Morningstar® Managed Portfolios℠

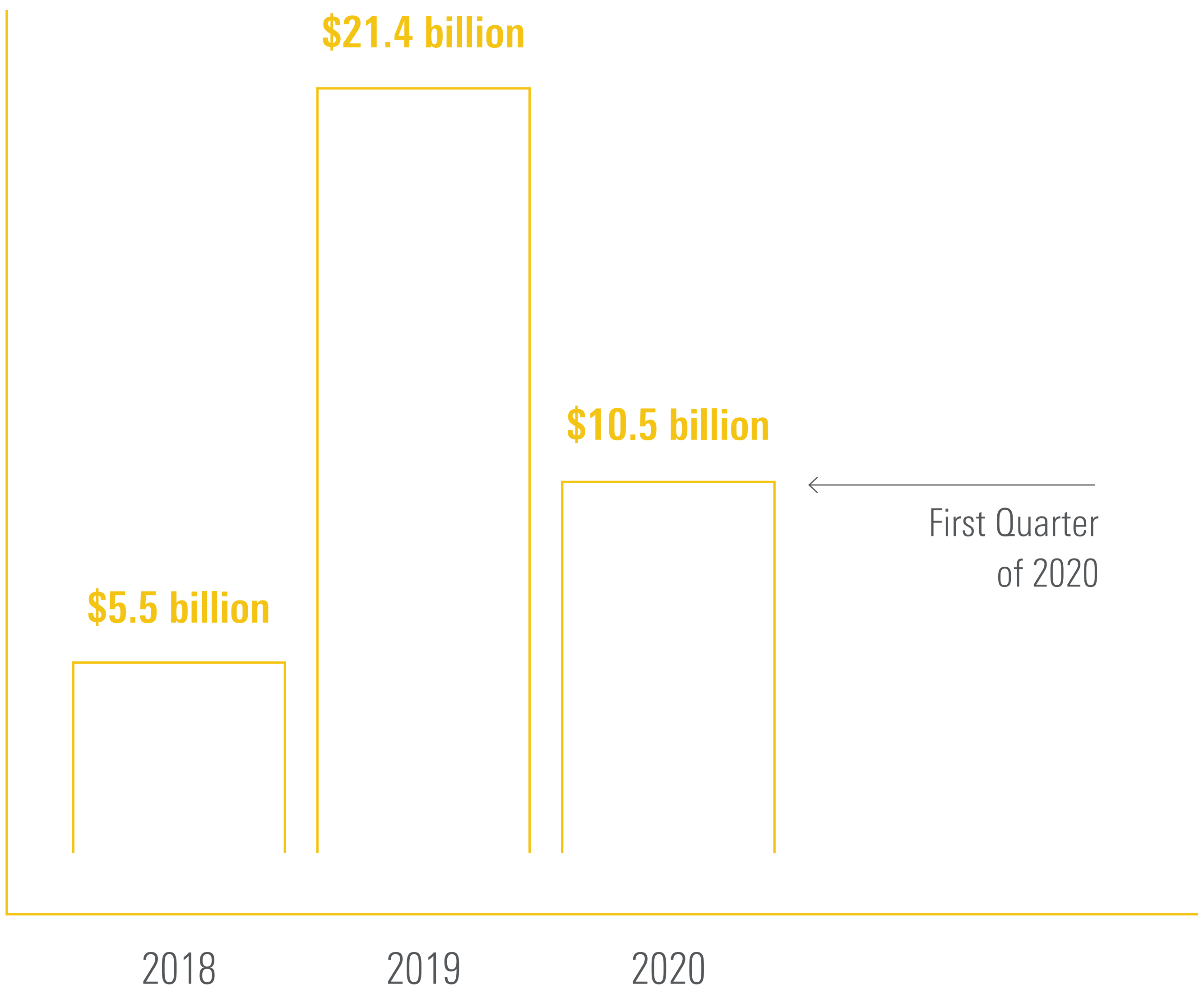
Help grow your business with ESG

A 4-step guide to offering ESG investments to your clients.

