

## **Sustainable Investing 2.0**

**by Brent Kessel**

**Fall Issue 2008**

I've been a yogi by dawn and a Certified Financial Planner by day for fourteen years. I've worked with people with hundreds of millions of dollars, as well as people who are a hundred thousand in debt. I've counseled captains of industry who are driven to ever-higher levels of success and social activists one paycheck from eviction. While there's no denying that it is easier to be rich than poor, I have found that without exception it makes little difference what people's outer life circumstances are - everyone struggles with some aspect of their relationship to money.

To create lasting change, we need to approach financial challenges from the inside out. My new book, *It's Not About the Money* draws on both my professional experience and my interviews with more than twenty of the world's top spiritual and financial leaders, including the Dalai Lama, Vanguard Funds founder John Bogle, Nobel Prize-winning economist Dr. Harry Markowitz, Thich Nhat Hanh, and Ram Dass, to help you make changes to your finances based on self-awareness. The first half of this article will focus on how our instinctual wiring gets us into trouble with our investment decision-making, and the second half will share details on two new funds that I believe will revolutionize sustainable investing.

### **Wired to Want**

All beings in nature have a biological imperative to survive. Without this imperative, they die. A tree grows toward whatever sunlight is piercing the forest canopy. Whales migrate thousands of miles to birth their calves in the warm Sea of Cortez. Without this inherent drive for survival, living organisms would die and evolution would cease. Our physiology is wired to constantly deliver messages about what threatens us. Nothing in modern society is as closely tied to our survival as money.

This fight-or-flight urgency has a tremendous impact on our investment success or lack thereof. Most investors don't know what's going to happen next, so their minds latch onto what has occurred in the past as the most likely thing to happen in the future. "What if the market goes down another 25 percent?" is a common refrain immediately following a market correction. In response, many people pull some or all of their money out of the stock market. Then, when it rebounds, they're left sitting on the sidelines and wondering why they're not reaping the benefits of the now-booming market. This emotional investing has disastrous consequences, because over 90 percent of stock

market returns are generated in less than 10 percent of the trading days. What's more, some of the best days have occurred during periods of overwhelmingly negative sentiment:

- \* The best one-month return in US equity market history, October 1974, happened immediately after the worst one-year period.
- \* The best single day ever was October 21, 1987, only two days after the Black Monday market crash.
- \* The four best days since 1933 occurred in October of 2002, in the midst of war, terrorism concerns, and declining corporate earnings.

The bottom line: Investors who attempted to wait out apparent downturns ran a high risk of missing these best periods. Further evidence of the costs of this behavior can be found in a study conducted by, one of the largest mutual fund companies in the United States, which found that its clients' investment returns from 1969 to 1999 were only 5 percent in a period when the average return of the company's mutual funds was about 16 percent. The difference was attributable to the fact that money was moved in and out of funds at inopportune times. Five percent is less than the investor would have made in a simple savings account over the same time period! In my experience, it's much more important that investors learn to manage their own psychology than their portfolios.

### **What's Your Money Type?**

To manage your psychology, you first must understand it in relation to money. One of the major hypotheses of *It's Not About the Money* is that we each have a Core Story with money, which is the mind's attempt to defend us from pain and suffering and seek pleasure and security. This story is formed at a young age, when we latch onto a collection of beliefs about money, including investing, that we hope will help us avoid pain (losses) and be happier (or richer) in the future

What's more, these Core Stories tend to manifest as archetypes within us. The book defines the eight money types that I've observed to be most common. They include the Guardian, the Pleasure Seeker, the Idealist, the Star, the Saver, the Innocent, the Caretaker, and the Empire Builder. No type is better or worse than another. What's important is that we understand which ones are dominant in us, and what our strengths and weaknesses are when it comes to money and investing. Then, we can use that information to strengthen our weakest financial muscles, a critical step for anyone who wants a better relationship to money or investing.

While the book delves deeply into financial behaviors of each archetype, here are two of the types and the specific characteristics they exhibit when it comes to investments, and what to do about them:

The Idealist places the greatest value on creativity, compassion, social justice, or spiritual growth. At the extreme, Idealists are skeptical, distrustful, or even rebellious when it comes to money. Socially progressive and creative investments have typically been given higher priority than those with higher financial returns. Unfortunately, the attitudes of the Idealist have often served to repel money, so there may be financial dependence on family or reliance on governmental or nonprofit assistance. The investment objective for many Idealists should be to earn appropriate rates of return for the risks they're taking without compromising their morals.

The Guardian is alert, careful and prudent with money. Guardians tend toward ultraconservative investing, or they bounce between investment vehicles in an attempt to avoid losses and feel safe. For these reasons, they often earn subpar returns, ironically increasing the chance that they might have something to worry about in the future. The best investment program for the Guardian would require no intervention or monitoring. For example, buy a collection of socially screened index or exchange-traded funds that track the market year-in and year-out, and keep adding to the investment no matter what.

