

Sustainable Investing Landscape for Canadian Fund Investors

Q4 2021

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Sustainable Fund and ETF Assets Double in 2021

Following another enthusiastic year of sustainable fund launches and ensuing interest from investors, Morningstar's data shows the continued accelerated growth of sustainable funds in Canada.

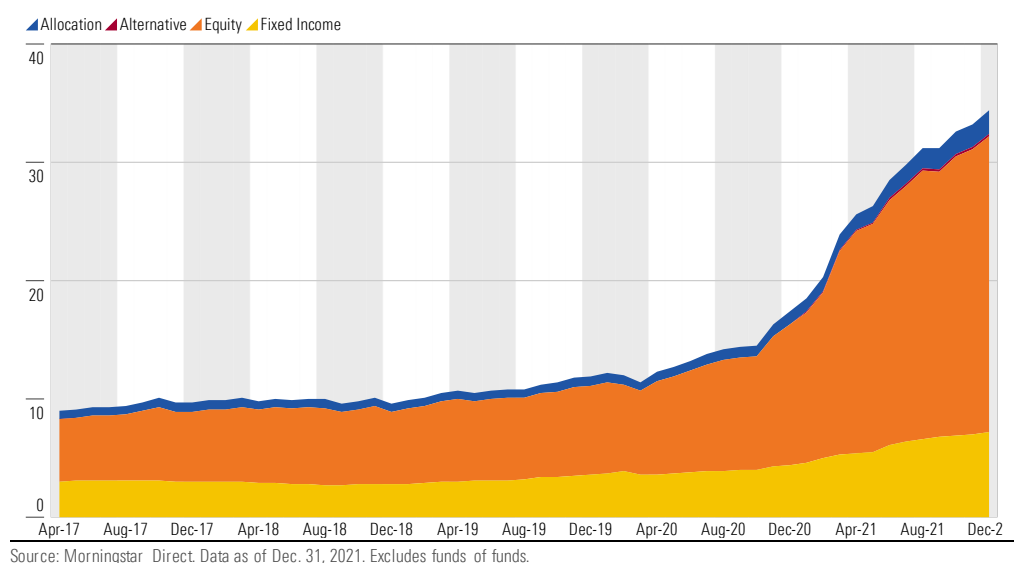
Key Takeaways

- ▶ Over the 2021 calendar year, assets invested in sustainable funds and exchange-traded funds grew from CAD 17.4 billion to CAD 34.5 billion. Over the fourth quarter alone, assets grew by 10%. Most of this growth continued to surface within the equity asset class, where funds exhibited a year-over-year growth rate in assets of 110%, followed by allocation and fixed-income funds, which grew by 89% and 62%, respectively
- ▶ In terms of assets invested in funds and ETFs, the leaders in the space remained largely unchanged, with likes of NEI Investments, RBC, Mackenzie, BMO, IA Clarington, Desjardins, and AGF Investments currently managing 80% of assets.
- ▶ There were 73 Canadian-domiciled investment products launched in 2021, compared with 42 products launched a year earlier. In total, new products launched in 2021 collected CAD 3 billion in assets under management, with Fidelity Climate Leadership collecting CAD 543 million alone.
- ▶ Asset flows for sustainable funds and ETFs were positive in all four quarters, though the first quarter outshone the others by a large margin, particularly in February prior to Canadians' Registered Retirement Savings Plan contribution deadline. As a proportion, 77% of net inflows in 2021 went to equity funds, 18% to fixed-income funds, and the remainder to allocation funds, reflective of product availability across these broad category groups.
- ▶ Sustainable funds and ETFs finished off the year strong in terms of after-fee risk-adjusted performance. In the fourth quarter, 57% (117 of 207) of sustainable investment products outperformed their respective Morningstar Category peers. Equity funds showed particular strength, with 61% (72 of 118) outperforming peers. Over longer periods, sustainable products performed much like their traditional counterparts.
- ▶ On the heels of the Canadian Securities Administrators' proposal in October that requires Canadian-listed issuers to report climate-related risks per the Task Force on Climate-Related Disclosures' framework, the CSA also issued a staff notice in early 2022 offering guidance to investment fund manufacturers on how to disclose sustainable investment considerations.

