

# U.S. Sustainable Funds Landscape 2023 in Review

Investor appetite for sustainable funds waned despite recovering performance.

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## Table of Contents

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<b><u>Key Takeaways</u></b>	<u>3</u>
<b><u>Flows</u></b>	<u>8</u>
<b><u>Assets</u></b>	<u>18</u>
<b><u>Arrivals &amp; Departures</u></b>	<u>23</u>

<b><u>Investment Performance</u></b>	<u>32</u>
<b><u>Sustainability Performance</u></b>	<u>50</u>
<b><u>Regulatory Developments</u></b>	<u>58</u>

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## Key Takeaways: Flows, Assets, & Product Development

U.S. sustainable funds **recorded their first year of net outflows** in 2023, while **conventional peers saw inflows**.

- Despite outflows, **assets in sustainable funds rose on the back of market appreciation** in 2023, surpassing the \$300 billion mark once again.

**Sustainable funds faced headwinds in 2023:** Returns lagged those of conventional peers, political scrutiny persisted, and greenwashing concerns endured.

- Macroeconomic pressures such as high interest rates continue to feature in 2024 outlooks.

### Sustainable Fund Flows & Assets



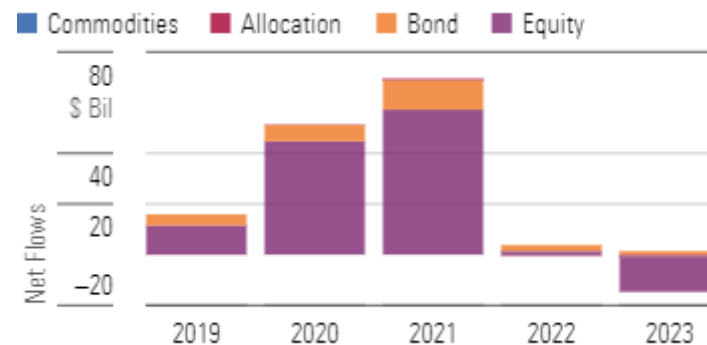
Source: Morningstar Direct. Data as of Dec. 31, 2023.

**While BlackRock remains the largest firm in terms of sustainable fund assets**, it fell to last place in terms of annual net flows in 2023.

- The firm's largest sustainable fund—**iShares ESG Aware MSCI USA ETF ESGU**—lost \$9.3 billion, more than any other sustainable fund.

**It wasn't all bad.** Two new climate-focused ETFs catapulted to the top for annual net inflows. Additionally, **sustainable bond funds stayed afloat**, collecting \$1.4 billion during the year.

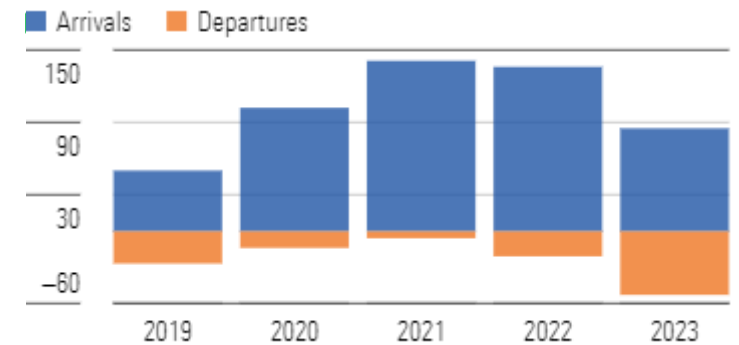
### Sustainable Funds Flows by Asset Class



In 2023, product development slowed as **66 new sustainable funds** launched compared with 87 in 2022.

- Nearly **two thirds of product launches were equity funds with active management** as the go-to for product development teams.
- There were **19 funds repurposed** to become sustainable, most of which were part of Putnam's sustainable target-date offering.
- Closures and departures reached an all-time high: **45 sustainable funds closed, and eight funds moved away from ESG mandates.**

### Arrivals & Departures



## Key Takeaways: Investment Performance

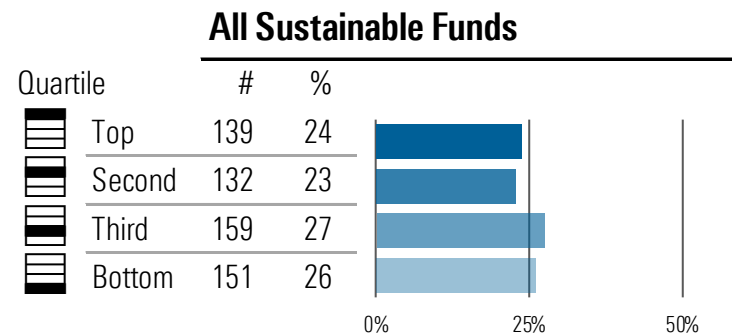
Sustainable funds held up much better in 2023 than 2022.

- On the whole, **sustainable funds lagged their conventional peers by a small margin**, with 53% of sustainable funds landing in the bottom half of their respective categories.

Volatility within the energy sector, combined with the **typical sustainable fund's underweighting to energy**, affected performance.

- When energy led markets in 2022, sustainable funds lagged. When it fell in 2023, sustainable funds saw a boost.

### Performance: Sustainable vs. Conventional

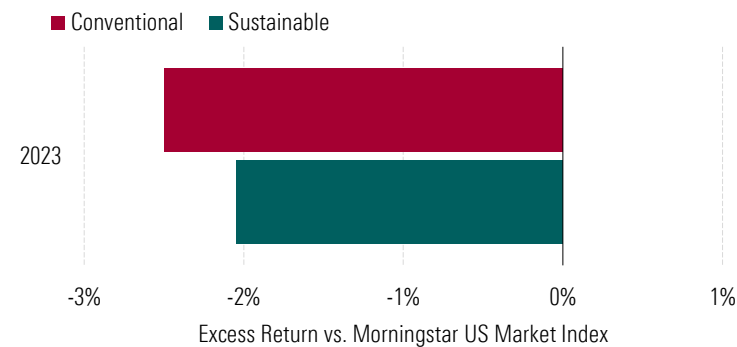


Source: Morningstar Direct. Data as of Dec. 31, 2023.

Within the large-blend equity category, sustainable funds' out- and underperformance over various time periods was often more muted than that of conventional peers.

- In 2023, both **sustainable funds and conventional peers lagged the Morningstar US Market Index**, but the median shortfall was smaller for sustainable funds than for conventional peers.
- The **top-performing sustainable large-blend equity fund** was IQ Candriam U.S. Large Cap Equity ETF IQSU, which gained 32 percentage points during the year, 6 percentage points better than the index.

### Excess Returns: Large-Blend Equity Funds



**More than 300 sustainable funds earn our higher ratings** under the Morningstar Medalist Rating system. Of those, 11 are offered by asset managers that earn top marks on the Morningstar ESG Commitment Level.

- Launched in 1992, **Parnassus Core Equity PRBLX leads the pack in terms of assets** and earns a Leader status under the ESG Commitment Level and Gold under the Morningstar Medalist Rating.

### Gold, Silver, and Bronze Sustainable Funds

Name	Ticker	Morningstar Medalist Rating	2023	
			Total Return	% Rank Category
Parnassus Core Equity	PRBLX	Gold	24.9	43
Boston Trust Walden Small Cap	BOSOX	Gold	10.1	91
Brown Advisory Sustainable Growth	BAFWX	Silver	39.1	46
Parnassus Mid-Cap	PARMX	Silver	12.7	78
TIAA-CREF Core Impact Bond	TSBIX	Bronze	6.0	32

## Key Takeaways: Sustainability Performance

### Sustainable funds delivered lower levels of ESG risk

compared with peers.

- At the end of 2023, nearly **three fourths of sustainable funds received the highest ratings** (4 or 5 globes), compared with less than one third of funds overall.
- At the other end of the scale, **less than one tenth of sustainable funds received the lowest ratings** (1 or 2 globes), compared with close to one third of funds overall.

Some sustainable funds target specific sustainability themes, such as Climate Action, Resource Security, and Basic Needs. As one would expect, **these funds delivered greater exposure to environmental and social impact** associated with their themes, compared with peers.

- The excess was greatest among Basic Needs funds, but the sample size was small.
- **Climate Action funds delivered 27 percentage points more exposure to positive, climate-related impact** (on average and compared with peers).

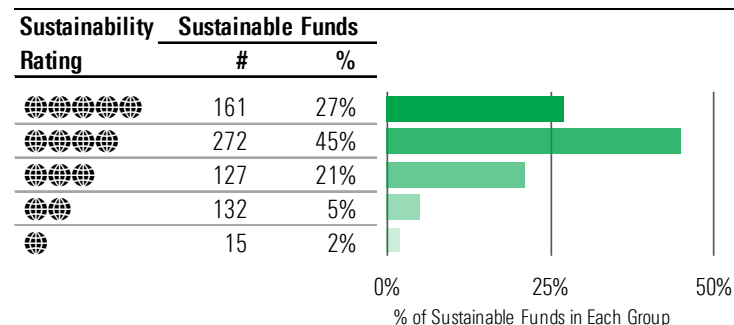
The number of **resolutions focused on environmental and social topics increased in 2023**, but [support fell](#).

- Out of 337 such proposals, 10 gained majority support.

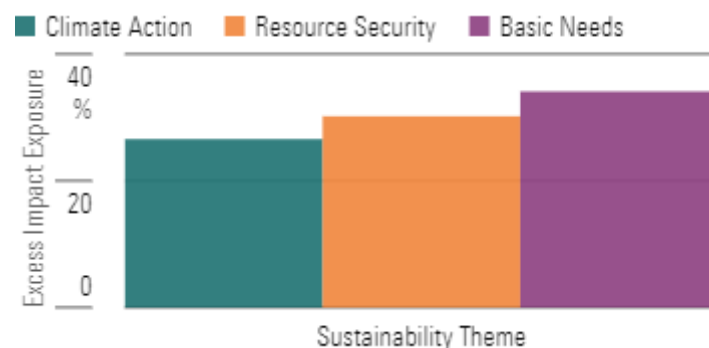
**Support from the largest sustainable fund shops varied widely.** Parnassus supported 100% of key ESG resolutions in each of the past three years.

- **BlackRock supported just 37% of key resolutions**, well down from the 68% support seen in 2021.
- **Vanguard backed 9% of the key resolutions** it voted in 2023, a significant drop from 51% support in 2021.

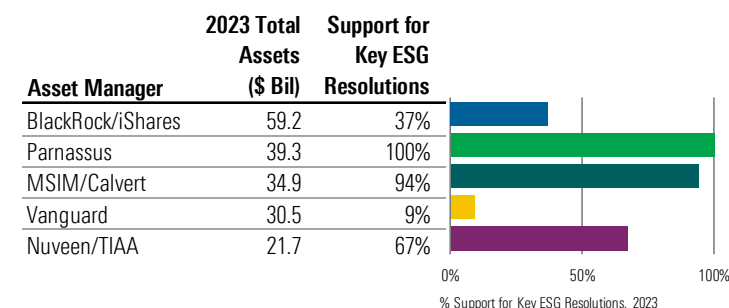
### ESG Risk in Sustainable Funds



### Sustainability Themed Funds' Exposure to Impact



### How the Largest Sustainable Asset Managers Voted



Source: Morningstar Direct. Data as of Dec. 31, 2023.

# Introduction

**Sustainable funds faced many headwinds in 2023.** Although returns moderated compared with previous years, most sustainable funds continued to lag those of conventional peers. Macroeconomic pressures such as high interest rates and recession fears weighed on investor appetite. Political scrutiny persisted, and individual states took action to limit the use of environmental, social, and governance factors in investment strategies. Additionally, in lieu of either industry consensus or U.S. regulatory guidance, confusion endured regarding terms often used interchangeably, for example, “ESG,” “sustainable,” and “impact.”\*

**These headwinds made a mark.** In 2023, sustainable funds notched their first calendar year of outflows in more than a decade. Meanwhile, conventional peers saw modest inflows. The pace of fund launches slowed while closures picked up. When it came to active ownership, U.S. managers showed less support for environmental and social shareholder resolutions than in previous years. Only 10 out of more than 300 such proposals gained majority support, compared with 40 in 2022.

**Still, the outlook for sustainable funds isn’t purely one of doom and gloom.**

Although demand for U.S. sustainable funds has moderated over the past two years, the pace of outflows and product closures comes nowhere close to the growth this landscape has seen over the longer term.

Sustainable funds have been around since at least the 1970s in the United States, but a switch flipped in 2019 when sustainable funds recorded their first annual inflows greater than \$10 billion. Since then, the offerings have not only proliferated but have also grown in sophistication because of improving data quality and increased attention from investors and regulators.

**Performance and demand may ebb and flow, but the investment case for these funds is based on long-term trends.** Mitigating and adapting to climate change will require [trillions of dollars of investment](#) over the next few decades, and individual investors seem [ready to dive in](#).

**Sustainable investing is here to stay.**

\*For more on how we define the U.S. sustainable funds landscape, please refer to slide 7 in this presentation and definitions listed in [Morningstar Sustainable Attributes: Frameworks & Definitions](#)

## Sustainable Fund Offerings Have Doubled in the Past Five Years

At the end of 2023, the group of sustainable open-end funds and exchange-traded funds available to U.S. investors numbered 646, up 12% from 2021 and more than double the number of investments available five years ago.

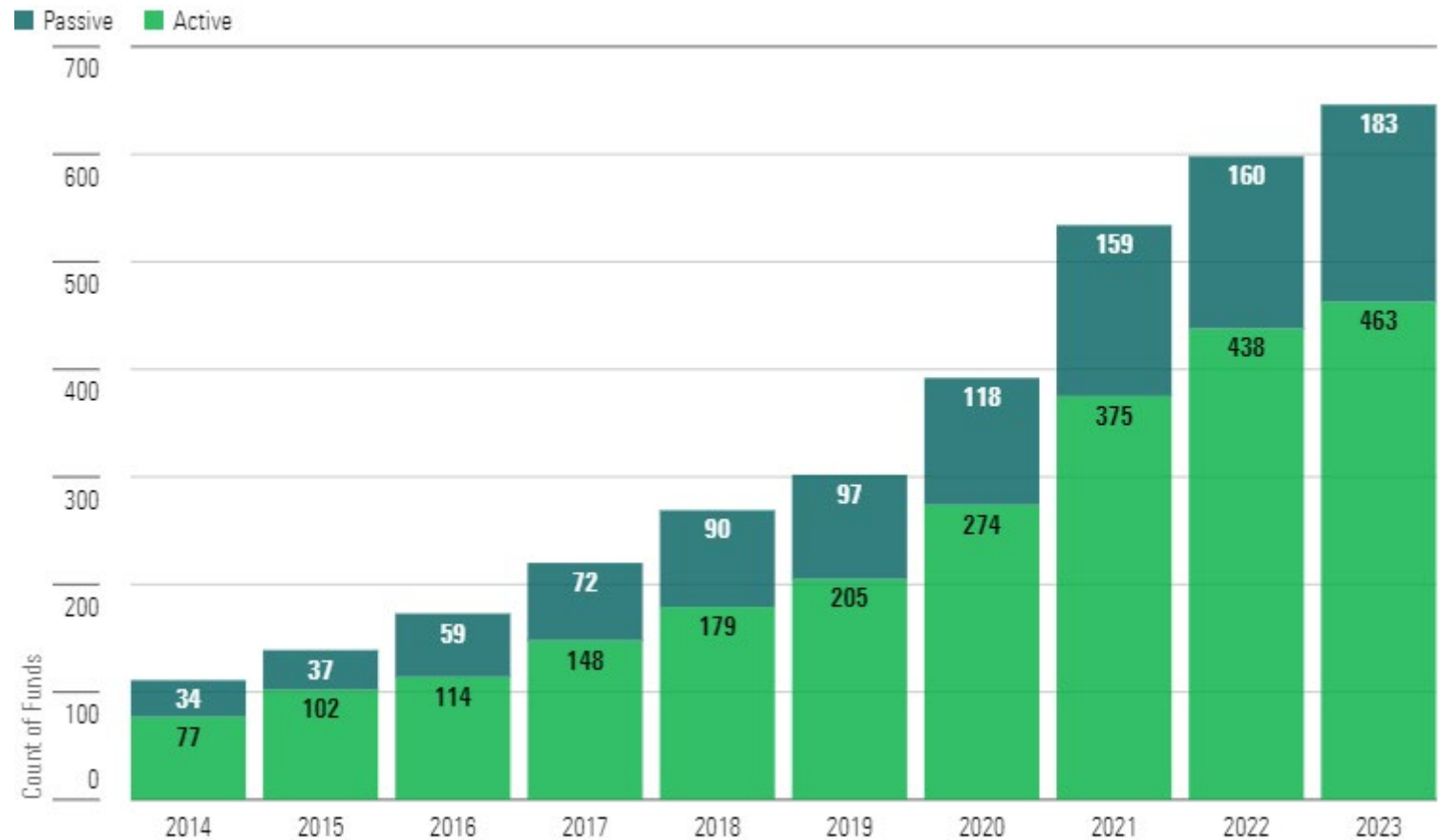
### How We Define the U.S. Sustainable Funds Universe

The U.S. sustainable funds universe encompasses open-end funds and exchange-traded funds that focus on sustainability, impact, or environmental, social, and governance factors (per the prospectus). While many funds now consider environmental, social, and governance criteria as one factor in the security-selection process, those included in the sustainable funds universe make their commitment clear and prominent, usually through binding guidelines.

Funds of funds and feeder funds are included in the count of funds but excluded from flows and assets calculations. Money market funds are excluded from this report.

For more on Morningstar’s Sustainable Attributes, see [Morningstar Sustainable Attributes: Frameworks & Definitions](#)

### The Sustainable Funds Universe



Source: Morningstar Direct. Data as of Dec. 31, 2023. Includes funds that have liquidated.

# U.S. Sustainable Funds: Flows

Sustainable funds saw their first annual outflows, but bond funds stayed afloat.



## Sustainable Funds Registered First Annual Outflows

U.S. sustainable funds recorded their first year of net outflows in 2023, shedding more than \$13 billion.

- Flows into U.S. sustainable funds picked up rapidly in 2019 but have fallen steadily since their record \$70 billion haul in 2021.

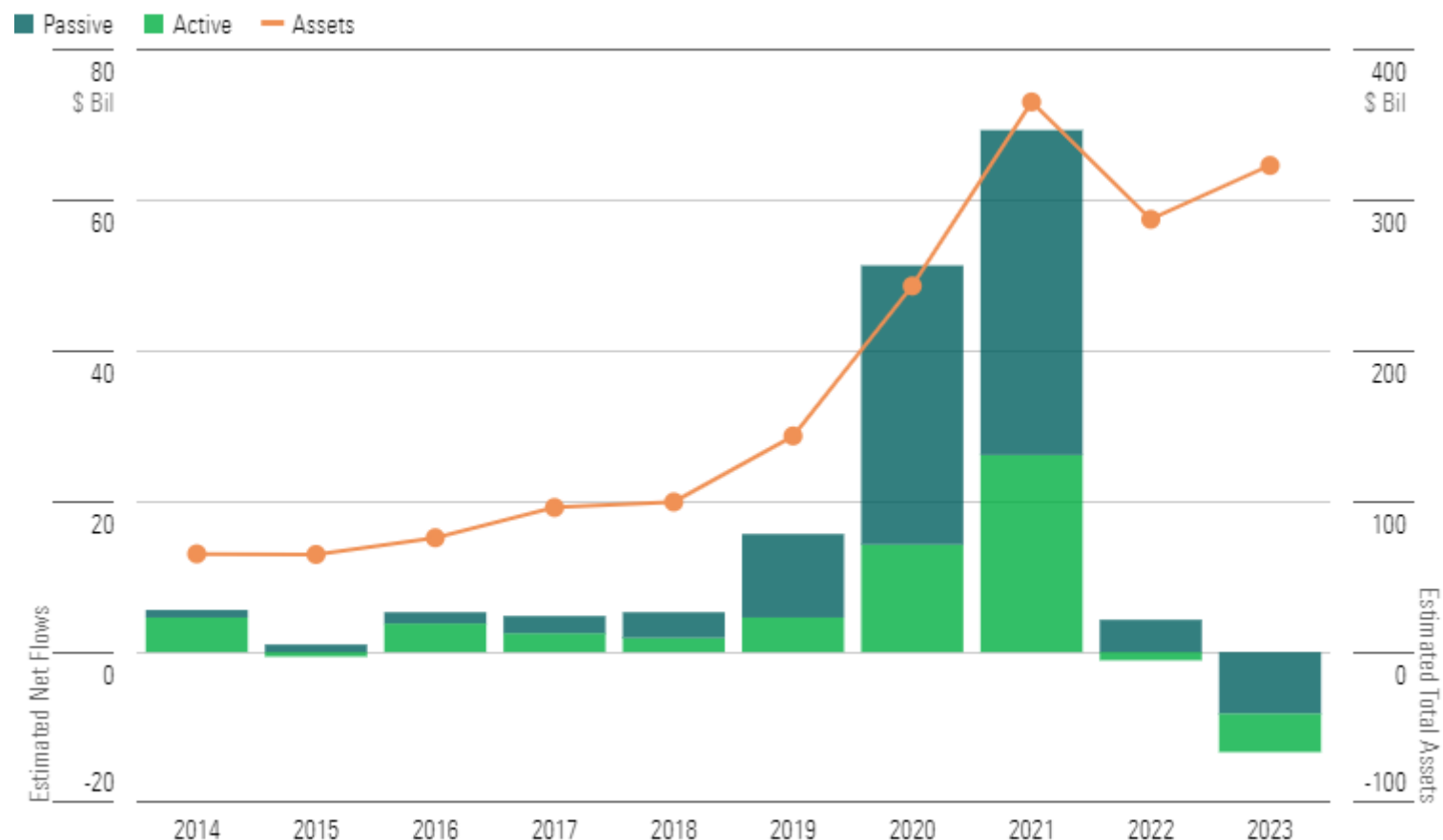
Neither active nor passive funds were spared, but in a surprising reversal of trends, passive funds suffered more than their actively managed counterparts.

- Index-tracking options gave up \$8.2 billion over the course of the year, accounting for more than 60% of overall sustainable fund outflows.
- On average over the past five years, passive funds have represented 80% of overall flows into sustainable funds.

In spite of net outflows, assets in sustainable funds rose on the back of market appreciation in 2023, surpassing the \$300 billion mark once again.

- This represents a 12% increase over assets at the end of 2022 but also nearly a 12% decline from their all-time high at the end of 2021.

