



Responsible Investing: Making Informed Investment Decisions

Global Conference 2009



Responsible Investing: Making Informed Investment Decisions

Tuesday, April 28, 2009; 2:30 PM - 3:45 PM

Moderator:

Betsy Zeidman, Research Fellow and Director of the Center for Emerging Domestic Markets,
Milken Institute

Speakers:

Harold Bradley, Chief Investment Officer, Ewing Marion Kauffman Foundation

Sean Harrigan, President, Los Angeles Fire and Police Pension Commission

Barbara Krumsiek, President, CEO and Chair, Calvert Group Ltd.

David Marchick, Managing Director and Global Head of Regulatory Affairs, The Carlyle Group



Many names for responsible investing

- Mission-related investing
- Mission-based investing
- Mission investing
- Impact investing
- Aligned investing
- Active investing
- Full value investing
- Double (or triple) bottom line investing
- Environmental, social, and corporate governance (ESG) investing
- Sustainable investing
- Socially responsible investing (SRI)
- Ethical investing
- Targeted investing
- Blended value investing

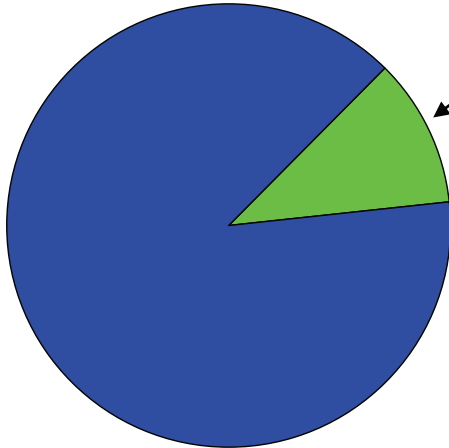


The premise

- Investments can generate collateral benefits – or costs – in addition to financial returns
- Environmental, social and governance (ESG) factors can positively (or negatively) affect the performance of the financial asset
- Investment decisions are better when based on financial returns and extra-financial impacts



Size of responsible investing in the U.S.

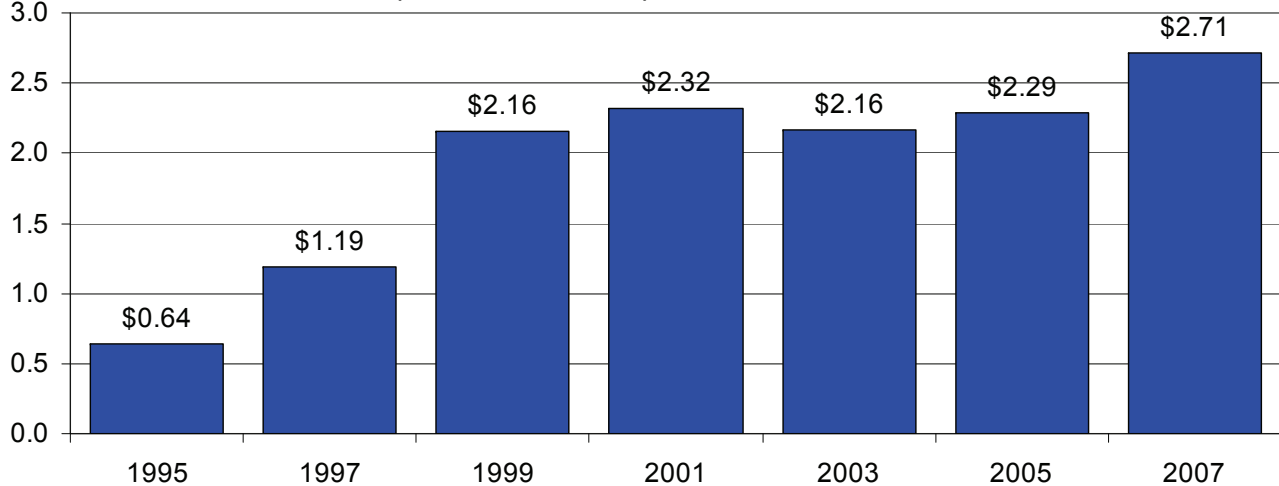


\$2.71 trillion or about **11 percent of total assets** under management in the U.S. is involved in socially responsible investing

Source: Social Investment Forum, "2007 Report on Socially Responsible Investing Trends in the United States."

Socially responsible investments are increasing

Assets involved in SRI (in US\$ trillions)



Source: Social Investment Forum, "2007 Report on Socially Responsible Investing Trends in the United States."

Principles for Responsible Investment



MILKEN INSTITUTE

An investor initiative in partnership with the UN

- Aim is to help investors integrate consideration of ESG issues into investment decision-making and ownership practices (consistent with fiduciary duty) and thereby improve long-term returns to beneficiaries
- Principles include commitment to incorporating ESG into investment analysis, to be active owners, and to seek ESG disclosure
- Signatories include 400 asset owners, investment managers and professional service partners from around the world

