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Will Millennials Finally Put An End To Tobacco (Altria), Gambling (Las Vegas Sands) And Vice Stocks?

Millennials are changing everything. They are rumored to be more socially conscious, more environmentally friendly and more concerned with good corporate governance. Some experts have rumored that Millennials might even be tempted to actually "vote" their stock share ownership in the never-ending stream of company board proposals and elections.

MSCI has released a "rating" system for this type of evaluation which is based on ESG (Environmental, Social, Governance). Naturally the so called "sin" stocks would rate relatively poorly on this scale. Altria (a.k.a. Philip Morris), Las Vegas Sands, and American Outdoor Brands Corp, more commonly known as the maker of Smith & Wesson guns, all score relatively poorly in some area of their ESG rating system due to their vice.

NRA members look over pistols in the Smith & Wesson display. (Photo by Scott Olson/Getty Images)

But will a poor rating by MSCI cause Millennials to avoid owning the sin stocks?

This article addresses two core questions about ESG. First, how will ESG scores affect the buy/sell/hold decisions of future investors, not just on a company by company basis, but within a portfolio. Second, is ESG a strong enough factor upon which to base a decision, or is it missing an element?

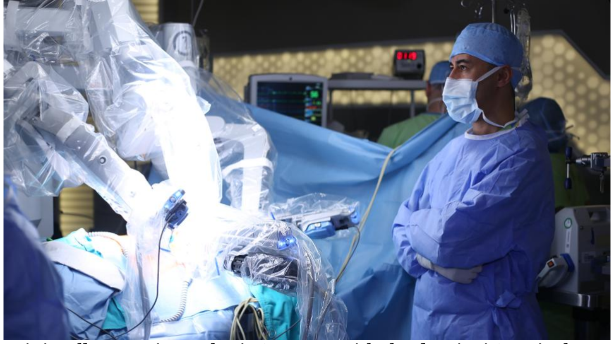
Consider the ESG ratings of non-sin-stock companies.

One that gets a high ranking is Tesla which designs, develops, manufactures and sells electric vehicles and energy storage products in the United States and internationally. The company operates in two segments, Automotive and Energy Generation and Storage. They have the best rating overall in terms of ESG standards. Will Millennials actually buy the stock "*because*" it has a high MSCI ESG rating?

But what about companies that might not sail through so smoothly?

Intuitive Surgical designs, manufactures and markets the da Vinci surgical system. It's a game changer in the medical field. It allows a surgeon's natural hand movements, which are performed on instrument controls at a console, to be converted to corresponding micro-movements of instruments positioned inside the patient through small incisions or ports. No longer do surgeons need to make long incisions to access the appropriate areas to perform surgery. Because of the ISRG robotic surgery system, there are a few small incisions made, instruments are inserted inside the patient and the operation is performed with much less collateral damage. The healing time from such an advancement is cut dramatically not to mention less chance of infection and certainly less pain and recovery time. But what about the ESG standards? ISRG gets the lowest rating due to ongoing malpractice litigation and scrutiny regarding the marketing and safety of its core product, the da Vinci system.

Regarding ISRG, is there more to consider than just a low ESG rating? After all, ISRG did pioneer the development of robotic surgery. It


Minimally Invasive Robotic Surgery with the da Vinci Surgical System. Credit Shutterstock.

might be expected that there will be growing pains associated with such an advancement in the medical field.

Another example is Veeva Systems Inc. VEEV provides cloud-based software for the life sciences industry in North America and internationally. VEEV is actively utilizing technology to reduce overall costs and improve data dependent outcomes which is desperately needed in the healthcare space. They received the lowest ESG rating due to concerns about privacy and information security and lagging employee benefits and training programs, despite the fact that VEEV rates highly among employees and were even in the Top 10 CRM Firms to work for in 2014 according to Glassdoor.

The ISRG and VEEV examples highlight the idea that perhaps a stock with a relatively low ESG rating could still be held in an ESG sanitized portfolio. Perhaps ESG is missing an element.

Another example involves Boston Scientific, Teleflex, C.R. Bard and Medtronics. Each has the lowest ESG rating due to the issue of product recalls. Each recall is different and has a varying impact on the company's legal, financial and brand image. Some recalls are fairly simple and create little impact while other recalls are due to patient deaths and cause legal and financial damage to the company.

The question for all investors is, "Should a company be left out of an ESG sanitized portfolio due to some low scores which may be the result of growing pains endured when pushing the boundary of science and seeking to improve or save lives?"

At Warren Financial, we believe it's important to look inside the ESG ratings and modify those ratings with one additional factor alluded to throughout this article. The "H", or Human factor.

A Tesla Model X electric SUV (Photo credit SAUL LOEB/AFP/Getty Images)

When considering the "H" factor, (the Human Factor) a relatively higher score would be given to a company that is pushing into new technologies or advancing the boundaries of science. A lower "H" factor score would be given to companies that produce products that are known to harm humans, such as tobacco. Tesla would receive a relatively strong "H" score because the company is advancing technology that is good for society since electric cars will decrease pollution in major cities around the globe. Another positive example of a relatively high "H" factor would be CREE Inc., a company known for the LED lightbulb which is decreasing power usage which decreases pollution and waste.

By adding the "H" factor, a poor "E" rating, or a poor "S" rating, would still apply, but a high "H" rating should make a company eligible for a sanitized ESGH portfolio by offsetting lower ESG scores.

The non-sin stocks mentioned in this article would all receive a very high "H" rating which would help to offset other lower scores. The sin stocks would receive a low "H" rating.

In our view, a high "H" factor makes the company a highly desirable investment, not just for the profit motive, but also as an investment that will advance the human race.

ESG is missing the "H" or "Human" factor. ESG should become ESGH.

Disclosures*: Warren Financial has long positions in some of the stocks mentioned in this article (ISRG, BSX, VEEV, BCR, MDT, LVS, TFX, etc) both for our clients and our own portfolios. We may be starting new long positions in some of these companies in the future. The fact that a company is mentioned is not a recommendation or offer to buy or sell that stock or bond. Investors should always seek advice from an advisor that knows their particular financial situation and not assume that general information such as the information in this article will apply directly to their portfolio. Investing includes the risk of loss.*

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Randy Warren is CEO of Warren Financial. For information on how to protect your investments from volatility visit WarrenFinancial.com and make sure to investigate our Safer-Equity strategies.