

EcoNotes



SHOREBANK PACIFIC
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Moving Towards a Sustainable Society – Framing the Context

By Kathleen Sayce, *Bank Scientist*

When we set ourselves the task, with your help, of lending money to help promote a more sustainable economy, we set out to do this from within communities. This is where perception becomes critical. No one can be an expert in every kind of business that operates in our society. But what we can do is define how a typical business works right now, and what its impacts are. Then we can define what this business might look like in an efficient, sustainable, community-oriented world. These two states are brackets, which give us today, the present state of operations and practices, and a goal, a more effective future way to operate. Within these brackets, we can reframe business operations and define goals that help communities thrive. Note that this process does not tell us how to get there, only where to go.

When we first started evaluating our clients, we had general ideas about what was good for a business and its community, and what was bad. Good was healthy, meaning reduced environmental impacts, and bad was unhealthy. So it was easy to see that organic farming on a small scale would be important for communities, because conventional farming exports capital (and food) out of a community instead of bringing economic and environmental health to the community.

Organic dairies have been clients of ours for several years because of this difference, but along the way we've learned to appreciate the difference between confinement and pasture-based, and direct local sales versus regional cooperatives and distributors. Each of them operates at a different scale and has a different impact on land, water resources, use of imported feed, and the community where the dairy is based.

We have shifted over the years from a very basic perception of good for life and the bank to a more systematic framework based in the principles of The Natural Step. This gave us a way to look more carefully at how to evaluate each client. The Natural Step principles are based on physics and biology. They help anyone, any business or community, to take a longer view than the next quarter, year or decade, and plan systematically for a more prosperous future. This framework helped us develop our evaluation process by understanding current conditions and defining possible

future conditions. We initially used five elements (natural productivity, green chemistry and engineering, efficiency, landscape conservation and community) to evaluate each client and ourselves (after all, if we can't apply TNS principles to ourselves, we can't expect anyone else to follow them).

The five-element process only took us so far. We kept running up against the need for more depth in community issues and in financial analysis. We took almost two years to revise our analysis process; shifting the physics and biology elements to a sector called Conservation, and adding two more sectors: Community and Economy. All sectors use three elements, scores in each one range from zero to three, for a total range of zero to nine for each sector, or zero to twenty-seven for all sectors.

The Conservation sector looks at energy, materials and land and water capacity; underneath these labels, we look at the same analytic points as before. The Community sector looks at jobs, necessities and quality of life; this is a departure from conventional community development thinking. A key premise is that not all development is necessarily good for a community; our focus is to understand this distinction, and to help clients be better for their communities. The Economy sector looks at risk, local business connections, and scalability. This goes beyond typical risk assessment to specifically evaluate each client in terms of its current management and their long-term plans.

Typically we do a preliminary evaluation, then work with clients on specific issues, and re-evaluate them annually. I take the lead on the conservation side, work with the lender on the community side, and the lender takes the lead on the economy side.

We've talked before about our clients and the range of enthusiasms with which they work with us on their long-term plans. Just as each one of us is somewhere on the change continuum, so is each client. Some are innovators, leading the way to the future with great new ideas and plans to get there. They show all of us how to make effective changes. Many are early adopters: if they see others using new ideas

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Mission Review

David C.E. Williams,
President, ShoreBank Pacific



It is interesting to note that Paul Hawken recently condemned the SRI mutual fund practice of negative screens in their selection of investment companies. While noting that their approach to responsible investing is “We won’t invest in ...”, he points out that such a system doesn’t really promote change but merely assuages the investor’s psyche.

He calls for a positive scoring system that measures companies against what is achievable.

The vision of ShoreBank Pacific is to assist in the development of sustainable communities in the Pacific Northwest by supporting companies practicing behaviors that will allow those businesses to continue in a healthy manner for generations. We understand that the environmental, social, and economic areas of a business or community are an interconnected system in which emphasis on one characteristic leads to the degradation of the others unless a careful balance is achieved. It is, therefore, incumbent on us to understand these dynamics with every customer with whom we work. Our science staff helps these customers to willfully change to better practices because (and only if) it is better business.

It is satisfying to know that that our scoring system is a positive, dynamic system. We apply these criteria to every borrower and loan deal to assess their mission behavior against a standard of potential performance. Thus, we determine if the company’s behavior is typical of the industry in which they reside or they do better than their peers, toward an absolute standard of “can’t be beat”. As a result, companies are encouraged to move toward improved behavior rather than just being screened out. Our bank scientist and the developer of our scoring system, Kathleen Sayce, details this system in her article in this issue.