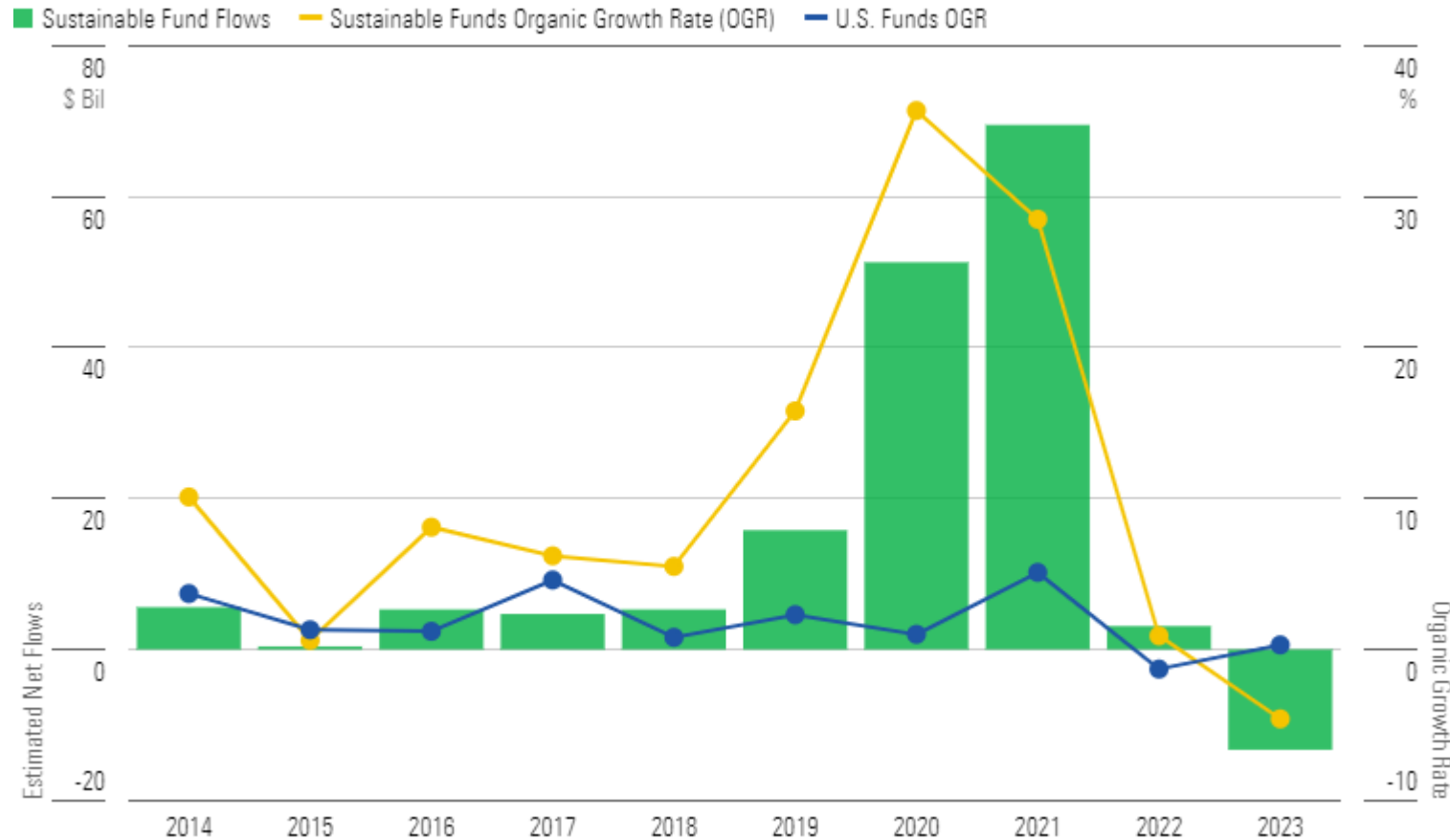
### Sustainable Fund Flows & Assets



Source: Morningstar Direct. Data as of Dec. 31, 2023. Includes funds that have liquidated. Excludes funds of funds.

# Sustainable Funds Suffered Worse Than Their Conventional Peers

## Sustainable Fund Flows Relative to Overall Fund Flows



Source: Morningstar Direct. Data as of Dec. 31, 2023. Includes funds that have liquidated. Excludes funds of funds.

For the first time in more than five years, sustainable funds lost more money than their conventional counterparts.

- While sustainable funds gave up \$13 billion during the year, the overall landscape of U.S. open-end and exchange-traded funds collected \$79 billion. This is tiny compared with these funds' average annual net inflows of \$430 billion from 2014 through 2021 but a significant recovery from last year.
- In 2022, the full group of U.S. funds (including sustainable as well as conventional) [suffered more than \\$370 billion in withdrawals](#), cementing their first calendar year of outflows since records began in 1993.

Sustainable funds constitute a small portion of the overall U.S. fund universe, so the organic growth rate (calculated as net flows as a percentage of total assets at the start of a period) puts the magnitude of fund flows into perspective.

- In 2023, sustainable funds contracted by 4.6%, and the overall U.S. fund universe stayed steady with growth of 0.3%. At its peak in 2020 and 2021, the sustainable funds universe swelled by 36% and 29%, respectively.

## Sustainable Funds Bled in Each of 2023's Four Quarters

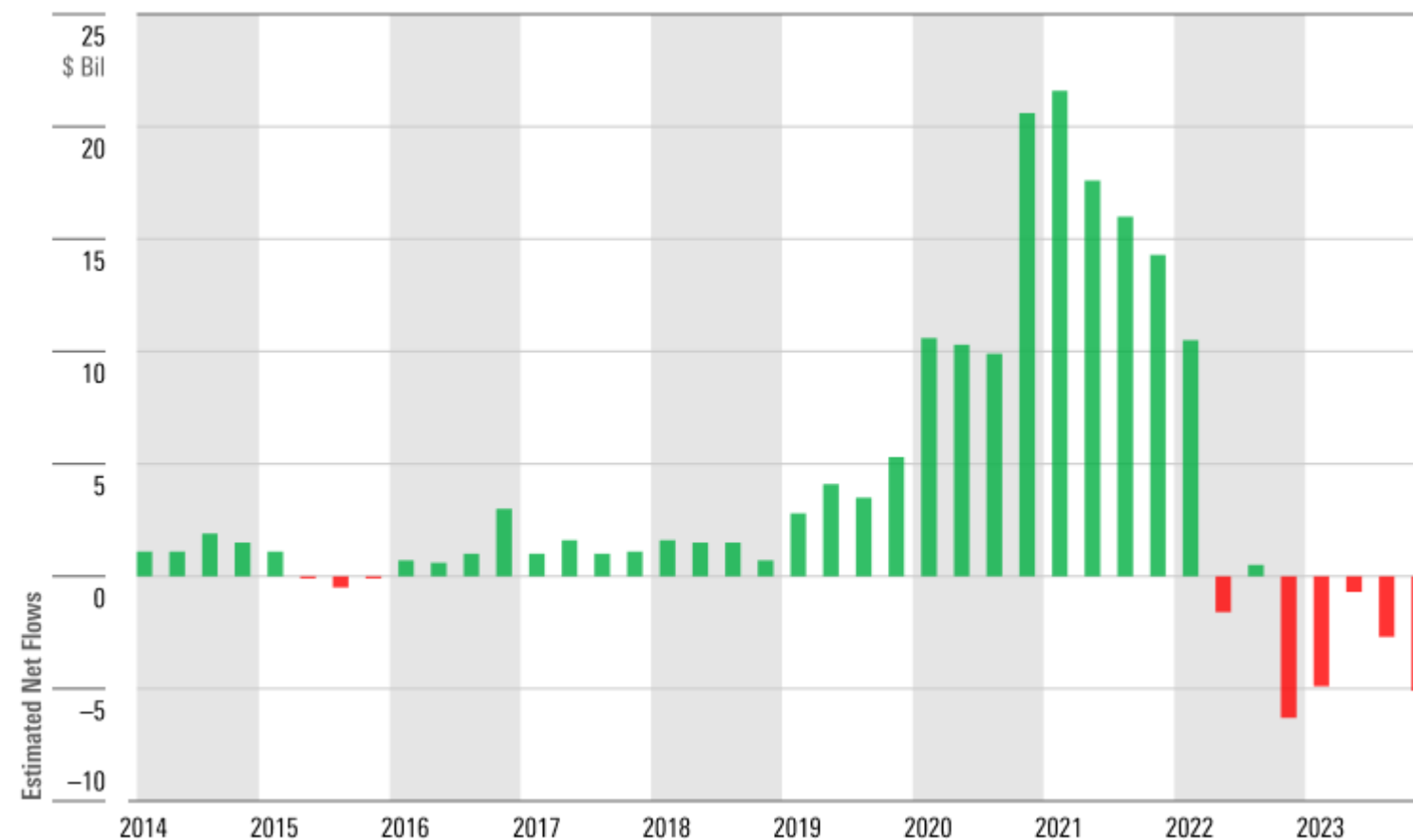
For the first time in more than a decade, sustainable funds suffered net outflows in every quarter last year.

- In the first quarter of 2023, one fund dominated the narrative. iShares ESG Aware MSCI USA ETF ESGU bled \$6.5 billion following a BlackRock portfolio manager's change to the BlackRock Target Allocation ETF model portfolio series.
- The full landscape of U.S. sustainable funds gave up \$5.2 billion during 2023's first quarter. Therefore, without the losses suffered by iShares ESG Aware MSCI USA ETF, the landscape would have recorded modest inflows.

Although outflows in the fourth quarter were slightly more severe than those seen in the first quarter, there wasn't a clear culprit behind the withdrawals.

- The fourth quarter's biggest loser was Parnassus Core Equity PRBLX, which shed \$644 million during the period. This is a relatively small amount considering the fund counted more than \$25 billion in assets at the beginning of the period.
- Less than 30% of sustainable funds recorded inflows during the fourth quarter.

### Sustainable Funds Quarterly Flows



Source: Morningstar Direct. Data as of Dec. 31, 2023. Includes funds that have liquidated. Excludes funds of funds.

## Sustainable Bond Funds Stayed Afloat

Over the course of 2023, sustainable equity funds recorded \$13.8 billion in net outflows.

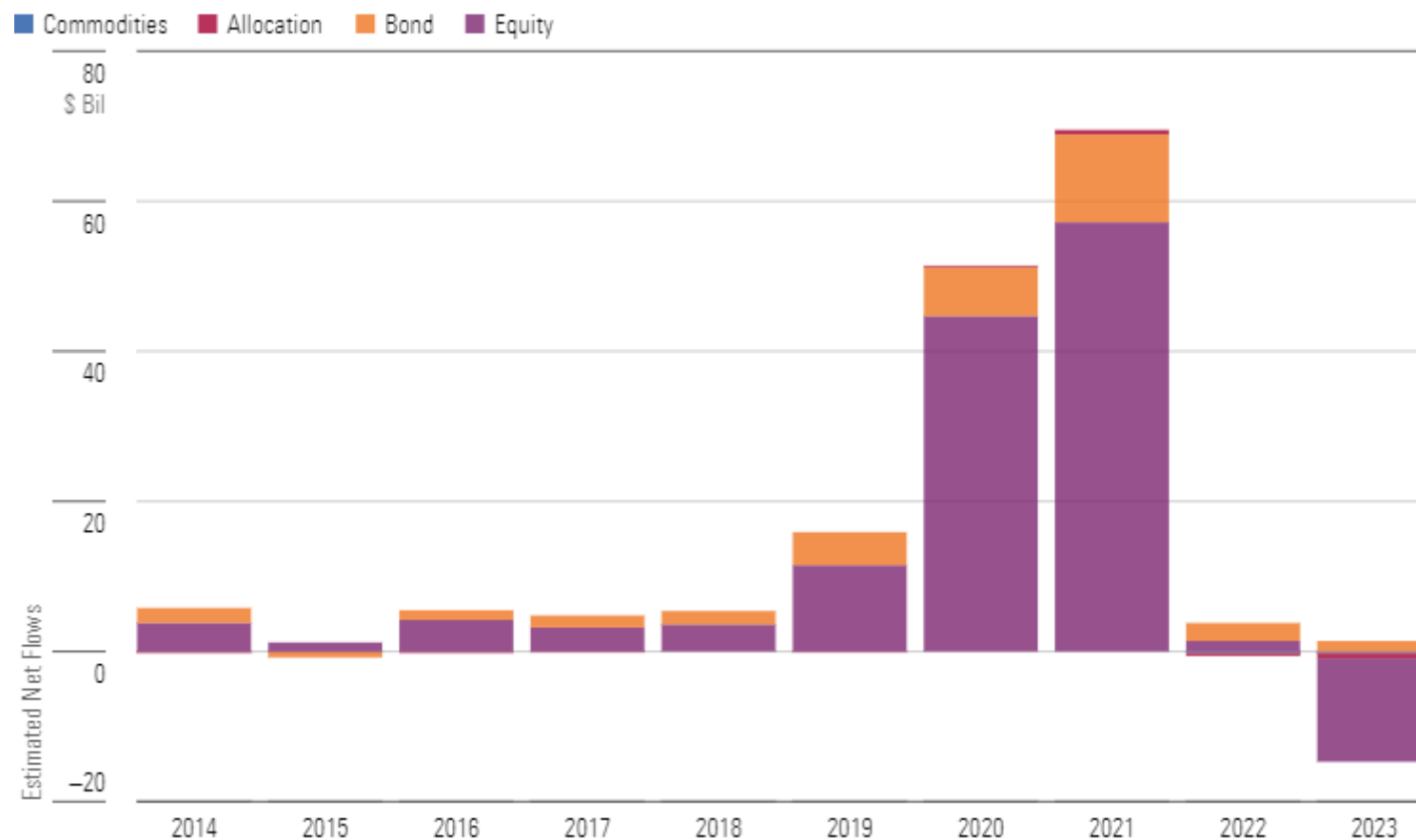
- Large-cap equity funds were the worst hit, shedding \$11.5 billion during the year. Two of the largest sustainable funds—iShares ESG Aware MSCI USA ETF and Parnassus Core Equity—sit in the large-blend Morningstar Category and were among the hardest hit during 2023.
- Large-growth funds managed to eke out net inflows in 2023, led by Brown Advisory Sustainable Growth BAFWX, which collected \$753.8 million over the year.

Equity funds remain the largest grouping within the U.S. sustainable funds landscape, representing more than 80% of total assets.

Sustainable bond funds stayed above water in 2023 as investors sought to lock in attractive yields.

- Led by intermediate core-bond strategies—especially iShares ESG U.S. Aggregate Bond ETF EAGG—sustainable fixed-income offerings brought in \$1.4 billion over the year.

### Sustainable Fund Flows by Asset Class



Source: Morningstar Direct. Data as of Dec. 31, 2023. Includes funds that have liquidated. Excludes funds of funds.

## Climate-Focused ETFs Catapulted to the Top

Two of 2023's new launches skyrocketed to the top of the chart for largest annual net inflows.

- iShares Climate Conscious & Transition MSCI USA ETF USCL launched on June 6 and netted \$2.2 billion before the end of the month, and Xtrackers MSCI USA Climate Action Equity ETF USCA followed close on its heels with a \$2 billion collection during the quarter.
- The funds track indexes that lean into companies that are well-positioned for the transition to a low-carbon economy or that are actively engaging in the climate transition, relative to peers.
- Amid persistent skepticism of ESG investing, climate-focused funds such as these continue to resonate with U.S. investors. Climate funds [collected more than \\$3.6 billion](#) in the first half of 2023, compared with net outflows of more than \$5 billion from sustainable funds over that time.
- Climate-related risks to company performance are thought to be more tangible and measurable than comparable social themes, from education access to diversity, equity, and inclusion. This contributes to their relative prevalence in investment strategies.

Three funds are repeat winners, having landed among the top 10 flow recipients in 2023 as well as 2022.

- iShares ESG U.S. Aggregate Bond ETF EAGG collected \$2 billion in net inflows over the past two years, while Brown Advisory Sustainable Growth BAFWX and iShares Paris-Aligned Climate MSCI USA ETF PABU collected more than \$1 billion each during that time.

### Sustainable Funds With Largest Flows in 2023

Name	Ticker	Inception Date	Estimated Net Flows (\$ Mil)
iShares Climate Conscious & Transition MSCI USA ETF	USCL	6/6/2023	1,556
Xtrackers MSCI USA Climate Action Equity ETF	USCA	4/3/2023	1,484
iShares MSCI USA ESG Select ETF	SUSA	1/24/2005	1,257
iShares ESG U.S. Aggregate Bond ETF	EAGG	10/18/2018	1,250
Brown Advisory Sustainable Growth	BAFWX	6/29/2012	754
Vanguard FTSE Social Index	VFTNX	1/14/2003	608
Calvert Core Bond	CLDAX	12/31/2004	520
Dimensional US Sustainability Core 1 ETF	DFSU	11/1/2022	477
BlackRock Sustainable Advantage Large Cap Core	BIRIX	10/5/2015	399
iShares Paris-Aligned Climate MSCI USA ETF	PABU	2/8/2022	371

Source: Morningstar Direct. Data as of Dec. 31, 2023. Excludes funds of funds.

## The Largest Sustainable Funds Faced Withdrawals

Two of the largest sustainable funds in the U.S. also landed among the hardest-hit in terms of net annual outflows.

iShares ESG Aware MSCI USA ETF lost \$9.3 billion over the course of 2023, driven in part by a BlackRock portfolio manager's change to the BlackRock Target Allocation ETF model portfolio series. This withdrawal was nearly 4 times greater than the runner-up—Xtrackers MSCI USA ESG Leaders Equity ETF USSG shed \$2.4 billion in 2023.

- iShares ESG Aware MSCI USA ETF ranked among the top flow-recipients in 2021, 2020, and 2019, collecting nearly \$19 billion in net deposits over that time. The fund gave up \$318 million in 2022, but this was relatively insignificant compared with peers.

Parnassus Core Equity continues to hold the crown as the largest U.S. sustainable fund despite suffering net withdrawals of \$1.9 billion during 2023.

- Outflows in 2023 accounted for nearly 8% of the fund's assets entering the year; however, market appreciation boosted the fund's assets higher by the end of 2023.
- Parnassus Core Equity also landed among the 10 funds suffering the largest outflows in 2022 and 2019, but its fortune reversed when it secured some of the largest deposits in 2021.
- Parnassus attributes a portion of the fund's outflows to the launch of a less-expensive collective investment trust and the subsequent conversion of investors from one vehicle to the other. Our data includes only open-end and exchange-traded funds.

### Sustainable Funds With Largest Outflows in 2023

Name	Ticker	Inception Date	Estimated Net Flows (\$ Mil)
iShares ESG Aware MSCI USA ETF	ESGU	12/1/2016	-9,333
Xtrackers MSCI USA ESG Leaders Equity ETF	USSG	3/6/2019	-2,394
iShares ESG MSCI USA Leaders ETF	SUSL	5/7/2019	-2,272
Parnassus Core Equity	PRBLX	8/31/1992	-1,871
Parnassus Mid Cap	PARMX	4/29/2005	-1,328
iShares Global Clean Energy ETF	ICLN	6/24/2008	-1,028
TIAA-CREF Social Choice Equity	TISCX	7/1/1999	-851
Pioneer	PIODX	2/10/1928	-696
Invesco Floating Rate ESG	AFRAX	5/1/1997	-661
American Century Sustainable Equity	AFDAX	11/30/2004	-651

Source: Morningstar Direct. Data as of Dec. 31, 2023. Excludes funds of funds.

## Offerings From Dimensional and Putnam Rose on the Charts

**Sustainable Equity Funds With Largest Flows in 2023**

<b>Name</b>	<b>Ticker</b>	<b>Inception Date</b>	<b>Estimated Net Flows (\$ Mil)</b>
iShares Climate Conscious & Transition MSCI USA ETF	USCL	6/6/2023	1,556
Xtrackers MSCI USA Climate Action Equity ETF	USCA	4/3/2023	1,484
iShares MSCI USA ESG Select ETF	SUSA	1/24/2005	1,257
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BlackRock Sustainable Advantage Large Cap Core	BIRIX	10/5/2015	399
iShares Paris-Aligned Climate MSCI USA ETF	PABU	2/8/2022	371
Fidelity U.S. Sustainability Index	FITLX	5/9/2017	368
Putnam Sustainable Leaders ETF	PLDR	5/25/2021	318

BlackRock dominates the list of top equity fund flows in 2023, with four offerings landing among the top 10. BlackRock is mostly known for its passive iShares offerings, three of which claimed spots on the list.

- However, BlackRock Sustainable Advantage Large Cap Core BIRIX made its debut among the top 10 equity flow-recipients this year, netting nearly \$400 million over the course of 2023.

Aside from BlackRock, 2023's equity investors spread their flows across a variety of asset managers. The top 10 equity funds came from seven different shops. This was the first time in at least five years that an offering from Dimensional or Putnam secured a spot among the top 10 equity fund flow-recipients.

- Dimensional US Sustainability Core 1 ETF DFSU was one of four sustainability-focused ETFs the firm launched in November 2022, and it quickly rose to prominence over the past five quarters. The fund seeks to invest in companies that have relatively positive impacts on the environment by accounting for a company's land use, water use, effect on biodiversity, and involvement in private prisons, among other factors.
- Putnam Sustainable Leaders ETF PLDR is the exchange-traded sibling to Putnam Sustainable Leaders PNOPX. The funds aim to invest in "sustainable" businesses as measured by factors such as water use and reuse, sourcing renewable energy to power operations, and employee safety and diversity.

Source: Morningstar Direct. Data as of Dec. 31, 2023. Excludes funds of funds.

## ESG Specialist Calvert Dominated Top Bond Funds

### Sustainable Fixed-Income Funds With Largest Flows in 2023

Name	Ticker	Inception Date	Estimated Net Flows (\$ Mil)
iShares ESG U.S. Aggregate Bond ETF	EAGG	10/18/2018	1,250
Calvert Core Bond	CLDAX	12/31/2004	520
iShares ESG USD Corporate Bond ETF	SUSC	7/11/2017	354
RBC BlueBay High Yield Bond	RGHYX	11/30/2011	195
Dimensional Global Sustainability Fixed Income ETF	DFSB	11/15/2022	157
CCM Community Impact Bond	CRAIX	8/30/1999	155
Praxis Impact Bond	MIIAX	5/12/1999	151
Calvert Bond	CSIBX	8/24/1987	145
Vanguard ESG U.S. Corporate Bond ETF	VCEB	9/22/2020	135
Calvert Ultra-Short Duration Income	CULAX	10/31/2006	130

Calvert was one of the first fund shops fully dedicated to sustainable investing in the U.S., and its funds are often among the most popular with investors.

- Although Calvert Bond CSIBX only secured eighth place for sustainable bond fund flows in 2023, the fund has featured among the top 10 in each of the past five years.
- Having launched in 1987, Calvert Bond is also one of the oldest surviving sustainable fixed-income offerings in the United States. Calvert manages all three of the oldest—Calvert Income CFICX, Calvert Responsible Municipal Income CTTLX, and Calvert Bond.
- Even following the firm’s acquisition by Morgan Stanley Investment Management in 2021, Calvert maintains an independent board to ensure rigorous adherence to the Calvert Principles for Responsible Investment, which direct investments toward companies that lead on issues ranging from mitigating negative impacts on biodiversity to respecting local traditions and Indigenous peoples’ rights.

iShares ESG U.S. Aggregate Bond ETF EAGG launched at the end of 2018 and has featured among the top 10 sustainable bond funds in each year since. Its \$1.2 billion haul in 2023 was more than double the runner-up.

One noteworthy fund lost its place among the top 10 sustainable bond funds in 2023. Invesco Floating Rate ESG AFRAX started following a sustainable mandate in 2020 and rose to become one of the top flow-recipients in 2021 and 2022 as the market started to anticipate rising interest rates. Now that high interest rates are here, floating-rate bonds are less attractive, and the fund saw net outflows in 2023.

Source: Morningstar Direct. Data as of Dec. 31, 2023. Excludes funds of funds.



## Vanguard Held on to the Crown, and Behemoth BlackRock Fell Off the Chart

With just seven sustainable funds, Vanguard stayed in first place in terms of net annual flows last year. Its \$1.3 billion haul was significantly weaker than the record \$7.4 collection in 2021, but it was enough to outdo passive-management rivals iShares, State Street, and Xtrackers.