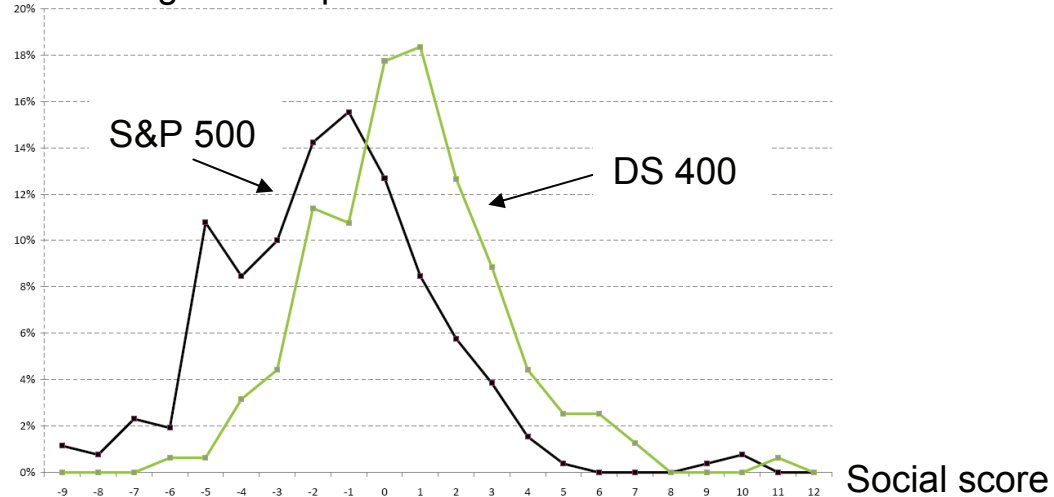
Source: UN Principles for Responsible Investment website.

Returns on responsible investments compare to traditional investments

- Statman and Glushkov (2008) analyzed returns of stocks rated on social responsibility for the years 1992–2007.
- They found that negative screening resulted in a return disadvantage relative to conventional investors, while investing in companies with high social responsibility scores resulted in a return advantage.

How S&P 500 and DS 400 compare in terms of social responsibility

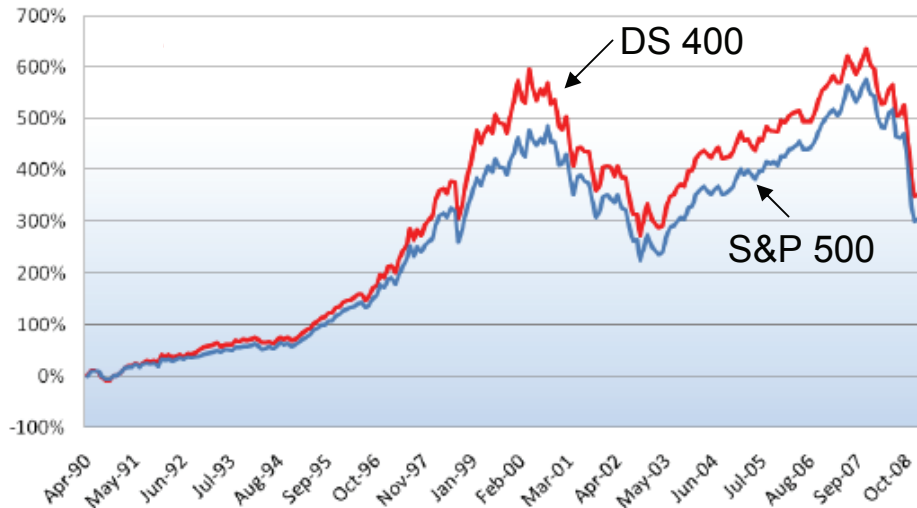
Percentage of companies



Note: Each index is measured using KLD scores.

Source: Meir Statman and Denys Glushkov, "The wages of social responsibility," working paper, December 2008.

How S&P 500 and DS 400 compare in terms of performance



Source: KLD Research & Analytics, Inc.

Performance of green funds against their benchmarks

	Green Century Equity Fund	S&P 500	Winslow Green Growth Fund	Russell 2000 Growth Index
1 year	-35.5%	-38.1%	-52.8%	-36.4%
3 years	-13.3%	-13.1%	-26.0%	-16.2%
5 years	-6.2%	-4.8%	-9.6%	-5.4%
10 years	-4.5%	-3.0%	5.3%	-1.6%

Green Century Equity Fund: Invests essentially all of its assets in the KLD 400 Index which is screened to exclude those companies with the worst environmental and social records

Winslow Green Growth Fund: Invests in small growth companies that have a positive or neutral impact on the environment

Sources: Green Century Capital Management, Inc. and Winslow Management Company websites.



Responsible investments toolbox

BELOW-MARKET-RATE TOOLS

- **Grants**
- **Recoverable grants**
- **Guarantees / credit enhancement**
- **Below-market loans**
 - Revolving loan funds
 - Gap financing
 - First-loss loans
- **Community development venture capital**

