
How Does European Sustainable Funds' Performance Measure Up?

Morningstar Manager Research

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Executive Summary

In this report, we measure the performance of sustainable open-end and exchange-traded funds versus traditional peers in seven popular Morningstar Categories. This report spans nearly 4,900 funds domiciled in Europe, including 745 sustainable open-end and exchange-traded funds.

We compare average returns among the sustainable and traditional fund cohorts over the past one, three, five, and 10 years through December 2019, as well as during the coronavirus crisis (in the first quarter of 2020). We evaluate sustainable funds against a composite of traditional funds in each category and measure the odds of picking a winner. We also assess the impact of fees on the ability of sustainable funds to deliver outperformance.

Key Takeaways

- ▶ Average returns and success rates for sustainable funds across seven Morningstar Categories suggest that there is no performance trade-off associated with sustainable funds. In fact, a majority of sustainable funds have outperformed their traditional peers over multiple time horizons.
- ▶ Over the 10 years through 2019, nearly 59% of surviving sustainable funds across the categories considered have beaten their average surviving traditional counterpart.
- ▶ More sustainable funds have survived in the past 10 years, in relative terms. Of sustainable funds available to investors 10 years ago, 72% have survived, compared with less than half (45.9%) of traditional funds.
- ▶ Sustainable funds held up better than their traditional counterparts during the COVID-19 sell-off, delivering superior returns in all but one category.
- ▶ Fees are a crucial consideration when selecting a sustainable fund. Lower-cost options tend to have greater odds of success.

Introduction

Despite the increased popularity of sustainable funds as measured by flows, assets, and new launches,¹ concerns about a potential performance trade-off persist. A growing body of research shows that sustainable investing has a positive effect on investment performance, but other research also shows that there isn't a clear link between firms' environmental, social, and governance attributes and performance. Morningstar has also recently published its own work on the performance of ESG stocks, ESG indexes and U.S. ESG funds^{2, 3, 4, 5}.

This study examines the performance of sustainable funds in seven European Morningstar Categories over the past one, three, five, and 10 years through December 2019, as well as during the coronavirus crisis (in the first quarter of 2020). The selected categories were determined based on the availability of sustainable funds with 10-year returns. The seven categories considered also happen to be the largest in terms of assets in and number of sustainable funds.

We define sustainable funds as funds that use environmental, social, and governance criteria as a key part of their security selection and portfolio-construction process, and/or indicate that they pursue a sustainability-related theme, and/or seek a measurable positive impact alongside financial return. The sustainable funds group does not contain funds that employ only limited exclusionary screens without a broader emphasis on ESG, nor does it contain the growing number of funds that now formally integrate ESG factors in a nondeterminative way in their security selection.

This study is built upon the same methodology as the Morningstar Active/Passive Barometer.⁶ We compare average returns, success rates, and survivorship rates for sustainable funds versus traditional funds in each category. To calculate success rates, we use a composite of traditional fund returns and count the number of sustainable fund returns that rank higher than this composite. In all our calculations, we account for repurposed sustainable funds.⁷

¹ [European Sustainable Funds Prove Resilient Amid COVID-19 Sell-Off in Q1. European Sustainable Funds Landscape.](#)

² [How Does Investing in ESG Companies Affect Returns?](#)

³ [How Did ESG Indexes Fare During the First Quarter Sell-off?](#)

⁴ [U.S. ESG Funds Outperformed Conventional Funds in 2019](#)

⁵ [Sustainable Funds Weather the First Quarter Better Than Conventional Funds](#)

⁶ [Morningstar European Active/Passive Barometer](#)

⁷ Survivorship bias. We account for funds that were available for purchase at the beginning of the surveyed periods and subsequently closed. Repurposed funds are traditional funds that changed investment objectives during the surveyed periods to make ESG their primary focus. We account for these funds from the date they repurposed. For more detail: [Surge in Funds Rebranding as Sustainable](#)

Positive Success Rates Over Multiple Time Periods

A majority of surviving sustainable funds outperformed their average surviving traditional peer over the past 10 years (Exhibit 1). The above-50% success rates for surviving sustainable funds in most categories over multiple time periods indicate that investors taking the ESG route were less likely to miss out on returns than if they had invested in traditional funds.

