would be paying over $1,000/gallon for gasoline." Oil was also plentiful. As Heinberg states, "And then the question was, what else can we use this stuff for?" As a society, we've found plenty of answers – enough to equate to about 20 million barrels per day in the U.S. for transportation, agricultural production, plastics, and chemicals.

So we've built a world-dominating U.S. economy based on cheap oil, persistently finding more and more stuff to do with it. I can't contemplate that these days without my thoughts going immediately to "The Lorax," Dr. Seuss' environmental tome, which my 3 year-old daughter (a budding environmentalist) counts among her favorite books. For anyone who hasn't read it lately, "The Lorax" is told in the voice of the ambitious industrialist Onceler who chops all the beautiful and once plentiful Truffula trees to make non-descript but much in demand "Thneeds," declaring "I meant no harm. I most truly did not. But I had to grow bigger. So bigger I got. I biggered my factory. I biggered my roads. I biggered my wagons. I biggered the loads… I went right on biggering selling more Thneeds. And I biggered my money, which everyone needs."

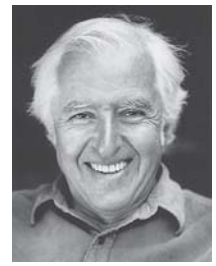
Globally, we've "biggered" our oil consumption to the point where we're now using oil at an estimated 4 to 5 times faster than it's being discovered. The scenarios around reaching peak oil production (not to mention global warming) are consistently dismal. For the Onceler, biggering for the sake of biggering ultimately leads to a ghastly, smoggy world devoid of animals, sun and the Truffula trees that began it all. We don't want similarly dire consequences.

There is great hope in new larger-scale global production of renewable and other alternative forms of energy, which in the U.S. is happening in spite of the lack of federal government leadership. It's widely believed, however, that supply-side fixes won't be sufficient to combat economic and environmental impacts of our oil dependency. Energy experts repeatedly remind us that the quickest and cheapest part of the solution is reducing demand. So it may be that the greatest hope comes from a shift in our thinking from "biggering" to "smallering" – which means rethinking transportation, communities, food production, and electricity on a global level. The big question is time. Can we shift away from oil dependency before we hit big energy shortages and/or irreversibly alter the climate? It's conceivable that, if we could build an economy based on oil in 150 years, we could reduce our oil dependency more quickly than most experts predict. And that leads back to the Onceler's ultimately wise warning: "Unless someone like you cares a whole awful lot, nothing is going to get better. It's not."

Extra, Extra: Get Your Newspaper While It's Still Available to Get

It Seems to Me

Milt Moskowitz



The death knell is sounding for an institution that has been a central guidepost in my life: newspaper publishing. When I was growing up in New York City, newspapers opened the world for me; there were then eight dailies being published in the city. I survived a 19-month tour of Army duty by serving as sports editor of the camp newspaper. I was editor of two college newspapers. I was a correspondent for two major newswires. For more than 20 years I wrote a three-times-a-week column that was syndicated to newspapers across the country. To this day, I am a news junkie. Four newspapers are delivered to my driveway every morning.

I am such a believer in newspapers that four years ago I bought 100 shares of **New York Times Company** stock. My rationale was simple: the *New York Times* is, arguably, the best newspaper in the world, why wouldn't it be a good stock to hold? Well, my investment has been halved.

Newspapers are clearly in trouble. Since 1970 the population of the U.S. has increased by 50% but the number of newspapers sold every day has declined from 62 million to 54 million. Over that span more than 300 daily newspapers have disappeared. **Knight-Ridder,** the nation's second largest newspaper chain, has just been dismembered. The *San Francisco Chronicle*, the original syndicator of my column, reported a circulation decline of 15% in the six months ended last March 31. And investments in any of the major publishers – **Dow Jones**, **Gannett**, **Tribune** (owner of the *Los Angeles Times*) – would have been dead money over the past four years.

People are obviously looking elsewhere for information – radio, television, the Internet. Advertisers have cut back or eliminated their space purchases in newspapers. The financial backbone of newspapers used to be classified ads – help wanted, houses for sales, apartments for rent. That business has shifted to the Internet.

Addicted to thumbing my way through newspapers every day, I am dismayed by this development. It's also affecting me professionally. I recently e-mailed the editor of the *San Francisco Chronicle's* Sunday magazine about the chances of doing a series of profiles on small and medium-sized companies. In fewer than five minutes, I got this reply: "Sorry, but I have a very limited budget and even more limited pages. I can't launch a series of any sort at this time."