MARKET-RATE TOOLS

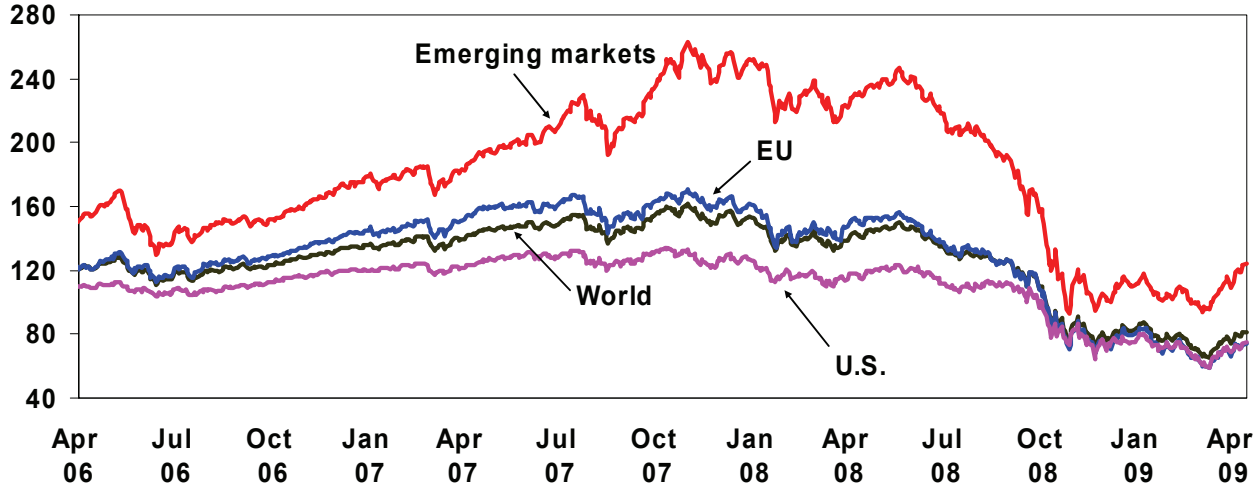
- **Cash (deposits)**
- **Loans**
 - Senior
 - Subordinated
 - Guarantees
 - Loan funds
 - Line of credit
- **Fixed income**
 - Bonds
 - Bond funds
 - Asset-backed securities
- **Public equity**
 - Screened funds
 - Direct public equity
 - Shareholder engagement
- **Alternative assets**
 - Direct private equity
 - Private equity funds
 - VC funds
 - Fund of funds
 - Buyout funds
 - Hedge funds
 - Real estate
 - Natural resources





Global equity index

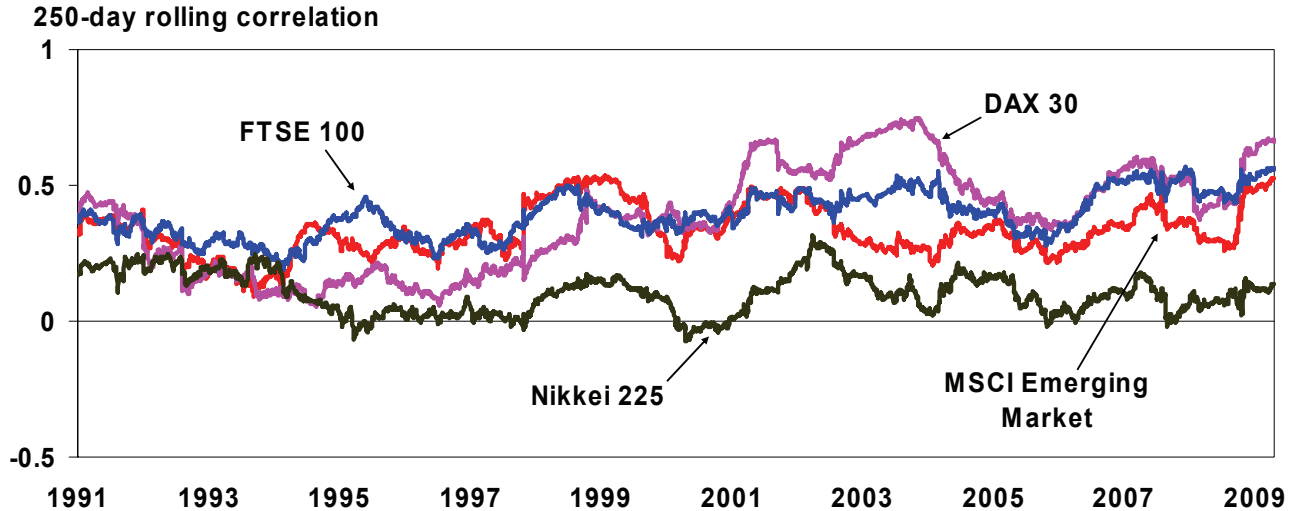
January 2005 = 100



Source: Datastream.