Over the 10-year period through 2019, 58.8% of surviving sustainable funds across the seven categories considered have beaten their average surviving traditional peer.

Exhibit 1 Sustainable Funds' Success Rates by Morningstar Category (%)

Category	Success Rate of Sustainable Funds			
	1-Year	3-Year	5-Year	10-Year
Global Large-Cap Blend Equity	75.1	73.7	76.9	67.3
Global Large-Cap Growth Equity	60.3	43.2	37.5	56.7
Global Emerging Markets Equity	41.3	60.0	58.8	50.0
US Large-Cap Blend Equity	76.4	71.4	76.9	81.3
Europe Large-Cap Blend Equity	71.1	75.0	67.2	55.1
Eurozone Large-Cap Equity	63.5	63.0	60.6	62.3
EUR Corporate Bond	58.0	58.5	62.2	33.3
All Categories	65.6	65.6	64.4	58.8

Source: Morningstar Direct. Morningstar Research. Data as of 31/12/2019.

The odds of picking a winning sustainable fund over the past 10 years were greatest in the U.S. large-blend category. More than seven out of 10 live sustainable U.S. large-cap equity funds delivered higher returns than their average surviving conventional counterpart.

But the same can't be said about global large-cap growth investors who would have seen their odds of success fluctuate significantly over time. Not even four sustainable global large-cap growth funds out of 10 that were selected five years ago, and are still available today, beat the average surviving traditional peer.

Higher Survivorship Rates

Sustainable funds have consistently exhibited higher survivorship rates than traditional funds over the past 10 years (Exhibit 2). This means that fewer sustainable funds have closed, in relative terms.

Of sustainable funds available to investors 10 years ago, 72% have survived, compared with less than half (45.9%) of traditional funds.

Exhibit 2 Survivorship Rates' Comparison Between Sustainable and Traditional Funds by Morningstar Category

Category	1-Year				3-Year			
	Sustainable Funds		Traditional Funds		Sustainable Funds		Traditional Funds	
	Number	Survivorship Rate (%)	Number	Survivorship Rate (%)	Number	Survivorship Rate (%)	Number	Survivorship Rate (%)
Global Large-Cap Blend Equity	199	99.0	1,377	95.3	140	82.1	1,327	81.2
Global Large-Cap Growth Equity	63	98.4	305	95.4	90	97.8	267	89.1
Global Emerging Markets Equity	66	95.5	568	93.0	100	95.0	562	83.8
US Large-Cap Blend Equity	56	98.2	489	91.4	76	96.1	470	80.2
Europe Large-Cap Blend Equity	102	95.1	633	92.4	151	94.0	625	82.1
Eurozone Large-Cap Equity	86	98.8	449	95.8	150	98.7	448	86.6
EUR Corporate Bond	69	100.0	340	94.7	112	97.3	344	83.4
All Categories		98.0		94.1		94.0		82.9

Category	5-Year				10-Year			
	Sustainable Funds		Traditional Funds		Sustainable Funds		Traditional Funds	
	Number	Survivorship Rate (%)	Number	Survivorship Rate (%)	Number	Survivorship Rate (%)	Number	Survivorship Rate (%)
Global Large-Cap Blend Equity	117	76.1	1,265	70.0	92	52.2	1,376	45.9
Global Large-Cap Growth Equity	42	90.5	243	81.1	37	75.7	224	47.8
Global Emerging Markets Equity	39	87.2	571	71.5	16	87.5	296	48.0
US Large-Cap Blend Equity	27	92.6	443	69.5	19	84.2	527	46.9
Europe Large-Cap Blend Equity	67	83.6	596	72.3	70	70.0	744	46.2
Eurozone Large-Cap Equity	68	97.1	477	75.1	58	91.4	616	42.9
EUR Corporate Bond	48	91.7	349	74.8	30	80.0	259	47.1
All Categories		86.3		72.2		72.0		45.9

Source: Morningstar Direct, Morningstar Research. Data as of 31/12/2019.

Attrition rates were the highest in the global large-cap blend category, which also happens to be the largest category in terms of number of funds. Just 52.2% of sustainable global large-cap blend funds survived to the end of the 10-year period ended Dec. 31, 2019. It is still better than the 45.9% odds of survival for traditional funds.

