July 14, 2003

M E M O R A N D U M

TO: Board of Directors
Society for the Study of Social Problems

FROM: Susan M. Carlson, Investment Advisor
Budget, Finance, and Audit Committee

RE: Annual Report on Investment Performance

Description of Investment Portfolio

On December 31, 2002, the Society for the Study of Social Problems had an investment portfolio of $399,448 at current market value. This portfolio comprised socially responsible investments of two types: (1) socially responsible mutual funds; and (2) certificates of deposit and money market account with community development financial institutions.

The Society holds investments with two socially responsible mutual funds. The managers of each of these funds use a stringent set of financial and social criteria in selecting securities for inclusion in the fund's portfolio. They also seek out companies that are model corporate citizens, and attempt to positively influence corporate behavior on important social issues by having a direct dialogue with corporate managers, filing shareholder resolutions, and proxy voting. While the specific criteria used by fund managers vary across funds, there are strong similarities. For example, all funds use "exclusionary screens" that avoid companies involved in the production, sale, or distribution of alcohol, tobacco, firearms and military weapons, and nuclear energy. They also avoid companies that pollute the environment, use animals to test products, have weak employee/labor relations, diversity, and human rights records, and produce or distribute unsafe products.

The Society's largest investment in socially responsible mutual funds is with the Pax World Fund ($248,415: $219,080 Minority Scholarship; $9,478 Lee Legacy; $19,857 Life Membership). The Pax World Fund was established in 1970 and has a solid performance record. It is classified as a "domestic hybrid" fund which includes stocks, bonds, and cash equivalents. A hybrid or balanced fund is lower risk than a growth fund which typically includes only stocks. Morningstar gives the Pax World Fund a five-star rating (out of five) when it is compared with all other balanced funds (both socially responsible and non-socially responsible). The Board has restricted the income from the Minority Scholarship part of this investment be used to fund the minority scholarship.

The Society's second largest investment in socially responsible mutual funds is with the Domini Social Equity Fund ($51,033), a "large blend" index fund. The primary investment objective of the Domini Social Equity Fund is growth, and its portfolio consists of stocks. Thus, it is slightly higher risk than a hybrid/balanced fund. Morningstar gives the Domini Social Equity Fund a three-star rating (out of five).

The Society deposits most of its cash reserves with two community development banks and one community development credit union. The Society's money market account is with the ShoreBank in Chicago, the oldest community development lending institution in the nation. Certificates of deposit are held with First American Credit Union in Window Rock, Arizona ($50,000) and the Louisville Community Development Bank in Louisville, Kentucky ($50,000). The Society's community development investments are at market rates of interest. The ShoreBank money market account and certificate of deposit with the Louisville Community Development Bank are insured up to $100,000 by the FDIC. The certificate of deposit with First American Credit Union is insured up to $100,000 by the National Credit Union Administration.

The mission of community development banks and credit unions is to promote economic development in wealth-disadvantaged communities by providing low interest small business loans, home mortgages, consumer loans, and banking services to people who otherwise would be denied these services and opportunities by conventional banking and credit institutions. Unlike conventional credit unions that are allowed only to accept deposits from a clearly defined group of clients, community development credit unions may accept deposits from individuals and institutions outside their client group. This increases resources available for promoting economic development in the disadvantaged communities these credit unions serve. Community development credit unions are democratically controlled, not-for-profit, insured and government regulated, and operated by voluntary boards of directors. The Society's investments in these community development institutions are used to provide the small business loans, home mortgages, and consumer loans that foster economic development within these communities.

Financial Performance: Socially Responsible Mutual Funds

In 2002, the Society's mutual fund investments suffered losses consistent with overall market trends. The Society's unrealized paper loss on investments was $49,251. Dividend and capital gains income was also down considerably for the year–$7,780 in 2002 compared with $23,483 in 2001. Despite this paper loss and decrease in investment income, however, the Society's investments performed well relative to market indicators and other comparable funds.

The Pax World Fund investments sustained a loss of 8.86% in net asset value in 2002. This was much less than the 22.10% loss experienced by the S&P 500, and less than the 10.69% drop in the Lipper balanced fund index. The Pax Fund paid a total of $4,539 in dividend and capital gains income–$4,014 minority scholarship, $182 Lee legacy, and $343 lifetime membership. Note that the income derived from the Pax minority scholarship fund ($4,014) was less than the value of one minority scholarship ($10,500). The good news is that so far this year, as of July 9th, the Pax Fund's net asset value has increased by 8.47% (see Figure 1).

The Domini Social Equity Fund recorded a total loss in net asset value of 21.08% in 2002. This is comparable to the 22.10% loss experienced by the S&P 500. Dividend income from the Domini Fund was $312 in 2002. Figure 2 shows that between December 31, 2002 and July 9, 2003, the net asset value of the Domini Fund increased by 14.49%.

