VALUES
Walden Asset Management ❁ Investing for Social Change Since 1975
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In This Issue

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I Was Lifted Up: A South African Testimonial

"I was lifted up!" With those four words, the waif of a woman in a flowered white cotton dress, blue plastic Chinese sandals, and hair in corn rows, stood tall, lifted up both hands, tilted her head and beamed.

We were in a Centre, a meeting of almost 50 other women micro-borrowers, in Molapo. This small town is in Limpopo Province, South Africa's poorest, on the rich, intensely developing, hundred mile long platinum reef on the northern escarpment of the Great African Rift Valley. The scene of the meeting was a rust-brick, small, dark, cloth-ceilinged, corrugated roof church. The question one of us had asked the women toward the end of their meeting was, "In your life, before your loan and after, how was the life you led then and how is your life now?"

"Before, I had nothing, I was nothing," continued the woman. "Now," she went on to explain, "my children can eat; I can pay their school fees and buy them their uniforms; and I can afford to pay fees for the Burial Society. I am something free. I have choices." And with that, another hand went up, followed by the description of another changed life. And then several hands, more testimony, and then a cascade of hands. The moderator at that moment, John de Wit, founding director of the microbank, the Small Enterprise Foundation (SEF), had to intervene so that the meeting could end on time and an anxious mother could return to her children. The women's enthusiastic responses were proof-personal that superbly managed microlending, targeted at those 50 percent below the South African poverty line, could reach deeply into the social fabric to touch those whose lives had had almost no hope, who were all but unreachable by government and charities.

Stephen Moody is a senior portfolio manager.

SEF currently has more than 100 field workers—organizers, mostly of around university age, who attend to over 600 such Centres—and almost 22,000 borrowers. Loan amounts start as low as $15, though first loans average $90; with average loans of about $160; and none over $1,500. Molapo is one of 12 villages in the region that are the object of a study sponsored by physicians from the University of Witswatersrand carefully measuring the impact of microlending on the incidence of HIV/AIDS. Noriya Manganyi, the very capable and charismatic fieldworker at our Centre meeting, said she was attending one or two funerals a weekend at the invitation of families in the Centres for which she was responsible. The hypothesis of the study, so far supported by anecdotal evidence, is that there is a significant reduction in AIDS with microlending, for many reasons, perhaps in part because transactional sex is no longer necessary for survival in this booming mining region.

Each woman (and almost all borrowers are women, including older teenagers and grandmothers caring for families without

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About Walden Asset Management

Walden Asset Management is the socially responsive investment division of Boston Trust & Investment Management Company. Walden began offering socially responsive investment services in 1975. We are among the largest and most experienced investment managers specializing in services for individual and institutional investors with social concerns.

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BEYOND THE NEXT QUARTER

I've heard it many times: Social investors may have their hearts in the right place, but that's a poor starting place for making money in the stock market. Conventional investors do better. They look at the cold facts of profit and loss and aren't distracted by sentimentality.

I beg to differ. Here's an outrageous claim: Social investors are better equipped than most to grasp the importance of the creation of long term value, the only thing that drives sustainable investment returns.

You don't have to cite the proponents of social investing to understand just how self-defeating some of the tactics of mainstream (a.k.a. Wall Street) investors have been. Warren Buffet, regarded by many as America's premier investor, shares our impatience with the standard approach, finding that Wall Street's advice is simply not worth the time. ("We never look at any analysts' reports…I don't understand why people do it.") Buffet further complains that when "managers dance to Wall Street's tune," as many do, they wind up following "operating and capital allocation policies far different from those they would choose if left to themselves." A terrific recent book, *The Number*, by New York Times reporter, Alex Berenson, makes a similar case. He attributes the market debacle of recent years to the obsessive primacy Wall Street analysts placed on the so-called "Number"—the earnings per share figure reported to Wall Street which, purportedly, encapsulated all one needed to know about a company's profitability. Berenson reviews in exquisite detail Wall Street's narrow and short term focus, how this impelled managers to make foolish business decisions, and how this self-reinforcing cycle often temporarily led to skyrocketing stock prices. We know, of course, how this all ended: Companies that damaged their own futures and investors with plenty of losses to show for following conventional wisdom.

How then, do I support my claim that social investors are better equipped to be successful? By pointing to my conviction that successful investors are more inclined to worry about the health of the entities they own rather than whether or not a quarterly earnings report pleases Wall Street. True, that inclination may often be motivated by a social or ethical concern, or the interests of a broader group of stakeholders, but it provides the proper starting point for identifying long term value. Think about some of the value destroying things that some companies have done that Wall Street frequently ignores (or even applauds) if it helps bolster short term profits: scaling back employee health benefits, reducing research and development, treating environmental risks cavalierly, borrowing more funds than otherwise prudent to sustain a faltering project or to enable repurchase of pricey shares.