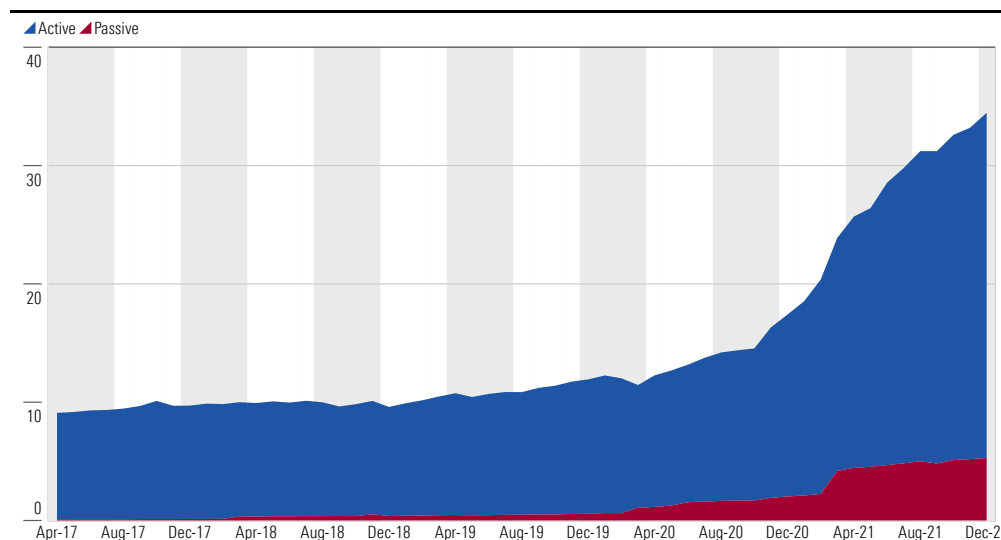
Market Size

Given that Canadian households recorded [elevated savings rates](#) over the 2021 calendar year, it is no surprise that flows into investment funds in general reflected positively. Given this, investments in sustainable funds grew substantially over the year, doubling assets from CAD 17.4 billion to CAD 34.5 billion in 12 months. Over the fourth quarter alone, assets grew by 10%. Most of this growth continued to surface within the equity asset class, with funds here exhibiting a year-over-year growth rate in assets of 110%, followed by allocation and fixed-income funds, which grew by 89% and 62%, respectively.

Exhibit 1 Canadian Sustainable Fund Assets by Asset Class (Excludes Funds of Funds, CAD, Billions)



Between active and passive mandates, funds identified as sustainable investments largely reflected the broader market, with 85% of assets sitting in actively managed strategies. Given their smaller base, passive strategies grew over the year at a faster clip (160% year over year) than active strategies (90%).

Exhibit 2 Canadian Sustainable Fund Assets, Active vs. Passive (Excludes Funds of Funds, CAD, Billions)

Source: Morningstar Direct. Data as of Dec. 31, 2021. Excludes funds of funds.

Also unsurprisingly, the sustainable investment fund and ETF market continued to be dominated by a handful of heavyweights, including NEI Investments, RBC, Mackenzie, BMO, IA Clarington, Desjardins, and AGF investments. Together these seven providers manage 80% of sustainable mutual funds and ETF assets.

