Global Sustainable Fund Flows: Q1 2023 in Review

A slow start to the year, with lower inflows and product development, but assets climb to USD 2.7 trillion.

Morningstar Manager Research
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Contents

Key Takeaways

- Global sustainable funds attracted USD 29 billion of net new money in the first quarter of 2023, down from nearly USD 38 billion in the previous quarter.
- Inflows were lower in most regions as macroeconomic pressures, including rising interest rates, inflation, and a looming recession, continued to weigh on investor sentiment. Sustainable funds in the United States experienced their third quarter of outflows in a year.
- Despite lower inflows but helped by higher valuations, global sustainable fund assets continued their recovery to hit USD 2.74 trillion at the end of March.
- Product development cooled down. Europe saw a significant reduction of new sustainable fund launches, amid regulatory uncertainty and fears of greenwashing accusations, while the rest of the world kept their momentum.

The Global Sustainable Fund Universe

The global sustainable fund universe encompasses open-end funds and exchange-traded funds that, by prospectus or other regulatory filings, claim to focus on sustainability; impact; or environmental, social, and governance factors[1]. (See the Appendix for more details on how we define the global sustainable fund universe.)

The global universe is divided here into three segments by domicile: Europe, United States, and rest of world. There is more-granular data available in this report for Canada, Australia and New Zealand, and Japan. China, Hong Kong, India, Indonesia, Malaysia, Singapore, Taiwan, Thailand, and South Korea are grouped under the Asia ex-Japan label because of their relatively low assets.

This report examines recent activity in the global sustainable fund universe and details regional flows, assets, and launches for the first quarter of 2023. A summary is provided in Exhibit 1.

1 Note: This is not the same as the definition under the European Union's Sustainable Finance Disclosure Regulation, which defines “sustainable investments” at a holding level.

Exhibit 1 Global Sustainable Fund Statistics

Q1 2023	Flows	Assets		Funds	
Region	USD Billion	Billion	% Total	#	% Total
Europe	32.3	2,296	84	5,410	77
United States	-5.2	299	11	638	9
Asia ex-Japan	1.7	63	2	515	7
Australia/New Zealand	0.1	31	1	201	3
Japan	-1.0	26	1	60	1
Canada	1.0	30	1	206	3
Total	**29.0**	**2,745**		**7,030**	

Source: Morningstar Direct, Manager Research. Data as of March 2023.

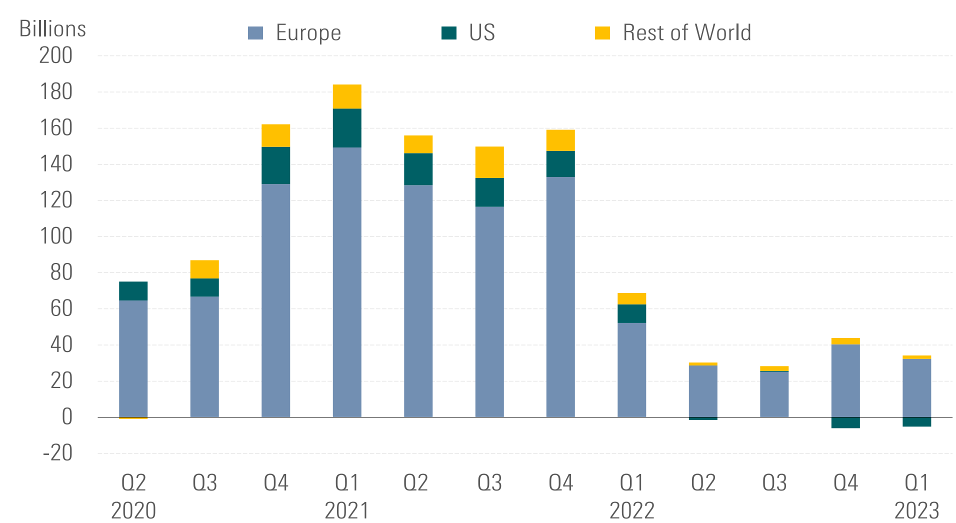
Sustainable Fund Inflows Slow

The global universe of sustainable funds attracted almost USD 29 billion of net new money in the first quarter of 2023. This inflow was lower than the revised USD 37.7 billion of the last quarter of 2022, amid continued macroeconomic pressures, including rising interest rates, inflation, and a looming recession.

The decrease was mirrored by a lower quarterly organic growth rate. Calculated as net flows relative to total assets at the start of a period, global sustainable funds saw their organic growth rate, or OGR, decline to 1.4%, from over 2% in the previous quarter.

The OGR for sustainable funds remained higher than the 0.2% OGR for the overall global fund universe from January to March. The overall global fund universe set off with an uptick in fund flows of USD 77 billion in the first quarter, putting a halt to the outflow trend of 2022.

Exhibit 2 Quarterly Global Sustainable Fund Flows (USD Billion)



Source: Morningstar Direct, Manager Research. Data as of March 2023.

Nevertheless, the decelerated growth in sustainable funds was felt across all regions apart from Canada. Europe, the biggest market for sustainable funds, attracted USD 32.3 billion of net new money in the first quarter, compared with USD 40.3 billion in the previous quarter, amid continued challenging macro conditions, including high inflation and interest rates, and a looming recession.

Meanwhile, United States-domiciled sustainable funds shed nearly USD 5.2 billion, albeit mainly owing to a single fund. If not for **iShares ESG Aware MSCI USA ETF**, which bled USD 6.5 billion, US sustainable funds would have registered an inflow over the quarter.

The other country experiencing net withdrawals was Japan, which bled USD 961 million. Meanwhile, in Australia and New Zealand, net inflows slipped to USD 108 million from USD 1.6 billion in the last quarter of 2022.

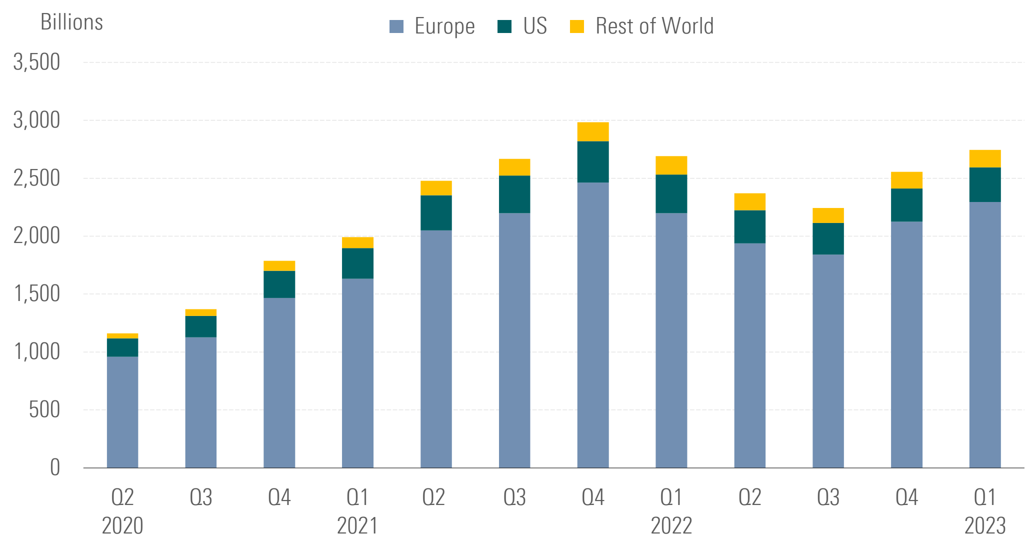
Global Assets Up 7.5% but Still Below Their Highs

Despite the lower inflows, global sustainable fund assets continued their recovery in the first quarter to hit nearly USD 2.74 trillion at the end of March, from the restated USD 2.55 trillion three months earlier. This 7.5% expansion exceeds the overall global fund market growth of 4% in the three months through March 2023.

The rebound of equity valuations had already started in the fourth quarter of 2022, and despite significant tensions in the U.S. and European banking sectors, equity markets closed the first quarter of 2023 on firm positive ground. Investors also took heart from China's abandonment of its zero-COVID policy as well as mounting expectations that the monetary policy-tightening cycle undertaken by major central banks could be close to peaking.

Europe continued to make up the lion's share of the sustainable fund landscape with 84% of global sustainable fund assets. It also remains by far the most developed and diverse ESG market, followed by the U.S., which housed 11% of global sustainable fund assets at the end of March 2023. Asia ex-Japan, of which China is the biggest sustainable market with more than 68% of the region's asset base, ranks third in terms of sustainable fund market size.

Exhibit 3 Quarterly Global Sustainable Fund Assets (USD Billion)

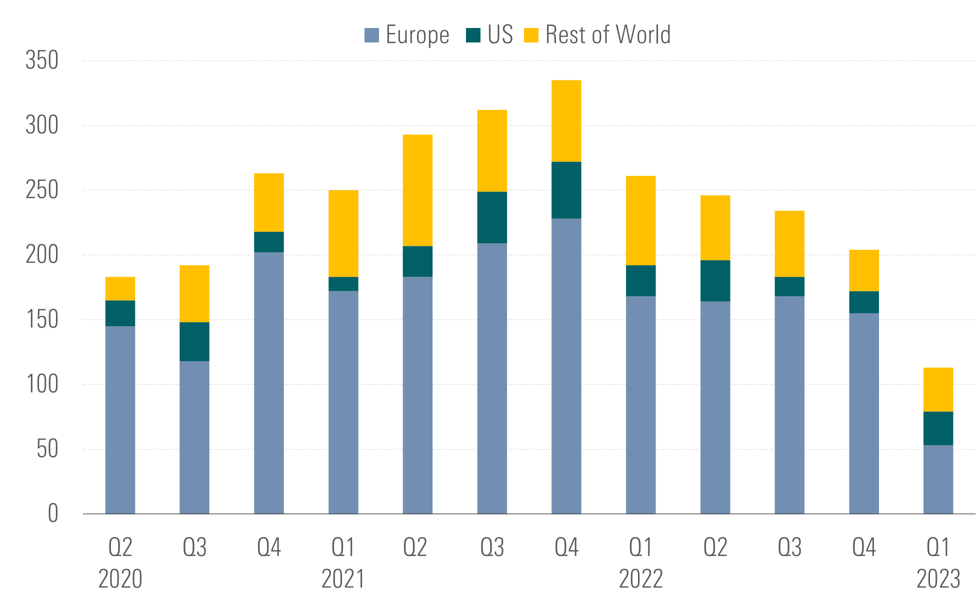


Source: Morningstar Direct, Manager Research. Data as of March 2023.

Global Fund Launches

An estimated 113 new sustainable funds hit the shelves globally in the first quarter. This represents a slowdown in product development activity compared with past quarters. However, this number will likely be higher in our next report as we identify more launches and additional ones are reported to Morningstar.

Exhibit 4 Global Sustainable Fund Launches per Quarter



Source: Morningstar Direct, Manager Research. Data as of March 2023.

The cooldown in new sustainable product development was entirely driven by a significant reduction of new sustainable fund launches in Europe, which slumped by almost two thirds. In contrast product development in the U.S. and the rest of the world continued their momentum.

Regulatory Update

The year 2023 has continued where 2022 left off on the regulatory front. In April, the International Sustainability Standards Board decided to require that IFRS S1 General Sustainability-related disclosures to be respectively effective for annual reporting periods beginning on or after 1 January 2025 and 1 January 2024. IFRS S1 will require a company to disclose information that enables investors to assess the effect of significant sustainability-related risks and opportunities on its enterprise value and will operate alongside separate IFRS S2 Climate-Related Disclosures.

Also at the global level, IOSCO published a Report on International Work to Develop a Global Assurance Framework for Sustainability-related Corporate Reporting. In the report, the global standards-setter encourages timely and high-quality profession-agnostic standard-setting outcomes responsive to the public interest and calls for early engagement with preparers, investors, and providers.

