Investing in Alignment with Your Values

A special report for socially-conscious investors with an ESG Focus

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Understanding which types of investments should be included in your financial plan is a big undertaking for anyone – let alone wanting to be a socially conscious investor.

So, ask yourself: What is the purpose of my investment portfolio?

For most of us, we hold investments to build wealth we can use for our children's education, to support us in our retirement, and to provide peace of mind. But your investments are also an extension of the values you uphold in the rest of your life. And if your investment portfolio is not aligned with those values, is it meeting your needs?

Sometimes called "sustainable," "socially responsible" or "impact" investing, ESG investing is a way of evaluating companies for their Environmental, Social and/or Governance practices. These labels all have specific meanings in the investment industry but are frequently used interchangeably. Mutual funds and exchange-traded funds (ETFs) that use ESG criteria hold companies that have higher scores in one or more of these metrics.

History of sustainable investing

One definition of sustainable investing is "Shunning profit from the expense of our neighbors." I like this definition as it focuses on why we are trying to align our investments with our personal values. This type of investment standard can be found throughout history. In Biblical times, Jewish law mandated ethical investing. The Koran established guidelines for the responsibilities of investors. In the 1700s, the Quaker and Methodist communities shunned investments in the slave trade, liquor manufacturing and gambling institutions.

In the United States, interest in Socially Responsible Investing (SRI) increased during the 1960s. Protestors of the Vietnam War demanded university endowments divest their defense contractor holdings. The Civil Rights movement led to community development banks being opened in largely minority neighborhoods. Community Development Financial Institutions (CDFI) have continued to grow since the '60s to address racial inequality and in 1977 the Community Reinvestment Act was passed forbidding discriminatory lending practices in low-income neighborhoods.

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Stone Wealth Management

As consumer concern about climate change and the environment grew, the U.S. Sustainable Investment Forum (US SIF) was launched in 1984. Today US SIF represents financial advisors managing over $5 Trillion in sustainable and impact focused assets.

In the 1980s, South African apartheid was opposed by US churches, state pensions and universities. Because of pressure from these groups, US companies were pressed to stop doing business with the South African government until Apartheid was ended. This contributed to economic instability in South Africa and eventually Apartheid was officially ended in 1994.

Although institutional investors like these endowments and pensions have a head start, over the last two decades interest in ESG funds has grown as well as the familiarity of the concept for everyday investors.

What's the difference between E, S and G?

Environmental factors are the easiest to understand. A company will be evaluated on pollution, strategy for climate change, energy efficiency, etc.

Social factors and governance factors overlap a little more. Social includes issues like a company's commitment to diversity, community support and labor practices.

Governance is more about the company itself. Examples include the diversity of the board of directors, where are the political donations of key employees going, and what is the company-approved procedure for addressing sustainability and climate issues?
As an investor, wading through all these letters, acronyms and overlapping information can be tough because ESG funds are measured through multiple lenses at the same time. A company that has a strong E score may not have a good S score. A good S score may have a bad G, etc.

An example is Amazon. According to the well-respected rating company MSCI, Amazon has an average **E**nvironmental score for their carbon footprint. **S**ocially, they get low marks for bad corporate behavior and labor management. But they also have a good **G**overnance score for corporate structure and good data security. Along with market return and other traditional financial metrics, all these criteria are taken into consideration by ESG funds deciding if they want to hold Amazon or other companies with mixed scores.

The important thing to remember is that funds using ESG criteria are not looking for a perfect company. They just want *better than average* management of these issues. Please study the chart below (source: Morningstar):

What Considerations Go Into Sustainable Investing?

Environmental	Social	Governance
Carbon emissions	Diversity & workplace policies	Board structure
Energy efficiency	Labor standards	Board composition
Water scarcity	Supply chain management	Executive compensation
Waste management	Product safety and usefulness	Political contributions & lobbying
Pollution mitigation	Customer privacy	Bribery and corruption policies & oversight
	Community impact	Strategic sustainability oversight

These are examples of ESG criteria but not a complete list.

