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SUSTAINABILITY: THE WALDEN INVESTMENT PERSPECTIVE

he word *sustainability* seems to have eclipsed most other investment buzzwords in use and popularity recently. Scores of companies, from American International Group to State Street

Corporation, have devoted countless glossy pages to trumpeting their commitment to sustainability, but what does sustainability mean, really? If you are an aficionado of words and usage, you will scorn the verb turned noun and expect that no selfrespecting dictionary will acknowledge its existence. Walden may even harbor a few such purists. As to sustainability as a concept, however, the search for companies with attraccharacteristics encompassing financial, environmental, social,

and governance dimensions (the latter three often grouped as the acronym ESG) has been a core pursuit of ours for over three decades.

Some people define ethical behavior, environmental stewardship, and social responsibility as distinct and separate criteria which, together with economic viability, may combine to achieve the coveted *sustainability* label. Are these concepts truly so separable? As a long-term investor, Walden has always been skeptical that economic viability can be

achieved and preserved in the absence of such factors as ethical behavior, environmental stewardship, and social responsibility. The risks and negative consequences of unethical behavior, environmental abuse, or socially

undesirable business practices have a cost we constantly integrate into our analysis of value. Conversely, attention to ESG factors places forward-looking companies in a better position to capitalize on business opportunities.

At Walden, the search for high-quality, reasonably-priced companies that possess a sustainable business model is a fundamental duty for analysts and portfolio managers alike. The focus on sustainable business models marries Walden's "conventional" investment analysis with our ESG research

and advocacy focus. Our analytical process provides the tools and the long-term focus required to identify companies whose business (i.e., products and services) and business practices combine to offer the sustainable advantage we seek.

Walden has focused on sustainable advantage and sustainable development for more than 30 years. In a 1994 issue of *Values* we noted the link between economic justice and sustainable development. "Socially



About Walden Asset Management

Walden Asset Management is the socially responsive investment division of Boston Trust & Investment Management Company. Walden began offering socially responsive investment services in 1975. We are among the largest and most experienced investment managers specializing in services for individual and institutional investors with social concerns

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TARGETED SUDAN DIVESTMENT

espite our repeated assertions of "never again," we have witnessed recurring waves of genocide over the past century. From Armenia to Germany, from Cambodia to Bosnia and Rwanda, the international community has stood passively by or made token ineffectual gestures in response to each new instance of crimes against humanity. Today, the world is witnessing genocide in Darfur, Sudan.

Since violence first broke out in 2003, the Sudanese government's genocidal policies, including systematic rape and torture, have led to the deaths of more than 400,000 innocent Darfurians and the displacement of over two million people. Four years genocide, Darfur's the Sudanese government in Khartoum has adopted a new strategy of destruction, disguising Sudanese military planes as United Nations planes before bombing unsuspecting Darfurian villages.

While all instances of genocide are alike in imparting unimaginable human suffering, something sets Darfur apart. For the first time in his-

tory, the United States government has declared "genocide" while the atrocities are still occurring. This time, we don't have to wait ten years for a Hollywood movie or a textbook to awaken our conscience. We already know what is happening in Darfur, and we can intervene today.

While the Khartoum government has proven essentially impervious to diplomatic pressure, it has demonstrated a historical responsiveness to economic pressure, largely a result of its dependence on foreign direct invest-

Viewing Khartoum's wallet as a significant pressure point, a global campaign designed to place economic pressure on the genocidal regime has emerged and flourished. The Sudan Divestment Task Force, spearheading this cam-

paign, has developed a unique approach to shareholder engagement and divestment, focusing its efforts on the most egregiously offending companies in Sudan. This approach, termed targeted divestment, seeks to maximize impact on the Sudanese government, while minimizing potential harm to both innocent Sudanese civilians and investment returns.

The concept is simple, and it's catching on

quickly. The first phase involves identification of com-

panies that have a business relationship with the government or a government-created project, deliver minimal benefit to the country's underprivileged, and have expressed no significant corporate governance policy regarding the genocide. The second phase involves engagement of these companies, encouraging them to dramatically alter their behavior in Sudan, to exert pressure on the government, or to curtail operations in the country until the Darfur conflict is resolved. In the final phase, shareholders divest from companies that prove insufficiently responsive within a specified time frame.

