

investing **in** communities

○ | Meritas Mutual Funds

Socially responsible investing (SRI) is concerned with balancing financial return and social impact. Meritas is a socially-responsible mutual fund company that integrates community investment as a core pillar of SRI. Community investment can be an important brand differentiator for SRI, and provide a significant social benefit to local communities.

○ | Socially-Responsible Investing

Socially Responsible Investing

Socially responsible investing (SRI) is defined as the integration of environmental, social and governance (ESG) factors in the selection and management of investments.¹ In addition to seeking a positive financial return, SRI strategies have reshaped the traditional risk-reward equation to include a fuller consideration of environmental and social issues. The scale of SRI has grown rapidly in Canada, and it is estimated that SRI represents nearly 20 per cent of assets under management in Canada (half a trillion dollars), a significant leap from the four per cent share garnered in 2004.² RBC, Canada's largest bank, recently launched 3 socially-responsible mutual funds in conjunction with Jantzi Research, a leader in SRI screening.

○ | Community Investment

○ | Brand Differentiation

- **Shareholder advocacy** involves investors playing an active role as the owners, including “dialoguing” with companies on issues of social, environmental or governance concerns.
- **Community Investment** (referred to as CI) directs capital from investors and lenders to communities that are underserved by traditional financial services institutions.

Community Investment

Screening strategies and shareholder advocacy are the more commonly-understood components of SRI, and many financial institutions utilize at least one of these in their SRI strategies. To date, however, CI remains a small niche segment of SRI in Canada with an estimated \$809 million in CI assets as of June 30, 2006.⁵ CI is capital used to finance deep-seated needs of local communities that cannot ordinarily be addressed by traditional investment models.⁶ These funds can be used to make loans, loan guarantees and/or private equity capital, in conjunction with technical assistance, to low-income individuals, micro-enterprises/small businesses, affordable housing projects, non-profits and environmental projects.⁷

SRI is also referred to as double or triple bottom-line investing, ethical investing, sustainable investing, or green investing.³ There are three components of SRI: ⁴

- **Screening** is the practice of evaluating investment portfolios or mutual funds based on social, environmental and good corporate governance criteria.

¹ *The Social Investment Organization (SIO) (2007) “Canadian Socially Responsible Investment Review 2006”, <http://www.socialinvestment.ca/documents/SRIReview.pdf>, p.5*

² *SIO (2007), p.34*

³ *Social Investment Forum (n.d.) “Socially Responsible Investing Facts”, <http://www.socialinvest.org/resources/sriguide/srifacts.cfm>*

⁴ *Ibid.*

⁵ *SIO (2007), p.17*

⁶ *Ibid, p.16*

“It is not just about how much you make, but how you make it.”

Gary Hawton
CEO, Meritas

⁷ Coro Strandberg (2004) “The Emergence of Community Investment as a Strategy for Investing in Your Community”, http://www.corostrandberg.com/pdfs/CommunityInvestment_E.pdf, p.6

⁸ SIO (2007), p.16; and Strandberg (2004), p. 6

⁹ SIO 2007, p.16

¹⁰ Strandberg 2004, p. 6

¹¹ Meritas Group of Funds (2007) “Semi Annual Report: Six months ended June 30, 2007”, http://www.meritas.ca/Asset/iu_files/2007SemiAREnglish.pdf

¹² Gary Hawton. Personal Correspondence, January 2008

¹³ A more comprehensive description of each category is available on the Meritas website at <http://www.meritas.ca/invest.shtml>

¹⁴ Gary Hawton. Personal Correspondence, January 2008

¹⁵ Figures and investments taken from the semi-annual report as at June 2007.

