

Investment Stewardship & Proxy Voting: Saturna Capital's Process



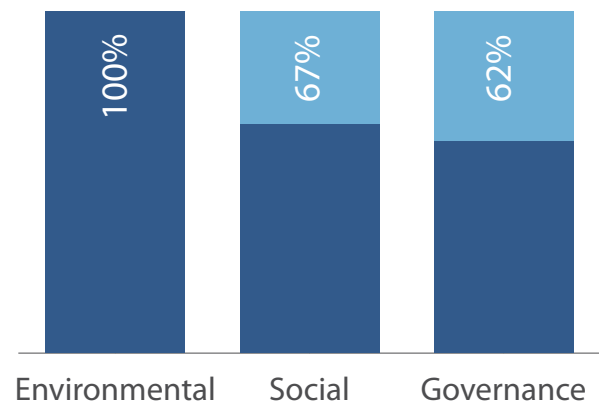
WHAT IS A PROXY?

When an investor owns stock in a company, they are granted voting rights to have a say in a variety of matters brought forward by company management or by other shareowners. When an investor owns shares in a mutual fund, however, the fund’s manager votes the underlying shares of securities held by the fund on behalf of the investor. The “proxy” refers to the assignment of voting rights to an individual who then votes on behalf of shareowners if they don’t attend the shareowners’ meeting in person.

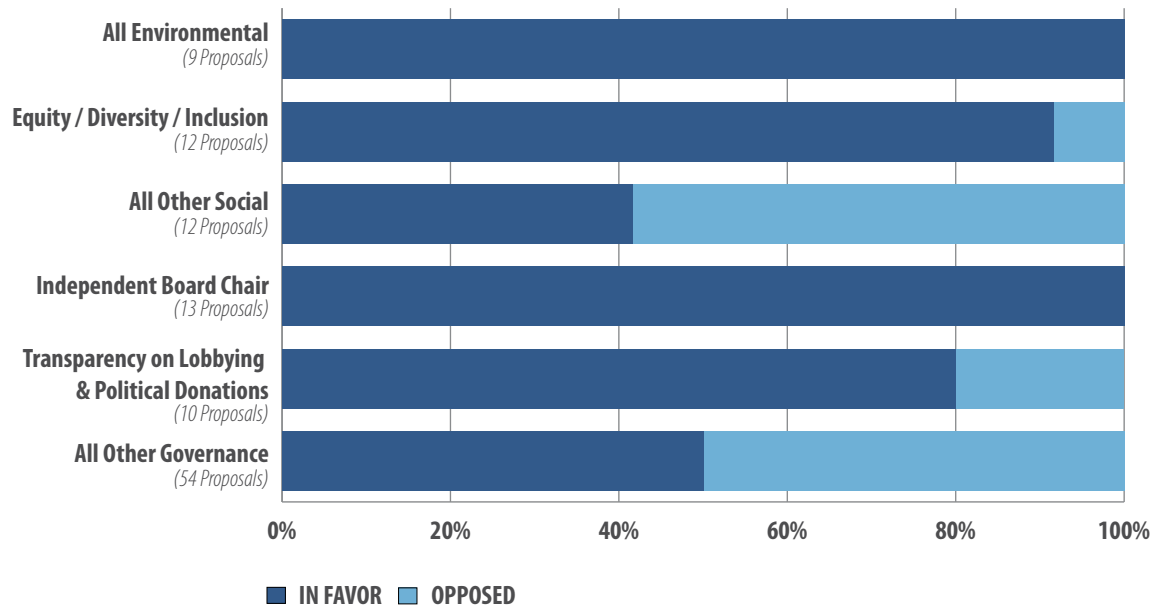
Many fund managers outsource their proxy voting duties to proxy advisory firms. These firms offer services including research materials on specific proxy issues, boilerplate guidelines for proxy voting, executing votes on behalf of their customers according to their customers’ guidelines, and executing votes on behalf of their customers according to the proxy advisor’s guidelines. Two leading firms are estimated to hold over 90% of market share in the US¹ and a 2018 study showed that among 175 asset managers in the US with over \$5 Trillion in assets under management (AUM), proxy votes aligned with recommendations of the largest of these two firms — ISS — 95% of the time.² Though outsourcing the proxy voting process to proxy advisory firms is ostensibly more efficient for a fund manager, it diminishes the value of active management and creates a lot of room for misalignment when it comes to environmental, social, and governance (ESG) issues.

Each year, Saturna’s analysts vote on a variety of environmental, social, and governance-themed shareowner proposals. These shareowner proposals can sound an alarm bell for investors on specific ESG risks that company management may not be proactively addressing. During the 2021 proxy voting year, Saturna voted on 9 unique environmental-themed shareowner proposals, 24 social-themed proposals, and 77 governance-themed proposals.