The knowledge that no company is perfect and all have room for improvement places a significant burden on the bank when deciding whether to provide funds to a company at all. Since we don’t use negative screens, this means that if we take on a borrower, we do so with the idea that we can help them improve their mission performance. This places on us the obligation to seriously consider how we can be helpful to the firm and to assess whether or not they will listen and learn. Our national deposit manager, Lucy Brehm, discusses in this issue the struggles we go through in determining if we can and should take on this responsibility.

THE PROCESS OF CHANGE is fascinating. We all deal with changes every day of our lives, and how we cope says much about each of us. Some people are innovators: creative and leading edge folks who take up new technology and ideas very quickly and spread the word about the innovation to everyone they know. Following them are the early adopters, who follow the vanguard but let others do the alpha and beta testing. Early adopters and innovators make up about half the population. The other half of the population is composed of late adopters and the trailing edge, who wait to take up new changes, new behaviors, new technologies.

FOR EXAMPLE, one of our clients in the wood products industry is an innovative young company that makes overlays for veneer products. The company’s conservation score is 5; they have developed innovative new processes to reduce or eliminate the need for organic solvents in the overlay process, which has major health benefits for their workers. The firm remodeled buildings to house the process lines rather than build new spaces, and the overlay product goes to regional plywood mills. The community score is also 5; this company has low turnover, good wages and benefits in a rural timber community, it is very active on the social side as a leader. The economy score is 6; the firm is very well run. The owners live in the community, are local leaders, and are well-connected to local businesses. They plan to grow this business appropriately. The overall score is 16, with room to improve, but with an outstanding innovative edge on similar firms that produce the same product in traditional (and more hazardous) ways.

All of the above is a longwinded way of saying that we operate on the fundamental principle that we will work with all companies that show an interest in improving their social, environmental, and economic behaviors toward a sustainable model. We try to work with companies that are integrated into the economy in addition to dealing exclusively with companies that are on the fringe. In so doing, we feel that it is more likely we will have true economic impact. Not everyone would agree with our individual decisions, but after reading the articles in this issue of EcoNotes, I hope you will understand that we take this work very seriously and make every attempt to actually make a difference in the sustainability of our companies and of the economy of the Pacific Northwest.

Living Our Mission

“The web of our life is a mingled yarn, good and ill together” — *William Shakespeare*.

Having a mission is one thing – living it is another. ShoreBank Pacific tries to “live” its sustainability mission every day whether we’re considering a loan or purchasing supplies. The expression “where the rubber hits the road” comes to mind. We decided early on that the best way to really change the world was to work not only with those business owners who already understand the importance of looking at the environmental consequences of their business practices, but also, and perhaps more importantly, with those who don’t.

The so called “green” or “socially responsible” entities are easy. We make the loan and feel good about it. But there are many more companies where some components of what they do adversely impact society. Yet these same businesses may bring jobs or important products and services to our region.

So beyond the scoring system, how should a bank, which strives to lead the financial world in sustainable banking, decide to lend money to a variety of enterprises that are a “mingled yarn”? Let’s talk about some of the sticky wickets we’ve encountered over the last few years:

Casinos: Most socially responsible investing companies screen out companies who are involved in gambling – for many good reasons. On the other hand, casino profits have provided millions of dollars to communities, and have been lifelines for many struggling Native American economies. Many tribes use these profits to provide support for valuable tribal programs. In ShoreBank Pacific’s early years it did lend to several tribal casino projects, but the loans were internally controversial from the beginning. Several years ago the bank took a hard look at the realities of casinos and the cost benefit of introducing broader gambling into communities. There was a great deal of internal discussion and research. Many people have strong feelings that the bank should support tribal decisions to go with gambling as the best way to improve their economies. Others felt that the social problems that come with casinos take a huge toll on a community’s resources. After months of debate and discussion we decided not to renew any of the previous casino loans and to consider future casino lending only if this was the only viable means for economic survival for the tribe.