- In 2023, Vanguard FTSE Social Index VFTNX was the firm's most popular sustainable fund, collecting nearly half of the firm's total sustainable fund flows.
- The fund features a straightforward approach to portfolio construction that harks to the early days of socially responsible investing. It tracks a diversified equity index that screens out firms involved in tobacco, cannabis, civilian firearms, and coal and oil. The fund's popularity is largely driven by its low fee of just 12 basis points.
- This fund launched in 2003, 15 years before the firm would launch its second and third sustainable funds, Vanguard ESG U.S. Stock ETF ESGV and Vanguard ESG International Stock ETF VSGX.

Just two firms—Vanguard and Dimensional—have featured among the top flow-recipients in each of the past five years.

Not shown on the exhibit to the right is BlackRock, still the largest asset manager in terms of U.S. sustainable fund assets and the largest recipient of U.S. sustainable fund flows from 2019 through 2021.

- BlackRock's sustainable fund offerings shed \$8.7 billion over the course of 2023, dropping it to last place in terms of annual net flows. Most of this came from one fund—iShares ESG Aware MSCI USA ETF—which gave up \$9.3 billion in 2023.

### Asset Managers With Largest Flows Into Sustainable Funds

<b>Asset Manager</b>	<b>2019 Net Flows (\$ Mil)</b>	<b>2020 Net Flows (\$ Mil)</b>	<b>2021 Net Flows (\$ Mil)</b>	<b>2022 Net Flows (\$ Mil)</b>	<b>2023 Net Flows (\$ Mil)</b>
Vanguard	2,742	4,006	7,376	1,853	1,345
Dimensional	585	2,176	1,944	386	871
Brown Advisory	945	1,852	1,311	818	792
Fidelity	3,825	4,722	4,446	128	679
MSIM/Calvert	271	626	2,309	253	599
Boston Trust Walden	-37	204	458	100	374
Northern Trust	301	75	384	221	270
GMO	5	87	275	315	261
State Street	-105	573	987	435	216
TCW	127	-21	243	210	202

Source: Morningstar Direct. Data as of Dec. 31, 2023. Includes funds that have liquidated. Excludes funds of funds.

# U.S. Sustainable Funds: Assets

The largest funds and asset managers stayed at the top.

## Assets Rose on the Back of Market Appreciation

Despite net outflows, assets in sustainable funds rose to \$323 billion at the end of 2023.

- This represents a 12% decline from the all-time record seen at the end of 2021 but a 12% increase over assets at the end of 2022.

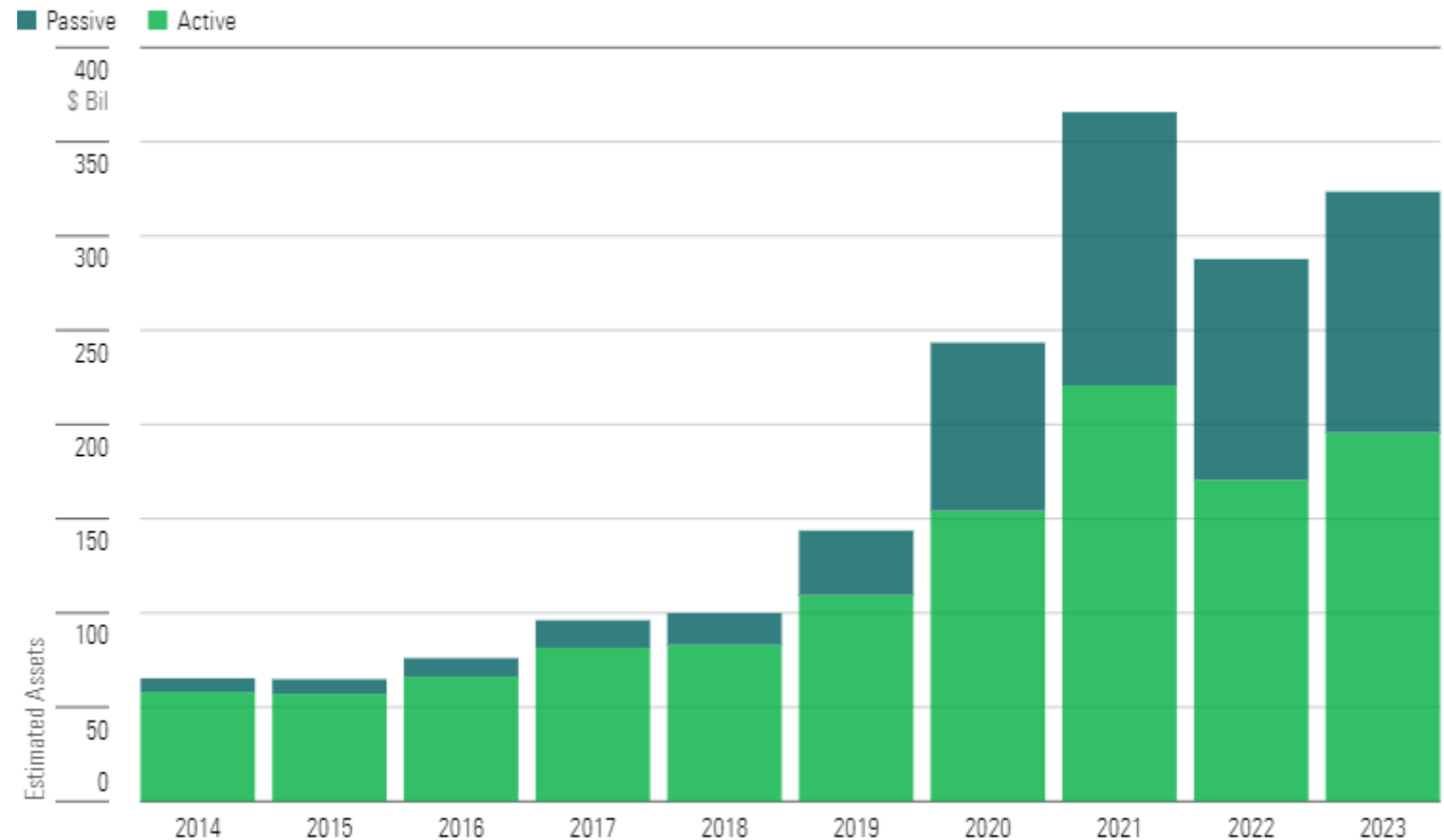
The U.S. sustainable funds landscape is nearly 6 times larger today than at the end of 2013. This is a result of growing investor demand as well as market appreciation.

- Investors have deposited nearly \$150 billion into sustainable funds over the past decade.
- Over the same period, equity markets have risen by 11.6% annualized, driving assets higher.

Actively managed funds continue to dominate the sustainable funds landscape, but low-cost passive funds have gained in popularity during recent years. As a result, active funds' market share has been on the decline.

- In 2014, active funds claimed nearly 90% of sustainable assets; that portion has hovered around 60% since 2020.

### Sustainable Fund Assets



Source: Morningstar Direct. Data as of Dec. 31, 2023. Includes funds that have liquidated. Excludes funds of funds.

## Parnassus Dominated the List of Actively Managed Sustainable Funds

Parnassus only offers six funds, but those offerings have a strong grip on U.S. investor appetite. Standing at \$27.8 billion in assets at the end of 2023, Parnassus Core Equity PRBLX has been the largest U.S. sustainable fund for more than 10 years.

- Parnassus has been fully dedicated to responsible and sustainable investing since the shop's founding in the 1980s. In addition to excluding fossil fuels, the funds rely on proprietary evaluations of environmental, social, and governance criteria to inform investment decisions. Furthermore, Parnassus has long been active in ESG-focused engagement and stewardship, using its status as a shareholder to encourage more sustainable practices among investee companies.
- The firm's process drives relatively concentrated portfolios, and at the end of 2023, Parnassus Core Equity, Parnassus Mid Cap PARMX, and Parnassus Value Equity PARWX each held fewer than 50 stocks.

It hasn't been easy for new active funds to break into the top 10 in terms of assets. Most of the largest active sustainable funds have held these spots for multiple years.

- Calvert Equity CSIEX and TIAA-CREF Social Choice Equity TISCX have remained among the top 10 largest active sustainable offerings for more than 10 years.
- TIAA-CREF Core Impact Bond TSBIX, DFA U.S. Sustainability Core 1 Portfolio DFSIX, Putnam Sustainable Leaders, and Parnassus Mid Cap all claim at least five years on the chart of the top 10 largest actively managed sustainable funds.

TIAA-CREF Core Impact Bond continues to be the only bond offering to reach the top 10 largest active funds. Its \$6.2 billion asset base is nearly double the runner-up, CCM Community Impact Bond CRAIX.

### 10 Largest Actively Managed Sustainable Funds

Name	Ticker	Inception Date	Total Assets (\$ Bil)
Parnassus Core Equity	PRBLX	8/31/1992	27.8
Brown Advisory Sustainable Growth	BAFWX	6/29/2012	8.8
Pioneer	PIODX	2/10/1928*	7.6
Calvert Equity	CSIEX	8/24/1987	7.1
TIAA-CREF Core Impact Bond	TSBIX	9/21/2012	6.2
DFA U.S. Sustainability Core 1 Portfolio	DFSIX	3/12/2008	6.1
TIAA-CREF Social Choice Equity	TISCX	7/1/1999	6.1
Putnam Sustainable Leaders	PNOPX	8/31/1990	5.8
Parnassus Mid Cap	PARMX	4/29/2005	5.4
Parnassus Value Equity	PARWX	4/29/2005	4.9

Source: Morningstar Direct. Data as of Dec. 31, 2023. Excludes funds of funds. \*Pioneer launched in 1928 and adopted a sustainable mandate in July 2021.

## iShares and Vanguard Traded Places but Stayed on Top

iShares and Vanguard are the incumbents when it comes to passive sustainable investing in the U.S. At the end of 2023, iShares claimed six of the top 10 spots for largest passive sustainable funds, and Vanguard claimed three.

- Vanguard FTSE Social Index was the largest passive sustainable fund until iShares ESG Aware MSCI USA ETF took its place in 2021. Outflows from the latter gave Vanguard the lead once more in 2023.
- From its inception in 2016, iShares ESG Aware MSCI USA ETF was on a rocket-launch growth trajectory. Looking at year-end assets, the fund nearly decupled (grew by 10 times) between 2019 and 2020. This matches the timing that it was added to BlackRock's Target Allocation ETF model portfolios. The fund nearly doubled again to reach \$25.7 billion at the end of 2021. However, market declines in 2022 and steep outflows in 2023 dropped assets back down to \$13.4 billion at the end of 2023.

Sustainable-investing specialist Calvert claims the oldest fund on the list. Calvert US Large-Cap Core Responsible Index CISIX is the only other fund—aside from Vanguard FTSE Social Index—to have landed among the top 10 largest passive sustainable offerings in each of the past 10 years.

- In 2023, Calvert launched an ETF version of this fund, which collected more than \$195 million over the course of the year. During the same period, the open-end vehicle shed \$48 million.

### 10 Largest Passive Sustainable Funds

Name	Ticker	Inception Date	Total Assets (\$ Bil)
Vanguard FTSE Social Index	VFTNX	1/14/2003	17.5
iShares ESG Aware MSCI USA ETF	ESGU	12/1/2016	13.4
iShares ESG Aware MSCI EAFE ETF	ESGD	6/28/2016	7.6
Vanguard ESG U.S. Stock ETF	ESGV	9/18/2018	7.5
iShares MSCI USA ESG Select ETF	SUSA	1/24/2005	5.3
Calvert US Large-Cap Core Responsible Index	CISIX	6/30/2000	4.8
iShares MSCI KLD 400 Social ETF	DSI	11/14/2006	4.1
iShares ESG Aware MSCI EM ETF	ESGE	6/28/2016	4.1
Vanguard ESG International Stock ETF	VSGX	9/18/2018	3.6
iShares ESG U.S. Aggregate Bond ETF	EAGG	10/18/2018	3.6

Source: Morningstar Direct. Data as of Dec. 31, 2023. Excludes funds of funds.

## Despite Outflows, BlackRock's Crown Refused to Budge

BlackRock's dominance in the sustainable-investing landscape is something to behold.

- In total, offerings from BlackRock and iShares gave up \$8.7 billion in 2023, the most of any asset manager in the U.S. These outflows made a small dent in the shop's sustainable fund assets, but it kept a \$20 billion lead over the runner-up.
- BlackRock has held first place since it passed Parnassus and Morgan Stanley/Calvert in 2020. At the end of 2019, BlackRock had just 16 sustainable funds in the U.S. One year later, it offered 44 sustainable strategies.

Although sustainable funds comprise less than 2% of BlackRock's assets in U.S. open-end and exchange-traded funds, its influence on the U.S. sustainable-investing landscape cannot be overstated.

- With nearly \$60 billion invested in sustainable funds, BlackRock manages more money than Vanguard and Nuveen, combined. Its mandate is also greater than the totality of the 138 smallest firms' sustainable assets.

Six of the top 10 asset managers have more than \$10 billion in sustainable assets each. Although they have traded places from year to year, these firms have held the top six spots since the end of 2017, when BlackRock's sustainable fund assets crossed \$2 billion for the first time.

Brown Advisory is the newest addition to this list, having nudged Eventide off the chart in 2022. Most of the firm's sustainable assets are concentrated in Brown Advisory Sustainable Growth, which has seen strong inflows in recent years and totaled \$8.8 billion in assets at the end of 2023.

### Top 10 Asset Managers by Sustainable Fund Assets

Asset Manager	2019 Total Assets (\$ Bil)	2020 Total Assets (\$ Bil)	2021 Total Assets (\$ Bil)	2022 Total Assets (\$ Bil)	2023 Total Assets (\$ Bil)
BlackRock/iShares	10.4	41.0	71.5	60.2	59.2
Parnassus	28.8	34.9	47.9	35.5	39.3
MSIM/Calvert	19.0	27.7	35.6	29.8	34.9
Vanguard	9.1	15.8	27.6	22.8	30.5
Nuveen/TIAA	11.1	17.1	23.0	19.6	21.7
Dimensional	9.1	13.2	17.3	10.0	13.1
Brown Advisory	2.1	5.1	7.9	6.3	9.8
Impax	4.8	6.3	9.0	7.6	8.5
Amundi	0.3	0.4	8.8	7.3	8.5
Invesco	3.0	10.7	11.9	9.0	7.8

Source: Morningstar Direct. Data as of Dec. 31, 2023. Includes funds that have liquidated. Excludes funds of funds. Although MSIM acquired Calvert in 2021, historical records are combined such that 2019 and 2020 data reflects MSIM as well as Calvert.

# U.S. Sustainable Funds: Arrivals & Departures

Launches slowed down, while closures picked up.

## Sustainable Funds Appear in a Variety of Asset Classes

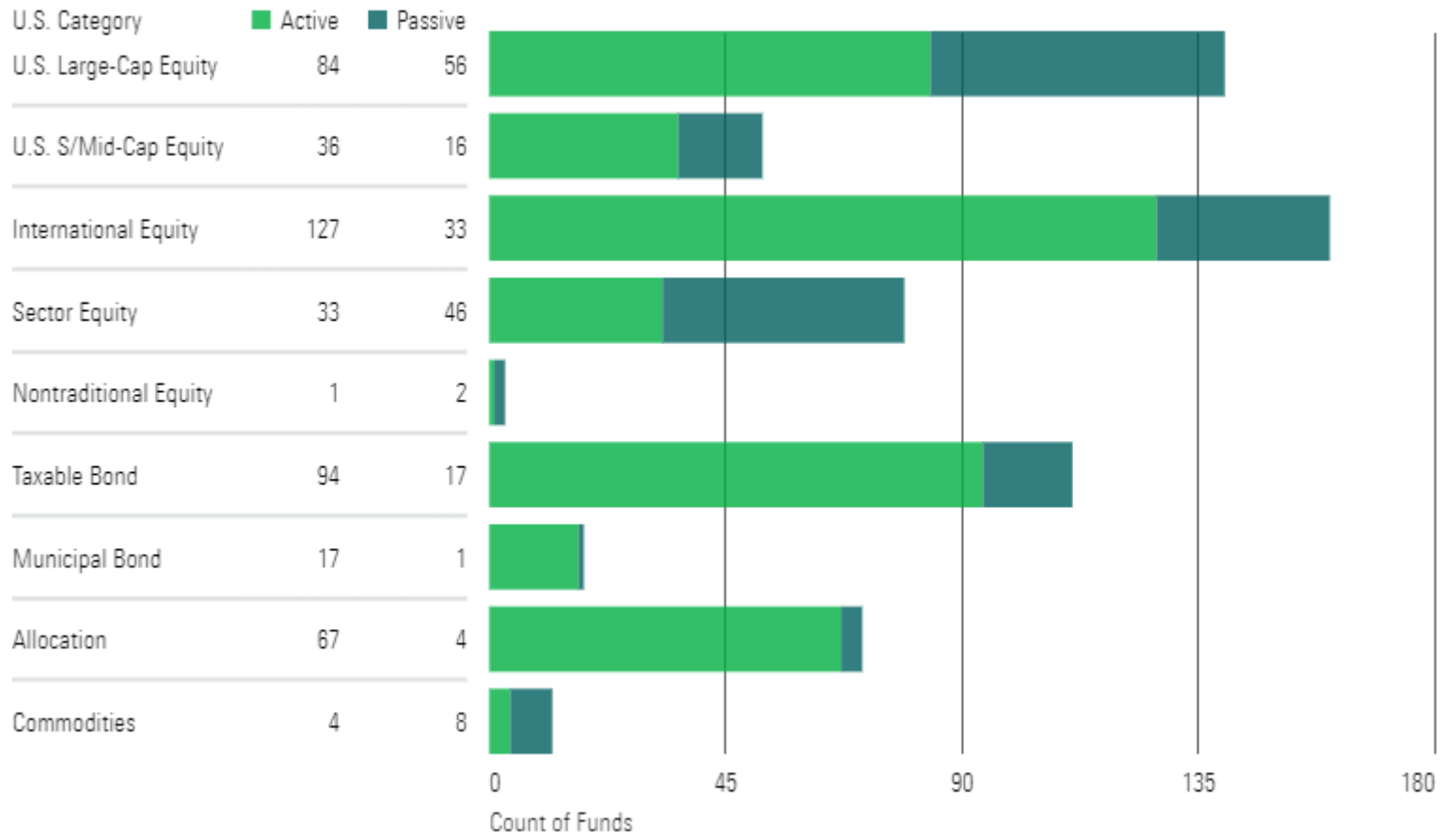
Of the 646 sustainable funds, 434 are equity funds, 129 are fixed-income funds, and 71 are allocation funds.

Commodities entered the stage in 2022 and counted one dozen offerings at the end of 2023, most of which trade carbon credits. Overall, investors can find sustainable funds in 72 Morningstar Categories.

Investors have the most choices in U.S. equity, with 192 funds, and another 160 funds are international-equity offerings. Taxable bonds, including high-yield and corporate bonds, dominate the sustainable fixed-income landscape because ESG data tends to be more readily available in the corporate space. However, access to data has steadily improved, and U.S. investors now have more than a dozen municipal-bond offerings to choose from.

Sustainable municipal-bond funds offer an opportunity to drive impact in local communities, since the proceeds often contribute to tangible improvements in areas such as literacy programs and revitalizing infrastructure. Data availability remains a barrier because small communities may not have resources to provide consistent reporting on these projects, but the opportunity is significant.

### Sustainable Funds by Asset Class



Source: Morningstar Direct. Data as of Dec. 31, 2023. Does not include obsolete funds.



## Product Development Slowed a Bit

Sustainable fund launches slowed compared with previous years. In 2023, 66 new funds came to market, well above the 15 seen 10 years ago but down from the incredible 100-plus funds launched in 2021 and 2022.

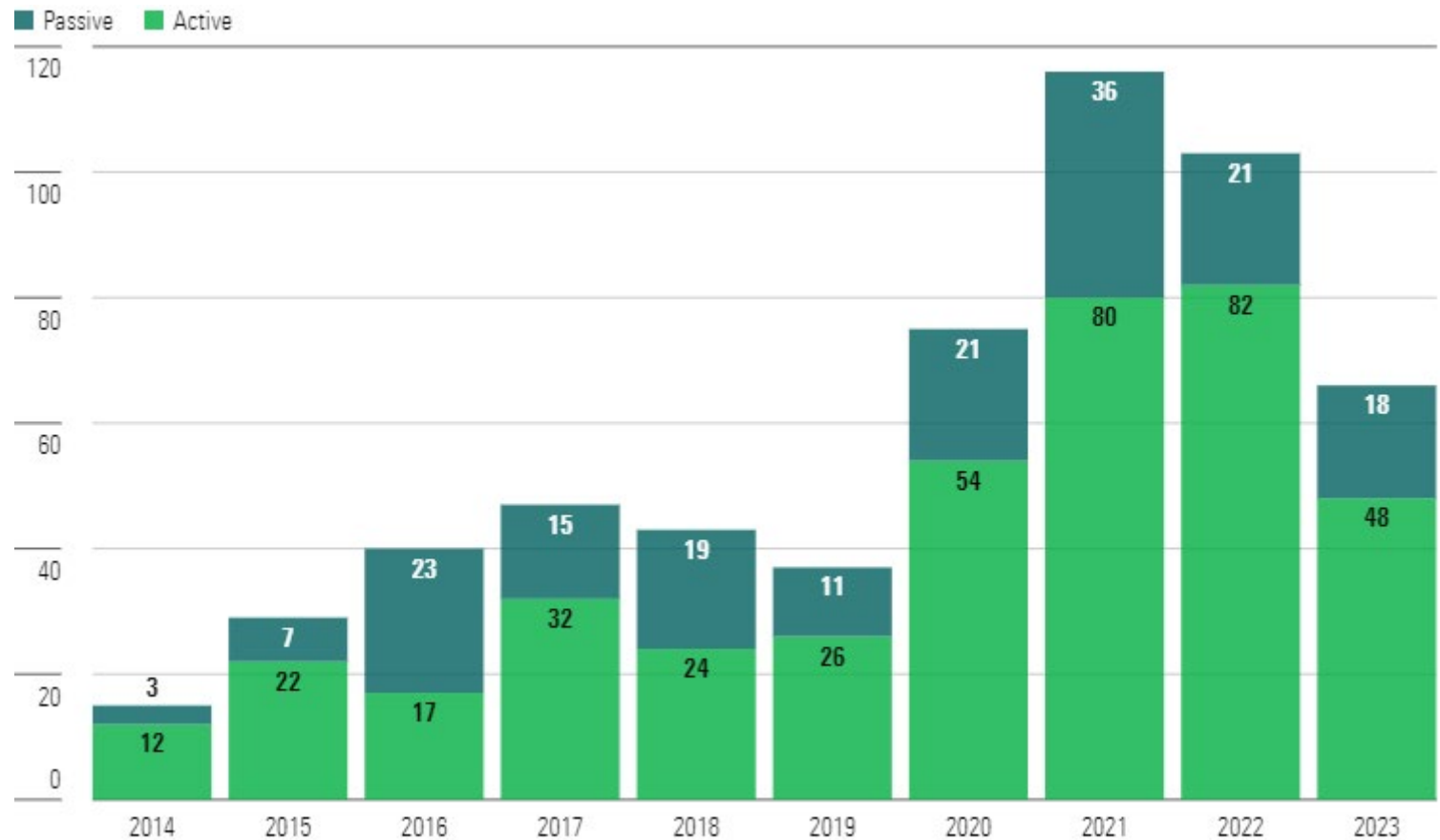
Active management continues to be the go-to for product development teams despite steady investor preference for index-tracking options. In 2023, nearly three fourths of all new sustainable funds were actively managed, slightly above average for the past 10 years.