Sustainable Investing Does Not Cost the Earth, but Fees Are a Crucial Consideration

While the majority of sustainable funds across the seven categories considered here have beaten their average traditional peer over the past 10 years, success rates have varied depending on fees. As shown in Exhibit 3, selecting a fund in the lowest-fee quartile five years ago would have improved the odds of picking a winner in all but one category. Global large-cap growth was the only category where fees didn't give much of an advantage. Only 33% of the cheapest sustainable funds beat the cheapest traditional funds in that category.

Exhibit 3 Success Rates of Sustainable Funds vs. Traditional Funds (%)

Category	1-Year	3-Year	5-Year	10-Year	5-Year Lowest-Fee Quartile		5-Year Highest-Fee Quartile	
	Success Rate (%)	Success Rate (%)	Success Rate (%)	Success Rate (%)	# at beginning of the	Success Rate (%)	# at beginning of the	Success Rate (%)
Global Large-Cap Blend Equity	75.1	73.7	76.9	67.3	17	88	31	65
Global Large-Cap Growth Equity	60.3	43.2	37.5	56.7	9	33	14	36
Global Emerging Markets Equity	41.3	60.0	58.8	50.0	7	71	13	54
US Large-Cap Blend Equity	76.4	71.4	76.9	81.3	5	100	9	56
Europe Large-Cap Blend Equity	71.1	75.0	67.2	55.1	12	92	17	35
Eurozone Large-Cap Equity	63.5	63.0	60.6	62.3	16	88	21	38
EUR Corporate Bond	58.0	58.5	62.2	33.3	10	70	14	29

Source: Morningstar Research. Data as of 31/12/2019.

These findings can be very valuable for performance-conscious investors looking to invest more sustainably. They can maximize their chances of success by limiting their choice to lower-cost funds. Like with any other type of investment, fees are a crucial consideration when selecting a sustainable fund.

Active Funds Dominates

To understand the success rates better and the makeup of the sustainable fund cohort, we look at the active/passive funds ratio in each Morningstar Category. As shown in Exhibit 4, active management dominates the sustainable funds' space, as it does the traditional funds' space. However, in most categories, the proportion of active sustainable funds has declined more over the past 10 years as passive funds have gained in popularity and more ESG ETFs and index funds have been launched.

In some categories, for example, the global and U.S. large-cap blend categories, where sustainable funds have the highest success rates, the percentage of passive sustainable funds has been higher than that of traditional funds. Lower fees offered by passive funds have contributed to the higher success rates.

Exhibit 4 Proportion of Active Sustainable and Traditional Funds by Morningstar Category (%)

Category	1-Year		3-Year		5-Year		10-Year	
	% Active Sustainable Funds	% Active Traditional Funds	% Active Sustainable Funds	% Active Traditional Funds	% Active Sustainable Funds	% Active Traditional Funds	% Active Sustainable Funds	% Active Traditional Funds
Global Large-Cap Blend Equity	76.6	90.3	78.0	90.4	78.0	90.4	80.8	94.6
Global Large-Cap Growth Equity	100.0	99.3	100.0	99.2	100.0	99.0	100.0	100.0
Global Emerging Markets Equity	69.8	85.7	68.9	86.4	79.4	87.1	100.0	93.9
US Large-Cap Blend Equity	52.7	70.8	45.7	70.1	46.2	71.7	62.5	77.2
Europe Large-Cap Blend Equity	76.3	83.8	75.0	83.3	75.9	84.4	81.6	86.2
Eurozone Large-Cap Equity	88.2	80.0	91.8	80.7	95.5	81.9	96.2	83.1
EUR Corporate Bond	85.5	86.6	88.7	86.6	86.7	87.4	91.7	91.7

Source: Morningstar Direct. Morningstar Research. Data as of 31/12/2019.