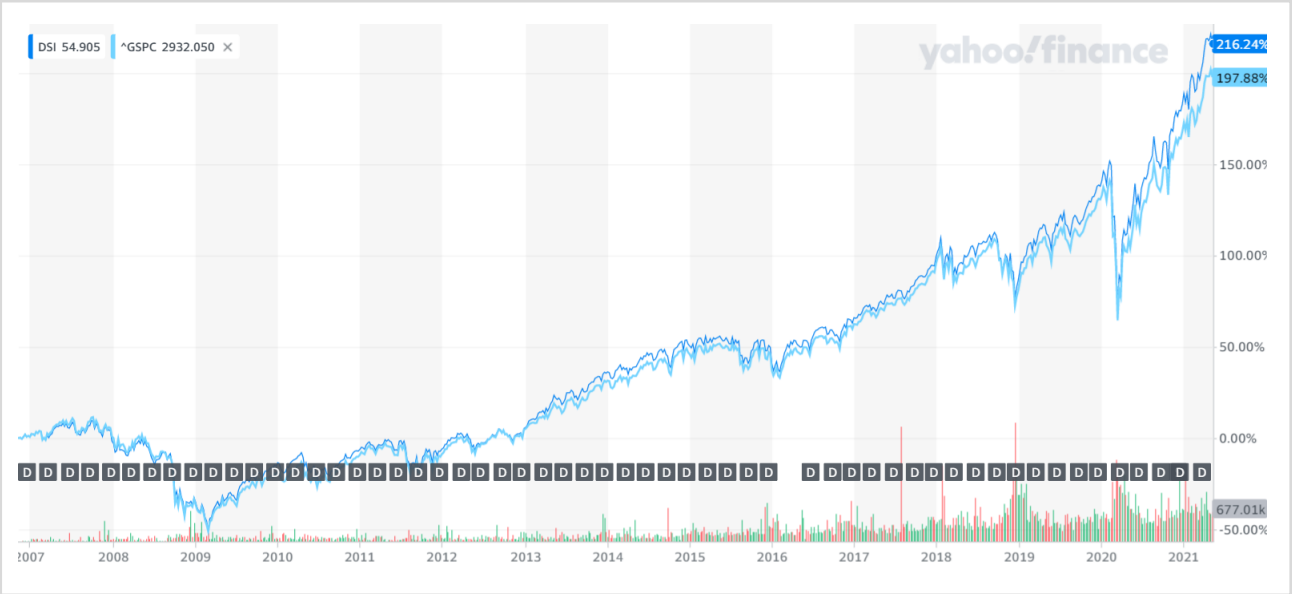
How's the performance?

You might be thinking "ok, enough with the explanations. How's the performance?"

ESG funds outperformed conventional funds in the year 2020, over the past 5 years, in the time period of the 2008 recession and overall since 2007. Below please see a chart from Yahoo! Finance comparing the return of the S&P 500 with the Social Index 400 since 2007. Companies with higher ESG scores outperformed their standard counterparts by over 18%.

And that makes sense! It's expensive for a company to clean up an oil spill. It's expensive to fight legal battles against class action lawsuits. During the recent labor shortages, employees have been loyal to companies that have fair labor practices and good benefits. All these elements impact PROFIT and profit drives investment dollars.

Consider the chart below (source: Yahoo! Finance):



So how does an investor choose a fund?

First, decide on which themes are the most important to you. Are you concerned about climate change? Affordable housing? One benefit of the recent increase of new funds is that you can find investment options for most concerns. But how do you evaluate those options?

Through your own research, or with your financial advisor, you can find funds that meet your personal criteria. If you are passionate about a cause, you'll also want to confirm that the fund engages with the companies it holds. Shareholder advocacy is one term for this action.

In 1970, consumer rights advocate Ralph Nader was able to get two socially based resolutions on the proxy ballot of the General Motors annual meeting. Both resolutions failed, but it was a milestone for consumer engagement with corporations. Today, fund managers are frequently making an impact by using the power of the shareholder proxies they hold to encourage companies to commit to changes like a commitment to net-carbon zero or better the working conditions in factories. These examples can be found in the marketing materials for most funds that engage in shareholder advocacy.

But isn't it ALL just marketing?

"Greenwashing" is the term for funds being misleading about their commitment to ESG criteria. Some funds have even been renamed and remarketed to meet the demand for ESG. This is bad not only for the investors who are misled but also for the causes these funds are supposed to be addressing. If companies don't see a financial impact tied to meeting ESG criteria, they have no incentive to change their practices.

