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On this week's show: On this week's show: The evolution of socially responsible investing. Its meaning and performance, with industry pioneers, Christina Alfandary and John Streur.

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CONSUELO MACK: This week on WEALTHTRACK, what socially responsible investing really means and why it is in so much demand. Two industry leaders fill us in next on Consuelo Mack WEALTHTRACK.

Hello and welcome to this edition of WEALTHTRACK, I'm Consuelo Mack.
Socially responsible investing has come a long way since the early days of excluding so called vice stocks from a portfolio. Guns, alcohol, tobacco and gambling were the original sin industries and the decision to avoid them was a value based one, not a financial one.
Over the years environmental, social and governance causes, ESG for short were added to the list. And what was an exclusionary strategy became an inclusionary one. Instead of eliminating companies based on their industry, socially responsible investors started to look for companies that were proactive in their fields.

Instead of avoiding companies that do harm, investing in companies that do good. On the environment, being more energy efficient, managing their emissions, water resources and waste for instance. In social issues, improving product and employee safety, being more family friendly and diversifying their workforce. And in governance, having an independent board of directors, board diversity, high ethical standards throughout the corporate culture and business and policy transparency.

Financial performance is a key factor now. And with a multi-year track record socially responsible investing has proven its competitiveness. One example is the Calvert U.S. Large Cap Core Responsible Index which has beaten its Russell 1000 benchmark over multi-year periods.

Joining us this week are two seasoned practitioners of socially responsible investing with firms who have used the approach for decades. Christina Alfandary is Managing Director of ESG and Sustainable Investments at GAMCO Asset Management, which has a 30-year track record of advising clients on socially responsible investing. Among her responsibilities is advising the firm's analysts and portfolio managers on ESG investing including the Gabelli ESG fund.
John Streur is President and CEO of Calvert Research and Management, a pioneer in responsible and sustainable investing and the parent company of the Calvert Funds which now offers both active and passive SRI strategies. Founded in 1976 specifically as socially responsible investors, more recently Calvert was a founder of the United Nations Principles for Responsible Investment, which now has 1700 large investors participating representing more than $70 trillion in assets.

I started off by asking each guest what socially responsible investing means to them and their respective firms.

CHRISTINA ALFANDARY: So at Gabelli I mean we're a fundamental bottom-up stock-picking firm, active manager. So for us it means having a broader lens to look at more issues, a broader set of non-financial issues and using that and incorporating it into the valuation and the investment process more so that we can design portfolios that meet the value objectives as well as an investment objective for our clients.

CONSUELO MACK: The kind of value objectives that you're looking at, because ESG and impact investing, sustainability, it just seems that there's been a huge evolution in this space. So what in particular are you looking at?

CHRISTINA ALFANDARY: Absolutely. Absolutely. Well, so it's evolved as the space has evolved. Originally the space really started with a lot of negative screening because that's really what was available in terms of data sets.

CONSUELO MACK: So no alcohol, no weapons.

CHRISTINA ALFANDARY: No alcohol, tobacco.

CONSUELO MACK: No tobacco.

CHRISTINA ALFANDARY: No weapons.

CONSUELO MACK: Those are still the screens that you have. Right? At the Gabelli Fund?

CHRISTINA ALFANDARY: Those are screens that we still have in the Gabelli Fund, and on customized portfolios we can use depending upon the clients' priorities, but then more so it's evolved into looking at environmental/social issues of other companies that we're investing in. So looking at a Johnson Controls for example and what they're doing in terms of product technology that touches on sustainability. They're the maker of the stop-start battery which is attributable to saving 660 million gallons of fuel, looking at how a company manages its own carbon emissions footprint, looking at how maybe a beverage company manages its water resources that it uses. So it's a wide variety of issues, but it allows the analyst and the investment portfolios for that fund to look at them more for clients.

CONSUELO MACK: So John, at Calvert what does social responsible investing mean at Calvert?

JOHN STREUR: Consuelo, Calvert is a global leader in responsible investing, and it really permeates everything we do at the firm. We think of it as both participating in positive change and, when appropriate, helping to create positive change. We define our process along the lines of four major pillars. First and foremost, part of responsible investing is getting the returns right; the right amount of investment return for a given level of risk.

CONSUELO MACK: You want financial performance.

