SFDR Article 8 and Article 9 Funds: Q3 2022 in Review

Managers downgrade more Article 9 funds ahead of 2023 enhanced disclosure regime.

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Executive Summary

Since the European Union's Sustainable Finance Disclosure Regulation came into force in March 2021, asset managers have been required to self-classify funds sold in the EU as Article 6, 8, or 9, depending on their sustainability objectives. In recent months, managers have been busy preparing to implement the regulatory technical standards that will come into effect in January 2023. These standards require managers to disclose more information on their funds' ESG approach, sustainability risks, and impact in precontractual documents and periodic reports. Ahead of this upgraded disclosure regime, some managers have reviewed their funds' classification and downgraded Article 9 products to Article 8.

This report provides an update on the rapidly evolving landscape of Article 8 and Article 9 funds at the end of the third quarter 2022, examining flows, assets, and products. Additionally, we analyze key data shared by asset managers via the European ESG Template, or EET, including minimum sustainable investment and taxonomy alignment exposures as well as principal adverse impact (PAI) consideration.

Key Takeaways

- In the third quarter of 2022, Article 8 funds bled EUR 28.7 billion, only slightly less than in the previous quarter, against a continuously challenging backdrop of high inflationary pressures, a looming global recession, and geopolitical risks following Russia's invasion of Ukraine.
- Despite this backdrop, Article 9 products recorded inflows of EUR 12.6 billion, double those of the second quarter, boosted by passive strategies.
- Article 8 and Article 9 fund assets rose by almost 3% over the third quarter to EUR 4.3 trillion. In comparison, Article 6 fund assets dropped by 9.6%.
- The market share of Article 8 and Article 9 fund assets continued to increase and reached 53.5% at the end of September.
- Over 380 products changed SFDR status in the last quarter. The vast majority were upgraded to Article 8 from 6, but 41 were downgraded to Article 8 from 9, and more are expected to follow suit in the coming months.
- While nearly all (95%) of Article 8 and Article 9 funds report considering PAIs, still less than half (48%) disclose a minimum percentage of sustainable investments, and just one third report a minimum percentage of taxonomy-aligned investments.
- Less than 5% of Article 9 funds target sustainable-investment exposure between 90% and 100%, and only 26 funds aim for a 100% allocation to sustainable investment, raising questions about the feasibility of some new regulatory guidance.

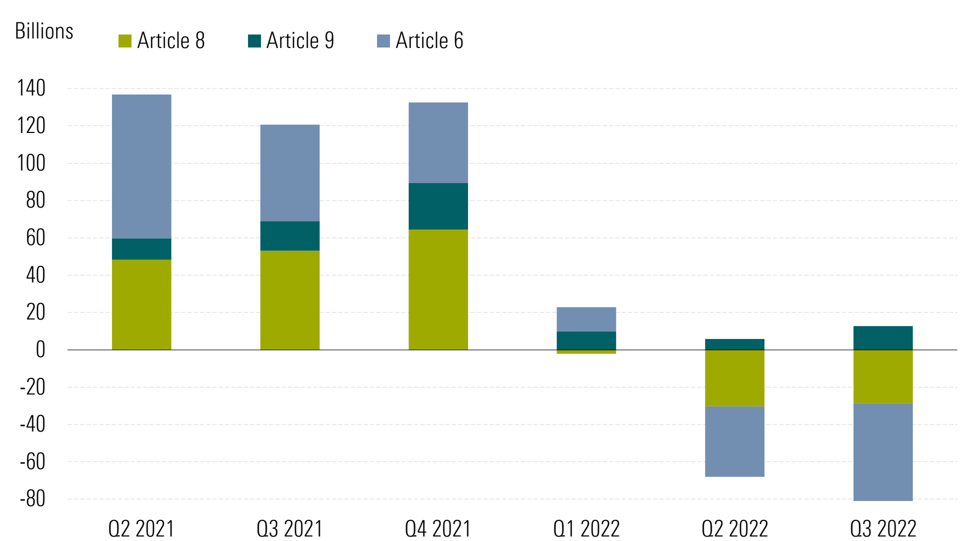
- Of the Article 8 and Article 9 products that report taxonomy alignment, 85% provide 0% values, while a mere 2% of Article 9 funds target exposure to taxonomy-aligned investments higher than 10%.

The Article 8 and Article 9 Fund Universe
Our Article 8 and Article 9 fund universe in this study encompasses open-end and exchange-traded funds in scope of the Sustainable Finance Disclosure Regulation that state in their prospectuses that they either promote environmental and/or social characteristics (Article 8, "light green" funds) or have a sustainable-investment objective (Article 9, "dark green" funds). We identified these funds using the EU SFDR Fund Type (Article 8 or Article 9) data point in the Morningstar Direct database. Funds in scope of SFDR that are neither Article 8 nor Article 9 are Article 6 funds (Not Stated in Morningstar Direct). This report uses SFDR disclosure collected from prospectuses on 97.4% of funds available for sale in the EU, excluding money market funds, funds of funds, and feeder funds.

Article 8 Funds Register Net Outflows for Another Quarter; Article 9 Funds Remain Resilient
Against a continuously challenging backdrop of inflationary pressures, interest-rate hikes, a looming global recession, and geopolitical risks following Russia's invasion of Ukraine, Article 8 funds bled EUR 28.7 billion in the third quarter. However, this is less than the updated EUR 31.6 billion in the previous quarter. Article 8 funds also held up better than their Article 6 peers, which saw outflows worsen to EUR 62.1 billion in the third quarter.

Meanwhile, investors continued to pour money into Article 9 products, as these registered EUR 12.6 billion in net inflows over the past three months, more than double the EUR 6 billion of inflows recorded in the second quarter.

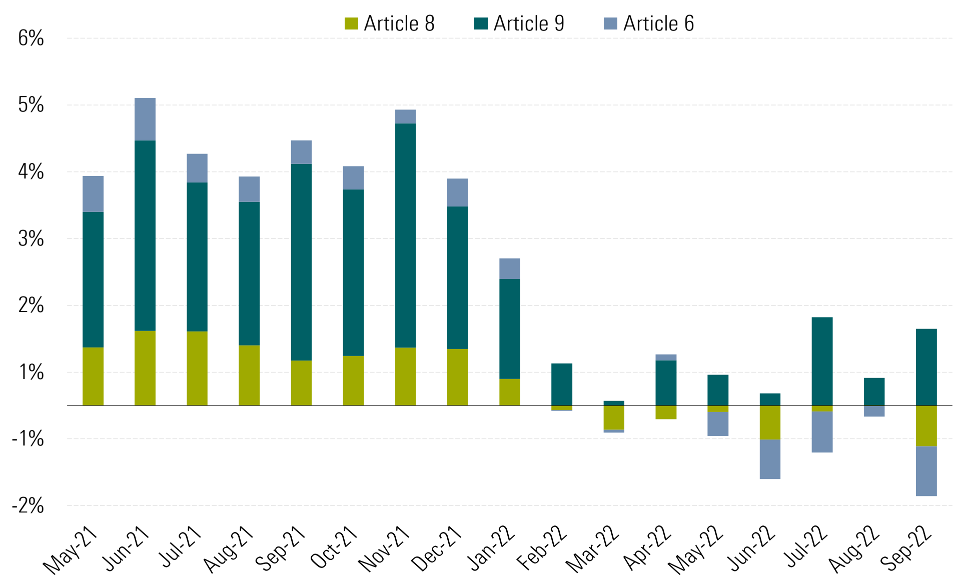
Exhibit 1 Quarterly Flows Into Article 8 and Article 9 Funds Versus Article 6 Funds (EUR Billion)



Source: Morningstar Direct. Data as of Sept. 30, 2022. Based on SFDR data collected from prospectuses on 97.4% of funds available for sale in the EU, excluding money market funds, funds of funds, and feeder funds.

The more positive picture for Article 9 funds is more striking when looking at organic growth rates, which measure the growth of flows relative to assets[1]. Organic growth rates for Article 9 products have been the highest since the introduction of SFDR and have remained positive this year. Meanwhile, organic growth rates for Article 8 and Article 6 funds sunk deeper into negative territory.

Exhibit 2 Organic Growth Rates

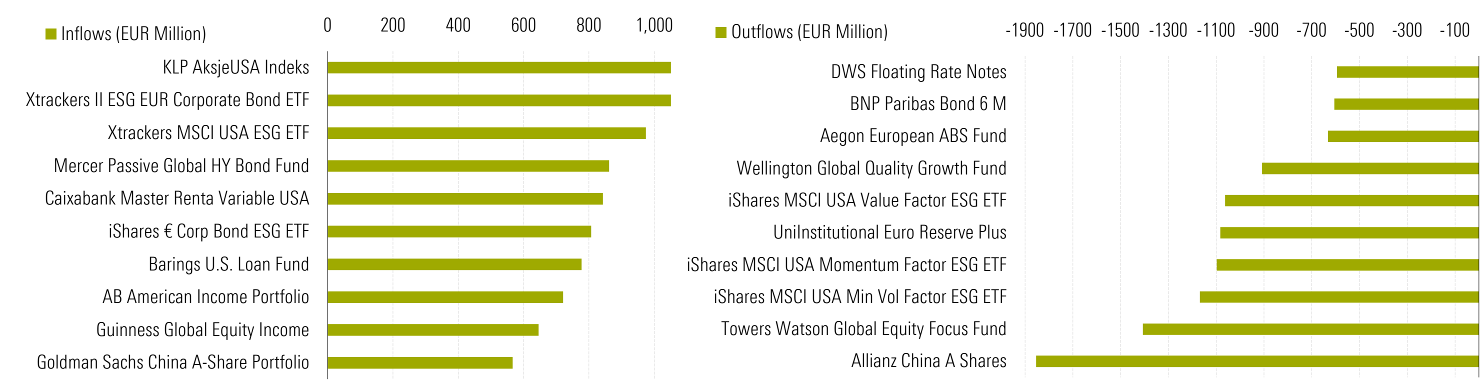


Source: Morningstar Direct. Data as of Sept. 30, 2022. Based on SFDR data collected from prospectuses on 97.4% of funds available for sale in the EU, excluding money market funds, funds of funds, and feeder funds.

Flows—Leaders and Laggards

Below are the Article 8 and Article 9 funds that experienced the largest inflows and outflows over the third quarter.

Exhibit 3 Article 8 Funds With the Largest Inflows and Outflows in the Third Quarter of 2022



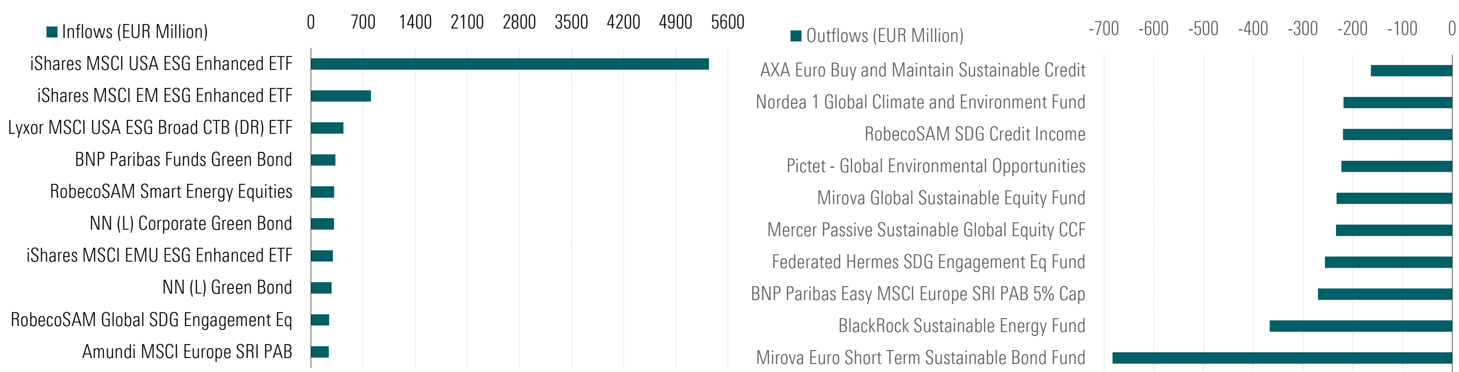
Source: Morningstar Direct. Data as of Sept. 30, 2022. Based on SFDR data collected from prospectuses on 97.4% of funds available for sale in the EU, excluding money market funds, funds of funds, and feeder funds.