Exhibit 3 Sustainable Fund Assets by Select Branding Names

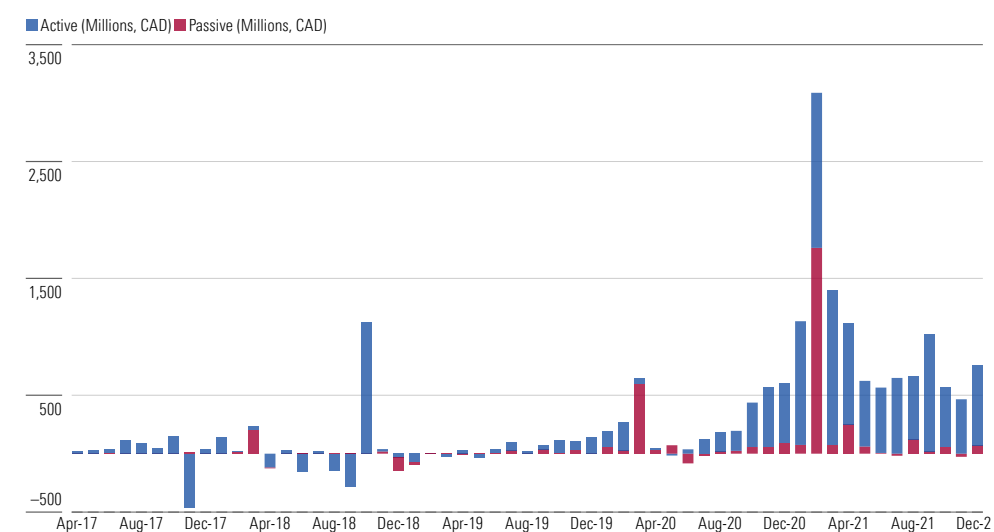
Branding Name	Total Net Assets (Aggregated from Share Class, CAD, Billions)	% of Total Sustainable Fund Assets
NEI Investments	9.2	34%
RBC	3.2	12%
Mackenzie	2.6	10%
BMO	2.5	9%
IA Clarington	2.0	7%
Desjardins	1.8	6%
AGF	0.8	3%
Franklin Templeton	0.8	3%
National Bank (Canada)	0.8	3%
Fidelity	0.7	3%

Source: Morningstar Direct. Data as of Dec. 31, 2021. Excludes funds of funds. Aggregation only includes share classes of ETFs and Mutual Funds reported to Morningstar.

Asset Flows

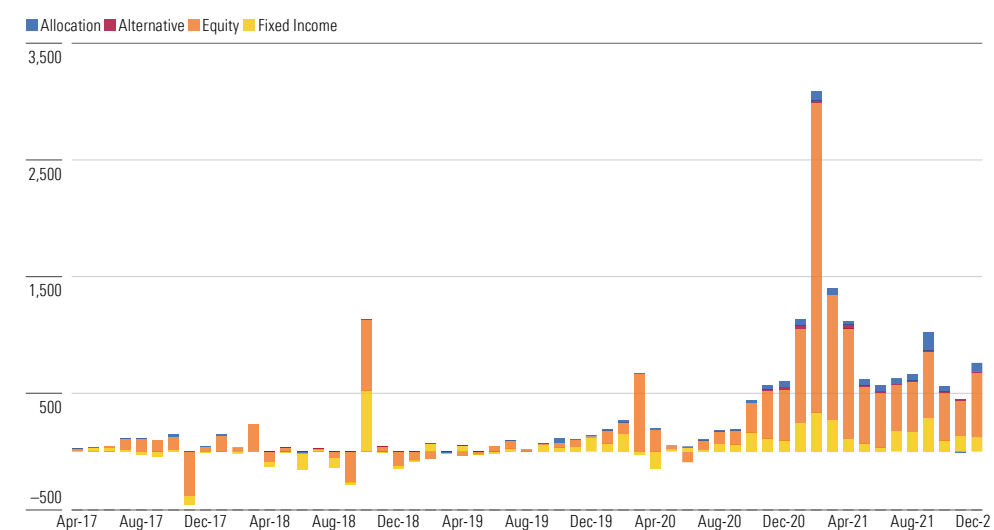
With 2021 in the rear view, we can see that asset flows into sustainable funds and ETFs were positive in all four quarters, though the first quarter outshone the others by a large margin, particularly in February. Flows following that month were still orders of magnitude larger than those observed over calendar-year 2020. In the fourth quarter, Canada-domiciled sustainable funds saw inflows of CAD 2 billion, which was similar to the third quarter. Inflows over each of month of 2021 largely outpaced prior history.

Exhibit 4 Estimated Net Flows, Active & Passive Sustainable Funds (CAD, Millions)



Seventy-seven percent of net inflows over 2021 went to equity funds, 18% to fixed-income funds, and the remainder to allocation funds, reflective of product availability across these broad category groups.

Exhibit 5 Estimated Net Flows, Broad Category Groups (CAD, Millions)



As mentioned above, sustainable funds saw record inflows in the month of February. Looking closer, much of this success can be attributed to BMO MSCI USA ESG Leaders ETF (a passive strategy), which by Morningstar's estimates took CAD 1.7 billion of inflows in February alone. Mackenzie Greenchip Global Environmental All Cap also recorded stellar inflows of CAD 306 million that month, noting that February marks the month just prior to Canadians' Registered Retirement Savings Plan contribution deadline.