- The only year that passive funds made up the majority of new sustainable fund launches was in 2016, when Nuveen and iShares each launched five new sustainable offerings.

More than three fourths of 2023's new launches came to market during the first half, when Fidelity debuted its sustainable target-date series and some stand-alone funds.

- Fidelity's target-date strategy marks the fourth such option available to U.S. investors, following the Natixis Sustainable Future series from 2017, the BlackRock LifePath ESG Index series in 2020, and the Putnam Sustainable Retirement series from first-quarter 2023.

### Sustainable Fund Launches



Source: Morningstar Direct. Data as of Dec. 31, 2023. Includes funds that have liquidated. Does not include original launches of funds that have subsequently repurposed.

## Most New Sustainable Offerings Were Equity Funds

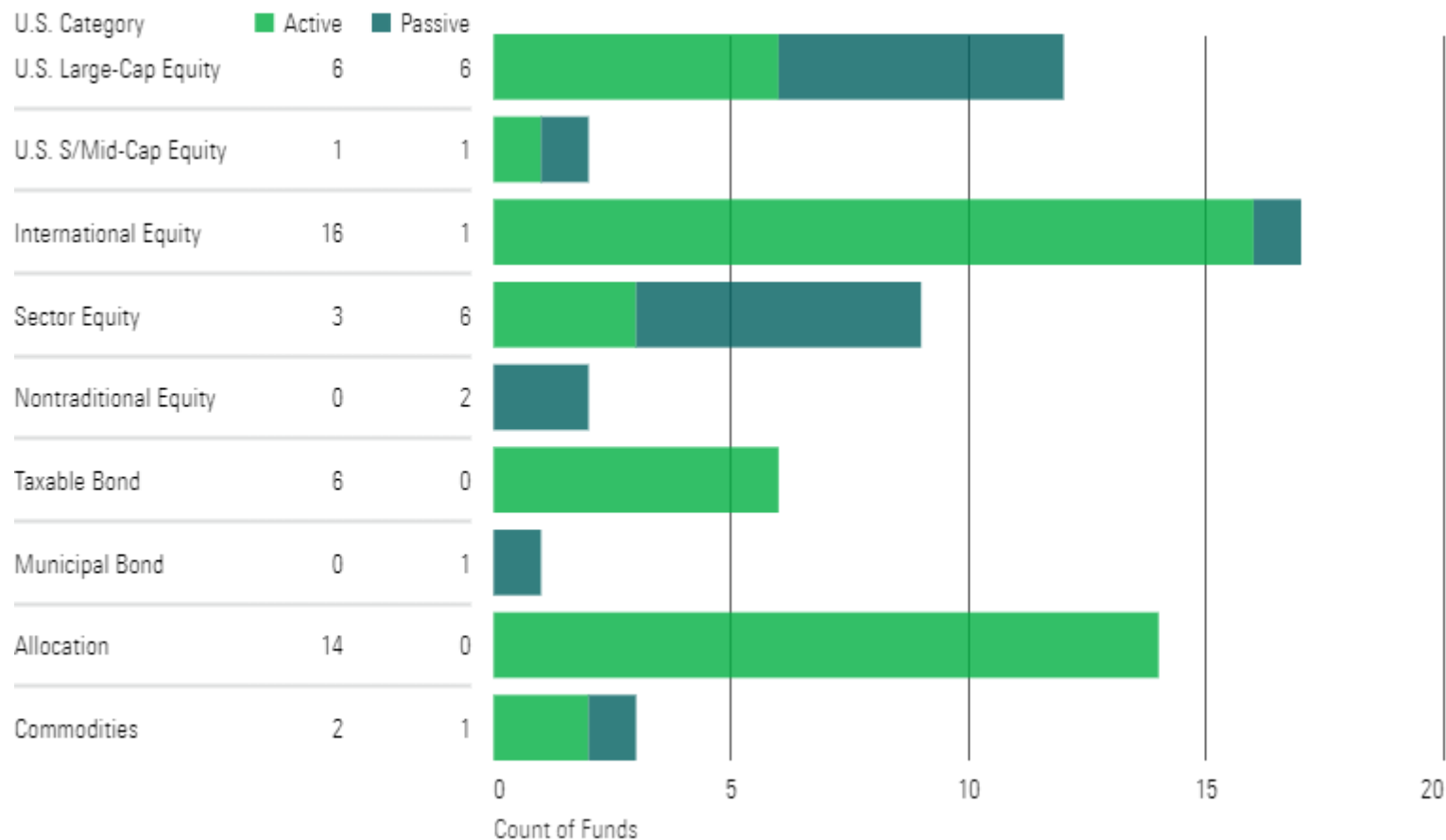
Nearly two thirds of new launches are equity funds. The ranks of international equity and sector equity funds increased by 17 and nine, respectively.

- International equity fund Impax Global Social Leaders IGSIX launched in November and aims to invest in companies whose products or services address societal challenges, such as broadening economic opportunities, and that foster diverse, inclusive, and equitable workplace cultures.
- GMO Resource Transition GMOYX launched in mid-February and invests primarily in equities that will benefit from the long-term rise in natural-resources prices caused by a combination of finite supply and increased demand.

The 66 new funds were placed in 34 Morningstar Categories—U.S. large blend and global large-stock blend claimed eight and seven new entrants, respectively. BlackRock Sustainable Advantage Global Equity Fund MASCX falls in the U.S. global large-stock blend category and aims to maintain certain ESG and climate risk characteristics relative to its benchmark.

### Sustainable Fund Launches in 2023 by Category Group

Nearly three fourths of new launches are index-tracking options.



Source: Morningstar Direct. Data as of Dec. 31, 2023.

## ETFs Were the Most Popular Vehicle for Sustainable Funds

Long heralded as a pioneer of responsible investing, Calvert brought seven new funds to market in 2023, all but one of which are passive ETFs. Calvert US Large-Cap Diversity, Equity, and Inclusion Index ETF CDEI falls in the U.S. large-blend category and looks to invest in companies that successfully manage DEI issues.

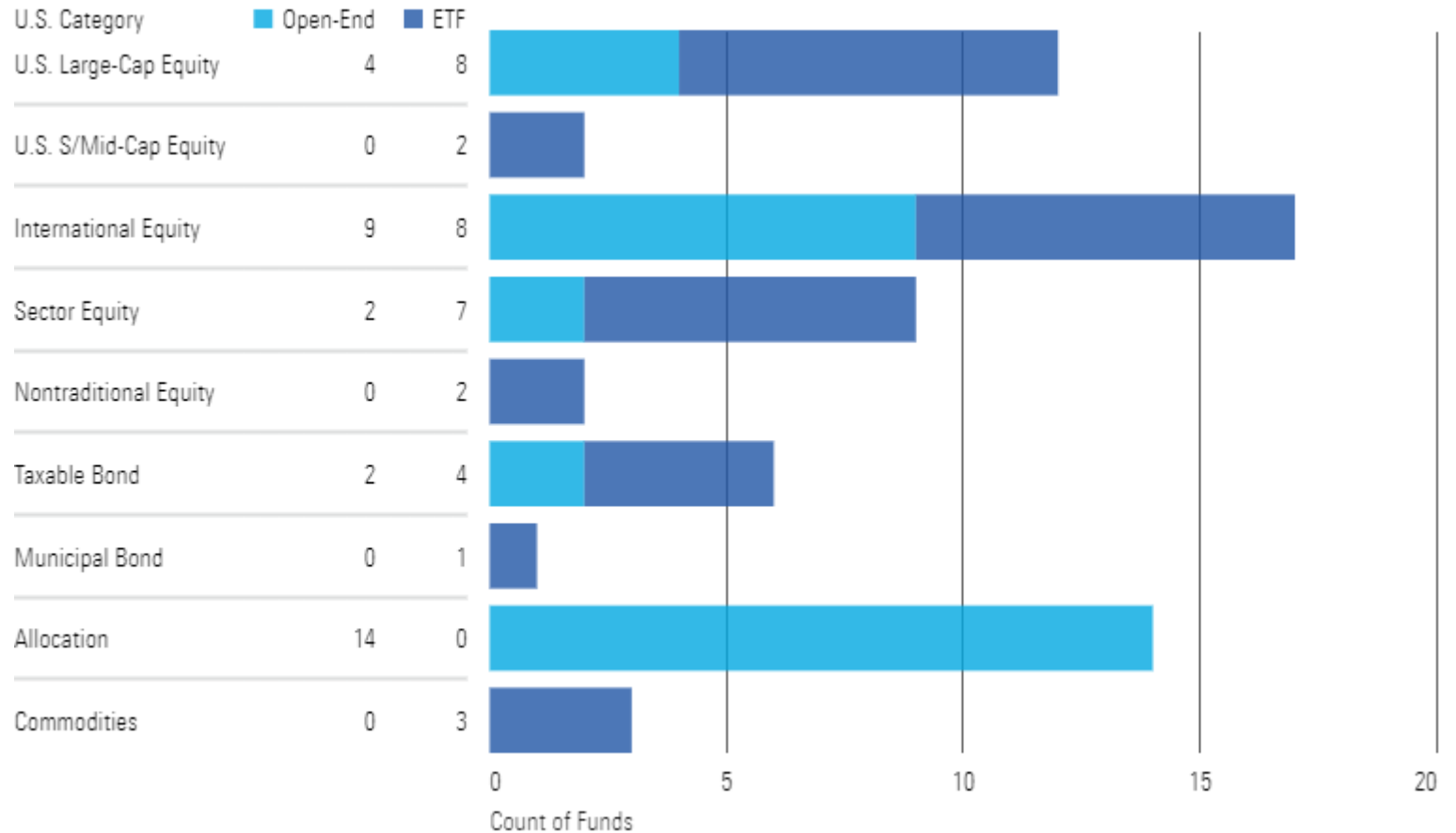
Similarly, Putnam launched five actively managed ETFs. Three of the funds offer exposure to different sectors of the fixed-income market.

ETFs have grown as the most popular vehicle for sustainable fund launches since the first—iShares MSCI USA ESG Select ETF SUSA—launched in January 2005. In 2021 and 2022, ETFs accounted for more than 60% of new sustainable fund launches in 2022. In 2023, however, that proportion dropped to 53%.

- On average over the past decade, nearly half of new sustainable funds have launched as ETFs.
- Increasingly, fund managers have looked to ETFs to house actively managed strategies, too. In 2020, one third of new ETF launches were actively managed; in 2023, that share was nearly 50%.

### Sustainable Fund Launches in 2023 by Category Group

More than half of new launches are exchange-traded funds.



Source: Morningstar Direct. Data as of Dec. 31, 2023.

## Xtrackers and iShares Provide Largest New Sustainable ETFs

Xtrackers MSCI USA Climate Action Equity ETF USCA led the pack as the largest new offering, with nearly \$1.9 billion in assets at the end of 2023. The fund provides a climate-friendly approach to investing in the U.S. large- and mid-cap space.

ETFs from iShares stay close to the top, with the second-largest offering in 2023.

- iShares Climate Conscious & Transition MSCI USA ETF launched in June 2023 and gained \$1.8 billion by the end of the year.
- Last year, iShares Paris-Aligned Climate MSCI USA ETF launched in February and amassed more than \$800 million by the end of the year.

Putnam launched various ETFs that topped the list of largest new funds.

- Putnam ESG Core Bond ETF PCRB launched in mid-January and amassed more than \$490 million by the end of the year.

### New Sustainable Funds With Assets Greater Than \$100 Million at the End of 2023

Name	Ticker	Inception Date	Fund Assets (\$ Mil)
Xtrackers MSCI USA Climate Action Equity ETF	USCA	4/3/2023	1,867
iShares Climate Conscious & Transition MSCI USA ETF	USCL	6/6/2023	1,809
Putnam ESG Core Bond ETF	PCRB	1/19/2023	491
Calvert US Large-Cap Core Responsible Index ETF	CVLC	1/30/2023	251
Putnam Panagora ESG International Equity ETF	PPIE	1/19/2023	139
GMO Resource Transition	GMOYX	2/15/2023	139
Putnam ESG Ultra Short ETF	PULT	1/19/2023	117
Putnam ESG High Yield ETF	PHYD	1/19/2023	109
GuideStone Funds-Impact Equity	GMEYX	1/27/2023	108

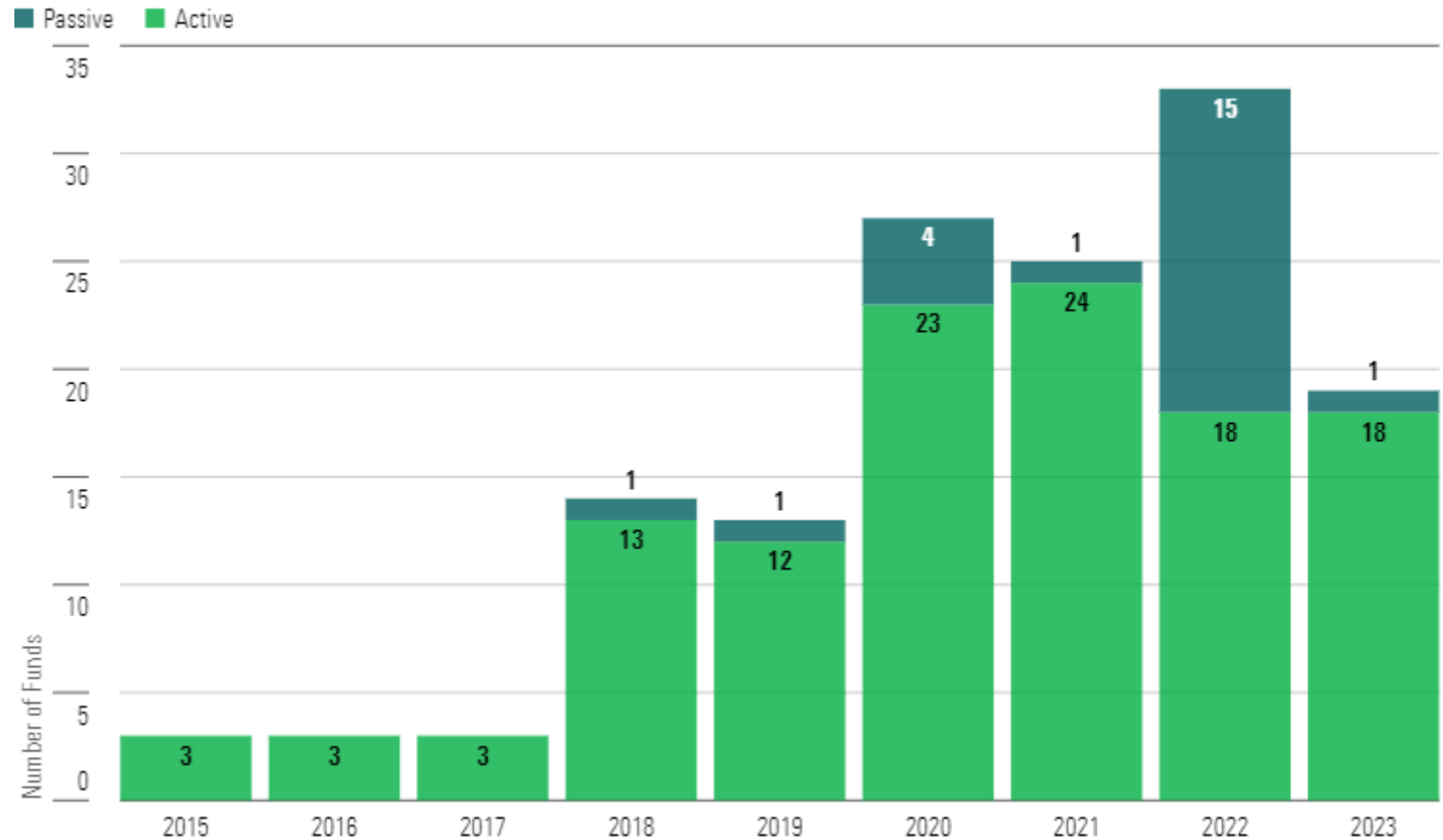
Source: Morningstar Direct. Data as of Dec. 31, 2023. Excludes funds of funds.

## Fund Shops Continued to Retool Active Funds

Last year, 19 existing funds changed their investment strategies to become sustainable funds. In many cases, these funds also changed their names to reflect their repurposing. That brings the total count of repurposed funds in the current sustainable funds universe to 119.

The most common candidates for retooling tend to be actively managed funds experiencing chronic outflows. As investor demand for sustainable funds continues to grow, converting these active funds into sustainable offerings, rather than launching new funds, can be an attractive strategy for some asset managers.

### Repurposed Funds



Source: Morningstar Direct. Data as of Dec. 31, 2023. The count of repurposed funds in 2022 was revised to include funds that qualified for the Sustainable Investment designation following Morningstar's update to the [Sustainable Attributes methodology](#).

## Putnam Had a Head Start in Garnering Assets for Its ESG Target-Date Series

The largest funds to adopt sustainable mandates in 2023 were part of Putnam's sustainable retirement series, which counted nearly \$1.5 billion in assets at the end of 2023. In the first quarter of 2023, the firm launched a handful of actively managed ETFs that are building blocks for its new sustainable retirement target-date strategy, Putnam Sustainable Retirement Funds. The series implements a similar retirement glide path philosophy as the firm's other target-date offering, Putnam Retirement Advantage, and offers vintages for every five years from 2025 through 2065, along with a maturity fund.

- The firm launched the new series in the wake of the Department of Labor's new rule for retirement plans allowing the plan sponsors to consider ESG factors when vetting investments.

Similarly, effective June 30, 2023, the name of the Nuveen Enhanced Yield 1-5 Year U.S. Aggregate Bond ETF was changed to Nuveen ESG 1-5 Year U.S. Aggregate Bond ETF NUSA as the investment strategy incorporated ESG in its investment criteria.

### Five Largest Funds Repurposed as Sustainable in 2023

Name	Ticker	Date of ESG Adoption	Inception Date	Fund Assets (\$ Mil)
Putnam Sustainable Retirement Series	PRZZX*	2/10/2023	11/1/2004	1,490*
Community Development Fund	CDCDX	5/1/2023	4/29/2016	134
Calvert Small/Mid-Cap	CMPAX	9/15/2023	4/22/1968	61
Calvert Global Small-Cap Equity	CSMAX	9/15/2023	3/4/2002	28
Nuveen ESG 1-5 Year U.S. Aggregate Bond ETF	NUSA	6/30/2023	3/31/2017	25

Source: Morningstar Direct. Data as of Dec. 31, 2023. \*Putnam Sustainable Retirement Series assets reflect the sum of assets across all open-end vehicles in the strategy.

## Closures and Departures Reached an All-Time High

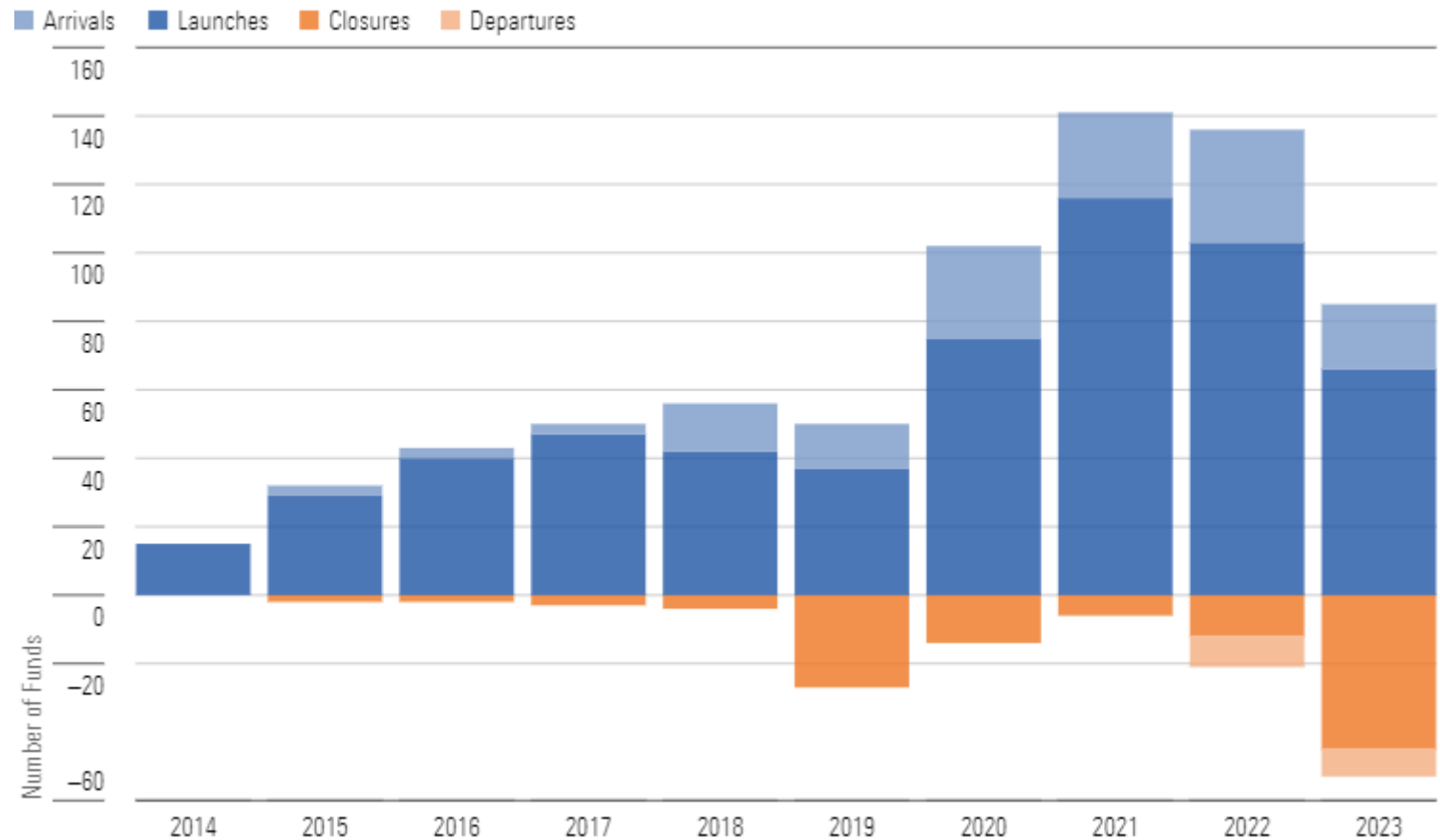
New launches continued in 2023, but closures and departures also reached an all-time high.

- In 2023, 66 new funds came to market, and 16 existing funds were added to the sustainable funds landscape (labeled “Arrivals” in the exhibit to the right).
- During the same period, 45 sustainable funds closed, and eight funds moved away from ESG mandates (labeled “Departures”).

Of the 45 sustainable funds liquidated in 2023, the largest (in terms of assets) came from Columbia Threadneedle and BlackRock.

- Columbia Threadneedle shuttered Columbia U.S. Social Bond Fund in August; it had amassed \$35.8 million in its eight years on the market.
- After 13 years on the market, BlackRock Sustainable Emerging Markets Flexible Bond fund was closed with \$34 million in assets.