1 Organic growth rate is calculated as followed: current period flows divided by beginning-of-period net assets.

Both Article 8 and Article 9 flow leaderboards are well staffed with passive funds, including several that track EU climate benchmarks. **IShares MSCI USA ESG Enhanced ETF** was by far the best-selling fund in the third quarter, attracting an eye-watering EUR 5.3 billion of net new money. Currently classified as Article 9, the fund tracks a climate-transition benchmark, which, through an optimizer, also maximizes exposure to issuers with higher ESG ratings.

Meanwhile, the biggest outflows (EUR 1.8 billion) were registered by Article 8 **Allianz China A Shares.** The fund saw Chilean pension providers withdraw their money following an SEC announcement in May that it had charged AllianzGI US for a multibillion-dollar securities fraud.

Exhibit 4 Article 9 Funds With the Largest Inflows and Outflows in the Third Quarter of 2022

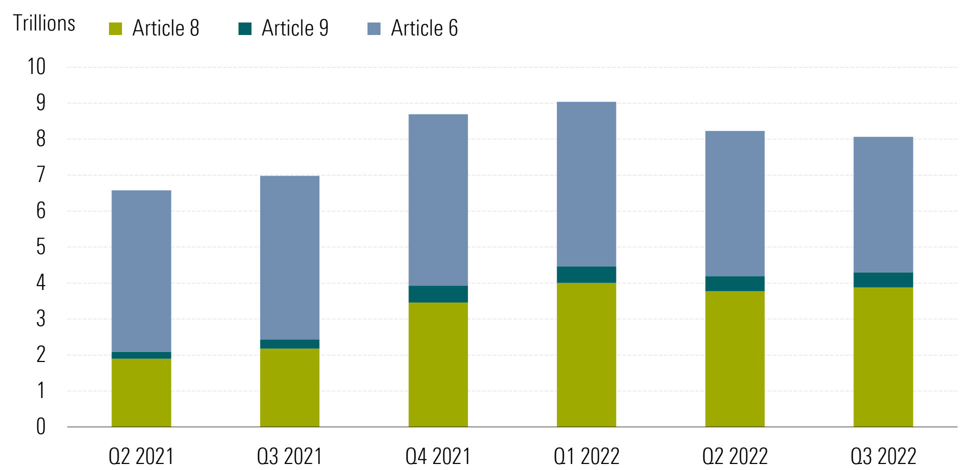


Source: Morningstar Direct. Data as of Sept. 30, 2022. Based on SFDR data collected from prospectuses on 97.4% of funds available for sale in the EU, excluding money market funds, funds of funds, and feeder funds.

Article 8 and Article 9 Fund Assets Surpass 50% Market Share

Despite net outflows and falling market prices, Article 8 and Article 9 fund assets rose by almost 3% over the third quarter of 2022, driven by newly launched and reclassified funds. Article 8 and Article 9 fund assets stood at EUR 4.30 trillion at the end of September, up from an updated amount of EUR 4.19 trillion at the end of June. In comparison, Article 6 fund assets dropped by almost 7%, or EUR 270 billion, over the period.

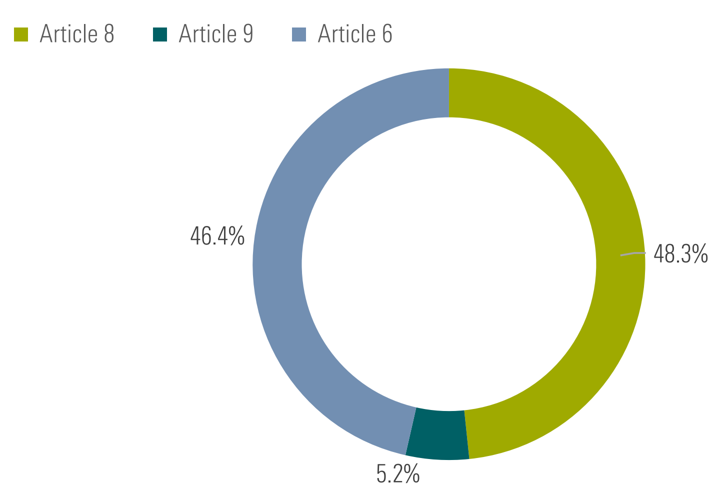
Exhibit 5 Quarterly Assets Breakdown by SFDR Classification



Source: Morningstar Direct. Data as of Oct. 13, 2022. Based on SFDR data collected from prospectuses on 96% of funds available for sale in the EU, excluding money market funds, funds of funds, and feeder funds.

As a result, the two fund groups accounted for an increased share of the EU universe of 53.5%, from 50.9% three months earlier. Asset managers continued upgrading strategies and launching new products that meet the articles' requirements. The 53.5% market share at the end of September was split into 48.3% (up from 45.9% in June) for Article 8 products and 5.2% (up from 5.1% in June) for Article 9 products.

Exhibit 6.a SFDR Fund Type Breakdown (by Assets)

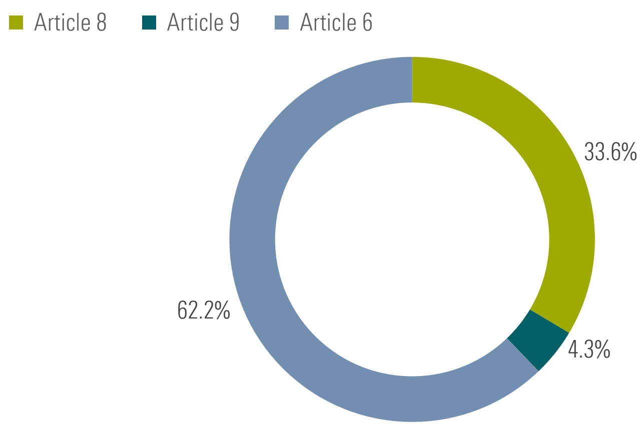


Source: Morningstar Direct. Data as of Sept. 30, 2022. Based on SFDR data collected from prospectuses on 97.4% of funds available for sale in the EU, excluding money market funds, funds of funds, and feeder funds.

In terms of number of funds,[2] the market share of Article 8 and Article 9 funds also grew in the third quarter, with 8,459 funds (33.6%) classified as Article 8 and 1,080 funds (4.3%) classified as Article 9 at the end of September.

Combined, the two categories represented 37.8% of the overall EU fund universe in September, up from 35.4% in June.

Exhibit 6.b SFDR Fund Type Breakdown (by Number of Funds)



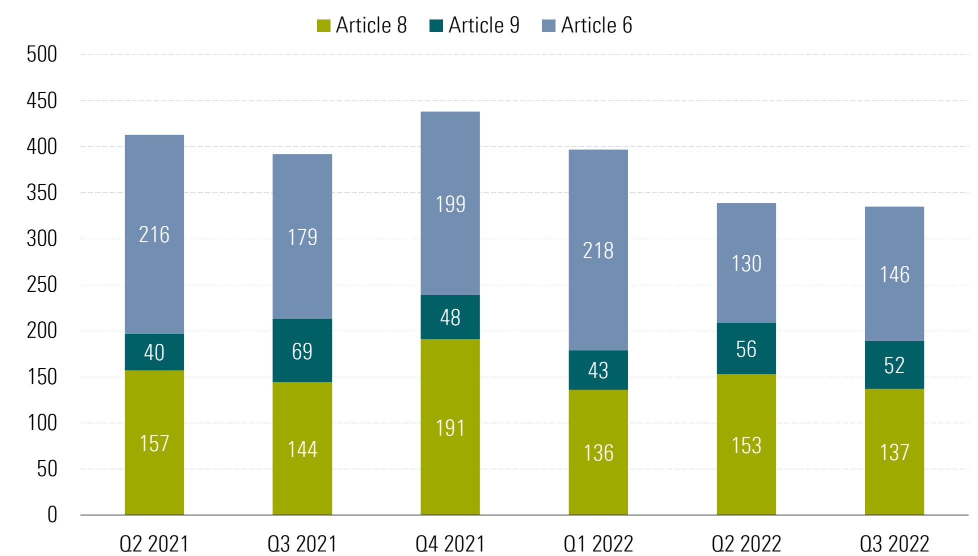
Source: Morningstar Direct. Data as of Sept. 30, 2022. Based on SFDR data collected from prospectuses on 97.4% of funds available for sale in the EU, excluding money market funds, funds of funds, and feeder funds.

Fund Launches: More Climate, Biodiversity, and Social Investment Options

Product development slowed down slightly, with an estimated 137 Article 8 funds and 52 Article 9 funds launched over the past three months. It is likely this number will be restated in future reports as we identify more launches and additional ones are reported to Morningstar.

2 Based on SFDR data collected from prospectuses on 97.4% of funds available for sale in the EU, excluding money market funds, funds of funds, and feeder funds.

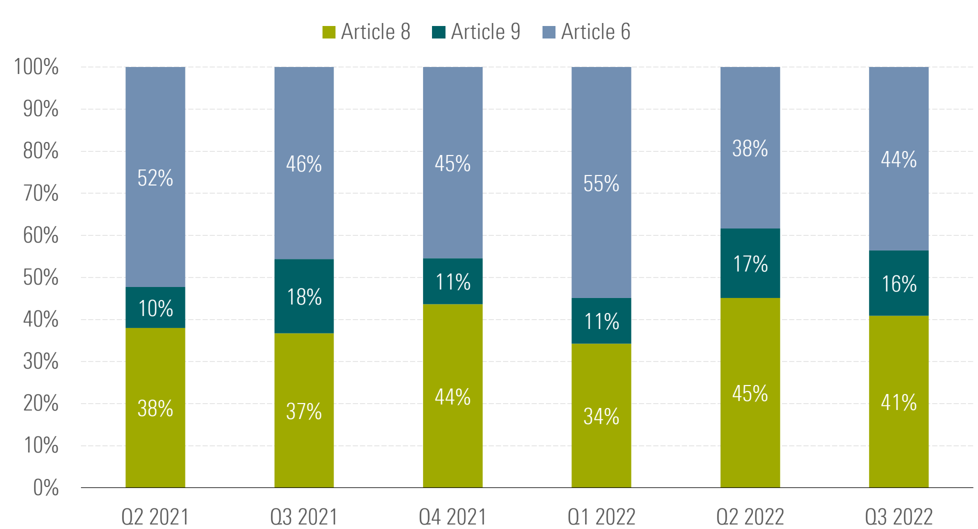
Exhibit 7 Quarterly Number of Fund Launches



Source: Morningstar Direct. Data as of Sept. 30, 2022. Based on SFDR data collected from prospectuses on 97.4% of funds available for sale in the EU, excluding money market funds, funds of funds, and feeder funds.

Compared with the second quarter, newly incepted Article 8 and Article 9 funds in the third quarter accounted for a smaller proportion of the overall new EU fund launches, but their market share remained above the 50% mark (56%).

