

Virtue's Rewards

For years, the conventionally wise have held that social investors put themselves at a financial disadvantage because they limit their stock choices to the universe of clean, responsible companies. Those of us in the SRI field have countered that environmental and social screens effectively point to companies that are well managed as a whole, and outstanding management is key for beating the market averages.

Until recently, the arguments on each side had been largely rhetorical. During the eighties, the sample of investments under broad screens was too limited to make robust comparisons. In the nineties, the markets were rising steadily, so SRI portfolios hadn't been tested in a downturn.

Now, with SRI dollars in the trillions and the market cycle having turned distinctly netherward, apples-to-apples studies are showing that, over time, SRI portfolios indeed perform at least as well as their unscreened counterparts.

The most compelling evidence comes from the two longer-standing social index funds. The Domini 400 Social Index, comprising about half the companies of the S&P 500 Index, plus another 150 notably "social" companies, has generally outperformed the S&P since the DSI started in 1990. The tech wreck took some of the sheen off DSI's sterling numbers, but a ten-year look has DSI averaging 19% annually, the S&P 500 Index, 17.5%. Similarly, the socially screened Citizen's Index of 300 large-cap companies, established six years ago, has handily outpaced the S&P 500 with a 299% cumulative gain vs. 227%.

None of this is a secret, of course, so the biggest players on the Street are joining in: First,

TIAA-CREF (the giant teachers retirement fund) and Merrill Lynch with its Eco-Logic Fund; more recently, Vanguard and even Dow Jones.

Studies linking corporate responsibility and financial performance are commonplace now, though they come from varied directions. Among them:

- NY-based Innovest has developed a 60-criteria environmental scale for ranking companies. The firm finds that the best environmental performers easily see the best financial returns.

- A Social Investment Forum study showed that despite 2000's market volatility, 14 of 16 socially screened mutual funds with assets over \$100 million earned 4 or 5 stars from Morningstar and/or an "A" or "B" rating from Lipper.

- In *Doing Well by Doing Good: The Bottom Line on Workplace Practices*, Ted Baker surveyed others' research and found that many "high-performance work practices" are associated with stronger bottom lines.

- Repetto and Austin of the World Resources Institute recently published *Pure Profit: the Financial Implications of Environmental Performance*. One conclusion: "Knowing ahead of time which companies are better positioned to deal with environmental issues could pay off handsomely in superior investment performance." continued on page 4

WORTH READING...

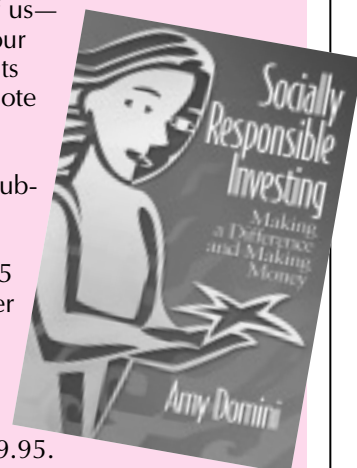
Amy Domini's New Book
Socially Responsible Investing: Making a Difference and Making Money

It's not easy writing books about social investing—finish one and its almost time to begin another. It certainly helps, though, to have Amy Domini's sense of timing.

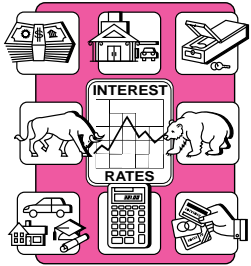
Domini's first book was *Ethical Investing*, co-authored with Peter Kinder in 1984. Since then, Domini has arguably become the leading figure in SRI by writing or co-writing numerous books and articles; speaking about SRI here and abroad and in all the major media; co-founding KLD, a major corporate social research firm; and helping develop the Domini Social Index and Domini family of mutual funds.

Now comes her latest book, introducing newcomers to social investing and updating the rest of us. Written in her signature style—clear and engaging, with as much space devoted to illustrative sidebars as general text—the book stays on the social, rather than financial, side of SRI. And without direct reference to the critics who maintain that social change won't come without financial sacrifice, Domini simply points out many areas in which SRI has succeeded on both the financial- and social-change fronts.

Domini's timing is right, as usual. Attractive financial returns have vast numbers of potential investors considering SRI. Amy Domini is here to help them—and all of us—see how our investments can promote a more humane society. Published by Dearborn Trade, 155 N. Wacker Drive, Chicago, IL 60606. 312-836-4400. \$19.95.



CLEAN PROFILES



Interest Draws Interest

Thanks to Alan Greenspan's change of heart, the stock groups that respond most positively to downward moves in interest rates have performed well during the last few months.

The banks and life and property casualty (P/C) insurance companies have led the sector.

The stocks of banks such as **First Virginia**, **Region's Financial**, **First Tennessee**, and one of our recent favorites, the Puerto Rican bank **Popular**, have responded to the fact that falling interest rates mean a more favorable spread between what banks lend money for and what they borrow it for. The stocks are also being driven up because value investors recognize that many banks are selling for prices that discount all but the apocalypse.