Correlation of global stock markets with S&P 500

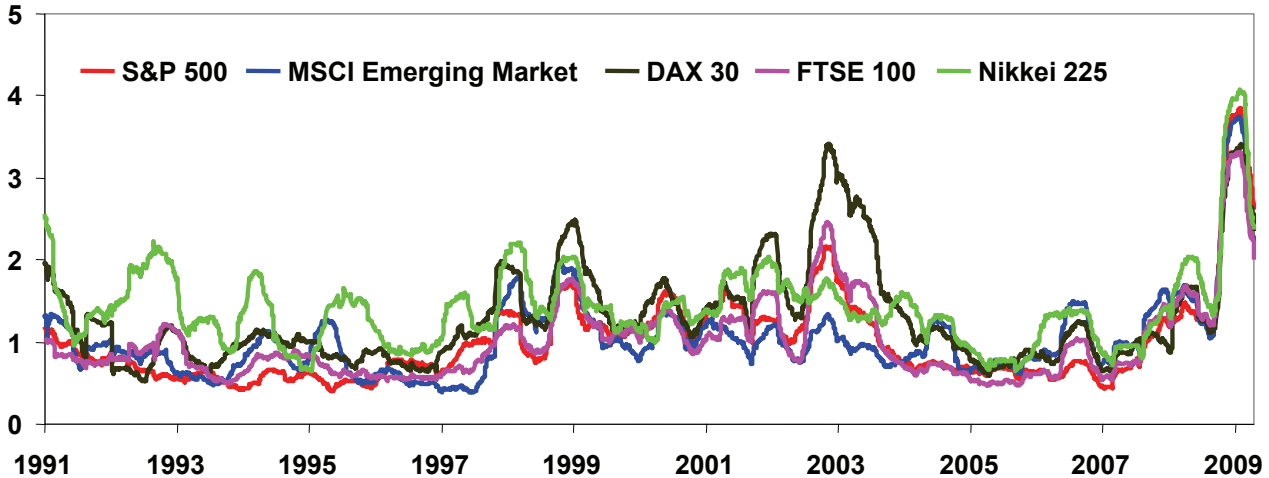


Source: Datastream.

Stock market volatility

Volatility is off its peak

A rolling 100-day standard deviation of equity prices



Note: The data is as of April 15, 2009; Source: Datastream.

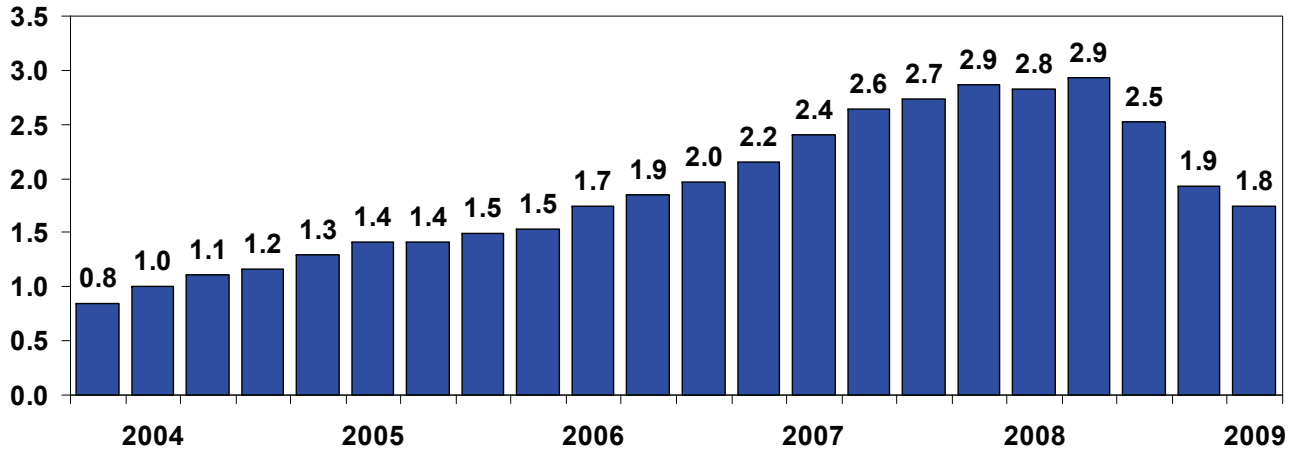
Private equity activities slow globally

	Deal value announced (US\$ millions)		Fund raised (US\$ millions)	
	2007	2008	2007	2008
United States	368,400	59,600	325,200	256,900
Western Europe	185,900	88,000	101,500	96,100
Asia	67,000	52,500	28,700	37,100
Middle East	898	1,700	5,000	6,400
Eastern Europe	27,900	8,000	14,600	5,400
Latin America	4,600	1,200	4,400	4,000
Africa	7,900	2,200	2,300	2,600
Total	662,598	213,200	481,700	408,500

Sources: Dow Jones, Dealogic.

Worldwide hedge fund assets drop by 40 percent since Q2 2008

US\$ trillions

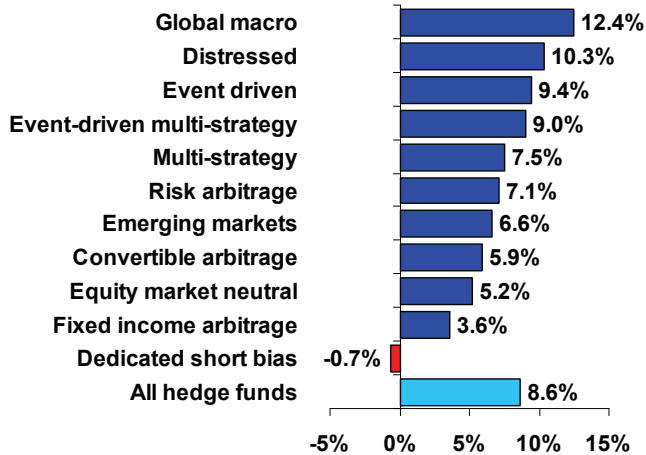


Sources: Hedgefund.net, The Milken Institute.

