

Global Sustainable Fund Flows: Q4 2020 in Review

ESG Fund Assets Reach USD 1.65 Trillion Boosted by Record Inflows

Morningstar Manager Research

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Key Takeaways

- ▶ Driven by increased investor interest in environmental, social, and governance issues and sustainable investing, sustainable funds notched up a record-breaking quarter in terms of flows, assets, and product launches.
- ▶ Global inflows into sustainable funds were up 88% in the fourth quarter of 2020 to USD 152.3 billion.
- ▶ Continuing to dominate the space, Europe accounted for almost 80% of these inflows. The United States took in 13.4%, up slightly from 12% in the last quarter, while flows in the rest of the world also grew, clocking in at USD 11.1 billion for Canada, Australia and New Zealand, Japan, and Asia combined. This is up from USD 9 billion in the second quarter.
- ▶ Assets in sustainable funds hit a record high of USD 1,652 billion as of the end of December, up 29% from the previous quarter.
- ▶ Product development in the fourth quarter hit an all-time high, with 196 new offerings, including 37 in countries outside of Europe and the United States. Asset managers also continued to repurpose and rebrand conventional products into sustainable funds, with at least 250 such funds in Europe.

The Global Sustainable Fund Universe

The global sustainable fund universe encompasses open-end funds and exchange-traded funds globally that, by prospectus, factsheet, or other available resources, claim to have a sustainability objective and/or use binding ESG criteria for their investment selection. The sustainable funds group does not contain funds that employ only limited exclusionary screens such as controversial weapons, tobacco, and thermal coal, nor does it contain the growing number of funds that now formally integrate ESG considerations in a nondeterminative way for their investment selection. Money market funds, feeder funds, and funds of funds are excluded.

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 because of the relatively low assets. This report examines recent activity in the global sustainable fund universe and details regional flows, assets, and launches for the fourth quarter of 2020. A summary is provided in Exhibit 1.

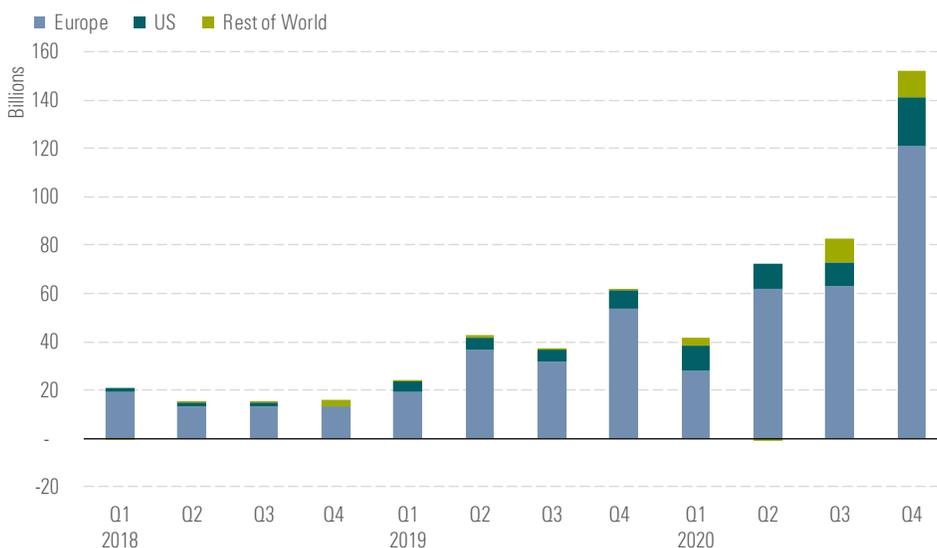
Exhibit 1 Global Sustainable Funds 4Q 2020 Statistics

Region	Q4 2020 Flows		Assets		Funds	
	USD billion	% Total	USD billion	% Total	#	% Total
Europe	120.8	79.3	1,342.8	81.3	3,196	77.0
United States	20.5	13.4	236.4	14.3	392	9.4
Asia ex-Japan	5.0	3.3	25.4	1.5	208	5.0
Australia/New Zealand	1.2	0.8	19.8	1.2	126	3.0
Japan	3.7	2.4	17.7	1.1	138	3.3
Canada	1.2	0.8	10.2	0.6	93	2.2
Total	152.3		1,652.3		4,153	

Source: Morningstar Direct, Morningstar Research. Data as of December 2020.

Global Flows

The global sustainable universe attracted USD 152.3 billion in net inflows in the fourth quarter of 2020, up 88% from USD 82.6 billion in the prior quarter. Europe took in the bulk of it (79.3%), while the U.S. accounted for close to 13.4% of it. Flows in the rest of the world were considerably higher than in previous quarters, clocking in at USD 11.1 billion for Canada, Australia and New Zealand, Japan, and Asia combined. This is compared with USD 9 billion in the previous quarter. This spike can be largely attributed to an uptick in flows in Japan.

Exhibit 2 - Quarterly Global Sustainable Fund Flows (USD Billion)

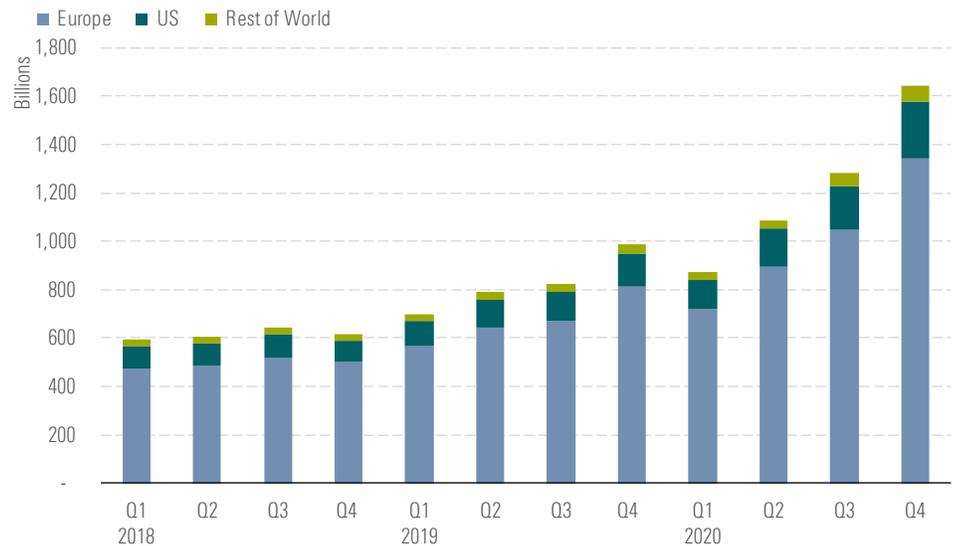
Source: Morningstar Direct, Manager Research. Data as of December 2020.

The strong inflows speak of the growing investor interest in ESG issues, especially in the wake of the coronavirus crisis. The disruption caused by the COVID-19 pandemic has highlighted the importance of building sustainable and resilient business models based on multistakeholder considerations. The average outperformance of sustainable funds in the first quarter globally has also helped alleviate some investors' concerns about a potential return trade-off in sustainable strategies.

Global Assets Climb 29% to USD 1.65 Trillion

Supported by record inflows, repurposed assets, and upward-trending markets, global sustainable fund assets climbed again in the fourth quarter of 2020 to USD 1,652 billion, from a revised USD 1,282 billion.

Exhibit 3 Quarterly Global Sustainable Fund Assets (USD Billion)



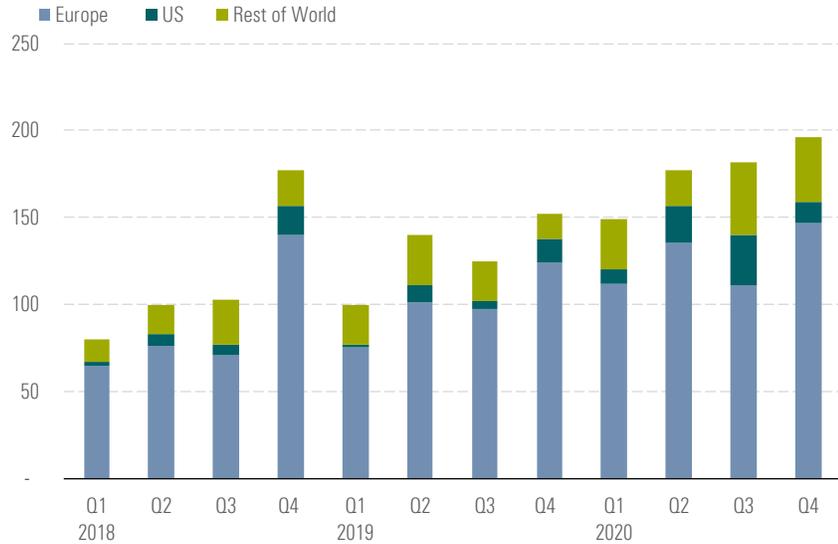
Source: Morningstar Direct, Manager Research. Data as of December 2020.