JOHN STREUR: Absolutely. So part of being a responsible participant in the capital markets is getting the right amount of return out of those markets. Secondly and I think very importantly, depth of research. So we make all of our decisions based on an intensive, in-depth research process that helps us understand how companies are dealing with environmental and social risks and opportunities. We want to differentiate one company from another and focus our index funds and our portfolios on companies that are real leaders in meeting our principles. Third – and this is a big differentiation for Calvert – comes engagement. We work directly with company management to help move companies forward when necessary. We're activists and we file shareholder resolutions, bring things to shareholder votes, and of course we participate in public policy development. The fourth big pillar is impact reporting. Our clients want to know that their portfolios have better attributes than the broad market. What's their exposure to fossil fuel, greenhouse gas emissions? What is their exposure to human rights issues? So we want to bring metrics to prove that our clients' portfolios look better than the broad market. Those are the four big pillars and, as I say, it's everything that we do at Calvert.

CONSUELO MACK: At Gabelli are there any differences on how you approach this field?

CHRISTINA ALFANDARY: Well, we're a traditional firm that recognized the importance of this field 30 years ago when clients came to us asking us to design portfolios around their values. As the space has evolved, we found ways that it's added to the alpha. Because we're fundamental, bottoms-up research, it adds to certain cultural nuances of companies and behaviors that can help look at these issues and make sure that they're reflected in the portfolio. So within our portfolio we have both the negative screening. We also have looking at ESG issues of the companies that we're investing in, but then perhaps very importantly we have some large, mega trend sustainable themes. So in our portfolio for example we have a water scarcity theme running through the portfolio. We own companies like Xylem that deal with the water scarcity issue. They make pumps. They deal with distribution around those issues. We also have exposure to a health and wellness theme. So as consumers' purchasing patterns have changed, we'll have a sustainability theme like health and wellness running through the portfolio or also a resource recovery theme in certain stocks.

CONSUELO MACK: So this is actually in the Gabelli ESG Fund specifically.

CHRISTINA ALFANDARY: Yes.

CONSUELO MACK: So what would be different is in the Gabelli ESG Fund from the other Gabelli funds, for instance, is if a company met all the criteria, the financial criteria, then if it doesn't meet the sustainability criteria or the environmental, social and governance criteria, it wouldn't make it. It wouldn't stay in the fund. Is that correct?

CHRISTINA ALFANDARY: It probably would not make it into the fund if it didn't suit those criteria.

CONSUELO MACK: How do you screen for companies at Calvert?

JOHN STREUR: Well, first of all we use a research process to identify a broad set of companies that are meeting our principled approach. So as opposed to using negative screens, we use an intense rating system to identify all the companies that might be eligible for a responsible investor to consider.

CONSUELO MACK: You said that research is one of the four pillars, and so you have a very intense ... you described it to me over the phone. I mean it's thousands of criteria. Right?

JOHN STREUR: That's right.

CONSUELO MACK: That you're looking at. So just explain how the research, how this screen works that a company could make it through this screen and what you're looking for.

JOHN STREUR: First of all, we have 20 people who are dedicated to research at Calvert. So we have a lot of experience on the team. Secondly, we have a big data system that desires to bring in all of the pieces of information about a company's environment impact, its social practices, its impact on community. As you said, thousands of different criteria, but what's really important to us are the criteria that are material to that company's bottom line and that are material to the environment or to society. The concept of materiality is a great leveler, and it really helps us focus in on the issues that are critical from an investor's perspective. One could come at SRI or responsible investing from an NGO's perspective or a charity's perspective. We're coming at it from an investor's perspective. So we often look at a data point and say, "What really matters to this entity as a business, and what matters to the environment and society?" That helps us focus in on the data points that are going to mean something in the market and have an impact on the return from the security.

CONSUELO MACK: So the materiality. What are those things that you're looking at, those values?

CHRISTINA ALFANDARY: The materiality changes by industry clearly, but the sort of development of ... and I think what John's referring to is the Sustainability Accounting Standards Board's framework of materiality for investors, and that is a very ... I mean in terms of what's changed over the last three year. In this case the development of that, and research and academic studies have been done about those companies that have been able to focus on those environmental, social, governance issues that are material to their business. Not to say that other issues are not important, but those being material to drive the performance of their business strategically.

CONSUELO MACK: There's now a direct link. That's been proven.

CHRISTINA ALFANDARY: There's a Harvard Business School case study that's often cited from 2015. There's been a number of meta studies done. Goldman Sachs just did another study linking that alpha driver from material Environmental, Social, Governance issues.

CONSUELO MACK: The role of the corporation in society is a paper that you've done at Calvert recently. It's a very broad mandate. You're looking at a lot of different qualities.