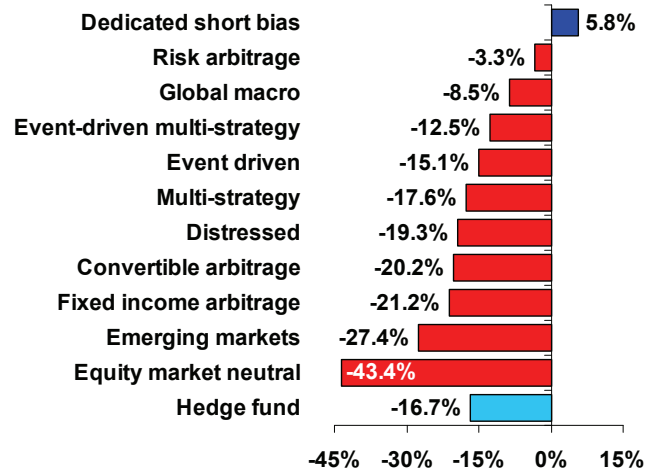


Hedge fund returns, different strategy

Annualized return, January 1994–March 2009



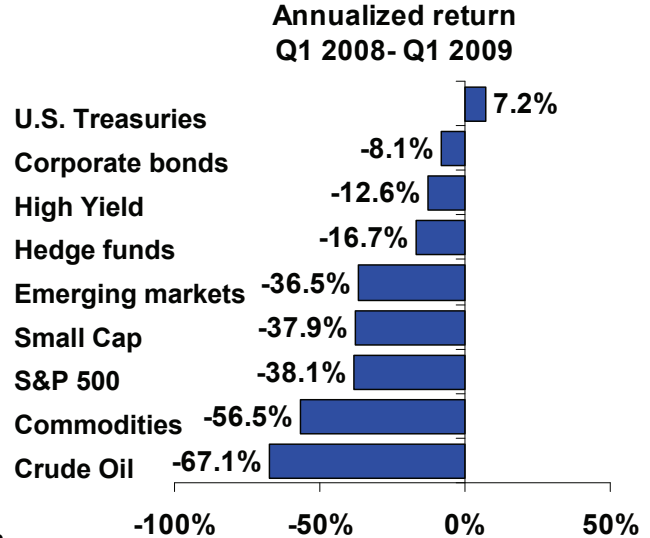
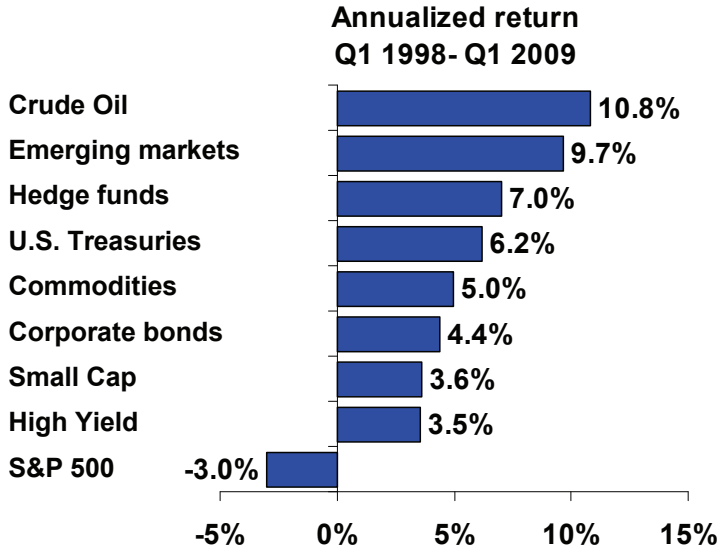
Annualized return, March 2008–March 2009



Sources: Bloomberg, The Milken Institute.



Total returns of selected asset classes



Sources: Bloomberg, Datastream, The Milken Institute.