Exhibit 8 Quarterly Breakdown of Fund Launches



Source: Morningstar Direct. Data as of Sept. 30, 2022. Based on SFDR data collected from prospectuses on 97.4% of funds available for sale in the EU, excluding money market funds, funds of funds, and feeder funds.

Asset managers continued to expand the range of Article 8 and Article 9 options available to investors in terms of asset class, market exposure, investment style, and theme. Equity remained the source of the greatest product proliferation with 98 new equity offerings, followed by fixed income and allocation, with 44 and 36, respectively. Alternatives, convertibles, and miscellaneous made up the rest.

While general ESG- and sustainability-focused offerings continued to account for the largest part of the product development activity, climate funds remained by far the most popular theme represented among new product launches. Thirty-four new funds with a climate flavor came to market[3], spanning all climate investment approaches. Climate-themed funds allow investors to reduce climate risk in portfolios and/or gain exposure to companies that will benefit from, or contribute to, the transition to a low-carbon economy. Nine were passive strategies tracking Paris-aligned benchmarks[4], including **Ossiam Bloomberg USA PAB ETF**, **SPDR MSCI Emerging Markets Climate Paris Aligned ETF**, and **Xtrackers Europe Net Zero Pathway Paris Aligned ETF**.

Other new sustainable products target a variety of environmental and social issues including biodiversity, healthy ecosystem, food security, and healthcare.

A record of four strategies launched with a focus on biodiversity, including **Fidelity Sustainable Biodiversity Fund**, **HSBC World ESG Biodiversity Screened Equity ETF**, **BNP Paribas Easy ESG Eurozone Biodiversity Leaders PAB**, and **AXA IM ACT Biodiversity Equity Fund**. The latter is a United Nations Sustainable Development Goals-aligned strategy primarily focused on companies offering solutions that address biodiversity loss, such as pollution on land and water, land degradation, fauna and flora protection, desertification, and overconsumption. The fund seeks to invest in companies across all sectors that support the targeted SDGs through the quality of their operations while minimizing negative biodiversity externalities.

Examples of socially focused products include **JPM Social Advancement**, **Nordea 1 - Global Social Solution**, and **Franklin European Social Leaders Bond Fund**.

The Great Reclassification: More Upgrades but Also More Downgrades

In the third quarter, asset managers continued to upgrade funds by enhancing ESG integration processes, adding binding ESG criteria (including carbon reduction objectives), or in some cases completely changing the mandate of the strategy.

Over the last quarter, we identified 383 funds that altered their SFDR status. 342 were upgrades, the vast majority (315) of which moved to Article 8 from Article 6, while seven upgraded to Article 9 from Article 6 and 20 funds reclassified to Article 9 from Article 8. Meanwhile, 41 downgraded to Article 8 from Article 9. We didn't identify downgrades to Article 6 from Article 8 or 9.

Exhibit 9 lists the largest funds that changed classification to Article 8 from Article 6.

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3 For more information on climate strategies, read Investing in Times of Climate Change - A Global View.

4 EU Paris-aligned benchmarks must have a carbon footprint (including scope 3 emissions) 50% below that of the investable universe. For EU climate-transition benchmarks, the carbon footprint only must be at least 30% lower. EU Paris-aligned benchmarks also employ additional activity exclusions on high-emitting fossil fuels and electricity producers, which EU climate-transition benchmarks do not have.

Exhibit 9 The 10 Largest Funds Upgraded to Article 8 From Article 6

Name	Old SFDR Fund Type	New SFDR Fund Type	AUM (EUR Million)	Morningstar Category	Active / Passive
BlackRock World Healthscience Fund	Article 6	Article 8	13,640	Sector Equity Healthcare	Active
BlackRock World Technology Fund	Article 6	Article 8	7,926	Sector Equity Technology	Active
UBS (Lux) Bond SICAV - Convert Global	Article 6	Article 8	4,108	Convertible Bond - Global, EUR Hgd	Active
BlackRock Sustainable Fixed Income Strategies Fund	Article 6	Article 8	3,850	Global Flexible Bond - EUR Hgd	Active
HSBC Global Government Bond	Article 6	Article 8	2,665	Global Bond - EUR Hgd	Active
BlackRock Next Generation Technology Fund	Article 6	Article 8	2,414	Sector Equity Technology	Active
PIMCO GIS Global Real Return Fund	Article 6	Article 8	2,371	Global Inflation-Linked Bond - EUR Hgd	Active
KBC Renta - Eurorenta	Article 6	Article 8	2,262	EUR Government Bond	Active
abdrn Asia Pacific Sustainable Equity	Article 6	Article 8	1,909	Asia-Pacific ex-Japan Equity	Active
Groupama Ultra Short Term Bond	Article 6	Article 8	1,787	EUR Ultra Short-Term Bond	Active

Source: Morningstar Research, Morningstar Direct. Data as of Sept. 30, 2022. Based on SFDR data collected from prospectuses on 97.4% of funds available for sale in the EU, excluding money market funds, funds of funds, and feeder funds.

Four BlackRock funds feature among the top 10 products that changed SFDR status to Article 8 from Article 6 in the third quarter, including three thematic funds, namely **BlackRock World Healthscience**, **BlackRock World Technology**, and **BlackRock Next Generation Technology**, which started applying BlackRock's EMEA baseline screens.

The ESG approach of **BlackRock Sustainable Fixed Income Strategies** goes a step further by seeking to enhance exposure to investments with positive externalities (that is, issuers with positive ESG credentials). The fund also seeks to reduce its carbon-emissions profile by allocating to green bonds, lower-carbon-emitting issuers, and issuers committed to decarbonization.

Another example of a large fund reclassified to Article 8 from Article 6 is **Aberdeen Asia Pacific Sustainable Equity Fund**, which aims to invest in sustainable leaders and improvers. In addition, the fund applies a set of company exclusions related to the United Nations Global Compact, Norges Bank Investment Management, weapons, tobacco, gambling, thermal coal, oil & gas, and electricity generation. The screen reduces the benchmark-investable universe by a minimum of 20%.

Exhibit 10 lists the largest funds that upgraded to Article 9 from Article 8 in the third quarter.

Allianz Global Water was one of them. According to its provider, the reclassification was the final step in a long process that saw the portfolio evolve over time to align with the Sustainable Development Goals. The fund invests in companies offering products or solutions that create positive environmental and social outcomes along water scarcity and quality issues.

Exhibit 10 The 10 Largest Funds Upgraded to Article 9 From Article 8

Name	Old SFDR Fund Type	New SFDR Fund Type	AUM (EUR Million)	Morningstar Category	Active / Passive
KBC Eco Fund - Water	Article 8	Article 9	1,087	Sector Equity Water	Active
Allianz Global Water	Article 8	Article 9	810	Sector Equity Water	Active
Fidelity Sust. Global Corp. Bond Paris-Align. Multifact. ETF	Article 8	Article 9	766	Global Corporate Bond	Active
Silver Autonomie	Article 8	Article 9	305	Global Large-Cap Growth Equity	Active
KBC Eco Fund - Alternative Energy	Article 8	Article 9	275	Sector Equity Alternative Energy	Active
Schroder US Smaller Companies Impact	Article 8	Article 9	268	US Small-Cap Equity	Active
UniInstitutional SDG Equities	Article 8	Article 9	267	Global Flex-Cap Equity	Active
AB Sustainable Euro High Yield Portfolio	Article 8	Article 9	267	EUR High Yield Bond	Active
Handelsbanken Latinamerika Tema	Article 8	Article 9	247	Latin America Equity	Active
GLS Alternative Investments - Mikrofinanzfonds	Article 8	Article 9	238	Other Bond	Active

Source: Morningstar Research. Morningstar Direct. Data as of Sept. 30, 2022. Based on SFDR data collected from prospectuses on 97.4% of funds available for sale in the EU, excluding money market funds, funds of funds, and feeder funds.

Meanwhile, **Fidelity Sustainable Global Corporate Bond Paris-Aligned Multifactor ETF** joined the growing list of passive funds that have switched to a Paris-aligned benchmark or a climate-transition benchmark from a broad ESG index. Both types of benchmarks are designed to be in line with the transition to a climate-resilient economy, while ensuring a yearly decarbonization target of at least 7%, in line with the decarbonization trajectory of the Intergovernmental Panel on Climate Change's 1.5˚C scenario[5].

Exhibit 11 lists funds that underwent more significant changes, as reflected by their reclassification to Article 9 from Article 6.

Exhibit 11 The 7 Funds Upgraded to Article 9 From Article 6

Name	Old SFDR Fund Type	New SFDR Fund Type	AUM (EUR Million)	Morningstar Category	Active / Passive
SEB Nordic Future Opportunity Fund	Article 6	Article 9	229	Nordic Equity	Active
TCW Emerging Markets Sustainable Income Fund	Article 6	Article 9	103	Global Emerging Markets Bond	Active
ACATIS Aktien Deutschland ELM	Article 6	Article 9	67	Germany Small/Mid-Cap Equity	Active
TCW High Yield Sustainable Bond Fund	Article 6	Article 9	55	USD High Yield Bond	Active
TCW Global Artificial Intelligence Sustainable Equity Fund	Article 6	Article 9	8	Sector Equity Technology	Active
TCW Select Sustainable Equities Fund	Article 6	Article 9	5	US Large-Cap Growth Equity	Active
TCW Relative Value Sustainable US Equities Fund	Article 6	Article 9	0.2	US Large-Cap Value Equity	Active

Source: Morningstar Research, Morningstar Direct. Data as of Sept. 30, 2022. Based on SFDR data collected from prospectuses on 97.4% of funds available for sale in the EU, excluding money market funds, funds of funds, and feeder funds.

TCW upgraded five strategies listed in the table above. In addition to the integration of ESG factors and sustainability risks, the funds seek to reduce the carbon intensity of the portfolios, employ exclusions, and proactively engage with issuers on ESG factors in order to improve sustainability practices and outcomes. TCW has developed a sustainability assessment framework based on the analysis of how

5 EU Paris-aligned benchmarks must have a carbon footprint (including scope 3 emissions) 50% below that of the investable universe. For EU climate-transition benchmarks, the carbon footprint only must be at least 30% lower. EU Paris-aligned benchmarks also employ additional activity exclusions on high-emitting fossil fuels and electricity producers, which EU climate-transition benchmarks do not have.

issuers' business activities align with several identified sustainability objectives, which is integrated into the investment process. The goal of this analysis is to provide a minimum threshold by which to assess whether an issuer is making a positive contribution to select environmental and social objectives, in addition to providing an assessment of governance that is broadly applicable.

Meanwhile, **ACATIS Aktien Deutschland ELM**, also among the few funds that upgraded their status to Article 9 from Article 6, primarily invests in German companies that contribute to at least one of the U.N. sustainable development goals.

Finally, we have identified 41 products that downgraded to Article 8 from Article 9 in the third quarter. These include funds from NN IP, Deka, AXA, and Neuberger Berman, among others. The exhibit below shows the 10 largest downgrades.