### Sustainable Funds: New Arrivals & Departures



Source: Morningstar Direct. Data as of Dec. 31, 2023.

# U.S. Sustainable Funds: Investment Performance

Sustainable funds lagged peers, but by a smaller margin than in 2022.  
Some sustainable funds stand out on multiple Morningstar metrics.



## Sustainable Funds Delivered Mediocre Returns in 2023

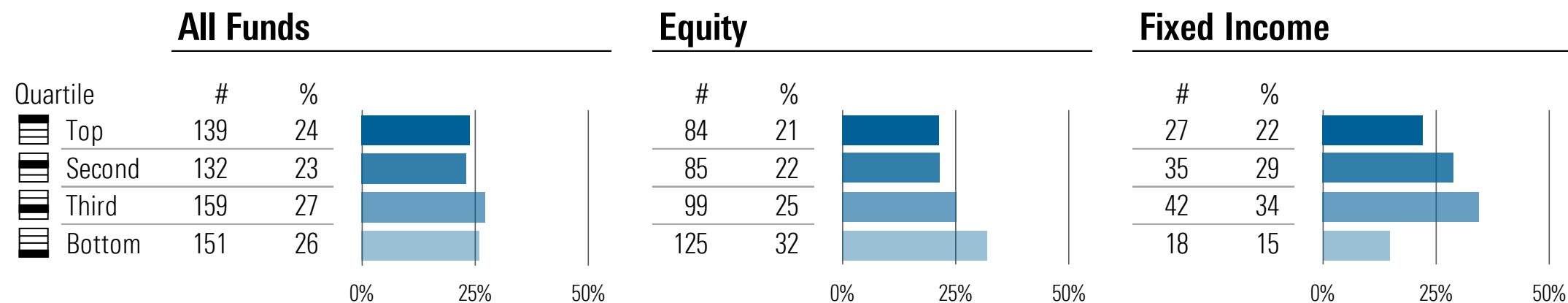
To evaluate the investment performance of sustainable funds, we can compare how their returns rank relative to their respective Morningstar Category peers. In terms of total returns, sustainable funds lagged their conventional peers slightly in 2023, with 53% of sustainable funds landing in the bottom half of their respective Morningstar Categories.

Equity funds suffered the worst of the underperformance, and 32% of sustainable equity funds dropped to the bottom quartile relative to peers.

- Among large-blend equity funds (the largest grouping within the U.S. sustainable funds landscape), the median return for sustainable funds was 24.4% in 2023. This beat the 23.9% median gain for the overall category (encompassing both sustainable and conventional funds) by a small margin but lagged the 26.4% gain for the Morningstar US Market Index.

In the case of fixed-income funds, roughly one third of sustainable offerings landed in the third quartile relative to peers. However, they did a better job than peers at avoiding the lowest returns, and only 15% landed in the bottom quartile.

### Sustainable Funds 2023 Return Rank by Morningstar Category Quartile



Source: Morningstar Direct. Data as of Dec. 31, 2023.

## Sustainable Equity Funds Stood Out in the Intermediate Term

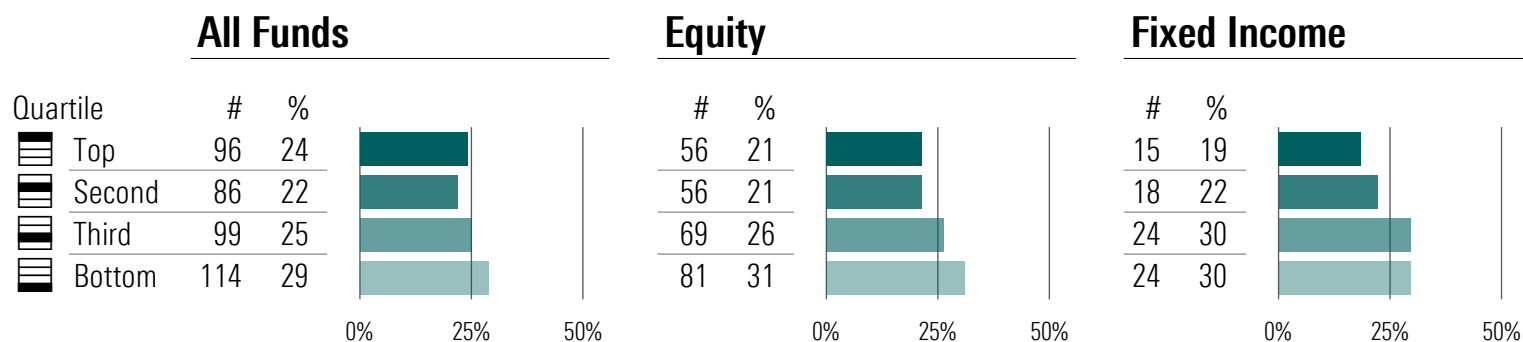
Overall, the distribution of sustainable funds across their respective categories looks similar in the trailing three-year period, compared with 2023. However, they held up better than conventional peers in terms of trailing five-year returns, where 60% of sustainable funds landed in the top half of their respective categories.

Although sustainable equity funds lagged conventional peers in terms of total returns over the trailing three-year period, their fortunes reversed when including 2019 and 2020 (as shown in the trailing five-year period).

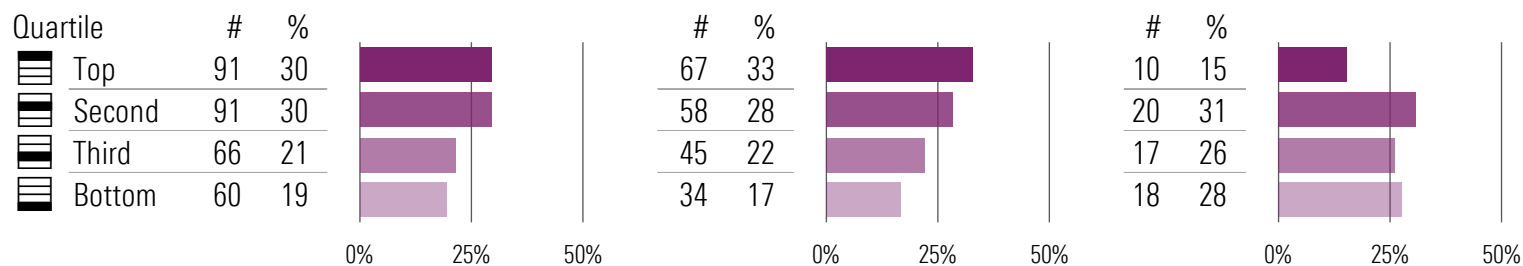
On the other hand, over the trailing three-year and five-year periods, sustainable bond funds found themselves in the bottom half of their respective categories more often than not.

### Sustainable Funds Three- and Five-Year Trailing Performance by Morningstar Category Quartile

#### Three-Year



#### Five-Year



Source: Morningstar Direct. Data as of Dec. 31, 2023.

# Sustainable Large-Blend Funds Posted Mixed Returns in 2023 but Held Up Well Over the Trailing Five Years

U.S. large-blend funds make up more than 13% of the sustainable funds landscape, and they tend to be the core allocation in most investor portfolios. Therefore, this category is often one of the first candidates for integrating ESG-focused funds into a portfolio.

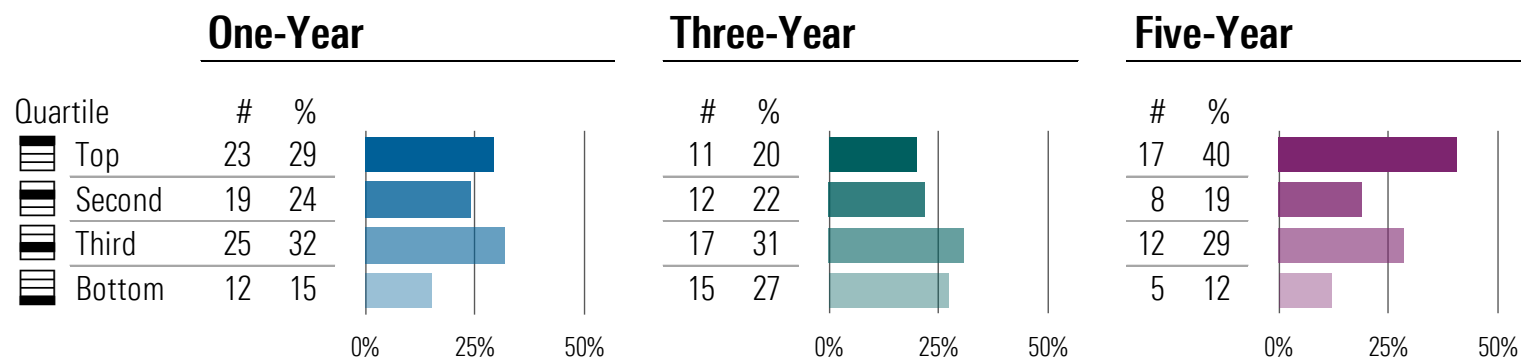
- In 2023, sustainable U.S. large-blend funds bounced back from poor performance in 2022. More than half of sustainable U.S. large-blend funds landed in the top half of the overall U.S. large-blend category.
- Medium-term returns benefited from strong gains in 2019 and 2020, and 40% of these funds remained in the top quartile for the trailing five-year period.

Venturing overseas, more than 50% of sustainable foreign large-blend funds finished in the top half of the overall category in 2023.

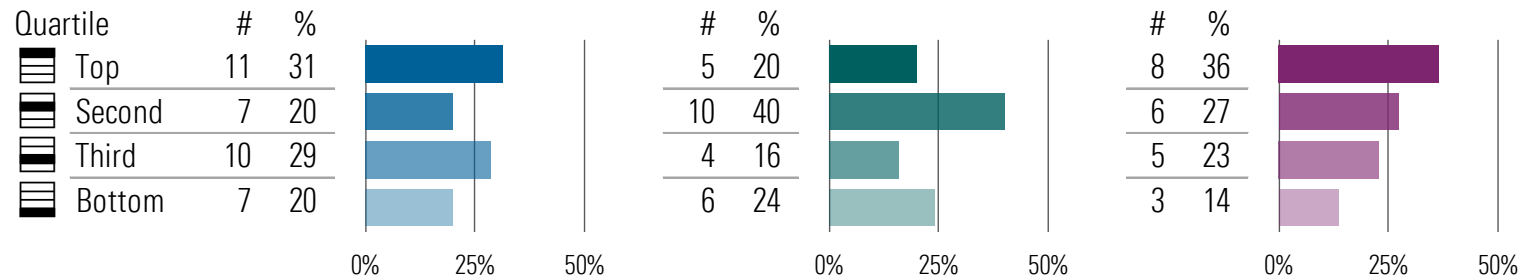
- Weak returns in 2022 weighed on these funds' three-year track records.
- Although not many sustainable foreign large-blend funds have five-year track records, more than one third of these funds remained in the top quartile over the period.

## U.S. and Foreign Large-Blend Sustainable Funds Three- and Five-Year Trailing Performance by Morningstar Category Quartile

### U.S. Large Blend



### Foreign Large Blend



Source: Morningstar Direct. Data as of Dec. 31, 2023.

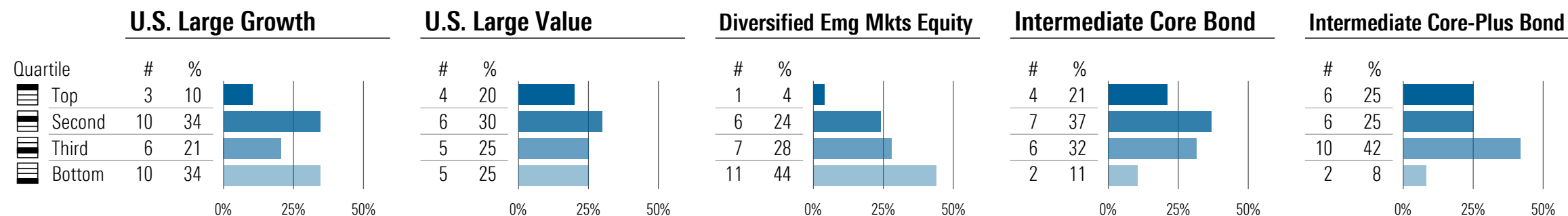
## Sustainable Funds in Various Asset Classes Performed on Par With Peers in 2023

Five other categories are worthy of examination: U.S. large growth, U.S. large value, diversified emerging-markets equity, intermediate core bond, and intermediate core-plus bond funds. We can look at one-year performance versus category peers, but conclusions should be tempered given the small sample size. For instance, 29 sustainable large-growth funds have a one-year track record, but only 19 sustainable intermediate core bond funds do.

To varying degrees, sustainable funds in our five other notable asset classes mostly performed on par with peers.

- Sustainable funds struggled overseas, especially in emerging markets, where nearly three fourths of diversified emerging-markets equity funds finished in the bottom half of the category.
- In U.S. large growth, sustainable funds were more likely to end up in the bottom half of their respective categories, but it was a 50/50 split for U.S. large-value funds.
- Within fixed-income, sustainable intermediate core bond funds didn't shoot the lights out, but they held up well relative to peers, and only 11% of these funds finished the year in the bottom quartile. Their core-plus bond counterparts were split evenly between the top and bottom half of the category and were similarly underrepresented in the bottom quartile. This matches the dynamic in 2021 and 2022, when sustainable core-plus bond funds saw an even 50/50 split between leaders and laggards.

### Sustainable Funds in Five Major Categories Deliver Mixed Returns vs. Category Peers



Source: Morningstar Direct. Data as of Dec. 31, 2023.

## A Handful of Sustainable Funds Stack Up Well on Multiple Morningstar Metrics

Looking ahead, we can consult forward-looking ratings to identify those funds that Morningstar’s manager research team believes will outperform. Under the Morningstar Medalist Rating system, more than 300 sustainable funds earn our higher ratings. Of those, 11 are offered by asset managers that earn top marks on the Morningstar ESG Commitment Level.

- The ESG Commitment Level is a qualitative measure of the extent to which asset managers incorporate ESG considerations into their investment processes. The scale runs from best to worst as follows: Leader, Advanced, Basic, and Low. In many cases, firms that earn the Leader or Advanced designation have focused on sustainable investing since day one, and this philosophy remains core to their identities today. They have stayed at the cutting edge of evolving investor expectations for sustainable strategies and ground their investment philosophies in outcomes-focused active ownership practices.

All but two—TIAA-CREF Green Bond TGRNX and TIAA-CREF Core Impact Bond TSBIX—of the top 11 are equity funds. Parnassus Core Equity PRBLX leads the pack in terms of assets and earns the highest merit under both ratings systems. Small but mighty Boston Trust Walden Small Cap BOSOX also fares well under both assessments. In terms of sustainability performance, seven of the top 11 earn High Morningstar Sustainability Ratings, a sign that their portfolios are exposed to little ESG risk compared with peers.

### Top Sustainable Gold, Silver, and Bronze Funds

	Ticker	Morningstar Category	Morningstar Medalist Rating	Morningstar Medalist Rating Analyst Driven Percentage (%)	Morningstar ESG Commitment Level	Inception Date	Fund Size (\$ Mil)	2023		Morningstar Sustainability Rating	Prospectus Adjusted Expense Ratio
								Total Return	% Rank Category		
Parnassus Core Equity	PRBLX	Large Blend	Gold	100	Leader	8/31/1992	27,806	24.9	43	5 stars	0.82
Boston Trust Walden Small Cap	BOSOX	Small Blend	Gold	100	Leader	12/16/2005	1,294	10.1	91	5 stars	1.00
Brown Advisory Sustainable Growth	BAFWX	Large Growth	Silver	100	Advanced	6/29/2012	8,750	39.1	46	5 stars	0.64
Parnassus Mid-Cap	PARMX	Mid-Cap Blend	Silver	100	Leader	4/29/2005	5,401	12.7	78	5 stars	0.96
TIAA-CREF Core Impact Bond	TSBIX	Intermediate Core Bond	Bronze	100	Advanced	9/21/2012	6,194	6.0	32	5 stars	0.37
TIAA-CREF Social Choice Equity	TISCX	Large Blend	Bronze	100	Advanced	7/1/1999	6,125	22.5	59	5 stars	0.18
Impax Global Environmental Markets	PGINX	Global Large-Stock Blend	Bronze	100	Leader	3/27/2008	2,447	16.9	63	5 stars	0.91
TIAA-CREF Social Choice International Equity	TSONX	Foreign Large Blend	Bronze	100	Advanced	8/7/2015	1,577	19.3	14	5 stars	0.37
Parnassus Mid Cap Growth	PARNX	Mid-Cap Growth	Bronze	100	Leader	12/27/1984	829	36.6	5	5 stars	0.80
TIAA-CREF Green Bond	TGRNX	Intermediate Core-Plus Bond	Bronze	100	Advanced	11/16/2018	153	6.4	43	5 stars	0.45
Impax Global Opportunities	PXGOX	Global Large-Stock Growth	Bronze	100	Leader	6/27/2018	122	15.5	84	5 stars	0.98

Source: Morningstar Direct. Data as of Dec. 31, 2023.

# U.S. Sustainable Funds: Investment Performance

Sustainable bond funds held up well on a risk-adjusted basis.

## Sustainable Equity Funds Trailed Their Benchmarks in 2023

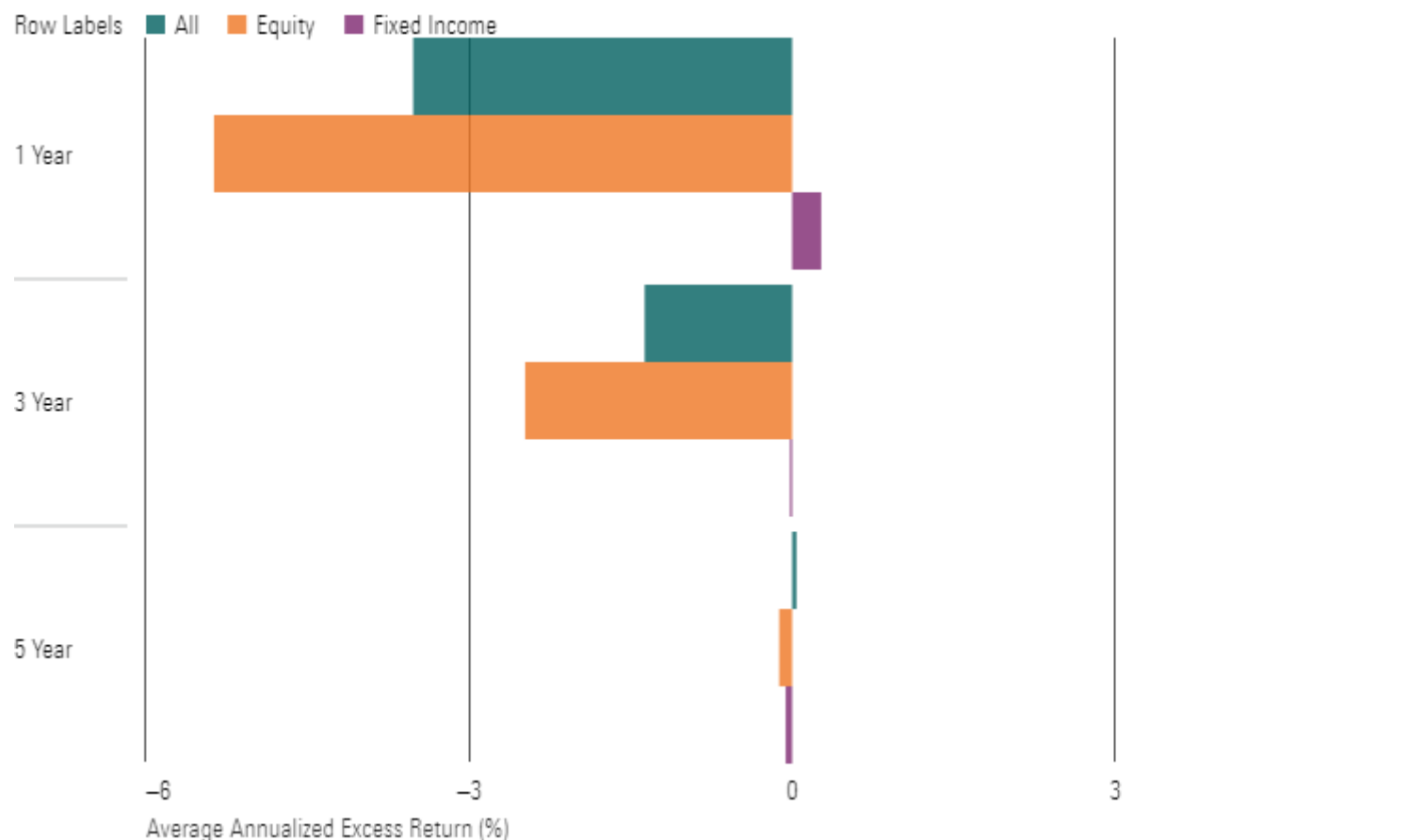
There are two main bogies against which we evaluate performance: category peers and the category index. Measuring a fund's performance relative to its category index helps to mitigate style biases and highlights the importance of fees. Compared against a costless benchmark, funds that charge high fees incur high hurdles to outperform.

On average in 2023, sustainable funds trailed their respective category benchmarks by 3.5 percentage points.

- Equity funds suffered the worst of the underperformance. More than half of sustainable equity funds lagged their respective benchmarks, and the shortfall was 5.4 percentage points on average.
- Within equities, clean energy funds were the hardest hit. ProShares S&P Kensho Cleantech ETF CTEX and Firsthand Alternative Energy ALTEX each lagged the Morningstar US Technology Index by more than 60 percentage points.

Fixed-income was the lone bright spot for sustainable investors in 2023. RBC BlueBay Strategic Income RBSRX achieved the highest excess returns, beating its category index by 4.7 percentage points.

**Sustainable Funds: Average Annualized Excess Return vs. Morningstar Category Indexes**



Source: Morningstar Direct. Data as of Dec. 31, 2023. 1 Year sample includes 393 equity funds and 119 fixed-income funds. 3 Year sample includes 262 equity funds and 81 fixed-income funds. 5 Year sample includes 204 equity funds and 65 fixed-income funds. Does not include obsolete funds.

## Sustainable Bond Funds Delivered Lower Levels of Risk

The previous slide showed that sustainable fixed-income funds slightly underperformed their respective category indexes over the trailing three- and five-year period. However, these funds held up relatively well on a risk-adjusted basis (as measured by the Sharpe ratio).

- Nearly 60% of sustainable bond funds delivered Sharpe ratios better than their respective category indexes.