The past three years have seen a steady increase in assets in sustainable funds globally. Assets remain dominated by Europe, accounting for close to 80% of the global sustainable fund universe owing to its long history of responsible investing and favorable regulatory environment. With currently 3,196 sustainable funds available and many more that now formally consider ESG factors in a nonconstraining way to better manage risks and improve returns, Europe is by far the most developed and diverse ESG market.

Global Fund Launches

Product development continued in the fourth quarter of 2020 in all seven geographic regions detailed in this report. The 196 new fund launches in fourth-quarter 2020 broke the record of 182 set in the previous quarter, thanks to record-high product development activity in Europe, while the U.S. and the rest of the world overall experienced a bit of a slowdown, although the number of fund launches may increase in the coming weeks as more funds are reported to Morningstar.

Exhibit 4 Global Sustainable Fund Launches Per Quarter



Source: Morningstar Direct, Morningstar Research. Data as of December 2020.

The latest fund launches and conversions bring the total number of sustainable funds globally to 4,153 at the end of December 2020.

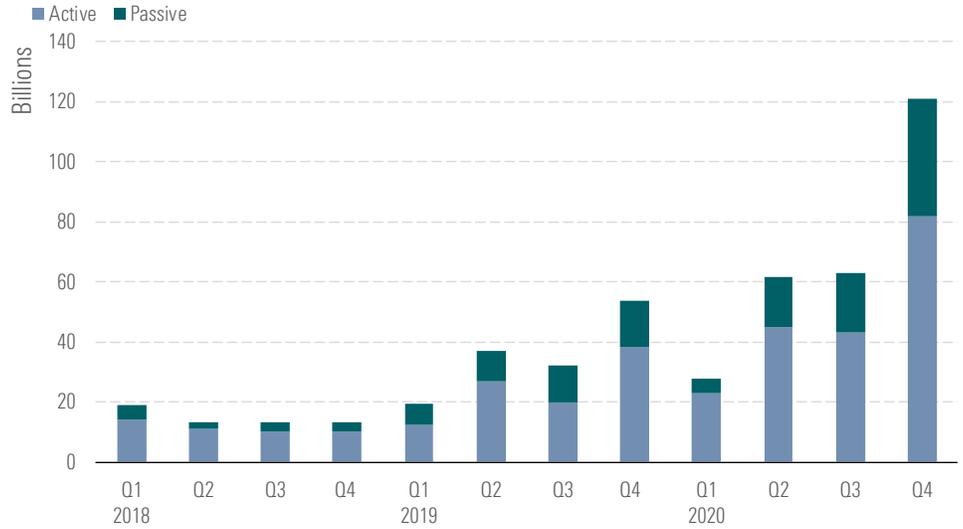
Quarterly Statistics Per Domicile

Europe

Flows

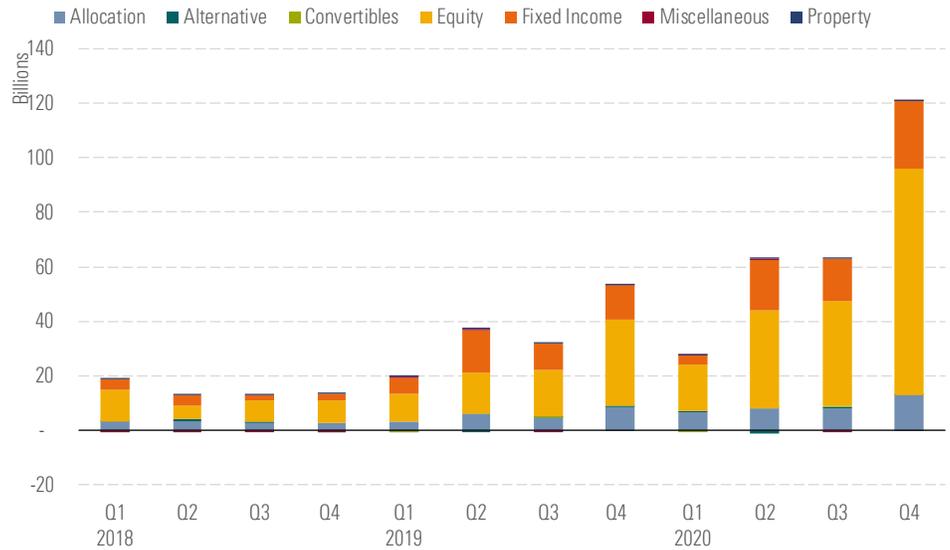
The year 2020 was pivotal for sustainable investing and ESG funds in Europe. After a decline in inflows during the COVID-19 market shock in the first quarter, sustainable fund flows recovered strongly to reach stratospheric heights in the fourth quarter, with just over of USD 120 billion in net new money. Flows were up 84% on the previous quarter, giving a strong finish to the year. The longer-term flow picture looks even more striking, with inflows into European sustainable funds almost 5 times higher in 2020 than they were three years ago and almost double last year's, at USD 273 billion.

Exhibit 5 European Sustainable Fund Flows (USD Billion)



Source: Morningstar Direct, Manager Research. Data as of December 2020.

Exhibit 6 European Sustainable Fund Flows by Asset Class



Source: Morningstar Direct, Morningstar Research. Data as of December 2020.

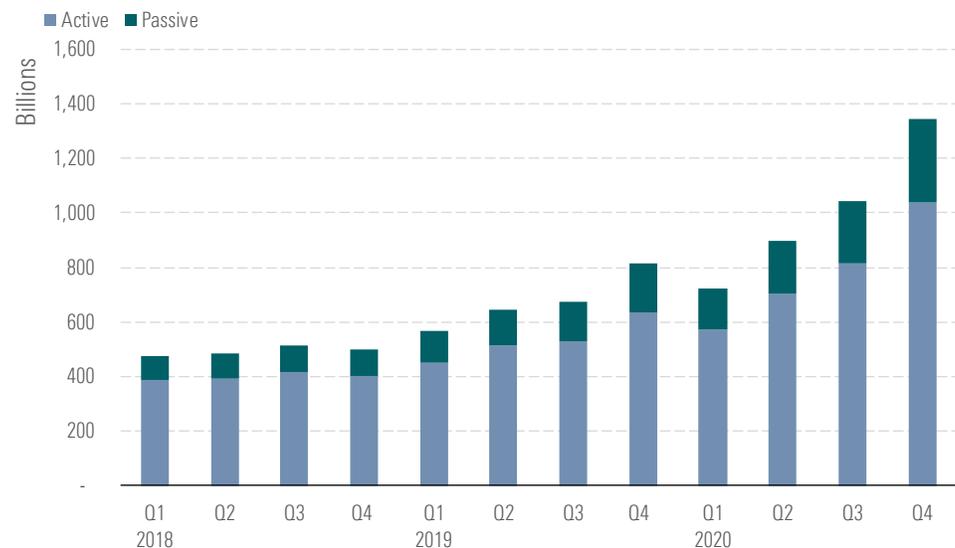
Equity remained the asset class of choice for ESG-oriented investors as they poured USD 82 billion into such funds, more than double that of the previous quarter.

Assets

Assets have been consistently high quarter over quarter, including in the first quarter 2020. To the surprise of many, sustainable funds proved remarkably resilient during the COVID-19 market sell-off. Assets dropped by only 10.6% in first-quarter 2020, while the overall European fund market took a greater hit of 16.2%. Assets in sustainable funds recovered in the second quarter to hit the USD 1 trillion-mark for the first time this year. The fourth quarter experienced the highest growth of 2020, amounting to over 23.2%.

Passive funds have seen their market share increase considerably over the years, now accounting for 22.5% of the European sustainable fund market, up from 18% three years ago.