Exhibit 12 The 10 Largest Downgraded Funds

Name	Old SFDR Fund Type	New SFDR Fund Type	AUM (EUR Million)	Morningstar Category	Active/ Passive
NN Enhanced Index Sustainable Equity Fund A	Article 9	Article 8	2,913	Global Large-Cap Blend Equity	Active
Deka MSCI USA Climate Change ESG UCITS ETF	Article 9	Article 8	958	Sector Equity Ecology	Passive
NN Enhanced Index Sustainable Emerging Markets Equity F	Article 9	Article 8	939	Global Emerging Markets Equity	Active
AXA Optimal Income	Article 9	Article 8	924	EUR Flexible Allocation	Active
NN Enhanced Index Sustainable Equity Fund	Article 9	Article 8	905	Global Large-Cap Blend Equity	Active
Agipi Actions Monde	Article 9	Article 8	801	Global Large-Cap Growth Equity	Active
NN Enhanced Index Equity Sustainable Equity Fund DPF	Article 9	Article 8	652	Global Large-Cap Blend Equity	Active
Deka MSCI Europe Climate Change ESG ETF	Article 9	Article 8	586	Sector Equity Ecology	Passive
Agipi Actions Europe	Article 9	Article 8	567	Europe Large-Cap Blend Equity	Active
AXA Obligations Objectif Rendement Responsable	Article 9	Article 8	551	Global Flexible Bond - EUR Hedged	Active

Source: Morningstar Research. Morningstar Direct. Data as of Sept. 30, 2022. Based on SFDR data collected from prospectuses on 97.4% of funds available for sale in the EU, excluding money market funds, funds of funds, and feeder funds.

Some of these reclassifications emerged as a result of the combination of both the EC's June 2021 Q&A and the AFM's investigation announcement in September 2022 (see regulatory update at the end of the report). These specified that funds making Article 9 disclosures may only invest in sustainable investments based on the definition provided by Article 2 No. 17 of the Disclosure Regulation, with the exception of cash and assets used for hedging purposes.

NN IP was among the first asset managers in the second quarter to have notified fundholders that it would reclassify Article 9 funds into Article 8. After regulatory approval, NN IP downgraded 10 strategies in the third quarter and plans to downgrade 10 more in the fourth quarter.

Deka Investment downgraded seven climate ETFs, two of which features in the table above. **Deka MSCI Climate Change ESG Select ETFs** track benchmarks designed to reduce the carbon intensity of the portfolios in line with the EU Climate Transition Benchmark standard. Deka noted that the underlying indexes are not designed to include only sustainable investments as defined by SFDR; therefore, the funds couldn't keep their Article 9 classification, adding that the products would be classified again as

Article 9 if there is a clear statement from the regulator that CTB (and PAB) benchmarks qualify automatically for Article 9.

Although not featured in Exhibit 12, Neuberger Berman also changed the status of four Article 9 funds to Article 8, including **Neuberger Berman Global Sustainable Equity Fund** and **Neuberger Berman Systematic Global Sustainable Value Fund**, all for the same reason. Neuberger Berman noted that originally it "had set a minimum sustainable investment threshold of 80% for Article 9 funds. However, the EU Commission and European Supervisory Authorities recently indicated that Article 9 funds should only make sustainable investments (excluding investments required for collateral, liquidity or hedging purposes). Therefore, Article 9 funds must have a 100% threshold reached and maintained."

Meanwhile, AXA IM has downgraded 21 strategies to Article 8 from Article 9 in recent months and shared its plan to downgrade 24 more in the near future. AXA explained that "SFDR Level II calls for a stricter interpretation of Article 9 criteria. It was clarified that Article 9 products are those invested in assets qualifying as 'Sustainable Investments' only with exception to cash and assets used for hedging purposes. While the notion of Sustainable Investment is still subject to various interpretation and no guidance had been given so far by the European regulator, we have taken the proactive decision to act ahead of the implementation of SFDR Level II by reviewing the classification of our products."

Further, in late September, Robeco announced it would reclassify seven Article 9 strategies into Article 8, the largest two being **RobecoSAM Global SDG Credits** and **RobecoSAM Global SDG Engagement Equities**.[6] According to Robeco, these strategies can't be considered sustainable investments as per SFDR's definition as they invest in companies that may negatively contribute to the SDGs. These companies are targeted for their potential to improve their sustainability profile through engagement.

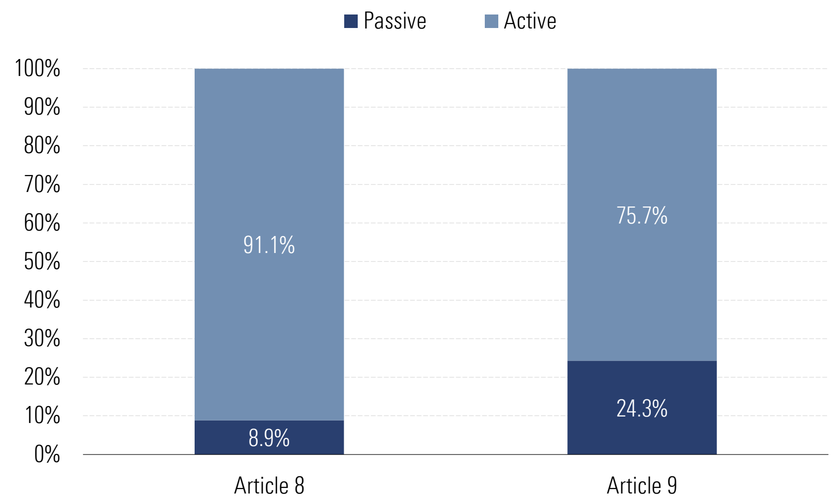
In light of all these recent developments and in expectation of further downgrades, we can expect the number of Article 9 products to decline in the next six months from its current level of 1,080 funds (representing 4.3% of funds distributed in the EU).

6 The seven Robeco funds are not included in third-quarter reclassified fund numbers, as their reclassification hasn't been implemented yet.

Passive Funds Account for Almost a Fourth of Article 9 Funds

Meanwhile, passive funds continued to gain ground in both Article 8 and Article 9 categories, reaching 8.9% and 24.3%, respectively, at the end of September, from 8.7% and 23.0% three months earlier.

Exhibit 13 Market Share of Active and Passive Funds Classified as Article 8 and Article 9



Source: Morningstar Direct. Data as of Sept. 30, 2022. Based on SFDR data collected from prospectuses on 97.4% of funds available for sale in the EU, excluding money market funds, funds of funds, and feeder funds.

The larger market share for passive Article 9 funds can be partly explained by the growing number of sizable index funds and ETFs tracking EU Climate benchmarks. Such strategies currently account for about EUR 75 billion, or 18% of overall Article 9 fund assets. But as asset managers follow in Deka's footsteps and start reclassifying their Paris-aligned and climate transition benchmark-tracking products as Article 8 in the coming months, we can expect the market share for passive Article 9 funds to drop.

The Largest Article 8 and Article 9 Funds

Despite the backdrop of market turbulences, the league tables of the largest Article 8 and Article 9 funds have remained stable over the last quarter.

The EUR 13.6 billion **BlackRock World Healthscience Fund** made its entrance in the top 20 Article 8 funds after being upgraded (see section on reclassified funds).

Exhibit 14 The 20 Largest Article 8 Funds

Name	SFDR Fund Type	Morningstar Global Category	AUM (EUR Billion)	Active / Passive	Morningstar Sustainability Rating
Flossbach von Storch - Multiple Opportunities	Article 8	EUR Flexible Allocation - Global	23.9	Active	🌐🌐🌐
Morgan Stanley Global Brands Fund	Article 8	Global Large-Cap Blend Equity	19.3	Active	🌐🌐🌐🌐🌐
DWS Top Dividende	Article 8	Global Equity Income	19.2	Active	🌐🌐
Deka-ImmobilienEuropa	Article 8	Property - Direct Europe	17.8	Active	—
hausInvest	Article 8	Property - Direct Europe	17.4	Active	—
AB American Income Portfolio	Article 8	USD Flexible Bond	15.9	Active	—
BlackRock World Healthscience Fund	Article 8	Sector Equity Healthcare	13.6	Active	🌐🌐🌐🌐
AB Global High Yield Portfolio	Article 8	Global High Yield Bond	13.6	Active	—
DWS Concept Kaldemorgen	Article 8	EUR Flexible Allocation - Global	13.6	Active	🌐🌐🌐🌐
Fidelity Funds - Global Technology Fund	Article 8	Sector Equity Technology	12.4	Active	🌐🌐🌐
Flossbach von Storch - Multiple Opportunities II	Article 8	EUR Flexible Allocation - Global	12.3	Active	🌐🌐🌐
Findlay Park American Fund ICAV	Article 8	US Large-Cap Growth Equity	11.0	Active	🌐🌐🌐🌐
DWS Vermögensbildungsfonds I	Article 8	Global Large-Cap Blend Equity	10.6	Active	🌐🌐🌐
Muzinich Enhancedyield Short-Term Fund	Article 8	Global Flexible Bond - EUR Hedged	10.6	Active	🌐🌐
JPMorgan Income Fund	Article 8	USD Flexible Bond	10.0	Active	—
Mercer Multi Asset Growth Fund	Article 8	GBP Allocation 60-80% Equity	9.9	Active	🌐🌐🌐🌐
grundbesitz europa	Article 8	Property - Direct Europe	9.9	Active	—
Fidelity Global Dividend Fund	Article 8	Global Equity Income	9.8	Active	🌐🌐🌐🌐🌐
WestInvest InterSelect	Article 8	Property - Direct Europe	9.5	Active	—
M&G (Lux) Optimal Income Fund	Article 8	EUR Cautious Allocation - Global	9.3	Active	🌐🌐🌐

Source: Morningstar Direct. Data as of Sept. 30, 2022. Based on SFDR data collected from prospectuses on 97.4% of funds available for sale in the EU, excluding money market funds, funds of funds, and feeder funds.

Exhibit 15 The 20 Largest Article 9 Funds

Name	SFDR Fund Type	Morningstar Global Category	AUM (EUR Billion)	Active / Passive	Morningstar Sustainability Rating
Pictet-Global Megatrend Selection	Article 9	Global Flex-Cap Equity	10.7	Active	🌐🌐🌐
iShares MSCI USA ESG Enhanced ETF	Article 9	US Large-Cap Blend Equity	10.0	Passive	🌐🌐🌐🌐
Nordea 1 - Global Climate and Environment Fund	Article 9	Sector Equity Ecology	9.5	Active	🌐🌐🌐🌐
Pictet-Water	Article 9	Sector Equity Water	8.1	Active	🌐🌐🌐🌐
Pictet - Global Environmental Opportunities	Article 9	Sector Equity Ecology	7.4	Active	🌐🌐🌐🌐🌐
BlackRock Sustainable Energy Fund	Article 9	Sector Equity Alternative Energy	5.9	Active	🌐🌐🌐🌐🌐
iShares Global Clean Energy ETF	Article 9	Sector Equity Alternative Energy	5.8	Passive	🌐🌐🌐🌐
Handelsbanken Global Index Criteria	Article 9	Global Large-Cap Blend Equity	5.3	Passive	🌐🌐🌐
Pictet-Clean Energy	Article 9	Sector Equity Alternative Energy	4.4	Active	🌐🌐🌐🌐🌐
Amundi MSCI USA SRI PAB	Article 9	US Large-Cap Blend Equity	4.3	Passive	🌐🌐🌐🌐🌐
Mirova Global Sustainable Equity Fund	Article 9	Global Large-Cap Growth Equity	3.9	Active	🌐🌐🌐🌐🌐
Handelsbanken USA Index Criteria	Article 9	US Large-Cap Blend Equity	3.7	Passive	🌐🌐🌐🌐
BNP Paribas Funds Aqua	Article 9	Sector Equity Water	3.3	Active	🌐🌐🌐
Handelsbanken Hållbar Energi	Article 9	Sector Equity Alternative Energy	3.2	Active	🌐🌐🌐🌐
RobecoSAM Smart Energy Equities	Article 9	Sector Equity Alternative Energy	3.2	Active	🌐🌐🌐🌐🌐
RobecoSAM Sustainable Water Equities	Article 9	Sector Equity Water	3.1	Active	🌐🌐🌐🌐
BNP Paribas Aqua	Article 9	Sector Equity Water	3.1	Active	🌐🌐🌐
DPAM L - Bonds Emerging Markets Sustainable	Article 9	Global EM Bond - Local Currency	3.0	Active	🌐🌐🌐🌐
Amundi Index MSCI World SRI PAB	Article 9	Global Large-Cap Blend Equity	3.0	Passive	🌐🌐🌐🌐🌐
AB Sustainable Global Thematic Portfolio	Article 9	Global Large-Cap Growth Equity	3.0	Active	🌐🌐🌐🌐