The P/C insurance companies, represented in our portfolios by companies such as **Harleysville Group** and **Progressive**, are benefiting from three assists to earnings: falling interest rates are boosting the performance of the bond portfolios the companies hold (P/C policies are usually sold at a slight loss, with most earnings coming from the security portfolios), commercial pricing is strengthening, and domestic weather disasters have been few and far between.

To be sure, a slowing economy hurts most industries, and that includes the financial services sector, but the two companies profiled here should weather even a recession in good shape. They both make it a policy to treat their employees and community well. Popular even issues a social responsibility report with every annual report.

INSURANCE



HARLEYSVILLE GROUP (HGIC)

Sales: \$824.8 Million

EPS: 2001E \$1.75
2000E \$1.45
1999A \$1.45

**Projected Annual
Growth Rate:** 10%

Dividend: 2.1%

52-Week High-Low: 30⁵/₈-12

Risk: Moderate (Market)

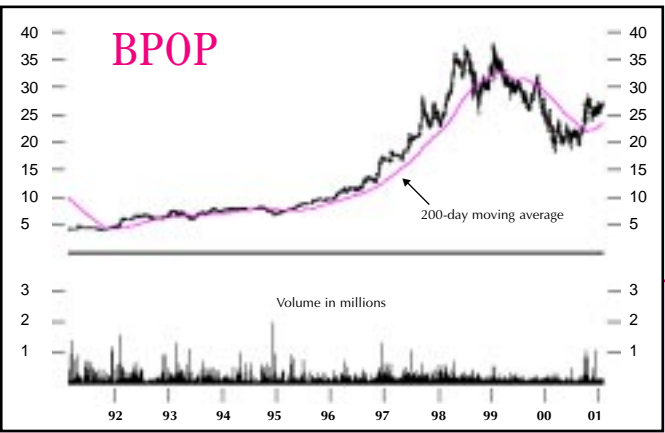
Web site: www.harleysvillegroup.com

PREMIUM VALUE

Top Rated A+ for financial condition and operating performance by the respected rating agency A. M. Best Co., Harleysville is a property casualty (P/C) insurance holding company. It derives much of its strength from pooling the premiums, losses, and expenses of numerous P/C subsidiaries and its parent, the Harleysville Mutual Insurance Co. HGIC's and Mutual's insurance policies are marketed primarily in the East and Midwest. Lines include homeowners, personal auto, commercial, and multi-peril. Nearly 3,000 independent agencies sell HGIC policies, with most commercial coverage written for midsize and small firms.

Natural disasters, fierce competition that has kept rates down, and rising interest rates that have punished bond portfolios led to many consecutive years of poor performance in the P/C industry. This past year, however, has been quite different. It has been notable for the absence of domestic physical catastrophes, a rise in premiums and prices, and appreciating bond prices. Harleysville, which continues to build a national presence by acquiring a network of regional insurance companies, has participated in the industry's good fortune. Earnings next year should jump 25%, and we suspect that the stock, which has already more than doubled off of its 52-week lows, will continue to forge ahead.

Corporate Responsibility: HGIC has a solid social profile. The State of Pennsylvania, in a new initiative to recognize local employers, recently named the company one of the "Best 100 Places to Work." In past years, the company had no female or minority representation on the board of directors. This changed last April when Mirian Graddick, an African-American woman, was named to the board.



POPULAR (BPOP)

Sales:	\$2.6 Billion	Projected Annual Growth Rate:	10%
EPS:	2001E \$2.17	Dividend:	2.4%
	2000A \$1.97	52-Week High-Low:	28 ³ / ₄ –18 ¹ / ₈
	1999A \$1.84	Risk:	Moderate (Market)
		Web site:	www.bppr.com

BANKING ON FALLING INTEREST RATES

Popular, Inc., is the holding company for 107-year-old Banco Popular, Puerto Rico’s dominant bank, with over \$25 billion in assets. Ranked by the FDIC as a Tier 1, “well-capitalized” institution, BPOP also operates an insurance subsidiary and has bank branches on the mainland and in other Caribbean nations. The company’s loan portfolio is well diversified, with commercial, industrial, and agricultural loans making up 45% of the portfolio, mortgages 26%, and commercial loans 22%. Net income has risen for 25 consecutive years, a record that few banks anywhere share.

The Fed’s recent interest rate cuts bode well for the banking sector. Long-term, loan demand picks up and banks are able to benefit from a better spread between what they pay for deposits and what they make on loans. In the short term, however, the stimulus for the lower rates—a slowing economy—will probably mean softening loan demand. Popular has been in this position many times in the past and has always made the adjustments necessary to stay well in the black. That is certainly one of the reasons more investors are buying Popular’s stock. In response to strong demand, the stock has jumped ten-fold during the last decade. We are banking on it to continue this performance.

Corporate Responsibility: Popular’s strongest social suit is its community relations program. A progressive, crusading newspaper publisher founded the bank in 1893. Today, his work is carried on by the Banco Popular Foundation. It has made generous contributions to hundreds of community, cultural, sports, and educational organizations. BPOP also has a long history of providing aid and volunteer manpower to assist the victims of the many natural disasters that have afflicted the area.