Results by Category

Global Large-Cap Blend Funds

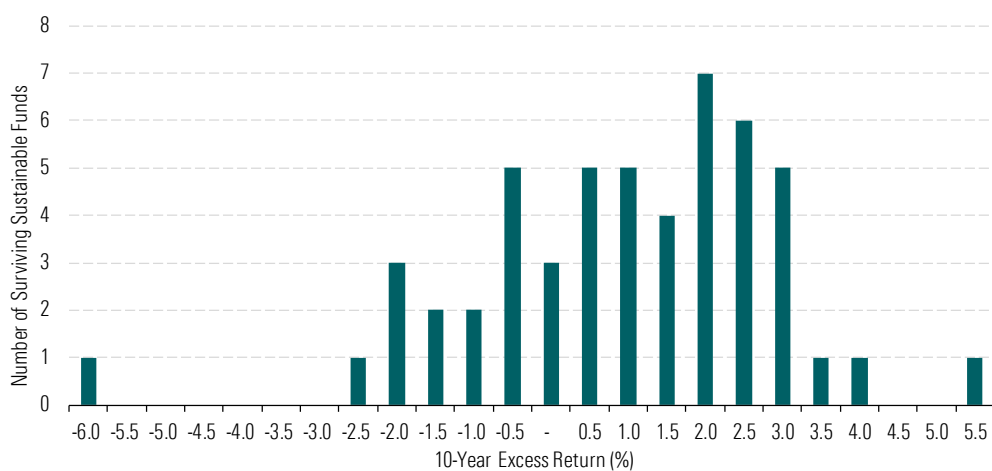
- ▶ The success rates for surviving sustainable global large-cap blend equity funds have been among the highest over multiple time periods.
- ▶ Investors in this category, however, should be mindful of the low-survivorship rate over the long term. Only one out of two (52.2%) sustainable funds available 10 years ago survived. This is still a better ratio than for traditional funds (45.9%).
- ▶ The distribution of excess returns for sustainable funds skews negative, indicating that the likelihood and performance benefit for picking a sustainable fund tends to be greater than the probability and penalty for finding an underperformer.

Exhibit 5 Global Large-Cap Blend Equity

Period	Sustainable Funds		Traditional Funds		Average Returns		
	# at beginning of the period	Survivorship Rate (%)	# at beginning of the period	Survivorship Rate (%)	Sustainable Funds (%)	Traditional Funds (%)	Sustainable Funds Success Rate (%)
1-Year	199	99.0	1,377	95.3	25.7	23.3	75.1
3-Year	140	82.1	1,327	81.2	11.3	9.9	73.7
5-Year	117	76.1	1,265	70.0	7.3	6.1	76.9
10-Year	92	52.2	1,376	45.9	6.9	6.3	67.3

Source: Morningstar Research. Data as of 31/12/2019. Returns are annualised and expressed in the currency of the categories.

Exhibit 6 Distribution of 10-Year Annualised Excess Return for Surviving Sustainable Large-Cap Blend Funds



Source: Morningstar Research. Data as of 31/12/2019. Excess returns are annualised and expressed in the currency of the categories.

Global Large-Cap Growth Funds

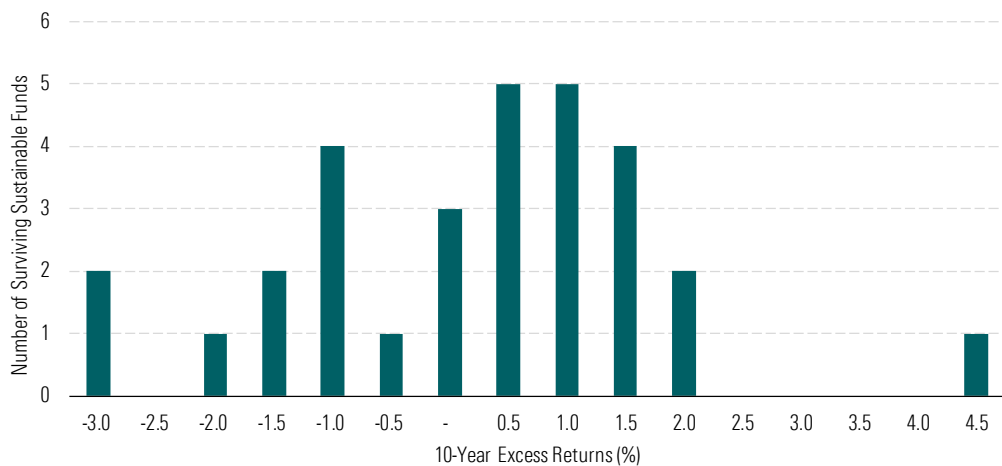
- ▶ Global large-cap growth investors have seen their odds of success fluctuate greatly over time, the lowest odds being 37.5% for investors who bought a sustainable global large-cap fund five years ago. This means that barely four sustainable global large-cap growth funds out of 10 selected five years ago beat the average traditional peer. The odds of success have improved to reach 60.3% last year.
- ▶ Survivorship rates for sustainable funds have been higher than those for traditional funds, especially the 10-year one (75.7% versus 47.8%).

