SUSTAINABLE ALPHA:

Creative Construction and the Allocation of Capital

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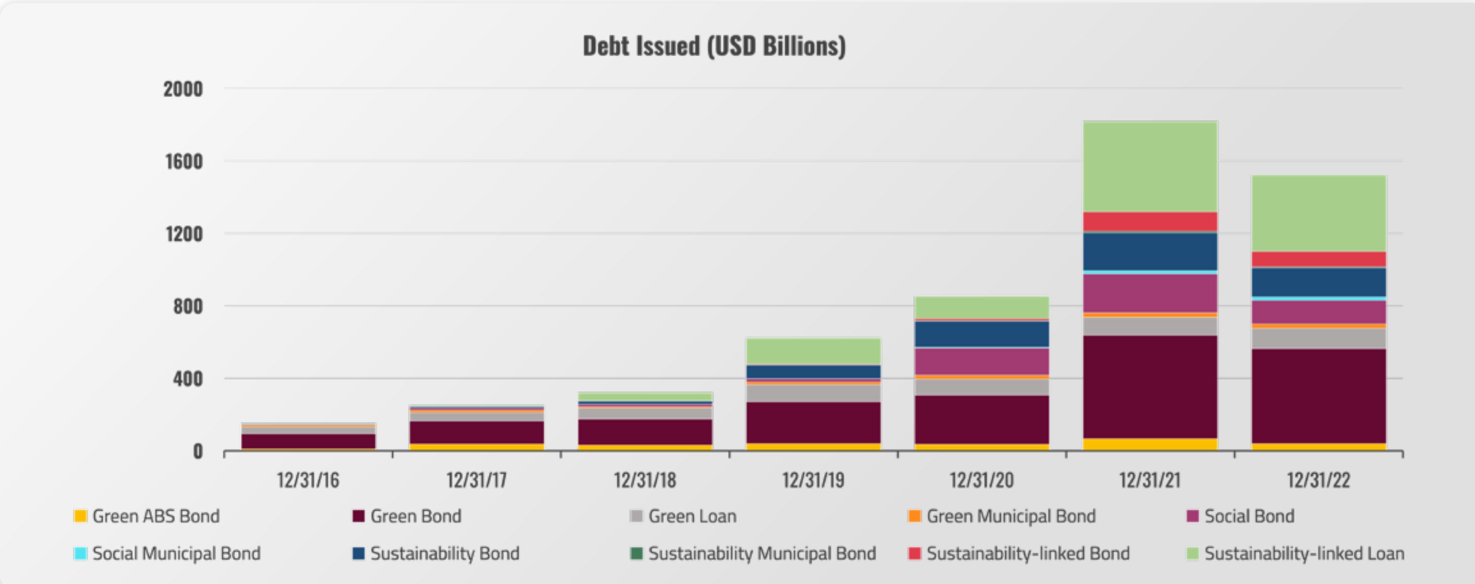
In 1987, the Brundtland Report articulated the first worldview on "**sustainability**." The guiding principles outlined in the report defined the term as "**development that meets the needs of the present without compromising the ability of future generations to meet their own needs.**" We believe this to be an economic statement, a lens through which we can look to interpret the world and take affirmative investment action as opposed to an ethics-based approach where specific industries or companies are excluded based on moral principles. In our view, by investing in attractively priced companies that demonstrate the implicit use of capital as purposefully in alignment with the Brundtland definition, Sustainable Alpha can be achieved.

Sustainability and Corporate Evaluation

It's safe to say the "**sustainability theme**" has become mainstream and is here to stay. According to the Governance & Accountability Institute, reporting around corporate sustainability practices is approaching 100%. From 2011 to 2021, the percentage of S&P 500 companies reporting on these criteria increased from 20% to 96%. In 2022, KPMG reported that the Top 100 Global Companies have continued to increase their sustainability reporting with 79% of companies reporting, up from 64% in 2011. Today, nearly all -- 96% -- of the world's top 250 companies report on sustainability.

