For years, social investment has offered investors the opportunity to help achieve their financial objectives in a way that is consistent with their ethical and social concerns. There is a growing body of evidence to suggest that societal issues in the workplace, environment and community are becoming increasingly important business issues for many companies and industries. As a result, how companies integrate these issues into their operations can potentially impact their competitive opportunities and future growth possibilities. These items, not normally included in the analysis of one’s investment portfolio, can become increasingly important, value-producing elements for successful investing.

This white paper presents how this convergence influences the manner in which we manage our social investment portfolios.

*Best of Class* refers to the way we use positive, or supportive, screening to identify companies that have the best practices within their sectors in terms of their corporate environmental, workplace, and community initiatives, among other traditionally ‘non-financial’ drivers.
BEHIND THE CONVERGENCE

Previous white papers\(^1\,\^2\) by our Social Awareness Investment team have examined the factors driving the convergence between a company’s business results and how it often manages the cultural factors strategic to its operating arena. Among the factors driving this convergence are the following:

- Globalization of the world’s major economies, and resulting changes in workforce demographics and customer and market populations.
- Increasing world population, growing prosperity and consumption among some segments of society, and the associated demand for goods and services.
- Expanding demands for goods and services on a limited natural resource base, and the resulting pressure to improve resource productivity.
- Better and more widely available information on the environmental and social impact of development on local communities and economies.
- Ever-increasing public and, consequently, governmental concerns about quality-of-life factors such as air and water quality, equity in the workplace, work-life balance, and human rights.
- Joining, or transfer, of behavioral attitudes developed by individuals in their daily lifestyles as workers, parents, consumer, and community volunteers to their newly enlarged role as investors.

A NEW FRAMEWORK

We believe that these trends are reshaping the competitive landscape in many industries and are transforming seeming non-financial, cultural issues from relatively minor factors in corporate decision-making into factors that are integral to competitiveness in the 21st century. Along these lines, it is our view that the companies likely to profit from these trends will be those whose leadership, values, and corporate culture enable them to go beyond compliance and derive and drive strategic value from their workplace, community, and environmental initiatives.

As one might expect, new issues will emerge from time to time and the importance of some issues over others may change as a result of new legislation, consumer value shifts, or other socio-economic conditions.

As one might expect, each sector (e.g., technology, energy and apparel) is likely to face a different portfolio of issues, given the different business environments in which they operate. Recognizing this, we selectively emphasize those particular issues that we believe are most relevant to their business performance. For example, workforce issues are generally critical success factors to technology and pharmaceutical companies because they operate in a creative environment, that is, their value depends on the innovation and intellect of their workforce.
On the other hand, issues around the environment and communities could be of particular interest when evaluating natural resource companies (forest products, energy, etc.) because they operate in the natural environment, which entails securing a social license to operate and extract resources from the land, through logging, drilling, etc.

It probably comes as no surprise that virtually every company will have some positive characteristics and some negative ones. Therefore, we as investment managers must weigh the “positives” against the “negatives” for each company and compare their performance to others in their sector, in order to determine those that are on the leading edge rather than lagging behind. This determination is made through our direct dialogue with corporate management, proprietary and third-party social research, as well as publicly available information from industry and trade organizations, government agencies, public interest groups and others.

As one might expect, new issues will emerge from time to time and the importance of some issues over others may change as a result of new legislation, consumer value shifts, or other socioeconomic conditions. Therefore, in a way, supportive screening is an ongoing process that is never complete.

THE IMPLICATIONS

We believe that an integrated approach to the stock selection and portfolio construction process enables us to identify top quality corporate management that are better positioned to create strong, competitive advantages in their companies and stay on the leading edge of their industries. In turn, that selectivity can, we believe, aid us in achieving our long-term portfolio goals of providing competitive, risk-adjusted investment returns.

In addition, we believe a supportive approach to social investment provides an opportunity to interact with companies on these issues and to provide leading edge companies with the economic leverage to advance these issues across their entire value chain. Given our focus on large-size companies, we believe that the implications of supportive investing could have significant, positive implications for the recognition of best practices in the marketplace.

The opinions and views expressed are those of the source provided and do not represent a complete discussion. Contrary views may exist. Neither Smith Barney Asset Management nor Citigroup Asset Management offers legal advice. Clients should consult their own legal advisors regarding their specific situation. The views expressed are current and are subject to change without notice. They should not be construed as investment advice or recommendations or used as the sole basis for an investment decision with respect to the information discussed. The views expressed are those of the management team specified and are not necessarily representative of the views of the other portfolio managers or of the firm as a whole. Factual information relating to the topics covered was obtained from sources believed to be reliable, but there can be no guarantee as to its accuracy. Past performance is not a guarantee of future results.

Investments are subject to risk including possible loss of principal and there is no guarantee that these investment objectives will be met.

1Smith Barney Asset Management, Environmental Drivers and Shareholder Value, 2004.


Some of the above endnote reference studies or articles reflect an author's perspective from a specific period and have been deemed relevant to the point that is being made in this white paper.