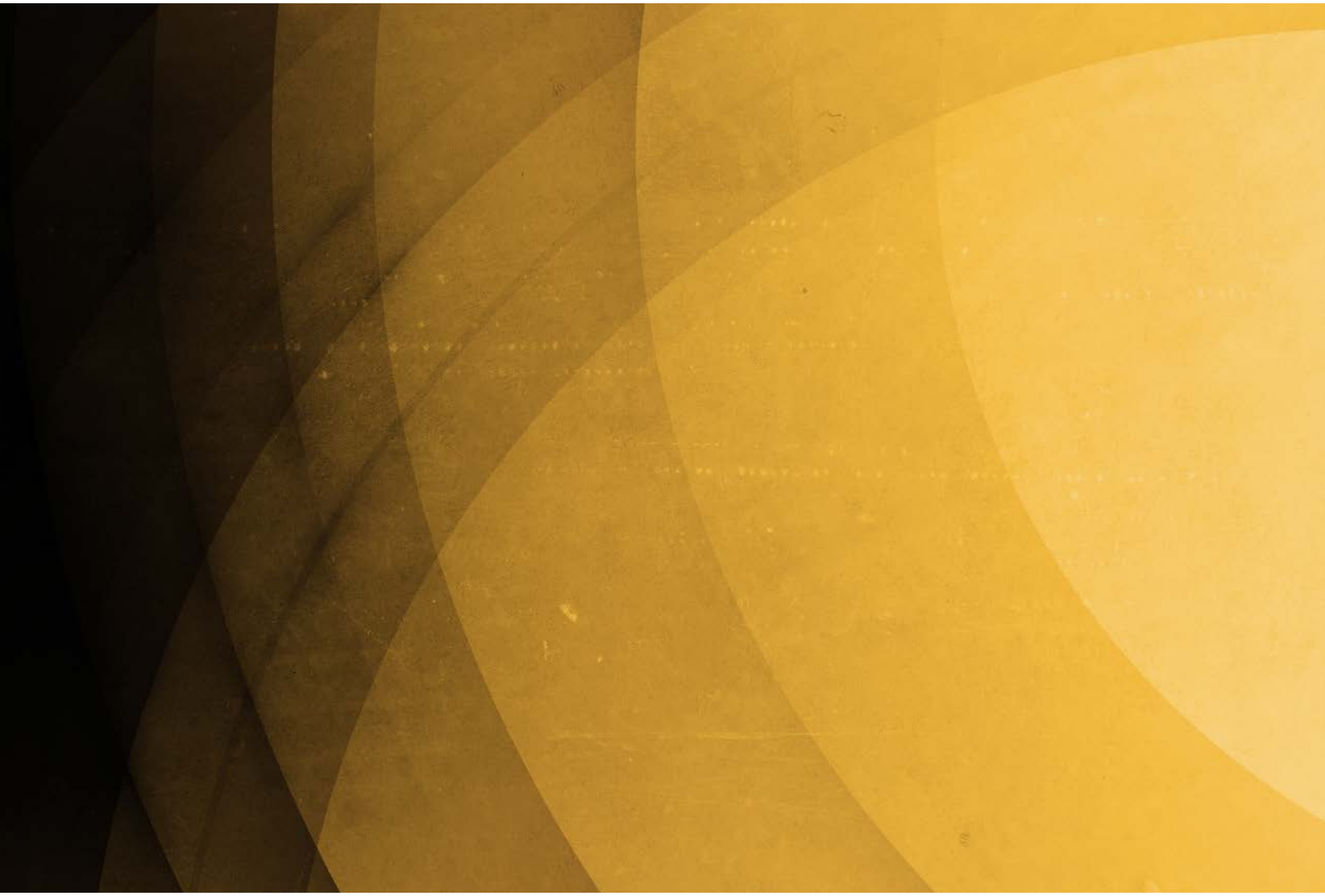
Saturna White Paper: Practice Management

Client Segmentation:
Re-engage Clients Through Sustainable Investing



SATURNA
SUSTAINABLE FUNDS

About Saturna Capital

Saturna Capital, manager of the Amana, Saturna Sustainable, Sextant, and Idaho Tax-Exempt Funds, uses years of investment experience to aid investors in navigating today's volatile markets. Founded in 1989 by professionals with extensive experience, Saturna has helped individuals and institutions build wealth, earn income, and preserve capital.