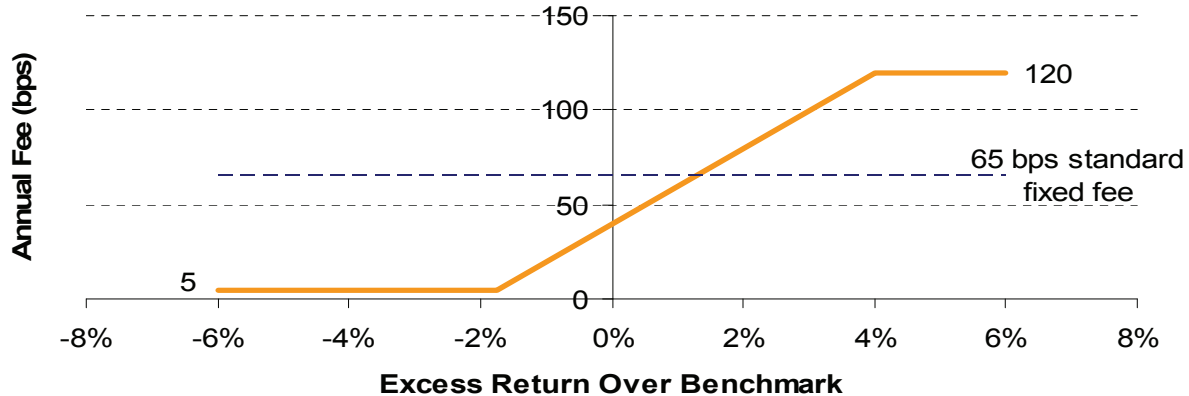
Panelists' slides



Harold Bradley
Chief Investment Officer
Ewing Marion Kauffman Foundation

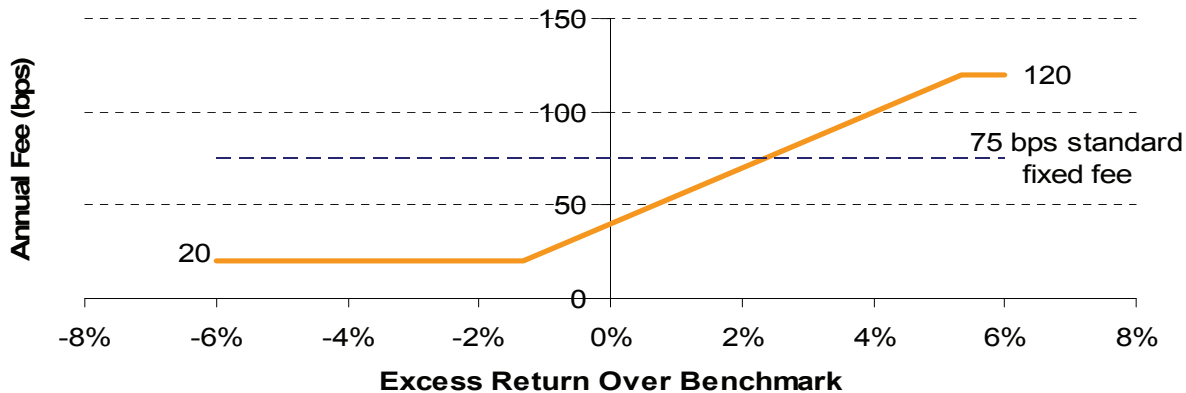
Using variable fee schedules for equity accounts

Fund A Variable Fee Schedule 40 bps + 20%*ER, min 5, max 120



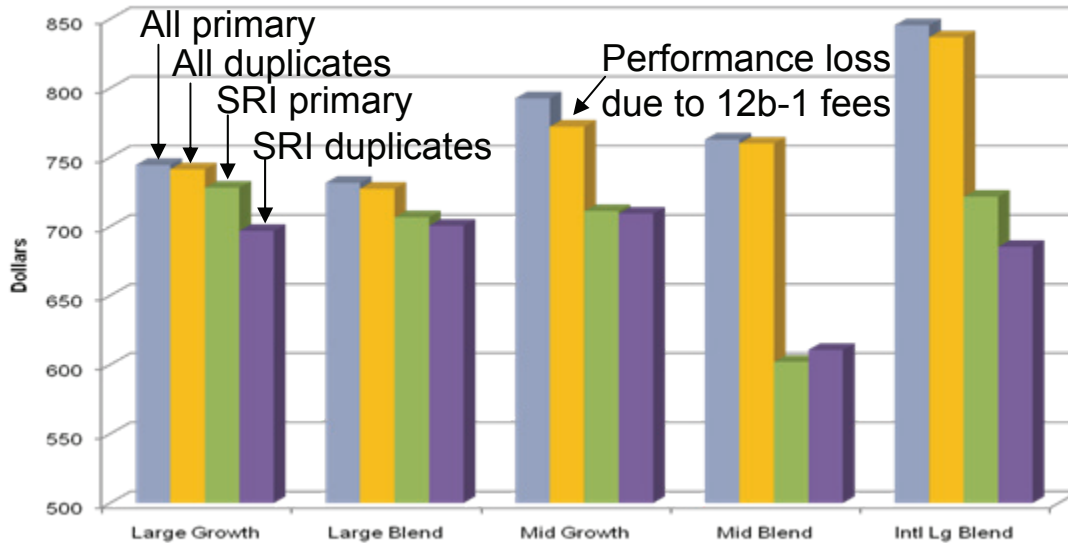
Using variable fee schedules for equity accounts

Fund B Variable Fee Schedule 40 bps + 15%*ER, min 20, max 120



Five-year impact on \$1,000 portfolio

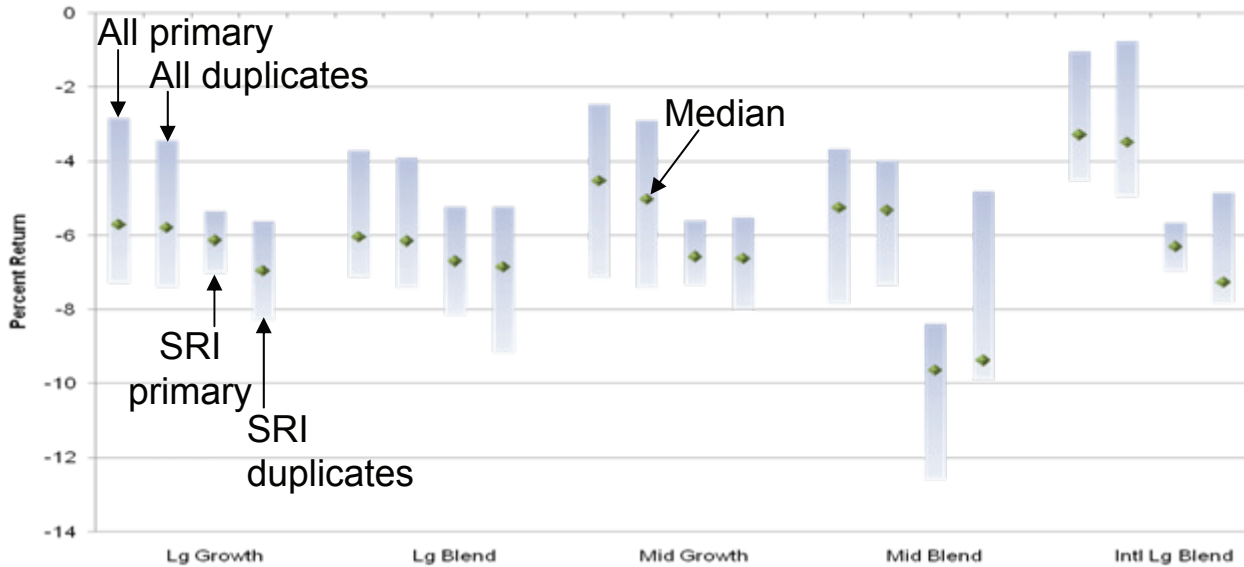
Implicit cost of advice (12b-1 fees) and ESG constraints



Source: Morningstar mutual funds database.