It bothers me on another level as well. Newspapers have often been the gadflies we need to puncture the hot air balloons of politicians. They have been bulwarks for human rights. Who is to take their place? Somehow I don't see **Google**, **AOL** or **Yahoo** playing this kind of role. I've noticed that when I am looking for information about a company on Google, the search rarely yields any articles which are negative.

The newspaper industry lost 2,000 jobs last year, and cost-cutting was carried to a ludicrous extreme at the **McClatchey**-owned *Minneapolis Star-Tribune*, a paper that used to carry my column. The paper installed vending machines in the newsroom so that staffers who wanted to see the paper have to plunk down a quarter to extract a copy. No more free copies. You might have guessed what would happen. Employees began inserting a quarter and pulling out multiple copies to share with colleagues. During the first week the racks were up, 43% of the papers removed were not paid for. Circulation director Steve Alexander was irate: "Taking more than one newspaper from a rack when you have only inserted enough money for one paper is unacceptable and will not be tolerated. Employees who steal newspapers will put their jobs at risk."

I read about this in my favorite newspaper, the **print** edition of the *New York Times*.

Milt Moskowitz is a journalist and author who has been writing about corporate social responsibility since 1968. He is co-author of the annual *Fortune Magazine* survey, The 100 Best Companies to Work for in America.

Sold on Social Responsibility: The Sell Side Finally Buys into CSR (cont'd)

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nored corporate social responsibility (CSR) concerns in their stock research. They often argued these issues were tangential to a stock's performance or impossible to quantify. Of course, we can quantify how many billions investors lost from ethics scandals like **Enron**, tort claims as companies got hit with asbestos lawsuits, and falling market share as customers shifted from gas-guzzling American SUVs and trucks to more fuel efficient Japanese hybrids. From these examples and a host of other reasons, the sell side of Wall Street is finally acknowledging what Trillium Asset Management and others on the buy side have known for decades: social and environmental issues can materially affect stock prices, particularly over the long-term and sometimes even in the short-term.

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Not only is this not news to socially responsible investors, it's not even news to many business leaders. The chair of food giant **Unilever** expressed it well last year in a speech at the London Business School, when he said, "Business is part of society, not outside it. When we talk about corporate social responsibility, we don't see it as something business does to society, but as something fundamental to everything we do... not just philanthropy or community investment, but the impact of our operations and products as well as the interaction we have with the societies we serve. CSR is not a soft issue or a nice to do activity on the fringe of business. It is central to doing business. It is challenging to manage and it is a hard edged business issue."

Although it isn't news that a company's social and environmental performance can influence its success or failure and thus its stock price, the fact that major sell side Wall Street firms like **Citigroup**, **UBS**, **Goldman Sachs** and others have finally clued into this fact is important news given their influence over financial markets, companies, and economic policymakers.

For instance, **Merrill Lynch's** top auto analyst wrote a June 2005 research note titled *Energy Security and Climate Change – Investing in the Clean Car Revolution* that said, "The global need to address energy security concerns and the impact of climate change on the earth's environment is intensifying pressure on the auto industry to create vehicles with higher fuel economy and lower emissions. This is not tomorrow's story – it is playing out right now in the changing competitive strategies of major automakers." The research piece goes on to name companies poised to benefit from demand for more fuel efficient vehicles, directing investors to those companies investing the most in clean car technologies. Other brokerage houses have issued similar research reports on which food companies are best addressing concerns about childhood obesity, which companies are best addressing the threats of climate change, and which companies are best responding to social changes in South Africa, to name just a few recent examples. Several brokerage houses like Citigroup, Goldman Sachs, UBS and others have also issued reports that look comprehensively at SRI and social responsibility issues across a range of companies and industry sectors.

There are a number of reasons why brokerage houses are finally giving social and environmental issues some of the coverage they deserve. Some of it is as a result of external prodding.

