

In 2003, investments using socially responsible criteria exceeded \$2.63 trillion worldwide.¹ The United States, with the most developed socially responsible investment (SRI) market, accounted for \$2.16 trillion of this total.² While the SRI market in Western Europe is a distant second at \$413 billion, it is growing rapidly—a trend that is expected to continue.³ Australia and Canada added another \$55 billion, while SRI in Asia and emerging markets is undeveloped; each totaled less than \$3 billion.⁴

Socially responsible investing, in the broadest terms, includes three major approaches: screening, shareholder advocacy, and community investment.⁵ Screening can involve negative screens that exclude unacceptable industries, such as tobacco, weapons, or nuclear energy, and positive screens that select companies with superior environmental and labor records that produce safe and useful goods. Shareholder advocacy, a strategy often coupled with screening, refers to investment in a company in order to influence its decisions through shareholder resolutions. The third strategy is community investing, in which people invest in communities, often ones that are underserved by other financial services, in order to increase total capital flows to them.

SRI has proved itself to be an investment strategy not just for social reformers but for all investors. The major SRI portfolios have shown themselves to be competitive with conventional ones. For example, over the past 10 years the Domini 400 Social Index—a portfolio based on the S&P 500 that screens out 250 unacceptable corporations and adds 150 socially responsible ones—has provided an average 12.6 percent in returns each year, while the S&P 500 has given 11.9 percent.⁶

SRI has a long history, especially with religious organizations. As early as the seventeenth century, the Quakers screened out weapons companies from their investments.⁷ In the 1920s, the Methodist Church in the United Kingdom used negative screens to avoid investment in “sin stocks.”⁸ But it was the Pax World Fund, an SRI mutual fund created in 1971, that launched the modern SRI movement.⁹ By 1984, \$63 billion

had been invested in SRI funds in the United States.¹⁰

In the 1990s, SRI started to flourish in the United States, with investments nearly doubling between 1995 and 1997 and almost doubling again two years later.¹¹ (See Figure 1.) While total SRI funds declined 10 percent between 2001 and 2003, the percentage of SRI funds compared with total investments under professional management remained stable at around 11 percent, since total investments declined from \$20.6 trillion to \$19.2 trillion.¹²

Of the \$2.16 trillion invested in SRI in the United States in 2003, \$1.7 trillion was in the form of screens, while \$441 billion used both screens and shareholder advocacy.¹³ Another \$7 billion went into just shareholder advocacy, and \$14 billion went to community investing.¹⁴ While the funds invested in shareholder advocacy declined 52 percent between 2001 and 2003, the number of resolutions filed increased 15 percent.¹⁵

The success of shareholder resolutions is often limited, both because successfully passed resolutions are nonbinding and because a large percentage of shares are owned by non-voting institutions.¹⁶ Indeed, the average vote in favor of resolutions that addressed social responsibility issues was just 11.4 percent in 2003 (compared with 8.7 percent in 2001).¹⁷ The power of shareholder advocacy comes more from the pressure that corporations feel to change policies when confronted by shareholder activists. Of the 292 resolutions filed in 2002, 95 were withdrawn before voting after policy changes were agreed on with the management.¹⁸

Community investments, while significantly smaller than the other forms of SRI, are growing quickly, with total investments increasing 84 percent between 2001 and 2003.¹⁹ Community development financial institutions (CDFIs), including development banks, credit unions, loan funds, and venture capital funds, finance projects that build affordable housing, create livable-wage jobs, or provide essential services such as health care.²⁰ Although the investments are comparatively small, the effects of community investing are impressive. A survey of 442

U.S. CDFIs found that in 2002 these institutions financed 7,800 small businesses that established or sustained 34,000 jobs, and they facilitated the building or renovation of 34,000 units of affordable housing and over 500 community facilities.²¹

Europe's SRI market is growing rapidly, with more than \$413 billion currently invested in this market.²² Of these funds, \$268 billion is in screened portfolios, while \$145 billion is used for shareholder advocacy.²³ The Netherlands and the United Kingdom account for 98 percent of the \$413 billion, primarily from the heavy investment of pension funds.²⁴

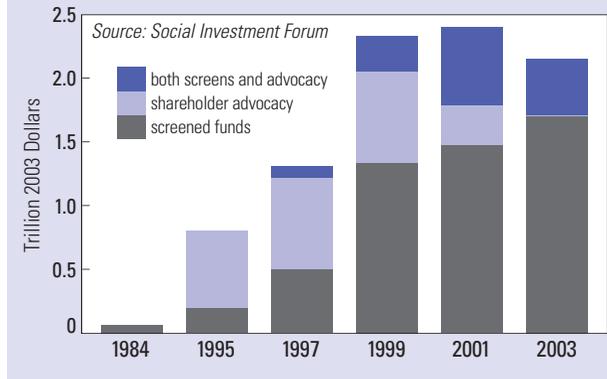
In the United Kingdom, the shift of pension funds to SRI was stimulated by a law requiring them to disclose how much consideration they give to social, environmental, and ethical issues.²⁵ A second law, which requires charities to ensure investments are in line with the charity's stated goals, further strengthened the SRI sector there.²⁶ While the SRI markets in other European countries are still undeveloped, as these countries pass similar pension legislation, which many are currently considering, SRI could become increasingly the norm across Europe.²⁷

The SRI market in Asia—just \$2.5 billion—is still very immature.²⁸ But it is growing quickly: between 2001 and 2002, the number of new funds increased 32 percent.²⁹ The Japanese market, 40 percent of the regional total, is poised to take off in coming years as pension funds—as in Europe—start to adopt SRI initiatives.³⁰

In most developing economies, SRI virtually does not exist. While the total is estimated at about \$2.7 billion, \$1.5 billion comes from investors from industrial countries and 95 percent of the remainder is invested in South Africa.³¹ In the short term, growth of SRI is expected to be slow because of the lack of data needed to maintain SRI initiatives, as well as strong competition with non-stock investments.³²

In addition to pension funds, another large

Figure 1. Socially Responsible Investing in the United States, Selected Years



source of funds may start being mobilized in 2005. In April a new investment group, 3iG (the International Interfaith Investment Group), plans to start working with religious leaders around the world to invest religious organizations' funds more responsibly. According to 3iG's estimate, the central institutions of religious organizations have more than \$7 trillion in assets.³³ Committing these monies to SRI could more than triple current global SRI investments and create a powerful new shareholder advocacy force. 3iG is optimistic that not only will it be able to leverage \$1 trillion of these assets but that involvement by religious leaders will spark investment by regional and local chapters as well as by individual members.³⁴ This "cascade effect" could multiply the total benefit severalfold and trigger unprecedented growth in SRI.³⁵

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