Exhibit 7 Global Large-Cap Growth Equity

Period	Sustainable Funds		Traditional Funds		Average Returns		
	# at beginning of the period	Survivorship Rate (%)	# at beginning of the period	Survivorship Rate (%)	Sustainable Funds (%)	Traditional Funds (%)	Sustainable Funds Success Rate (%)
1-Year	63	98.4	305	95.4	29.0	29.2	60.3
3-Year	90	97.8	267	89.1	14.3	14.5	43.2
5-Year	42	90.5	243	81.1	8.2	8.8	37.5
10-Year	37	75.7	224	47.8	8.0	8.0	56.7

Source: Morningstar Research. Data as of 31/12/2019. Returns are annualised and expressed in the currency of the categories.

Exhibit 8 Distribution of 10-Year Annualised Excess Return for Surviving Sustainable Large-Cap Growth Funds



Source: Morningstar Research. Data as of 31/12/2019. Excess returns are annualised and expressed in the currency of the categories.

Global Emerging-Markets Funds

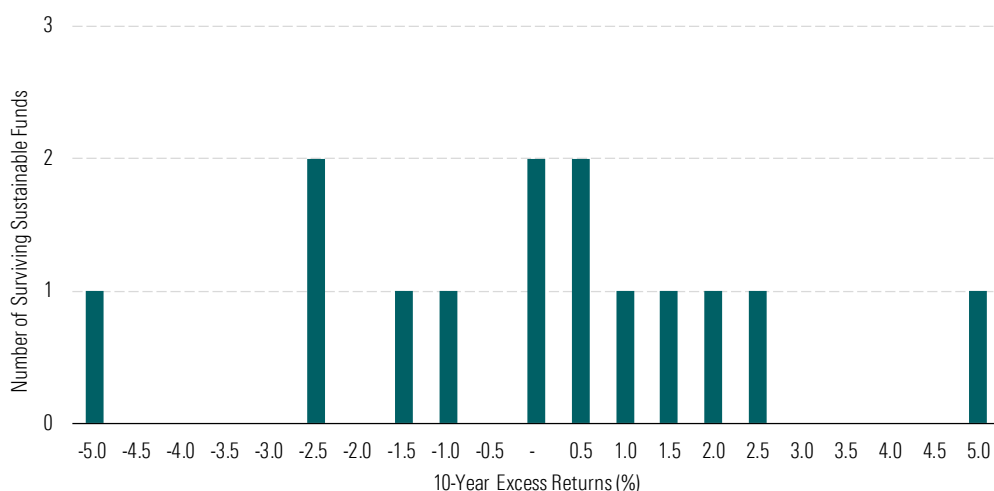
- ▶ Success rates for surviving sustainable global emerging-markets equity funds have fluctuated over time, albeit not as much as those for surviving sustainable global large-cap growth funds. An investor selecting a sustainable fund in this category that would still be alive today would have had a 50/50 chance to pick a winner.
- ▶ Survivorship rates for sustainable funds have been much higher than for traditional funds here again.

Exhibit 9 Global Emerging Markets

Period	Sustainable Funds		Traditional Funds		Average Returns			Sustainable Funds Success Rate (%)
	# at beginning of the period	Survivorship Rate (%)	# at beginning of the period	Survivorship Rate (%)	Sustainable Funds (%)	Traditional Funds (%)		
1-Year	66	95.5	568	93.0	17.9	18.9	41.3	
3-Year	100	95.0	562	83.8	10.6	10.3	60.0	
5-Year	39	87.2	571	71.5	4.7	4.6	58.8	
10-Year	16	87.5	296	48.0	2.3	2.6	50.0	

Source: Morningstar Research. Data as of 31/12/2019. Returns are annualised and expressed in the currency of the categories.

