

Ethical Investing and Investment Performance

Perspectives on Audit Value
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The
**Ethical
Funds**
Company™

There's good money to be made™

Order of presentation

- About The Ethical Funds Company
- About Socially Responsible Investing (SRI)
- SRI Indexes and Performance
- Performance Studies

About us

The
**Ethical
Funds**
Company™
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The Ethical Funds Company

- Socially responsible mutual fund company
- Based in Vancouver, BC
- Canada's largest family of SRI funds
- 12 funds with C\$1.8 billion AUM
- Owned by Canada's credit union system
- Sustainable funds, shareholder action, proxy voting

Our vision

- Encourage companies to adopt the values of sustainability as guiding framework
- Provide solid investment returns throughout the economic cycle
- Contribute to the wider evolution of a sustainable world

Respect for the Environment

- Companies must:
 - **reduce adverse environmental impacts**
 - **adopt a precautionary approach to the environment**
 - **help restore ecological health**

Respect for Stakeholders

- Companies must:
 - offer solid financial performance & contribute to the local economy;
 - demonstrate good ethics, governance, & accountability;
 - develop mechanisms for effective stakeholder engagement

Respect for Human Rights & Security

- Companies must:
 - **avoid complicity in human rights violations**
 - **support human & labour rights**
 - **reduce hunger, disease, & repression**
 - **encourage peaceful resolution of conflict**

What are the corporate drivers?

- Reduced operating costs
- Reduced exposure to legal action
- Enhanced brand image
- Increased sales and customer loyalty
- Increased productivity and quality
- Ability to attract and retain employees
- Reduced regulatory oversight
- Access to resources

Implementation

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Sustainable Investing Program

Corporate
Sustainability
Scorecard

Shareholder
Action
Program

Elements of the Program

Corporate
Sustainability
Scorecard

What is the CSS?

- Data collection and scoring system
- Models corporate sustainability
- Grades sustainability performance
- Determines Green and Red Lists
- Assists in determination of Focus List for our Shareholder Action Program

Corporate
Sustainability
Scorecard

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Corporate Sustainability Scorecard

A	Leaders	}	Green List, eligible
B	Fast Followers		
C	Followers		
D	Borderline	→	Green List & Focus List

E	Non-compliant	→	Red List, ineligible

Corporate
Sustainability
Scorecard

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Who qualifies for our Funds?

- Companies in our portfolios are not 'ethically perfect'
- No such companies exist
- *On balance*, the companies we own are:
 - reducing negative impacts of their activities
 - contributing to sustainability

Elements of the Program

Shareholder
Action
Program

Shareholder Action Program

- Philosophy of engagement
- Shareholders have rights
- Access to decision-makers
- Provide 'early warning system'
- Contribute to positive change

Shareholder
Action
Program

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Proxy Voting

- Vote on resolutions at company AGMs
 - Management resolutions
 - Shareholder resolutions
- Engage all holdings
 - Focus List is 10% of portfolio
- Accountable to our unitholders
 - Proxy voting disclosure

Shareholder
Action
Program

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Success Stories

- Home Depot phases out old growth
- IPSCO improves enviro disclosure
- Bristol Myers Squibb phases out PVC
- Morgan Stanley adopts enviro policy
- Citigroup adopts the Equator Principles

Shareholder
Action
Program

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Ethical Investing

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Ethical Investing

“Integration of social and environmental criteria into the investment process”

“Making a profit while making a difference”

Ethical Investing

- Mutual funds
- Pension funds
- Charitable foundations
- University endowments
- Research and consulting firms
- Industry associations
- Non-governmental organizations

