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Socially Responsible Mutual Funds (corrected)

Meir Statman

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Abstract

Conversations about socially responsible investing are difficult because they combine facts with beliefs. Proponents of socially responsible investing believe that combining
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S&P 500 ... onventional
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Errata

Socially ... l funds in
the peri ... (DSI), an
index of ... S&P 500
Index.

The DSI is a capitalization-weighted index modeled on the S&P 500 but with a combination of exclusionary and qualitative screens used in its construction. The screens eliminate from the DSI companies that derive 2 percent or more of sales from military weapons systems, derive any revenues from the manufacture of alcohol or tobacco products, or derive any revenues from the provision of gaming products or services. The qualitative screens reflect the entire company record on diversity, employee relations, the environment, and similar issues.

For the May 1990 to September 1998 period, the DSI beat the S&P 500 by a small margin when performance was measured by raw returns. The mean arithmetic annualized return of the DSI in the study period was 17.31 percent, which exceeded the 16.95 percent mean return of the S&P 500. Beta and standard deviation both indicated that the DSI is somewhat riskier than the S&P 500. When risk-adjusted returns were measured, the S&P 500 beat the DSI by a small, statistically insignificant, margin.

The Domini Social Equity Fund, a mutual fund indexed to the DSI, uses the DSI social screens. Some other socially responsible mutual funds, however, do not use the DSI screens. For example, the Amana Fund screens reflect Islamic principles, and the Meyers Pride Fund screens in companies that support gay rights. The screens do share some common themes: 84 percent of socially screened portfolios exclude tobacco, 72 percent exclude gambling, 69 percent exclude weapons, and 68 percent exclude alcohol.

The risk-adjusted performance of the study's 31 socially responsible mutual funds lagged the S&P 500 by an average of 5.02 percentage points a year when risk was measure [illegible] onventional mutual f [illegible] ntage points. The diffe [illegible] conventi [illegible] formance of both soc [illegible] e general tilt of m [illegible] stocks in the p [illegible]

Socially [illegible] rs or as swords i [illegible] le funds act as sword [illegible] ises those compani [illegible] ally responsible investing acts as a banner when it rallies the public to use political action as swords. For example, the social responsibility movement played a role in the battle that led to the imposition of high taxes and settlement costs on tobacco companies.

Socially responsible investments provide insights into the general demand for securities that meet investors' search for value-expressive as well as utilitarian features in their investing. In the future, a comprehensive model of asset pricing will need to describe how both utilitarian and value-expressive features determine the demand for investments and their expected returns.

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