### **The search for investment solutions that work for all eight money types**

As we worked longer with our clients, we realized that some were most wired to want security (the Saver and Guardian), others wanted better investment returns to be able to afford 100 percent organic foods, a yoga retreat to Costa Rica, or a new Prius, (the Pleasure Seeker and Star), some wanted an investment program they could start and forget about (the Innocent), while another group intensively focused on wanting their money to change the world (the Idealist, Empire Builder and Caretaker). As we scanned the SRI landscape, we found that while 93 percent of the U.S. population has the conscious willingness to include sustainability in their lives by basing some of their purchases on "concern for issues such as the environment and social well-being," only eight mutual funds in the U.S. focus on sustainability. Furthermore, most SRI funds exclude companies and often, entire industries, in order to avoid environmental polluters or other violators of their screens. In contrast, our clients were looking for an investment strategy that would financially incentivize corporate managers to become better environmental stewards, as well as earn them appropriate rates of return for the risks they were taking, something that very few SRI funds have been able to do over time.

So I approached Dimensional Fund Advisors, a \$150 billion firm in Santa Monica, California, which manages money for the likes of CalPERS and Stanford University's endowment, about creating such a fund. To my surprise, they had already put some thought into launching a sustainable fund, and had begun discussions with Sustainability Holdings, a new environmental screening company led by leading environmental experts from Yale, Dartmouth, the World Bank, GE's Ecoimagination initiative, and the Carbon Disclosure Project.

## **An Entirely Different Way to Screen Companies**

Sustainability Holdings ("SH" from now on) begins with data from KLD, Sustainable Investment Research International, and the Carbon Disclosure Project, and then ranks companies across fourteen different environmental variables including CO2 emissions, environmental regulatory issues, management's focus on products and services beneficial to the environment, and company-wide environmental initiatives like pollution prevention and recycling. But instead of just blacklisting the "polluters," SH instead applies a score to each company, which is then compared to its industry peers. Then, Dimensional takes that score and formulaically either overweights or underweights the company within the mutual fund. This creates a reward and punishment system, because the best stewards of the environment get more investment capital, and over time, their cost of capital goes down, while the opposite happens to the polluters.

In addition, SH measures each company against its industry peers, so that instead of entirely eliminating chemical or oil companies because they pollute more than banks, the fund overweights the chemical companies with the best environmental records, and underweights those with the worst. This way, the fund invests the same amounts of money in each industry as its non-screened counterparts, leading to better tracking of the market's performance over time, while still helping to effect real change in corporate behavior. A good example of how this works can be found in the oil and gas industry.

You might think that ExxonMobil would get a high environmental sustainability ranking due to their focus on reducing their environmental impact through site remediation, spill prevention, and controlling air emissions from their plants. But SH gave the corporate giant a lower than average rating due to its notable weakness on environmental vulnerabilities. Its vulnerability score is tied for the lowest of its peers and is three times lower than that of Chevron, the sector leader. ExxonMobil emits some of the largest volumes of toxic chemicals per dollar of revenue of any US company, and has been implicated in a number of significant environmental controversies and negative community impacts. This led to a 50 percent underweighting, while Chevron enjoys a 160 percent overweighting.

In addition to robust and scientific environmental screening, the new Dimensional funds offer some of the lowest expense ratios in the industry, with their domestic equity fund charging 0.37 percent, compared to 1.27 percent for the average domestic SRI fund, and their international fund charging 0.57 percent compared to the average SRI international fund which charges 1.63 percent. The Dimensional funds are also more diversified, containing a total of 8,400 stocks (domestic and international combined) compared to about 350 stocks for the average SRI fund.

These new funds are only available through Registered Investment Advisors and some 401k's, although some companies, like mine, require as little as a \$50,000 minimum investment.

There is so much to be concerned about as our environmental and economic resources

are squandered left and right. By knowing your money type, avoiding more self-destructive tendencies and emphasizing strengths, you can align your investment decisions with the latest scientific research instead of emotional hype. With the advent of new cutting edge funds like the two I describe above, you can invest your money in a way, which benefits the planet without compromising your own values, and achieve your unique vision of a fulfilling life, no matter what your investment track record has been. \_

Article by Brent Kessel, CFP, Co-founder of Abacus Portfolios and the author of *It's Not About the Money: Unlock Your Money Type to Achieve Spiritual and Financial Abundance* (HarperCollins 2008). He has been named one of the top 250 financial advisors in the U.S. by *Worth* magazine and is *Yoga Journal's* monthly columnist on the yoga of money.

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