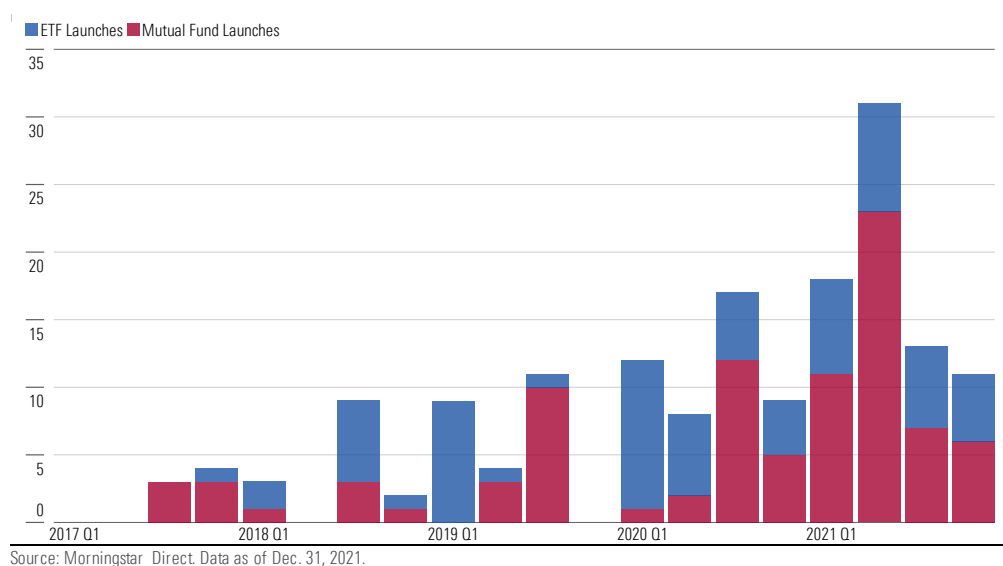
Exhibit 6 Top 10 Funds by Estimated Net Inflows, February 2021

Name	Est. Net Inflows (CAD, Millions)
BMO MSCI USA ESG Leaders ETF	1,659.2
Mackenzie Greenchip Global Environmental All Cap	306.5
NBI Sustainable Canadian Corporate Bond ETF	105.9
RBC Vision Global Equity	84.2
RBC Vision Fossil Fuel Free Short-Term Bond	83.1
BMO Sustainable Opportunities Global Equity	72.2
Dynamic Energy Evolution	63.9
NEI Environmental Leaders Series	53.7
RBC Vision Fossil Fuel Free Global Equity	52.4
AGF Global Sustainable Growth Equity	46.6
Desjardins SocieTerra 100% Equity	38.6

Source: Morningstar Direct. Data as of Dec. 31, 2021. Excludes funds of funds.

Product Launches

Over the fourth quarter, 11 new sustainable funds and ETFs were launched, bringing the year's total to 73 products. Comparatively, 42 sustainable funds and ETFs were launched in 2020. These products have evidently garnered interest from investors. In total, new products launched in 2021 collected CAD 3 billion, with Fidelity Climate Leadership collecting CAD 543 million alone.

Exhibit 7 Canada-Domiciled Sustainable Mutual Fund and ETF Launches**Exhibit 8** Select Funds and ETFs Launched in 2021

Name	Inception Date	Morningstar Category	Fund Size, CAD, Millions
Fidelity Climate Leadership	5/18/2021	Global Equity	543.2
RBC Vision Fossil Fuel Free ST Bond	1/22/2021	Canadian ST Fixed Income	277.1
FERIQUE Global Sustainable Dev Bond	1/29/2021	Global Fixed Income	236.6
Mackenzie Global Sustainable Bond ETF	9/23/2021	Global Fixed Income	200.4
Franklin ClearBridge US Sus Leaders	6/10/2021	US Equity	184.8
NBI Sustainable Canadian Corp Bond ETF	1/28/2021	Can Corp Fixed Income	173.7
Franklin Martin Currie Sus Emer Mkt	6/10/2021	Emerging-Markets Equity	165.0
FERIQUE Global Sustainable Dev Eq	1/29/2021	Global Equity	143.6
Desjardins RI Em Mkts Low CO2 ETF	3/12/2021	Emerging Markets Equity	121.6
Fidelity Climate Leadership Bal	5/18/2021	Global Neutral Balanced	97.5

Source: Morningstar Direct. Data as of Dec. 31, 2021. Aggregation only includes share classes of ETFs and Mutual Funds reported to Morningstar.