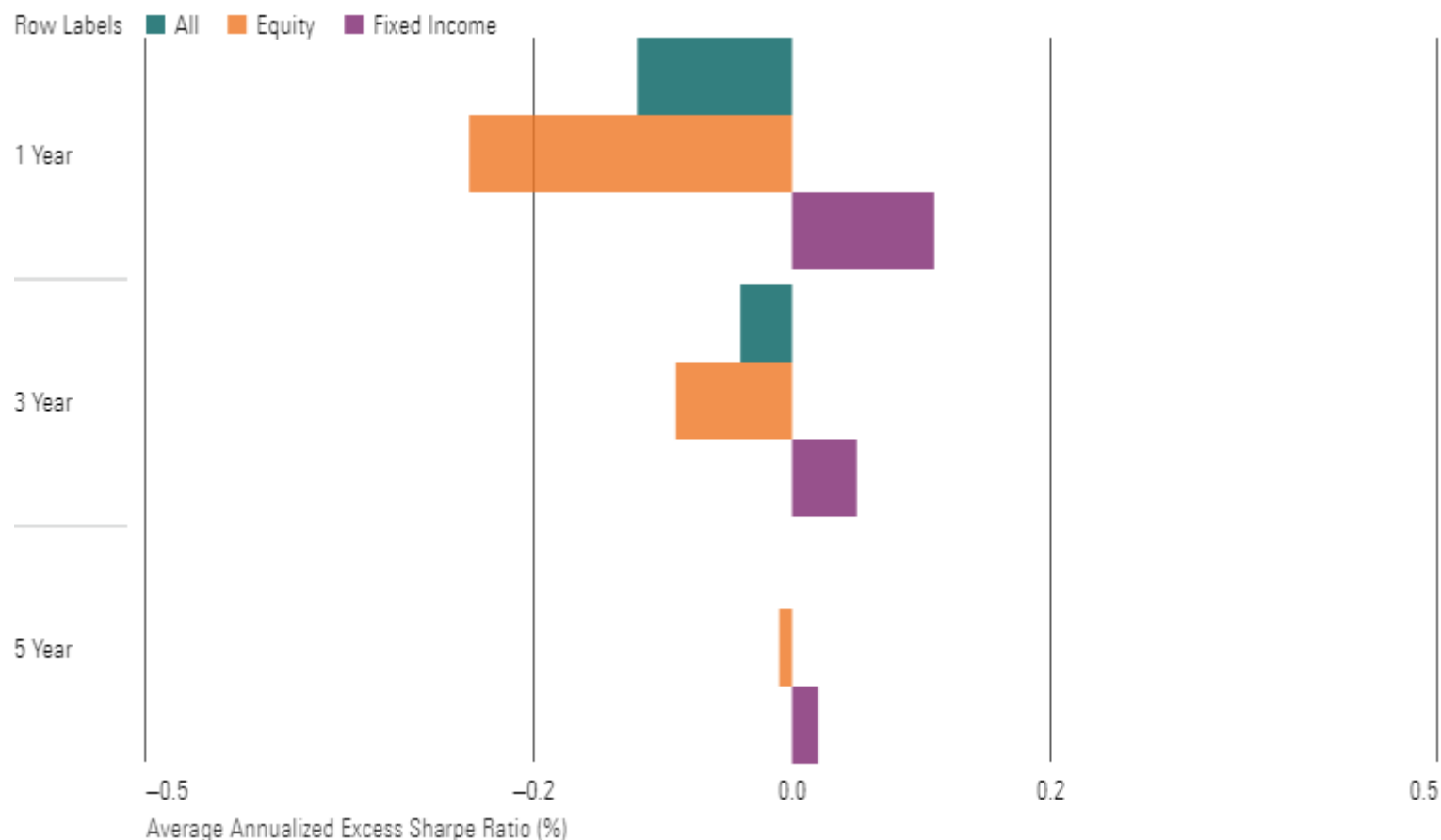
In 2023, most sustainable equity funds underperformed their respective category indexes, but those funds in the natural resources Morningstar Category stood out.

- On average, these funds beat the S&P Global Natural Resources Index on a total- and risk-adjusted basis, by 6.4 percentage points and 0.3%, respectively.

Across the market-cap spectrum, sustainable value funds held up well, too.

- Small-value funds, global large-stock value funds, and foreign large-value funds beat their respective benchmarks in terms of total- and risk-adjusted returns.

**Sustainable Funds: Average Annualized Excess Sharpe Ratio vs. Morningstar Category Indexes**



Source: Morningstar Direct. Data as of Dec. 31, 2023. 1 Year sample includes 393 equity funds and 119 fixed-income funds. 3 Year sample includes 262 equity funds and 81 fixed-income funds. 5 Year sample includes 204 equity funds and 65 fixed-income funds. Does not include obsolete funds.



## Sustainable Funds Didn't Shoot the Lights Out, for Better or Worse

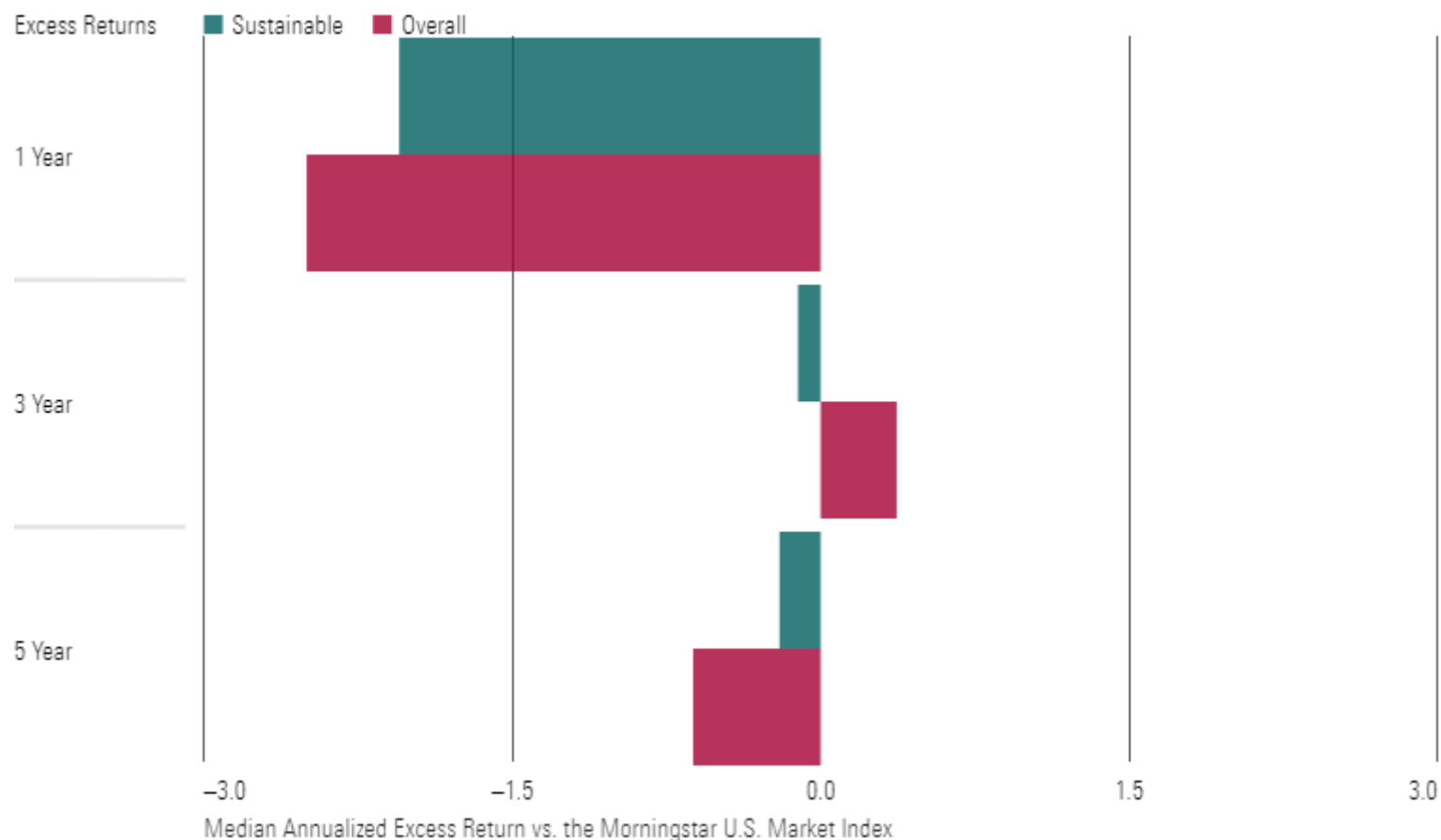
Within the large-blend equity category, sustainable funds' out- and underperformance over various time periods was often more muted than that of conventional peers.

- In 2023, both sustainable funds and conventional peers lagged the Morningstar US Market Index, but the median shortfall was smaller for sustainable funds than for conventional peers.
- The top-performing sustainable equity fund was IQ Candriam U.S. Large Cap Equity ETF IQSU, which gained 32 percentage points during the year.

In 2022, sustainable funds underperformed their conventional peers, in part because they didn't participate as fully in the energy rally that followed Russia's invasion of Ukraine.

- This is reflected in the trailing three-year comparison, where the median sustainable fund lagged the index by roughly 10 basis points and conventional funds outperformed.

### Large-Blend Funds: Median Annualized Excess Return vs. the Morningstar US Market Index



Source: Morningstar Direct. Data as of Dec. 31, 2023. 1 Year sample includes 82 sustainable and 526 conventional funds. 3 Year sample includes 58 sustainable and 459 conventional funds. 5 Year sample includes 45 sustainable and 410 conventional funds. Does not include obsolete funds.

## Diversity-Focused Funds Were Among the Strongest and Weakest for Returns

The trend is fairly similar when it comes to risk-adjusted returns. On a risk-adjusted basis, sustainable funds lagged the Morningstar US Market Index in 2023, came up even over the trailing three-year period, and outperformed over the trailing five-year period.

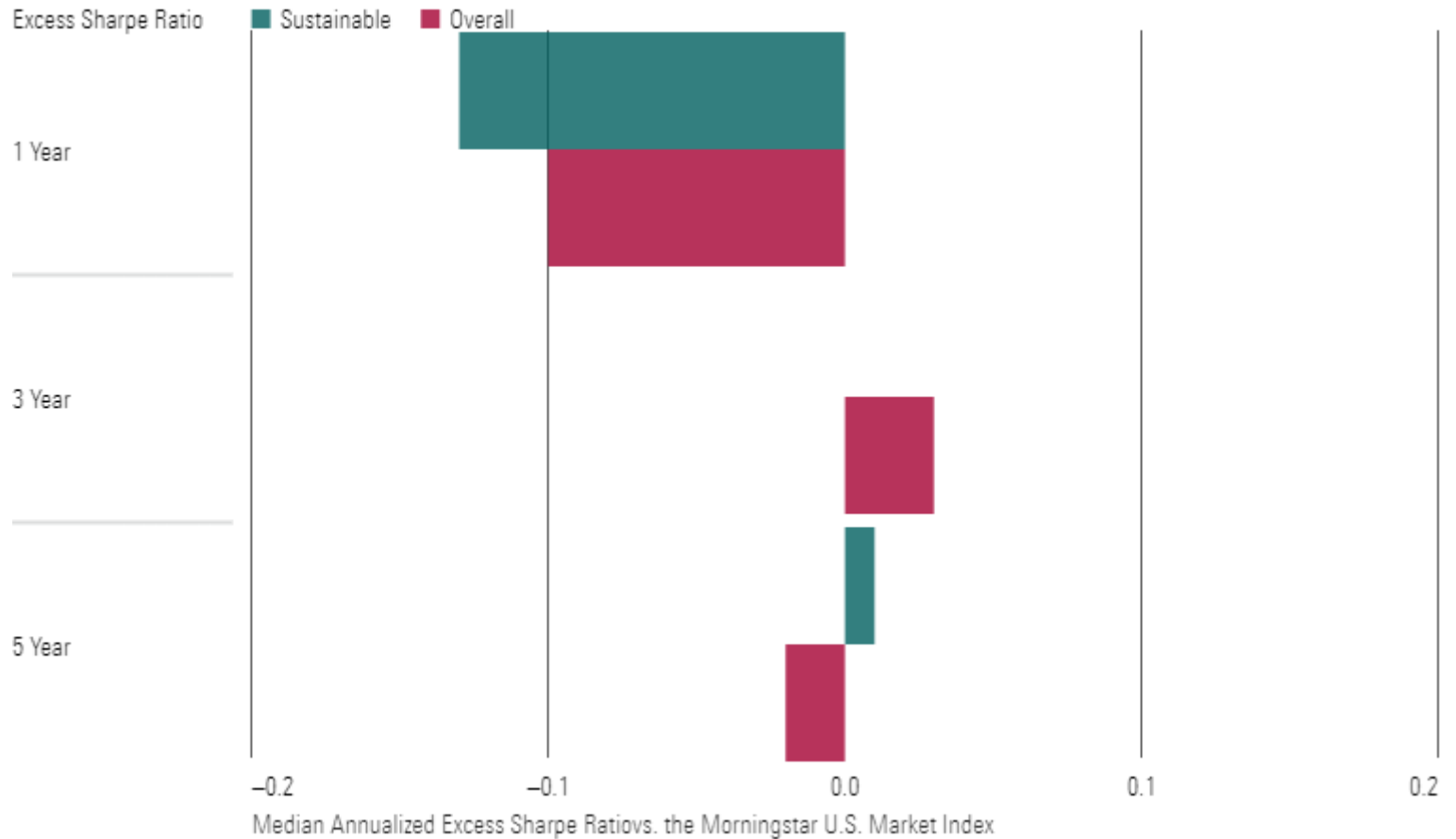
In 2023, IQ Candriam U.S. Large Cap Equity ETF led sustainable funds on a total- and risk-adjusted basis. The fund’s Sharpe ratio of 1.5 bested the benchmark by more than 20 basis points.

For the trailing three-year period, SPDR MSCI USA Gender Diversity ETF SHE brought up the rear with its modest 3.3-percentage-point gain and meager Sharpe ratio of 13 basis points.

Over the trailing five-year period, Impact Shares YWCA Women's Empowerment ETF WOMN achieved the second-highest returns among all large-blend equity funds.

➤ Furthermore, its Sharpe ratio of 91 basis points beat the benchmark handily.

**Large-Blend Funds: Median Annualized Excess Sharpe Ratio vs. the Morningstar US Market Index**



Source: Morningstar Direct. Data as of Dec. 31, 2023. 1 Year sample includes 82 sustainable and 526 conventional funds. 3 Year sample includes 58 sustainable and 459 conventional funds. 5 Year sample includes 45 sustainable and 410 conventional funds. Does not include obsolete funds.

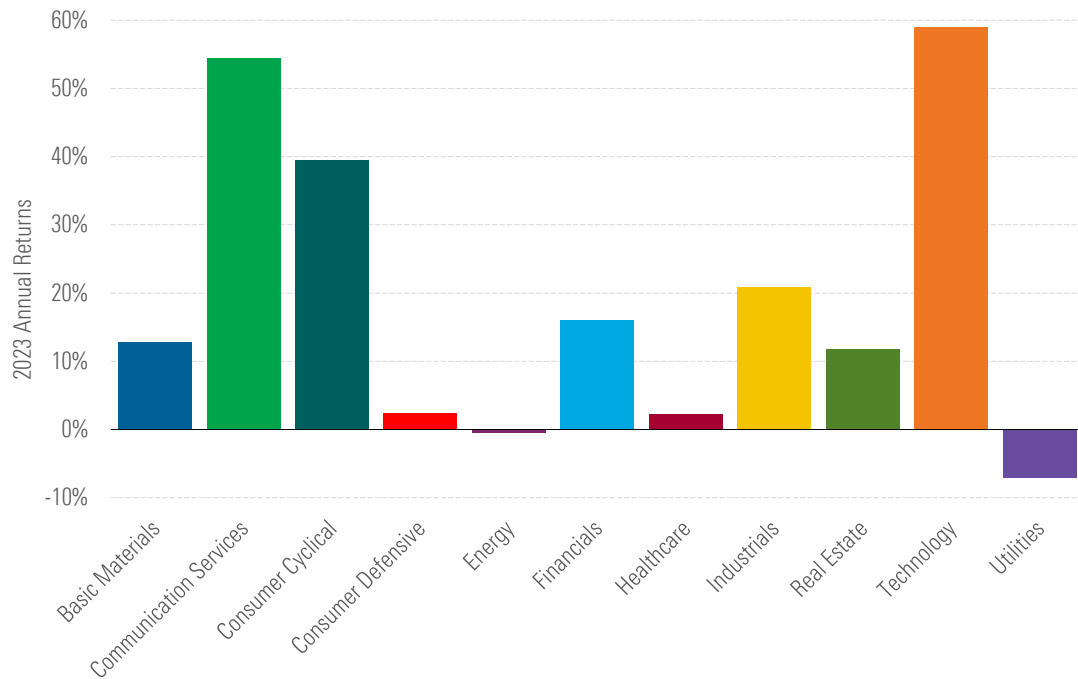
# U.S. Sustainable Funds: Investment Performance

Uncovering what worked and what didn't for sustainable funds.

## In 2023, Technology Overweightings Boosted; Utilities Exposure Hurt

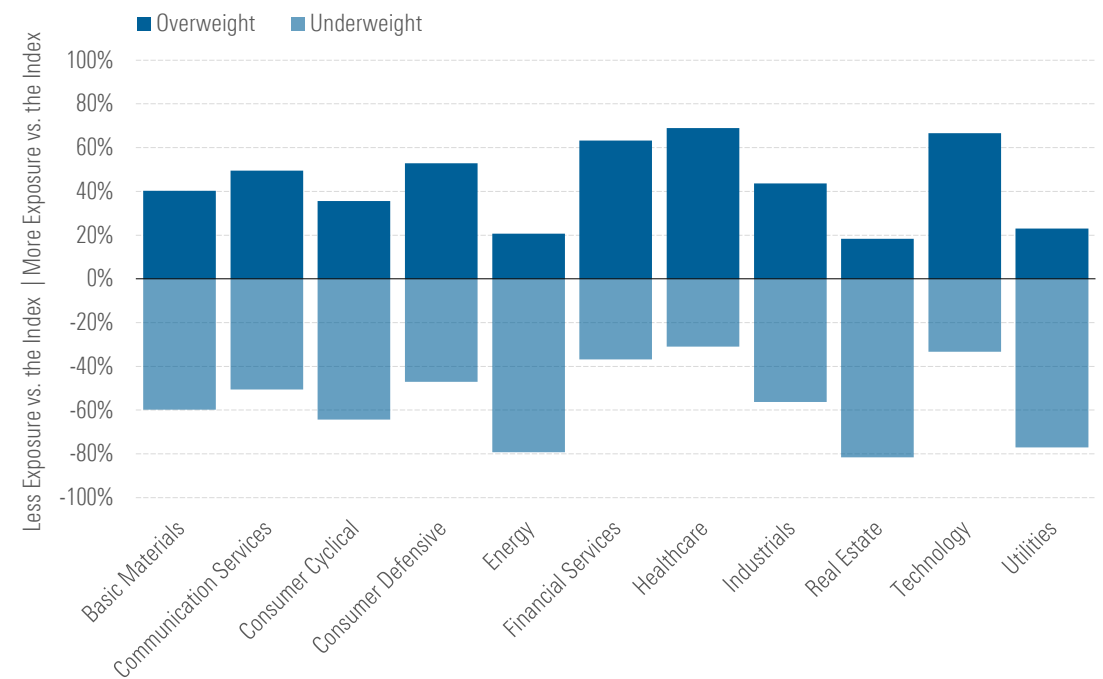
The median sustainable large-blend equity fund outperformed conventional peers but lagged the Morningstar US Market Index in 2023. To understand what drove these returns, we compared the sector profiles for nearly 90 sustainable large-blend equity funds with that of the Morningstar US Market Index (over- and underweightings are shown in the exhibit on the right). Entering into 2023, two thirds of the universe held relative overweightings to technology, which trounced all other sectors with its 59% gain. On the other hand, nearly one fourth of the group maintained an overweighting to utilities stocks compared with the market index. Since the sector lost 7% in 2023, funds with a relative overweighting were punished.

### Equity Sector Annual Returns in 2023



Source: Morningstar Direct. Data as of Dec. 31, 2023. Returns reflect Morningstar sector indexes, whose parent index is the Morningstar US Market Index.

### Sustainable Funds Sector Exposure vs. the Morningstar US Market Index Going Into 2023



Source: Morningstar Direct. Data as of Dec. 31, 2023. Sample includes 87 large-blend equity funds. Sector exposures reference portfolios from December 2022 (before the start of the 2023 annual return period).

## A Look Inside: Palo Alto and CrowdStrike Were Top Tech Picks in 2023

Eventide Large Cap Focus ETLAX maintained a 40% allocation to technology, nearly 26 percentage points higher than the Morningstar US Market Index. The sector bested all others in 2023, so this additional exposure helped the fund’s returns.

- Additionally, stock picks such as Palo Alto Networks PANW, CrowdStrike CRWD, Shopify SHOP, and Dlocal DLO contributed significantly to the fund's success. Each of these carry Low or Medium levels of ESG risk compared with peers.
- Because of the firm's values-based approach, Apple AAPL did not make the cut into the portfolio. In this case, the exemption of Apple helped, as the fund reallocated its capital to other higher-performing technology names.

Unlike many other sustainable funds, iShares ESG MSCI USA Min Vol Factor ETF ESMV entered 2023 with a roughly 5-percentage-point overweighting in utilities.

Because this sector was the worst performer in 2023, the additional exposure hurt the fund's performance relative to the benchmark.

- Stock picks within the utilities sector hurt, too. Compared with the benchmark, the fund held higher allocations to Eversource Energy ES and NextEra Energy NEE, each of which lost more than 20% during the year and ate on the fund’s returns.
- On the flip side, Constellation Energy CEG and Vistra VST gained 37% and 71%, respectively. Both companies court High levels of ESG risk and were excluded from the portfolio, so the fund missed out on their wins.

### Eventide Large Cap Focus: Top 5 Technology Bets Going Into 2023

Name	Ticker	Weighting in Portfolio (%)	Morningstar Rating Overall	2023 Return (%)	Selection Effect	ESG Risk Rating Assessment
Palo Alto Networks	PANW	5.4	★★	111.3	2.0	🌐🌐🌐🌐
CrowdStrike Holdings	CRWD	2.2	★★	142.5	1.7	🌐🌐🌐🌐
Shopify	SHOP	0.9	★★	124.4	1.1	🌐🌐🌐
Dlocal	DLO	1.2	★★★	13.6	1.7	🌐🌐🌐
Apple	AAPL	0.0	★★	49.0	1.0	🌐🌐🌐🌐

### iShares ESG MSCI USA Min Vol Factor ETF: Main Utilities Detractors Going Into 2023

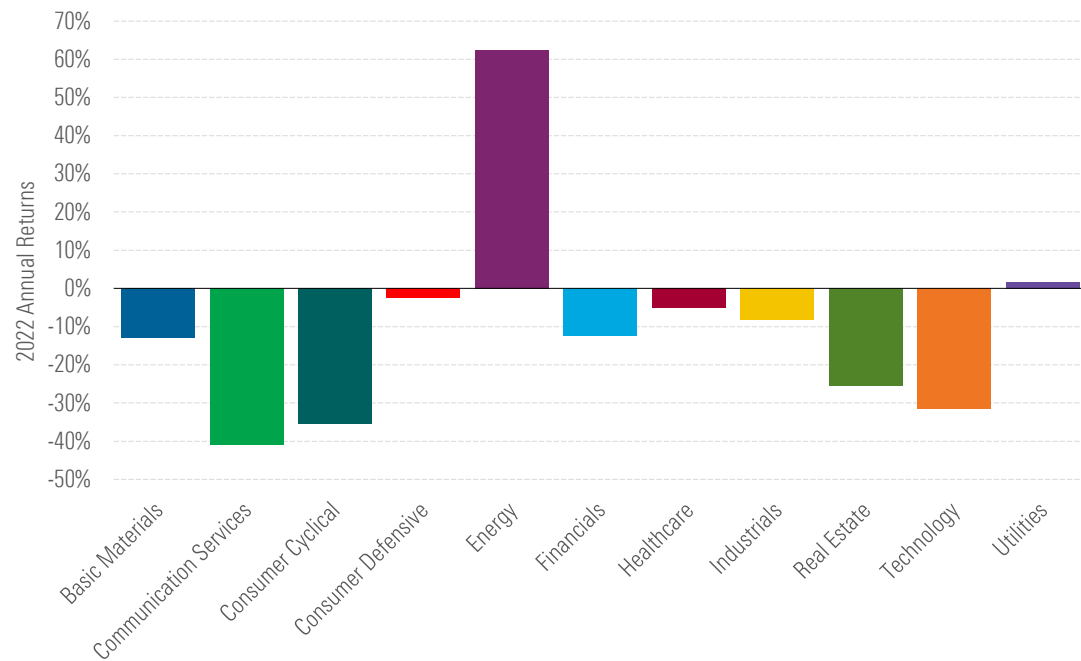
Name	Ticker	Weighting in Portfolio (%)	Morningstar Rating Overall	2023 Return (%)	Selection Effect	ESG Risk Rating Assessment
Eversource Energy	ES	1.3	★★★★★	-23.3	-0.3	🌐🌐🌐🌐
Constellation Energy	CEG	0.0	★★★	37.2	-0.1	🌐🌐
NextEra Energy	NEE	1.2	★★★★★	-25.3	-0.1	🌐🌐🌐
Vistra	VST	0.0	★★	70.7	-0.1	🌐🌐
Southern Co	SO	0.0	★★★	2.3	-0.1	🌐🌐🌐

Source: Morningstar Direct. Data as of Dec. 31, 2023, except for the Morningstar Rating, which is effective as of Jan. 29, 2024. Stocks shown are those with the most positive selection effect (top) or negative selection effect (bottom) relative to the Morningstar US Market Index in 2023. In the ESG Risk Rating Assessment, 5 globes are equivalent to Negligible ESG Risk, and 1 globe is equivalent to Severe ESG Risk.