Exhibit 7 European Sustainable Fund Assets (USD Billion)



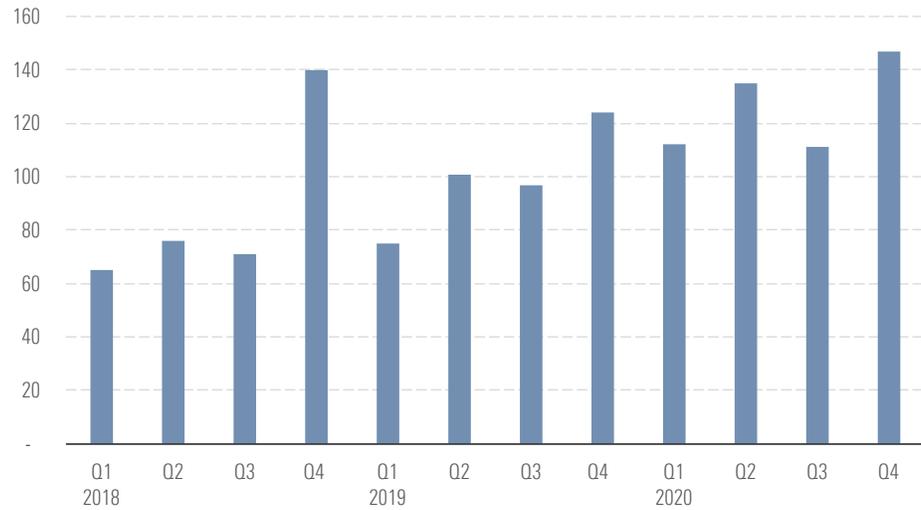
Source: Morningstar Direct, Morningstar Research. Data as of December 2020.

Launches

The fourth quarter was the most prolific quarter of all times in terms of product development. We have so far identified 147 new sustainable fund launches in Europe. This represents the funds currently on the Morningstar Direct database as of the third week of January 2021. This number may increase in the coming weeks as more funds are reported to Morningstar.

Passive products, however, saw a slowdown compared with the previous quarters. Only 15 ETFs and one index fund hit the shelf.

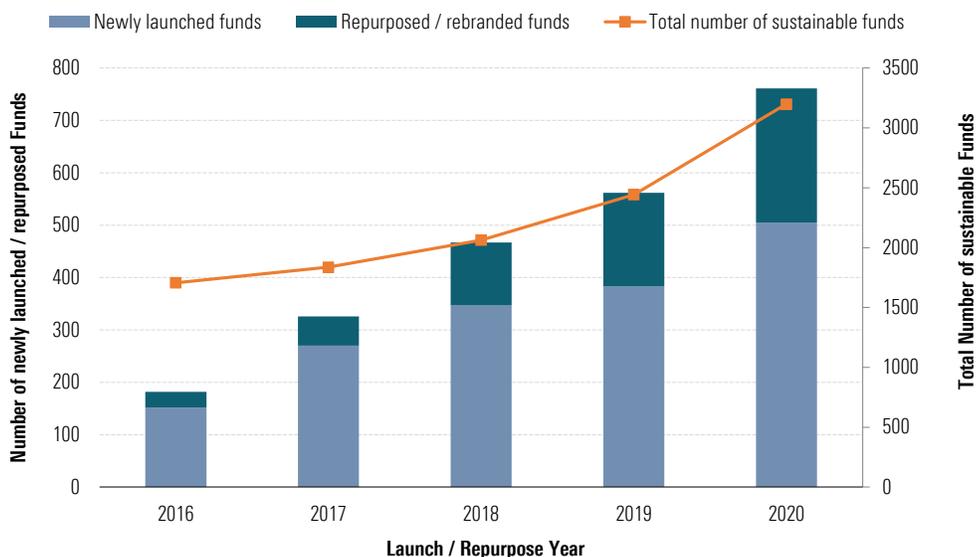
Exhibit 8.a European Sustainable Fund Launches



Source: Morningstar Direct, Morningstar Research. Data as of December 2020.

Transforming existing funds into sustainable strategies is a way for asset managers to leverage existing assets to build their sustainable-funds business, thereby avoiding having to create funds from scratch. This may also be a way for fund companies to reinvigorate ailing funds that are struggling to attract new flows. Others may choose to "green" their entire range of funds by, for example, expanding their exclusions policies and divesting from the biggest carbon emitters.

Consistent with record numbers of fund launches, repurposed funds hit new highs last year. We identified 253 such funds, 87% of which reflected the change by rebranding. Repurposed funds that rebrand add terms such as *sustainable*, *ESG*, *green*, or *SRI* to their names as a way to increase their visibility among investors who are looking to invest more sustainably.

Exhibit 8.b Newly Launched and Repurposed Funds in Europe

Source: Morningstar Research. Data as of December 2020.

The year 2020 was an important one in the European regulation of ESG investing and encouraging increasing flow of investment into sustainable activities in order to meet the EU goal of a net-zero economy by 2050. Perhaps the biggest—yet uncertain—piece of the EU Sustainable Finance Action Plan keeping asset managers busy last year was the Sustainable Finance Disclosure Regulations. Taking effect on 10 March 2021, the new rules require firms to provide information about the ESG risks in their portfolios and classify their products into one of three categories that will dictate additional disclosure requirements (Article 8 or 9 products).

For investors, the new rules will constitute welcome protections from being green-washed. Regulators developed the disclosures to require clearer articulation of funds' ESG objectives and for those objectives to be substantiated with metrics. Investors will get more data on how a fund is doing against its objective, together with guidance on how to compare that progress. They will also be told not only about the sustainability risks that pose a threat to their investments but also about any negative effects, or principal adverse impacts, those investments might have on sustainability—the so-called *double materiality*. This regulation is opening up a new era packed with possibilities for investors and will bring confidence to the sector.

United States

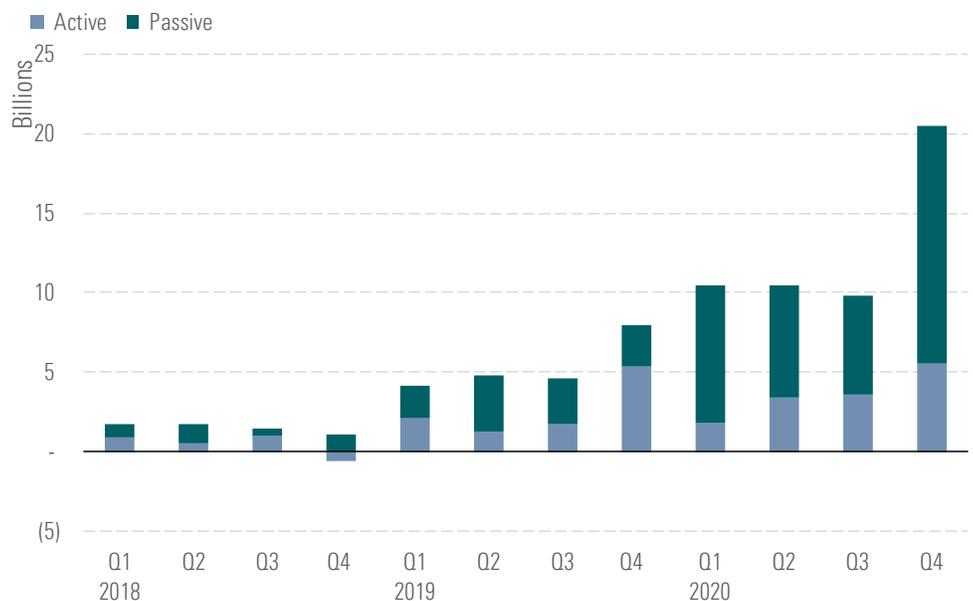
Flows

Sustainable funds in the United States attracted an all-time record level of flows in the fourth quarter. After averaging just more than USD 10 billion per quarter during the first three quarters of 2020, sustainable funds raked in USD 20.5 billion in the fourth quarter. That brings the total U.S. sustainable fund flows for 2020 to USD 51.2 billion, more than doubling the previous calendar-year record of USD 21.4 billion set in 2019. Prior to that, the record for a calendar year was only USD 5.5 billion, set in 2018.

Equity funds attracted about 90% of sustainable-fund flows in the fourth quarter and for the year overall. While fixed-income funds attracted far fewer ESG flows, they surpassed the USD 2 billion-mark in the third quarter for the first time and did so again in the fourth quarter.