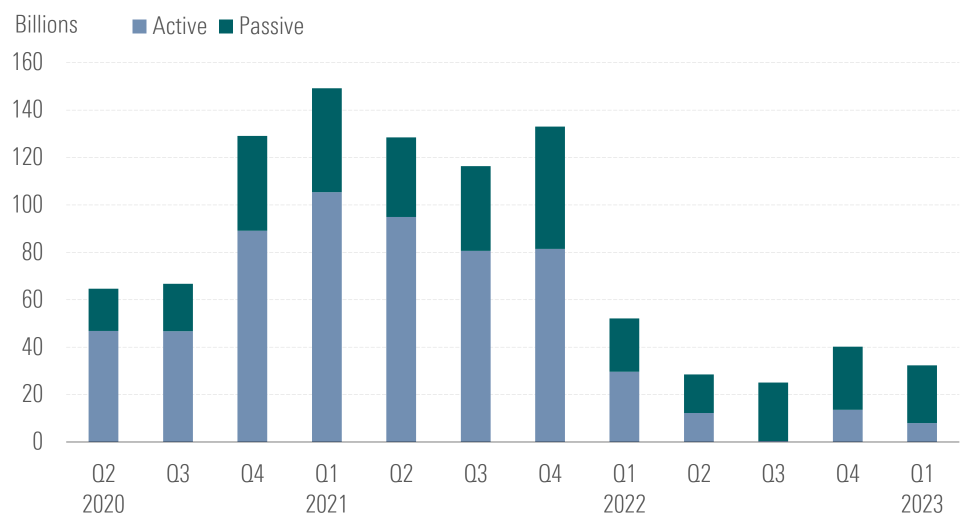
Quarterly Statistics per Domicile

Europe

A Slow Start to the Year

After rebounding toward the end of 2022, net flows into the European sustainable fund universe declined to USD 32.3 billion in the first quarter of 2023 from the readjusted USD 40.3 billion of the previous quarter. Once more, passive strategies captured most (75%) of the net new capital.

Exhibit 5 European Sustainable Fund Flows (USD Billion)



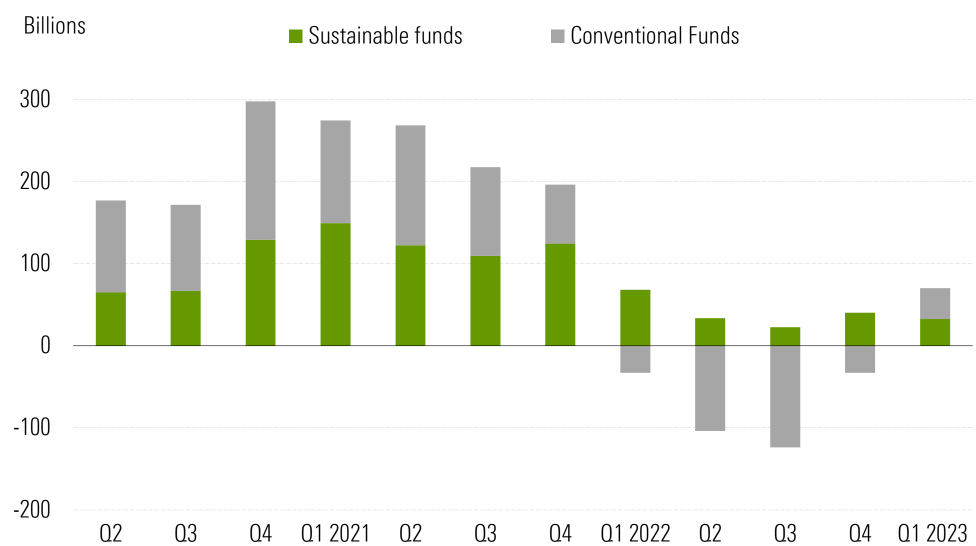
Source: Morningstar Direct, Manager Research. Data as of March 2023.

The decline in net subscriptions was further confirmed when looking at organic growth rates. Calculated as net flows relative to total assets at the start of a period, the organic growth rate for the European sustainable fund universe in the first quarter was 1.5%, compared with 2.2% in the fourth quarter of 2022. The first-quarter 2023 OGR also remains below the 2022 average OGR of 1.7%.

The sustainable funds' OGR in the first quarter was still twice as high as that of the broader market. The overall European fund market had an organic growth of 0.73% over the period, after suffering four quarters of contraction amid continued geopolitical tension, high inflation and interest rates, and a looming recession.

Inflows into sustainable funds represented 43% of total European fund flows.

Exhibit 6a Sustainable Fund Flows Compared With Conventional Fund Flows (USD Billion)



Source: Morningstar Direct, Manager Research. Data as of March 2023.

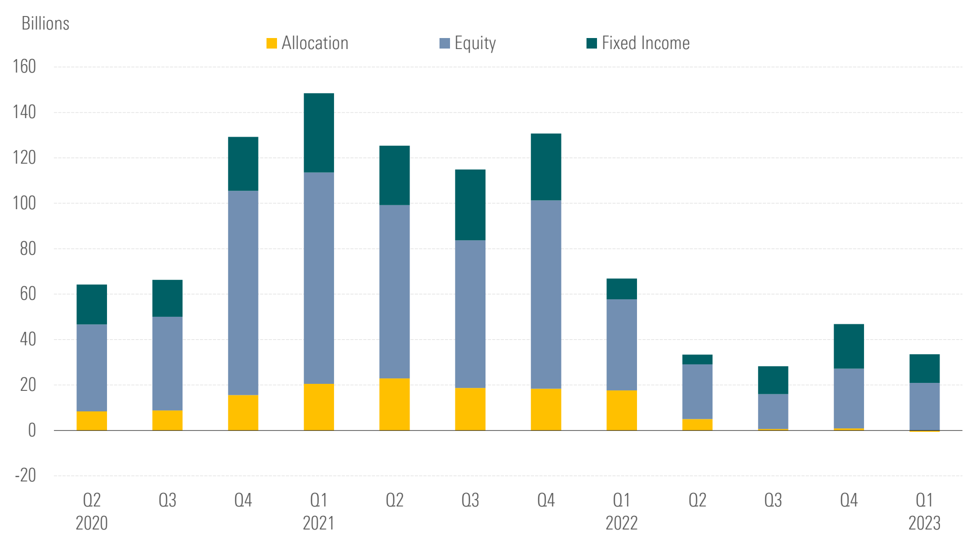
Exhibit 6b Sustainable Fund Flows Compared With Conventional Fund Flows by Asset Class (USD Billion)

USD Billion	Sustainable Funds		Conventional Funds		Overall Fund Universe	
	Q4 2022	Q1 2023	Q4 2022	Q1 2023	Q4 2022	Q1 2023
Allocation	-1.5	-0.6	-11.3	-10.8	-12.8	-11.4
Alternative	0.3	0.0	-5.9	-6.9	-5.6	-6.9
Commodities	0.0	0.1	-4.3	0.5	-4.3	0.6
Convertibles	0.0	-0.2	-1.5	-1.9	-1.4	-2.1
Equity	22.0	20.9	-21.9	11.3	0.1	32.2
Fixed Income	19.2	12.6	1.1	51.2	20.3	63.8
Miscellaneous	0.2	-0.6	1.2	0.0	1.4	-0.6
Property	0.1	0.0	-0.2	-0.5	-0.2	-0.4
Total	**40.3**	**32.3**	**-42.7**	**42.8**	**-2.5**	**75.0**

Source: Morningstar Direct, Manager Research. Data as of March 2023.

Sustainable equity funds remained the most favored, pocketing nearly USD 21 billion. This is almost twice as much as the net subscriptions registered by conventional funds. Meanwhile, sustainable bond funds gathered only USD 12.6 billion, which is much less than in the previous quarter. By contrast, conventional bond funds experienced a strong rebound in inflows over the last three months, driving the strong recovery of conventional funds overall. Sustainable funds in the other asset classes gathered close to zero net new money.

Exhibit 7 European Sustainable Fund Flows by Asset Class



Source: Morningstar Direct, Manager Research. Data as of March 2023.

Leaders and Laggards

In the first quarter of 2023, active and passive strategies split the best-selling sustainable products, netting altogether almost USD 11 billion of net new money. Amid easing inflation pressure in the U.S., **Swisscanto IPF I IEF USA Responsible** topped the leaderboard, capturing an inflow of USD 3.1 billion. In addition to sectoral exclusions, the fund screens out ESG laggards based on Swisscanto's proprietary rating and aims for a 20% lower carbon dioxide equivalent intensity score than the parent benchmark.

The second-biggest money-gatherer last quarter was **BlackRock ACS World ESG Insights Equity Fund**, which combines both exclusionary screens and a tilt toward companies better aligned with the longer-term sustainable, transformative change. The fund seeks to have 50% lower exposure to carbon emission intensity and potential emissions from fossil fuel reserves relative to its reference benchmark.

Exhibit 8a Top 10 Sustainable Fund Flows in First-Quarter 2023

Fund Name	Net Flows (USD, Million)
Swisscanto IPF I IEF USA Responsible	3,146
Blackrock ACS World ESG Insights Equity Fund	1,459
Swisscanto Index Equity Fund Europe (ex CH) Responsible	859
M&G Sustainable Total Return Credit Investment Fund	849
SG BlackRock Obligations Euro ISR	696
iShares MSCI EM ESG Enhanced ETF	664
UBS MSCI Emerging Markets Socially Responsible ETF	628
ASR Duurzaam Wereldwijd Aandelen Fonds	622
KBC Corporate Bonds Responsible Investing	612
Swisscanto Bond Fund Sustainable CHF	601

Source: Morningstar Direct, Manager Research. Data as of March 2023.

In the table below, active and passive funds were also equally represented among the worst-selling funds. **Royal London US Equity Tilt Fund** registered a USD 8.1 billion outflow in the first quarter due to a single client moving its assets into a tax-transparent version of the same strategy. The same operation was implemented in the **Royal London Japan Equity Tilt Fund**, thus explaining the USD 1 billion withdrawal from that fund too. Both strategies seek to achieve carbon intensity of at least 30% lower than the reference index while also considering a company's ability and willingness to transition and contribute to a low-carbon economy.

Exhibit 8b Bottom 10 Sustainable Fund Flows in First-Quarter 2023

Fund Name	Net Flows (USD, Million)
Royal London US Equity Tilt Fund	-8,099
Mercer Passive Global High Yield Bond Fund	-1,251
Royal London Japan Equity Tilt Fund	-1,069
UBS Global Gender Equality ETF	-886
UBS MSCI ACWI Socially Responsible ETF	-828
Amundi Ultra Short Term Bond SRI	-465
Northern Trust Pacific Custom ESG Index Fund	-461
G.A.-FUND-B Sustainable World Bonds	-449
Allianz Enhanced Short Term Euro	-372
Allianz Advanced Fixed Income Euro	-360

Source: Morningstar Direct, Manager Research. Data as of March 2023.

Meanwhile, **Mercer Passive Global High Yield Bond Fund** bled over USD 1.2 billion after its stellar flow performance in the previous quarter. The fund tilts toward issuers ranked higher on ESG criteria and green-bond issues, and it underweights or excludes issuers that rank lower.

The table above also shows a strong presence of fixed-income strategies (five out of 10). This is perhaps unsurprising given that rising interest rates have propelled investors to readjust their duration exposure. With market narrative shifting from "transitory" to "stickier than expected," taming inflation may take longer than initially expected.

The aggregate inflows among the top 10 best-selling firms netted USD 27.5 billion in the first quarter, a 20% contraction from the previous quarter. By and large, such decrease was due to the decelerated inflows into BlackRock's sustainable funds after its stellar performance toward the end of 2022. In fact, net new money into the other firms in the leaderboard totaled USD 18.7 billion, overshooting the previous quarter's 17.7 billion.

Exhibit 9a Top 10 European Sustainable Fund Providers by Flows in First-Quarter 2023

Firm	Net Flows (USD Million)
BlackRock (inc. iShares)	8,738
Swisscanto	7,265
DWS (inc. Xtrackers)	1,725
KBC	1,706
JPMorgan	1,617
UBS	1,549
M&G	1,333
ASR	1,306
Schroders	1,164
Handelsbanken	1,088

Source: Morningstar Direct, Manager Research. Data as of March 2023.