## In 2022, Energy Stocks Led, and Sustainable Funds Lagged

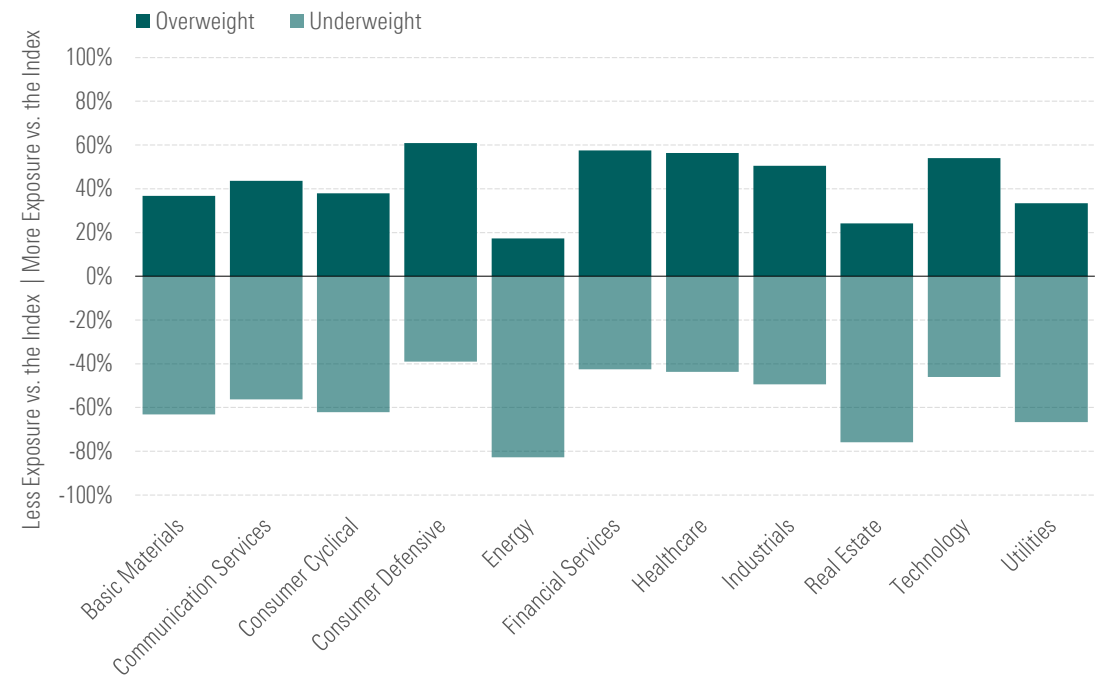
On the flip side, the median sustainable large-blend equity fund held up better than the Morningstar US Market Index in 2022 but lagged its conventional peer. In 2022, energy stocks took the lead with a 63% gain. One commonality among sustainable funds is a tendency to underweight the energy sector, and the 83% of funds with less exposure to energy stocks were left out of the sector’s rally. On the other hand, more than three fourths of the group maintained an underweighting to real estate, compared with the market index. Since the sector lost 26% in 2022, the relative underweighting muted these funds’ losses.

### Equity Sector Annual Returns in 2022



Source: Morningstar Direct. Data as of Dec. 31, 2023. Returns reflect Morningstar sector indexes, whose parent index is the Morningstar US Market Index.

### Sustainable Funds Sector Exposure vs. the Morningstar US Market Index Going Into 2022



Source: Morningstar Direct. Data as of Dec. 31, 2023. Sector exposures reference portfolios from December 2021 (before the start of the 2022 annual return period).

## A Look Inside: Ventas and Equity Lifestyle Were Top Real Estate Picks in 2022

Fidelity Women's Leadership ETF FWOMX maintained a slight underweighting to real estate, relative to the index, which saved the fund from some of the sector's losses.

- Picking the right names within real estate helped. The fund overweighted STORE Capital STOR and Equity Lifestyle Properties ELS, some of the best performers in an otherwise underperforming sector. Both companies carry Low levels of ESG risk.
- In addition to overweighting the best performers, avoiding the worst performers also mitigated the fund's losses. For example, Opendoor Technologies OPEN lost 92%, which dragged on the benchmark's performance. Since the fund did not own Opendoor Technologies, it dodged some significant losses.

Like many sustainable funds, Nuveen ESG Large-Cap ETF NULC entered 2022 with relatively low exposure to energy. Because of this, the fund didn't participate in the sector's eye-popping returns.

- Because of the fund's ESG mandate, it omitted Exxon Mobil XOM and Occidental Petroleum OXY, both of which carry Severe levels of ESG risk. Excluding these names means the fund missed out on their respective gains of 87% and 119%.
- The energy companies the fund held didn't perform nearly as well. The fund held overweightings in Medium-ESG-risk names ONEOK OKE, Baker Hughes BKR, and Cheniere Energy LNG. Although these stocks posted gains, they trailed Occidental's surge by up to 100 percentage-points.

### Fidelity Women's Leadership ETF: Top Real Estate Picks Going Into 2022

Name	Ticker	Weighting in Portfolio (%)	Morningstar Rating Overall	2022 Return (%)	Selection Effect	ESG Risk Rating Assessment
STORE Capital		0.8			0.3	🌐🌐🌐🌐
Ventas	VTR	0.7	★★★★★	-8.6	0.1	🌐🌐🌐🌐
Equity Lifestyle Properties	ELS	1.1	★★★★	-24.5	0.0	🌐🌐🌐🌐
Prologis	PLD	0.0	★★★	-31.3	0.0	🌐🌐🌐🌐
Opendoor Tech	OPEN	0.0	★★★	-92.1	0.0	🌐🌐🌐🌐

### Nuveen ESG Large-Cap ETF: Main Energy Detractors Going Into 2022

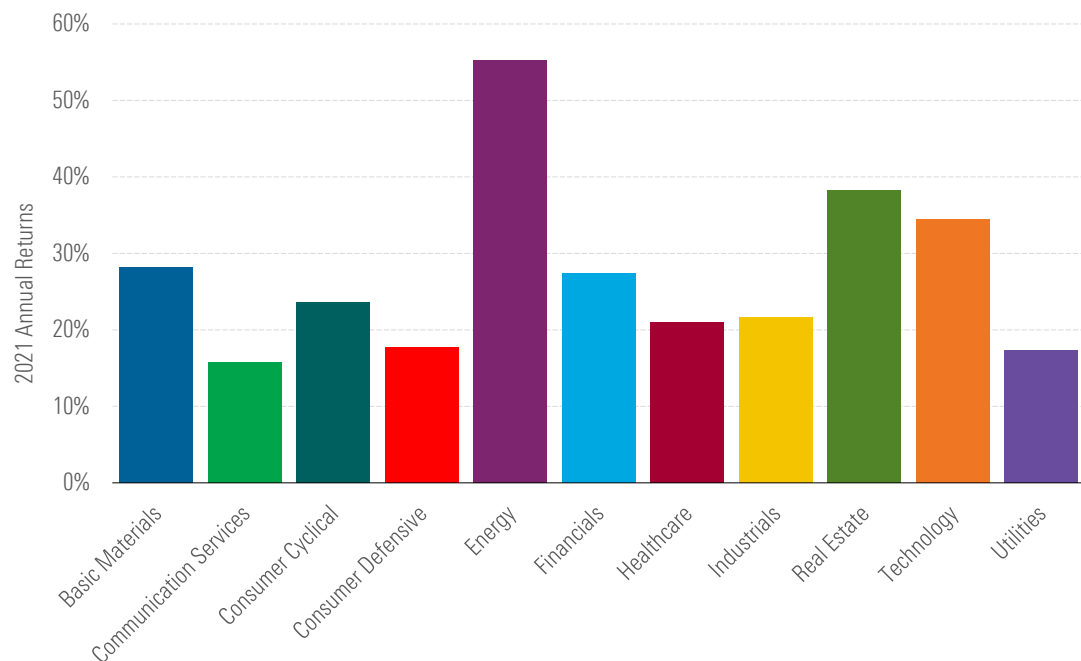
Name	Ticker	Weighting in Portfolio (%)	Morningstar Rating Overall	2022 Return (%)	Selection Effect	ESG Risk Rating Assessment
ONEOK	OKE	0.8	★★	18.9	-0.2	🌐🌐🌐
Baker Hughes Co	BKR	0.7	★★★	25.8	-0.1	🌐🌐🌐
Cheniere Energy	LNG	0.9	★★★	49.2	-0.1	🌐🌐🌐
Exxon Mobil	XOM	0.0	★★★★★	87.2	-0.1	🌐
Occidental Petroleum	OXY	0.0	★★★	119.2	0.0	🌐

Source: Morningstar Direct. Data as of Dec. 31, 2023, except for the Morningstar Rating, which is effective as of Jan. 29, 2024. Stocks shown are those with the most positive selection effect (top) or negative selection effect (bottom) relative to the Morningstar US Market Index in 2023. In the ESG Risk Rating Assessment, 5 globes are equivalent to Negligible ESG Risk, and 1 globe is equivalent to Severe ESG Risk.

## In 2021, Financial-Services Overweightings Lifted Returns; Energy Exclusions Dragged

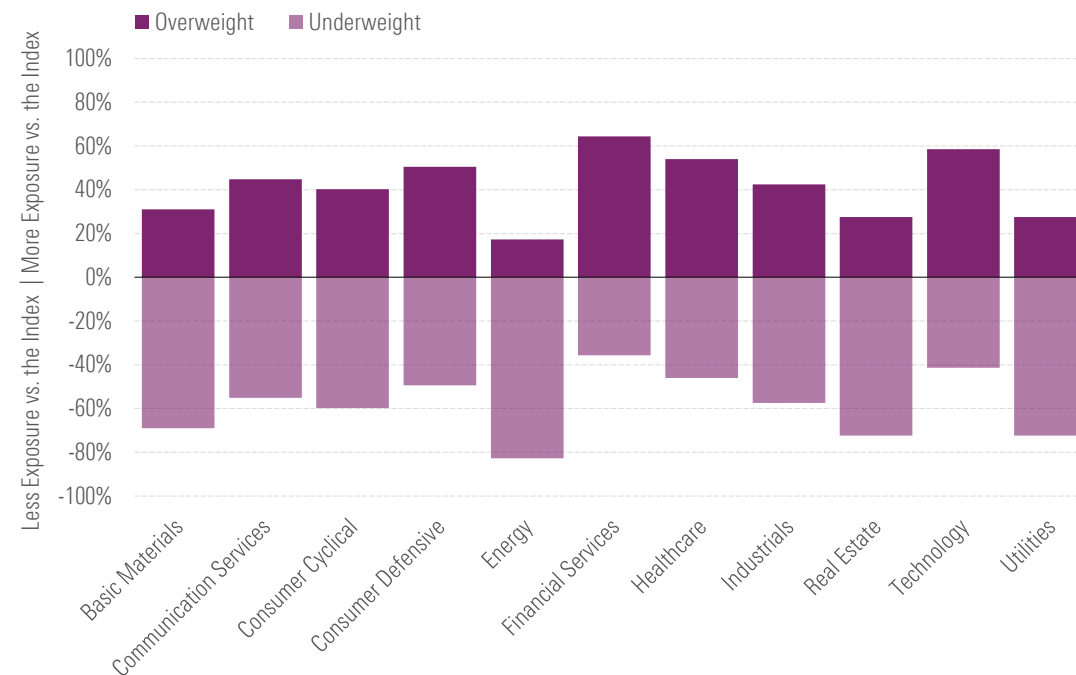
The median sustainable large-blend equity fund outperformed both the Morningstar US Market Index and median conventional peer in 2021. One of the most common sector tilts in sustainable funds is an overweighting to financial services; entering 2021, 62% of funds had greater exposure than the index. Although financial-services stocks didn't perform as well as energy, the sector posted a decent 27% gain and boosted these funds' returns. On the other hand, nearly half of sustainable funds held an overweighting to communication services, and this sector's 16% gain was the worst of the bunch. Relative to the broad market index, these overweightings dragged on returns.

### Equity Sector Annual Returns in 2021



Source: Morningstar Direct. Data as of Dec. 31, 2023. Returns reflect Morningstar sector indexes, whose parent index is the Morningstar US Market Index.

### Sustainable Funds Sector Exposure vs. the Morningstar US Market Index Going Into 2021



Source: Morningstar Direct. Data as of Dec. 31, 2023. Sector exposures reference portfolios from December 2020 (before the start of the 2021 annual return period).



## A Look Inside: Ameriprise and Fidelity Were Top Financial-Services Picks in 2021

Entering 2021, CCM Core Impact Equity Fund QUAGX maintained a 21% allocation to financial services, more than 7 percentage points higher than the benchmark. The financial-services sector returned 27% in 2021, so the fund’s overweighting boosted its performance relative to the benchmark.

- Additionally, stock picks such as Ameriprise AMP, Fidelity National Financial FNF, BlackRock BLK, and Discover DFS contributed to the fund's success. These names, each of which carries Low or Medium levels of ESG risk, were among the strongest performers in the sector, and the fund benefited as a result.

Nearly half of sustainable funds held overweightings in communication services at the end of 2020, iShares Climate Conscious & Transition MSCI USA ETF USCL being one of them. Because this sector was one of the worst performers in 2021, the fund’s additional exposure weighed on the fund’s returns relative to the benchmark.

- Stock picks within the communications services sector hurt, too. Compared with the benchmark, the fund held higher allocations to Disney DIS, Verizon VZ, T-Mobile TMUS, Activision Blizzard AIY, and Comcast CMCSA. All equities ended the year in the red, thus hurting the fund's returns.

### CCM Core Impact Equity Fund: Top 5 Financial-Services Bets Going Into 2021

Name	Ticker	Weighting in Portfolio (%)	Morningstar Rating Overall	2021 Return (%)	Selection Effect	ESG Risk Rating Assessment
Ameriprise Financial	AMP	1.4	★★★	57.9	0.4	🌐🌐🌐
Fidelity National Financial	FNF	1.6	★★★	33.4	0.2	🌐🌐🌐
Discover Financial Services	DFS	2.9	★★★★	29.8	0.2	🌐🌐🌐
BlackRock	BLK	3.0	★★★	29.4	0.1	🌐🌐🌐🌐
JPMorgan Chase & Co	JPM	1.8	★★★	27.7	0.0	🌐🌐

### iShares Climate Conscious & Transition MSCI USA ETF: Main Comm. Services Detractors Going Into 2021

Name	Ticker	Weighting in Portfolio (%)	Morningstar Rating Overall	2021 Return (%)	Selection Effect	ESG Risk Rating Assessment
The Walt Disney Co	DIS	1.4	★★★★	-14.5	-0.2	🌐🌐🌐🌐
Verizon Communications	VZ	0.9	★★★★	-7.5	-0.1	🌐🌐🌐🌐
T-Mobile US	TMUS	0.4	★★★	-14.0	0.0	🌐🌐🌐
Activision Blizzard	AIY	0.3		-25.3	0.0	🌐🌐🌐🌐
Comcast	CMCSA	1.0	★★★★	-2.2	0.0	🌐🌐🌐

Source: Morningstar Direct. Data as of Dec. 31, 2023, except for the Morningstar Rating, which is effective as of Jan. 29, 2024. Stocks shown are those with the most positive selection effect (top) or negative selection effect (bottom) relative to the Morningstar US Market Index in 2023. In the ESG Risk Rating Assessment, 5 globes are equivalent to Negligible ESG Risk, and 1 globe is equivalent to Severe ESG Risk.

# U.S. Sustainable Funds: Sustainability Performance

Sustainable funds delivered on multiple sustainability characteristics.

## Sustainable Funds Delivered Lower Exposure to ESG Risk

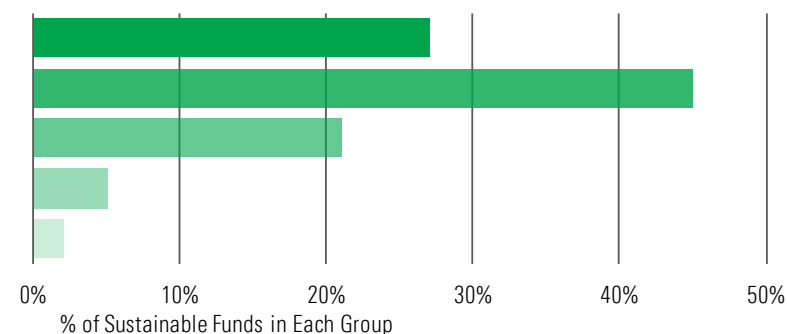
How well do sustainable funds limit exposure to ESG risk, compared with peers? The Morningstar Sustainability Rating can help answer this question.

The Morningstar Sustainability Rating is an asset-weighted roll-up of Sustainalytics' company and sovereign ESG Risk Ratings based on the trailing 12 months of a fund's portfolios. Each sleeve (corporate or sovereign) of the fund's portfolio is ranked within the global peer category group, and 1 to 5 globes are assigned. Each sleeve's rating is multiplied by its respective globe rating to arrive at the fund's overall globe rating.

Although the consideration of material ESG risks is becoming more common in traditional investment management, sustainable funds continue to deliver lower levels of ESG risk, compared with peers. Nearly three fourths of sustainable funds receive the highest ratings, 4 or 5 globes, compared with 28% of funds overall. At the other end of the scale, less than one tenth of sustainable funds receive the lowest ratings, 1 or 2 globes, compared with close to one third of funds overall.

### ESG Risk in Sustainable Funds

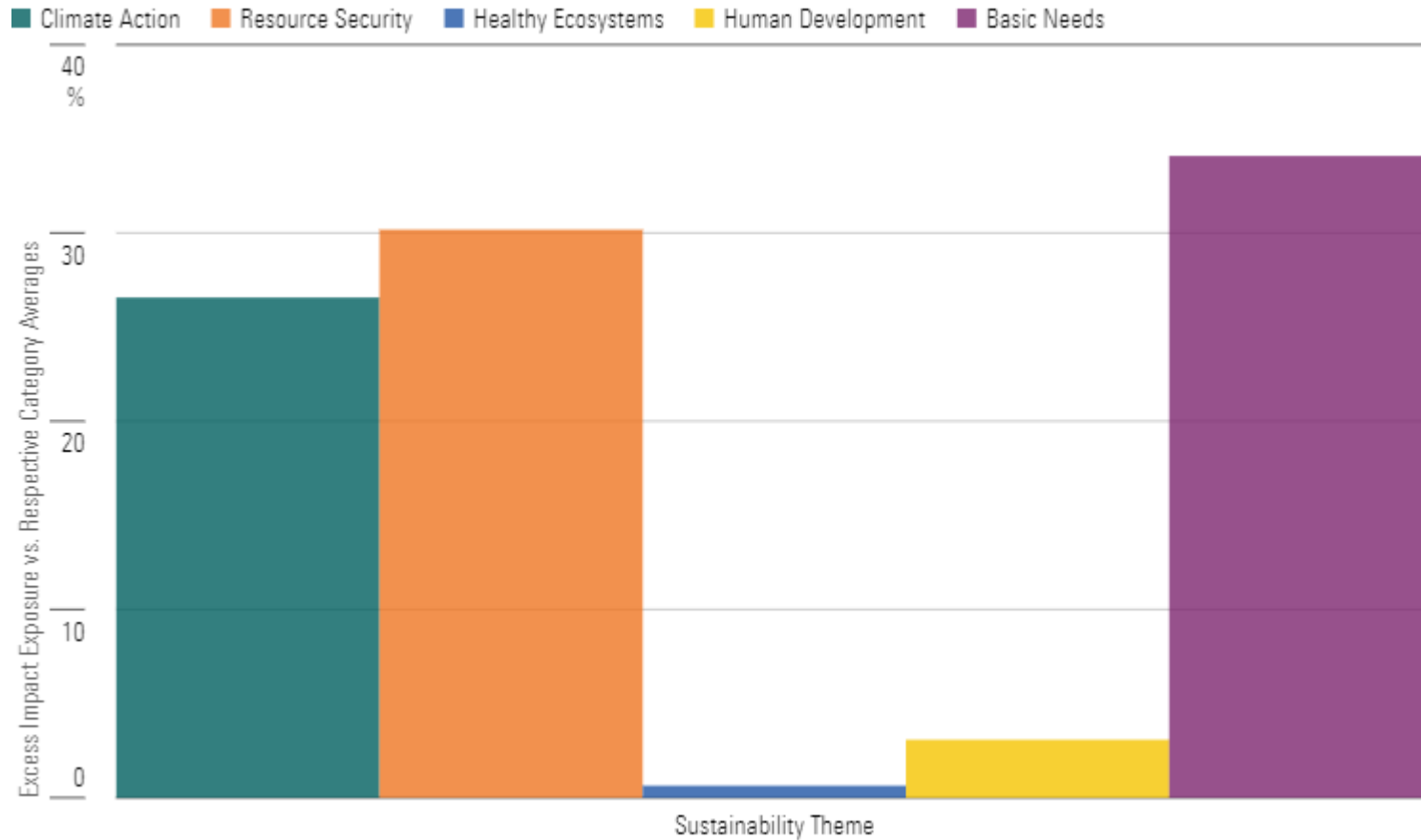
Sustainability Rating	Overall Universe %	Sustainable Funds	
		#	%
🌐🌐🌐🌐🌐	7%	161	27%
🌐🌐🌐🌐	21%	272	45%
🌐🌐🌐	43%	127	21%
🌐🌐	22%	132	5%
🌐	8%	15	2%



Source: Morningstar Direct. Data as of Dec. 31, 2023. Does not include obsolete funds. Overall universe includes the oldest share class of all U.S.-domiciled funds. In the Morningstar Sustainability Rating, 5 globes are equivalent to a High Sustainability Rating, and 1 globe is equivalent to a Low Sustainability Rating.

