Investing in virtue vs. vice

CURIOUS INVESTOR | 'Sin' stocks doing far better this year, but many funds shun them

Comments

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Are you a "virtuous" investor? Are you ready to put your righteousness to the test?

This could be an uncomfortable exercise. As the idea of investing with a social or moral conscience has spread, so has the opposite notion. You can invest in a portfolio of "vice" or "sin" stocks. Judging purely on financial performance, there's evidence that sin has been winning, at least lately.

The International Securities Exchange has an index for sin stocks, its ticker symbol is **SIN** so there can be no mistake, and it's up by 34 percent so far this year, easily beating the major market indexes. It's also well ahead of the **Domini400 Social Index,** a widely used measure of companies that pass tests of values-oriented investors. The Domini400 is up around 11 percent year to date.

Looking beyond just 2009, the comparisons are mixed, and this is where one gets bogged down in the definitions of social and sin investing. In general, the socially conscious mutual funds such as those in the **Calvert** or **Ariel** families try to beat the Standard & Poor's 500. In these generalized, big-company weighted portfolios, stocks connected to alcohol, tobacco, wagering and weaponry are usually verboten, although all are legal products and some arguably have redeeming value.

Mutual fund investors need to look a little harder if they want to exclude companies on the basis of pollution, labor relations or involvement in abortions or stem-cell research. Several companies offer funds that screen for values based on teachings of the Catholic Church.

Don Cummings, principal of Wheaton-based **Blue Haven Capital,** said the social values that apply in a fund can have a substantial impact on performance. Funds that leave out oil companies suffered last year when oil prices were high and the refiners were raking in record profits. Now those funds are faring better, Cummings said.

The issue is complicated on the vice side of the question, as well. The ISE's SIN index covers companies only in alcohol, tobacco and gaming. Bloomberg Financial Markets indicate that an exchange-traded fund that was licensed to track the SIN index was liquidated, but investors who want to walk on this wild side could find themselves in the **Vice Fund (VICEX),** which is operated by Dallas-based Mutuals Advisors.

VICEX, however, hasn't matched the returns of the SIN index. The Vice Fund is up only 3 percent this year. Unlike SIN, the Vice Fund broadens its umbrella of disrepute to include defense contractors. It also tends to invest in smaller companies, while the SIN index is mostly for large capitalization stocks. So definitions matter.

The Vice Fund takes as its benchmark the Russell 1000 index, which it has outperformed. As a result, Morningstar has given the fund a four-star rating out of a possible five stars. But because of an awful 2008, the fund has posted a total gain of only around 6 percent since its inception in 2002.

I couldn't find a vice fund or index that includes producers of sexually explicit material, but if it's a stock such as **Playboy Enterprises (PLA)** that you are after, it makes more sense just to set your money on fire.

A couple of academics weighed in on the virtue vs. vice question in stocks. They came down in the side of vice, and in the Journal of Financial Economics, no less.

Marcin Kacperczyk of New York University and **Harrison Hong** of Princeton University analyzed 41 years of data for alcohol, tobacco and gaming companies. They found that the taint they carry kept many buyers such as pension funds or universities from investing in them. They said that created better values for those not so inhibited. They got in at a cheaper price and often received higher dividends as a reward.

The research also indicated that the vice stocks performed better during recessions, although that hasn't been the case in our current one.

So the choice can be tough. Investors should consult a higher authority than a mere broker.

CROP WATCH: The cool, wet weather that has dominated the Chicago summer is bringing down crop futures prices at the Chicago Board of Trade. Over time, that could ease pressure on food prices. Corn futures are down about 20 percent this year, and soybean futures are off about 7 percent. "With the cool temperatures and rain somewhere every second or third day, the weather has been stress-free for the crops," grain analyst **Dan Cekander** of **Newedge USA** told Bloomberg News.

Wheat also has spun into a deep decline of 34 percent over the last 12 months. Here, the influence includes talk from Washington regulators that they might end waivers that index traders use to exceed position limits. Volatile trading has caused gaps between the cash and futures prices, and some wonder if speculators are to blame.

The Board of Trade, part of **CME Group (CME),** argues that the waivers should remain and that terms of its wheat contract, such as delivery points, can be changed instead.

CLOSING QUOTE:"Bargains abound in the U.S. stock market. Bull markets typically begin when the following four conditions are present: the economy is bottoming, profits are bottoming, the Fed is stimulating and valuations are low. That's where we are now." -- **Bill Miller,** *chairman, Legg Mason*