Since Harvard University sold shares of PetroChina (whose parent company, China National Petroleum Corporation, is the largest player in Sudan's oil industry) in 2005, 17 states have adopted policies of divestment from Sudan, and eleven of these states have adopted the targeted divestment model. Over 52 universities have adopted policies related to their Sudan-linked investments, and dozens of socially responsible investing (SRI) firms have provided support for the movement by committing to divest from Sudan, supporting shareholder engagement initiatives, and offering research and advocacy assis-

While the general paradigm of shareholder activism favors continued engagement over divestment, the situation in Sudan is unique,



Actor Don Cheadle at a press conference shortly before California adopted a targeted divestment policy in September 2006.

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RUGMARK

partnerships at work

This column highlights selected groups and organizations working to promote social and economic justice, environmental leadership, or corporate accountability. Walden frequently partners with featured groups in research and advocacy initiatives.

hile you are reading this, over 300,000 children in South Asia are being exploited and forced to work illegally in the handmade rug industry. Some are bonded laborers living as virtual slaves, others are employed/working for a pittance in dangerous factories. All are being exploited and forced to work in violation of their own countries' laws. And the carpets they weave end up in American homes.

RugMark International is working to stop child labor/exploitation in India, Nepal, and Pakistan through loom and factory monitoring, consumer labeling, and rescuing, rehabilitating, and educating former child weavers.

In North America and Europe, Rugmark recruits importers and retailers to sell certified child-labor-free rugs, requiring these businesses to open the



A RugMark inspector in Nepal ensures that hand-made carpets are child labor free.

doors of their overseas production sites to random, surprise inspections. By adhering to RugMark's strict no child labor guidelines, manufacturers receive the right to use the RugMark® certification on the back of a rug, offering the best possible assurance that no child labor was employed. The individually numbered label also verifies that a portion of the purchase price helps educate children.

Rugmark is already a successful model: In just over a decade and with one percent of the total market of handmade rugs it has reduced the number of child weavers by two-thirds. To reach the remaining "carpet kids," RugMark USA recently launched a national consumer awareness campaign, *The Most Beautiful Rug.* It educates people to make humanitarian purchasing choices, sending a message up the supply chain—from consumer to retailer to manufacturer—that child labor won't be tolerated. The core campaign message is that a rug made by child labor is ugly no matter what it looks like, and that the RugMark® ensures a rug's inner beauty.

RugMark is encouraging major U.S. retailers, such as Macy's and Bloomingdale's, to sell certified rugs. If the biggest retailers commit to selling child-labor-free carpets, RugMark could quickly meet its goal of 15 percent market share, the projected tipping point to end child labor on an industry-wide basis.

–N. Smith

Nina Smith is Executive Director of RugMark USA. To learn more about Rugmark or The Most Beautiful Rug Campaign, visit www.RugMark.org.





TARGETED SUDAN DIVESTMENT continued from page 2

and targeted divestment represents a unique approach. Extended engagement through traditional mechanisms such as proxy voting and coalition building often takes years—a timeframe wholly unsuited to the urgency of ongoing genocide. Many companies operating in Sudan have already been engaged for years by numerous shareholders, and while some have altered their behavior, others have explicitly expressed their unwillingness to do so. While the targeted divestment model still calls for engagement, it calls for that engagement to be expedited and

followed by the "stick" of divestment should company behavior fail to change. This targeted approach has already succeeded in changing the behavior of several major firms operating in Sudan—Rolls Royce and CHC Helicopter are the latest in a series of large companies that have left Sudan in response to shareholder pressure and the specter of divestment.

As the targeted divestment movement continues to pick up momentum, investors and companies alike are beginning to realize that genocide is a bad investment. And as the movement

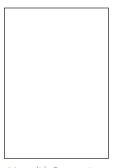
expands internationally, with active campaigns in seven countries outside of the United States, the Khartoum government may soon come to the same conclusion.

-A. Sterling and N. McMurry

Adam Sterling is the director of the Sudan Divestment Task Force and Nina McMurry is the organization's lead analyst. The Sudan Divestment Task Force is a project of the Genocide Intervention Network. For more information, visit www.sudandivestment.org.



SOCIAL RESEARCH AND ADVOCACY IN ACTION



Meredith Benton is Associate Director of Social Research.

United we stand...

his spring, Walden worked with our colleagues, sometimes in the chorus and sometimes as the conductor, to raise awareness of key public policy issues.