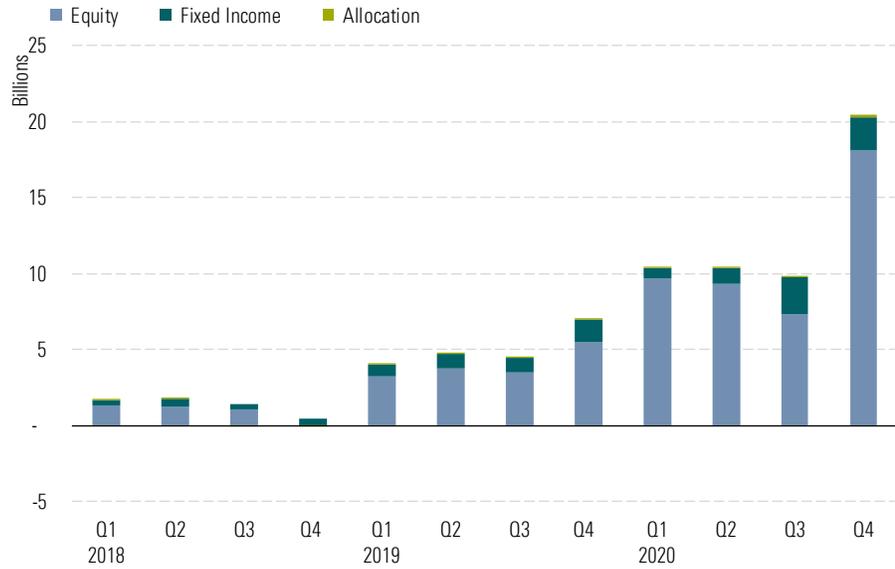
Passive funds easily outdrew active funds for the quarter and the year, garnering more than 70% of flows in each. The dominance of passive flows is more recent among sustainable funds than it is in the broader U.S. funds universe. In 2019, for example, the passive/active split was about 50/50 among sustainable funds. Since 2015, many more passive sustainable funds have launched, and, as they have built performance records, they have attracted more assets. Notably, too, BlackRock has aggressively built out its passive sustainable iShares ETF offerings, and these have captured a significant share of assets.

Exhibit 9 U.S. Sustainable Fund Flows (USD Billion)



Source: Morningstar Direct, Manager Research. Data as of December 2020.

Exhibit 10 U.S. Sustainable Fund Flows by Asset Class

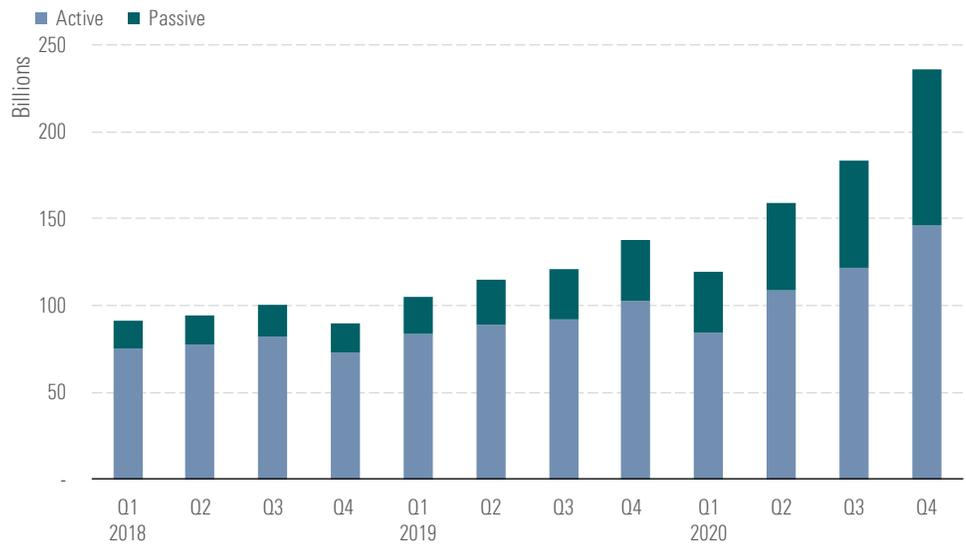


Source: Morningstar Direct, Morningstar Research. Data as of December 2020.

Assets

Assets in U.S. sustainable funds topped the USD 200 billion-mark for the first time, growing to USD 236 billion in the fourth quarter. That represents a 29% increase since the end of the third quarter and a 72% increase year over year. Most assets, 62%, still reside among active funds.

Exhibit 11 U.S. Sustainable Fund Assets (USD Billion)

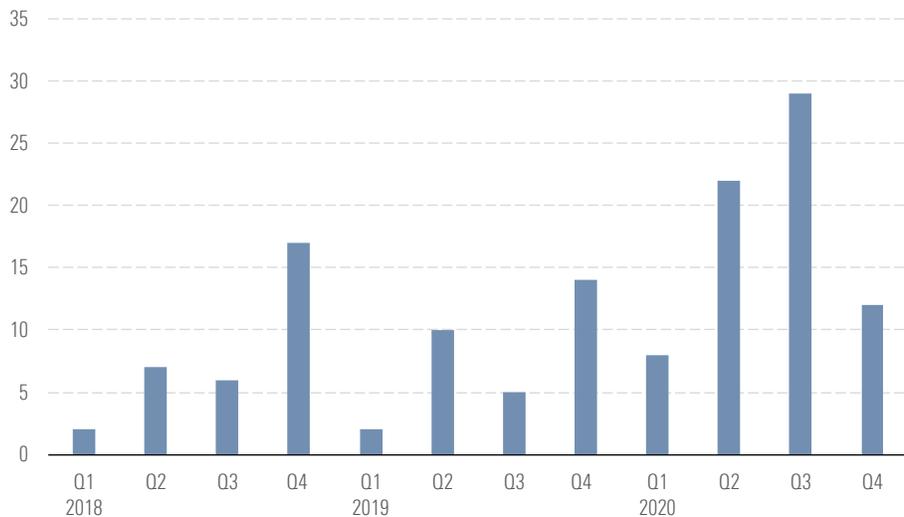


Source: Morningstar Direct, Morningstar Research. Data as of December 2020.

Launches

Last year, 71 new sustainable funds were launched in the U.S., a calendar-year record. Twelve of those launched during the fourth quarter. Ten are ETFs. Invesco added two actively managed ETFs, **Invesco US Large Cap Core ESG ETF** and **Invesco Real Assets ESG ETF**. Several offerings focus on the carbon transition: **GlobalX CleanTech ETF**, **JPMorgan Carbon Transition US Equity ETF**, and **SmartETFs Sustainable Energy II ETF**. Three of the new additions are fixed-income funds: **Pimco ESG Income**, **Pacific Funds ESG Core Bond**, and **SPDR Bloomberg SASB Corporate Bond ESG Select ETF**.

Exhibit 12 U.S. Sustainable Fund Launches



Source: Morningstar Direct, Morningstar Research. Data as of December 2020.

The U.S. sustainable funds universe is also growing as a result of repurposed funds. In 2020, 24 existing funds changed their investment strategies to become sustainable funds. In most cases, these funds also changed their names to reflect their new emphasis on sustainability. Twelve funds were repurposed in the fourth quarter, including four funds from Aberdeen and three WisdomTree ETFs. The largest fund repurposed in the fourth quarter was the USD 1.4 billion USAA Sustainable World, formerly USAA World Growth. The new offerings and the repurposed funds brought the total number of open-end and exchange-traded sustainable funds in the U.S. to 392 at the end of the quarter.

Canada

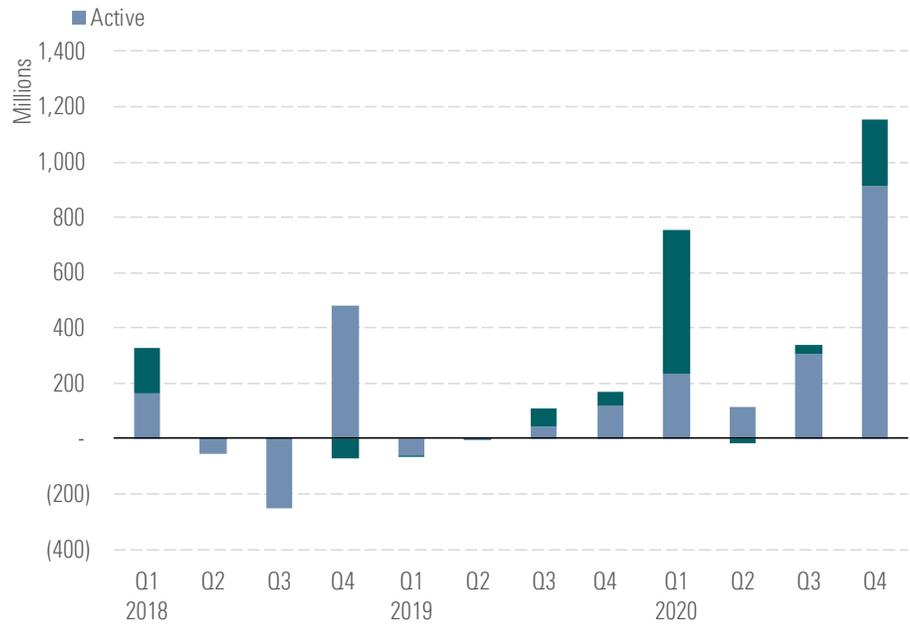
Although the pandemic and the U.S. presidential election stole much of the spotlight for Canadians in 2020, the growth and performance of the sustainable investing space in Canada also deserves an honourable mention. As the space continues to evolve, it is clear that the momentum in supply of products from manufacturers and demand from investors continues to build as evidenced through the rapid growth in assets and positive net inflows despite a turbulent year in financial markets, particularly

in Canada where the energy sector makes up a significant portion of gross domestic product and is well-represented in equity benchmarks.