Exhibit 10 Distribution of 10-Year Annualised Excess Return for Surviving Sustainable Global Emerging-Markets Funds



Source: Morningstar Research. Data as of 31/12/2019. Excess returns are annualised and expressed in the currency of the categories.

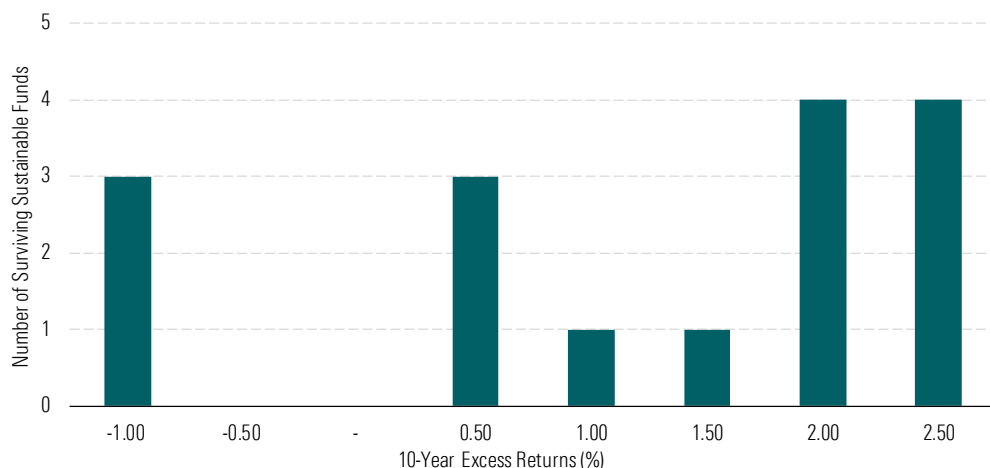
U.S. Large-Cap Blend Funds

- ▶ The success rates for surviving sustainable U.S. large-cap blend equity funds have been among the most consistently high over multiple time periods.
 - ▶ Sustainable funds' survivorship rates have been also very high, especially in comparison with traditional peers' rates in this category. Of U.S. large-cap blend funds available 10 years ago, 84.2% remain open. This contrasts with only 46.9% for conventional peers.
- The distribution of excess returns for sustainable funds also skews negative. This means that not only have investors in this category been more likely to pick a winner by taking the ESG route, but the performance reward for doing so also has been much greater than the penalty for picking an underperforming sustainable fund.

Exhibit 11 U.S. Large-Cap Blend

Period	Sustainable Funds		Traditional Funds		Average Returns		
	# at beginning of the period	Survivorship Rate (%)	# at beginning of the period	Survivorship Rate (%)	Sustainable Funds (%)	Traditional Funds (%)	Sustainable Funds Success Rate (%)
1-Year	56	98.2	489	91.4	29.8	28.1	76.4
3-Year	76	96.1	470	80.2	13.4	12.6	71.4
5-Year	27	92.6	443	69.5	9.8	8.9	76.9
10-Year	19	84.2	527	46.9	11.3	10.3	81.3

Source: Morningstar Research. Data as of 31/12/2019. Returns are annualised and expressed in the currency of the categories.

Exhibit 12 Distribution of 10-Year Annualised Excess Return for Surviving Sustainable U.S. Large-Cap Blend Funds

Source: Morningstar Research. Data as of 31/12/2019. Excess returns are annualised and expressed in the currency of the categories.

Europe Large-Cap Blend Funds

- ▶ The success rates for surviving sustainable Europe large-cap blend funds have improved over the past 10 years, to 71.1% last year from 55.1% 10 years ago.
- ▶ Survivorship rates have also been higher for sustainable funds than conventional funds over the four time horizons considered here.
- ▶ The distribution of excess returns for surviving sustainable funds also skews negative. This means that the reward for finding an outperforming sustainable fund has been greater than the penalty for picking an underperforming sustainable fund. Only three sustainable funds have lagged by more than 2%.