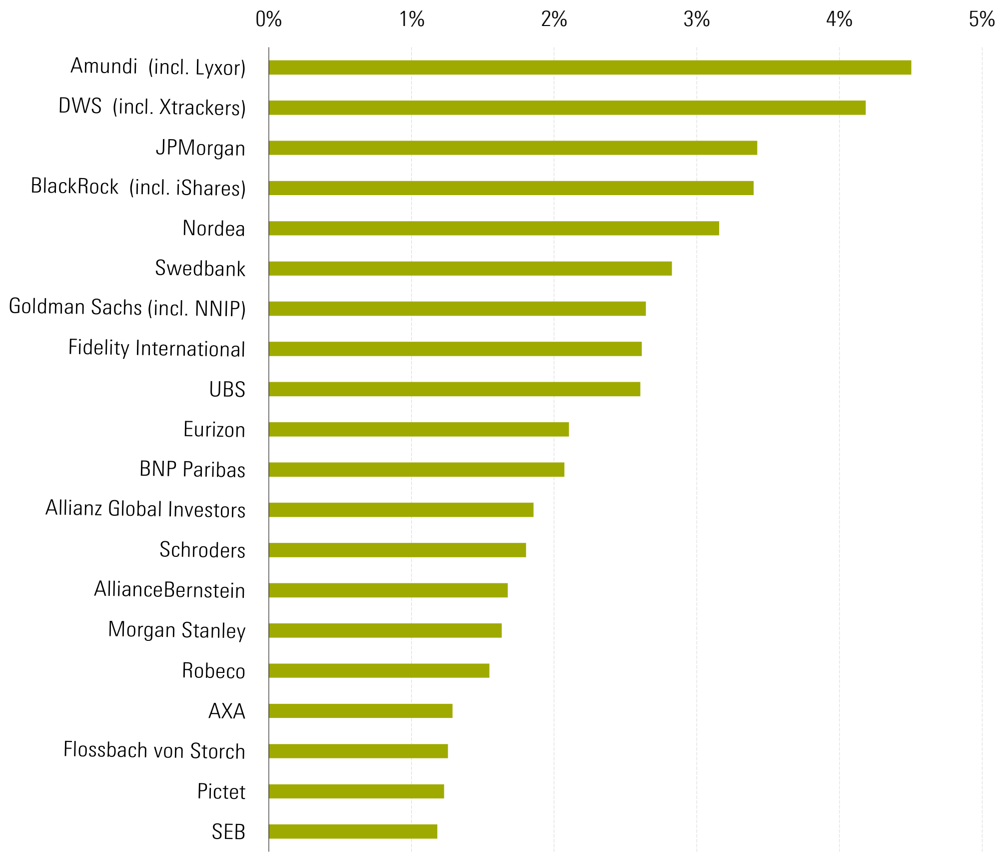
Source: Morningstar Direct. Data as of Sept. 30, 2022. Based on SFDR data collected from prospectuses on 97.4% of funds available for sale in the EU, excluding money market funds, funds of funds, and feeder funds.

The leaderboard of Article 9 funds is well staffed with products focused on the environment and themes such as renewable energy, climate transition, and water.

Provider League Tables

Exhibits 16 and 17 show the 20 asset managers with the highest market share in Article 8 and Article 9 funds, ranked by assets in Article 8 and Article 9 funds, respectively.

Exhibit 16 Top 20 Asset Managers by Article 8 Fund Assets

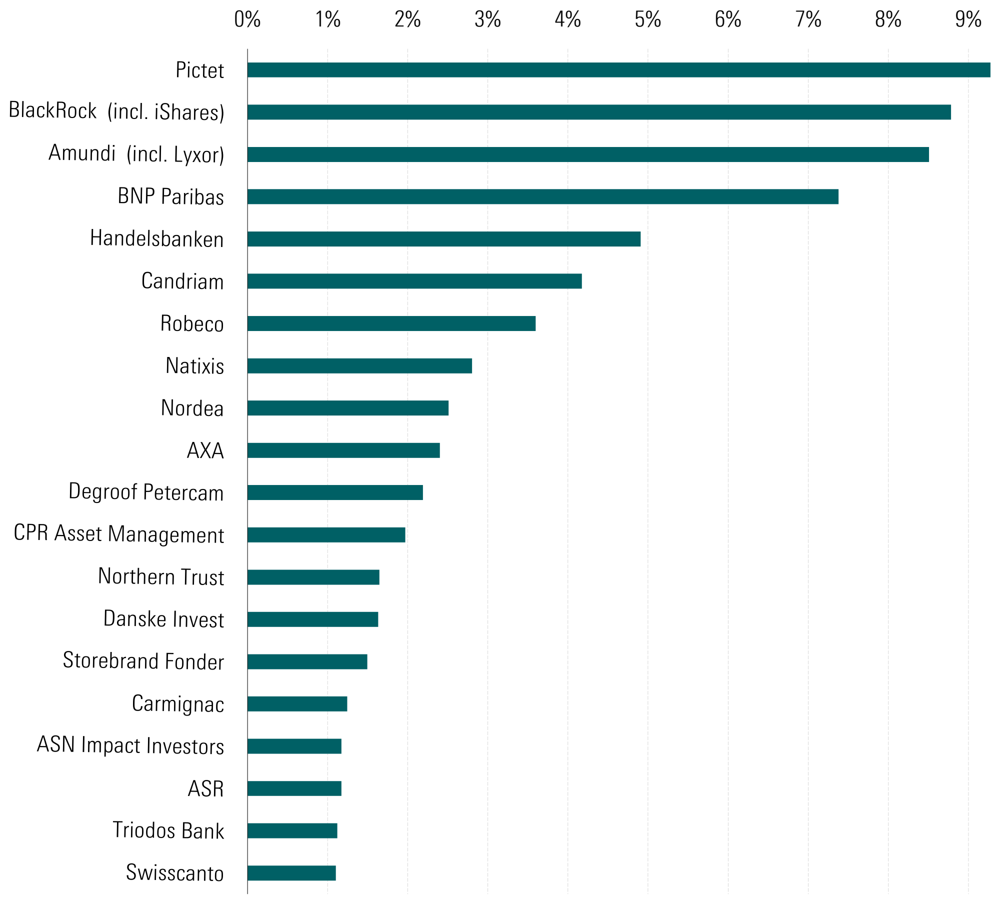


Source: Morningstar Direct. Data as of Sept. 30, 2022. Based on SFDR data collected from prospectuses on 97.4% of funds available for sale in the EU, excluding money market funds, funds of funds, and feeder funds. Using Branding Name in Morningstar Direct, a manager's market share is calculated as following: manager's Article 8 fund assets divided by total market Article 8 fund assets.

At the end of September, Amundi, DWS, and JPMorgan remained the top three managers of Article 8 products, while BlackRock moved up to the fourth position (from the ninth at the end of June).

BlackRock moved up the rank in the Article 9 league table, too, bypassing both BNP Paribas and Amundi to land in second position, right on the heels of Pictet.

Exhibit 17 Top 20 Asset Managers by Article 9 Fund Assets



Source: Morningstar Direct. Data as of Sept. 30, 2022. Based on SFDR data collected from prospectuses on 97.4% of funds available for sale in the EU, excluding money market funds, funds of funds, and feeder funds. Using Branding Name in Morningstar Direct, a manager's market share is calculated as following: manager's Article 9 fund assets divided by total market Article 9 fund assets.

Article 8 and Article 9 Funds Through the Lens of the European ESG Template

Since Aug. 2, 2022, the amended MiFID II requires financial advisors to consider clients' sustainability preferences when conducting suitability assessments. If clients express interest in making sustainable investments, advisors will have to accommodate. Depending on the specific client's preferences, advisors will have to source products that have a minimum proportion of sustainable investments as defined by the Sustainable Finance Disclosure Regulation or the EU Taxonomy. Clients may also choose only investments that consider principal adverse impacts, or PAIs.

To facilitate this process, a new European environmental, social, and governance template, or EET, has been developed by industry representatives (FinDatEx) to ease the exchange of data between asset managers and distributors. Asset managers marketing their funds in the European Union started to submit EET data on a voluntary basis from June 1.

As of Oct. 13, Morningstar collected EET data on 87,229 share classes, accounting for 61% of all share classes in scope of MiFID II. These represent 17,084 funds[7], including 7,169 Article 8 funds and 886 Article 9 funds[8].

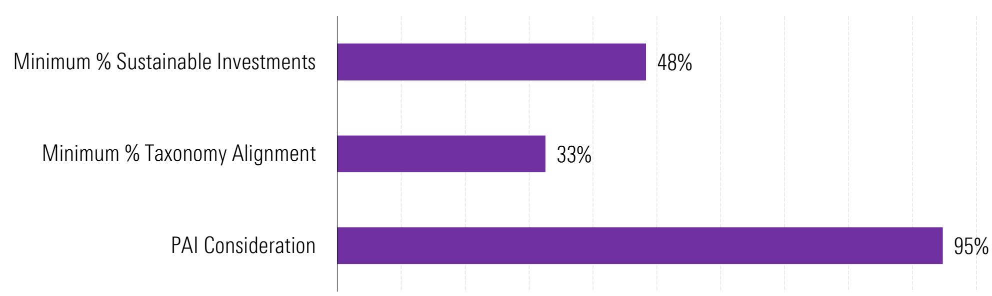
In this section, we share insights on the coverage and values of the following three EET fields, as featured in the Morningstar Direct database, namely:

1) **Principal Adverse Impact Consideration**, indicating if a product considers Principle Adverse Impact in its investments. Answers are "Yes" or "No."[9]
2) **EU Sustainable Finance Disclosure Regulation Minimum or Planned Investments Sustainable Investments**, representing the minimum percentage of portfolio investments that are deemed sustainable but are not taxonomy-aligned. Answers are numerical values.[10]
3) **EU Sustainable Finance Disclosure Regulation Minimum or Planned Investments Sustainable Investments Taxonomy Aligned**, representing the minimum percentage of the portfolio that are aligned with the EU Taxonomy. Answers are numerical values.[11]

We also discuss the challenges that asset managers will face when selecting suitable products for clients given the patchiness of the data available to them and the lack of comparability between products caused by the different approaches taken by asset managers to calculate sustainable investment and taxonomy-alignment exposure.

Exhibit 18 shows the coverage of these three fields for the surveyed Article 8 and Article 9 funds.

Exhibit 18 Coverage of Key EET Data Points for the Surveyed Article 8 and Article 9 Funds



Source: Morningstar Direct. Data as of Oct. 13. Based on 7,169 and 886 reported as Article 8 and Article 9 products, respectively.

7 The number of funds and share classes estimated to be in scope of the EET is 38,330 and 143,179, respectively. Money market funds, funds of funds, and feeder funds are included in this section on the EET.

8 As of July 18, Morningstar had collected SFDR data types for 30,060 funds based on fund prospectuses, including 10,462 Article 8 and Article 9 funds.