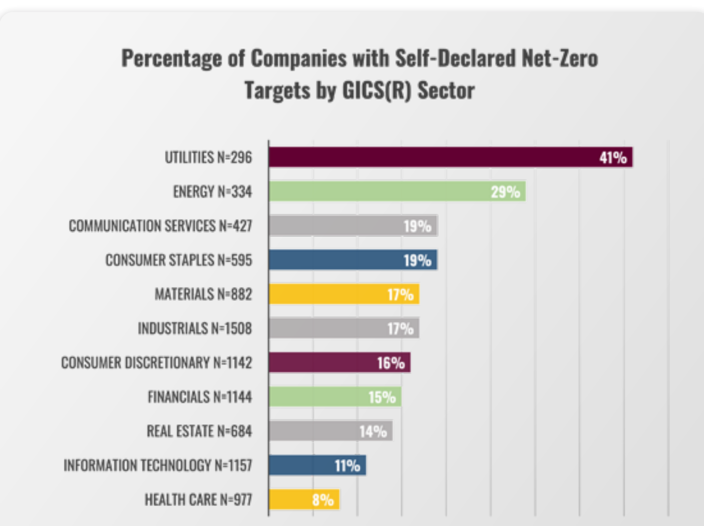
Evidence: Corporate Commitments to Sustainability

Corporations are not only talking about sustainability, they are also taking action, as evidenced by the increase in Sustainability Bond Issuances where the yields are predicated on specific sustainability outcomes and use of proceeds. Not only has the Sustainability-Linked Bond grown substantially, but the sheer volume of Green Loans has also expanded. Examples of these types of bonds and loans include funding for green buildings, electric vehicles, and renewable power.

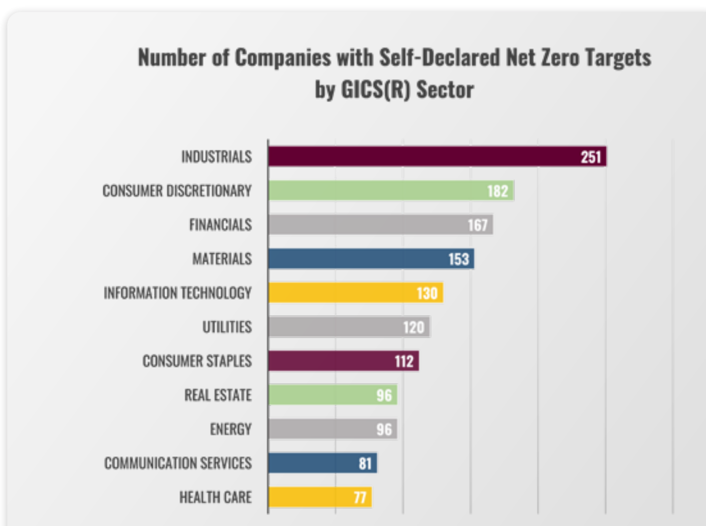


Source: Bloomberg Intelligence

Furthermore, according to the MSCI Net-Zero Tracker, a large number of companies in the MSCI ACWI IMI Index have committed to net-zero targets with the goal of reducing their overall greenhouse gas emissions. Net Zero is a term corporations are using to express their commitment to reducing the Greenhouse Gas Intensity of their business. The goals are to reduce emission to "Net" Zero by 2050, in order to achieve the global average temperature change (1.5 °C) target the end of the century. While these commitments in themselves are important, we are tracking "how" companies are going to achieve these goals, through watching their Capital Expenditures, monitoring their M&A activity and tracing their carbon offset initiatives, such as sourcing renewable power. What stands out here is not only the large number of companies in hard to abate sectors such as Industrials and Utilities that are on a Net Zero journey, but the commitments across all 11 Sectors of the GICS classification.



MSCI ESG Research, based on companies in the MSCI ACWI IMI Index, as of Aug. 31, 2022. Sectors from the Global Industry Classification Standard (GICS®)



MSCI ESG Research, based on companies in the MSCI ACWI IMI Index, as of Aug. 31, 2022.

How Sustainability Informs Our Investment Approach

Our set of Sustainable Investing Principles are guided by what we call our **PRIME Criteria**. We seek out companies that align with, or fulfill, one or more of the requirements of the following precepts:

- **P**rinciples: Encourage and improve human well-being and personal freedom
- **R**esearch: R&D of new technologies that provide for more efficient resource utilization
- **I**mpact: Help scale the above advantages to a broader range of beneficiaries
- **M**itigation: Reduce environmental risks and halt or reverse the effects of climate change
- **E**volution: Increase economic efficiencies and limit the effects of systematic economic risks

Shelton Sustainable Equity Investment Process

Our investment process begins with an examination of the investable universe. Very importantly, we believe pure sustainable alpha is based on a well-defined beta from a benchmark index rather than from a sustainable beta or from a norms-based framework on what is "good."