Saturna's deep-rooted belief in value investing shines through in the quality of our investments. We don't follow trends, we analyze opportunities. Years of experience have given Saturna financial strength and stability. Most important to Saturna's success, however, is our clients' success. We believe that our clients' interest always come first.

At Saturna, we believe in making your investment dollars work hard for you. Toward this end, Saturna strives to not only offer the best investment opportunities from mutual funds to IRAs, but to match those sound investments with superior customer service.

Amana Mutual Funds Trust

SEXTANT MUTUAL FUNDS

IDAHO TAX-EXEMPT FUND

SATURNA SUSTAINABLE FUNDS

Please consider an investment's objectives, risks, charges, and expenses carefully before investing. To obtain this and other important information about the Amana, Sextant, Idaho Tax-Exempt, and Saturna Sustainable Funds in a current prospectus or summary prospectus, please visit www.saturna.com or call toll free 1-800-728-8762. Please read the prospectus or summary prospectus carefully before investing.

The Amana, Sextant, Idaho Tax-Exempt, and Saturna Sustainable Funds are distributed by Saturna Brokerage Services, member FINRA / SIPC. Saturna Brokerage Services is a wholly-owned subsidiary of Saturna Capital Corporation, adviser to the Funds.

MARKETING 101: CUSTOMER SEGMENTATION

At its most basic, customer segmentation simply means dividing your clients into different groups. Groups can be established using many different criteria, such as spending patterns, location, age, gender, etc. Ultimately, the segmentation strategy should be based on factors that affect purchasing behavior.

There are a variety of methods for advisers to segment clients including:

» Assets under management
» Letter grades, such as A, B, C, and D
» Precious metals (platinum, gold, silver, bronze).

Creating a categorization tool can help an adviser make sense of the clients they have in their book.

Customer segmentation can yield a number of benefits, from being more efficient with tailored marketing messages to gaining insights into how to improve products and customer service (and ultimately, sales). Understanding your customers at a deep level helps you interact with them in more relevant ways which fosters trust.

In this piece, we're using engagement criteria to segment and identify clients that may be disengaged for various reasons, and then we present one possible method of re-engaging those clients.

No segmentation strategy is foolproof, but the effort is worth the potential gains.

Experienced financial advisers are familiar with the concept of categorizing–or segmenting–their client base. Client segmentation offers a practical approach to assessing the client-adviser relationship among a variety of client profile metrics. And while you are likely familiar with some clients' personal interests and values, that may not be the case for the portion of your clients who range from distant to outright frustrating.

The objective of this white paper is to familiarize advisers with new segments of investors based upon their awareness of sustainable, responsible, and impact investing, and to provide guidance on how advisers should position themselves to have a conversation with their clients about these topics.

SUSTAINABLE STRATEGIES

Traditional

Typically no consideration of ESG factors, or application of negative or positive screens. Investors at this end of the spectrum focus solely on maximizing financial gain.

Integrated

Evolved from traditional finance. Combines an emphasis on financial results with the the consideration of material ESG factors.

Ethical / Advocacy

Ethical investing seeks to build portfolios that reflect the values of the investor's religious denomination. These portfolios typically exclude specific industries by employing negative screens.

Advocacy seeks to make specific, measured change on a variety of ESG issues through the engagement practices of proxy voting and shareholder resolutions.

Thematic / Impact

Thematic Investing reflects sector-specific issues while impact investing tends to allocate capital toward enterprises.

Philanthropic

Philanthropic investors fall on the opposite end of the spectrum from Traditional Finance, with a focus on maximizing impact and with little regard for returns.