Flows

Net asset flows for Canada-domiciled sustainable investments were positive in each month of the fourth quarter of 2020 with growing momentum. Total inflows amounted to a record USD 1.2 billion for the fourth quarter. Over the full calendar year, overall net flows were positive in all months inclusive of March during the crux of the pandemic sell-off.

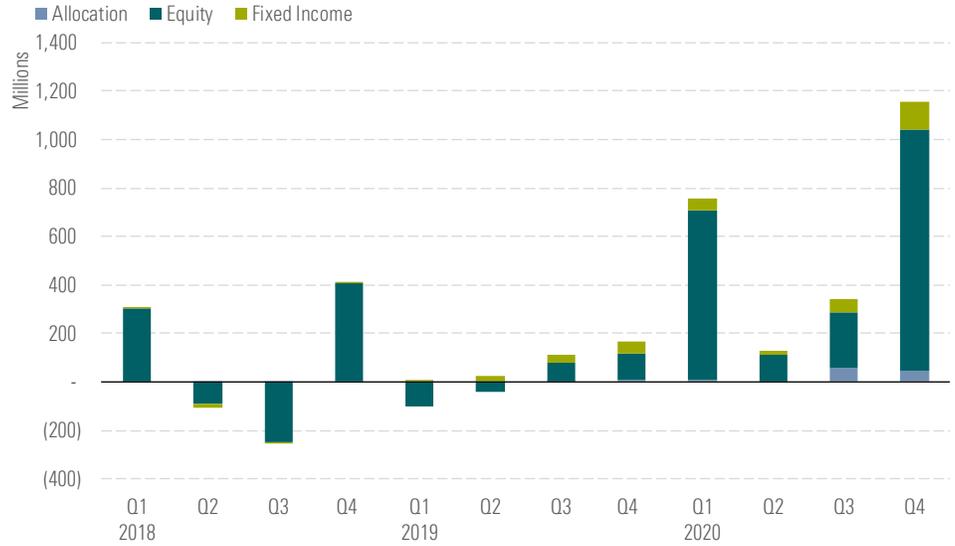
Exhibit 13 Canadian Sustainable Fund Flows (USD Million)



Source: Morningstar Direct, Manager Research. Data as of December 2020.

Consistent with previous quarter, equity funds attracted most of the new money into sustainable products in Canada in the fourth quarter of the year.

Exhibit 14 Canadian Sustainable Fund Flows by Asset Class

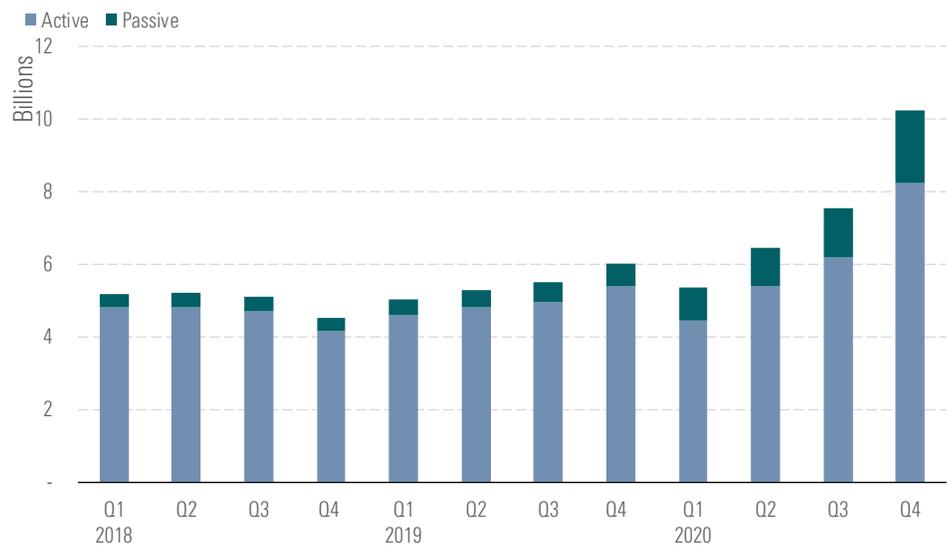


Source: Morningstar Direct, Morningstar Research. Data as of December 2020.

Assets

Retail sustainable assets continue to gain traction in Canada, though are still a small fraction of total retail assets. Excluding funds of funds, sustainable funds and ETF assets total USD 10.2 billion. This represents a year-over-year growth rate of 67%.

Exhibit 15 Canadian Sustainable Fund Assets (USD Billion)

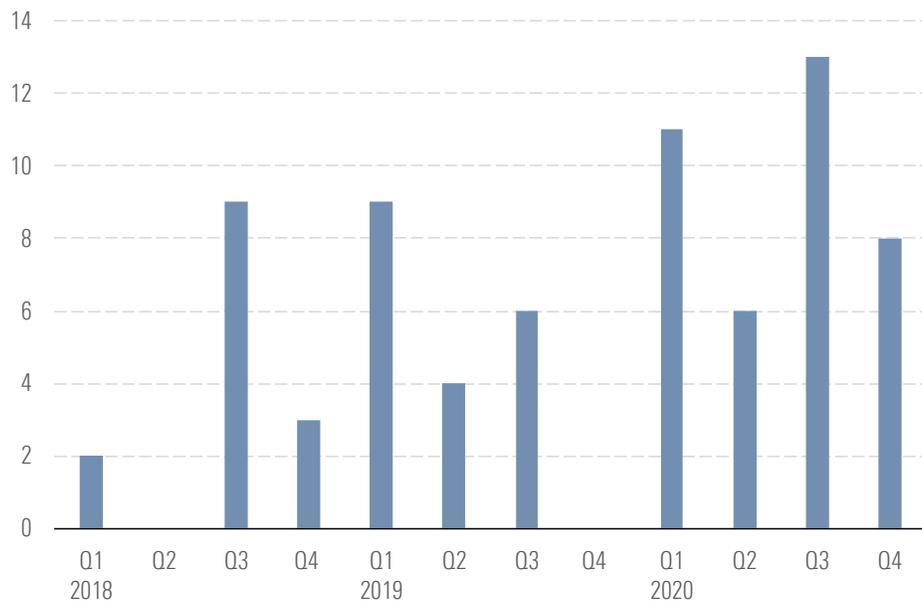


Source: Morningstar Direct, Morningstar Research. Data as of December 2020.

Launches

Eight new sustainable products were launched in the fourth quarter. In total, 41 new sustainable funds and ETFs were launched in 2020, more than doubling the number launched in the prior year. Total assets invested in sustainable funds launched in 2020 alone totaled USD 1.2 billion. Just over half of new products launched were indexed/passive investments.

Exhibit 16 Canadian Sustainable Fund Launches



Source: Morningstar Direct, Morningstar Research. Data as of December 2020.

Performance

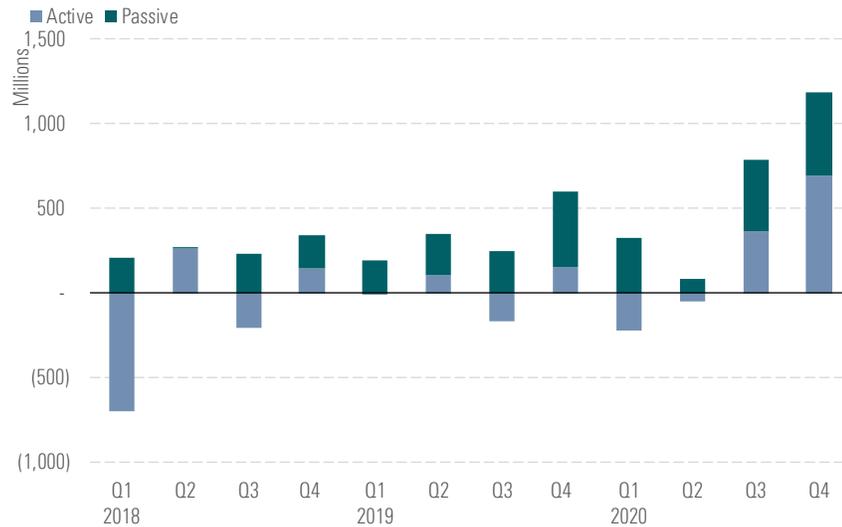
Over the calendar year, the majority (64 of 87) of funds that were ranked and rated by Morningstar outperformed their category peers on a risk-adjusted basis after fees. A look across all 2,407 Canada-domiciled funds that received a Morningstar Sustainability Rating (regardless of intentionality) showed that, over the 2020 calendar year, 60% of funds that received 5 globes outperformed their category benchmarks. On average, this group of funds outperformed their respective category benchmarks by 3.7%.