Total sustainable investments with a focus on environmental, social or governance (ESG) factors are estimated at $30 trillion[1] — 1 of every 3 investment dollars.

The Opportunity for Sustainable Investing

Financial markets suffered through a severe downturn in the first half of 2020, but even during the early pandemic-related turbulence, data shows how ESG-focused portfolios continued to attract investors. Morningstar, Inc. fund flow data shows sustainable investments recording net inflows of $5.5 billion in 2018, $21.4 billion in 2019, and a record $10.5 billion in just the first quarter of 2020.[2]

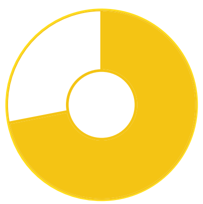


Source: For illustrative purposes only.

1 Global Sustainable Investment Review 2018, Global Sustainable Investment Alliance, gsi-alliance.org.
2 Morningstar Direct, as of March 31, 2020.

Who's Interested in ESG?

Recent research dispels the idea that ESG-focused investing is only of interest to younger generations. This interest is actually very consistent across all age groups. Morningstar, Inc. research supports this study, with 72% of respondents (of various ages and genders) expressing interest in sustainable investing.[3]



72% of people express interest in sustainable investing.

Breakdown by age[4]

% of investors who considered ESG factors before investing:

77% of millennials (ages 19 to 35)

64% of Gen Xers (36 to 55)

61% of baby boomers (56 to 73)

Talk About ESG Investing With Your Clients

Research shows your clients have interest in sustainable investing, and most advisors have yet to develop a strategy to offer and review these options with clients. Advisors who have this conversation will likely discover it helps grow their practice by differentiating it from others, deepening relationships with families and retaining more assets from generation to generation. Be sure to at least assess client interest in ESG products—if you don't, it is likely someone else will.

3 The True Faces of Sustainable Investing Busting Industry Myths Around ESG, Morningstar, Inc.
4 The Allianz ESG Investor Sentiment Study as of Dec. 2018.

51% of non-ESG investors want their advisor to speak to them about ESG Investing.[5]

83% of investors agree that advisors who discuss sustainable investing are more forward-thinking.[6]

5 State Street Center for Applied Research Survey of Retail Investors, December 2016
6 Nuveen, The Fifth Annual Responsible Investing Survey, Dec. 9, 2019

How Advisors Can Explain and Offer ESG Products to Clients

Step 1: Start With the Basics

What is Sustainable Investing?

We define sustainable investing as a long-term approach that incorporates environmental, social, and/or governance (ESG) factors into the investment process. Here are examples of some of the issues ESG investors consider important.

Exhibit 1 ESG Factors Investors Care About

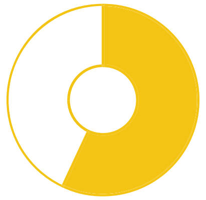
Environmental
Climate and environmental stewardship
- Climate change and carbon emissions
- Air and water pollution
- Energy efficiency
- Waste management
- Water scarcity
- Biodiversity and deforestation

Social
Well-being of multiple stakeholders
- Gender and diversity policies
- Safety and quality controls
- Human rights
- Labor standards
- Privacy and data security
- Employee engagement

Governance
Transparency, capacity, purpose
- Board diversity
- Corporate ethics
- Executive compensation
- Bribery and corruption policies
- Lobbying activities
- Accounting practices

It is important to discuss ESG factors with clients clearly and succinctly so they understand what sustainable investing means. We offer the ESG Factors graphic as a useful guide for describing the variety of considerations in play.

In spite of its rise in popularity and demand, ESG investing and related investment products can be a mystery to many clients. The oldest (and most limited) type of ESG investing focuses on exclusionary screening, which simply avoids investing in industries with negative ESG characteristics. A broader, and more modern, type of ESG investing is based on sustainability—these products feature a strong tilt toward the highest-scoring ESG companies and often involve direct engagement to promote better sustainability outcomes as part of the investment objectives. A company that builds small water treatment facilities (and trains local residents on construction and maintenance) may be a sustainable investment.