The increasing interest among investors in sustainable and values-aligned investing may provide opportunities to reinvigorate and add depth to relationships which have grown distant. Initiating a conversation about your disengaged client's interests and values shows thoughtfulness and may renew your discussions regarding their financial planning needs. The personalization of a values-aligned portfolio may speak to a particular client in a way that your traditional line-up does not and can offer a meaningful way for you to differentiate your practice in a highly commoditized and competitive business.

The adoption of values and interests into a client's financial plan is simply another evolution of the complex adviser-client relationship: where once investors only needed a stock broker to initiate their trades, the relationship evolved to that of a fee-based asset allocator, then to a planner taking a much more holistic view of their clients' financial affairs. Advisers now assist in all sorts of complex planning and lifestyle decisions including eldercare, intergenerational wealth planning, and long-term care. We are in the midst of an era where advisers must continue to evolve to assert their worth by considering their clients' more specialized goals beyond time horizon and risk tolerance. An Allianz survey found that 65% of clients who spoke to their adviser about Environmental, Social, and Governance (ESG) investing pursued the investment, and that it's not just women and millennials who seek these strategies: 68% of investors age 65+ have a positive opinion of ESG investing, and men and women are almost equally interested in ESG strategies. Allianz also notes that "advisors should proactively reach out to their clients on this subject—they are waiting to hear from you!"[1]

Despite the tremendous growth and increased visibility of sustainable investing, advisers have been slow to add values-aligned and sustainable options to their practice. Meanwhile, retail investors continue to express an interest in having their investments reflect their values: a Morgan Stanley survey from 2017 shows awareness and interest in sustainable investing climbing steadily—with 75% of individual investors and 86% of millennials interested in sustainable investing.[2] A State Street report, *The Investing Enlightenment: How Principle and Pragmatism Can Create Sustainable Value through ESG*, found that "49% of non-ESG investors believe talking to their adviser about ESG investing would be useful," and that "more than half of retail investors say ESG factors will be increasingly important to them in the next five years." The report goes on to advise that "financial advisors should be prepared with concrete solutions for these investors, which are only set to grow."[3]

We know that clients are constantly making lifestyle choices based on their values and interests–so it should be no surprise that many clients will want their savings and investments to align with those values and interests as well.

As we learn more about client demand for socially responsible, sustainable, and ESG investment products, it becomes clear that most advisers are leaving opportunities to strengthen their relationships with clients on the table. These statistics beg the question: *why has there been hesitation among the financial adviser community to adopt sustainable and values-aligned investment options?*

Whether advisers are hesitating due to concerns about performance, fiduciary duty, lack of education, or other reasons, we firmly believe that sustainable investing is the best way to differentiate one's practice and potentially engage distant clients.

MAPPING CLIENT TYPES AND CONVERSATIONS

Once you are ready to initiate conversations with your clients around values-based and sustainable investing, you can map these conversations by further segmenting clients based upon their awareness of sustainable investing strategies. We see investors falling into the following three categories:

- Aware of and interested in opportunities to engage in values-based or sustainable investing
- Unaware of opportunities to engage
- Aware of, but skeptical toward, sustainable investing

THE AWARE

Clients who are already aware of and interested in sustainable investing are spread across a diverse spectrum of values and interests ranging from faith-based principles to thematic environmental or social concerns, such as fossil fuel avoidance, gender equality, or animal cruelty. It is very likely that these investors already believe that their investments can be a means to an end by encouraging the environmental, social, or governance behavior they wish to see. Offering these clients sustainable portfolios is the best way to engage and retain them. Initiating conversations with these clients will be very straightforward: simply asking them about their opinions or lifestyle habits will give you tremendous insight and invite further conversation. Saturna's *Sustainability Workbook* provides a number of exercises that you can use to pinpoint a client's interest and determine what success will look like.