Bill Apfel is a senior portfolio manager and director of securities research.

Consider this contrasting example from our own experience. Costco, the warehouse retailer, and long term Walden holding, recently saw its stock decline briefly but sharply when one analyst criticized the company, subsequent to a quarterly earnings shortfall, for providing workers a best in industry package of wages and benefits. Of course, high labor costs did limit recent earnings, but investors with a broader, longer term perspective understood that Costco's industry-leading past success and future prospects had been built on a low turnover, well motivated workforce. It is no surprise that Costco has a sensible executive compensation policy as well.

Even big technology companies, once Wall Street favorites, sometimes fail to get sufficient credit from conventional investors for conserving shareholder value. Intel, for instance, has made a point of addressing the adverse environmental effects that are inherent in semiconductor manufacturing. Given the volatility of the company's earnings, and the obsession Wall Street holds for forecasting to the penny each quarter's report, most investors probably don't pay much attention to such a long term concern. But we think Intel is among a growing group of companies that is protecting share-

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community development investing

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parents, often lost to AIDS) belongs to a borrowers circle of four or five others, each of whom is an entrepreneur. Some are vendors of fruit or cell phone calls or curios; some are beauticians; some have opened a kiosk. They all attend every Centre meeting; nominate one spokesperson who reports on savings, borrowing, and repayments. Each must pay interest and a portion of principal at each meeting. Each must help the others of her circle succeed. Being late, failing to attend without reporting why, or failing to make payments brings a hefty fine of five Rand, or about 75 cents. Each report, each payment, each achievement is met with applause. The Centre leader and the Centre treasurer handle all funds openly. Accounting records are maintained by the SEF field worker who never touches funds. The aggregation of the day's monies is taken to a bank in town, a long bus ride away, by two borrowers who volunteer and are approved by the committee of the whole for the errand. Talk of the Centre's business is confidential and does not leave the meeting at the church to protect the borrowers and especially the couriers, for crime is still a problem. The meetings are serious and polite, very disciplined, but very warm.

Toward the end of the meeting we attended, the chairperson pointed out that the guests, who sat to the right of the table at the head of the room, were late and, to more broad grins, each had to pay a five Rand fine. John de Wit covered for us, commenting that as driver he had been responsible for our tardiness. (Actually, our plane was late!) His payment was met with applause, laughter, and a little ululation. On that note, the woman in the white flowered dress rose, and began to sing, joined by her sister borrowers, a strong, joyous tone that pierced the heat, the dust, and our fatigue, a hymn of exuberance not unlike the South African national anthem *Nkosi Sikelel' iAfrika,* "Lord, Bless Africa!"

—Stephen Moody

SEF (www.sef.co.za) is the most recent beneficiary of a guarantee arranged by the Thembani International Guarantee Fund (TIGF) and issued by Shared Interest (http://www.shared interest.org), a community development finance institution (CDFI) supported significantly by clients as part of the CDFI program of Walden Asset Management. De Wit hopes SEF will quadruple in less than a decade should it receive sufficient funds. Shared Interest is one of three major nonprofit organizations derived from the Fund for a Free South Africa in 1992. Robert Zevin, who helped build our social investment program, was one of its founders and first chairs. Tim Smith, director of socially responsive investing at Walden is also a founding board member. Stephen Moody, the author of this vignette, was in a Shared Interest delegation, led by executive director Donna Katzin, which visited projects of TIGF and was a guest of President Thabo Mbeki at his second inauguration, April 27, 2004, the tenth anniversary of South Africa's first democratic election. ◆

The beginning of the domestication of wild African bees at the forest experimental station of the Bee Foundation, a beneficiary of TIGF.

Through our Community Development Investment Service, Walden clients have invested over $8 million in community development banks, credit unions, and loan funds. We are pleased to have included Shared Interest in this service.

SOCIAL RESEARCH AND ADVOCACY IN ACTION

Heidi Soumerai is director of social research.

Tim Smith is director of socially responsive investing.

The company briefs below report on the progress of shareholder initiatives led or participated in by Walden, as well as other newsworthy company actions.