Along with several Boston-based investment firms, Walden wrote in support of a Massachusetts Sudan divestment bill, S. 1474. The bill proposes a targeted divestment strategy that prohibits investment in about two dozen companies of strategic significance to the government of Sudan. Massachusetts would join a growing list of states, municipalities, and academic institutions divesting to help end the government sponsored genocide and displacement of innocent civilians in Sudan.

At the end of April, the Employment Non-Discrimination Act (ENDA) was introduced in the House of Representatives as H.R. 2015 by Congressman Barney Frank (D-Mass.). ENDA calls for national measures to protect lesbian, gay, bisexual, and transgender persons from job discrimination. Walden has been working to build corporate support of ENDA, coordinating a letter that was co-signed by 20 investors and, with the help of other investors, sent to more than 400 companies. These letters asked that companies publicly endorse the Act.

Walden also expressed support for H.R. 1257, legislation proposed by Congressmen Frank, which requires an annual shareholder advisory vote on executive compensation reports. The legislation complements Walden's efforts with a working group of institutional investors and companies, led jointly with Pfizer and the American Federation of State, County and Municipal Employees (AFSCME) union, to study how best to implement the advisory vote. Working group participants have agreed that the nonbinding shareholder vote has merit as a mechanism for investors to weigh in on executive compensation policies and practices.

Walden has joined with more than 50 institutional investors representing \$4 trillion in assets and a dozen major companies calling on U.S. legislators to enact strong policies to address climate change. Voices as disparate as Merrill Lynch, CalPERS, and DuPont appealed to the U.S. government to set aggressive greenhouse gas emissions reduction targets; to increase support for

research and development of clean technologies; and to have the U.S. Securities and Exchange Commission illuminate how companies should disclose climate risk in their public documents.

Walden continues to support another investor initiative on climate change—the Carbon Disclosure Project (CDP). The CDP, which provides a coordinating secretariat for a group of 280 institutional investors, has sent an annual questionnaire focused on climate change to the largest companies in the world since 2002. This questionnaire, of which Walden is a signatory, asks for the disclosure of investment-relevant information concerning climate change. Walden, as in years past, has written to portfolio companies strongly encouraging them to respond to the questionnaire.

Walden, as part of Boston Trust & Investment Management Company, has become a signatory to the Principles for Responsible Investment (PRI), an initiative of UNEP Finance Initiative and the UN Global Compact. While the voluntary and aspirational PRI reflects a commitment Walden has long held, we have been delighted to see 183 signatories representing more than \$8 trillion joining this group. The PRI ask signatories to integrate environmental, social, and governance (ESG) issues into investment analysis and decision-making processes, actively seek disclosure from companies around ESG issues, and report on progress made in implementing and promoting the Principles.

Walden's Environmental Footprint

Last year, Walden/Boston Trust began offsetting our own greenhouse gas emissions through Carbonfund.org, an organization supporting renewable energy, energy efficiency, and reforestation. This year, we are further lightening our step through participation in the U.S. Environmental Protection Agency's Acid Rain Program. We successfully bid for a sulfur dioxide (SO₂) allowance. Walden, by purchasing and retiring this allowance, has decreased the allowable U.S. emissions of SO₂. We are pleased to participate in this market-based solution that provides a model for tackling other environmental challenges. •

-M. Benton

SUMMARY OF WALDEN'S 2007 SHAREHOLDER RESOLUTIONS

Sponsoring shareholder resolutions is one of several options available to investors seeking a voice in company practices. Much of Walden's success in advocating for greater corporate social responsibility comes from constructive dialogues with companies over many years, entirely outside the resolution process. Nonetheless, shareholder resolutions can be an important tool for change, as illustrated in this summary of our 2007 shareholder resolutions.

HUMAN RIGHTS

Vendor Standards

Resolutions at **Applied Materials**, **Hershey's**, and **Wrigley's** requested that the companies adopt vendor codes of conduct, establish an independent monitoring process, and report publicly on progress. Walden withdrew the resolution at Wrigley's based on its commitment to establish a code and an audit process. The resolution at Hershey's was withdrawn as it committed to establish a supplier code of conduct, develop a monitoring and implementation plan, and continuously improve its program over time. Applied Materials agreed to expand its auditing and published reporting.