It is misleading to examine only short-term gains and losses of stock investments. Figures 3 and 4 show the percentage change in the net asset value of the Pax and Domini funds compared with the S&P 500, respectively, for the period July 9, 1998 through July 9, 2003 (weekly averages). Figure 3 shows that the Pax Fund gained less in net asset value during the boom period in 1999-2000 than the S&P 500, but its losses were less than the S&P 500 during the downward turn in the market. The Pax Fund's performance is less volatile than the S&P 500 due to the balanced nature of its holdings.

The Domini Fund tracked with and at times outperformed the S&P 500 prior to September 11, 2001. Since that time, the Domini Fund has performed somewhat less well than the S&P 500. The correlation between the two was .983 prior to September 11th, and .965 thereafter.

Social Performance: Socially Responsible Mutual Funds

The Society's investments in socially responsible mutual funds are not merely about financial gains and losses; they are also about doing social good. The Domini Social Equity Fund files and encourages others to file shareholder resolutions with companies designed to change socially irresponsible and/or undesirable corporate behavior. Most of Domini's activism efforts focus on sweatshops, workplace diversity and safety, and issues related to the environment. During the current proxy-voting year, Domini took the lead in filing six shareholder resolutions and was the co-filer in eight additional resolutions. In addition, Domini engaged six companies in dialogue without filing resolutions: Proctor & Gamble (fair trade coffee and recycled content); Gap, Nordstrom, McDonald's, Walt Disney (vendor standards); and Merrill Lynch (environmental issues). I would encourage Board members to visit the Domini website to see the full range of resolutions, proxy votes, and social activist initiatives of the Domini Fund (www.domini.com).

The Pax World Fund also promotes social activism and community development, and posts proxy votes on its website. This year, Pax was one of the key supporters of an SEC rule requiring public disclosure of proxy votes of mutual funds. This initiative was successful. This initiative and others are detailed on the Pax website (www.paxfund.com).

Community Development Investments

The Society's certificates of deposit with the First American Credit Union and Louisville Community Development Bank are at market-based rates of interest, as is the money market account at the ShoreBank. What social good is being done through the use of the Society's funds in the disadvantaged communities served by these financial institutions?

First American Credit Union (FACU) in Window Rock, Arizona, serves native peoples throughout Arizona, and in parts of New Mexico and Utah. Since its inception in 1962 as the Navajo Tribal Employee's Credit Union to 2001, FACU expanded its membership to 18,685, and made 663,678 loans totaling $196,106,796, 80 percent in rural areas. In 2001 alone, FACU made 41,132 loans totaling $15,940,003. Half of the current borrowers are women, 85 percent are Native American and 10 percent are Latino. Its mission is three-fold: (1) to develop and provide the best possible financial services and products to both the membership and the credit union, (2) to encourage regular savings, and (3) to promote community service while strengthening the long term stability of the credit union. By making deposits, the Society helps FACU to achieve this mission.

The mission of the Louisville Community Development Bank (LCDB) is to stimulate economic growth and revitalize the West End, and Smoketown, Shelby Park and Phoenix Hill distressed, inner-city neighborhoods of Louisville Kentucky by making small business, construction, remodeling, and housing acquisition/rehabilitation loans. Approximately 80,000 people live in the 12 neighborhoods served by LCDB. Unemployment in the investment area is three times the national average and 38 percent of the population, including 13,000 children, live below the poverty line. About 70 percent of the city's African Americans live in the West End and Smoketown areas. Nearly half of the adults over age 25 lack a high school diploma or GED certificate.

LCDB loans stimulate economic development by supporting small business development and expansion, making homeowners out of home renters, improving the quality and value of real estate, increasing the number and quality of goods and services available to residents, and creating jobs and linking neighborhood residents to career-path employment. Many of the borrowers were rejected as being too high risk by traditional lenders. Since opening its doors in January 1997, LCDB has made loans totaling $34 million. These loans have created or saved 1,044 jobs in the investment area, which is one way the bank measures success. Seventy-five percent of the bank's clients are African American, 24 percent are Caucasian, and one percent from other racial backgrounds.

One LCDB success story concerns a loan that saved a small minority-owned business. Four years ago, Betty and Tony Berry started a business in their basement laundering and pressing table skirts for banquet tables in large hotels. Impressed with their work, one of the leading hotels in Louisville asked the Berrys to launder and press table linens and offered to allow them to rent the hotel's laundry facilities to do so. However, the hotel was bought out and the new management would not allow rental of their laundry facilities. LCDB provided a loan that allowed the Berrys to purchase both a building and laundry equipment. Today the Berry's business is booming. They now serve hotels, country clubs, and rent-all companies throughout the city, and they have increased their employees from four to fourteen, expecting the number to grow in the future. Deposits from outside investors like SSSP make such loans, and success stories, possible. I would encourage Board members to visit LCDB's website: http://www.morethanabank.com.