The votes have been tabulated on the 2004 Walden-led shareholder resolutions that went to ballot. The conclusion: The results reveal continuing shareholder resolve for strengthened corporate governance and social responsibility practices. Each of the three companies that received our resolution to enhance board accountability by encouraging a policy of annual election of directors, as opposed to their practice of staggering director elections over three year periods, won overwhelming majority support (at **Costco** by 75.7 percent; **Gillette** 68.1 percent; and **TJX** 76.5 percent). The investor perspective is certainly clear as these companies and others continue to deliberate this proposed governance reform. Our repeat resolution at **ALLTEL** requesting a more comprehensive nondiscrimination policy that explicitly includes sexual orientation garnered a record level of support of 27.5 percent, more than twice the previous year's results. Finally, a very solid 14.3 percent voted in favor of our first-time resolution asking **Amgen** to disclose equal employment opportunity statistics.

In addition to the above actions, Walden led five proposals that were withdrawn when the companies agreed to the proposed reforms. **Stryker** and **Dover** adopted inclusive nondiscrimination policies and **Avon, BellSouth**, and **SBC Communications** implemented annual election of directors. The Securities and Exchange Commission for "ordinary business" reasons omitted our two climate change resolutions posed to insurance companies **American International Group** and **Chubb,** but we have been in dialogue with both companies. Walden also participated in more than a dozen other proxy resolutions on a variety of issues including climate change, diversity and glass ceilings, vendor standards, human rights, water scarcity, HIV/AIDS reporting, and executive compensation.

Company dialogues continue

In May, **Dell** committed publicly to boost its recovery and recycling of computer equipment by 50 percent in 2005 from the 2004 fiscal year level of approximately 21 million kilograms worldwide (about 45 million pounds). Dell will be reporting its results quarterly. This industry-leading precedent sets a "best practice" standard for other technology companies and requires strong tracking systems to monitor computer equipment recovery on a global basis. (For more information see the *Dell Sustainability Report* for 2004 on the company's Web site.)

Alberto-Culver has communicated to Walden its intention to phase out polyvinyl chloride (PVC) plastic packaging in its Alberto VO5 product line. Relative to other plastics favored by many personal care product manufacturers, PVC plastic has a negligible recycling rate and can contaminate an otherwise recyclable plastic waste stream. Walden is monitoring its phase-out of PVC.

Marsh McLennan has added employees to work on emerging environmental risk initiatives. Part of their focus is to explore the potential impact and opportunities of climate change risk across the company's diverse business lines. This level of attention to climate change is notable within the financial services sector.

Colgate Palmolive is demonstrating a strong commitment to address the HIV/AIDS crisis in Southern Africa through prevention, treatment and public-private partnerships with other organizations there. In May Walden met with the senior human resource staff person for South Africa and other Colgate-Palmolive executives, including a representative from the office of the Chairman, for an open discussion of its policies and practices to address the enormous economic and human implications of the health pandemic. Colgate is beginning to take lessons learned from Africa to high HIV/AIDS growth rate countries in other regions of the world where the company's presence is significant.

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Clear Momentum for Social Investors and Corporate Responsibility

We have seen some amazing developments, prompted by investors active in shareholder advocacy, as well as leadership by companies on corporate social responsibility and governance. These actions contribute to a positive difference for stockholders, employees, the environment, and society at large.

- The pension boards of the State of Vermont passed a carefully crafted set of Proxy Voting Guidelines covering governance and social/environmental issues, highlighting the importance with which they view their responsibility to vote proxies conscientiously. This is a valuable model for other pension funds (available at www.tre.state.vt.us).

- Co-hosted by CERES, a coalition of investors and environmental organizations working with companies to promote best practices in environmental performance and transparency, investors representing over $1 trillion in assets met at the United Nations in November to discuss the financial impact of climate change on their portfolios. The outcome was an $800 billion strong coalition of union, state, and city pension funds working together to press companies on climate change. At about the same time, the State of Maine pension funds filed its first shareholder resolution, with ExxonMobil, on climate change.

- In April, California's CALPERS, the largest U.S. pension plan with $168 billion in investments, announced a proactive program on the environment and climate change, becoming a hugely influential leader on these issues.

- On a parallel track but with a global perspective, the London based Carbon Disclosure Project gathered support from institutional investors representing $10 trillion in assets to ask the 500 largest companies in the world to answer questions on greenhouse gas emissions. Seventy-one percent of them provided information—that fact in itself a testament that companies are increasingly responsive. Yet surprisingly, some continued to ignore this appeal, even in instances when Carbon Disclosure Project signatories represented over ten percent of their shares (see www.cdproject.net).