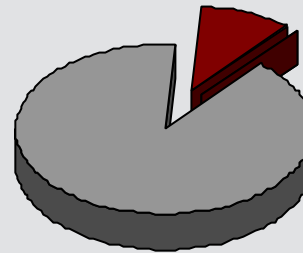
SRI around the world

US



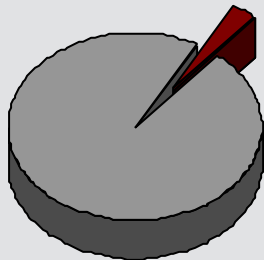
US\$2.16 trillion
11.3% of market

UK



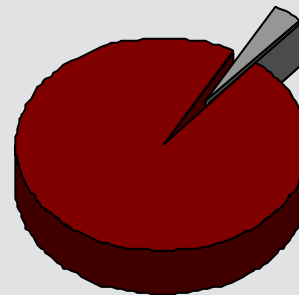
\$403 billion USD
11% of market

Australia



US\$14.3 billion
3.2% of market

Canada



C\$51 billion
3.3% of market

SRI Indexes and Performance

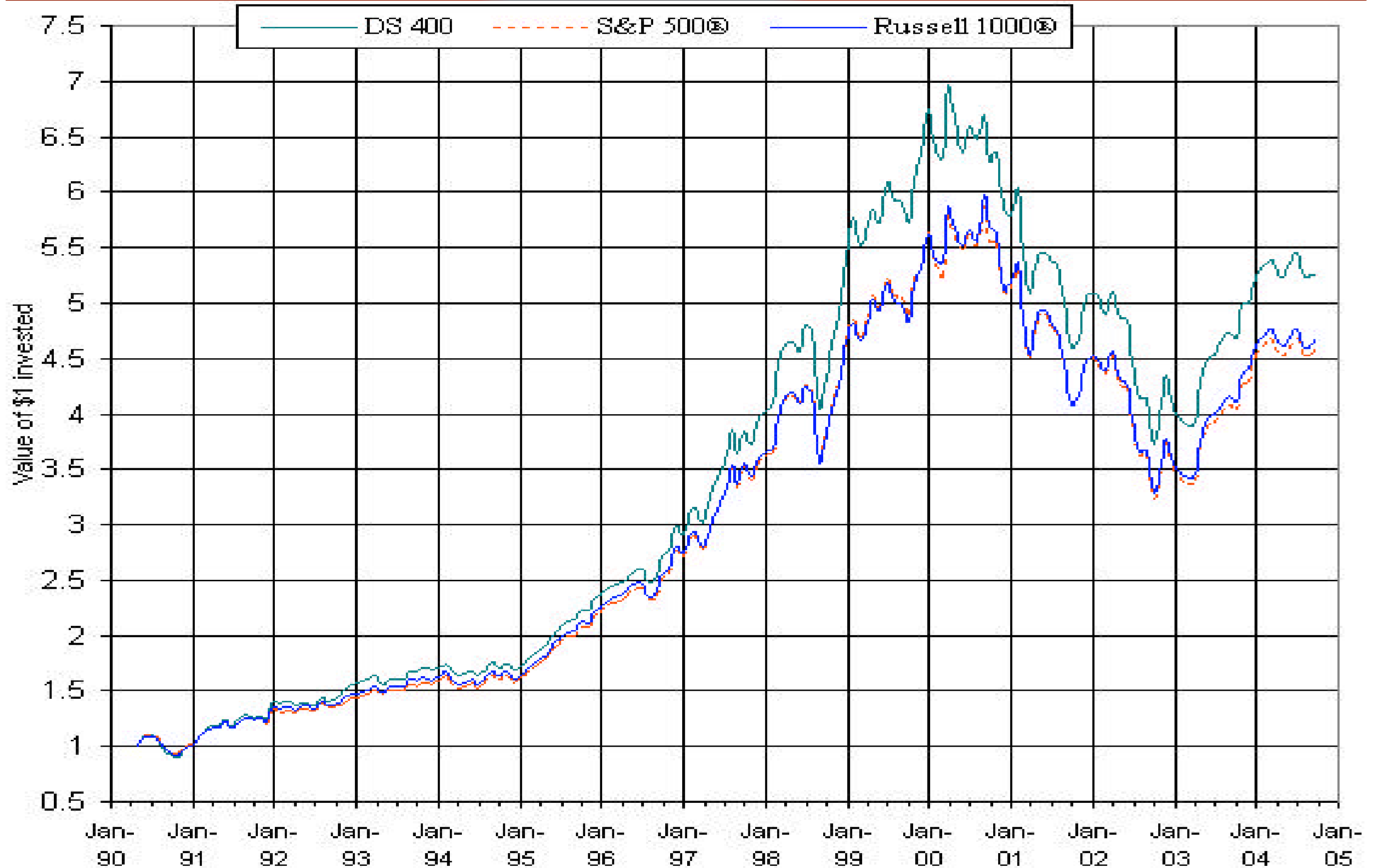
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SRI Indexes

- Dow Jones Sustainability Group Indexes
- FTSE4Good
- **Domini Social Index 400**
- KLD Broad Market Index
- KLD Large Cap Social Index
- KLD Nasdaq Social Index
- KLD Select Social Index
- Calvert Social Index
- **Jantzi Social Index**
- **Ethical Canadian Index**