One early catalyst for more sell side CSR research came from the United Nations Environment Program's Finance Initiative (UNEP-FI), which works with large financial institutions to promote sustainable development. Over the past two years, UNEP-FI has persuaded nearly

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two-dozen brokerage houses from across the globe to contribute research to two reports it compiled linking environmental and social issues to stock performance. The first report, titled *The Materiality of Social, Environmental, and Governance Issues to Equity Pricing* came out in 2004 and included 11 sector-specific studies by sell side research analysts. UNEP-FI just released its second compilation of sell side research, with the catchier title, *Show Me the Money: Linking Environmental, Social, and Governance Issues to Company Value*. The second report concludes: "(1) ESG [Environmental, social, and governance] issues are material – there is robust evidence that ESG issues affect shareholder value in both the short and long term. (2) The impact of ESG issues on share price can be valued and quantified. (3) Key material ESG issues are becoming apparent, and their importance can vary between sectors."

Another catalyst for more sell side research has come from the Enhanced Analytics Initiative, a coalition of mostly European asset managers and pension funds with over $1 trillion in assets that have set aside a portion of their sell side research budgets specifically for coverage of environmental and social issues. In addition to earmarking funds towards ESG research, the Enhanced Analytics Initiative commissions reviews of sell side research providers and publicly names those doing the best job covering environmental and social issues, another strong incentive for brokerage houses to address these issues in their analyses. Although the EAI has only operated since 2004, it has sent strong market signals that the buy side expects the sell side to cover ESG issues. That demand has also increased as assets under SRI management continue to grow, and more large pension funds and other so-called mainstream investors incorporate consideration of SRI issues into their investment processes.

In addition to these external catalysts, there is growing evidence that major brokerage houses have come to recognize environmental and social issues as important business issues. Citigroup, **J.P. Morgan Chase**, Goldman Sachs and other major banks have all adopted their own environmental policies committing to address issues like climate change, which has driven internal awareness about the importance of these issues. In some cases, their environmental policies include specific commitments to address these issues in their sell side research. Wall Street is also under increasing criticism for overly focusing on short-term quarterly results to the detriment of long-term value creation for companies, investors, or society, and consideration of ESG issues injects some much-needed consideration of long-term issues back into sell side research. Finally, in an increasingly complex global business environment where U.S. companies must meet European environmental regulations on their products, instability in Nigeria affects Western oil supplies, and most governments around the world are taking action to address climate change, the materiality of environmental and social issues is now just too obvious to ignore. In short, as UBS wrote in a research note last spring with the provocative title *Corporate Social Responsibilities: Why Try to Quantify the Unquantifiable?*: "Social risk is business risk and business risk translates into financial risk." With both sides of Wall Street now increasingly recognizing that fact, the power and influence of socially responsible investing is poised to increase dramatically.

The materiality of environmental and social issues is now just too obvious to ignore.

Resources

www.unepfi.org

www.enhancedanalytics.com

Battle for the Soul of Organic

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tler treatment of animals, better treatment of farm workers, and the elimination of chemical aids to production.

Major producers and retailers – abhorring a vacuum at least as much as nature – are capitalizing on the public's appetite for organics and its willingness to pay a sometimes hefty premium at the checkout line. Major food producers with organic lines, most of them acquired through buyouts, include **Coca Cola** (Odwalla), **Kraft** (Boca Foods), **Unilever** (Ben & Jerry's), **Kellogg** (Kashi and Morningstar Farms), **General Mills** (Cascadian Farms) – and the list goes on. According to the Organic Trade Association, while organics are only about 2% of overall food and beverage sales, they are the fastest growing sector in the food business, having grown between 20 and 24% each year since 1990. According to the *New York Times,* organic foods could become a $23 billion market over the next three years, or even higher, given Wal-Mart's entry into the market.

By ignoring issues of water, animal well-being, long-distance food transport, and labor standards, the new federal rules have facilitated the movement of most organic production to large farms and industrial-size feedlots.

The entry of these players has changed the game. For a dozen years, the large food concerns locked horns with small farmers and consumers during the formulation of national organics regulation known as the National Organic Plan, adopted in 2002. As a result, these regulations have loopholes that you can drive a herd of cattle through, holding costs down for large agricultural concerns but disadvantaging farmers struggling to remain true to the spirit of organics. By ignoring issues of water, animal well-being, long-distance food transport, and labor standards, the loopholes have facilitated the movement of most organic production to large farms and industrial-size feedlots.