- Continued convergence of corporate governance and social issues was evidenced by strong YES votes for many shareholder resolutions, in part the result of a strengthening business case for good governance and environmental performance. Numerous resolutions won overwhelming majority votes, for example, on annual election of directors and stock option expensing. On environmental issues, record breaking votes poured in at Apache (38 percent), Anadarko (31 percent) and others.

- Coca-Cola Company's board asked its investors to vote in favor of a shareholder resolution requesting a report on the economic impacts of the HIV/AIDS pandemic, resulting in more than a 95 percent positive vote. Similarly, Tyco supported a resolution asking for an environmental report that passed overwhelmingly. By supporting these resolutions, the two companies acknowledge that these proposals were consistent with their long-term best interests and shareholder value.

- Gap, in an extraordinary example of company transparency, released its *Social Responsibility Report* (see *Transparency, Not Invisible* on page 6). Advised by a working group of shareholder advocates, Gap released an honest assessment of the challenges it faces in dealing with labor conditions in its supply chain. With descriptions of operations from China to El Salvador, Lesotho to Cambodia, the report stands as a stark reminder of the hard work ahead for companies that strive for their products to be made in safe and responsibly run factories.

- Finally, we observe remarkable progress toward more inclusive nondiscrimination policies. Now, 98 of the *Fortune* 100 companies explicitly prohibit discrimination based on sexual orientation (with ExxonMobil and Alcoa being the outliers). ◆

—Tim Smith

TRANSPARENT, NOT INVISIBLE

Meredith Benton is a social research associate.

When I was in grade school we read *The Hobbit,* the prelude novel to the now much-hyped *Lord of the Rings* trilogy. The teacher asked us the following question: If we had a ring that made us invisible, and we knew we would not be caught, would we steal from stores? The question made a strong impression on me. I liked to think I was honest folk, but passing the candy section in our local Woolworths, I had to admit, if I had that ring, I would be severely tempted.

After Enron/WorldCom/etc., U.S. investors of every ilk joined together and called loudly for greater transparency in the reporting of financial information, and helped to spawn an unprecedented push for corporate disclosure and accountability on a range of issues. The logic behind this push reflects a pessimistic assumption about human behavior: There are certain decisions people will make only when they are "invisible," when they are confident that they will not be held accountable for, nor have to take ownership of, their actions.

Given the role multinational companies play in the global economy, the importance of reporting in building trust, helping understand the broader impacts of business decisions, and developing knowledge about complex issues cannot be overstated. Transparency, and a clear line of responsibility at a company, appears to be a precondition for improving the social behavior of companies.

Fortunately, social issues are increasingly being addressed in company reporting, not only in response to activist pressure, but as leaders associate the long-term success of their companies with a more holistic approach to financial, social, and environmental challenges. For instance, this year, both Novartis and PepsiCo included social reporting in their annual reports. In explaining this choice Steve Reinemund, chairman and chief executive officer, wrote in PepsiCo's 2003 Annual Report, entitled *Growth and Trust,* "We're focused squarely on a commitment to deliver sustained growth through empowered people, acting with responsibility and building trust. Put simply, this commitment represents our priorities in the pursuit of creating value."

Gap's recent report on vendor relationships perhaps best exemplifies the changing trend toward transparency. When released, the report made international headlines because it did more than admit to vendor compliance flaws in its sourcing system. It reported on its difficulties and demonstrated that it is responding with thoughtful, determined actions. The 40-page report covers a range of topics from country-by-country monitoring data about factory conditions, the complex challenges facing the company, the building of stakeholder relationships, and the work still needing to be done. Most importantly, Gap took responsibility for recognizing and responding to labor abuses in supplier facilities.

The strongest reports, like Gap's, detail the thought processes that support company decision making, acknowledge accomplishments and challenges, set goals and incorporate stakeholder feedback. This style of reporting truly enables a company to "tell its story," and demonstrate that it is

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TRANSPARENT, NOT INVISIBLE

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working to understand the complexities involved in responding to social and environmental concerns.

Another sign that companies are embracing more open reporting is the increasing use of the Global Reporting Initiative (GRI). Formulated in part to respond to "survey fatigue," the GRI seeks to create an internationally standardized format with which companies can address a range of economic, social, and environmental issues. By harmonizing reporting structures, the expectation is that readers will be more easily able to assess a company's social performance against its industry peers.

Still, only some companies have voluntarily given up their invisibility rings. Many remain as they have always been—superficial in their reporting of social and environmental issues. Much work is being done to remedy that, with activists fighting to ensure the accuracy of the information within the reports, and investors fighting for greater disclosure.