The good news is that ESG disclosure by companies is becoming more commonplace and is required by some very large asset managers. This kind of transparency makes it easier for the third-party rating agencies to evaluate ESG criteria and provide ESG scores investors can rely on.

However, sometimes investors may not realize that a sustainable fund is going to hold a lot of familiar names. It's important to research why a fund holds a certain company before deciding you have been deceived by greenwashing.

Conclusion

Using ESG criteria to screen companies is just another way of evaluating investments. It may seem new and different, but it's still just investing. Good business practices will result in higher ESG scores and higher profitability, so adding an ESG screen to your investment portfolio makes good sense.

Transitioning to an investment portfolio that holds ESG funds is one of the easiest ways we can make a positive impact on the future of our environment and the way our children will interact with global companies. Consult your financial advisor to learn more about how you can align your portfolio to reflect your personal values.

About the Author

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Kacie Swartz has been helping individuals and families pursue financial independence as a CERTIFIED FINANCIAL PLANNER™ practitioner since 2012. Kacie is an advocate of socially responsible investing and is a frequent public speaker promoting general financial literacy and educating investors about sustainable investing. Her background in investment education makes her a good fit for clients broadening their knowledge of financial planning and investments and helping people through major life changes like ending a marriage or losing a spouse.

Kacie's interest in Environmental, Social & Governance funds (ESG) started as an extension of her personal commitment to living a more sustainable lifestyle. Kacie turned her years of experience constructing advance portfolios as a Certified Investment Management Analyst® to researching ESG fund options. She found clients were also drawn to the topic and has helped countless people better understand how their dollars are invested and how best to align their values with those investments. Kacie has spoken to local groups, including the Austin Women's Investing Group, about the fundamentals of ESG investing and how to get started. Kacie also recently spoke to other advisors about ESG investing as a panelist at the Investment News Women Advisers Summit in New York City.

Kacie is a member of the Financial Planning Association, the National Association of Personal Financial Advisors (NAPFA), the Investments & Wealth Institute, and is a spokesperson for the CFP® board's Women's Initiative to attract women to the financial planning profession. She has been published in national media outlets such as Real Simple, Money Magazine, Kiplinger's and others.

Kacie has been in the financial services industry since 2001 and joined Stone Wealth Management in 2013. Originally from Kansas, Kacie graduated from Wichita State University with a degree in Finance. She is an active supporter of the Austin Diaper Bank, American Gateways and Health Alliance for Austin Musicians.

Kacie happily lives in South Austin where she and her husband enjoy exploring playgrounds with their two small children.

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Specializations

- Life Transitions (Examples: changing careers, divorce, widowhood)
- Navigating Retirement from the UT System
- Investing in Sustainable and Environmental, Social and Governance (ESG) Focused Investing
- Incorporating Pension Plans into Retirement Strategies
- Social Security Claiming Strategies
- Designing Investment Strategies

As Seen In:

The New York Times Kiplinger Money REALSIMPLE

About Stone Wealth Management

The truth is, there's no one-size-fit-all formula for constructing the right portfolio. Utilizing a knowledgeable and experienced team like Stone Wealth Management means delegating this responsibility to someone who understands both your unique financial concerns as well as the larger market and its changing conditions.

In recent years, environmental, social, and governance (ESG) criteria are an increasingly popular way for investors to evaluate companies in which they might want to invest. Investors have shown an interest in putting their money where their values are. **Contact us** if you are interested in learning more about ESG investing, commonly referred to as socially responsible investing.

Stone Wealth Management also provides comprehensive wealth management services such as investment management, financial planning, tax planning, estate planning, insurance planning, and business exit planning, Established in 2004 in Austin, TX by Austin native Morgan Stone, we are an independent Registered Investment Advisory* firm. As an independent firm, we are free from conflicts of interest associated with proprietary financial service firms.

If you are looking for clarity and confidence in a complex world – especially when it comes to your money and how you might with a little grit and the right guidance achieve your biggest life-goals – then Stone Wealth Management might just be the right team for you.

** Stone Wealth Management is registered with the Securities and Exchange Commission (SEC) as an investment adviser. Registration does not imply a certain level of skill or training.*

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