ShoreBank is a full-service commercial bank headquartered in Chicago. It is the oldest community development bank in the nation. Its mission is to promote community development by providing commercial, consumer, and real estate loans, and retail banking services to residents in targeted distressed inner-city neighborhoods in Chicago and Detroit. Current borrowers are 70 percent African American, 8 percent Latino, 7 percent Asian/Pacific Islander, and 15 percent Caucasian. Since opening its doors in 1973, ShoreBank has made approximately $600 million in loans to 13,000 families and businesses. Approximately 25 percent of the bank's total deposits come from individuals and organization outside the retail area, like SSSP, who choose ShoreBank because of its community development mission.

Gwen Duncan-James attests to the success of ShoreBank's community development initiatives. She is President and CEO of Gareda Diversified Business Services, a company that provides nursing care and homemaker assistance throughout Chicago. The company employs almost 900 people, many of whom were formerly unemployed. ShoreBank has provided lines of credit and a mortgage loan which have helped Gwen to expand the business over the years. She states, "ShoreBank has played a very important role in the success of my business." You can read more about ShoreBank at http://www.sbk.com.

In sum, the Society's reserves that are deposited in community development financial institutions are being used to economically empower both urban and rural communities in different parts of the nation. The few examples noted above show just some of the good work these community development financial institutions are accomplishing.

Figure 1. Pax World Fund

12/31/2002 - 07/09/2003

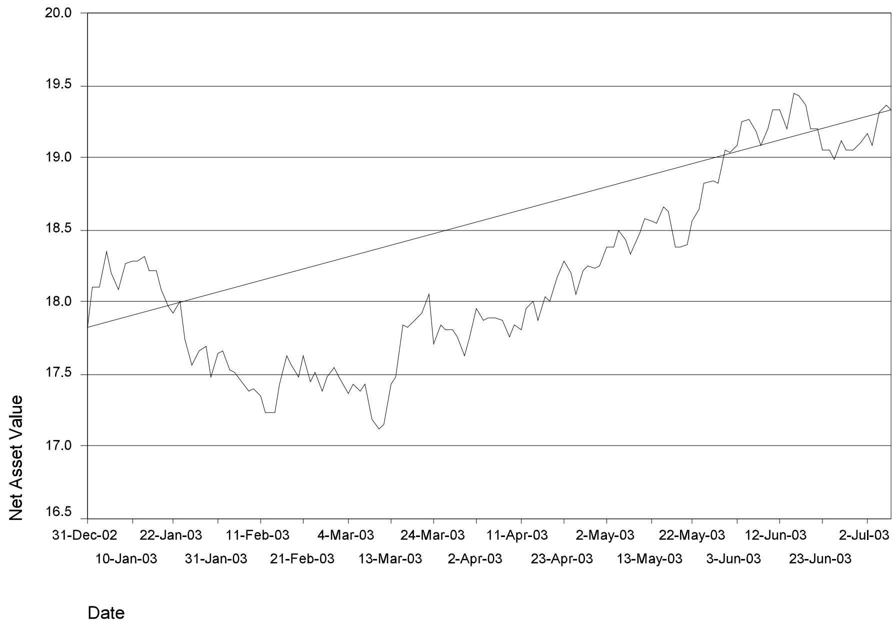

Figure 2. Domini Social Equity Fund

12/31/2002 - 07/09/2003

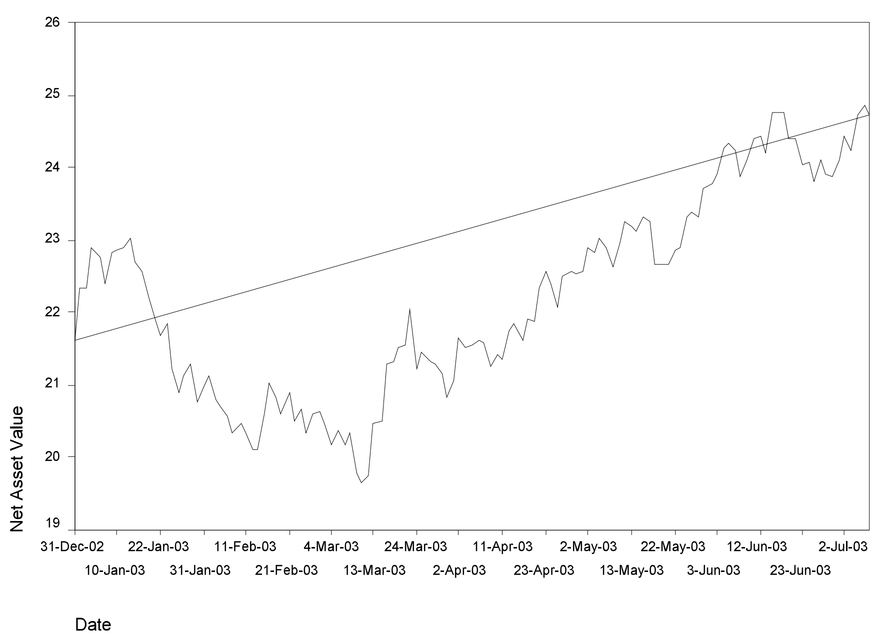

Figure 3. Five-Year Comparison of the Pax

World Fund and the S&P 500

Figure 4. Five-Year Comparison of the

Domini Fund and the S&P 500