Exhibit 13 Europe Large-Cap Blend

Period	Sustainable Funds		Traditional Funds		Average Returns		
	# at beginning of the period	Survivorship Rate (%)	# at beginning of the period	Survivorship Rate (%)	Sustainable Funds (%)	Traditional Funds (%)	Sustainable Funds Success Rate (%)
1-Year	102	95.1	633	92.4	26.2	24.2	71.1
3-Year	151	94.0	625	82.1	7.2	6.0	75.0
5-Year	67	83.6	596	72.3	6.3	5.6	67.2
10-Year	70	70.0	744	46.2	6.8	6.6	55.1

Source: Morningstar Research. Data as of 31/12/2019. Returns are annualised and expressed in the currency of the categories.

Exhibit 14 Distribution of 10-Year Annualised Excess Return for Surviving Sustainable Europe Large-Cap Blend Funds

Source: Morningstar Research. Data as of 31/12/2019. Excess returns are annualised and expressed in the currency of the categories.

Eurozone Large-Cap Blend Funds

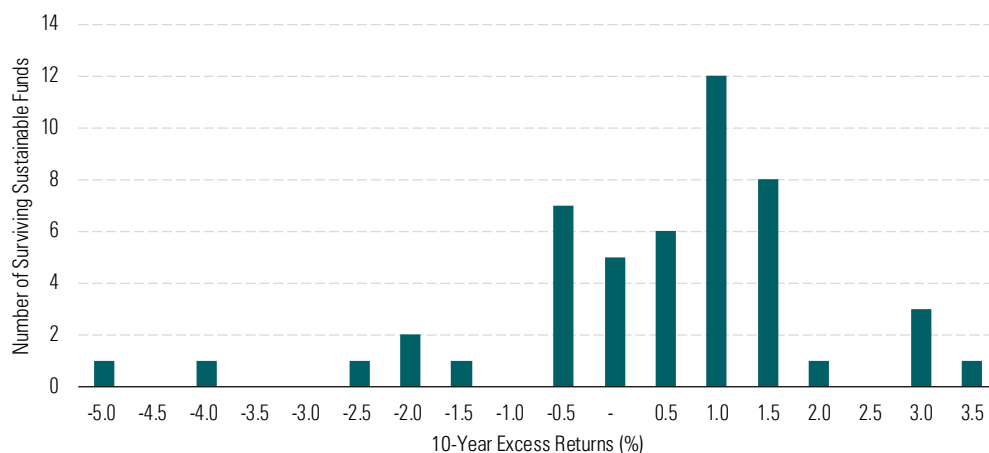
- Success rates for surviving sustainable Europe large-cap blend funds have remained almost constant at 61%-64% over the past 10 years.

Survivorship rates have been much higher for sustainable funds than conventional funds, especially when looking at the five- and 10-year time horizons.

Exhibit 15 Eurozone Large-Cap Blend

Period	Sustainable Funds		Traditional Funds		Average Returns		
	# at beginning of the period	Survivorship Rate (%)	# at beginning of the period	Survivorship Rate (%)	Sustainable Funds (%)	Traditional Funds (%)	Sustainable Funds Success Rate (%)
1-Year	86	98.8	449	95.8	24.4	23.7	63.5
3-Year	150	98.7	448	86.6	6.0	5.6	63.0
5-Year	68	97.1	477	75.1	6.1	5.9	60.6
10-Year	58	91.4	616	42.9	5.6	5.5	62.3

Source: Morningstar Research. Data as of 31/12/2019. Returns are annualised and expressed in the currency of the categories.

Exhibit 16 Distribution of 10-Year Annualised Excess Return for Surviving Sustainable Eurozone Large-Cap Blend Funds

Source: Morningstar Research. Data as of 31/12/2019. Excess returns are annualised and expressed in the currency of the categories.