Fish Farms: ShoreBank Pacific believes strongly in the idea that the Pacific Northwest is part of Salmon Nation. We understand the decimation of the fishing economy of the Northwest due to low prices from the glut of fish produced by net pen farms – especially those in Chile and elsewhere. These threaten local bio-diversity because fish do escape from net pens and breed with local wild stock. However, SBP was offered an interesting lending opportunity. A fish farmer in the PNW was growing native and endangered Chinook from specific rivers in tanks on land –

away from the water. He was also researching ways to grow organic farmed salmon. Discussion began to intensify at the bank as the review progressed. Some of us thought that this was a way to provide cheap, healthy, nutritious protein to people who might not otherwise eat seafood. Others felt it was another step towards industrializing a resource base that we and many others have been trying to decommo-ditize. Because these fish are native to the bioregion and kept in tanks away from the water, there is little threat to local fish runs. We discussed and studied this issue for so long that eventually the borrower went to another bank!

BT corn: ShoreBank Pacific was asked to provide financing for an alternative fuel program in the Midwest using corn to produce ethanol. This seemed to be right up our alley until we found out that most of the corn in the area was BT corn. How do you weigh the benefit of alternative fuel against the dangers inherent in GMO? Once again our bank scientist earned her keep by researching and studying the pros and cons of the project. It turned out that the production method started with wet milling. Dry milling denatures the active herbicide compounds in this GMO line. So we decided that if a dry milling opportunity came along, we’d take a good look at it, and pass on the wet milling processors.

Gas Stations: Yes – we have loaned money to gas stations. In the future our cars will be powered by bio-diesel or other means, but for now we’re stuck with gasoline. The gas stations that we have financed have all been small independently operated businesses and some have been clean-ups of brownfields. These were considered non-fundable by other banks, yet provide needed fuel and other services to their communities. Our position is that so long as we have gasoline, and the potential for ground contamination, let’s keep those stations in areas of prior contamination to protect “clean” ground. These gas stations will most likely be the distribution system for the fuels of the future. We are very interested in both alternative fuels and power generation but recognize that the transition will take years.

Alcohol: Liquor shows up on most screens for socially responsible investing. ShoreBank Pacific lent money for an organic vineyard in Northern California and has considered other specialty products. For example, in the Pacific Northwest there are small producers of very high quality specialty liquors that highlight local fruits. The wine industry is one of the regional businesses that are supporting the retention of family farms. We have discussed the social problems inherent in alcoholic products – especially those with marketing that targets youth. We came to a consensus that small local producers of high quality products play an important role in our communities and are less likely to be consumed in an abusive manner by underage drinkers.

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Framing the Context *(continued from page 1)*

to be more successful, they follow right behind them. Others are late adopters, who take up changes only after they've been thoroughly tested by others. Trailing edgers follow the pack, and may gripe all the way about the need for change, any change.

We work with all of them, learning from the innovators, helping the trailing edgers to understand that long-term planning will help each one to run a better business. We are agents of change: we had to recognize this early on to be successful. This means that we had to step outside the traditional bankerly role of risk assessment and fiscal management, and into the murky waters of planning for change. By understanding where typical operations are

today, and where they can go, we have been able to construct a systematic way to evaluate our clients. There are many details behind this overview. To read about some of those details, see recent additions to our website.

[We suspect that many of you, our depositors, are also innovators and early adopters. We would like hear from you with your self-assessment. You may write, e-mail or call; this can be as simple as your name and the appropriate phrase. Let us know, and in a later issue, we'll report back what we learned.]

New CD Product Announcement

EcoDepositors frequently request a Certificate of Deposit that allows additional deposits. In response to this customer demand we've created a new product, the EcoDeposits Add-On CD.

This account offers you the ability to make deposits at any time and features a one-time rate bump as an added bonus. Please contact us at ecobank@sbpac.com or (888) 326-2265 for application information. Offer expires 6/15/05.

The EcoDeposits Add-On CD

Additional deposits OK

30-month term, automatic renewal

Starting rate of 3.50% (3.55% APY) with one rate bump at your discretion during the 30-month term.

FDIC coverage up to \$100,000

Living Our Mission *(continued from page 3)*

These are not all of the issues we've struggled with, nor does this essay attempt to capture all of the discussion, but by highlighting some of our internal discussions we want to share with you our attempts to be thoughtful, pragmatic and remain true to our mission. We now have a mission committee, which includes the bank science staff and top management, which focuses on these issues, providing different points of view and ongoing discussion.

We know that not everyone will come to the same conclusions as we did on these issues, but hope you appreciate our intention to be transparent. From a mission perspective, our decision to lend to problematic clients means that we also have to figure out how we can help them change. Only by engaging with these businesses can we help to move our economy towards sustainability and our society to a healthy, enduring world.