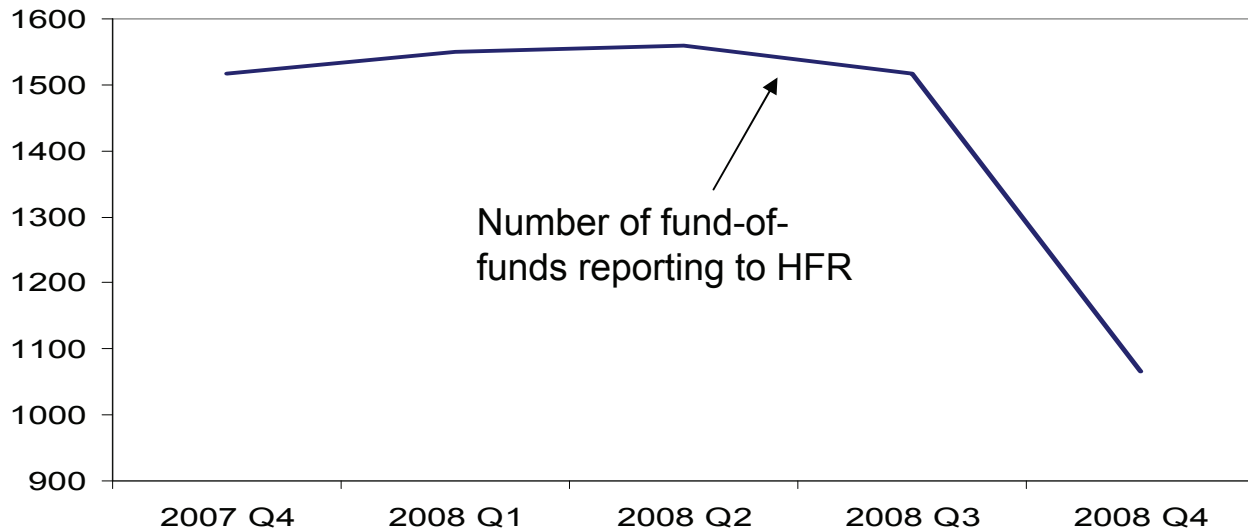
Distribution of annualized five-year returns

Broad peer group vs. SRI peers



Hedge funds as an asset class

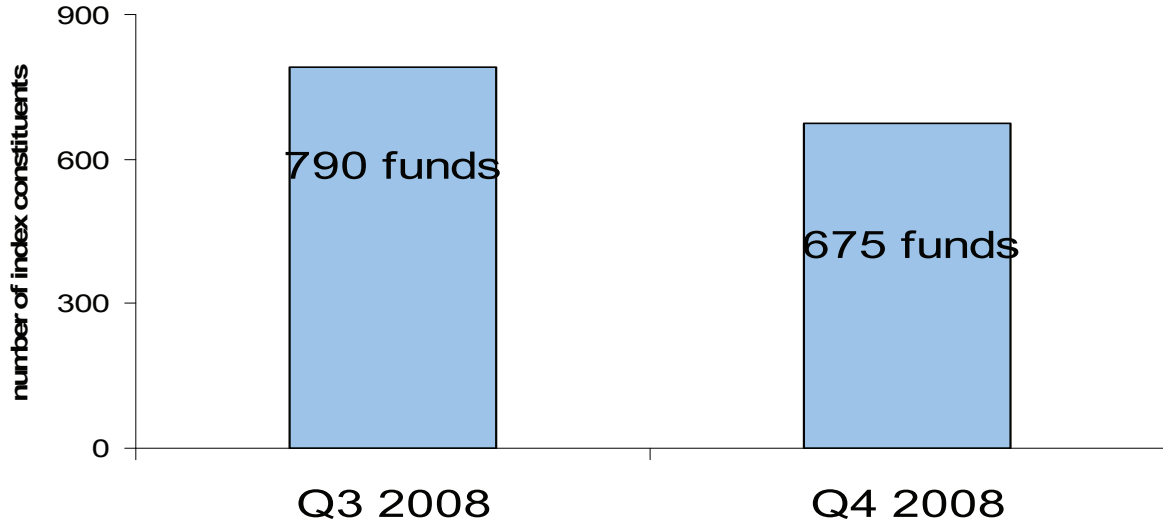
Survivorship bias: Many fund-of-funds stopped reporting in Q4 '08



Source: HFRI database.