Percentage of votes in support of ESG shareowner proposals



SHAREOWNER PROPOSALS



SATURNA'S PROCESS

Saturna believes that proxy voting is a critical job for a fund's management team and that research analysts and portfolio managers should be exceedingly familiar with the implications of proposed corporate actions among the companies they cover, as well as the potential gaps in ESG-related policies. Indeed, we believe this expertise is one way active management can distinguish itself from other methods of investing. At Stanford, Copland et al. found that "among large institutional investors with AUM greater than \$100 Billion, portfolio managers are involved in only 10 percent of voting decisions [demonstrating] that the individuals within investment firms who have the most detailed knowledge of specific companies are not very involved with actual proxy voting decisions."³ The experience, careful analysis, and depth of knowledge our analysts bring to the investment selection and monitoring process is a critical component of responsible investment stewardship — and is a process that leaves no room for one-size-fits-all proxy voting.

Instead, Saturna has always viewed investing like a business partnership; we build portfolios with a view toward long-term investment and a bias against frequent turnover. These principles require us to seek issuers who have superior practices in the areas of corporate governance and employee welfare, and who demonstrably value the long-term sustainability of their business and the environments in which the business operates. Our principles also require that we maintain a close eye on management's decision-making and the company's unique ESG risks. While we tend to support and trust the management of the companies in which we choose to invest, we also fully know that each company has unique opportunities to do better and grow.

For these reasons, Saturna's longstanding approach to active management has always included voting proxies of fund portfolio securities in-house according to our own proxy voting guidelines, while holding thoughtful dialog among research analysts and portfolio managers when it comes to ESG-related shareowner proposals. The proxies of each underlying security held in a fund are voted by the research analyst covering the sector in which an issue falls, and the analyst is encouraged to bring any proxy proposal to the investment committee for discussion.

Vote tracking and analysis is another important part of this process, and Saturna's proxy voting duties include an annual review of our funds' voting records — in effect, an audit of how we've voted on different measures. This can sometimes look like supporting a specific type of management or shareowner proposal at one company, but voting against it at another. We know that our analysts understand the nuances unique to each company, and our proxy voting review provides a chance for our extended team to see those nuances in action.

Saturna's proxy voting guidelines outline our views on a variety of ESG issues and are available at www.saturna.com/about/proxy-voting

Footnotes

¹ Shu, Chong, *The Competitive Landscape of the Proxy Advice Market*, *The CLS Blue Sky Blog*, June 25, 2020. <https://clsbluesky.law.columbia.edu/2020/06/25/the-competitive-landscape-of-the-proxy-advice-market/>

² Doyle, Timothy M., *The Realities of Robo-Voting*, *American Council for Capital Formation*, November 2018. https://accfcorp.gov/wp-content/uploads/ACCF-RoboVoting-Report_11_8_FINAL.pdf

³ Copland, James R., Larcker, David F., Tayan, Brian, *The Big Thumb on the Scale: An Overview of The Proxy Advisory Industry*, *Stanford Closer Look Series Corporate Governance Research Initiative*, May 2018. <https://www.gsb.stanford.edu/faculty-research/publications/big-thumb-scale-overview-proxy-advisory-industry>

ESG DEBATES

While a fund whose vote record is 100% in favor of all ESG-themed shareowner proposals is not necessarily "more sustainable" than a fund with mixed votes, consistent votes against ESG proposals suggests that a fund is not considering ESG factors in their investment process. There are some issues on which Saturna's analysts uniformly agree, such as having an independent board chair and for requests for greater transparency around the environmental impacts of a business. But because we believe in looking at issues company by company, and within the unique environment of each business, our analysts' votes reflect nuance. In cases where our analysts' votes differ on a specific topic, we encourage discussion among the investment committee.

To that end, in late 2020, Saturna's investment team organized a series of more formal ESG debates on a range of topics presented as shareowner proposals during the 2020 proxy voting year. Covering 15 different ESG-themed proposals filed with 31 different issuers, Saturna's investment

analysts were paired up at random and assigned a topic, with priority placed on those topics where analysts had mixed votes. Each team was asked to prepare both an affirmative case (in favor of the shareowner resolution) and a negative case (against the shareowner resolution). The "for" and "against" sides were then chosen at random immediately before the debate began.

The exercise of having our analysts prepare arguments both for and against a topic was a critical component to the ESG debating process. Exploring these arguments demonstrates the value Saturna's team puts on thoughtful examination of an issue from all angles. The dissection of issues reveals their nuances, which should be the goal of any proxy voting process. It is this deeper thinking and closer looking, we believe, that is the value active management brings to investors.





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