Majority of advisors avoid discussing ESG due to a perceived lack of knowledge.

Conversation Tip:
Ask your clients about their values and convictions surrounding environment, social, and governance principles.
80% of advisors report having a deep conversation about values with their clients has resulted in clients increasing their investment and loyalty.[7]

7 Nuveen, The Fifth Annual Responsible Investing Survey, Dec. 9, 2019

Step 2: Answering the "Why"

Why ESG investing matters to your clients.
The consideration and assessment of company ESG practices is rapidly becoming more important for long-term investments. Therefore, all investors should understand why ESG matters.

Conversation Tip:
Review how companies managing ESG risks may have a competitive advantage over others.

Assessing and Mitigating Risk:
There is a growing awareness of the potential financial impact of environmental, social, and governance issues. In recent years, there have been numerous events with wide-reaching implications for company leadership, sales and stock prices. Current business models must be responsive, and investors need to have the information to identify successful leaders whose companies aim to mitigate risk by having good sustainability practices.

Emerging Regulations
New ESG regulations are accelerating globally, underpinned by a movement to make these disclosures a standard part of corporate communications. EU and UK regulations now require asset managers, advisors, and pension funds to consider ESG risk as part of their fiduciary duties. EU regulators also require credit rating agencies to disclose how ESG factors are considered. This reflects a broader trend toward integrating ESG into financial decisions.

About 97% of sustainable finance policy revisions were developed since 2000, with over 80 new or revised policy instruments in 2019.[8]

8 Taking Stock: Sustainable Finance Policy Engagement and Policy Influence, PRI, 2020

Step 3: Tackling Common ESG Myths

Even with the exponential growth and adoption of sustainable investing, there are still many misconceptions on the topic.

Sustainable Investing is a Fad

There are currently over 2,700 signatories of the UN-led Principles for Responsible Investment (PRI) agreement. This group represents global assets totaling about $90 trillion.[8]

By signing, these asset management firms agreed to:

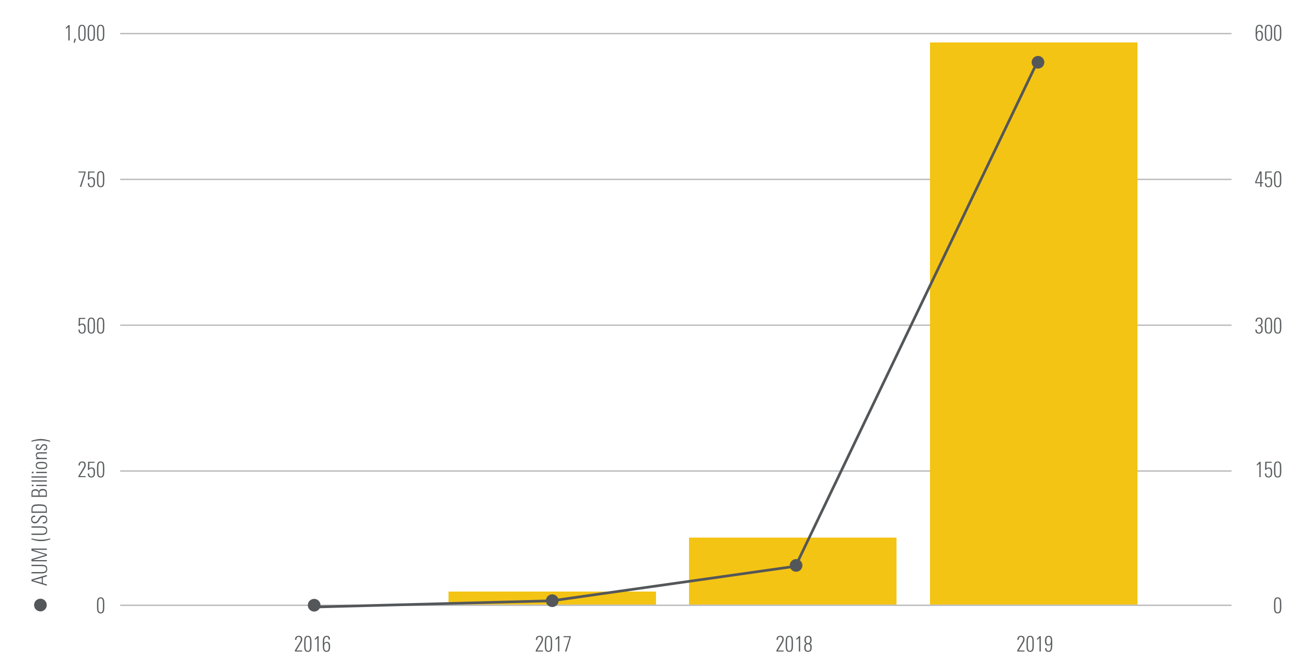
1. Incorporate ESG into investment decisions,
2. Be active shareholders,
3. Promote ESG disclosures from companies invested in,
4. Promote ESG adoption across the industry,
5. Be transparent in all ESG activities and
6. Work with signatories to promote these principles.