EQUALITY

Inclusive Non-Discrimination Policies

Walden filed a number of resolutions requesting that companies modify their non-discrimination policies to explicitly include sexual orientation. Resolutions were withdrawn when: **Clarcor** confirmed that its policies were inclusive and added explicit language on its website; **CenturyTel** internally formalized its inclusive policy, posted its policy publicly and shared information on internal diversity training programs; and **Precision Castparts*** modified its policy to include sexual orientation, posted its policy online, and communicated the changed policy to its subsidiaries. 43% of shareholders demonstrated their support of the proposal at **Commercial Metals**, 26% at **Leggett & Platt** and 43% did so at **Expeditors International***.

Equal Employment Opportunity (EEO) Disclosure and Board Diversity

A resolution at **Lehman Brothers** requesting public disclosure of equal employment opportunity statistics was withdrawn when it shared its diversity programs and provided comprehensive workforce composition statistics. This resolution was supported by 26% of shareholders at **Home Depot**. A resolution requesting increased board diversity at **Linear Technology*** has not yet gone to vote.

ENVIRONMENTAL IMPACT

Climate Change

Walden filed a resolution asking industry outlier **ExxonMobil*** to adopt quantitative goals, based on current technologies, for reducing total greenhouse gas emissions from the company's products and operations and to report to shareholders on plans to achieve these goals. 31% of shareholders supported this resolution.

Recycling

Resolutions were withdrawn at **Coca-Cola** and **PepsiCo** requesting reports on beverage container recycling programs and goals. PepsiCo agreed to encourage publication of an industry document on recycling and to continue working to establish industry-wide container recycling goals. If PepsiCo is not able to mobilize industry support, it will supplement its own sustainability report to stakeholders. Coca Cola agreed to boost recycling and to increase disclosure of its recycling activities, including source reduction, use of recycled content, and container recovery.

CORPORATE GOVERNANCE

Political Contributions

Walden withdrew a resolution at **3M** when it committed to enhance its transparency on policies and practices related to political contributions. Both **BellSouth*** and **Caremark** were acquired, making similar resolutions at these companies moot. A resolution requesting increased reporting from **FedEx** has not yet come to vote.

Executive Compensation

Walden filed resolutions requesting that shareholders be able to cast an advisory vote to ratify the compensation of executive officers. Walden withdrew the resolution after **Pfizer** agreed that the suggested reform had merit and to study the details of its implementation. Pfizer agreed to help convene a working group with companies, investors, and experts to consider methods to implement an advisory vote system in the U.S. The resolution at **Procter & Gamble** was withdrawn with its commitment to participate in the working group and to study how to improve communications with investors on executive compensation. 35% of shareholders supported this resolution at **Wells Fargo**.

SUSTAINABILITY REPORTING

Resolutions were filed at **Comerica**, **Dover** and **Medtronic** requesting that the companies prepare sustainability reports, detailing their social and environmental impacts policies, and programs. Shareholders supported the resolution's request with 39% votes at Comerica and 35% at Dover. Walden withdrew the resolution at Medtronic, given the company's commitment to develop a sustainability report, work constructively with shareholders, and continuously improve its reporting.

*In filing shareholder resolution Walden often collaborates with other concerned investors to strengthen our influence on managements. Of the 25 resolutions described above, 5 were not led or co-led by Walden. In order of appearance, these resolutions were led by: Pride Foundation, Trillium Asset Management, Calvert, Sisters of St. Dominic of Caldwell, NJ, and Domini Social Investments.

SUSTAINABILITY: THE WALDEN INVESTMENT PERSPECTIVE

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responsive investors are intensely concerned with the . . . issues of sustainable development: creating and maintaining good jobs and wholesome communities, making our social system more durable by adding to the fairness and justice of its outcomes, sustaining the natural environment on which all life and development depends, and increasing the time horizon

for considering the consequences of economic decisions." We continue to believe companies that demonstrate the integration of these sustainability concepts to have a business advantage.

What tools do we use in our search for companies with a sustainable advantage? Our financial analysis focuses on current and long-term profitability; leverage; consistency of sales, earnings, and cash flows over time; and the quality

of earnings. Financial engineering, as evidenced by aggressive pension assumptions, significant gain on sale accounting, frequent charges or write-offs, or a significant increase in debt (among other things) are clearly not sustainable, meaningful sources of earnings growth and increases in cash flows. Similarly, companies operating in an increasingly competitive environment with low barriers to entry will find any advantage difficult to

sustain. Can this view of sustainability exist independent of and distinct from our ESG analysis? We don't believe so.