Swisscanto featured in second place thanks to its two best-selling passive ESG funds, namely **Swisscanto Index Equity Fund Europe (ex CH) Responsible** and **Swisscanto Bond Fund Sustainable**. UBS appeared as one of the new joiners in the leaderboard despite recording significant outflows in two passive strategies, namely **UBS Global Gender Equality ETF** and **UBS MSCI ACWI Socially Responsible ETF**.

At the other end of the spectrum, Royal London topped the ranking of the worst-selling firms of sustainable funds, but this is attributed almost entirely to a single client switching assets from **Royal London US Equity Tilt Fund** and **Royal London Japan Equity Tilt Fund** to tax-transparent versions of the same strategies, as previously mentioned.

Exhibit 9b Bottom 10 European Sustainable Fund Providers by Flows in First-Quarter 2023

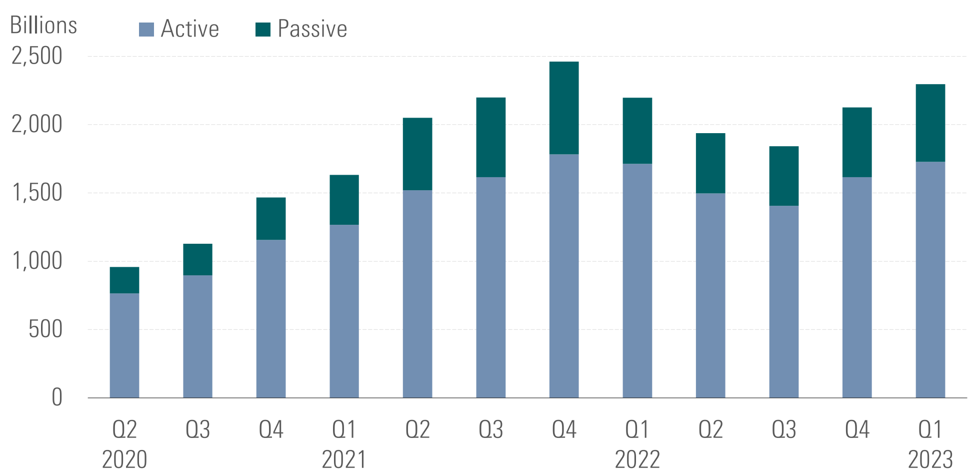
Firm	Net Flows (USD Million)
Royal London	-9,303
Pictet	-1,010
Mercer Global Investments	-979
ABN AMRO	-641
Ofi Invest	-499
Eurizon	-415
Liontrust	-353
Carmignac	-300
La Banque Postale	-279
CaixaBank	-257

Source: Morningstar Direct, Manager Research. Data as of March 2023.

European Sustainable Funds Assets Edging Toward Historical High

Despite lower inflows, assets in European sustainable funds rose for the second-consecutive quarter and reached USD 2.3 trillion at the end of March 2023, up 8.2% from December 2022. Meanwhile, assets in the overall European fund universe inched ahead by less than 3%. As a result, the market share of sustainable funds in Europe rose to 22% from 18%.

Exhibit 10 European Sustainable Fund Assets (USD Billion)



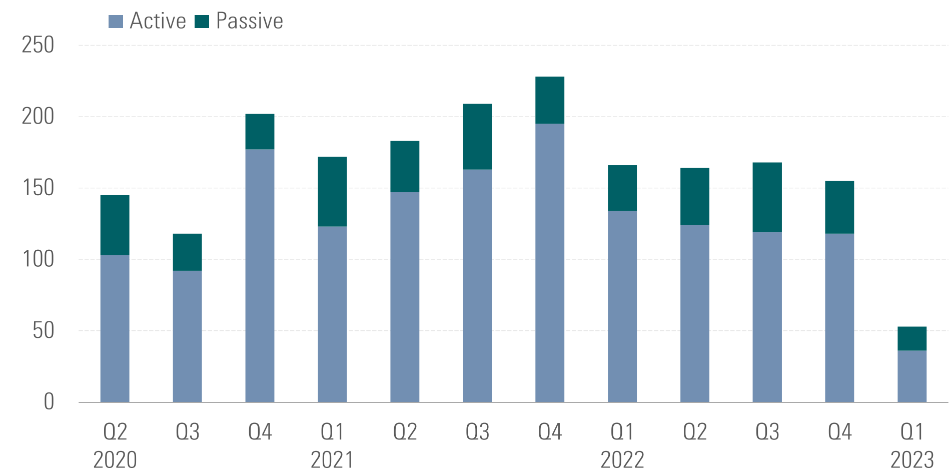
Source: Morningstar Direct, Manager Research. Data as of March 2023.

Sustainable funds should continue to gain ground as investor demand grows for strategies that align with their sustainability preferences, prompting asset managers to launch additional sustainable products and repurpose existing conventional ones. The MiFID II amendment, which came into effect in August 2022 and which requires financial advisers to consider their clients' sustainability preferences, has the potential to accelerate adoption of sustainable investments among retail investors despite macroeconomic headwinds.

Launches

After the slowdown in product development over 2022, the number of newly launched sustainable funds at the beginning of 2023 declined further at a historical low of 53, from 155 in the fourth quarter of 2022. However, it is likely the first-quarter 2023 number will be restated in future reports as we identify more launches and additional ones are reported to Morningstar.

Exhibit 11a European Sustainable Fund Launches



Source: Morningstar Direct, Manager Research. Data as of March 2023.

The decline in new products can be partly attributed to the overall market sentiment damped by the challenging macro backdrop but also to greenwashing accusations and the ever-evolving regulatory environment. A clarification by ESMA[2] last summer led many product manufacturers to downgrade Article 9 funds to Article 8 funds in the second part of the year, while waiting for further guidance on fund classification and how to interpret the definition of a "sustainable investment" provided by Article 2 No. 17 of the EU's Sustainable Finance Disclosure Regulation.

For more details on SFDR: Read SFDR Article 8 and Article 9 Funds: Q1 2023 in Review (from 2 May 2023)

Equity offerings constituted half of new fund launches.

The table below shows the 10 largest new fund launches in the first quarter. The overwhelming majority of newly incepted funds distributed in the EU were classified as either Article 8 or 9 under SFDR.

2 ESMA clarifies the EC's June 2021 Q&A over the summer last year. It specified that funds making Article 9 disclosures may only invest in sustainable investments based on the definition provided by Article 2 No. 17 of the Disclosure Regulation, with the exception of cash and assets used for hedging purposes.

Exhibit 11b Top 10 European Sustainable Fund Launches by Assets

Fund Name	SFDR Fund Type	Fund AUM (USD, Million)
ASR Duurzaam Azië Aandelen Fonds	Article 8	469
Invesco Global High Yield Corporate Bond ESG ETF	Article 8	200
Amundi MSCI Pacific ESG Climate Net Zero Ambition CTB ETF	Article 8	190
LBPAM ISR Protect 80-85 Mai 2028	Article 8	110
Amundi S&P SmallCap 600 ESG ETF	Article 8	80
L&G Future World Global Equity Focus Fund	Article 9	79
Amundi MSCI Europe Small Cap ESG Climate Net Zero Ambition CTB ETF	Article 8	74
iShares MSCI World Quality Factor ESG ETF	Article 8	57
DWS StepIn ESG Future Trends	Article 8	49
BLKB Equity Switzerland Focus	N/A	49

Source: Morningstar Direct, Manager Research. Data as of March 2023.

While general ESG-focused offerings continued to account for most of the product development in the last three months, climate remained by far the most popular theme represented among new product launches. Fifteen new climate-related funds came to market in the last quarter. Unlike diverse climate investment approaches seen in the past, spanning from green bonds to climate solutions strategies, these new climate launches focused mostly on climate transition. Examples include **Amundi MSCI Pacific ESG Climate Net Zero Ambition CTB ETF**, which aims to reweight securities in the parent index based on the opportunities and risks associated with the climate transition to meet the EU Climate Transition Benchmark, or EU CTB, regulation minimum requirements. The fund had gathered USD 190 million of assets at the end of March. Pictet launched **Pictet China Environmental Opportunities**, which invests in companies involved in renewable energy, green transportation, industrial decarbonization, resource efficiency, and environmental protection.

Furthermore, among the new launches, we see eight Xtrackers MSCI Global SDG ETFs that cover a wide range of sustainability themes, including climate transition, healthcare, clean water, and sanitation. In addition to the common sectoral and norm-based exclusion, these funds invest in companies that must pass certain SDG criteria, including revenue and relevance thresholds from associated business activities.

The overwhelming majority of newly incepted funds distributed in the EU were classified as either Article 8 or 9 under SFDR.

Along with fund launches, we also saw continued rebranding activities. **BNP PARIBAS Easy MSCI EMU ESG Filtered MIN TE**, rebranded from **BNP Paribas Easy MSCI EMU ex Controversial Weapons,** now excludes 20% of the companies from its parent MSCI Emerging Market Index by combining ESG score screening and controversial sector exclusion. Another passive strategy, **Ofi Invest ESG Global Emerging Debt**, switched from **Single Select Platform OFI RS Global Emerging Debt** and tracks the JP Morgan ESG GBI EM Global Diversified Index. In addition to sectoral exclusion, the index applies an ESG scoring and screening methodology to tilt toward issuers ranked higher on ESG criteria and green-bond issues.

Regulatory Update

Things continue apace on the regulatory front in Europe. The three European Supervisory Authorities (European Banking Authority, European Insurance and Occupational Pensions Authority, and European Securities and Markets Authority) published a consultation paper with amendments to extend sustainability disclosures as required by Sustainable Finance Disclosure Regulation, while the European Commission provided answers to clarifying questions that the ESAs had posed last year.

For more details on SFDR: Read SFDR Article 8 and Article 9 Funds: Q1 2023 in Review (from 2 May 2023).

The commission is also currently consulting on criteria in respect of the remaining four taxonomy objectives—Water, Circular Economy, Pollution Prevention and Control, and Biodiversity—as well as proposing targeted amendments to the Taxonomy Climate Delegated Act and to the Taxonomy Disclosures Delegated Act.

The European Green Bond Standard was concluded, and all companies choosing to use the standard when marketing a green bond will be required to disclose much information about how the bond's proceeds will be used, as well as show how those investments feed into the transition plans of the company as a whole. The standard therefore requires companies to be engaging in a general green transition. The adoption of the standard will also guarantee to investors that the bond is mainly taxonomy aligned (85%).

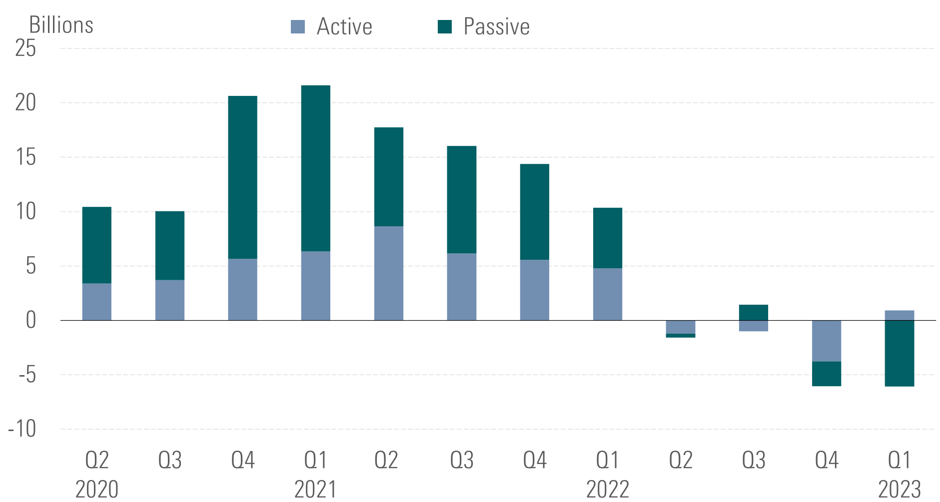
Meanwhile, the UK regulator has deferred its follow-up to sustainable disclosures and labels until the third quarter, while it assesses around 240 responses to its consultation, which closed in January. In the meantime, the Financial Conduct Authority has issued another discussion paper seeking views on the extent to which additional regulation or guidance is necessary to frame firms' responsibilities in the areas of sustainability-related governance, incentives, and competencies.