Examples of Community Investment⁸

- Micro-credit to individuals
- Risk capital and loans dedicated to not-for-profits and co-operatives
- Local risk capital for development of small and medium-sized enterprises (SMEs)
- Lending for social or affordable housing
- Lending for environmental regeneration and conservation initiatives

For CI, two principles are important: the local control and administration of funds, and the expectation of a return on investment. For the latter, the principal is returned to investors, with financial returns ranging from zero up to market rates. The emphasis is on the social return rather than a singular focus on investment risk and return, since CI is driven primarily by a values-based approach that seeks to improve the quality of life in the targeted communities.⁹ This is consistent with evidence that typically the social impact is greatest with those investments offering the lowest financial return.¹⁰

Meritas Mutual Funds

Meritas Mutual Funds is a socially-responsible mutual fund company formed in 2001 with \$265 million in assets under management. It is a joint venture of the Mennonite Foundation of Canada, Mennonite Savings and Credit Union (Ontario) Ltd. and Mennonite Mutual Aid. As a financial management company grounded in ethical principles, Meritas’ goal is to join beliefs with deeds using the tools of socially responsible investing.¹¹ Meritas offers a family of seven mutual funds that includes money market and bond funds, and Canadian, US and international equity funds – all driven by socially-responsible investment strategies.

Knowing that a key measure of success is the financial returns that they get for investors, Meritas invests in companies that display strong financial fundamentals. However, financial performance needs to be aligned with

the corporation’s “social conscience”. Gary Hawton, CEO of Meritas, explains that, “it is not just about how much you make, but how you make it.”¹² In balancing financial and social performance, Meritas’ has approached SRI in a holistic manner, and is the only Canadian mutual fund company to embrace all three components for SRI within their portfolio of funds:

- **Screening** – Meritas utilizes both negative and positive screens, seeking to both “punish” bad companies, but also reward companies with good social and environmental performance.
- **Shareholder Advocacy** – Meritas employs an active shareholder approach to encourage companies to become better social performers. Proxy voting is carried out in manner consistent with their social investing criteria (*see box*).
- **Community Investments** – Meritas allocates up to 2% of the assets in each of its portfolios towards Community Development Initiatives both domestically and internationally.

Meritas’ Social Investing Criteria¹³

- Respect the dignity and value of all people.
- Build a world at peace and free from violence.
- Internalize a concern for justice in a global society.
- Exhibit responsible management practices.
- Support and involve communities.
- Practice environmental stewardship.

Unique to Canada, Meritas has committed to allocating up to 2% of their assets to community development investing (CDI). To date they have invested over \$1 million in community investments, with another significant investment tranche forthcoming.¹⁴ In addition to the positive social return, financial returns range from 1.75% to 5.38%.¹⁵ Much of the investment is channeled to microfinance and microenterprise development in developing countries using diversified investment pools through organizations like MicroVest, MEDA’s

Sarona Fund, First Oiko Credit Canada, and the Calvert Foundation. Investments in community development and environmental sustainability in Canada are channeled through VanCity and Ecotrust Canada.

Community Investment as Branding

Branding is the process of differentiating a product or company in the minds of its customers. For Meritas, it achieves this through a number of avenues. The commitment to SRI is reflected in everything the company does, including its products, values, and corporate culture. This is further built on by allowing the customer to engage in areas such as shareholder advocacy. Even though there are many other mutual fund companies that offer SRI-branded products, Meritas' distinguishes itself from others by including community investment in its portfolio.

Meritas' commitment to CI represents an important brand differentiator that has contributed to their corporate growth. Meritas grew by 90% in 2007, significantly higher than any other SRI fund company, and tends to be among the top two SRI fund companies each month for net sales.¹⁶ In a crowded investment sector, they were "willing to tell a different story than everyone of the risk-reward tradeoff". Meritas has stated that, in providing opportunity in areas that might not normally have access to capital, the effect on return to the investor should be insignificant, but the effect on recipient of the funds could be very significant.¹⁷ For instance, targeted microfinance investments in developing countries can improve access to capital for microenterprises in the short-term, and contribute to poverty alleviation efforts over the long-run.