JOHN STREUR: Sure, and I think this is an incredibly exciting time in responsible investing. One of the reasons it's so exciting is that these operating companies are beginning to develop real expertise in terms of moving their own sustainability programs forward. So there's a lot for us to analyze when we look at a company, and you're exactly right. Energy efficiency is very important to companies who use a lot of energy. Obviously if they can reduce their costs and reduce their risks of how they use energy and how they bring it in, that's good for the business, good for the bottom line. For companies in the technology sector, it is relevant to the data centers and the energy they use there, but also a lot of technology companies have to attract a certain type of worker to the company, workers who want to be part of a mission, be part of positive change, and they have expectations for how the company they work for is going to behave. So it's become a sophisticated system of creating wellbeing for employees, creating wellbeing for the communities in which companies do business as well as creating significant operational efficiency based on resource utilization and their environmental footprint, and again what's very, very exciting is that boards and senior executives of some of the largest companies in the world have come to focus on this, and they've come to understand how to do this work in ways that work for people, planet and the bottom line.

CHRISTINA ALFANDARY: Well, maybe it would be great for an example, and I think what John's referring to. So if you look at a company like Danone, from an investment thesis when we looked at the company, we can run through the cash flow values, but what's very interesting about Danone specifically is they've really tapped into the large mega trend of how consumers now are much more focused on ...

CONSUELO MACK: Health issues.

CHRISTINA ALFANDARY: ... eating better, healthier eating. They recently bought Happy Baby or Happy Family, the organic baby food company whose growth rate is multiples of what normal baby food is or non-organic baby food. They also completed the acquisition of WhiteWave which makes plant-based dairy products or non-dairy products, almond milk, coconut milk. So that's a sustainable theme, but then also when you look at Danone, they've done an amazing job of not only mapping their water use because they're in sort of a water-intensive business but then also working with the farmers where they source dairy from and making sure that their supply chain of dairy products also how are those farmers managing their water issue. By doing that – and water is just one example – they're essentially enhancing and allowing their sustainability of their own business to persist.

CONSUELO MACK: I mean they're going obviously where the demand is with the two companies, the acquisitions that you mentioned, but also from an investor point of view aside from you two and your firms, are investors looking at, gee, are they being efficient with their water usage?

CHRISTINA ALFANDARY: They are.

CONSUELO MACK: They are.

CHRISTINA ALFANDARY: They are. I mean we get client requests for carbon footprint analysis on portfolios. You can look at the companies and how they're metricking and managing those issues. Most of the companies have target baseline reductions over three to five years, and you can see how they're doing on those targets.

CONSUELO MACK: Would I apply the same standards to an oil company or a chemical company that I would to a Danone which is a consumer products company that's creating healthy products? So how do you differentiate to have a diversified portfolio if you want to invest in a chemical company or an energy company?

JOHN STREUR: That's a great point. So we do our work what we call subsector by subsector. We divide up all the companies in the world into about 200 different peer groups based on common characteristics of the business that they're in, 200 peer groups, and these peer groups have specific characteristics in common, and that drives our understanding of what's really important to those businesses to be paying attention to. So a paper company, water-intensive, forestry-intensive. Those are going to be very, very big factors in that model. Interestingly, corporate governance is important across the board. So we can talk about the things that are different sector by sector, but let's talk for a minute about the things that I think are common across the board. Corporate governance is very, very important, board structure, diversity on the board, gender diversity on the board and then also human resource practices. Today we see real difference between how companies that have mastered the ability to create wellbeing for a talented workforce versus the rest of the pack, and this is becoming a more heavily researched area. I still think there's big opportunity there. So today there's a real competition for talent, and the best companies want to be able to attract the best people across ethnic background, across gender, across age group. So being able to create wellbeing for a diverse workforce starts with having knowledge on the board and diverse board, diverse executive team. When we get into environmental considerations, an interesting area to talk about is supply chain. So there are some companies where all the risk happens at the company, but there are other companies where most of the risk has essentially been outsourced to the supply chain.

CONSUELO MACK: Where they're getting their products.

JOHN STREUR: Exactly, and these are globally extended supply chains that may employ hundreds of thousands of people. Those are big impacts and big risks. So we spend a lot of our time researching supply chain practices in the industries for which it matters.

CONSUELO MACK: What's the newest trend in Socially Responsible Investing?

JOHN STREUR: Well, first I think from a client perspective, we're in a transition period from wanting to avoid bad companies, if you will, to differentiating and understanding who are the leaders. Which are the companies that are really able to master these management disciplines and do it in a way that works for their customers and for their shareholders? So I think that's a big shift in how people are thinking about this. We're moving into the opportunity-seeking phase. This applies to the largest companies in the world as well as the small companies.
I think the biggest trend that I see is expanding this work into asset classes that may not have been covered by responsible investing in the past, so areas like bank loans, emerging market debt, emerging market equity, global small cap, ultra short duration fixed income, municipal bonds, areas where the big ESG research data vendors – which are very important to the system – but areas that they haven't covered yet. So as we're always doing in the investment industry, where can we get an edge? Where can we create information where the rest of the industry hasn't gotten to yet? So I think extending our work into these other asset classes is a big trend that certainly we're involved with and we're pushing forward on.