the *aware*

THE UNAWARE

Investors who are truly unaware of the opportunities for sustainable investing are unbiased and likely open-minded; they also present the best opportunities for you to more deeply engage with prospective or disengaged clients. A 2017 study by global asset managers Allianz found that though only 4% of survey participants could explain what the letters ESG stand for, 90% care about at least one of the underlying issues, and 80% act on these issues in their daily activities.[4]

the *unaware*

Initial conversations with unaware clients will introduce the concept that it is possible to align their investments with their values and will explore the advantages that consideration of ESG factors can add to a portfolio. Saturna's practice management white paper, *Adding Sustainability: Having the Conversation,* offers a helpful framework for initiating conversations with these clients.

the skeptical

Clients who are aware of, but skeptical toward, sustainable investing may have misconceptions that can be remedied. Listening is key to engaging these clients; understanding your client's biases and level of knowledge will be important in gauging how to move forward.

Clients who are skeptical can be broken down into the following sub-segments:

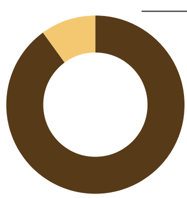
- The underinformed and
- The uninterested

UNDERINFORMED

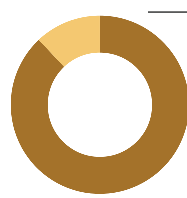
Underinformed investors are best categorized as somewhat aware but potentially biased: sustainable investing—and its predecessor, socially responsible investing—continue to suffer from a reputation of underperformance. Conversations with your clients in this sub-segment should be focused on listening to their views and biases and being prepared to address their questions about performance that will almost certainly arise. It will also be helpful to walk through the various forms of socially responsible investing; philanthropic investing and impact investing look very different from ESG investing, for example.

Numerous studies have shown that incorporating a broader set of ESG factors in conjunction with standard financial considerations demonstrates results that are in line with market results. Studies tend to reveal that investors are not "giving up" on returns but can potentially benefit from the risk mitigating processes typically associated with ESG-screened investments.

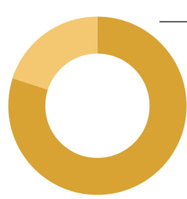
A 2015 meta-study by the University of Oxford and Arabesque Partners reviewed 190 of the highest quality academic studies that examined the relationship between sustainability and firm performance and drew the following key conclusions:[5]



90% OF STUDIES SHOWED THAT SOUND SUSTAINABILITY STANDARDS LOWERED THE COST OF CAPITAL.



88% OF STUDIES INDICATED THAT OPERATIONAL PERFORMANCE OF FIRMS WAS IMPROVED BY ROBUST ESG PRACTICES.



80% OF STUDIES SHOWED A POSITIVE RELATIONSHIP BETWEEN STOCK PERFORMANCE AND GOOD SUSTAINABILITY PRACTICES.

In another study entitled, "Corporate Sustainability: First Evidence of Materiality," authors Mozaffar Khan, George Serafeim, and Aaron Yoon found that "firms with good performance on material sustainability issues significantly outperform firms with poor performance on these issues, suggesting that investment in sustainability issues are shareholder value-enhancing."[6] Not all investments enhance shareholder value, however. The authors differentiate between "material" sustainability factors and "immaterial" factors using information provided by the Sustainability Accounting Standards Board (SASB) to determine materiality. Companies that demonstrated high performance on material issues and low performance on immaterial issues demonstrated alpha[7] of 6.01% against a broad universe of stocks.

The root of addressing questions about performance is to ask your client to clarify what they believe the benchmark is. Opening up a conversation about these issues is another way for you to create value and strengthen the relationship.

THE UNINTERESTED

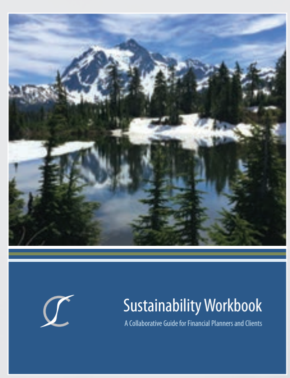
Clients who are uninterested in sustainable investing strategies may share many of the same biases as underinformed investors, but with a less open approach to discussion. There are any number of reasons clients may conclude that sustainable investing is not right for them—it could even be that they just want to do their own research. Your best strategy with a client who expresses disinterest is to simply prepare to have a conversation about sustainable investing strategies when or if the client is ready.