Constituents for HFR fund-of-funds index

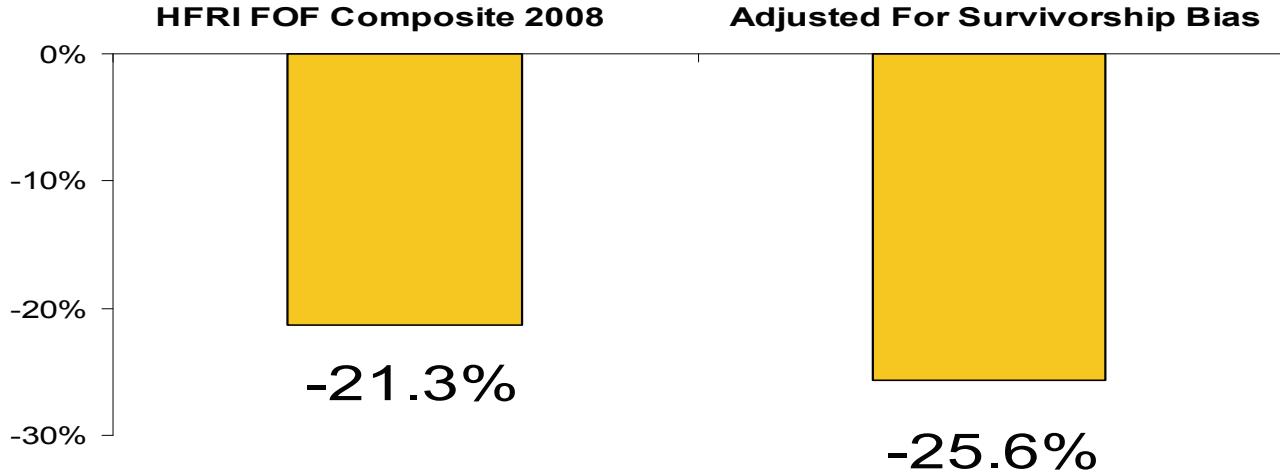
Does anybody know the real returns and volatility?



Source: HFRI.

Hedge funds as an asset class

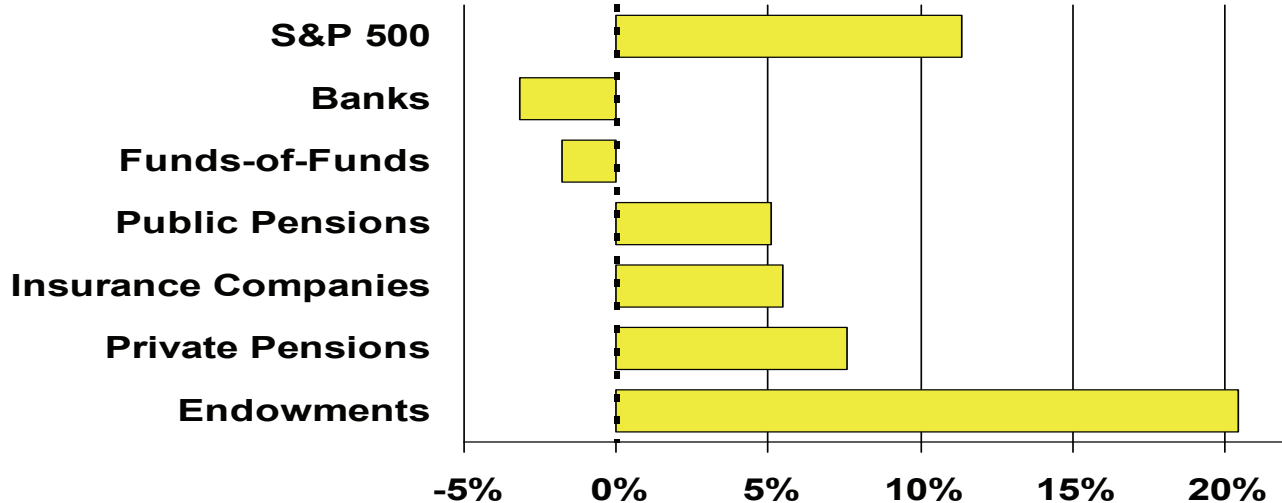
How did they perform?



Assumption: Funds that stopped reporting lost half their value on average.

Private equity performance by investor type

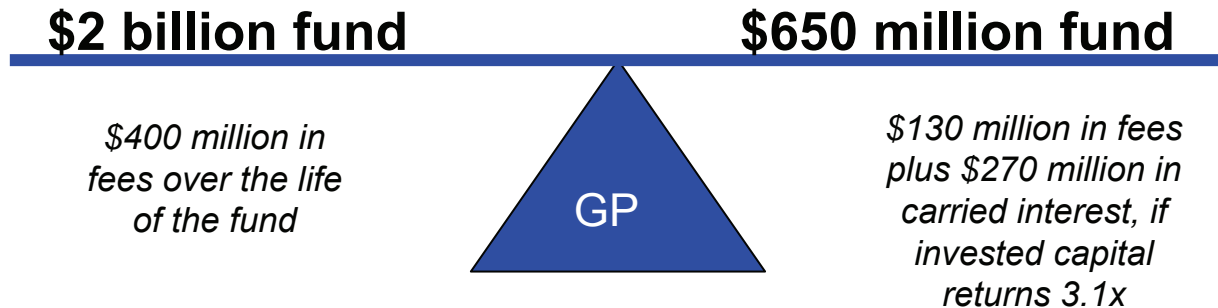
Funds between 1992 and 2001



Source: Lerner, Schoar and Wang, 2007.

Courtesy of Josh Lerner, HBS.

Why do we pay GPs to get huge...



Source: Andrew Metrick and Ayako Yasuda, "The Economics of Private Equity Funds," Wharton School, University of Pennsylvania, 2007.