Meritas' clients and advisors have also acknowledged that CI is a key differentiator and could be used to draw in more assets, and one of Meritas' top-selling advisors uses CI to cement

the relationship with clients.¹⁸ Customers are not only interested in asking, "what does the company stand for?", but also "how does this align with my personal values?" Customers place a value on both the tangible (such as community investment products) and intangible (such as the holistic corporate commitment to SRI) elements of branding. Together, these qualities have built a brand that resonates with customers interested in investing responsibly.

Investing in Communities

SRI allows investors to express values-based choices through their financial investment decisions, and more institutional and retail investors are keen to ingrain environmental and social factors into the risk-reward equation.¹⁹ While the retail SRI market has not developed as rapidly in Canada, there is evidence that Canadians are very open to investing in funds that have SRI components.²⁰

As more institutional and retail investors embrace SRI, financial institutions will have to pay attention to ways in which they can distinguish themselves from their competitors. Community investment (CI) offers one such strategy. To date, CI remains a small niche segment of SRI in Canada; however, prospects for growth in community investment remain high, particularly drawing on the US experience where more sophisticated investment vehicles and models have emerged.²¹

Meritas has shown that CI represents an innovative way to differentiate in a crowded mutual fund market. Brand differentiation can have positive impacts on customer loyalty, and contribute to the growth of mutual funds in an increasingly-competitive financial investment arena.²² As well, Meritas has shown that CI is an important component of SRI to supplement investment screening strategies and active shareholder advocacy. Moreover, in exchange for a small financial and risk premium, the social impact on communities can be substantial.

“Community investment is an important component of SRI strategies. Moreover, in exchange for a small financial and risk premium, the social impact on communities can be substantial.”

¹⁶ Gary Hawton. *Personal Correspondence*, January 2008

¹⁷ Meritas (2007) "SRI", <http://www.meritas.ca/sri.shtml>

¹⁸ Gary Hawton. *Personal Correspondence*, January 2008

¹⁹ Greenberg Quinlan Rosner Research (2006) "TIAA-CREF Releases Participant Survey on Socially Responsible Investing", http://www.tiaa-cref.org/about/press/about_us/releases/pressrelease182.html

²⁰ Chris Coulter (2005) "Expectations of Companies: Key Trends and Findings from the GlobeScan 2005 Corporate Social Responsibility Monitor", http://www.socialinvestment.ca/SIO_press_GlobeScan_.pdf

²¹ Strandberg (2004), p. 7

²² Cone Millennial Cause Study (2006) http://www.coneinc.com/oldsite/Pages/pr_45.html

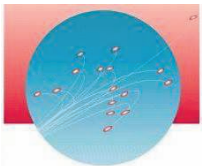
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Selected Resources

Meritas Mutual Funds: www.meritas.ca

The Social Investment Organization:
www.socialinvestment.ca

Tessa Hebb (2002) "Mutual Interest, Options for Cause Related Marketing with the Mutual Fund Industry", Council for International Co-operation, Ottawa: Canada., http://www.ccic.ca/e/docs/002_development_mutual_interest.pdf

Coro Strandberg and Brenda Plant (2004) "Scan of the Community Investment Sector in Canada." National Roundtable on the Environment and Economy, Capital Markets and Sustainability Program, http://www.corostrandberg.com/pdfs/nationalRoundtable_sept2004.pdf

Coro Strandberg (2004) "The Emergence of Community Investment as a Strategy for Investing in Your Community", presented at "Investing In Your Community" conference, Saskatchewan, http://www.corostrandberg.com/pdfs/CommunityInvestment_E.pdf

Carleton Centre for Community Innovation

The Carleton Centre for Community Innovation (3CI) brings together superior academic research and knowledge dissemination to Canadian communities in ways that promote long-term growth and sustainable development. One of Canada's leading sources of expertise in social finance, 3CI has also played a leadership role in grant-making, evaluation and policy analysis in the fields of community economic development and social enterprise. From 1997 to 2008, the Centre managed the Community Economic Development Technical Assistance Program (CEDTAP), with the support of The J.W. McConnell Family Foundation, The Ontario Trillium Foundation, Bell Canada and other partners. Other action-research priorities for 3CI include local governance, community learning and community-university partnerships.

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