The industry has also become increasingly concentrated. The retail market for organics is split roughly evenly between conventional supermarkets and natural foods chains, with only 7% covered by farmers' markets, food service and other non-retail store sales.[2]

A 2002 study conducted at the University of California at Davis found that 2% of California's organic farms – just 27 growers – owned over half of the state's market share.[3] **Whole Foods** dominates the natural supermarkets sector with over four times the revenues of its closest competitor **Wild Oats.** Wal-Mart is the country's largest seller of organic milk, and could surpass all others in overall volume sold of all organic products within a few years.[4] **Horizon Organic** produces 70% of organic milk in the U.S.[5]

What exactly is at stake?

One way companies like Wal Mart and General Mill's Cascadian Farms save money is by sourcing organic foods from China, Mexico and Brazil.[6] The globalizing of organic food is a growing problem because it:

- Compromises local variety and diminishes freshness,
- Undermines rural communities by displacing shelf space formerly reserved for local growers,
- Emits vastly more greenhouse gas emissions by increasing "food miles."

The Organic Consumers Association (OCA) is currently protesting the food importation from China and Brazil due to their permissive labor laws.

Ironically, squeezing domestic labor costs is not a strategy that would enhance the new market entrants' margins substantially, since there's so little room to squeeze. Organic agriculture workers have not, except for rare exceptions, enjoyed better treatment than their counterparts on traditional farms. *The Nation's* recent excellent "Food Issue" (September 11, 2006) contains an investigative piece by Felicia Mello that examines working conditions for processors of organic car-

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Battle for the Soul of Organic

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rots at Grimmway, which sells 40% of the world's carrots. Like their counterparts working on traditional farms, the organic workers are non-unionized, earn low wages, and rarely enjoy health benefits. Repetitive stress injuries are common. Mello found that although many small farmers would like to provide benefits to their workers, most struggle simply to survive.

Another cost-squeezing device is the exploitation of the loosely written regulation concerning the welfare of animals on organic farms. Chances are quite good that the organic meat on your table did not originate from animals that enjoyed a pastoral lifestyle before meeting their fate. The National Organic Plan requires that animals be given "access to pasture" but the term is not defined, and as a result, industrial feedlots that cram livestock into inhumanely small pens and coops can still claim the organic label if the animals enjoy just the barest exposure to the outdoors.[7] An additional problem is that the waste products of so many animals, in the words of one organic farmer, are "a critical resource for maintaining soil health in reasonable amounts, but a fetid nightmare when produced at mountainous levels."[8]

Small and large organic farmers are also duking it out over the use of synthetic ingredients in organic products. Currently, federal regulations permit organic foods (defined as products that contain at least 95% organic ingredients) to include up to 38 synthetic ingredients that don't have to be listed on the product's label. Consumer groups are upset that a 2005 Congressional amendment makes it easier for the USDA to permit up to 500 additional synthetic ingredients without rigorous review from the National Organic Standards Board; loosens restrictions on the use of non-organic ingredients when organic ingredients cost too much; and allows farmers to feed dairy cows more non-organic feed.[9] Succinctly illustrating the ill will between consumer groups and the Organic Trade Association (which represents corporations), Consumers Union analyst Urvashi Rangan characterized the OTA's position on synthetic ingredients as "frankly written without any understanding of chemistry or science."[10]

Backlash and Hope

Organic farmers are not taking this sitting down (they never have time to sit anyway). The Organic Consumers Association is promoting a boycott of **Dean Foods** and **Aurora Organic Dairy**, the former for sourcing soy from Brazil and China, and the latter for "its practice of intensive confinement" of animals, "greenwashing," and its "bogus certification of animal welfare."[11]

Organic Valley stopped supplying to Wal-Mart two years ago, due to lack of supplies to meet the company's voracious demands. Once Wal-Mart's largest supplier, Organic Valley has now left it to its larger competitors to "duke it out figuring out how to service Wal Mart," a spokeswoman told *Consumer Reports.*[12]

There are also signs of hope. A spate of new books is shedding light on the current state of organic agriculture such as Michael Pollan's *Omnivore's Dilemma,* Julie Guthman's *Agrarian Dreams: The Paradox of Organic Farming in California*, and *Organic, Inc.: Natural Foods and How They Grew* by Samuel Fromartz. If problems cannot be solved overnight, raising awareness about the contradictions between hype and reality is a first step.

Footnotes

[1] "Wal-Mart Eyes Organic Foods," May 12, 2006, *The New York Times,* by Melanie Warner.

[2] Source: Organic Trade Association.