9 EET Name: 20100_Financial_Instrument_Does_This_Product_Consider_Principle_Adverse_Impact_In_Their_Investment

10 EET Name: 20420_Financial_Instrument_EU_SFDR_Minimum_Or_Planned_Investments_Sustainable_Investments

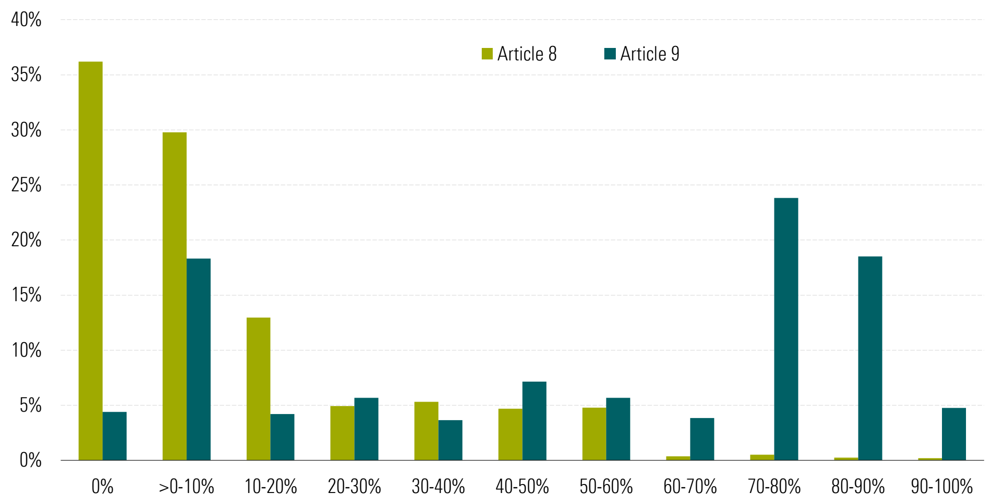
11 EET Name: 20450_Financial_Instrument_EU_SFDR_Minimum_Or_Planned_Investments_Sustainable_Investments_Taxonomy_Aligned

All Article 8 and Article 9 products are required to disclose whether or not they consider principal adverse impact indicators, explaining the high percentage of 95% of surveyed funds that populated the PAI consideration field mid-October. However, fewer than half (48%) of the surveyed Article 8 and Article 9 funds reported a minimum percentage of sustainable investments and only one third disclosed a minimum percentage of taxonomy-aligned investments.

Minimum Proportion of Sustainable Investments

Exhibit 19 shows the distribution of the surveyed Article 8 and Article 9 funds that reported the field.

Exhibit 19 Minimum % of Sustainable Investments for Article 8 and Article 9 Funds



Source: Morningstar Direct. Data as of Oct. 13, 2022. Based on 3.345 Article 8 funds and 546 Article 9 funds that report the field.

Since mid-July, the distribution of Article 8 funds' minimum exposure to sustainable investments hasn't changed much. We note a similar level of Article 8 funds (36%) with 0%-values; a slight increase in Article 8 funds targeting between 0% and 10% exposure (30% versus 25% in July) and in those targeting an allocation greater than 50% (6.1% versus 3.8% in July).

Meanwhile, surprisingly, Article 9 have decreased their targeted exposure to sustainable investments. Only 47.1% of Article 9 products now plan to have more than 70% exposure to sustainable investments, compared with 55.7% three months ago, while 43.4% of Article 9 funds (up from 39.4%) target less than 50% of sustainable investments.

That said, a higher number of Article 9 funds now target between 90% and 100%: 4.8%, compared with just 2.3% mid-July. As of Oct. 13, we identified only 26 Article 9 funds targeting 100% exposure to sustainable investment, up from eight.

The exhibit below shows the 20 Article 8 products with the highest minimum exposures to sustainable investments ranked by fund size.

Exhibit 20 Top 20 Article 8 Funds by Minimum or Planned Investments Sustainable Investments

Fund Name	SFDR Type	Min % of Sustainable Investments	Fund Size (Euro Mil)	Morningstar Category	Broad Category
Scandinavian Credit Fund I AB (publ)	Article 8	100	290	Other Bond	Fixed Income
GP Bullhound Global Technology Fund	Article 8	100	39	Sector Equity Technology	Equity
GP Bullhound Thyra Hedge	Article 8	100	1	Long/Short Equity - Global	Equity
La Française Euro Souverains	Article 8	96	8	EUR Government Bond - Short Term	Fixed Income
Aegon Global Sustainable Sovereign Bond Fund	Article 8	95	96	Global Bond - EUR Hedged	Fixed Income
La Française Obligations LT	Article 8	95	60	EUR Diversified Bond	Fixed Income
AEAM Global Sustainable Real Estate Fund	Article 8	95	20	Property - Indirect Global	Equity
ODDO BHF Artificial Intelligence	Article 8	90	219	Sector Equity Technology	Equity
Aegon Global Sustainable Diversified Growth Fund	Article 8	90	10	EUR Flexible Allocation - Global	Allocation
WI Immobilienaktien EMEA ESG TX	Article 8	89	24	Property - Indirect Europe	Equity
WI Immobilienaktien Asia Pacific ESG TX	Article 8	88	26	Property - Indirect Asia	Equity
WI Immobilienaktien America ESG TX	Article 8	86	36	Property - Indirect North America	Equity
HSBC Global Sustainable Government Bond Index Fund	Article 8	85	369	Global Bond - USD Hedged	Fixed Income
La Française Trésorerie ISR	Article 8	81	3,110	EUR Money Market	Money Market
WI Aktien Europe ESG Leaders T	Article 8	81	30	Europe Large-Cap Blend Equity	Equity
Brown Advisory US Sustainable Growth Fund	Article 8	80	3,196	US Large-Cap Growth Equity	Equity
Brown Advisory Global Leaders Fund	Article 8	80	2,229	Global Large-Cap Growth Equity	Equity
UBS Sustainable Development Bank Bonds ETF	Article 8	80	1,842	USD Government Bond	Fixed Income
Aegon Global Sustainable Equity Fund	Article 8	80	407	Global Flex-Cap Equity	Equity
Brown Advisory Global Leaders Sustainable Fund	Article 8	80	130	Global Large-Cap Growth Equity	Equity

Source: Morningstar Direct. Data as of Oct. 13, 2022. Based on 3.345 Article 8 funds that report the field. Funds are ranked first by sustainable-investment exposure and second by fund size.

Topping the list are three funds that reported minimum sustainable-investment allocations of 100%, which may come as a surprise as one would typically expect to see such a high level of targeted sustainable-investment exposure in the Article 9 category. Among the three strategies is **Scandinavian Credit Fund**, which offers short-term direct lending to small and medium-size companies that need to finance expansion, investment, restructuring, refinancing, generational financing, or seasonal needs. The investee companies are selected based on a combination of positive and negative screening, compliance with international standards, and active ownership criteria where applicable.

The rest of the table includes strategies with similarly high targeted exposure to sustainable investments. For example, **ODDO BHF Artificial Intelligence Biotech** and **Brown Advisory US Sustainable Growth Fund** reported minimum sustainable-investment allocations of 90% and 80%, respectively.

Exhibit 21 lists the 20 Article 9 funds with the highest minimum exposures to sustainable investments ranked by fund size. These are among the 26 funds that, as of Oct. 13, reported 100% exposure to sustainable investments. While representing an improvement over our July number of eight, 26 remains low, raising questions about the feasibility of funds exclusively aiming sustainable investments as interpreted by AFM and certain market participants. These percentages are in any case difficult to gauge given the different interpretations made by asset managers of the definition of a "sustainable investment" as well as the different methodologies used to calculate exposure to sustainable investments, as we will see in more detail in the next section.

Exhibit 21 Top 20 Article 9 Funds by Minimum or Planned Investments Sustainable Investments

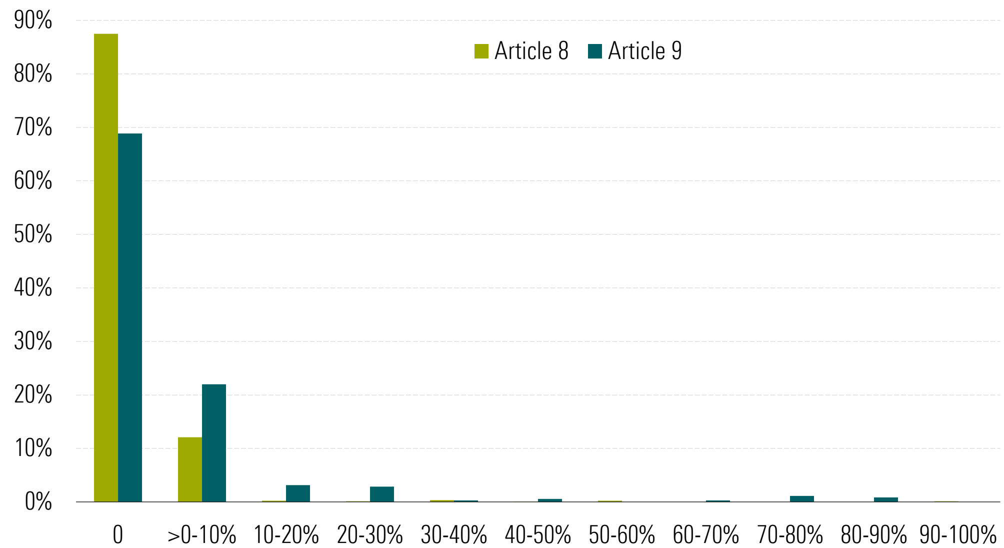
Fund Name	SFDR Type	Min % of Sustainable Investments	Fund Size (Euro Mil)	Morningstar Category	Broad Category
ÖkoWorld ÖkoVision Classic	Article 9	100	2,004	Sector Equity Ecology	Equity
ÖkoWorld Klima	Article 9	100	698	Sector Equity Ecology	Equity
ÖkoWorld Growing Markets 2.0	Article 9	100	304	Global EM Small/Mid-Cap Equity	Equity
ÖkoWorld Rock 'n' Roll Fonds	Article 9	100	298	EUR Flexible Allocation - Global	Allocation
DNCA Invest Beyond Semperosa	Article 9	100	274	Europe Large-Cap Growth Equity	Equity
La Française LUX - Inflection Point Carbon Impact Global	Article 9	100	255	Global Large-Cap Blend Equity	Equity
JPMorgan Climate Change Solutions Fund	Article 9	100	222	Sector Equity Ecology	Equity
La Française Carbon Impact Floating Rates	Article 9	100	175	EUR Corporate Bond - Short Term	Fixed Income
Symphonia Lux SICAV – Electric Vehicles Revolution	Article 9	100	105	Sector Equity Technology	Equity
Prima Global Challenges	Article 9	100	99	Sector Equity Ecology	Equity
La Française Obligations Carbon Impact	Article 9	100	97	EUR Diversified Bond	Fixed Income
EB-Öko-Aktienfonds	Article 9	100	97	Sector Equity Ecology	Equity
La Française Actions Euro Capital Humain	Article 9	100	88	Eurozone Large-Cap Equity	Equity
DNCA Invest Beyond Climate	Article 9	100	84	Sector Equity Ecology	Equity
Oaktree Oaktree Global High Yield Responsible Fund	Article 9	100	67	Global High Yield Bond - GBP Hedged	Fixed Income
La Française Carbon Impact 2026	Article 9	100	63	Fixed Term Bond	Fixed Income
ÖkoWorld Water Life	Article 9	100	62	Sector Equity Water	Equity
BlueBay Impact-Aligned Bond Fund	Article 9	100	35	Global Corporate Bond - GBP Hedged	Fixed Income
La Française Green Tech Europe	Article 9	100	31	Eurozone Large-Cap Equity	Equity
La Française LUX - Inflection Point Carbon Impact Euro	Article 9	100	26	Eurozone Large-Cap Equity	Equity

Source: Morningstar Direct. Data as of Oct. 13, 2022. Based on 546 Article 9 funds that report the field. Funds are ranked first by sustainable-investment exposure and second by fund size.