Also in the UK, the government published its updated UK Green Finance Strategy, in which it confirmed its intention to mandate disclosures against ISSB standards. The UK taxonomy will be consulted again in late 2023 with nuclear included and interoperability with other taxonomies stated as an objective. A period of at least two years of voluntary disclosures will apply before mandatory reporting. It also announced an intention to explore how the final Taskforce on Nature-Related Financial Disclosures framework, due to be published in September 2023, should be best incorporated into UK policy and legislative architecture. Lastly, in the area of stewardship, there will be a review of the Financial Reporting Council code of conduct toward the end of the year.

United States

Investors pulled USD 5.2 billion from sustainable funds in the first quarter, marking it the third quarter of outflows in a year. In total, investors have withdrawn USD 12.4 billion from these funds over the past year. Market volatility and global macroeconomic pressures, including an ongoing energy crisis, hiking interest rates, and rising fears of recession, have contributed to this retreat. Another possible factor damping investor demand for ESG products is the growing political backlash against sustainable investing. Republican governors from at least 19 US states have pledged to resist ESG investing over antitrust, consumer protection, and discrimination concerns.

Exhibit 12 U.S. Sustainable Fund Flows



Source: Morningstar Direct, Manager Research. Data as of March 2023.

The weaker demand for sustainable funds in the last three months was a notable departure from the total universe of U.S. open-end and exchange-traded funds, which saw USD 17 billion in net inflows during the same period, down from their typical USD 100 billion-plus quarterly haul, but positive, nonetheless.

Consequently, for the second quarter in more than five years, the U.S. sustainable funds segment saw a lower organic growth rate than the total U.S. fund universe. Calculated as net flows as a percentage of total assets at the start of a period, the organic growth rate puts the magnitude of fund flows into perspective. During the first quarter, sustainable funds contracted by 1.8% compared with a tiny 0.08% growth in the overall U.S. funds landscape.

Sustainable actively managed funds broke a three-quarter outflows streak and bounced back into positive territory, netting a modest USD 91 million during the period. This is a brighter picture than their outflows in 2022 but still well below their average quarterly intake of USD 6.7 billion in 2021.

Meanwhile, sustainable passive funds shed nearly USD 6.1 billion during the quarter, bucking a multiperiod trend of holding down the fort for U.S. sustainable funds. If not for one fund, namely iShares ESG Aware MSCI USA ETF ESGU, which bled nearly USD 6.5 billion, passive funds would have ended the quarter in the black.

Leaders and Laggards

Topping the table of the worst-selling sustainable funds with net withdrawals of nearly USD 6.5 billion, it's hard to miss iShares ESG Aware MSCI USA ETF. The fund favors stocks with high ESG ratings and avoids stocks involved in controversial activities such as civilian firearms and thermal coal.

Exhibit 13a Bottom 10 Sustainable Fund Flows

Fund Name	Net Flows (USD Million)
iShares ESG Aware MSCI USA ETF	-6,463
Invesco Floating Rate ESG Fund	-443
Parnassus Core Equity Fund	-393
TIAA-CREF Social Choice Equity Fund	-355
iShares MSCI KLD 400 Social ETF	-342
Parnassus Mid Cap Fund	-254
iShares Global Clean Energy ETF	-237
iShares ESG Advanced Total USD Bond Market ETF	-213
iShares MSCI USA ESG Select ETF	-207
Pioneer Fund	-199

Source: Morningstar Direct, Manager Research. Data as of March 2023.

IShares ESG Aware MSCI USA ETF was the top money-getter among U.S. sustainable funds in 2020 and 2021. This was partly due to its inclusion in BlackRock's flagship target allocation ETF model portfolios (which had nearly USD 40 billion in assets under advisement as of December 2022). However, in March, BlackRock's model portfolio management team pared back the allocation to iShares ESG Aware MSCI USA ETF in its portfolios and largely replaced it with iShares MSCI USA Quality Factor ETF QUAL[3], hence the USD 6.5 billion of outflows.

Some of the funds in the bottom 10 have sustained outflows over multiple quarters. Four of these funds, namely Parnassus Core Equity PRBLX, TIAA-CREF Social Choice Equity TISCX, Parnassus Mid Cap PARMX, and iShares MSCI USA ESG Select ETF SUSA, were among the bottom 10 funds for outflows in 2022 too. This marks the sixth-consecutive quarter for outflows from Parnassus Core Equity, though it remains the largest U.S. sustainable fund to this day.

Looking at the best-selling sustainable funds in the first quarter of 2023, ironically, it's another iShares fund from the same product range that stands out, namely iShares ESG Aware MSCI EM ETF, with net inflows of USD 477 billion.

3 As model portfolios are not directly investable, it is impossible to perfectly track the impact of management recommendations. But by looking at these two funds' daily net flows, we can approximate the effect the models have had.

Exhibit 13b Top 10 Sustainable Fund Flows

Fund Name	Net Flows (USD Million)
iShares ESG Aware MSCI EM ETF	477
BlackRock Sustainable Advantage Large Cap Core Fund	475
GMO Resource Transition Fund	460
iShares ESG U.S. Aggregate Bond ETF	419
Calvert Equity Fund	419
Brown Advisory Sustainable Growth Fund	306
Vanguard FTSE Social Index Fund	240
Dimensional US Sustainability Core 1 ETF	209
iShares ESG USD Corporate Bond ETF	159
Vanguard ESG International Stock ETF	157

Source: Morningstar Direct, Manager Research. Data as of March 2023.

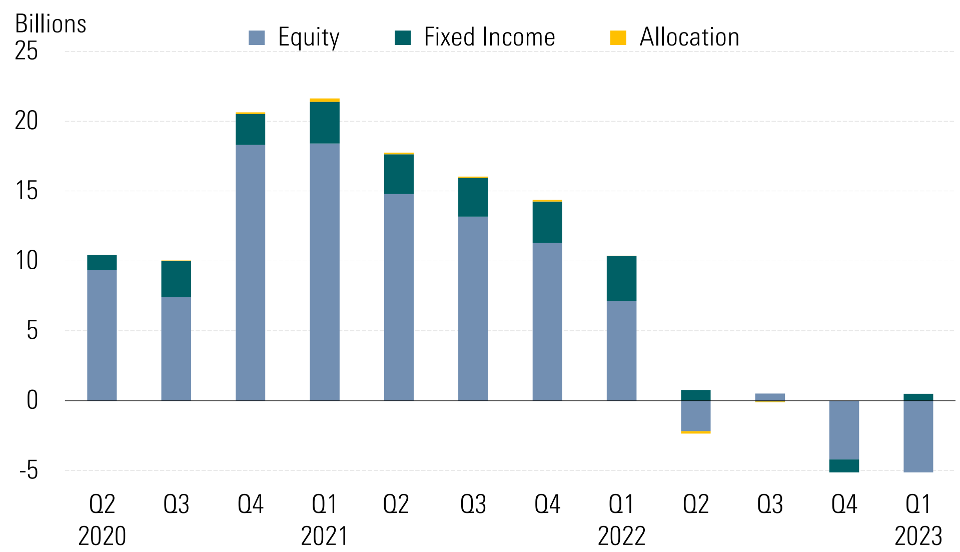
Meanwhile, GMO launched GMO Resource Transition GMOYX on Feb. 15, and it quickly catapulted to third place in terms of first-quarter flows. The fund invests in natural-resources companies that it believes will benefit from the clean energy transition. This includes companies involved in mining, precious metals, forestry, and building materials, but it generally excludes traditional oil & gas companies.

Aside from GMO's new entrant, BlackRock and Vanguard dominated the top flows table, as they usually do, with four and two funds making it to the top 10, respectively. One of these funds—iShares ESG U.S. Aggregated Bond ETF EAGG—has landed among the top 10 for each of the past three quarters.

Sustainable Bond Funds Bounce Back

During the first quarter of 2023, sustainable bond funds boomeranged back into positive territory with a modest USD 500 million collection. Two funds from BlackRock—iShares ESG U.S. Aggregate Bond ETF and iShares ESG USD Corporate Bond ETF SUSC—led the way, netting USD 420 million and USD 159 million, respectively. Meanwhile, sustainable equity funds shed USD 5.4 billion during the quarter, their third quarter of outflows in the past year. Here, too, iShares ESG Aware MSCI USA ETF drove the overall narrative.

Exhibit 14 U.S. Sustainable Fund Flows by Asset Class

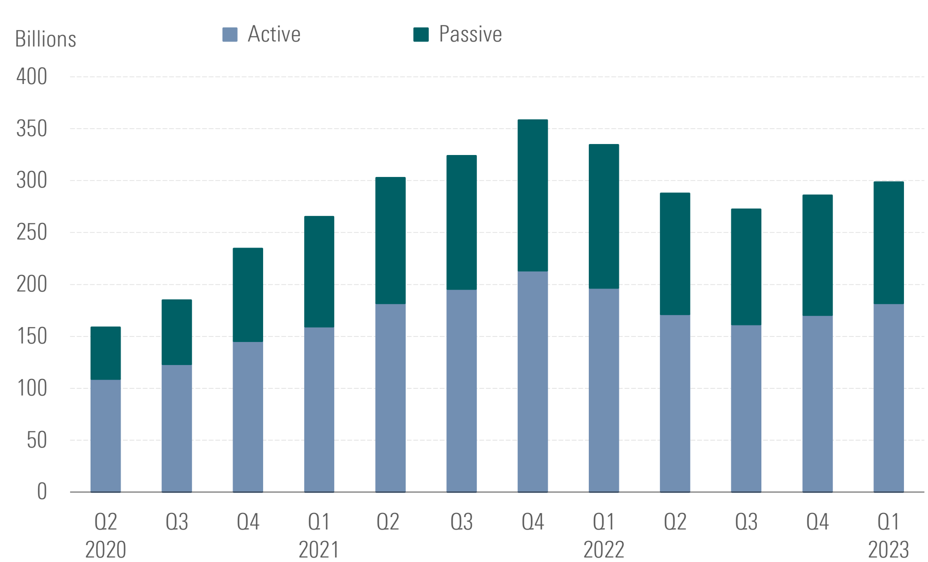


Source: Morningstar Direct, Manager Research. Data as of March 2023.

Assets in U.S. Sustainable Funds Rose on the Back of Market Appreciation

Despite outflows from sustainable funds, rising equity and bond markets drove assets in these funds to nearly USD 296 billion, their highest point in a year. This still represents a 17% decline from the record of USD 358 billion at the end of 2021. By comparison, assets in the broader U.S. market also peaked at the end of 2021 and slid by 14% at the end of 2023's first quarter.

Exhibit 15 U.S. Sustainable Fund Assets

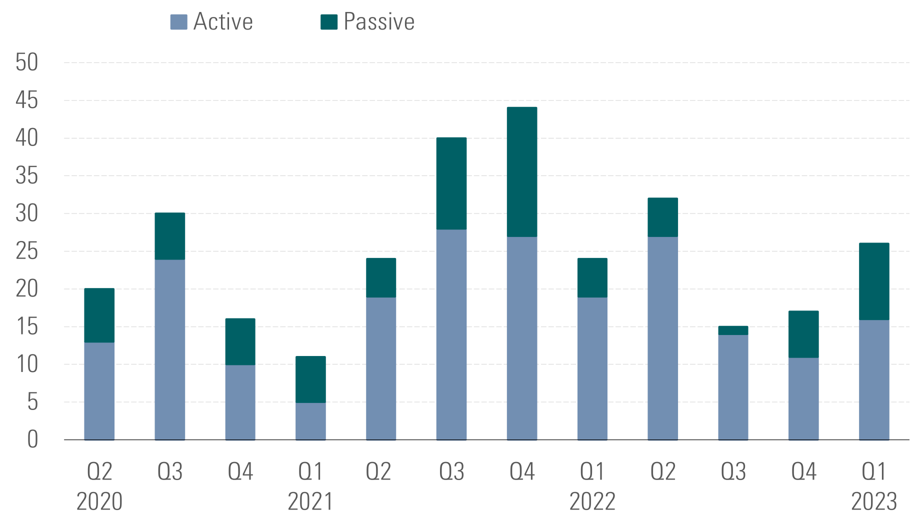


Source: Morningstar Direct, Manager Research. Data as of March 2023.