[3] "Is Bigger Better? Corporate Clouds on the Organic Horizon," November 25, 2004, www.corpwatch.org, by Carmelo Ruiz-Marrero.

[4] "The Green Machine," July 27, 2006, *Fortune*, Marc Gunther.

[5] Ruiz-Marrero.

[6] "Up Against the Wal-Mart," August 23, 2006, *Grist.org*, by Tom Philpott.

[7] Ruiz-Marrero.

[8] "Sour Milk," August 2, 2006, *Grist.org*, by Tom Philpott.

[9] "Activists Move to Protect Organic Standards from USDA, Trade Group," *New Standard,* October 5, 2005, by F. Timothy Martin.

[10] Transcript of United States Department of Agriculture National Organic Standards Board Meeting, April 19, 2006, p. 90.

[11] See www.democracyinaction.org.

[12] "When It Pays To Buy Organic," *Consumer Reports*, February 2006.

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Cemex (CX – NYSE) produces, distributes, markets, and sells cement, ready-mix concrete, aggregates, and clinker worldwide. It delivers its products through direct sales and distribution channels to the residential, industrial, commercial, and public sectors.

Cemex has higher profit margins than its competitors and is reducing its debt. Management is focused on putting its excess cash flow into expansion and optimization projects instead of acquisitions. Cemex is also modernizing plants in Europe to optimize efficiency of existing operations.

Cemex has more exposure than other cement companies to the expected growth in emerging markets. Over 60% of Cemex's earnings are from emerging markets where cement demands will be increasing more than in developed countries. In addition there is high growth in the construction sectors in U.S. and Mexico.

In addition to Cemex's exposure to emerging markets the company has increased its participation in the Eastern European market through its acquisition of RMC. In addition, Cemex's dependence on Mexico has decreased; last year Mexico made up 32% of sales vs. 21% in the first quarter of this year.

Cemex has a strong expressed commitment to sustainable development, and has undertaken a broad range of social and environmental initiatives to address its impacts. The company won the World Environment Center's Gold Medal for International Corporate Achievement in 2002. The company has pledged to cut its CO_2 emissions per unit of cement produced 25% from 1990 baseline levels by 2015.

— Sonal Mahida & Eric Becker, CFA

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Ormat Technologies (ORA – NYSE) is a leading geothermal power producer. Geothermal energy is among the cleanest, cheapest and most dependable alternative energy sources. The company has grown rapidly through acquisitions of geothermal properties, primarily in the western U.S.

Geothermal power production harvests the heat from the earth to power turbines, which in turn produce electricity. In a geothermal plant, wells are drilled to access hot geothermal fluids. These fluids are pumped to the surface, where they generate steam to turn the turbines before being pumped back into the ground to replenish the geothermal source.

With 364 Megawatts of operating geothermal generating capacity (and an additional 131MW under construction), Ormat is one of the largest geothermal players in the world and the second largest in the U.S. Geothermal is experiencing significant growth due to high oil and gas prices, state renewable portfolio standards and its clean profile. The company estimates that it will grow its generating capacity at a 21% annual rate from 2005 through 2008. Beyond that there remain significant expansion opportunities, particularly in Nevada, California and Indonesia.

The core technology of a geothermal plant is transferable to the recovered energy generation market, particularly associated with natural gas pipelines and processing plants. In these applications, the power plant uses waste heat from an industrial source to generate steam to power the turbines. Ormat estimates the addressable market at 1,500MW, offering a second major growth market for the company.

— Eric Becker, CFA

The CDFI Assessment and Rating System (CARS™)

The Community Development Financial Institutions Assessment and Rating System (CARS™) is a third-party-administered analysis and rating system of non-bank/credit union Community Development Financial Institutions (CDFI). It was developed by the Opportunity Finance Network (OFN) (formerly the National Community Capital Association) to aid investors in their investment decision process.

Opportunity Finance Network has more than ten years experience evaluating and underwriting CDFIs, providing consulting services to CDFIs and investors, and gathering and analyzing data about the CDFI industry.

CARS™ looks at impact performance as well as financial strength and performance of CDFIs, and issues a combined rating between AAA+1 (the highest) and B 5 (the lowest). The letter designation is for impact performance (on a scale of AAA, AA, A, B) and the "+" signifies whether the CDFI plays a leadership role in policy. The number is the financial strength and performance rating and is an assessment based on creditworthiness.