Minimum Proportion of Taxonomy-Aligned Investments

As previously mentioned, the number of surveyed Article 8 and Article 9 funds that reported minimum sustainable investment exposure as defined under the EU Taxonomy remains small. Although up from 27% in mid-July, only 33% populated the **Minimum or Planned Investments Sustainable Investments Taxonomy Aligned** field by mid-October. Exhibit 22 shows the distribution of reported values.

Exhibit 22 Minimum % of Taxonomy-Aligned Sustainable Investments for Article 8 and Article 9 Funds



Source: Morningstar Direct. Data as of July 18, 2022. Based on 2.282 Article 8 funds and 350 Article 9 funds that report the field.

Unsurprisingly, 0%-values account for the overwhelming majority of the responses received (88% for Article 8 funds and 69% for Article 9 funds), while just over 22% of Article 9 funds (up from 17.0% three months ago) reported minimum taxonomy-aligned sustainable investments between 0% and 10%. Very few Article 9 funds, only 3% (up from 2.2% earlier), target exposure higher than 10%. Eleven funds reported exposure higher than 60%. These low figures can be explained by the fact that issuers will only start disclosing their level of taxonomy-alignment in 2023 and that, in the meantime, European Supervisory Authorities have pushed asset managers to be conservative in their taxonomy disclosure (for example, by not allowing the use of estimates).

Exhibit 23 features the 20 Article 8 funds with the highest level of taxonomy-alignment ranked by fund size. We are seeing again a few WI strategies at the top, with taxonomy-aligned sustainable investments as high as 30%. But very quickly the proportions fall to below 10%. Only seven Article 8 products reported exposure of 10% or greater.

Exhibit 23 Top 20 Article 8 Funds by Minimum % of Taxonomy-Aligned Investments

Fund Name	SFDR Type	Min % of Taxonomy Aligned Sustainable Investments	Fund Size (EURO Mil)	Morningstar Category	Broad Category
WI Immobilienaktien Asia Pacific ESG TX	Article 8	30	26	Property - Indirect Asia	Equity
WI Immobilienaktien EMEA ESG TX	Article 8	23	24	Property - Indirect Europe	Equity
Assenagon Credit Selection ESG	Article 8	20	257	EUR Flexible Bond	Fixed Income
R-co Thematic Real Estate	Article 8	20	169	Property - Indirect Eurozone	Equity
3 Banken Mensch & Umwelt Mischfonds	Article 8	15	192	EUR Moderate Allocation - Global	Allocation
WI Immobilienaktien America ESG TX	Article 8	12	36	Property - Indirect North America	Equity
WI Global Challenges Index-Fonds	Article 8	11	364	Global Large-Cap Blend Equity	Equity
WERTGRUND WohnSelect D	Article 8	10	457	Property - Direct Europe	Property
Assenagon Funds Value Size Global	Article 8	10	377	Global Flex-Cap Equity	Equity
R-co Opal 4Change Sustainable Trends	Article 8	10	84	Global Flex-Cap Equity	Equity
Assenagon Asymmetric Beta US	Article 8	8	34	US Large-Cap Blend Equity	Equity
3 Banken Mensch & Umwelt Aktienfonds	Article 8	7	191	Sector Equity Ecology	Equity
Assenagon Funds Substanz Europa	Article 8	6	80	Europe Equity Income	Equity
HSBC Global Sustainable Long Term Dividend	Article 8	5	38	Global Equity Income	Equity
hausInvest	Article 8	5	17,361	Property - Direct Europe	Property
Pictet Global Utilities Equity	Article 8	5	7812	Sector Equity Utilities	Equity
RMM Trésorerie	Article 8	5	1150	EUR Money Market	Money Market
HSBC Global Equity Climate Change	Article 8	5	268	EUR Money Market	Money Market
R-co Valor Bond Opportunities	Article 8	5	242	EUR Money Market	Money Market
Oddo BHF Immobilier	Article 8	5	204	EUR Money Market	Money Market

Source: Morningstar Direct. Data as of Oct. 13, 2022. Based on 2.282 Article 8 funds that report the field.

Exhibit 24 features the 20 Article 9 funds with the highest proportions of taxonomy-aligned sustainable investments. Unsurprisingly, most focus on an environmental theme such as climate, alternative energy, and water. The strategies with the highest taxonomy-alignment are fixed-income strategies investing in green bonds and other types of "impact" bonds for which it is easier to evidence the contribution to environmental objectives.

Exhibit 24 Top 20 Article 9 Funds by Minimum % of Taxonomy-Aligned Investments

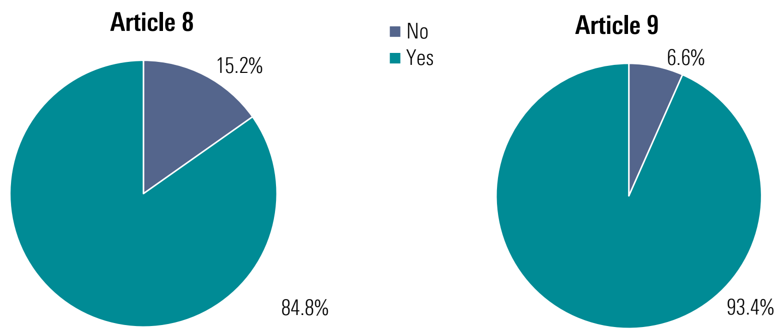
Fund Name	SFDR Type	Min % of Taxonomy Aligned Sustainable Investments	Fund Size (EURO Mil)	Morningstar Category	Broad Category
Triodos Energy Transition Europe Fund	Article 9	90	184	Other	Miscellaneous
Triodos Emerging Markets Renewable Energy Fund	Article 9	90	35	Other Allocation	Allocation
Sustainable Alpha Fund	Article 9	90	10	EUR Aggressive Allocation - Global	Allocation
KlimaVest ELTIF	Article 9	75	959	Other Allocation	Allocation
Luxembourg Selection Fund Active Solar	Article 9	75	239	Sector Equity Alternative Energy	Equity
R-co 4Change Green Bonds	Article 9	75	105	Global Corporate Bond - EUR Hedged	Fixed Income
Federal Global Green Bonds	Article 9	75	46	Global Bond	Fixed Income
Assenagon Funds Green Economy	Article 9	65	25	Sector Equity Ecology	Equity
Xtrackers USD Corporate Green Bond ETF	Article 9	50	234	USD Corporate Bond	Fixed Income
Xtrackers EUR Corporate Green Bond ETF	Article 9	50	151	EUR Corporate Bond	Fixed Income
Triodos Groenfonds	Article 9	33	887	Other Bond	Fixed Income
Pictet-Clean Energy	Article 9	25	4,261	Sector Equity Alternative Energy	Equity
Raiffeisen-SmartEnergy-ESG-Aktien	Article 9	25	315	Sector Equity Alternative Energy	Equity
GAM Sustainable Climate Bond	Article 9	25	17	EUR Subordinated Bond	Fixed Income
AB SICAV I - Sustainable Climate Solutions Portfolio	Article 9	25	1	Sector Equity Ecology	Equity
Arabesque SICAV - Global Climate Pathway Equity	Article 9	25	1	Global Large-Cap Blend Equity	Equity
ÖkoWorld ÖkoVision Classic	Article 9	21	2,004	Sector Equity Ecology	Equity
ÖkoWorld Klima	Article 9	21	698	Sector Equity Ecology	Equity
ÖkoWorld Growing Markets 2.0	Article 9	21	304	Global Emerging Markets Small/Mid-Cap Equity	Equity
ÖkoWorld Rock 'n' Roll Fonds	Article 9	21	298	EUR Flexible Allocation - Global	Allocation

Source: Morningstar Direct. Data as of Oct. 13, 2022. Based on 350 Article 9 funds that report the field.

PAI Consideration

As previously mentioned, around 95% of surveyed Article 8 and Article 9 funds in mid-October populated the Principal Adverse Impact Consideration field, showing significant improved coverage of the data field since mid-July (43%). And among those, the vast majority stated they do consider PAIs (85% for the respondent Article 8 funds and 93% for the respondent Article 9 funds), although it may come as a surprise that not all Article 9 funds do. As shown below, 6.6% of Article 9 do not consider PAIs.

Exhibit 25 SFDR Product Type and PAI Consideration



Source: Morningstar Direct. Data as of Oct. 13, 2022. Based on 6,897 Article 6 funds, 6.786 Article 8 funds, and 845 Article 9 funds that reported the field.

PAI indicators are intended to show investors what adverse impacts a financial product may have on sustainability factors relating to environmental, social, and employee matters, respect for human rights, anticorruption, and antibribery matters.

Exhibit 26 shows a sample of the PAIs that product manufacturers should disclose using the EET. The EET data fields cover the 64 PAI indicators designed under SFDR. The sample here includes 14 PAI indicators for corporates, two for sovereigns, and two for real estate assets.

Exhibit 26 18 of the 64 PAI Indicators Under the EET

Corporate		
Greenhouse gas emissions	1	GHG emissions
	2	Carbon footprint
	3	GHG intensity of investee companies
	4	Exposure to companies active in the fossil fuel sector
	5	Share of nonrenewable energy consumption and production
	6	Energy consumption intensity per high impact climate sector
Biodiversity	7	Activities negatively affecting biodiversity-sensitive areas
Water	8	Emissions to water
Waste	9	Hazardous waste ratio
Social and employee matters	10	Violations of the UNGC principles and OECD Guidelines for Multinational Enterprises
	11	Lack of processes and compliance mechanisms to monitor compliance
	12	Unadjusted gender pay gap
	13	Board gender diversity
	14	Exposure to controversial weapons
Sovereign and supranational		
Environmental	15	GHG intensity of investee countries
Social	16	Number of investee countries subject to social violations
Real estate		
Fossil fuels	17	Exposure real estate assets involved in the extraction, storage, transport of fossil fuels
Energy efficiency	18	Exposure to energy-inefficient real estate assets

Source: SFDR delegated regulation-annex I.

Exhibit 27 shows the percentages of surveyed Article 8 and Article 9 funds that consider a sample of PAIs.

Exhibit 27 Consideration Levels for a Sample of PAIs

Source: Morningstar Direct. Data as of Oct. 13, 2022. The exact numbers for Article 8 and Article 9 funds that reported each of the data fields vary.

The exhibit reveals a wide range of PAI consideration, with the most considered PAIs, including "controversial weapons" and "UNGC principles or OECD guidelines violations," showing high consideration rates (97% and 94%, respectively, for Article 9 funds), while the two least considered PAIs, namely "exposure to energy-efficient real estate assets" and "exposure to fossil fuels extraction, storage, transport & manufacture," exhibit consideration rates of less than 16%.

As expected, environmental impacts such as greenhouse gas emissions, carbon footprint and intensity, as well as fossil fuel exposure, are currently being considered by more funds than social impact indicators such as gender pay gap and board gender diversity.

It may come as a surprise to some that no PAI achieve a consideration rate of 100% and that not all Article 9 funds consider all PAIs given the definition of “sustainable investment” by SFDR and the "do not significantly harm" requirement that apply. This can be explained, as we will see in the next section, by the different interpretations that asset managers have taken of the definition of "sustainable investment" and the fact that they have set their own criteria for assessing "significant harm" to a sustainability objective. While some managers are indeed considering all PAIs for their Article 9 funds, others have taken a selective approach and are considering only the most relevant indicators for their strategies.