Despite Turbulent Demand, Product Development Picks Back Up

Although investors have largely pulled out of sustainable funds over the past year, some asset managers continue to see prospects for growth. During the first quarter, 27 new sustainable funds came to market, down from the record 44 in 2021's fourth quarter but up from the latter half of 2022.

Exhibit 16a U.S. Sustainable Fund Launches



Source: Morningstar Direct, Manager Research. Data as of March 2023.

Calvert, long seen as a sustainable-investing pioneer in the U.S., launched six new ETFs during the period, most of which replicate preexisting U.S. mutual funds from the firm. One exception is Calvert US Large-Cap Diversity, Equity, and Inclusion ETF CDEI, which has been available in Europe since early 2022 but just debuted to U.S. investors.

Three of the first quarter's largest new U.S. sustainable funds were fixed-income ETFs from Putnam. Putnam ESG Core Bond ETF PCRB, together with its ultrashort and high-yield siblings, follows a straightforward sustainable investing approach, which focuses on the best performers (from an ESG perspective) within each fixed-income sector.

Exhibit 16b Largest New Sustainable Funds

Fund Name	Fund AUM (USD Million)
Putnam ESG Core Bond ETF	463
GMO Resource Transition Fund	448
Putnam Panagora ESG International Equity ETF	129
Putnam ESG Ultra Short ETF	119
GuideStone Funds- Impact Equity Fund	112
Calvert US Large-Cap Core Responsible Index ETF	110
Putnam ESG High Yield ETF	102
GuideStone Funds- Impact Bond Fund	63
Cromwell Foresight Global Sustainable Infrastructure Fund	48
Brown Advisory Sustainable Value Fund	31

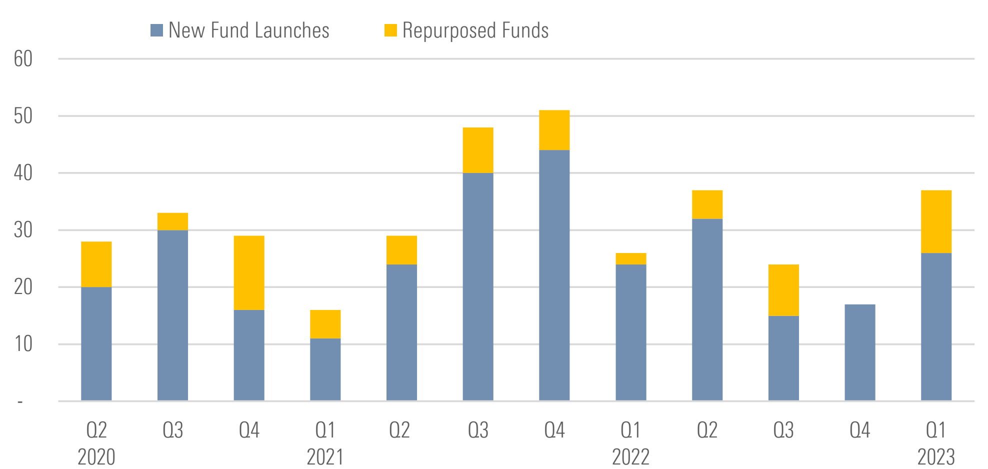
Source: Morningstar Direct, Manager Research. Data as of March 2023.

These ETFs, along with two new Putnam Panagora ESG ETFs and a couple of funds with longer track records, are destined to be building blocks for Putnam's new Sustainable Retirement target-date strategy, borne out of the firm's previous Retirement Ready funds.

One Retirement-Ready Series Gets a Sustainable Makeover

Most of the new options available to investors were launched with sustainable mandates, but firms also occasionally change the investment strategies of existing funds to target sustainable outcomes. In the first quarter of 2023, 11 funds were repurposed to adopt sustainable mandates. Of the quarter's 11 repurposed funds, 10 were individual vintages of the aforementioned Putnam Sustainable Retirement target-date strategy, which the firm overhauled in February.

Exhibit 16c New U.S. Sustainable Funds



Source: Morningstar Direct, Manager Research. Data as of March 2023.

The new offerings and repurposed funds brought the total number of sustainable open-end and exchange-traded funds in the U.S. to 638 at the end of the quarter.

For more details: Read U.S. Sustainable Fund Flows: First-Quarter 2023 in Review | Morningstar

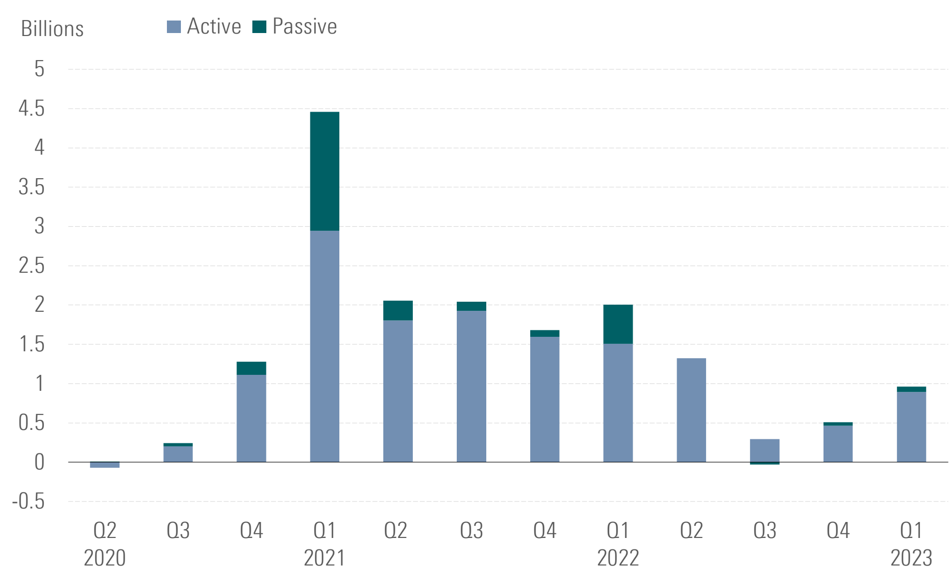
Canada

Flows

The first quarter of 2023 saw a continued rebound in inflows into Canada-domiciled sustainable funds totaling USD 963 million. In absolute terms, this represents an 89% increase from the previous quarter although still down nearly 50% from the same period last year. In terms of organic growth, which is calculated as net flows relative to total assets at the start of a period, the Canadian sustainable funds grew by 3.4% in the last three months, compared with 2% in the previous three months. This aligns with the broader trend seen across various markets in the first quarter as investor appetite to participate in the market picked up.

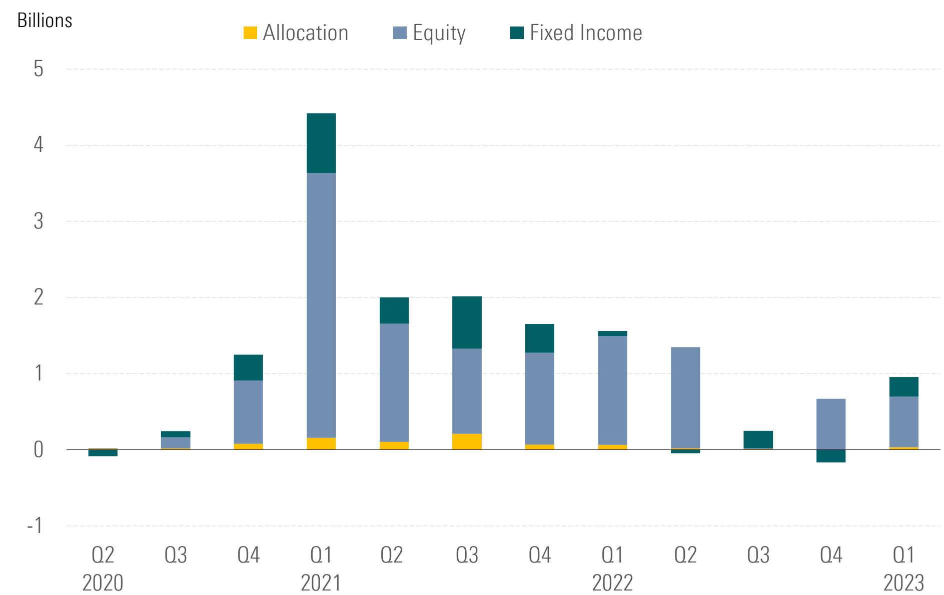
As previously observed, active strategies captured the quasi-totality of the inflows.

Exhibit 17 Canada Sustainable Fund Flows



Source: Morningstar Direct, Manager Research. Data as of March 2023.

Exhibit 18 Canada Sustainable Flows by Asset Class



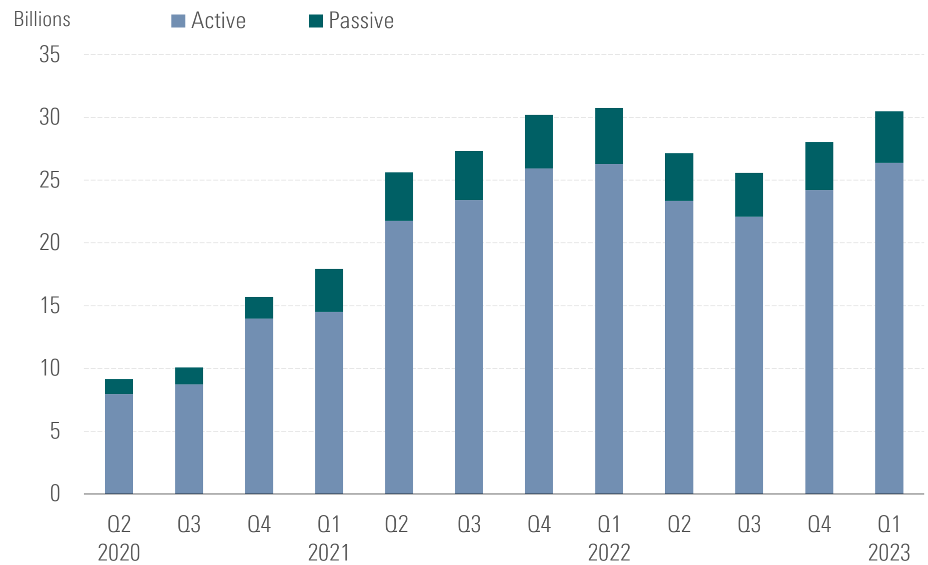
Source: Morningstar Direct, Manager Research. Data as of March 2023.

The top 10 funds by net inflows experienced a significant increase in investment, with an estimated USD 823 million invested during the quarter. This represents a 7% decrease from the previous quarter. Among these top funds, NBI products attracted the largest portion of net new money, accounting for 58% of the total inflows within the top 10 funds. Most of these inflows occurred in January and February, accounting for 96% of the flows, with March representing only 4% of the total inflows for the quarter. This pattern contrasts with prior periods where March saw most of the flows, as it coincides with the Canadian Registered Retirement Saving Plan contribution deadline.

Assets

During the first quarter of 2023, Canadian sustainable fund assets surged by 8.7%, almost reaching the record high of a year ago, at USD 30.5 billion. Both actively and passively managed strategies experienced an increase in assets from the previous quarter, with a growth rate of 9.0% and 7.2%, respectively.

Exhibit 19 Canada Sustainable Fund Assets



Source: Morningstar Direct, Manager Research. Data as of March 2023.