The diagram below, Walden's Sustainable Investment Process, highlights the integration of Walden's research and analysis on financial and ESG topics. To find suitable long-term investments for the portfolio, Walden analysts consider these fundamental aspects of a company's performance and profile. The first two aspects, Profit Growth and ESG Analysis overlap meaningfully as we con-

sider sustainable advantage. The third critical input, Valuation, represents our quantitative and qualitative long-term value model used to determine an attractive price.

While others often regulate ESG analysis to the dusty corners of securities research, Walden prioritizes these topics in the belief that they are intimately linked to long term value. Key among them are transparency and disclosure to the public and shareholders.

Strong corporate practices regarding transparency and disclosure are fundamental and critical to financial analysis as well. How can we be confident in the quality of a company's earnings in the absence of clear, consistent disclosures regarding both qualitative and quantitative aspects of the company, its operating environment, and business practices?

Walden has long worked to understand the links between financial and

ESG topics as the following excerpts from past *Values* demonstrate.

Can companies with boards and senior management teams bereft of women and minorities operate a sustainable business model? As we noted in a 2006 issue of *Values*.

The negative ramifications of persistent inequalities in

Walden's Definition

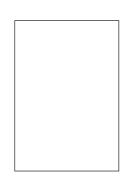
A sustainable system is able to continue in perpetuity. In any context—ecological, economic, or societal—sustainability requires balancing the needs of the present with the needs of the future.

For Walden, sustainable investing means focusing on businesses with the potential to operate successfully over the long term. It is an investment discipline that requires more than identifying companies with strong, long-term financial prospects. Walden considers environmental, social, and governance matters to be integral to investment decision-making and enduring shareholder value. As such, Walden seeks companies committed to nurturing the human and natural resources essential to ongoing business success. To maximize the sustainability of its investments, Walden actively encourages continuous improvement in business practices.

the workplace pose risks not only to society, but also to long-term business success. . . . Customers are becoming increasingly diverse. A representative workforce is apt to anticipate and respond effectively to evolving consumer demand. . . . Conversely, allegations of discrimination in the workplace have created a significant burden for shareholders due to the high cost of litigation and potential loss of government contracts.

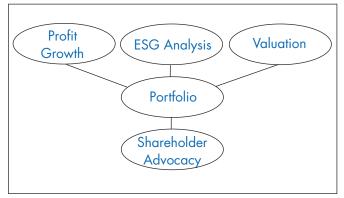
In a 2003 edition of *Values* we highlighted the issue of climate change and the Carbon Disclosure Project, and noted,

Climate change creates unpredictable, extreme weather, greatly impacting water resources, agriculture, and habitats, and creating flooding, drought, and desertification. . . . As with so many environmental problems, the impacts may be disproportionately felt by



Lucia Santini is a Senior Portfolio Manager.

Walden's Sustainable Investment Process

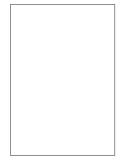


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CHOOSING AN IRA BENEFICIARY: NOT YOUR ESTATE

fter years of personal retirement savings or the accumulation of funds in your company's retirement plan, your IRA may be your largest financial asset. If you fail to elect beneficiaries of your IRA, the default beneficiary will probably be your estate. Besides missing out on the opportunity to specifically list who inherits the funds, there are other significant drawbacks to having your estate as the beneficiary.

When your estate is the beneficiary, the IRA becomes subject to the probate process and the related legal complications, and the funds may be subject to any creditors of your estate. You also lose the ability to stretch out the distributions of the IRA, which provides for continued tax deferred growth. In contrast, when your spouse is the beneficiary, he or she can treat the inherited IRA as their own and wait until reaching age 70 ½ to begin the required, but gradual, distributions. Individual non-spouse beneficiaries and qualifying trusts are required to begin taking



Stephen Benevento is an Administrative Officer

minimum distributions by the end of the year following the IRA holder's death, regardless of the beneficiary's age. But these distributions are based on the beneficiary's own life expectancy, thereby often greatly extending the life of the IRA. Since an estate has no life expectancy, the payout occurs quickly, eliminating any chance of further income tax deferral.