Rich Americans appear to be in for a tax-cut bonanza, but, thanks to **Intuit, Inc.**, lower-income citizens are at least able to get their refund checks a little more quickly. Last tax season, the Quicken Tax Freedom Project provided over one million free online tax returns to taxpayers with incomes under \$20,000. This year Intuit has upped the income minimum by \$5,000, and many more are expected to take advantage of the offer.

“We have to look at ways to continue to attract and retain a talented and diverse workforce,” said **BellSouth’s** vice chairman Jere Drummond in a recent press release. The context of his statement is the board’s decision to extend a full range of medical and life insurance benefits to same-sex domestic partners of management employees. Given that talent is needed at all levels of a company, perhaps BellSouth should follow its own logic and offer the benefits to rank-and-file workers’ same-sex partners as well.

The **Charles Schwab Corp.** recently set up an internal Web site to help employees find community volunteer opportunities and avenues for charitable giving. The Schwab corporate foundation already double-matches employee charitable giving up to \$5,000 per calendar year.

Kudos to **Fannie Mae** for handily exceeding its goals in serving low- to moderate-income households. The huge, federally chartered mortgage company had been criticized in recent years for neglecting low-income households. HUD oversees Fannie Mae, and that agency had set up guidelines requiring the company to serve 42% of households in the low- to moderate-income range in 2000. FNM reached 49%. The company also exceeded goals for financing under-served areas and very low income households.

Yum's the Word

We received so many compliments on the Bien Fait teacakes we sent out to clients for the holidays that we thought we ought to give credit where it's due. Our neighbor, Alice Perron, creates the tasty fruitcakes that have brought us so much goodwill.

Alice started her mini-bakery seven years ago when it became clear that income from the family dairy farm wouldn't cover all the bills, so she decided to open a farmhouse-based baking business. Sticking to all-natural ingredients, Alice spent a year developing recipes before she made her offerings public. "Fruitcakes have a horrible reputation," she says, "so I had to make something that was really good-tasting."

In a fortuitous fluke, in her first year, a Bien Fait morsel crossed the palate of a *NY Times* food editor who was passing through. The resulting rave review jump-started the business. But Alice's products also do a lot of speaking for themselves, and now she produces over 3,000 cakes a year.

Sampling Alice's wares via brochures and Web sites is admittedly a far cry from tasting them, but you can see her fruitcakes, granola, and pancake mix by calling 888-313-7128 or visiting www.allroutes.to/bienfait.com.




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Viva la Resolution

Several readers have requested an update on recent and planned proxy resolutions. We are happy to oblige.

Early last year, on behalf of a client, we co-filed a shareholder resolution at Home Depot asking HD to produce a report on the advancement of women and minorities. In discussions led by primary filer Heidi Soumerai of Walden Asset Management, HD hardly budged. Our coalition won a respectable 10.3% of the vote, but HD still isn't budging, so we may file again.

In the spring, we co-filed at Heinz at the behest of a foundation client. The resolution asked that foods containing genetically modified organisms be labeled and eventually phased out if not proven safe. After fruitful across-the-table discussions with upper-echelon Heinz staff, the primary filer, Sr. Barbara Aires of the Sisters of Charity, suggested the proposal be withdrawn. We concurred. The dialogue with Heinz' General Counsel's office is continuing.

More recently, a charitable-trust client became the primary filer of a board diversity initiative at Clarcor, a manufacturer of filters and packaging. A trustee teamed up with us in researching and drafting the resolution, which urged the all-white-male

board to add women and minority members. As the printing deadline loomed, Clarcor's counsel telephoned in a conciliatory mood. In the end, the board committed publicly to use its "best efforts" to bring on at least one woman or minority within the next two years. Our client agreed to withdraw the resolution.

Based on a preliminary survey by ICCR, which coordinates most social resolutions, there will be at least thirty initiatives at CY companies. Some examples: AIG—no sexual orientation discrimination; AT&T—tying executive pay to customer satisfaction; Coca-Cola—phase out GMO foods; Lincoln National—no investments in tobacco; Home Depot—endorse the CERES environmental principles; First Tennessee Bank—bar predatory lending; Heinz—implement a code to eliminate sweatshops and child labor.

We are pleased to work with clients interested in joining these campaigns or starting their own. To meet SEC requirements, a shareholder must own a minimum of \$2,000 of stock for one year. Typically, filing deadlines are in the fall, in advance of annual meetings that take place April through June.

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- Analyst John Hale studied Morningstar's mutual funds data. He found, among many favorable comparisons, that 20% of the SRI funds achieve a 5-star rating, which is earned by only 10% of Morningstar's full universe.
- Professor Curtis Verschoor of DePaul University, in a study of 500 companies, found those that publicly commit to an ethics code perform better financially.
- Professor James T. Hamilton of Duke University in *Pollution as News: Media and Stock Market Reactions to the Toxic Release Inventory Data* found that the day after companies get negative press for TRI disclosures, their stock prices drop significantly.

Our Web site, www.cleanyield.com, features researcher Lloyd Kurtz' ongoing survey of studies which explore social factors and financial outcomes. Click on "SRI Research" in the News section.