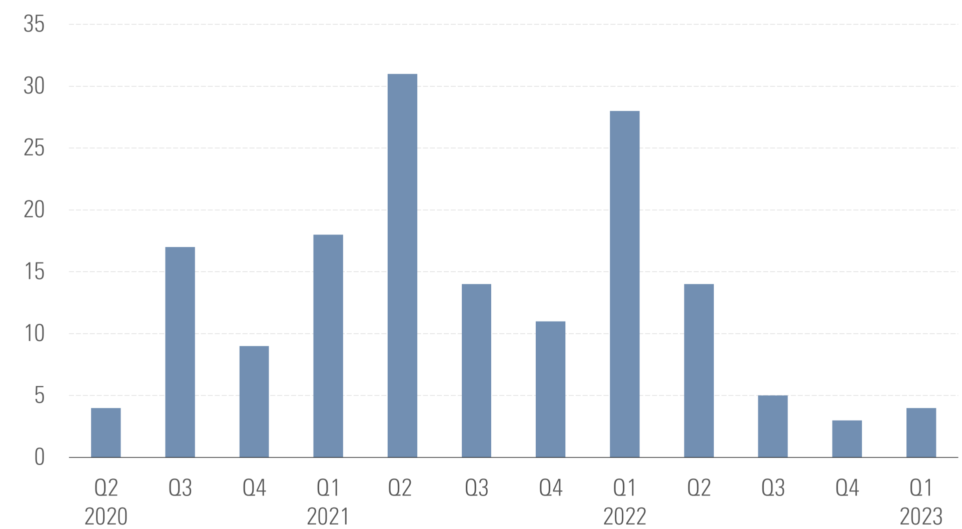
Allocation and equities saw the largest increase, with 8.7% and 9.5%, respectively, followed by fixed income with 6.6%, and alternatives with 1.1%. This pattern was consistent with the situation two quarters ago (third quarter of 2022), but not with the same period last year (first quarter of 2022), where allocation and fixed income experienced a decline of 20% and 9.1%, respectively, while alternatives and equities funds grew by 10.4% and 3.2%, respectively.

In terms of market share dominance, equities remained the dominant asset class, accounting for 72% of sustainable fund assets, followed by fixed income at 23%, with the remaining assets allocated to allocation and alternative funds. However, no asset class showed any significant changes in market share compared with the previous quarter.

New Launches

Product development in the sustainable funds and ETF market in Canada increased compared with the previous quarter, although it remained down compared with a year ago. According to Morningstar data as of this writing, the first quarter of 2023 saw the launch of one new sustainable mutual fund and three ETFs, an improvement compared with the fourth quarter of 2022. However, the appetite for product launches has been low for both sustainable and traditional investment products in the past year. This trend may be partly attributed to concerns of a potential global recession.

Exhibit 20 Canada Sustainable Fund Launches



Source: Morningstar Direct, Manager Research. Data as of March 2023.

Regulatory Update

In February 2023, the Canadian Investment Funds Standards Committee, or CIFSC, published an inaugural list of mutual funds and ETFs that fall under its Responsible Investment Identification Framework, after lengthy consultations with the industry and several rounds of prospectus reviews with input from fund manufacturers.

In March, Canada's Department of Finance published the Sustainable Finance Action Council, or SFAC, recommendations for the development of a green taxonomy for sustainable investment, as the country moves toward its goal of net-zero greenhouse gas emissions by 2050. "The Taxonomy Roadmap Report" sets out emissions-based criteria for categorizing financial investments or assets into one of two investment categories—"green finance" and "transition finance." The TTEG has designed the taxonomy with the objective of encouraging the issuance of both green and transition financial instruments in a way that is consistent with Canada's Paris-aligned commitment to limit global warming to 1.5° C.

Australia and New Zealand

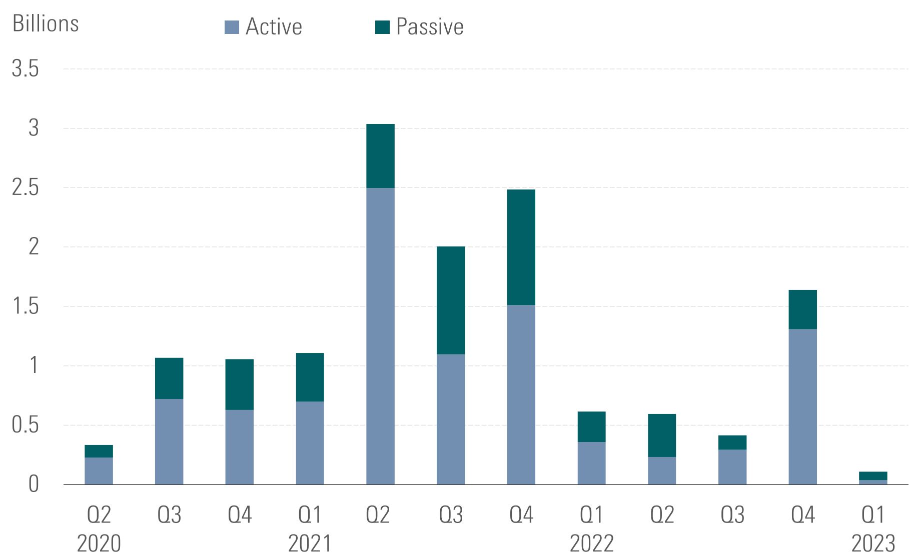
Flows

Inflows into the Australasian (Australia and New Zealand) sustainable funds universe during the first quarters of 2023 were significantly lower than in previous quarters. They amounted to USD 108 million, compared with USD 1.53 bilion in the fourth quarter of 2022. The last three months were marked by market volatility exacerbated by U.S. regional bank insolvencies and concerns around the viability of

European bank Credit Suisse (since acquired by UBS). Furthermore, the rising interest rates added to concerns about the possibility of an economic recession.

Passive strategies were the primary recipients of the new money into sustainable funds in the first quarter, attracting USD 72 million, nearly twice the amount of their active counterparts' inflows. Passive fund inflows accounted for two thirds of all sustainable fund flows.

Exhibit 21 Australia and New Zealand Sustainable Fund Flows



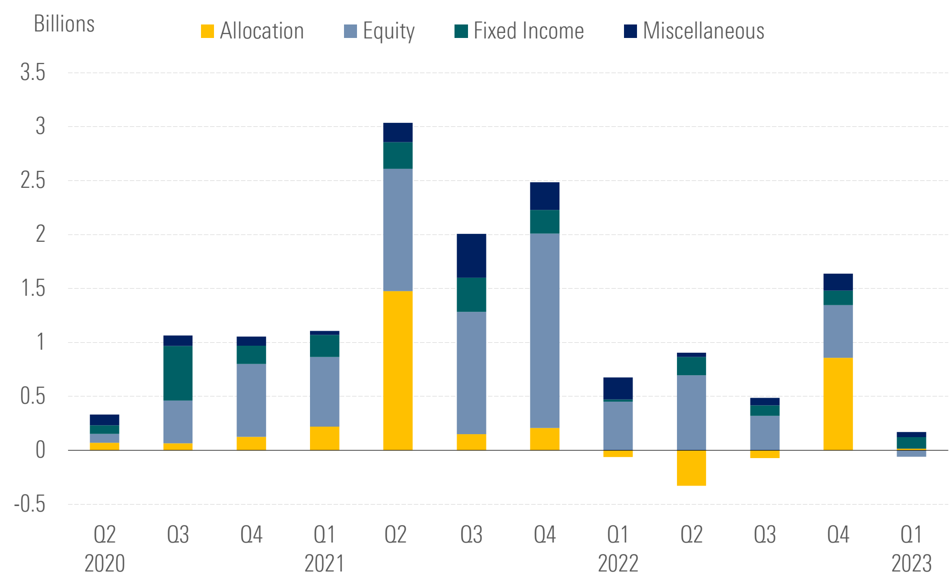
Source: Morningstar Direct, Manager Research. Data as of March 2023.

The top five fund houses by sustainable fund assets are Australian Ethical, (with market share of 17.2%), Vanguard (12.7%), DFA (10.3%), Beta Shares (9.3%), and Mercer Investments (5.1%).

Flows by Category

Fixed-income strategies dominated the flow story in the first quarter as they attracted USD 108 million of net new money, while equities experienced withdrawals of USD 60 million. Allocation strategies contributed USD 15 million of inflows, miscellaneous USD 45 million, or USD 60 million combined, neatly offsetting equity fund outflows. This picture contrasts with the historical trend. Over the last three years, equity funds have tended to capture the bulk of quarterly inflows. The only previous time sustainable equity funds experienced outflows was the first quarter of 2020 during the COVID-19 pandemic.

Exhibit 22 Australia and New Zealand Sustainable Flows by Asset Class

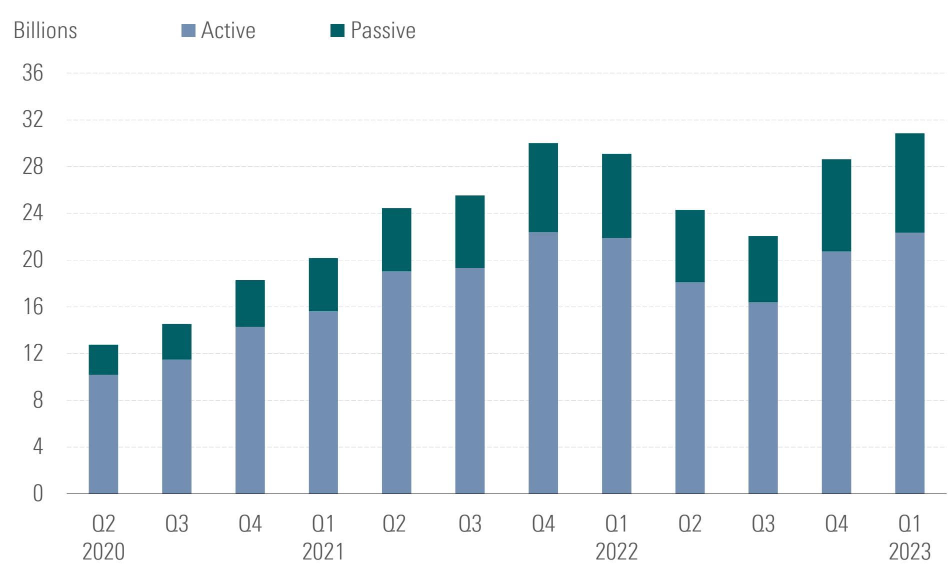


Source: Morningstar Direct, Manager Research. Data as of March 2023.

Assets

Despite the lower inflows, assets in Australasian sustainable funds increased by 7.8% during the first quarter of 2023, reaching a record high of USD 30.8 billion. This growth was driven by higher equity and bond valuations.

Exhibit 23 Australia and New Zealand Sustainable Fund Assets



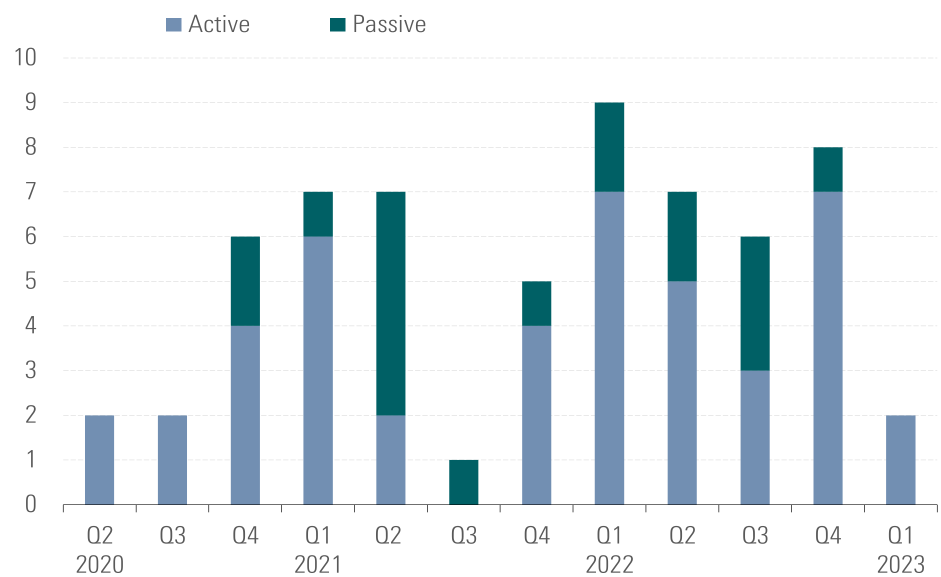
Source: Morningstar Direct, Manager Research. Data as of March 2023.