The Impact Performance rating is an assessment of how well the CDFI does what it says it is trying to do. This rating is based on an assessment of the CDFI's effective use of its financial resources to achieve its stated mission and the CDFI's own evidence of how its activities contribute to its mission. The impact performance assessment is based on four key criteria:

- Alignment of strategy and operations: how well the CDFI's mission, strategies, products and services, output data and impact data are tied together.
- Effective use of financing resources: how well the CDFI uses its financing resources in support of its mission and target population.
- Tracking of outputs that show effectiveness: how well the CDFI tracks and uses its own relevant output indicators.
- Tracking of outcomes or impacts that show effectiveness: how well the CDFI tracks and uses data and information about the actual outcomes of its work (such as jobs actually created, housing units occupied by low-income families, improved community conditions).

The financial strength and performance analysis is in a CAMEL (capital, assets, management, earnings, liquidity) format, and assesses each of these areas in detail. The financial analysis includes key ratios and indicators for the past three years, financial statements for the past five years, tables and charts showing trends, and a peer comparison that investors can use to provide context for the investment opportunity they are considering.

Each CARS™ report includes the ratings and a thorough written analysis. A site visit, including management interviews and a review of documents and files, is part of the ratings process, as are conversations with board members.

As investors incorporate the CARS™ ratings and analyses into due diligence reviews, OFN believes CARS™ will become a recognized benchmark in the community investment field. To date, twenty-one CDFIs have been rated, seven are currently in the review process, and an additional twenty are in the pipeline.

One of the most significant, early impacts of CARS™ has been that it is prompting improved transparency and performance on the part of CDFIs. Because of the rigor of the process and analysis, CARS™ helps CDFIs understand their own strengths and challenges.

TAMC is part of the inaugural group of sixteen CDFI investors, including banks, socially responsible investors, and foundations, to use CARS™ in our due diligence process.

Community Investment News™

Randy Rice

"Although still in its early stages, this initiative, if successful, will have the double benefit of attracting more funds into community development and helping to ensure that those funds are effectively used."

—Ben Bernanke, Federal Reserve Board Chairman

For more information on CARS™, visit www.opportunityfinance.net

What I Advocated on My Summer Vacation

Shareholder Activism

Steve Lippman

Over a third of the S&P 100 Index (34 companies) now base their corporate social responsibility reports on a widely recognized external standard for reporting called the Global Reporting Initiative's (GRI) Sustainability Reporting Guidelines.

The Fall issue of *Investing for a Better World* seems an appropriate time for a "What-I-Did-On-My-Summer-Vacation"-style update on some of my recent advocacy. Demonstrating that those of us in the United States just don't take vacations like our European counterparts, in August alone I had in-person or phone meetings with staff at **AIG**, **Bank of America**, **Citigroup**, **Coca-Cola**, **Ecolab**, **Intel**, **Microsoft**, **PepsiCo**, **Sysco**, and **Weyerhaeuser**. I didn't even try for French-based **Danone**, assuming anyone I wanted to talk to would be out for the month of August. Among some of the highlights:

- We led two calls for dozens of investors to ask Coca-Cola and PepsiCo how they are addressing allegations that their products in India have unsafe levels of pesticide residues. Although India's Health Minister has dismissed these allegations, we pressed the companies to take steps to safeguard their products, engage with their critics, and put the controversy behind them. Both companies have installed new filtration systems to ensure the safety of their products, are working to decrease pesticide use by their suppliers, and are moving towards agreeing to a common test method that will allow the Indian government to finalize safety standards for their products.
- We learned that we helped convince Intel, which already had strong programs in place to reduce its water use, to adopt a new formal Water Conservation Strategy with new water use reduction goals to meet by 2010.
- We worked to hold Weyerhaeuser accountable for its lobbying by pointing out the disconnect between its laudable announcement this summer that it will reduce its greenhouse gas emissions by 40 percent and its lead role in opposing a citizens initiative in Washington state to require utilities in the state to boost their use of renewable energy sources 15 percent by 2020.

Of course, we meet with lots of groups other than companies. This August, for instance, I talked with staff at Business for Social Responsibility, the Pacific Institute for Studies in Development, Environment, and Security, and the Bill and Melinda Gates Foundation looking to identify leading edge practices in water stewardship we should promote in the corporate sector.

