Sustainable investing shift

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By Debbie Carlson, Special to Tribune Newspapers

At one time, people who sought to align their social or religious beliefs with their investment portfolios often had to accept lower rates of return for a clear conscience.

They often sought out mutual funds that shunned investments in "sin" stocks such as alcohol, tobacco and gambling, or they avoided investing in companies that produced weapons or used sweatshop labor. Staying out of certain sectors of the market sometimes meant lower returns versus a more diverse portfolio.

Now this type of investing, called sustainable and responsible investing, has evolved to include companies that consider environmental and social impact or corporate governance as much a part of the bottom line as making a profitable product. That's opened a greater universe for socially minded investors who don't want to compromise their beliefs to suit their pocketbooks.

Researchers at Morningstar Inc. and Lipper, two firms that independently research mutual funds, said this investing style has seen a wider number of choices spring up within the past five to 10 years. It's now possible to have an investment portfolio that includes every sector — from small-cap to large-cap domestic and international equity funds to debt instruments — sustainably focused.

David Kathman, senior mutual fund analyst at Morningstar, said several studies have shown sustainably focused funds are competitive over the long-term.

"The theory ... is that if you go with a less diversified portfolio, you'd expect lower return with the same level of risk, all else being equal. But in practice they often have favorable returns. A good manager who is skilled at stock-picking will do well. In the short run some funds do better than others, but over the long run there's no real difference," he said.

Investors can be confident these fund managers have done their research, so if a fund says it is environmentally focused, it's not just a marketing ploy.

"The advantage you have with mutual funds is that they are doing a lot of the dirty work for us. Some funds are hanging their hat on their ability to create well-researched portfolios," said Tom Roseen, head of research services at Lipper.

As of the end of 2011, $3.74 trillion out of $33.3 trillion of investment assets were held by individuals, institutions, investment companies or money managers that practice sustainable investing, according to research from US SIF, a nonprofit that tracks sustainable investing on behalf of member investors. This is up 22 percent since 2009, US SIF said in their biennial study on trends in sustainable investing, released in November.

Some companies now are promoting their track records on being good corporate citizens because they see a financial return to do so, said Chris Laszlo, associate professor, Weatherhead School of Management, Case Western Reserve University.

"Leading companies are starting to look at sustainability as a smart business model. Some of them are not labeling it (as such), but they see this as a way to reduce risk, whether it's regulatory risk or environmental risk. Some want to reduce costs and energy by recycling waste material, for instance," Laszlo said.

Considering sustainability as a profitable way to do business has its roots in advocacy work in the 1990s by socially-minded investment firms and non-governmental organizations to improve corporate social responsibility, said Bennett Freeman, senior vice president for sustainability research and policy at Calvert Investments. Founded in 1976, with over $12 billion in assets under management, Calvert is the largest private asset management firm focusing on sustainable investment.

"This is a hard-headed investing approach. It's part of the business analytical model," he said.

Chad Horning, chief investment officer for Praxis Mutual Funds, a $770 million fund family, said shareholder advocacy and community development is part of what the fund considers when seeking investments. Everence Financial is the adviser to Praxis and the stewardship agent of the Mennonite Church USA.

His fund screens out the traditional "sin" stocks but they also seek to work with companies to improve how they do business on a social or environmental scale. Praxis and other sustainable funds recently worked with Hershey to help them start sourcing cocoa beans that don't involve child labor by 2020.

"As an investor, we want these companies to succeed. If we didn't like them, we wouldn't invest in them in the first place," he said.

Like any investment, someone who wants to include sustainability as a selection criteria needs to compare a particular fund against a similar benchmark and take into consideration fund manager fees.

"This is such a diverse asset class. It's hard to make too many generalities. You need to look at the same things you'd look at for any mutual fund. See how it performs relative to its peers," Kathman said.

For instance, Roseen said, an investor interested in adding A-rated corporate debt should compare one of the 11 sustainably focused funds investing in this field to the average of all A-rated corporate debt. Lipper's research shows the one-year return for the full range of A-rated corporate debt funds was 8.04 percent, while the average of sustainable funds that offer A-rated corporate debt was 8.7 percent.

Those who want to find out more about this investment style can start by looking at online fund research firms like Morningstar, Lipper or others. Typically, they will break down a fund's overall investments, its track records, fees and perhaps other factors and rate their performance versus peer group.

One of the top picks included from both Morningstar and Lipper are the Amana funds, a religious-themed fund, while in the secular funds, Morningstar highly rates the Neuberger Berman Socially Responsive Fund.

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