The Australian sustainable funds market remains quite concentrated, with the top 10 funds accounting for 70% of total assets. Australian Ethical, with total assets of USD 5.3 billion, is the dominant Australasian provider of sustainable strategies on the Morningstar database, followed by Vanguard with USD 3.9 billion, and DFA closely behind with USD 3.2 billion.

Launches

There were just two new sustainable funds launched in the first quarter of 2023, both active sustainable credit strategies from Janus Henderson. Launches were significantly lower than in the previous quarter where there were eight new funds launched, seven active and one passive. We have observed when new sustainable strategies are launched, they tend to be skewed to active approaches.

Exhibit 24 Australia and New Zealand Sustainable Fund Launches



Source: Morningstar Direct, Manager Research. Data as of March 2023.

With the two new strategies launched, we counted 201 strategies in our Australasian sustainable fund universe at the end of March 2023.

Regulatory Update

In the first three months of the year, Australia continued to release ESG-related legislation, the most recent being the Safeguard Mechanism (Crediting) Amendment Bill 2023, which was passed by parliament in March and will take effect in July. The bill provides a framework for the reporting measurement and management of emissions capturing large emitters (those producing more than 100,000 metric tons of scope 1 greenhouse gas per financial year) and ensuring they are contributing to a reduction in greenhouse gas emissions. Importantly, the emissions baseline for each facility will reduce over time to align with Australia's net-zero ambitions.

In addition, March saw the passing of the Workplace Gender Equality Amendment (Closing the Gender Pay Gap) Bill 2023, which was designed to help achieve gender pay equity by being transparent about the gender pay gap. In 2024, any company with more than 100 employees must publish their gender pay gap.

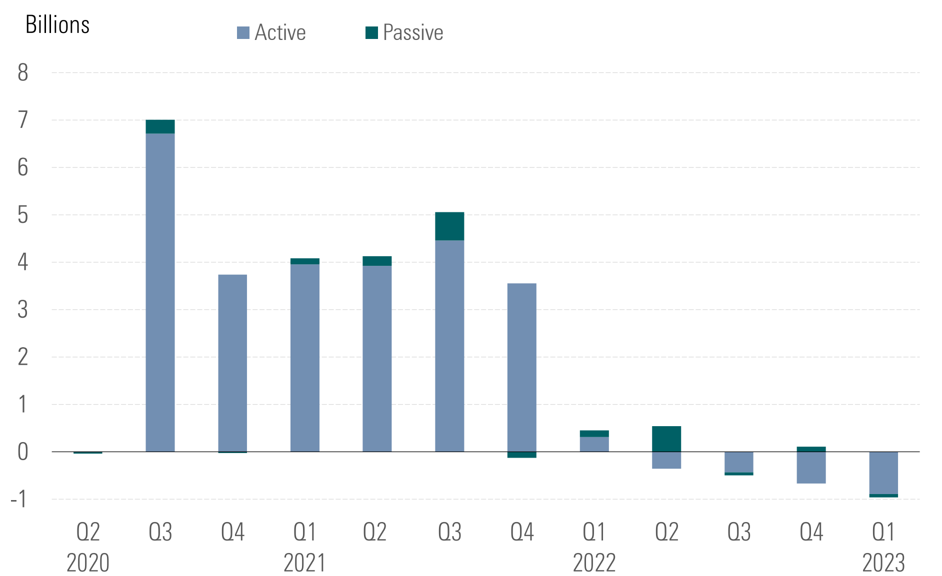
Japan

Flows

In the first quarter of 2023, the Japanese sustainable fund market saw its third-consecutive quarter of net outflows, with net withdrawals amounting to USD 961 million. This is in contrast with the overall Japanese fund market, which experienced net inflows of over USD 10 billion in the same period.

In Japan, newly launched funds tend to attract inflows, but within a few years after inception, investors take their money out. The decrease in newly launched ESG funds in the first quarter meant that inflows into newer funds couldn't offset the outflows from older funds. Notably, eight out of top 10 funds in terms of outflows were launched in either 2020 or 2021. Furthermore, nine out of the top 10 funds with the highest outflows were actively managed equity funds, which in aggregate, bled USD 569 million. This mainly explains the active/passive and asset-class split of the flows in the two exhibits below.

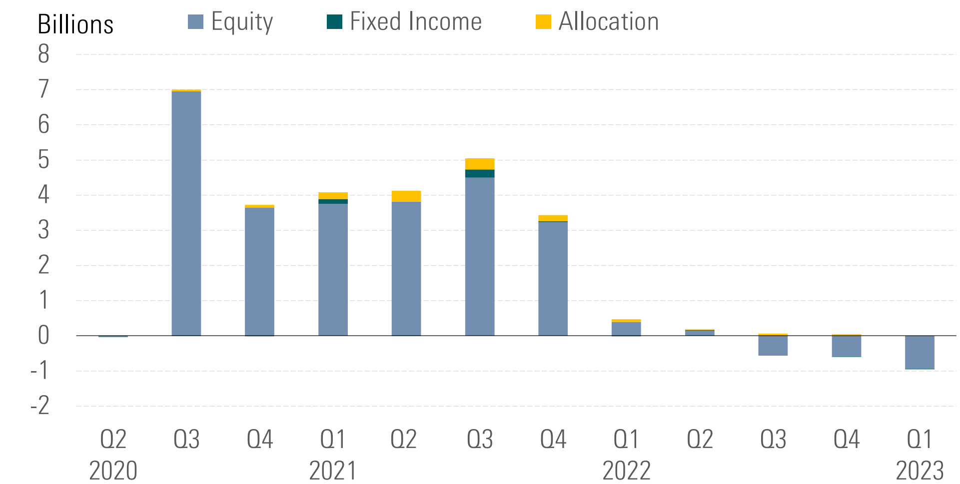
Exhibit 25 Japan Sustainable Fund Flows



Source: Morningstar Direct, Manager Research. Data as of March 2023.

It should be noted that there is a possibility of double-counting at the global level. We include Japan-domiciled funds of funds and feeder funds in this review to better reflect the actual flow situation in the Japanese fund market, as many Japanese funds of funds are invested in European funds.

Exhibit 26 Japan Sustainable Fund Flows by Asset Class

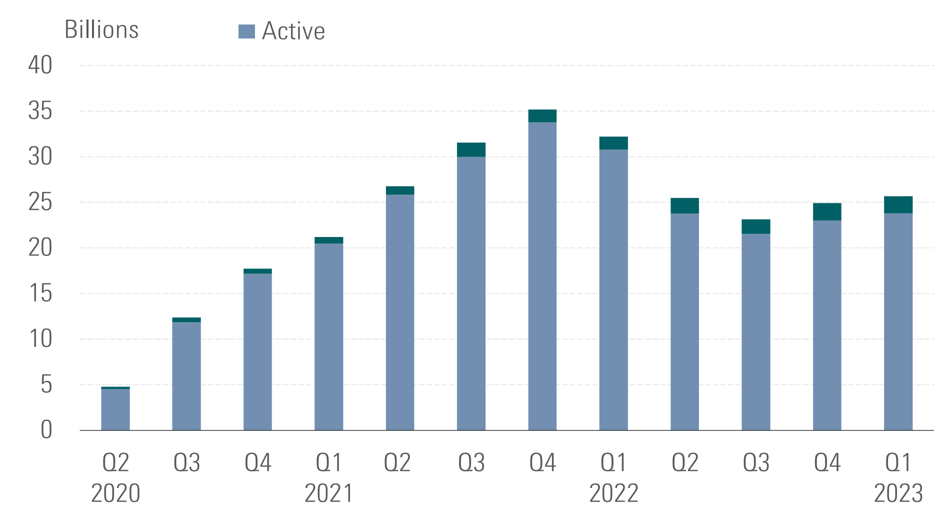


Source: Morningstar Direct, Manager Research. Data as of March 2023.

Assets

Total assets in Japan-domiciled sustainable funds increased by 3% in the first quarter, reaching a total of USD 26 billion at the end of March. Despite the outflows mentioned earlier, this growth was mainly due to higher stock prices. Equity funds make up 95% of Japan-domiciled sustainable funds, most of which are invested in global equities, which rose by about 8%.

Exhibit 27 Japan Sustainable Fund Assets

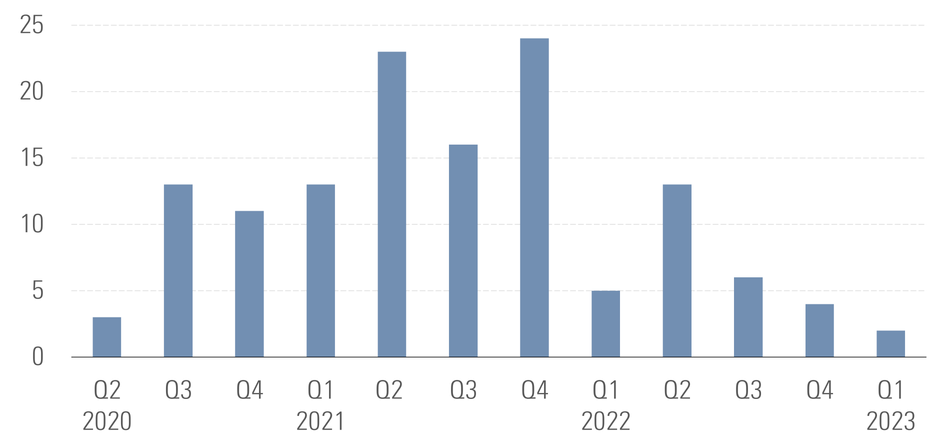


Source: Morningstar Direct, Manager Research. Data as of March 2023.

Launches

Only two new sustainable funds were launched in Japan in the first quarter of 2023, marking a decrease from the previous quarter's four new funds. The two funds are the currency-hedged and unhedged versions of the Schroder Sustainable World Equity Fund, managed by Asset Management One. The fund seeks to invest in companies managed for the long term that recognize their responsibilities to customers, employees, and suppliers, and those who respect the environment.

Exhibit 28 Japan Sustainable Fund Launches



Source: Morningstar Direct, Manager Research. Data as of March 2023.

Regulatory Update

In Japan, the Financial Services Agency revised the comprehensive supervisory guidelines to prevent greenwashing. The revision provides specific points for supervisors to check fund disclosures and organizational resources of asset managers regarding ESG. "ESG investment trust" is defined as a fund that considers ESG as a key factor in the selection of investment assets and describes its content in the "Objective and Characteristics of the Fund" section in the fund prospectus. Funds that include ESG-related terms such as "ESG," "SDGs," "green," "decarbonization," "impact," "sustainable," and so on, in their names but are not categorized as "ESG investment trusts," will be required to remove the ESG-related terms from their names as soon as possible.