After identifying the investable universe, we implement a macro-ecological/economic framework that traces and isolates opportunities stemming from changes in ***Natural Capital*** assets and that meet the Brundtlandt standard of Sustainability. We start by identifying a trend, then unpacking it and building a roadmap of the economic impacts and ultimately the attached financial assets. A good example would be ocean acidification, a breakdown in coral reefs' ability to thrive resulting in a decline in fishery recovery rates. The knock-on consequences from this degradation is almost certain to affect local and regional economies. Natural resource status data can be used to develop alert systems that forecast changes in natural capital asset levels.

Natural Capital is the basis for our economy

- Natural Capital, or the goods and services that come from a well-structured and well-functioning ecological system, is fundamental to our economy.
- Natural Capital Indicators, such as water quality and quantity, soil health, air quality, etc., are essential for the long-term provision of benefits on which society relies.
- Social and economic systems built upon the natural capital economy operate and function in a manner that aspire to be governed by rule of law and is equitable to all.
- Financial assets reflect the agency of an organization's response to pressures on natural capital.
- Markets respond to fluctuations in supply and demand of natural capital and is often reflected in financial markets if you are looking for it.

Once we understand the macro-trends, we can evaluate sectors with attractive attributes and a low correlation to overall market beta. For our purposes, these sectors must align with broader economic and policy trends and have somewhat predictable volatility profiles. This approach allows us to build a diversified portfolio across all sectors, but highlighting where firms are involved in sustainability themes such as cleantech, renewable energy, agriculture, water, health care, and cybersecurity.

We further enhance our analysis by using data that is supplemental to financial statements to understand the context in which companies are performing. Environmental, social and governance (ESG) data, as well as other alternative data, adds to this additional context by providing information about a company's supply chain as well as other stakeholder issues it may be facing. **ESG data sorting by itself does not identify a sustainable investment**. These are starting points to do further research on how companies operate within their context.

All of this analysis leads us to a list of companies that demonstrate the implicit use of capital as purposefully in alignment with the Brundtland definition of Sustainability.

These trends highlight that the course of economic development towards a green economy is exhibiting ***Creative Construction*** (amending Schumpeter's Creative Destruction[1]) , where industrial transformation ceaselessly improves but without destroying incumbent industries or wealth. ***Creative Construction*** is additive building ***additional*** industries and growing wealth. For example, companies that acquire or develop technologies that enhance their efficiency without eliminating the previous products.

Sustainable Alpha

While the purpose of an investment is to achieve financial goals, the corporate strategy behind the investment must be built upon the effective allocation of capital into the economy that seeks to further sustainable development. Sustainable Alpha, then, is where investors are allocating capital for creative construction and can earn relatively attractive returns generated by those allocations.

Economies are dynamically changing and will continue to create new industries that are providing for the advancement of the human experience. Sustainability is a world view that captures those companies and industries that are at the intersection of efficient natural resource use efficiency, social equity, and economic development. Sustainable Alpha is generated by understanding those trends and channeling capital in that direction.

We believe sustainable development is paramount to humanity's stability, and Sustainable Alpha generated by ***Creative Construction*** is key to meeting those needs.

1 Joseph Schumpeter, particularly in his book Capitalism, Socialism and Democracy, first published in 1942.

Important Information

Investors should consider a fund's investment objectives, risks, charges and expenses carefully before investing. The prospectus contains this and other information about the fund. To obtain a prospectus, visit www.sheltoncap.com or call (800) 955-9988. A prospectus should be read carefully before investing.

Fund information is not intended to represent future portfolio composition. Portfolio holdings are subject to change and should not be considered a recommendation to buy individual securities.

The Fund's environmental focus may limit investment options available to the Fund and may result in lower returns than returns of funds not subject to such investment considerations. There are no assurances that the Fund will achieve its objective and or strategy. Investing in securities of small and medium sized companies, even indirectly, may involve greater volatility than investment in larger and more established companies.

The Shelton Sustainable Equity Fund is distributed by RFS Partners, a member of FINRA and affiliate of Shelton Capital Management.

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