In the United States there is a campaign underway to encourage the Securities and Exchange Commission (SEC) to both enforce its existing disclosure laws and to develop new mandates regarding social and environmental reporting. In doing so, the SEC would keep pace with existing regulations in countries such as South Africa, France, and the UK. In South Africa, companies listing on the Johannesburg Stock Exchange must report following the GRI Guidelines; in France, regulations passed in 2001 require social reporting on human resources, community and labor standards; and in the UK, a consultative draft of potential reporting regulations was released in May 2004. The draft regulations call for mandatory reporting of the company's impact on the environment, employees, supplier relationships, and the community. Beginning in 2005, these regulations would require directors to explain their reasoning behind inaction on social and environmental issues.

Without mandated disclosure in the U.S., however, companies with something to hide have the legal flexibility to mask their flaws, and this puts the environment, employees, shareholders, and other stakeholders at risk. Companies that are openly and actively addressing social and environmental issues through reporting are seizing opportunities and building relationships that we, and they, believe will support them in the long term. These companies, regardless of their challenges, deserve commendation for their willingness to reveal. ◆

—Meredith Benton

SOCIAL RESEARCH AND ADVOCACY IN ACTION

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Company breakthroughs

In May **Bank of America** joined **Citigroup** in pledging to adopt a "no go zone" policy for all new extensions of credit and project specific bond underwriting. Among its most salient features, Bank of America will not finance resource extraction from, or the clearing of, primary tropical moist forests and intact forests identified by World Resources Institute (see *Bank of America Forests Practices: Global Corporate Investment Bank Policy* on the company's Web site). The commitment includes funding to help map intact tropical, temperate, and boreal forest ecosystems to protect their future use and development. The bank's initiative, in addition to other new policies on climate change and indigenous rights, earned strong praise from the nongovernmental organization Rainforest Action Network for bringing a new model of best practice leadership to the financial sector.

BP, **Intel** and **Novartis** recently published extensive sustainability reports that are available on their Web sites. Walden views the Novartis report as an exceptional model in that it is an "all-in-one" annual report that combines financial, corporate governance, social and environmental reporting. A combined report encourages its varied users to explore the complexities and interrelationships that exist in the multi-stakeholder environment of the "sustainable" corporation. ◆

—Heidi Soumerai

BEYOND THE NEXT QUARTER

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holder value in this area, something that may prove vastly more important than next quarter's earnings report. Perhaps it is just a coincidence, but Intel's management has a similar long term focus in its employment practices. The company is regularly included in Fortune's list of "100 Best Companies to Work For."

Of course, I know that it would be foolish to push my "outrageous claim" of the superior talents of social investors too far. Statisticians can argue about performance results, but I suspect that the issues are far too murky to be settled conclusively. And, no doubt, attentiveness to the creation of long term value is not the exclusive preserve of social investors. Still, I feel confident learning from the analysis of a social investor who starts by asking questions about the vibrancy and sturdiness of the organization under consideration for an ownership stake. If instead the first question asked is, "Will this company beat the Wall Street earnings forecast next quarter?" I think it's time to put my profit seeking cash back in my pocket. ◆

—Bill Apfel

cutting edge companies

POWER INTEGRATIONS

This column highlights companies in the business of providing solutions to social and environmental challenges. Featured companies are typically held in the SmallCap Innovations portfolios offered to Walden's clients.

The mascot of Power Integrations is an "energy vampire slayer," fitting for a company with a Web site Green Room that promises: "We're spending all our energy to save yours." The energy vampires that Power Integrations targets are "energy-sucking devices"—older, inefficient power supplies. According to the company, more than $4 billion of electricity is estimated to be wasted each year on household power products believed to be turned "off." Power Integrations reports that standby power waste used to support instant-on in TVs, DVDs, and other household power consuming equipment represents the total amount of power generated by 26 average size power plants.

Power Integrations makes semiconductors for integrated circuits that convert AC power to DC power. The company's products enable original equipment manufacturers to make smaller and cheaper power supplies for portable devices such as cell phones, personal digital assistants (PDAs), digital cameras, portable computers, and other electronic devices. The integrated circuits conserve energy by reducing energy leakage that occurs in larger power supply adapters. Conventional power supplies, which continue to drain power even when the devices they are supplying are turned off or are fully charged, waste nearly 10 percent of the electricity purchased by consumers. According to Power Integrations, its products eliminate 90 percent of this energy waste.

In July 2001, President Bush issued an executive order stating that federal agencies must purchase products with standby energy consumption of 1 watt or less, and the European Union has issued even stricter standby power requirements. Power Integrations products allow equipment manufacturers to meet both of these requirements as well as other energy efficiency regulations. ◆

—Ken Scott

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