A global survey of institutional investors and hedge fund managers (representing $6 trillion in assets). They found 84% of managers had demonstrated increased interest in ESG-oriented funds and strategies.[9]

Global survey found 84% of managers increased their interest in ESG-oriented funds[9]

It would be easy (but incorrect) to claim that data supporting the increased interest in environmental, social and governance-focused investing is being pushed by fund producers. Per Statista, there were nearly 8,000 mutual funds available in 2019 just in the US, so investors have no shortage of choices. This is why the dramatic jump in ESG-focused funds is so meaningful. Per Morningstar, Inc., funds that use ESG in investment analysis jumped from 20 in 2017 to 81 in 2018 to 564 in 2019. This interest continues even in this pandemic year.

Sustainable Funds Annual Flow Set Record in 2019



Source: Morningstar Direct, as of 12/31/19. For illustrative purposes only.

8 PRI welcomes 500th asset owner signatory, Lorenzo Saa, Jan. 27, 2020
9 KPMG International, CREATE-Research, AIMA and CAIA, "Sustainable investing: fast-forwarding its evolution", as of Feb. 2020.

Second Myth: ESG Investors Must Accept Lower Returns

This is one of the most hotly debated elements of the ESG growth story, but it doesn't need to be. In theory, if an investment is restricted to a certain subset of the investing universe, one would expect some reduced returns. However, the data suggest ESG funds may outperform traditional funds, especially for ESG funds with lower fees. The above-50% outperformance rate for surviving sustainable funds (those that existed 10 years ago and still exist today) in most categories over multiple time periods indicate that investors taking the ESG route were less likely to miss out on returns than if they had invested in traditional funds. However, because ESG funds represent a subset of the investment universe, returns may differ from traditional investments.

Sustainable Funds' Outperformance* Rate by Morningstar Category (%)

	Outperformance* Rate of of Sustainable Funds			
Category	**1-Year**	**3-Year**	**5-Year**	**10-Year**
Global Large-Cap Blend Equity	75.1	73.7	76.9	67.3
Global Large-Cap Growth Equity	60.3	**43.2**	**37.5**	56.7
Global Emerging Markets Equity	**41.3**	60.0	58.8	50.0
US Large-Cap Blend Equity	76.4	71.4	76.9	81.3
Europe Large-Cap Blend Equity	71.1	75.0	67.2	55.1
Eurozone Large-Cap Equity	63.5	63.0	60.6	62.3
EUR Corporate Bond	58.0	58.5	62.2	**33.3**
All Categories	**65.6**	**65.6**	**64.4**	**58.8**

Source: Morningstar Direct. Morningstar Research. Data as of December 31, 2019. For illustrative purposes only. Past performance is not a guarantee of future results.
*This table shows the percentage where the sustainable fund outperformed the equivalent "traditional" fund over the term shown

Conversation Tip:
Based on data, it appears there is no direct performance impact for sustainable investing.