CONCLUSION

The market is developing a broad supply of values-based and sustainable investment solutions that serve diverse investor needs and interests, and surveys indicate with increasing frequency that investor interest in these solutions is growing. Financial advisers who seek to keep up with this latest evolution in the industry are wise to educate themselves on the underlying values and products that now make up a quarter of the professionally managed assets in the US. And beyond retaining existing clients and attracting new clients, configuring your practice to include a wider array of sustainable investment vehicles may better position you to reinvigorate or strengthen relationships with clients who may have slipped through the cracks.

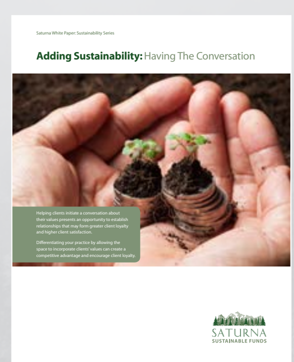
Saturna Sustainable Funds Sustainability Workbook:
A Collaborative Guide for Financial Planners and Clients

A practical guide for integrating a client's interest in values-based and sustainable investing within the parameters of standard financial planning. Structured to initiate a discussion with clients about their values, the Sustainability Workbook comprises three workbook exercises and a reference guide to help you gauge client interest in and promote adoption of sustainable investing strategies.



Adding Sustainability: Having The Conversation

Helping clients initiate a conversation about their values presents an opportunity to establish relationships that may form greater client loyalty and higher client satisfaction. Differentiating your practice by allowing the space to incorporate clients' values can create a competitive advantage and encourage client loyalty.



Industry Groups

UN PRI – The United Nations Principles of Responsible Investment is "the world's leading proponent of responsible investing." Asset owners, investment managers, and service providers are eligible to sign on as signatories, which requires affirming six principles.

The UN PRI provides excellent resources as well as a reporting framework for its nearly 2,000 global signatories.

US SIF – The Forum for Sustainable and Responsible Investment is a US-based association with a membership model that includes financial planners and advisers as well as investment management and advisory firms. With the mission to "rapidly shift investment practices toward sustainability, focusing on long-term investment and the generation of positive social and environmental impact," US SIF produces a notable biennial trends report. It also provides a database of sustainable mutual funds.

Resources

UN SDGs – In 2015, the United Nations ratified 17 goals for global sustainable development, ranging from "No Poverty" (Goal #1) to "Peace, Justice, and Strong Institutions" (Goal #16). Asset managers are adapting their portfolios to include the SDGs with increasing frequency, and the 17 goals provide an excellent framework for understanding many of the most pressing sustainability issues we face.

CDP – The CDP (formerly the Carbon Disclosure Project) is a voluntary reporting system for cities, companies, and states that wish to track and report their environmental impact, and then report that impact to investors. The CDP reports that over 6,300 companies responded to their climate change, water, forests, and supply chain questionnaire this year.[8]

SASB – The Sustainability Accounting Standards Board was founded in 2011 to develop and disseminate sustainability accounting standards. SASB has created helpful materiality maps among sectors and industries.

MORNINGSTAR SUSTAINABILITY RATING – Morningstar has created a process to evaluate the sustainability for over 20,000 funds worldwide, similar to their star rating but using globes instead. Morningstar also has a number of explainer resources available online, including their Sustainable Investing Handbook.