Australia and New Zealand

Flows

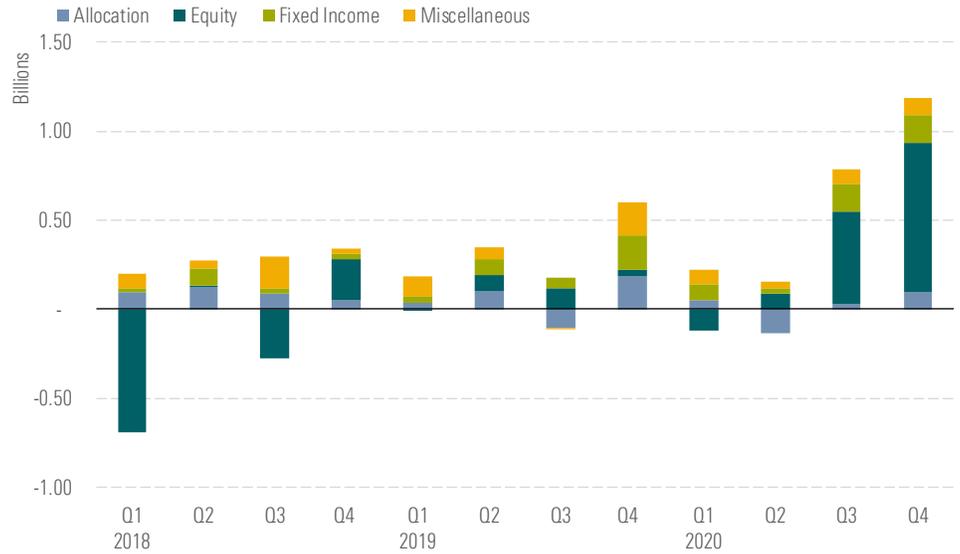
The Australasian (Australia and New Zealand) sustainable funds universe attracted record inflows of USD 1.187 billion in the fourth quarter of 2020. This is the first time Australia has experienced quarterly flows of over USD 1 billion. Fifty-eight percent of inflows went into active products (USD 689 million), with passive strategies (USD 498 million) receiving 42% of flows. Four fund houses dominated fund flows, with Vanguard (USD 218 million), BetaShares (USD 217 million), Australian Ethical (USD 192 million), and Dimensional (USD 167 million), accounting for the majority of inflows for the quarter. Corporate issues at AMP would likely explain the outflows of USD 23 million from the AMP Capital sustainable fund range, broadly bucking the overall inflow trend. Equity managers captured the bulk of inflows over the December quarter with USD 834 million. Active equity strategies accounted for USD 420 million of inflows, slightly ahead of the USD 414 million accumulated by passive strategies. This has reversed the recent trend of passive equity strategies dominating equity inflows.

Exhibit 17 Australian and New Zealand Sustainable Fund Flows (USD Million)



Source: Morningstar Direct, Manager Research. Data as of December 2020.

Exhibit 18 Australian and New Zealand Sustainable Fund Flows by Asset Class

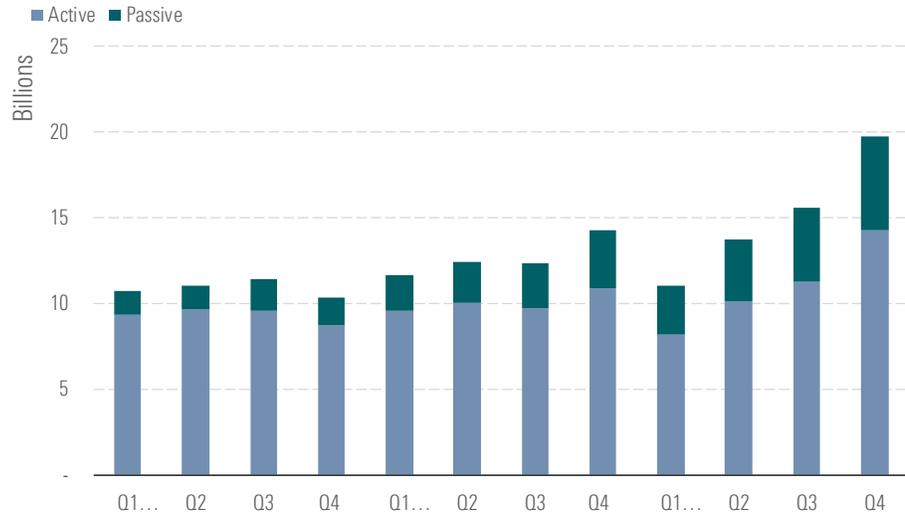


Source: Morningstar Direct, Morningstar Research. Data as of December 2020.

Assets

Assets in Australasian sustainable funds materially increased in fourth-quarter 2020, amounting to a record USD 19.7 billion, up from a revised USD 15.5 billion at the close of third-quarter 2020, a 27% increase. The Australian sustainable funds market remains quite concentrated, with the top 15 funds accounting for 52% of total assets in the sustainable fund universe. Australian Ethical remains the dominant Australasian provider of sustainable funds, with total assets of USD 3.9 billion on the Morningstar database. With more intensive data collection, we now count 126 strategies in our Australasian sustainable fund universe.

Exhibit 19 Australian and New Zealand Sustainable Fund Assets (USD Billion)

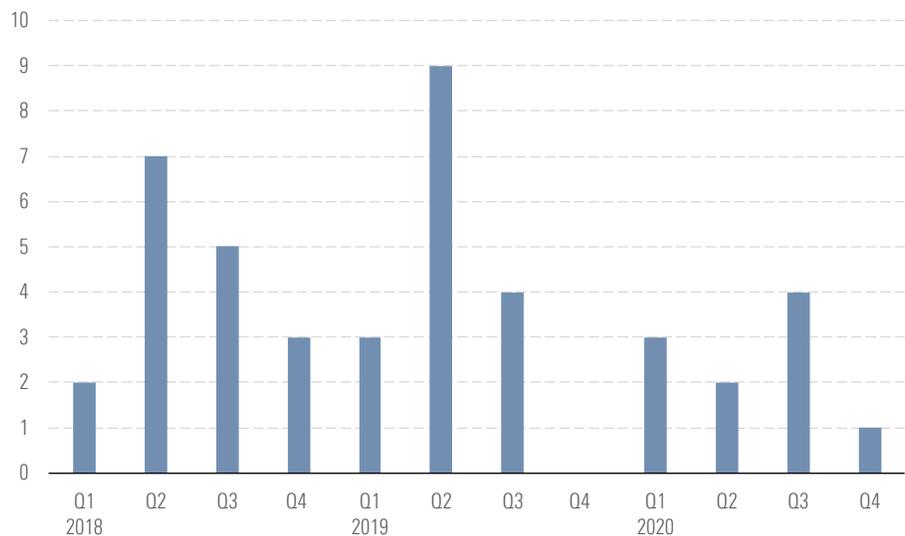


Source: Morningstar Direct, Morningstar Research. Data as of December 2020.

Launches

Only one new sustainable fund was launched (Regnan Global Equity Impact Solutions) in Australasia in fourth-quarter 2020. This is a positive development, given the lack of Impact investment option in the Australasian market. The sustainable funds universe does not contain the growing number of Australasian funds that now formally consider ESG factors in a nondeterminative way in their security selection.