CONSUELO MACK: At the Gabelli ESG Fund, Christina, I mean are you investing in areas that you wouldn't have five years go?

CHRISTINA ALFANDARY: I think some of the sustainable drivers, the mega trend. We had done a large amount of research on water scarcity many, many years ago, and that's part of our research framework. It's not as if ESG drove us there. It's just a lot of mega trend research that naturally happens within the organization, but it does drive you to certain sustainability themes such as the ones I mentioned before, resource recovery, health and wellness because of what's going on in the United States with obesity, water scarcity and climate change. Then looking at those companies that have product in those issues but then also how are they managing around those ESG issues in sum.

CONSUELO MACK: Performance, you both mentioned it right from the get-go. So the performance of the Gabelli ESG Fund for instance versus an equivalent fund that's not an ESG fund. How does it stack up?

CHRISTINA ALFANDARY: It's about the same. It does well. It does well. We're value, but we're an active manager, but the ESG fund does well relative to a non ESG fund at Gabelli subject to those additional issues and per the client.

CONSUELO MACK: Calvert has created indexes as well with a 15-year track record. So how do those stack up for instance in the large cap universe?

JOHN STREUR: We're so happy to be able to say that over the 15-year record of the Calvert Large Cap Core Index, it's slightly outperformed the market with similar risk levels. So I think that's the proof point, and we've done that recently with no exposure to fossil fuels, with no exposure to companies that were mentioned earlier that would get knocked out by negative screens. So I think the concept that one can have their cake and eat it too, in other words investing in companies that are helping to make the world a better place, is also good for performance.

CONSUELO MACK: One last question and that is the one investment for a long-term diversified portfolio. What should we all have some of in a long-term diversified portfolio, Christina?

CHRISTINA ALFANDARY: I would say investors should really make sure that they have some exposure to some of the big mega trend sustainability themes going on in the world related to climate change or water scarcity and things like that. Those are very long-term trends that will play out. In terms of stocks, we like Danone. They pay a lot of attention to the environmental/social issues. They have done water scarcity mapping. They're a leader in that definitely within the food and beverage industry for looking at water issues. They also have set very specific carbon reduction targets and they've met those, but more importantly when you look at them as an investment thesis, they've tapped into this long trend that's started already about consumers paying more attention to what they eat.

CONSUELO MACK: John.

JOHN STREUR: I think broadly it's important for investors to have exposure to emerging markets including China, India and throughout Southeast Asia and ultimately Africa. Those are real sources of population growth and economic growth, and from a responsible investment perspective, it's essential that we have companies that can properly steward those development paths forward. So go find a fund that has responsible investing and exposure to emerging markets. I think that's a great place to be. For more conservative investors who want to come in through a global company, Unilever is really the top of the class in terms of being the largest consumer product company in the world that embraces sustainability from the board all the way through the staff.

CONSUELO MACK: All right, we'll leave it there. Thank you both so much for being with us on WEALTHTRACK. So John Streur from Calvert and Christina Alfandary from Gabelli. Thanks so much for being with us.

CHRISTINA ALFANDARY: Thank you.

CONSUELO MACK: At the close of every WEALTHTRACK we try to give you one suggestion to help you build and protect your wealth over the long term.
This week's Action Point is: Consider investing in a socially responsible fund, either actively managed or passive. Value based investing has more than come into its own with nearly $9 trillion dollars worth of investments in the U.S. alone and performance that's competitive with traditional approaches. There are many options to choose from as well across asset classes and geographies.

Among Morningstar's favorites are funds from socially responsible fund families including Calvert and Parnassus. One recently highlighted fund is the 4-star, bronze medal rated Parnassus Fund, a large growth fund with a strong long term track record. Making money while having a positive impact is a nice combination.

Next week, we will sit down for an exclusive interview with a third generation Great Investor, the Davis Funds Chris Davis joins us to discuss where he is finding value in today's market.

This week however, on our website, WEALTHTRACK.com, you can find out how Christina Alfandary and John Streur became so involved professionally in Socially Responsible Investing, we would welcome your thoughts on the subject as well, so please reach out to us on Facebook and Twitter.

Thanks for watching. Have a great weekend and make the week ahead a profitable and a productive one.