Performance of Sustainable Investments Relative to Morningstar Category Averages

Sustainable funds and ETFs finished off the year strong in terms of risk-adjusted performance after fees. In the fourth quarter, 57% (117 of 207) sustainable investment products outperformed their respective Morningstar Category peers. Equity funds showed particular strength, with 61% (72 of 118) of funds outperforming peers. Given that a single quarter of performance is not nearly enough information to base performance on, the subsequent tables show the trailing one-, five-, and 10-year summaries of performance quartiles. Though the sample size decreases as we look to longer periods, the data shows

that historically on average, sustainable investment products perform much like their traditional counterparts.

Exhibit 9 Total-Return Quartile Ranks of Sustainable Investments, Q4 2021

Broad Category/Morningstar Category	Top Quartile	Second Quartile	Third Quartile	Fourth Quartile	Total
Allocation	16	13	10	12	51
Canadian Equity Balanced		1		1	2
Canadian Fixed Income					
Balanced		1	1		2
Canadian Neutral Balanced				1	1
Global Equity Balanced	8	1	5	1	15
Global Fixed Income Balanced	3	3	2	3	11
Global Neutral Balanced	5	6	2	6	19
Tactical Balanced		1			1
Equity	34	38	28	18	118
Canadian Equity	6	11	5	2	24
Canadian Focused Equity		2	1		3
Canadian Small/Mid-Cap Equity			1		1
Emerging Markets Equity	2		1	4	7
Energy Equity				2	2
Global Equity	14	11	12	5	42
Global Infrastructure Equity	1		1		2
Global Small/Mid-Cap Equity	2	2	2		6
Greater China Equity	1				1
International Equity		7	3	3	13
North American Equity	1	2			3
US Equity	7	3	2	2	14
Fixed Income	7	9	16	6	38
Canadian Corp. Fixed Income		1	1		2
Canadian Fixed Income	2	5	5	4	16
Canadian ST Fixed Income			3		3
Global Corporate Fixed Income	1		1		2
Global Fixed Income	3	2	6	2	13
High Yield Fixed Income	1	1			2
Grand Total	57	60	54	36	207

Source: Morningstar Direct. Data as of Dec. 31, 2021. Oldest share class only.

Exhibit 10 Total-Return Quartile Ranks of Sustainable Investments, Calendar-Year 2021

Broad Category/Morningstar Category	Top Quartile	Second Quartile	Third Quartile	Fourth Quartile	Total
Allocation	7	3	13	14	37
Canadian Equity Balanced	1			1	2
Canadian Fixed Income Balanced			1	1	2
Canadian Neutral Balanced				1	1
Global Equity Balanced	2	1	3	4	10
Global Fixed Income Balanced	1	1	4	3	9
Global Neutral Balanced	3	1	4	4	12
Tactical Balanced			1		1
Equity	20	32	19	17	88
Canadian Equity	5	6	4	3	18
Canadian Focused Equity		3			3
Canadian Small/Mid-Cap Equity		1			1
Emerging Markets Equity	1		1	2	4
Energy Equity				1	1
Global Equity	10	9	6	8	33
Global Small/Mid-Cap Equity	1	1	1		3
International Equity		6	4	1	11
North American Equity	1	2			3
US Equity	2	4	3	2	11
Fixed Income	2	6	7	4	19
Canadian Fixed Income		5	5	2	12
Canadian ST Fixed Income			1		1
Global Corporate Fixed Income				1	1
Global Fixed Income	1	1	1	1	4
High Yield Fixed Income	1				1
Grand Total	29	41	39	35	144

Source: Morningstar Direct. Data as of Dec. 31, 2021. Oldest share class only.