Exhibit 20 Australian and New Zealand Sustainable Fund Launches



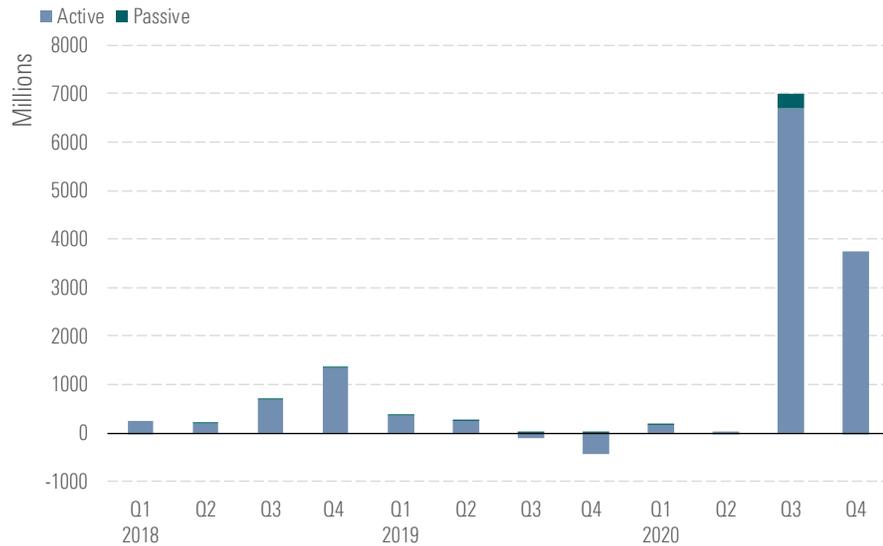
Source: Morningstar Direct, Morningstar Research. Data as of December 2020.

Japan

Flows

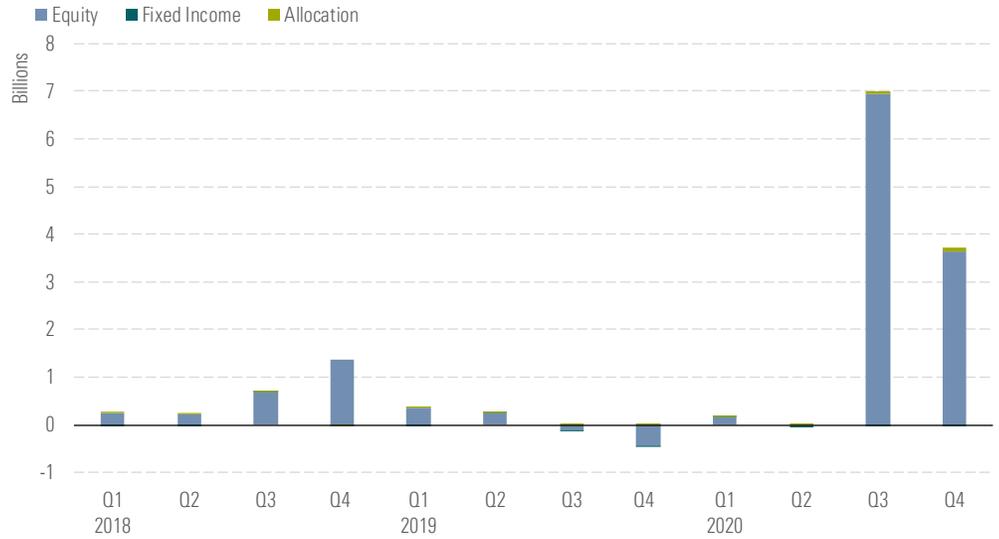
The Japanese sustainable fund market recorded inflows of USD 3.7 billion in the fourth quarter of 2020. Actively managed equity funds were the main drivers of inflows. Asset-class-wise, 98% of inflows came from equity funds whereas fixed-income funds recorded outflows, although in relatively small amounts. All top 10 inflows funds for ESG in the quarter were active equity funds, where six out of 10 funds were launched in either the third or fourth quarter of 2020. Launched in July 2020, the actively managed **AMOne Global ESG High Quality Growth Equity Fund** continued to attract new money, with USD 2 billion of inflows for fourth-quarter 2020. The fund registered the biggest inflows among all Japan-domiciled funds in 2020, reflecting the increased interest of Japanese investors in ESG investing. Although the issue of double-counting cannot be eliminated, 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 21 Japanese Sustainable Fund Flows (USD Million)



Source: Morningstar Direct, Manager Research. Data as of December 2020.

Exhibit 22 Japanese Sustainable Fund Flows by Asset Class



Source: Morningstar Direct, Morningstar Research. Data as of December 2020.

Assets

Assets in sustainable funds increased over 40% to USD 17.7 billion as of December 2020 compared with the previous quarter-end. Ninety-eight percent of sustainable funds consisted of equity funds and 97% are active funds, respectively. Inflows to newly launched sustainable active equity funds in the third- and fourth-quarter 2020 drove the increase in assets, together with the bullish equity market environment over the period.

Exhibit 23 Japanese Sustainable Fund Assets (USD Billion)

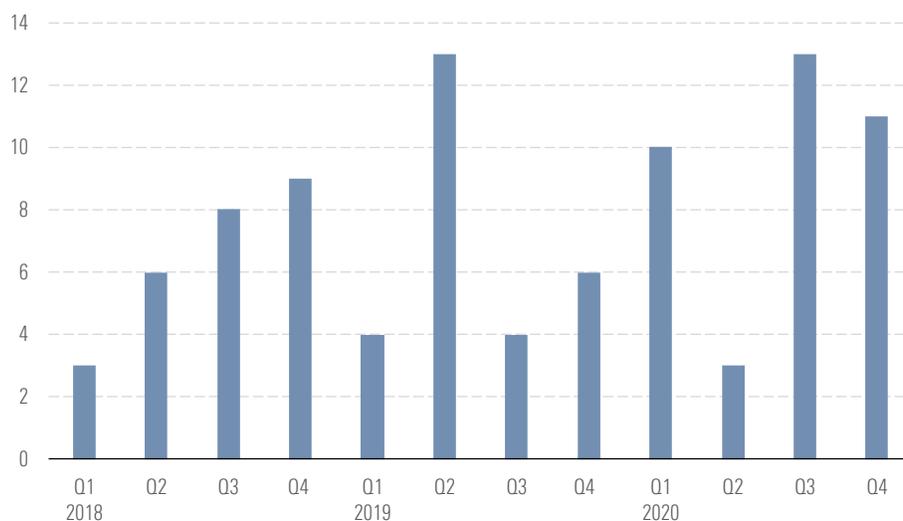


Source: Morningstar Direct, Morningstar Research. Data as of December 2020.

Launches

Eleven new sustainable funds came to the Japanese market in fourth-quarter 2020, eight of which are active funds, while three are index funds. Flows into these newly launched funds were USD 922 million in total, contributing to the overall inflows. Two Nomura Environment Leaders Strategy Funds, launched in October 2020, both of which are actively managed equity funds managed by Nomura Asset Management and distributed by Nomura Securities, gathered USD 860 million in total, which contributed mostly to the inflows of newly launched funds.

Exhibit 24 Japanese Sustainable Fund Launches



Source: Morningstar Direct, Morningstar Research. Data as of December 2020.

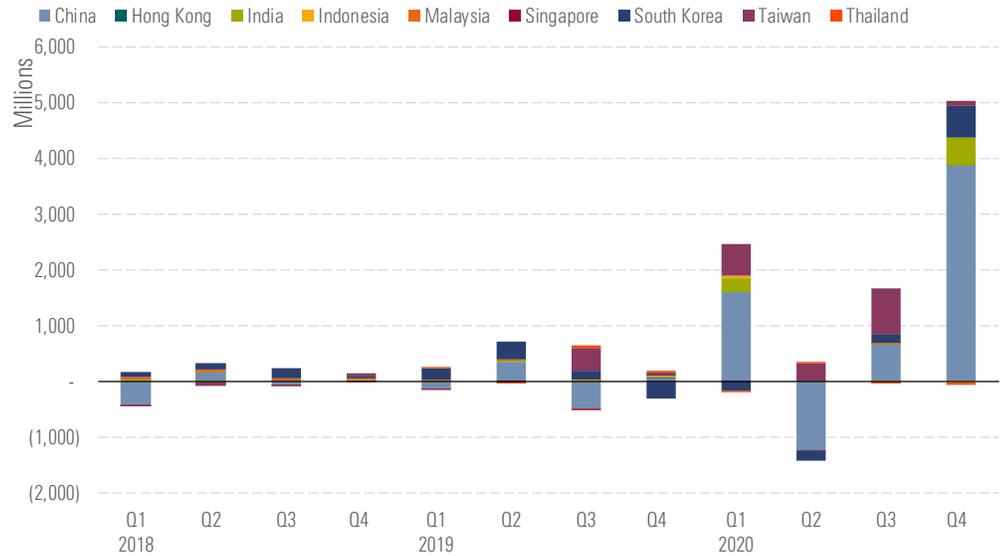
Asia ex-Japan

Flows

China, South Korea, and India had strong positive ESG flows for the fourth quarter of 2020, propelled by new launches. While China's fourth-quarter data captured only 60% of ESG funds at the time of publication, investors' interest in the electric-vehicle theme drove China's fourth-quarter ESG flows to a record USD 3.8 billion.