In a recent letter, the European Supervisory Authorities asked the European Commission to clarify what “considering principal adverse impacts” means, as it currently can be interpreted as simply disclosing PAIs or taking action to address the adverse impacts.

Different Approaches to Calculating Sustainable-Investment Exposure

In this section, we discuss the challenges faced by asset managers in implementing MiFID II requirements, especially the reporting of sustainable-investment exposure.

Calculating a fund's minimum percentage of sustainable investments as defined under SFDR or the EU taxonomy isn't easy. In addition to the well-known conundrum of issuer data availability, there is a definitional problem.

Article 2(17) of SFDR defines the term *sustainable investment* as:

- An investment in **an economic activity that contributes to an environmental objective**, as measured, for example, by key resource efficiency indicators on the use of energy, renewable energy, raw materials, water and land, on the production of waste, and greenhouse gas emissions, or on its impact on biodiversity and the circular economy,
- Or an investment in **an economic activity that contributes to a social objective**, in particular an investment that contributes to tackling inequality or that fosters social cohesion, social integration, and labor relations, or an investment in human capital or economically or socially disadvantaged communities,
- Provided that **such investments do not significantly harm any of those objectives**,
- And [provided] that the investee **companies follow good governance practices**, in particular with respect to sound management structures, employee relations, remuneration of staff, and tax compliance.

The issue with this definition of "sustainable investment" is that it leaves too much room for interpretation, especially when it comes to the "do no significant harm," or DNSH, condition.

For the purpose of the DNSH test, a list of PAI indicators as outlined in Exhibit 26 must be considered. But regulators haven't specified any thresholds, so the determination of what these should be has been left to the discretion of asset managers.

Another aspect left to the discretion of managers relates to the way sustainable companies are counted in portfolios. While one firm might count the entirety of a sustainable company (beyond a certain level of revenue derived from sustainable activities), another might count only the proportion of revenue attributed to those activities. These two approaches, broadly referred to as *revenue-weighted* and *pass-fail approaches* (and highlighted in the exhibit below), would produce opposite results: high percentages of sustainable investments in the first case and much lower levels in the latter case[12].

Exhibit 28 The Two Main Approaches to Calculating 'Sustainable Investment Proportion'

	Revenue-weighted approach	**Pass-Fail approach**
% of Sustainable Investments (After the DNH test is applied)	Only the % of revenue generated from sustainable activities	100% of companies that generate a minimum level of revenue from sustainable activities
Example	If 20% of a company's revenue contribute to the UN SDGs and the company is not involved in any business activities deemed significantly harmful, then the 20% of the investment in the company is considered	If 20% of a company's revenue contribute to the UN SDGs and the company's remaining business activities are not deemed significantly harmful, then an investment in the whole company is considered a sustainable one.
% of Sustainable Investment typically reported	20-40%	60-80% (and in some cases 100%)

Source: Morningstar Research.

Other factors that could drive divergent numbers reported by different asset managers for similar portfolios include different criteria and thresholds to set sustainable activity eligibility, among others.

Different interpretations of the regulation have led asset managers to adopt different approaches to the calculation of sustainable-investment exposure, rendering it impossible to compare competing products directly. Products with similar mandates and portfolios will report divergent exposures to sustainable investments depending on the methodology chosen by their providers.

To illustrate the wide range of numbers that investors should expect to see, we have selected 12 global large-cap ETFs that track a Paris-aligned benchmark and have similar portfolios.

12 For more detail on the benefits and limitations of these approaches, read this blog.

Exhibit 29 Minimum % of Sustainable Investments and Taxonomy- Alignment for 12 Funds Tracking Large-Cap Paris-Aligned Benchmarks

Fund Name	Min. % Sustainable Investments	% Taxonomy Alignment
UBS MSCI World Climate Paris Aligned ETF	80%	-
UBS MSCI ACWI Climate Paris Aligned ETF	80%	-
UBS Climate Aware Global Developed Equity CTB ETF	80%	-
BNP PARIBAS EASY - Low Carbon 300 World PAB	45%	0%
BNP Paribas Easy MSCI World SRI S-Series PAB 5% Capped	45%	0%
HSBC MSCI World Climate Paris Aligned ETF	20%	0%
Amundi Index MSCI World SRI PAB	10%	-
iShares MSCI World Paris-Aligned Climate ETF	10%	-
Lyxor Net Zero 2050 S&P World Climate PAB (DR) ETF	10%	-
Amundi MSCI World Climate Paris Aligned Pab	5%	-
Amundi MSCI World Climate Paris Aligned Pab Umweltzeichei	5%	-
Xtrackers World Net Zero Pathway Paris Aligned ETF	1%	1%

Source: Morningstar Direct. Data as of September 2022.

Despite the holding similarities, the minimum percentages of sustainable investments reported by the 12 ETFs diverge significantly, from 1% for an Xtrackers fund to 80% for three UBS ETFs. Hence, the need to go beyond headline numbers and dive into the methodologies.

It is also worth mentioning that diverging approaches may be found even within an asset-management firm. For example, a firm offering both active and passive investments would apply the index provider's methodology for each of its passive products, while it would use another approach to calculate the proportion of sustainable investment in its actively managed products. This situation will certainly be even more confusing for financial advisors and investors.

In the absence of a standardized approach to calculating sustainable-investment exposure, we expect to continue to see asset managers implement a variety of methodologies, including ones that enable them to report higher sustainable-investment allocations and meet the sustainability preferences of clients expressed under the new MiFID suitability assessment.

Regulatory Update

The third quarter saw the European Supervisory Authorities formally flag to the European Commission legal interpretation challenges that materialized via the entry application of the amendment to MiFID, while continuing to roll out technical measures to implement SFDR and the EU Taxonomy regulation.

The combination of the entry into application of the amendment to MiFID and the persistent lack of clarity around regulatory definition of a "sustainable investment" has indeed pushed the ESAs to issue on Sept. 9, 2022, a series of fundamental questions to the European Commission. Many of these relate to the core components of the sustainable-investment definition under SFDR.

For instance, one question asks whether a revenue-weighted approach or a pass or fail approach (see Exhibit 28) should be considered by asset managers when assessing equity/debt holdings. Another question tackles the meaning of "considering" principal adverse impacts at the product level.

It is unclear if the EC intends to respond to these questions ahead of the entry into application on Jan. 1, 2023, of the delegated regulation, which requires among others to disclose their minimum taxonomy and sustainable-investment alignments and the consideration of PAI in precontractual documents.

Separately and in spite of the fundamental legal interpretation challenges mentioned above, the Dutch regulator (Autoriteit Financiële Markten, the AFM) announced on Sept. 8, 2022, that this fall, it would investigate the status of investment fund managers' compliance with the SFDR and the Taxonomy regulation. In 2021, the AFM had published a report on the implementation of the SFDR by Dutch funds in which it noted "that the objective of many of these funds appears to be broader than sustainable investing alone, and that the investment portfolio is not usually aimed exclusively at sustainable investments. This could lead to investors believing incorrectly that a fund is aimed exclusively at sustainable investing when this is not the case. The AFM expects managers, when offering funds that have sustainable investment as their objective, to clearly state how the (underlying) investments fit into the definition of sustainable investment as defined in Article 2(17) of the SFDR." This was understood by certain market participants as a clear ask to only invest in sustainable investments in context of Article 9 funds (with the exception, however, of instruments that are used for specific prudential purposes, such as hedging or liquidity, which are only subject to the DNSH requirement).

In parallel, the ESAs have responded to the mandates that they had received and continued to roll out implementation tools:

- On Sept. 23, 2022, ESMA published its guidelines on the consideration of sustainability preferences under MiFID II suitability requirements. The definition of sustainability preferences in the Delegated Regulation refers to a "minimum proportion" being invested in taxonomy-aligned investments or sustainable investments. The guidelines state that this does not have to be collected as an exact percentage but by minimum percentages (for example, minimum 20%). ESMA has confirmed that, where a client's sustainability preference is for financial instruments that consider principal adverse impacts, it is possible to collect information on the consideration of PAI on either quantitative or qualitative elements (rather than both quantitative and qualitative). ESMA has also added further guidance to state that "firms could also ask the client if there are specific economic activities that, on the basis of relevant PAIs, it wishes to exclude from its investments (for example, specific economic activities that are considered as significantly harmful under the EU taxonomy framework and/or that are opposed to the environmental and ethical views held by the client and that are linked to certain principal adverse impacts on sustainability factors)". Overall, ESMA is trying to give the industry room to maneuver via the guidelines especially in light of the data challenges mentioned above (that is, patchy sets of data for PAI, no use of estimates for Taxonomy data, and lack of comparability of sustainable-investing data).

- On Sept. 30, the ESAs published their Final Report with draft Regulatory Technical Standards regarding the disclosure of financial products' exposure to investments in fossil gas and nuclear energy activities. They suggest adding a yes/no question in the financial product templates of the SFDR Delegated Regulation to identify whether the financial product intends to invest in such activities; if the answer was yes, a graphical representation of the proportion of investments in such activities would be required.

Furthermore, the Platform on Sustainable Finance (EC's expert group) issued a report advising on the application of minimum safeguards and a report to improve the usability of the EU Taxonomy Regulation. The EC has indicated that, while these reports may not be translated into legal acts, they may be used in the context of other regulatory tools in light of the FAQs issued on Oct. 6 regarding Taxonomy reporting at the entity level (Article 8 EU Taxonomy regulation).

Finally, as we conclude this report, the UK's Financial Conduct Authority has just issued a consultation paper on its version of SFDR called Sustainability Disclosure Requirements. The draft SDR regime is notably built on three labels (Sustainable Focus, Sustainable Improvers, Sustainable Impact), sustainability disclosures for all products and asset managers and anti-greenwashing provisions. Below is a description of the three labels.

Exhibit 30 UK FCA's Draft Criteria for Sustainable-Fund Labels

Category Name	No sustainable label	Sustainable Focus	Sustainable Improvers	Sustainable Impact
Description	Products that do not meet the criteria for a sustainable label	Products with an objective to maintain a high standard of sustainability in the profile of assets by investing to (i) meet a credible standard of environmental and/or social sustainability; or (ii) align with a specified environmental and/or social sustainability theme	Products with an objective to deliver measurable improvements in the sustainability profile of assets over time. These products are invested in assets that, while not currently environmentally or socially sustainable, are selected for their potential to become more environmentally and/or socially sustainable over time, including in response to the stewardship influence of the firm	Products with an explicit objective to achieve a positive, measurable contribution to sustainable outcomes. These are invested in assets that provide solutions to environmental or social problems, often in underserved markets or to address observed market failures
Consumer-facing description		Invests mainly in assets that are sustainable for people and/or planet	Invests in assets that may not be sustainable now, with an aim to improve their sustainability for people and/or planet over time	Invests in solutions to problems affecting people or the planet to achieve real-world impact

Source: FCA.

Even though the concepts of the DNHS, PAI, and Taxonomy are not retained, the UK framework could be a lot more stringent than the EU SFDR. On the one hand, the consultation paper notes that "ESG integration" funds cannot qualify for the labels, and the other hand, it advocates to ban funds that do not qualify for any label (including ESG funds) to use terms such as "ESG," "Responsible," and so on. Most ESG funds will either need to change considerably to meet the Sustainable Focus label or Sustainable Improvers label or rebrand themselves (see high-level requirements for each label above). This certainly goes far beyond the EU SFDR, which simply require ESG funds to elect their type and produce a set of disclosures accordingly.

Corrections and Clarifications

Correction

On Page 11, Exhibit 12 was updated to include the correct 10 funds.

On Page 11, NN's plan for reclassifying its funds was corrected. It currently has addressed 10 strategies and will downgrade 10 more in the fourth quarter.

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