Be sure to elect both a primary and contingent beneficiary to ensure that your estate will not be elected by default. The institution holding your IRA will keep a record of your elections, but keep your own copy in a safe place and let the appropriate people know where it is. •

-S. Benevento, CFP®

As always, we strongly recommend consulting with your tax or estate professional prior to making any decisions regarding your estate or planning goals.



SUSTAINABILITY: THE WALDEN INVESTMENT PERSPECTIVE

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the poor, who have limited resources to adapt.

Clearly, the link between a company's operating environment and stable, uninterrupted business processes cannot be overlooked. In addition, we noted the economic justice and resource issues inherent in global warming. To long-term investors, these must be critical considerations in the assessment of value.

Staples, a holding in many client portfolios, provides a case in point. The office supply superstore combines an attractive financial profile of superior sales and earnings growth, stable financial position, and strong earnings quality with an industry-leading environmental profile and strong employee benefits. Staples pledged to increase the average post-consumer recycled content in its paper products to 30 percent, and to source 10 percent of its energy from renewable sources. Its benefits package is attractive and it has developed "Staples University" to provide employees with additional skills and training. In recent years Staples has increased its disclosure and transparency markedly.

Shareholder Advocacy is the final component featured in

Walden's Sustainable Investment Process diagram. A core focus of our work as sustainable investors is to encourage greater corporate disclosure on key social, environmental, and governance issues. In addition, when we are able to make a clear business case for modifying company policies or practices, we will advocate for these changes. As examples, we have encouraged companies to decrease their greenhouse gas emissions, make their non-discrimination policies more inclusive, and increase the diversity of and opportunities for their employees. We have done so believing that these changes increase the sustainability of a company's business model.

For Walden, the commitment to the sustainable business model, sustainable development, and sustainable advantage—to wit: sustainability (the non-word)—is longstanding and is evidenced by our relationahip with the companies held in client portfolios. Long-term value is created by the development of superior products and services which have incorporated financial, social, environmental, governance, and strategic policies and practices. This commitment and approach has been at the core of our work for decades. •

-L. Santini



LIFEWAY FOODS

cutting edge companies

This column highlights companies in the business of providing solutions to social and environmental challenges. Featured companies are typically held in the SmallCap Innovations portfolios offered to Walden clients.

Got Kefir?

efir is a cultured, enzyme-rich food filled with "good" microorganisms that promote digestive health. Like yogurt, kefir is a cultured milk product. The types of active yeast and bacteria found in kefir provide more nutritive value than those found in yogurt due to their ability to colonize the intestinal tract. The relationship between "good" bacteria and "bad" bacteria in your gut is an important contributor to overall health. Probiotic foods like kefir contain the good bacteria that enable the body to resist intestinal parasites and pathogens such as E. coli. Kefir has additional benefits as well. The curd size of kefir is smaller than yogurt and easier to digest, which makes it a particularly nutritious food for babies and the elderly. Kefir has also reportedly been shown to boost the immune system. And, in the humble opinion of this writer,

kefir is delicious! Lifeway Foods, Inc., a 19 year old public company in stores, major supermarkets like Whole Foods and Ralph's, and discount stores like Costco and Target. The Organic Trade Association reports that dairy foods are the second largest segment of the \$14 billion organic foods industry. Lifeway makes organic kefir under both the Lifeway and Helios Nutrition brand names. Lifeway operates its own organic dairy thus assuring a steady supply of organic milk. Control of the supply chain is a competitive advantage; Lifeway is the number one organic kefir manu-

facturer in the United States.

dairy) soy based kefir, low-carb kefir and Greek-style kefir.

Lifeway's latest product to hit the market, ProbugsTM, is an

organic whole milk kefir product targeted for children. The

drinks include creative flavors like Orange Creamy Crawler and Sublime Slime Lime. Lifeway sells its products in health food

> The demand for kefir is not limited to the organic market. The functional and probiotic (meaning live cultures consumed for a health benefit) food market is growing over 20 percent per year. MarketResearch.com believes the functional food

segment will approach \$30 billion in revenues by 2010, thus catapulting the functional food market from 4 percent to 6 percent of the total U.S. food market. Cultured beverages like kefir are currently more popular internationally, but U.S. consumers are enjoying kefir in greater numbers as they become aware of its health benefits. Lifeway stands to benefit from this trend. •



Morton Grove, Ill., is the largest supplier of kefir in the United States and reports that it offers the largest selection of kefir in the world. Its kefir product line includes organic kefir, (non-

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