# Sustainable Funds Delivered Greater Exposure to Environmental and Social Impact

## Sustainability Themed Funds' Average Excess Exposure to Impact, Compared With Category Peers



How well do sustainability-themed funds deliver exposure to positive impact, compared with peers? Morningstar's Sustainable Attributes and Portfolio Impact Metrics can help answer this question.

The Sustainable Attributes include subcategories that highlight funds focused on five environmental and social themes: Climate Action, Resource Security, Healthy Ecosystems, Human Development, and Basic Needs. These classifications are not mutually exclusive—for example, funds included under Climate Action may also be included under Healthy Ecosystems. Morningstar also rolls up Sustainalytics' company-level impact exposures to the portfolio level. In the exhibit to the left, we compared the average sustainability-themed portfolio's impact exposure with that of its category peers.

In all five categories, sustainability-themed funds delivered greater exposure to environmental and social impact, compared with peers. The excess was greatest among Basic Needs funds, but the sample size was small. Climate Action funds delivered, on average and compared with peers, 27 percentage points more exposure to impact.

Source: Morningstar Direct. Data as of Dec. 31, 2023. Does not include obsolete funds. Sample includes 94 Climate Action, 21 Resource Security, 26 Healthy Ecosystems, 26 Human Development, and 13 Basic Needs funds.

## Thematic Offerings From Impact Shares, RBC, and Fidelity Delivered Above-Average Exposure to Impact

### Human Development Funds With High Exposure to Impact

Name	Ticker	Inception Date	Morningstar Category	Total Assets (\$ Mil)	Human Development	
					% of Covered Portfolio Involved	% Involved Category Average
CCM Affordable Housing MBS ETF	OWNS	7/27/2021	Intermediate Government	120	100.0	88.2
The Community Development Fund	CDCDX	4/29/2016	Intermediate Government	134	100.0	88.2
RBC BlueBay Access Capital Community Investment	ACCSX	6/23/1998	Intermediate Government	660	100.0	88.2
CCM Community Impact Bond	CRAIX	8/30/1999	Intermediate Core Bond	3,353	82.7	45.4
RBC BlueBay Impact Bond	RIBRX	12/18/2017	Intermediate Core Bond	246	63.2	45.4

Source: Morningstar Direct. Data as of Dec. 31, 2023.

### Resource Security Funds With High Exposure to Impact

Name	Ticker	Inception Date	Morningstar Category	Total Assets (\$ Mil)	Resource Security	
					% of Covered Portfolio Involved	% Involved Category Average
Fidelity Water Sustainability	FLOWX	4/16/2020	Natural Resources	92	98.6	37.0
Global X Clean Water ETF	AQWA	4/8/2021	Natural Resources	10	97.6	37.0
Ecofin Global Water ESG	EBLU	2/14/2017	Natural Resources	50	97.1	37.0
Invesco Global Water ETF	PIO	6/13/2007	Natural Resources	282	95.4	37.0
iShares Environmental Infrastructure and Industrials ETF	EFRA	11/1/2022	Infrastructure	5	92.4	27.6

Source: Morningstar Direct. Data as of Dec. 31, 2023.

On average, the 26 sustainable offerings [classified as Human Development funds](#) delivered greater exposure to Human Development impact than their respective category peers. Human Development includes measures that support education, equality, and employment opportunities.

- In the case of four sustainable funds, 100% of their covered portfolio holdings can be connected to Human Development impact.
- For example, RBC BlueBay Impact Bond RIBRX invests in the Reinvestment Fund, a Philadelphia-based nonprofit that supports efforts related to affordable housing, access to nutritious food and healthcare, and local businesses supporting job growth.

Out of more than 20 Resource Security funds, Fidelity Water Sustainability FLOWX stands out. Nearly 99% of its covered portfolio holdings can be connected to Resource Security impact. Resource Security comprises water and wastewater management, eco-efficient product innovation, forest conservation, and recycling.

- One of Fidelity Water Sustainability's top holdings is Energy Recovery ERll, which develops technology for activities such as seawater desalination and industrial wastewater management.
- Pennon Group PNN, another of Fidelity Water Sustainability's top holdings, is a U.K.-based environmental utility company that provides clean water and wastewater management to more than 3 million residents.

## Support for Environmental and Social Shareholder Proposals Fell Dramatically in 2023

An increasingly important dimension of sustainable investing is stewardship: how a fund engages with the companies it owns, votes proxies, and seeks to drive measurable positive change beyond financial return.

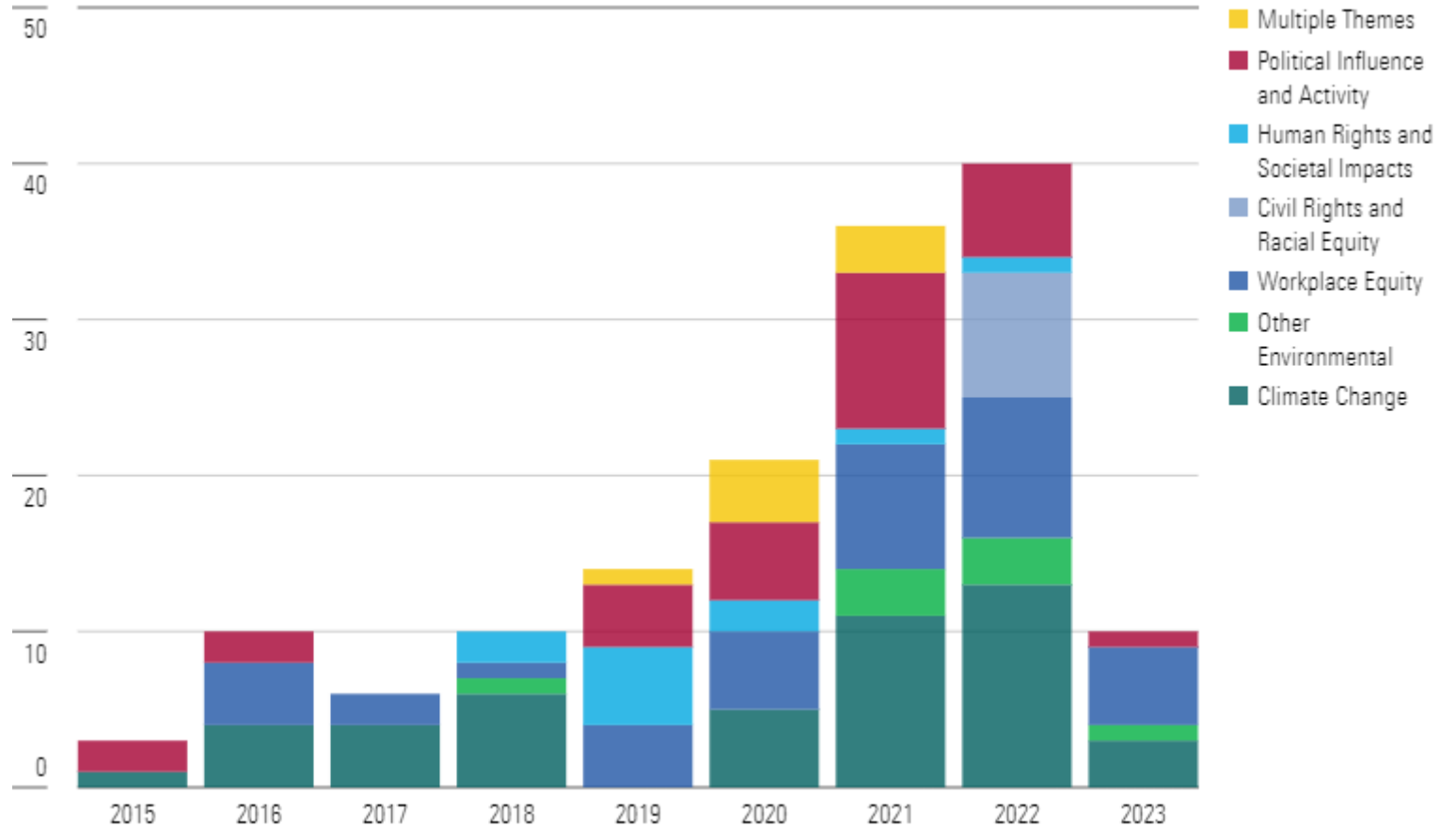
- Often called *active ownership*, this activity is not easy to evaluate overall, in part because many company engagements take place behind closed doors. However, we can assess the extent to which sustainable equity funds use their proxy votes to support progress on key sustainability initiatives.

The number of resolutions focused on environmental and social topics increased in 2023, but [support for these resolutions fell sharply](#).

- In 2023, Morningstar identified 337 such resolutions, up 23% from the 273 seen in 2022.
- On average, these resolutions gained support from 20% of shareholders, down significantly from the 30% average support seen in 2022.

In 2023, just 10 resolutions gained majority support, down from 40 in 2022. Half of the well-supported resolutions focused on workplace equity.

### Majority-Supported Environmental and Social Shareholder Resolutions



Source: Morningstar Proxy-Voting Database. Data as of Jan. 16, 2024. Years represent proxy-voting years ended June 30.

## Well-Supported Shareholder Resolutions Focused on Social Topics

In line with overall lower levels of support for environmental and social shareholder resolutions, the number of key ESG resolutions practically halved to 53 in 2023 from 102 in 2022.

- Morningstar defines key resolutions as those that address environmental and social topics and gain more than 40% adjusted support—that is, support from shareholders who are independent of the company and its management.

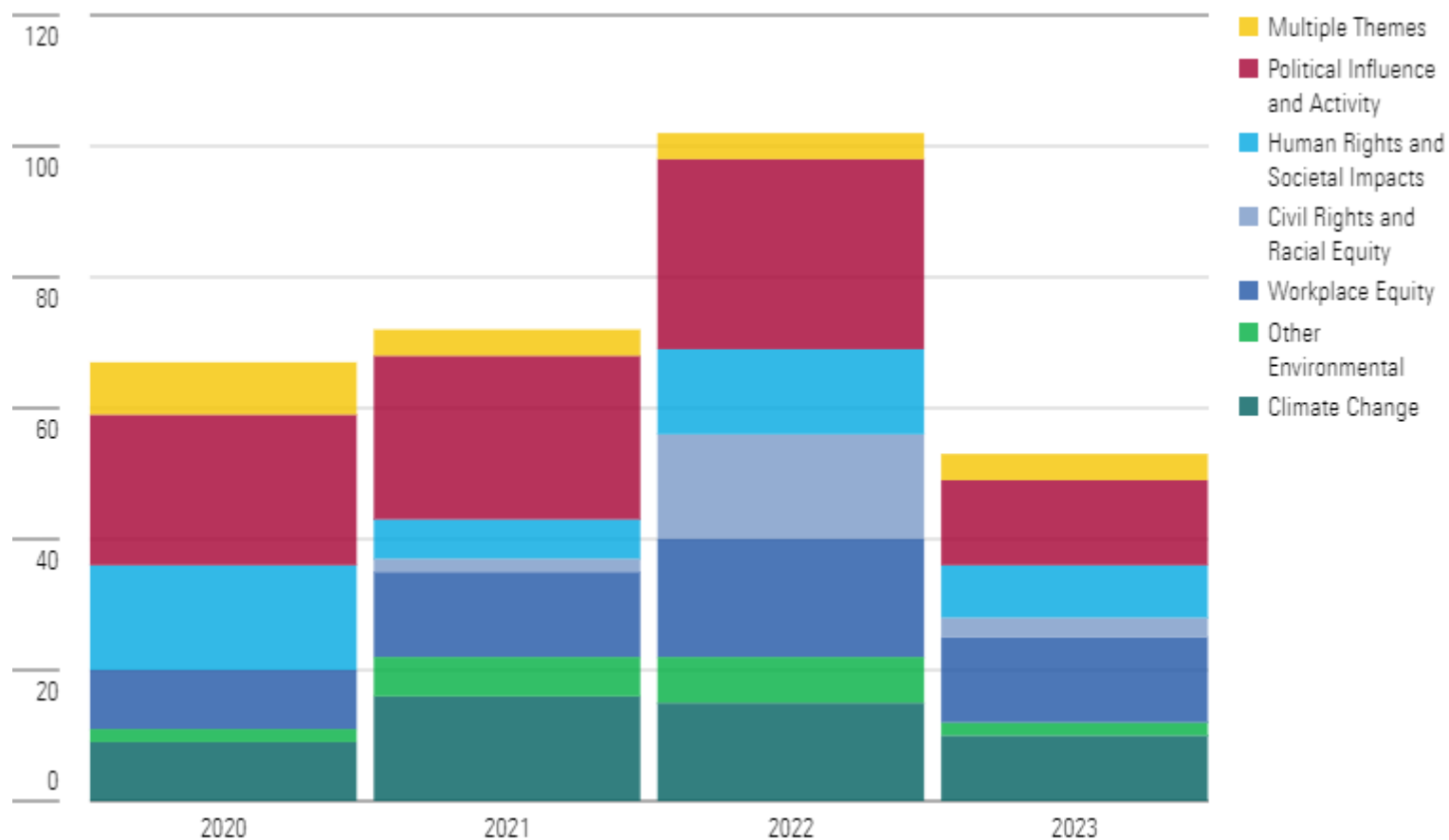
Average adjusted support for key environmental and social resolutions fell below 50% in 2023 amid fund manager concerns that resolutions were unduly prescriptive.

- In 2021, adjusted support for these resolutions was 63%, falling to 56% in 2022 and 48% in 2023.

Just two resolutions achieved more than 70% adjusted support in 2023.

- One was a proposal concerning Board Diversity and EEO-1 Reporting at Red Rock Resorts RRR.
- The other related to the Reliability of Methane Emission Disclosures at Coterra Energy CTRA.

### Key Environmental and Social Shareholder Resolutions



Source: Morningstar Proxy-Voting Database. Data as of Jan. 16, 2024. Years represent proxy-voting years ended June 30.

## Most Sustainable Funds Supported 2023’s Key ESG Resolutions, but the Largest Voted Against

As expected, sustainable funds showed a higher rate of support for key environmental and social shareholder resolutions, compared with peers.

- Out of 153 sustainable funds with sufficient proxy-voting data, the average level of support was more than 70%.

Most funds exhibited strong support, but support ranged from 100% all the way down to zero.

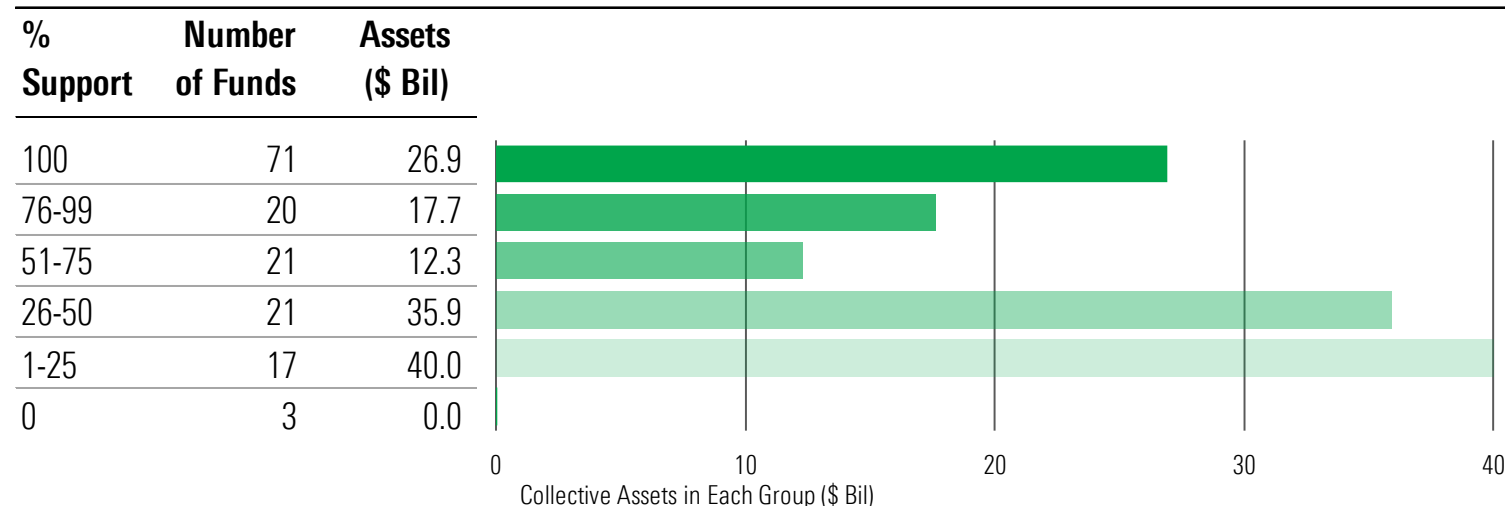
- The largest group—71 funds—supported 100% of the key ESG resolutions they voted in 2023.

Still, size matters. Fund votes are cast in proportion to the value of their shares, meaning that a fund's size is a key factor in determining the impact of its voting stance.

- In terms of collective assets, the largest group—representing \$40 billion in assets—supported less than one fourth of 2023’s key ESG resolutions.

The two largest passive sustainable funds—Vanguard FTSE Social Index and iShares ESG Aware MSCI USA ETF—supported just 3% and 34% of 2023’s key ESG resolutions, respectively.

### Sustainable Fund Support for Key ESG Resolutions in 2023



Source: Morningstar Proxy-Voting Database. Data as of Jan. 16, 2024. Includes funds voting on at least 10 key ESG resolutions.



## The Largest Fund Shops Often Voted Against Key Environmental and Social Proposals

Because of their size, [the largest asset managers wield significant power](#).

- The exhibit on the right shows how the 10 largest shops by sustainable fund assets voted on 2023’s key ESG resolutions (including sustainable and conventional offerings).

Parnassus and Impax are both fully dedicated to sustainable investing and have supported 100% of key ESG resolutions in each of the past three years.

Some of the largest asset managers are among the least supportive of key ESG resolutions.

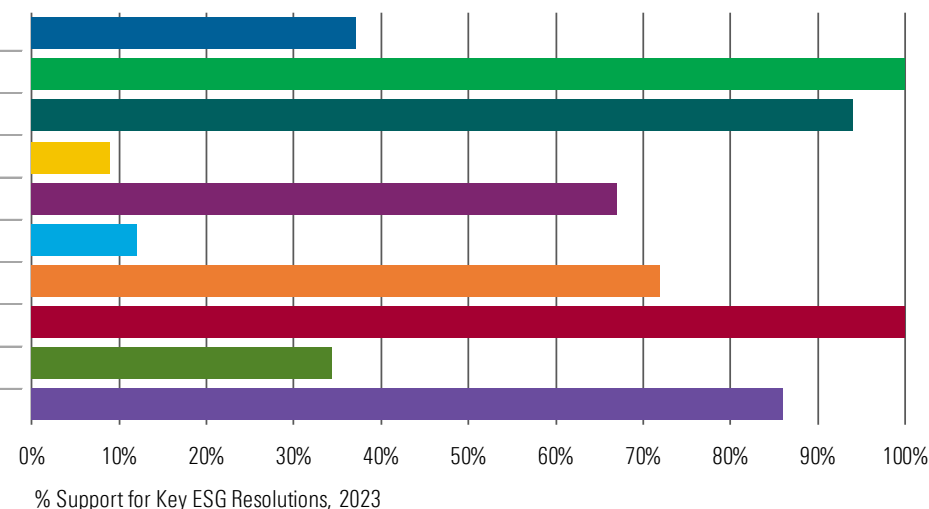
- BlackRock increased its support for key environmental resolutions in 2023, compared with 2022, but its support for social proposals dropped significantly.
- Vanguard’s support declined across all categories.

Dimensional has shown consistently low levels of support for key ESG resolutions, voting for less than 20% of such proposals in each of the past three years.

- Still, its sustainable funds follow a separate process and exhibit much higher support—55% in 2023.

### How the Largest Fund Shops in Terms of Sustainable Assets Voted on 2023’s Key ESG Resolutions

Asset Manager	2023 Total Assets (\$ Bil)	Support for Key ESG Resolutions
BlackRock/iShares	59.2	37%
Parnassus	39.3	100%
MSIM/Calvert	34.9	94%
Vanguard	30.5	9%
Nuveen/TIAA	21.7	67%
Dimensional	13.1	12%
Brown Advisory	9.8	72%
Impax	8.5	100%
Amundi*	8.5	34%
Invesco	7.8	86%



Source: Morningstar Proxy-Voting Database. Data as of Jan. 16, 2024. Includes funds voting on at least 10 key ESG resolutions. \*Amundi’s U.S. sustainable funds have separate governance that makes voting decisions independently of the firm’s central team.

# U.S. Sustainable Funds: Regulatory Developments

Key guidance still to come.

## Slowly but Steadily, Regulation Is Emerging

### Updates

#### Funds Should Do What Their Names Imply

- In September 2023, the U.S. Securities and Exchange Commission **finalized one guardrail for funds with ESG key-terms in their names.**
- The commission [adopted an amendment](#) to the Investment Company Act's Names Rule, which requires a fund with a name suggesting a focus on a particular type of investment to invest at least 80% of its assets in that style. The amendment broadened the scope of the rule to include "ESG" and "sustainable" funds, compared with the previous focus on terms like "stock" and "bond."
- Depending on firm assets, fund shops have between two and two-and-a-half years to come into compliance with the updates, following the effective date.

#### ESG Options for Retirement Savers

- The Department of Labor [finalized a rule](#) titled "Prudence and Loyalty in Selecting Plan Investments and Exercising Shareholder Rights" in November 2022.
- The rule states that **the duty of prudence\* could include the consideration of climate change and other ESG issues**, and it allows for collateral benefits (such as positive impact on people and planet) to act as tiebreakers in plan selection. The rule also lifted prior guidance that made it difficult and risky for employers that wanted to use ESG-focused investment options as default investments for workers automatically enrolling in a qualified 401(k) plan.
- In September 2023, a **federal judge sided with the DOL** in a lawsuit concerning this rule, an extra layer of assurance that the rule is legitimate.

\* The duty of prudence is a retirement plan fiduciary's responsibility to make investment decisions based on financially material factors.

### Still in the Works

#### Climate Disclosures Should Be Comprehensive, Consistent, and Comparable

- SEC Chair Gary Gensler [testified](#) before the House Financial Services Committee in September 2023, casting doubt over the timeline of the upcoming Climate-Related Disclosures rulemaking and potential inclusion of scope 3 emissions.
- Proposed in March 2022, the rule would require **public companies to enhance and standardize the disclosure of climate-related risks and opportunities.**
- While federal guidance remains in limbo, **California is forging ahead.** In October 2023, California [signed into law](#) a bill requiring large businesses to disclose their scope 1, 2, and 3 greenhouse gas emissions. This bill is largely viewed as a test case for the SEC, as market reactions will highlight parts of the SEC's proposal that may be disputed.

#### Standardizing ESG Fund Disclosures

- In March 2022, the SEC [announced a proposal](#) to standardize disclosures concerning funds' incorporation of ESG factors. The proposed rule would **require funds that use ESG criteria in their investment process to disclose more about how they do so** in their prospectuses and annual reports.
- The proposal identifies and defines three broad types of ESG funds: ESG integration, ESG focused, and impact. The three categories would have different levels of required disclosure.

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