Analytics Vendors

- **Bloomberg**
- **MSCI**
- **Sustainalytics**
- **Thomson Reuters Eikon**
- **CSR Hub**

Further Reading

- **The Investing Enlightenment:** *https://arabesque.com/research/Final_The_Investing_Enlightenment.pdf*
- **The Business Case for Sustainable Investing:** *http://www.morganstanley.com/ideas/business-case-for-sustainable-investing/*
- **RobecoSAM (video): The truth about sustainability investing: fact or fiction:** *https://www.robeco.com/me/insights/2018/04/the-truth-about-sustainability-investing-fact-fiction.html*
- **Corporate Sustainability: First Evidence on Materiality:** *https://dash.harvard.edu/bitstream/handle/1/14369106/15-073.pdf?sequence=1*
- **BNP Paribas: Great Expectations ESG** *https://securities.bnpparibas.com/insights/great-expectations-esg.html*
- **Allianz: ESG Clarity:** *https://us.allianzgi.com/en-us/ria/resources/esg-clarity/what-we-found*
- **Arabesque: From the Stockholder to the Stakeholder, How Sustainability Can Drive Financial Outperformance:** *https://arabesque.com/research/From_the_stockholder_to_the_stakeholder_web.pdf*

About The Author

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Senior Investment Analyst and Portfolio Manager

Patrick T. Drum, Research Analyst and Portfolio Manager, joined Saturna Capital in October 2014.

He is a former adjunct professor of finance for the Sustainable MBA Program at the Bainbridge Graduate Institute (BGI) currently known as Presidio Graduate School. Mr. Drum holds a BA in economics from Western Washington University and an MBA from Seattle University Albers School of Business. He is a Chartered Financial Analyst Charterholder and a Certified Financial Planner®.

Prior to joining Saturna Capital, Mr. Drum led environmental, social, and governance (ESG) research and was director of fixed income portfolio management since 2007 with a private account group at UBS Institutional Consulting Services specializing in investment management for global conservation and national wildlife park endowments as well as sustainable-social screened client portfolios. He is a former Chair of the United Nation's Principles for Investment (UN PRI) Fixed Income Outreach Subcommittee and a current member of the UN PRI's Bondholder Engagement Working Group (BEWG), an advisory committee working to elevate important ESG considerations and best practices among issuers and investors.

Mr. Drum's past experience also includes business valuation at Moss Adams and portfolio management at Washington Mutual Bank. Mr. Drum is a member of the board of trustees to the Museum of Glass in Tacoma and a member of Rotary.

Stephanie Ashton

Manager of Corporate Social Responsibility

Stephanie Ashton joined Saturna Capital in 2012. As Manager of Corporate Social Responsibility she develops Saturna's internal sustainability initiatives, manages sustainability reporting, and contributes to overall sustainability strategy.

Ms. Ashton graduated from Western Washington University in 2006, majoring in English (Creative Writing emphasis) and minoring in French. Her professional background includes eight years in legal support as well as non-profit experience. She is passionate about a number of sustainability issues—notably sustainable agriculture and local food—and currently serves on the Board of Directors for the Bellingham Food Bank.

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[1] ESG Clarity. https://us.allianzgi.com/en-us/ria/resources/esg-clarity/what-we-found

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[5] Clark, G.L., Feiner, A, and Viehs, M. "From the Stockholder to the Stakeholder: How Sustainability Can Drive Financial Outperformance," University of Oxford, March 5, 2015.

[6] Khan, M, Serafeim, G, and Yoon, A.S. Corporate Sustainability: First Evidence on Materiality, The Accounting Review, Vol. 91, No. 6, February 1, 2017. http://ratesustainability.org/wp-content/uploads/2015/04/Serafeim_etal_Corporate_Sustainability.pdf

[7] Alpha is a measure of risk-adjusted return relative to a benchmark return. Generally expressed as either positive or negative, alpha represents the difference between actual return and expected return based on the level of risk taken.

[8] CDP Disclosure Insight Action, About Us. https://www.cdp.net/en/info/about-us

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The Saturna Sustainable Funds limit the securities they purchase to those consistent with sustainable principles. This limits opportunities and may affect performance.

The Amana Funds limit the securities they purchase to those consistent with Islamic and sustainable principles. This limits opportunities and may affect performance.

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