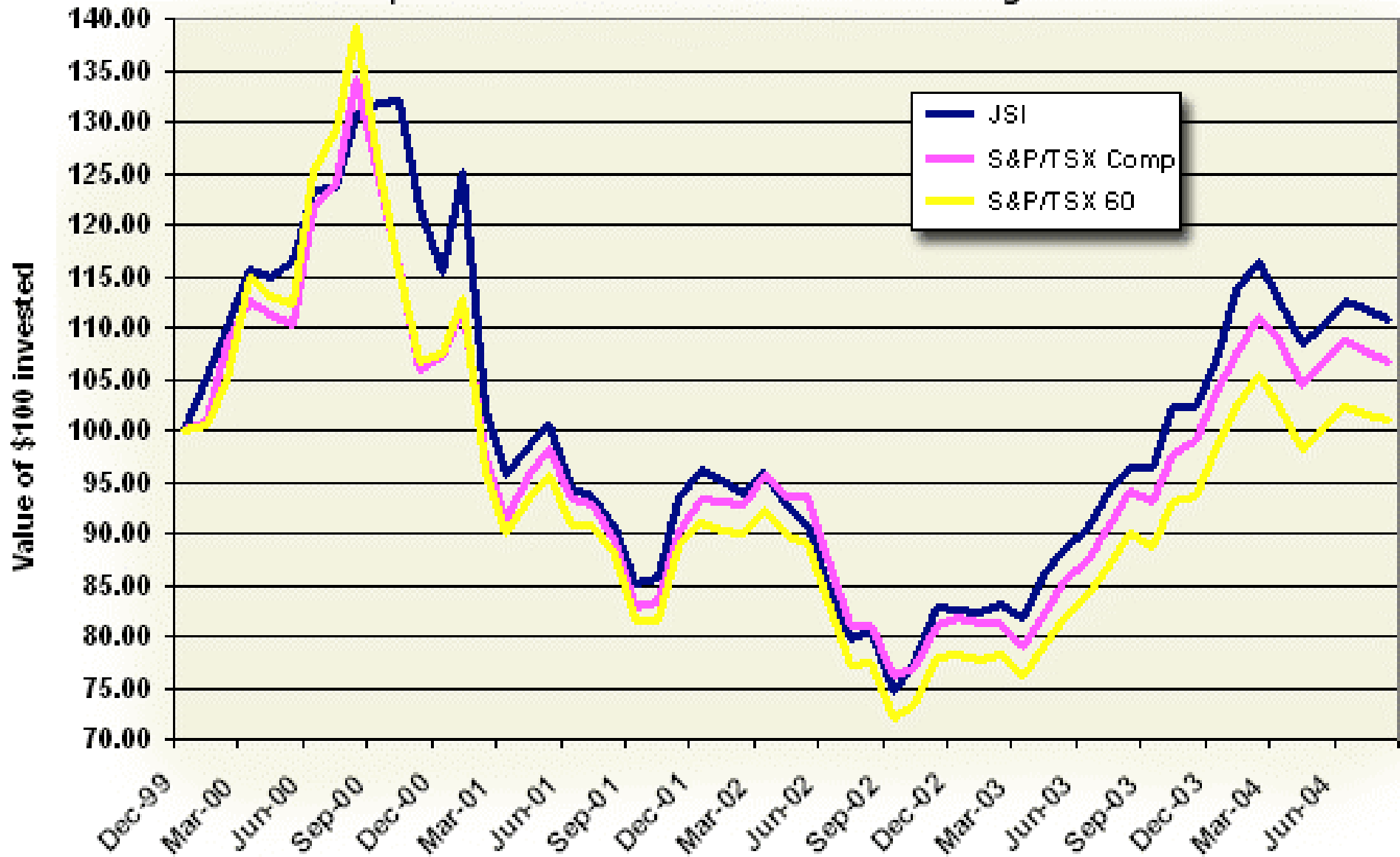
Domini Social Index

September 30, 2004

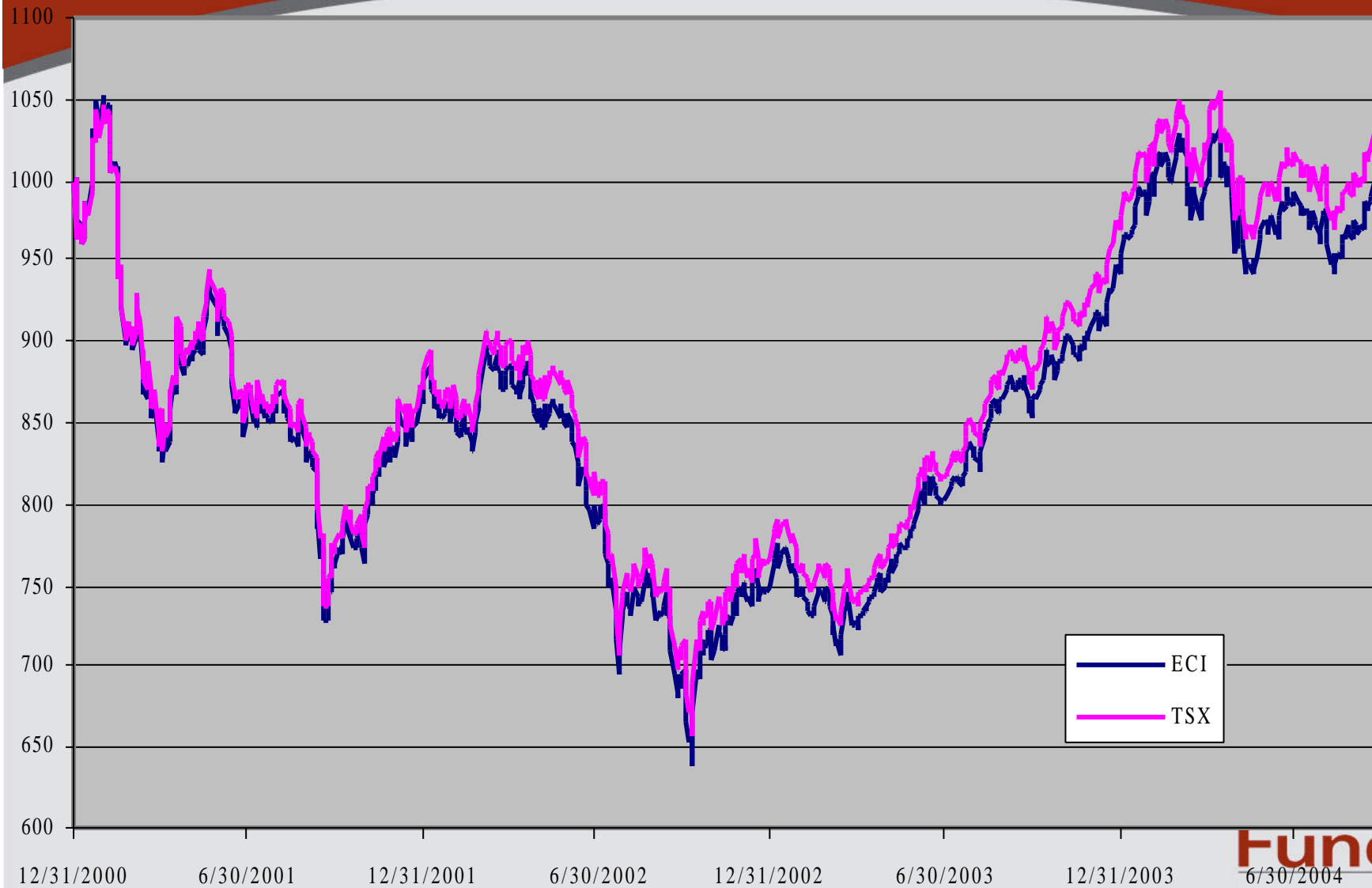


Jantzi Social Index

Comparative Returns - Dec 1999 to Aug 2004



Ethical Canadian Index



Performance Studies

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The Literature

- **Financial Academics**
 - Journal of Finance, Journal of Investing
- **Management Academics**
 - Academy of Management Journal, Journal of Business

The Question

Do portfolios consisting of socially responsible companies outperform the market over the long term?

Finance Academics

- MPT: the application of screens to any universe of stocks will mean underperformance
- “Tying the hands of the fund manager”
- Problem: performance of screened indexes means that we observe a tie

Management Academics

- Stakeholder theorists:
 - Reduced operating costs
 - Reduced exposure to legal action
 - Enhanced brand image
 - Increased productivity and quality
 - Ability to attract and retain employees
 - Reduced regulatory oversight
 - Access to resources
- Arguments used by proponents of corporate social responsibility and ethical investing

The Latest: Orlitzky's Meta-Analysis

- 2004 Moskowitz Prize Winner
- Orlitzky, Marc, Frank L. Schmidt, and Sara L. Rynes, "Corporate social and financial performance: A meta-analysis." *Organization Analysis*, 24, 2003

What is Meta-Analysis?

- Complex statistical technique
- Aggregates many studies
- Widely used in medical research

Bringing meta-analysis to CSR

- Large body of quantitative work (33,878 observations)
- Determine correlation between CSR factors and return on assets and return on equity (NOT SHARE PRICE!)

Orlitzky's Results

- There is a statistically significant relationship between CSR and Corporate Financial Performance
- The two factors are mutually reinforcing (“concurrent bidirectionality”)
- The correlation is due to improved managerial competency and improved corporate reputation

Bob's Meta-Answer

Companies benefit by adopting socially responsible practices, but these benefits are not fully recognized by the market.

For more information...

www.sristudies.org.

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Question Period

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