Step 4: A Dual Mandate: Helping reach clients financial and sustainability goals

Morningstar Managed Portfolios offers the Morningstar ESG Asset Allocation Portfolios which are focused on helping reach financial and sustainable goals in your clients portfolios.

Morningstar ESG Asset Allocation Portfolios help provide a professionally managed diversified investment with exposure to ESG-friendly assets across the globe. This allows an investor to make the entire portfolio ESG-friendly while aiming to reduce risk and improve return potential.

Sustainable Approach

We aim to generate a competitive long-term financial return as well as positive societal impact. We select funds with high levels of ESG integration.

Diversified Exposure

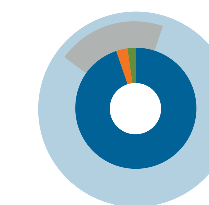
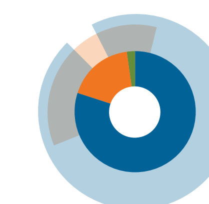
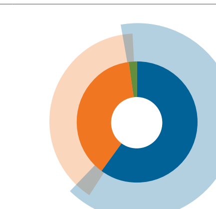
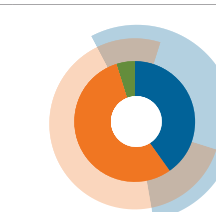
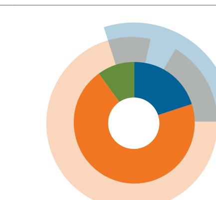
We offer professionally managed portfolios that are diversified both financially and across ESG investing styles. We diversify our ESG approach by investing across a variety of ESG strategies rather than catering to an isolated ESG issue.

Morningstar ESG Focus

Incorporates research from Morningstar, Inc., a sustainable investing leader who has recently acquired Sustainanalytics—a global leader in ESG research. This ensures that our ESG-managed portfolios are informed by quality information and insight.

Conversation Tip:
The Morningstar ESG Asset Allocation investments must meet strict ESG practice criteria and be selling for less than market value based on our analysis to meet your financial goals.

● Equity ● Fixed Income ● Alts ● Cash

PORTFOLIOS	GOAL	ASSET CLASS RANGE	ALLOCATION
Aggressive Growth	Long-term capital appreciation. The portfolio invests primarily in domestic and foreign equities, while seeking to cushion equity market downturns with modest exposure to fixed-income securities.	80-100% 0-20% 0-20% 0-25%	
Growth	Long-term capital appreciation. Designed to help investors to take advantage of the potential for stock market growth by investing primarily in domestic and foreign equities.	65-95% 5-35% 0-20% 0-25%	
Moderate Growth	Long-term growth with moderate volatility. Built with a focus on providing balanced and varied exposure by investing in both equity and fixed-income securities.	45-75% 25-55% 0-20% 0-25%	
Income and Growth	Moderate capital appreciation combined with current income. Combines the growth potential of equities with the balance that fixed-income securities can provide.	25-55% 45-75% 0-20% 0-25%	
Conservative	Protection from capital loss and a safeguard against inflation. Invested in fixed-income and equity securities, it's designed to be best suited for investors who seek current income and stability.	5-35% 65-95% 0-20% 0-25%	

Asset classes shown are determined by Morningstar Category groups. Allocation at the individual account level may vary. Neither diversification nor asset allocation ensure a profit or guarantee against a loss. Those asset classes noted may be known to be a growth engine, income producer, or volatility dampener but there is no guarantee this will hold true. For illustrative purposes only.

Alternative strategies may not be suitable for all investors and should be considered as an investment for the risk capital portion of the investor's portfolio. The strategies employed in the management of alternative investments may accelerate the velocity of potential losses.

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