Thinking back to earlier in the summer, we led an initiative by the Social Investment Research Analysts Network (SIRAN) in partnership with research firm KLD Research and Analytics to produce a new study on how some of the biggest companies in the U.S. are reporting on their environmental and social performance. The study of reporting practices among the S&P 100, found that more than three-quarters (79 companies) now have special sections of their websites dedicated to sharing information about their social and environmental policies and performance. This represents a 34% increase from last year, when 59 companies in the S&P 100 included this information on their websites. Over a third of the S&P 100 Index (34 companies) now base their corporate social responsibility reports on a widely recognized external standard for reporting called the Global Reporting Initiative's (GRI) Sustainability Reporting Guidelines. This was up sharply from 2005, when 25 companies in the S&P based their reports on the GRI guidelines. The uptick reflects a concerted outreach effort by Trillium Asset Management and other SIRAN members to promote reporting based on the GRI standard. For more on the study, visit www.siran.org/csr.php.

Oh, one little thing I shouldn't forget to mention is that I also got married this summer and am heading out on my honeymoon. Then it's back to work just in time for shareholder filing season this fall. Well, unlike grade school when I had to rely on the use of the word "very" a lot towards the end of my essays, I'm actually over my word limit and will sign off for now.

When Do You Divest?

Trillium Adopts a Sudan Divestment Policy

Shareholder Activism

Shelley Alpern

When the chairman of a company authorizes spying on fellow board members? When earnings have been manipulated to meet forecasts? When its investment in renewable energy technologies shines like a green-and-yellow sunburst logo but its pipeline maintenance needs to go back to engineering school? What if it seems to be paying its debts and moving forward?

Likewise, when do you divest from a *country*? Do you wait for U.S. or international sanctions? Do you wait for an internal, 'legitimate' voice of the people to call for economic disengagement? Do you need evidence that you won't hurt the people you are trying to help – or do you just go ahead and break a few eggs for the sake of the omelet?

Ethics aside, the practical considerations of divestment are also tricky business. The would-be ex-investor should feel pretty certain that constructive engagement is a dead end because the act of divesting is a one-time, high-minded gesture of protest; it may help to confer a pariah status on a country or company, but except in very rare circumstances, it won't depress a stock price and keep it low.

For all these reasons and more, we don't do a lot of splashy divestments here at Trillium. We prefer to manage the risks of corporate misbehavior through pre-screening and engagement. Nonetheless, managing stock portfolios while wearing the "socially responsible" hat is a constant exercise in moral ambiguity. I often wish Trillium could create a dazzlingly competitive product that exceeds all investment benchmarks, consisting of nothing but renewable energy companies offering the next generation of employee benefits, and donating 10% of their pre-tax profits to social justice organizations. Until that breakthrough moment, however, we just accept a certain background level of angst that periodically spikes when one of our companies makes the papers in an article also containing words like 'controversy' or 'indictment.'

But this summer, Trillium's decision to throw our modest weight behind the Sudan divestment movement came rather easily. Regardless of the peace agreement that exists on paper, the Sudanese government can't seem to stop itself from committing genocide against the people of Darfur. (See "Sudan Divestment Campaign Begins to Bear Fruit" in the December 2005 edition of *Investing For A Better World*). Frustrated by the ineffectiveness of existing U.S. sanctions and the inattention of the Bush administration, grassroots activists snuck under the radar and created a divestment movement that just keeps gathering force. No one seems to have a good answer to the question, "If divesting from a genocidal regime isn't appropriate, when is divestment *ever* appropriate?"

Fourteen states and 25 universities have taken action to address the question of investing in companies that do business with Sudan. Over a dozen more states and 20-plus additional universities have active divestment movements.[1] Their activities include direct engagement with companies doing business in Sudan, monitoring their investments more closely to identify any holdings linked to Sudan or other terrorist states, and complete or selective withdrawal from companies with ties to Sudan, particularly those in key sectors such as oil and gas, electric power, or telecommunications.

We chose the last option, also known as "targeted divestment." Reviewing client portfolios (which contain legacy holdings as well as stocks chosen by us), we found only one holding that we need to attend to: **Schlumberger**, which has been described as "the French Halliburton." Since the genocide began, Schlumberger's business in Sudan has only increased. Frankly, we don't have a lot of confidence that our letter to the company threatening a few thousand dollars of divestment will turn this company around, but in piling onto a rising tide of pressure from investors the world over, something may eventually give. It did in South Africa.