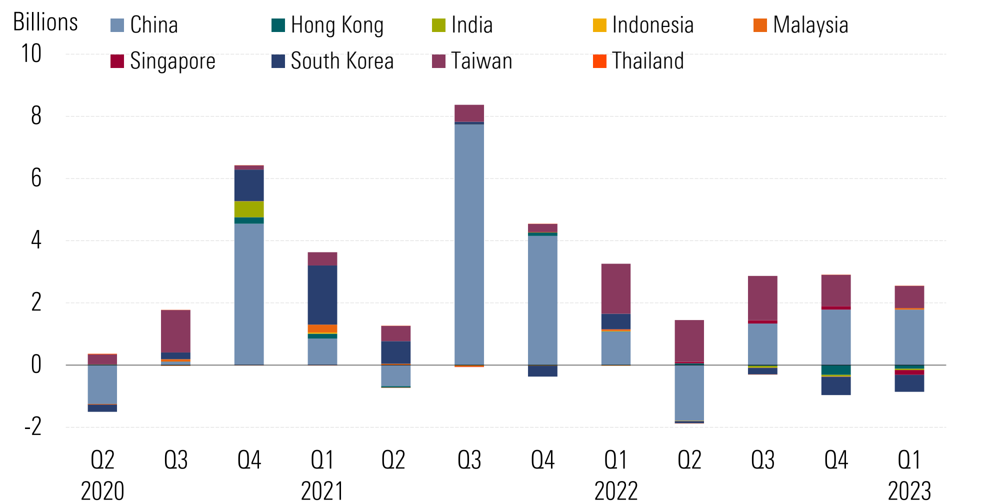
Asia ex-Japan

We used the most-recent data available within the past quarter for funds whose full quarterly data was unavailable at the time of publication. Because China's data was not available at the time of publication, we used fourth-quarter 2022 data as a proxy for first-quarter 2023 data in every exhibit of this section.

Flows

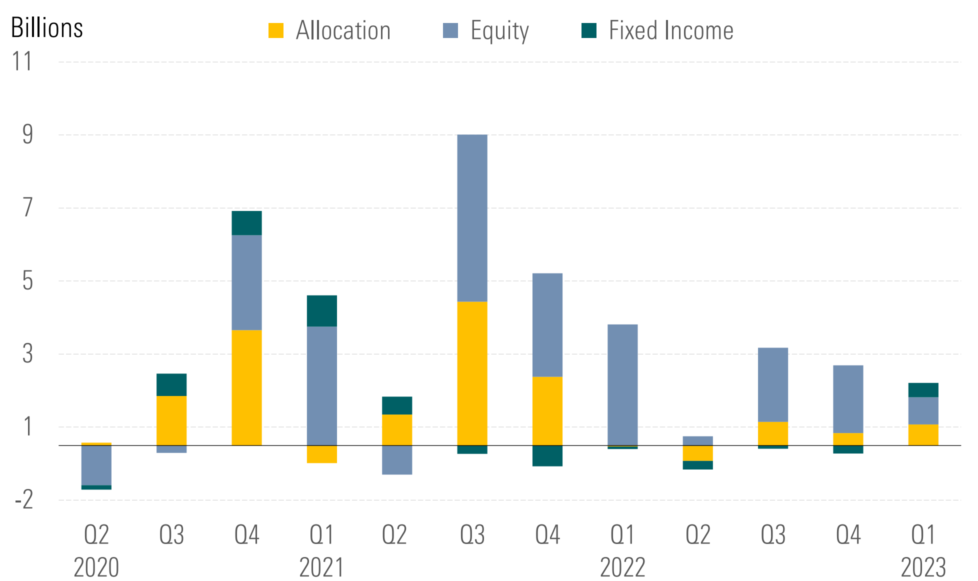
Excluding China, the Asia ex-Japan region recorded net outflows of roughly USD 97 million over the first quarter. South Korea experienced the highest outflows in the region at USD 545 million, its fourth-consecutive quarter of net withdrawals. Thematic equity funds investing in secondary batteries and electric car manufacturers drove the outflows, while fixed-income funds registered inflows. Meanwhile, Singapore and Hong Kong saw outflows of USD 157 million and USD 117 million, respectively, followed by India at USD 41 million. By contrast, Taiwan experienced the largest net inflows at USD 710 million, while Malaysia saw the second-most net inflows at USD 49 million.

Exhibit 29 Asia ex-Japan Sustainable Fund Flows (USD Billion)



Source: Morningstar Direct, Manager Research. Data as of March 2023.

Exhibit 30 Asia ex-Japan Sustainable Fund Flows by Asset Class (USD Billion)

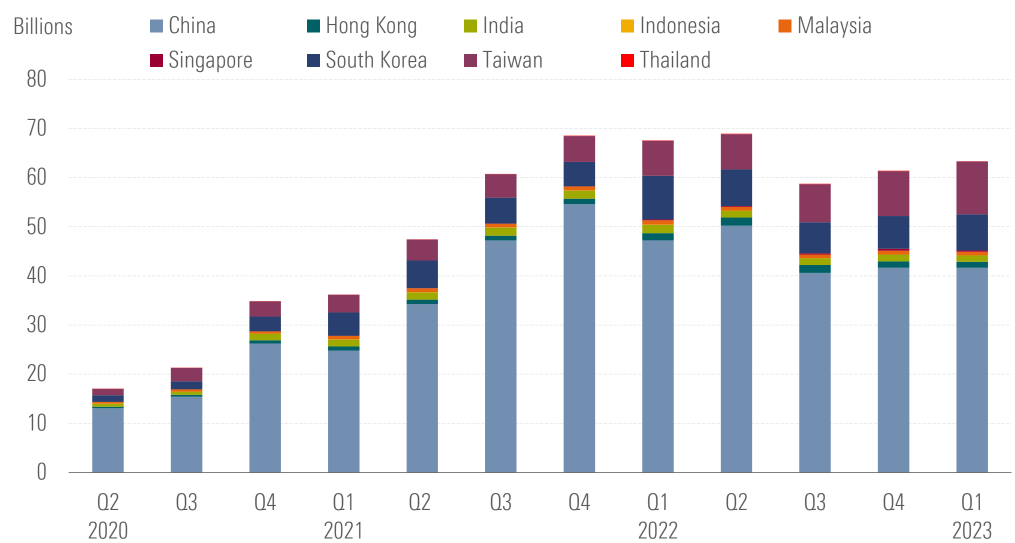


Source: Morningstar Direct, Manager Research. Data as of March 2023.

Assets

Total assets in sustainable funds across Asia ex-Japan experienced a quarter-over-quarter growth of 3.1% and reached USD 63 billion at the end of March 2023. Outside of China (for which data was not available at the time of publication), Taiwan and South Korea remained the two largest markets, accounting for 17% and 11.6% of the region's assets, respectively. Despite facing outflows, South Korea recorded a growth in sustainable fund assets during the first quarter of 2023 to USD 7.3 billion, owing to a rise in both equity and fixed-income markets.

Exhibit 31 Asia ex-Japan Sustainable Fund Assets (USD Billion)



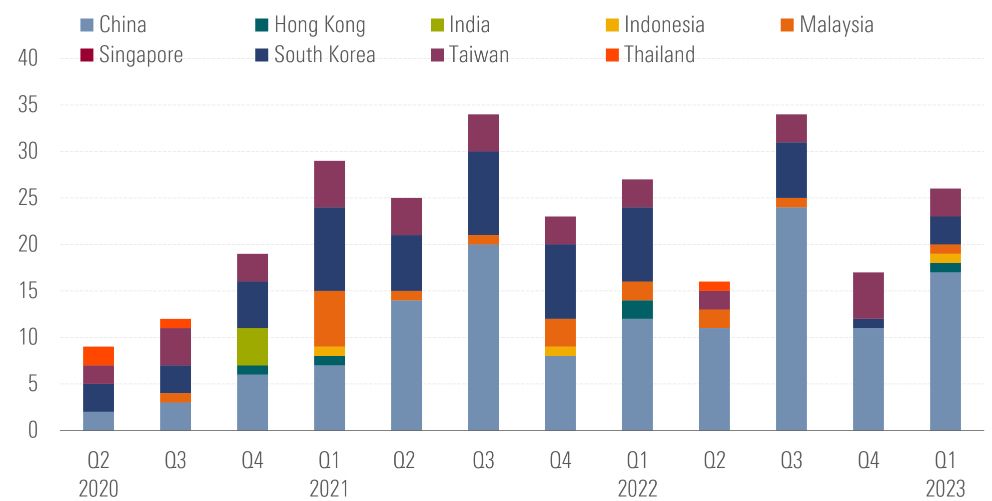
Source: Morningstar Direct, Manager Research. Data as of March 2023.

Following a quarter-over-quarter increase of 3.1% in assets, equities represented 70% of Asia ex-Japan sustainable fund assets at the end of March, while allocation and fixed-income funds comprised 25% and 5.4%, respectively. Passive funds accounted for 43.1%, a slight increase from 42.4% in fourth-quarter 2022.

Launches

In the first three months of the year, 26 new sustainable funds were launched across the region, 17 of which were from China. The remaining nine launches were from Taiwan (3), South Korea (3), Hong Kong (1), Malaysia (1), and Indonesia (1). Allocation and equity funds comprised the bulk of the new launches, accounting for 13 and 12, respectively, with just one sustainable fixed-income fund launched during the quarter, namely ChinaAMC Asia ESG Bond Fund, which aims to maximize income by investing in Asia debt issuers that meet the manager's ESG selection criteria. The largest sustainable funds launched with fund size data available at the time of publication was the Taiwan-domiciled Capital TIP Customized Taiwan ESG Low Carbon 50 ETF, which had assets of USD 158 million at the end of February and tracks an index of 50 Taiwan Stock Exchange-listed stocks filtered by liquidity, sustainability ratings, carbon intensity, financial strength, and market capitalization.

Exhibit 32 Asia ex-Japan Sustainable Fund Launches



Source: Morningstar Direct, Manager Research. Data as of March 2023.

Regulatory Update

The Asia ex-Japan regulatory landscape continued to evolve in first-quarter 2023. Thailand's Securities and Exchange Commission issued new voluntary guidelines for asset managers to help them assess, manage, and disclose climate-related risks in order to enhance transparency and mitigate potential greenwashing risks. Furthermore, Thailand's SEC issued regulations exempting the application fees for the establishment of Sustainable and Responsible Investing, or SRI, funds and the amendment fee for mutual fund schemes to be designated as an SRI fund. The new rules aim to better promote sustainable and responsible investment in the domestic market.

Malaysia's Securities Commission revised its guidelines for SRI funds to incorporate provisions for qualification as ASEAN SRI funds, requiring them to meet the standards issued by the ASEAN Capital Markets Forum. Neighbouring Singapore issued a third consultation on its taxonomy for green and transitioning.

Meanwhile, the Korea Financial Supervisory Service, or FSS, launched a taskforce to form the ESG Fund Disclosure Standards for Korea-domiciled sustainable funds, targeting the implementation of the standards within the first half of 2023. By referring to the trends in disclosure regulations in major foreign countries, the FSS plans to prepare disclosure standards such as investment objectives and strategies, relevance of ESG, investment capabilities, and performance evaluation.

Appendix—Defining the Global Sustainable Fund Universe

The global sustainable fund universe encompasses open-end funds and ETFs that, by prospectus or other regulatory filings, claim to focus on sustainability; impact; or environmental, social, and governance factors.

Our universe of sustainable funds is based on intentionality rather than holdings. For example, a portfolio can score well on ESG metrics such as the Morningstar Sustainability Rating, but if ESG issues are not the focus of the fund's investment strategy, it will not be included in our universe. To identify intentionality, we relied on a combination of fund names (a strong indicator of intentionality) and information found in fund documents. The fund's documents should contain enough details to leave no doubt that ESG concerns figure prominently in the security selection and portfolio construction process.

The global sustainable fund universe does not contain the growing number of funds often referred to as "ESG integrated funds," which formally consider ESG criteria in the investment process and engage with portfolio holdings but do not make ESG considerations the focus of the investment process.

Furthermore, the global sustainable fund universe doesn't include funds that employ limited exclusionary screens such as controversial weapons, tobacco, and thermal coal (combined with an ESG integration approach or not). We, however, include ESG-screened passive funds in our universe as, typically for these, the exclusions are the sole purpose of the strategy.

Finally, the global sustainable fund universe excludes money market funds, feeder funds, and funds of funds to avoid double-counting and inflating flows and assets. We make an exception for Japan and South Korea to better reflect the actual flow situation there as many Japanese funds of funds are invested in European funds.

To identify sustainable funds in their respective regions, manager research analysts use the "Sustainable Investment–Overall" data point in Morningstar Direct. We also use the "Sustainable Investment Overall Start Date" data point to account for repurposed funds, where relevant.

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