Exhibit 11 Total-Return Quartile Ranks of Sustainable Investments, 5-Year Trailing

Broad Category/Morningstar Category	Top Quartile	Second Quartile	Third Quartile	Fourth Quartile	Total
Allocation	5	5	5	3	18
Canadian Equity Balanced	2				2
Canadian Fixed Income Balanced	1				1
Canadian Neutral Balanced	1				1
Global Equity Balanced	1	3	1	1	6
Global Fixed Income Balanced		1	1	1	3
Global Neutral Balanced		1	3		4
Tactical Balanced				1	1
Equity	11	4	12	3	30
Canadian Equity	2	1	1	1	5
Canadian Focused Equity			3		3
Canadian Small/Mid-Cap Equity			1		1
Emerging Markets Equity	1				1
Global Equity	6	2	5	1	14
Global Small/Mid-Cap Equity	1				1
International Equity			1	1	2
North American Equity		1			1
US Equity	1		1		2
Fixed Income	4	2	4	1	11
Canadian Fixed Income	2	1	3	1	7
Global Fixed Income	1	1	1		3
High Yield Fixed Income	1				1
Grand Total	20	11	21	7	59

Source: Morningstar Direct. Data as of Dec. 31, 2021. Oldest share class only.

Exhibit 12 Total-Return Quartile Ranks of Sustainable Investments, 10-Year Trailing

Broad Category/Morningstar Category	Top Quartile	Second Quartile	Third Quartile	Fourth Quartile	Total
Allocation	3	5	4	5	17
Canadian Equity Balanced	2				2
Canadian Fixed Income					
Balanced		1			1
Canadian Neutral Balanced		1			1
Global Equity Balanced	1	2	1	1	5
Global Fixed Income Balanced			2	1	3
Global Neutral Balanced		1	1	2	4
Tactical Balanced				1	1
Equity	4	6	3	8	21
Canadian Equity	2	1		2	5
Canadian Focused Equity		1		2	3
Canadian Small/Mid-Cap Equity		1			1
Global Equity	2	3	2	2	9
International Equity			1	1	2
US Equity				1	1
Fixed Income	3		1	1	5
Canadian Fixed Income	2			1	3
Global Fixed Income			1		1
High Yield Fixed Income	1				1
Grand Total	10	11	8	14	43

Source: Morningstar Direct. Data as of Dec. 31, 2021. Oldest share class only.

Despite the growth of assets deemed to be sustainable in Canada, the universe of products with an investment mandate aligned with a sustainable-investing objective is notably smaller than the universe of products with effective management of environmental, social, and governance risks as framed through the Morningstar Sustainability Rating. Only 10% of mutual funds and ETFs with low ESG risk (earning Above Average or High Sustainability Ratings) also identify themselves as intentionally sustainable investment products. Although this is mostly due to a lack of intentionally sustainable products in the alternative asset class, representation is low among all asset classes, with only 8.6% of balanced, 11.4% of equity, and 15.0% of fixed-income products satisfying both criteria.

Over the past six-month and one-year time periods, low-ESG-risk products generally outperformed sustainable products, particularly in the Canadian neutral balanced, Canadian small/mid-cap equity, global small/mid-cap equity, and international-equity peer groups. Of note is that in the tactical balanced, Canadian equity, North American equity, and US equity peer groups, sustainable products outperformed low-ESG-risk products.

Canadian Regulatory Updates

On the heels of the Canadian Securities Administrators' proposal in October that requires Canadian-listed issuers to report climate-related risks per the Task Force on Climate-Related Financial Disclosures framework, the CSA also issued a [staff notice](#) in early 2022 offering guidance to investment fund manufacturers on how to disclose sustainable investment considerations. The intent of the guidance is ultimately to prevent misleading information on ESG-related practices of a particular fund, also known as greenwashing.

We also note Canada's support of the International Sustainable Standards Board, which, through its creation, will likely leverage the TCFD framework for climate-related disclosure and the Sustainability Accounting Standards Board framework for broader ESG-related disclosures as these pertain to issuers. Both frameworks are globally recognized and offer detailed guidance on disclosure requirements. Both frameworks also leverage a "building block" approach, focusing first on financially material disclosures, followed by broader impact-oriented metrics in the future. Given the successful bid for an ISSB office in Montreal, we hope that additional ongoing guidance will be made available by local ISSB staff to issuers that may soon be required to report new climate-related information. This support and additional reporting requirements will add much needed depth and breadth in aiding investment decisions by sustainable fund managers and will likely proliferate into an even larger universe of sustainable products in the years ahead. ■■

Helpful Links:

[Morningstar Sustainable Fund Attributes](#)

[Morningstar Sustainability Rating Methodology](#)

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