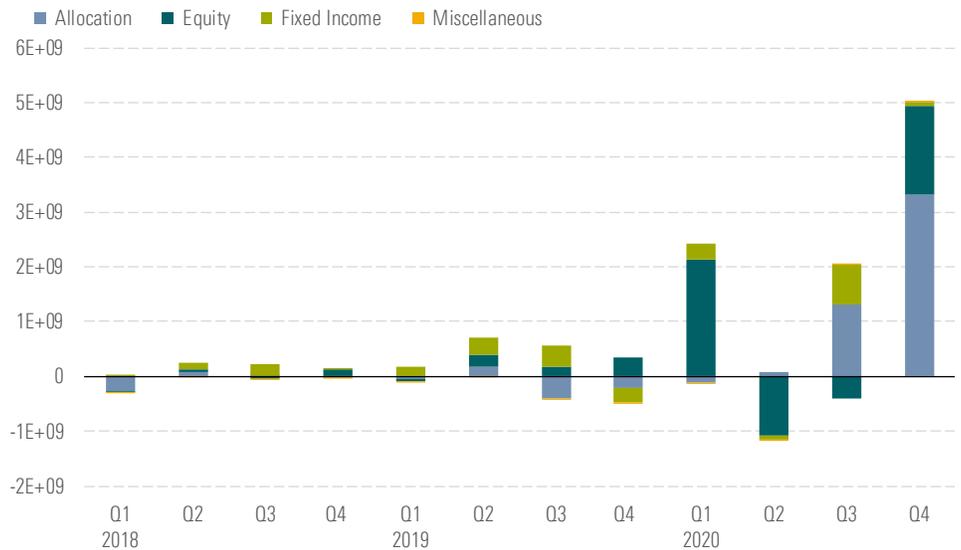
Despite not capturing the full data from China for the fourth quarter, Asia ex-Japan saw net inflows of USD 7.9 billion in 2020 compared with USD 810 million in 2019. Allocation funds raised USD 4.6 billion in net flows in 2020, followed by equity with USD 2.3 billion and fixed income with USD 1.0 billion.

Exhibit 25 Asia ex-Japan Sustainable Fund Flows (USD Million)



Source: Morningstar Direct, Manager Research. Data as of December 2020.

Exhibit 26 Asia ex-Japan Sustainable Fund Flows by Asset Class



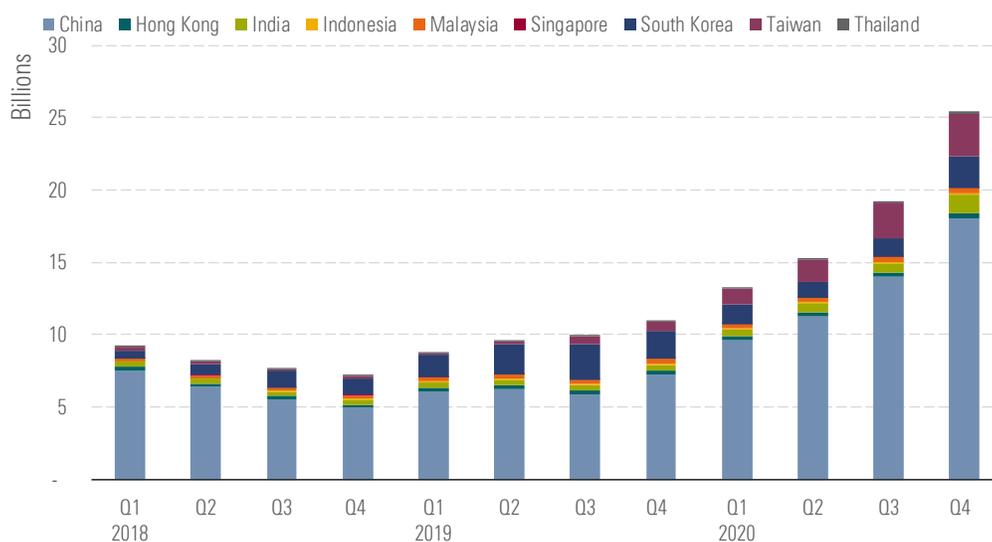
Source: Morningstar Direct, Morningstar Research. Data as of December 2020.

Assets

India had the largest quarter-on-quarter asset growth as new launches resulted in the doubling of ESG fund assets to USD 1.3 billion. South Korea also saw significant growth in the fourth quarter, while Taiwan’s steady growth maintained it as Asia ex-Japan’s second-largest ESG market after China.

ESG assets in Asia ex-Japan reached the USD 25 billion-mark in 2020, growing by 130% compared with 2019. Allocation funds registered a 215% growth, while fixed-income offerings grew by 120%. However, equity remained the largest asset class represented, with USD 13.2 billion in assets, recording a strong growth of 94% in 2020 over 2019.

Exhibit 27 Asia ex-Japan Sustainable Fund Assets (USD Billion)



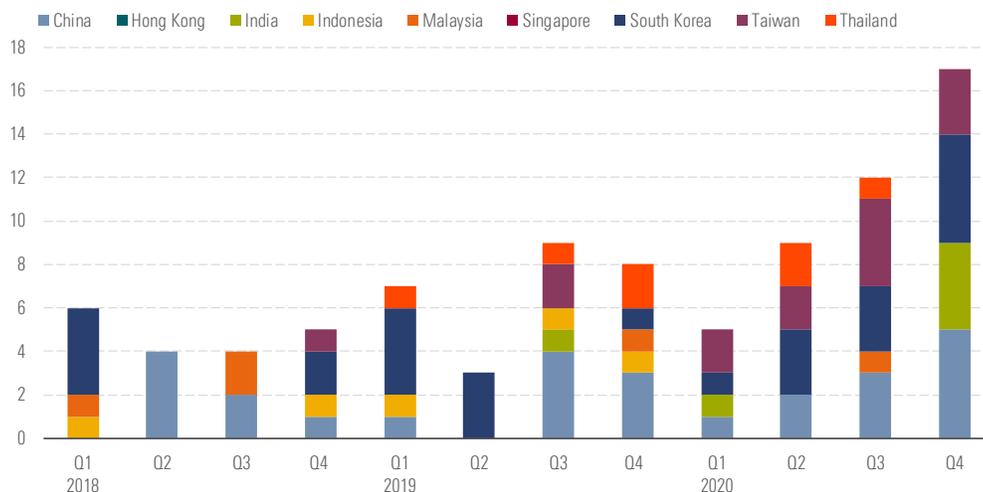
Source: Morningstar Direct, Morningstar Research. Data as of December 2020.

Launches

Product development activity reached new highs in the fourth quarter of 2020, with 17 new ESG fund launches from China, South Korea, India, and Taiwan. A majority of the new launches in China and India were equity funds, while South Korea's and Taiwan's new launches were allocation and fixed-income products. Building on its success with the launch of the **Global ESG Quant Bond fund** in January 2020, Pinebridge launched the **ESG Quant Multi-Asset fund**, which garnered the largest assets (USD 311 million) among new ESG fund launches in Taiwan over the fourth quarter. **ICICI Prudential ESG fund** raised USD 225 million in assets, making it the most successful new ESG launch in India.

New launches in Asia ex-Japan continued to remain robust, with 43 funds in 2020 compared with 27 in the prior year. New fund launches in Taiwan jumped from two in 2019 to 11 in 2020, which generated USD 1.7 billion in new inflows. India's five new fund launches in 2020 managed to attract USD 716 million in new inflows. At the time of publication, we are unable to provide comprehensive analysis on new launches from China for 2020.

Exhibit 28 Asia ex-Japan Sustainable Fund Launches



Source: Morningstar Direct, Morningstar Research. Data as of December 2020.

Interest in ESG investment has been widely spread in the Korean market. There were several ESG seminars held as well as new products launched. Equity funds are still dominant in the Korean ESG fund market, but bond funds continued to be launched as institutional investors' interest increased. In the fourth quarter, five new products hit the shelves, four of which provide exposure to bonds, bringing the total number of ESG bond funds in Korea to seven.

After three quarters of outflows, **KBSTAR ESG SRI (Equity ETF)** registered the largest inflows in Korea in the fourth quarter. **Woori HiPls ST Fdr Supr ESG Bd 1 Ce** experienced a similar turn of fortune after it changed its name and converted to an ESG investment in September 2020. The growing number of repurposed and rebranded ESG funds in Korea has led the Korean Financial Supervisory Service to toughen its approval policy for name changes. Asset managers have to prove that they have been managing their portfolios according to ESG principles for a certain period of time. **IM**

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