No one seems to have a good answer to the question, "If divesting from a genocidal regime isn't appropriate, when is divestment ever *appropriate?"*

Footnote

[1]For more detail, see the regularly updated "State of Sudan Divestment Report" by the Sudan Divestment Task Force at www.sudandivestment.org.

Strategic View: Taking Responsibility for Market Returns

By Adam Seitchik, CFA

Over twenty years ago Charlie Ellis published the first edition of his investment classic, *Winning the Loser's Game*. His core message was simply to invest in markets, and resist trying to outsmart them. Stocks and bonds provide attractive returns to patient investors, so invest for the long run.

While Ellis' ideas have gained widespread popularity, they have also led to an unfortunate passivity among many owners of capital. In fact, the kind of exposure to a market index (such as the S&P 500) that Ellis promoted has become known as "passive" investing.

But should investing in the market be a passive exercise, and does it always lead to good outcomes? Market returns do not occur in a vacuum, but are the product of political, social, technological and economic trends that investors themselves help influence. A passive investor in German bonds would have lost 100% of their value during the hyperinflation of 1923, and a German equity investor would have lost 87% of value in 1948.[1] So just sitting back and watching your money grow does not work in all times and places. U.S. markets in the first half of the 20th century endured two world wars, multiple financial panics, the Great Depression, the rise of communism and fascism, widespread labor discrimination, and the detonation of atomic bombs killing several hundred thousand human beings. The result was global investment returns less than half as good as what came after the War.

Our perception of long-term market outcomes is colored by the positive developments that emerged in the five decades following World War II: no global wars, a regulated and insured banking system, limited nuclear proliferation, the Marshall Plan, expansion of the middle class, improved social justice via the civil rights movement and related legislation, the EPA, the end of the Cold War, healthy economic growth with no depressions, and Federal Reserve economic management. The result was phenomenal market returns for 50 years in a variety of markets, with global stocks rising 9% annually *in excess of inflation*.

Results like these are by no means guaranteed, and being a passive investor abdicates responsibility for the world that underpins economic and financial prosperity. The corporations that investors own now exert tremendous global power relative to government and labor. Investors can and should demand that companies desist in externalizing costs onto society and ignoring looming risks in the service of short-term gain.

It is encouraging that some investors and companies are taking a leadership role in analyzing critical long-term risks such as CO_2 emissions and biodiversity loss. Nothing will do more to secure market returns in this century than reversing global warming and limiting nuclear proliferation. It is all too easy to put issues like this into the box of "politics," disconnected from investment policy-making. But while investors can debate the appropriate course of action, there should be little disagreement that dire outcomes are possible and imminently material. When shareholder activism can reduce market risk, passivity is not the winning strategy.

[1] All market return data from Dimson, Marsh and Staunton. Their book, *Triumph of the Optimists* (Princeton University Press, 2002), reviews 101 years of global investment returns.

Dear Reader *(continued)*

Gore has been studying and working on this issue for decades. In his view, and in the view of most of the scientific community, this damage will irrevocably change our ability to inhabit the Earth in ways that are very likely to cause massive social unrest and devastating environmental degradation.

Yet like the frog that is slowly heated to boiling in a pot of water, the gradual change of our human surroundings are not enough to convince us that we should in any way alter our day-to-day activities. Priorities remain the same – faster, bigger, glitzier, trumps conserving, saving, or appreciating such natural blessings as the Flying Yellow Circus. Anxious to rid our yards of pesky mosquitoes we kill mosquito predators and benign insects alike in noisy glowing bug zappers or spray dropped from airplanes, and drive our kids to school in automobiles each of which could serve as a school bus. But we know the drill. The question is, what will get our attention and better yet, what can we do about it? Will Cape Cod and Florida have to sink into the Atlantic Ocean before we sacrifice one small piece of our current life style?

Socially responsible investors play a pivotal role. The economic system within which we participate is largely dependent on the status quo – a petroleum-based, growth economy in which conservation often leads to lower profits in the short run. Social investors need to do what they have been doing for years—ask questions and demand answers, and continue to search for ways to invest in a sustainable economy. In the end, the economic answers might provide the only true solutions.

Sincerely,

Joan L. Bavaria

Joan L. Bavaria, President
Trillium Asset Management Corporation