EUR Corporate Bond Funds

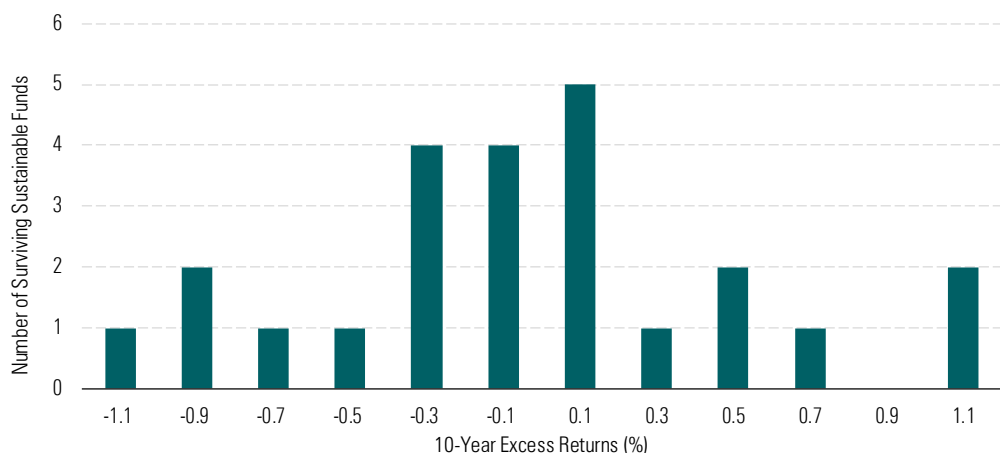
- EUR corporate bond investors have seen their odds of success fluctuate through time—the lowest odds being 33.3% for investors who bought a sustainable EUR corporate bond fund 10 years ago. This means that only three sustainable EUR corporate bond funds out of 10 that are still alive today beat the average traditional peer. The odds of success have improved to reach 58.0% last year. Survivorship rates for sustainable funds in this category have been high, especially relative to those for conventional funds. Eight out of 10 sustainable EUR corporate bond funds available 10 years ago were still alive at the end of last year. This compares with less than a 50/50 ratio for traditional funds.
- The distribution of 10-year excess returns skew negative, indicating that the likelihood and performance reward for picking an outperforming sustainable fund in this category tends to be greater than the probability and penalty for finding an underperforming one.

Exhibit 17 EUR Corporate Bond

Period	Sustainable Funds		Traditional Funds		Average Returns		
	# at beginning of the period	Survivorship Rate (%)	# at beginning of the period	Survivorship Rate (%)	Sustainable Funds (%)	Traditional Funds (%)	Sustainable Funds Success Rate (%)
1-Year	69	100.0	340	94.7	5.5	5.6	58.0
3-Year	112	97.3	344	83.4	1.9	1.9	58.5
5-Year	48	91.7	349	74.8	1.8	1.8	62.2
10-Year	30	80.0	259	47.1	3.4	3.5	33.3

Source: Morningstar Research. Data as of 31/12/2019. Returns are annualised and expressed in the currency of the categories.

Exhibit 18 Distribution of 10-Year Annualised Excess Return for Surviving Sustainable EUR Corporate Bond Funds



Source: Morningstar Research. Data as of 31/12/2019. Excess returns are annualised and expressed in the currency of the categories.

Sustainable Fund Performance Proved Resilient During COVID-19 Sell-Off

Sustainable funds held up better than their traditional counterparts during the COVID-19 sell-off. In all but one category considered in the study, sustainable funds outperformed, with average excess returns in the first quarter of 2020 ranging between 0.09% and 1.83% across categories. The global large-cap growth category was again the exception. Less than half of sustainable funds in that category beat their average conventional peer, and on average they lagged by 0.11%.

Exhibit 19 Sustainable Funds vs. Traditional Funds Over the First Quarter of 2020

Category	Sustainable Funds		Traditional Funds		ESG Success Rate (%)
	# at beginning of the period	Average Returns (%)	# at beginning of the period	Average Returns (%)	
EAA Fund Global Large-Cap Blend Equity	250	-20.1	1,435	-21.1	74.0
EAA Fund Global Large-Cap Growth Equity	64	-16.6	308	-16.5	46.9
EAA Fund Global Emerging Markets Equity	76	-23.9	555	-25.0	65.8
EAA Fund US Large-Cap Blend Equity	66	-19.7	464	-20.2	65.2
EAA Fund Europe Large-Cap Blend Equity	115	-21.1	607	-22.4	71.3
EAA Fund Eurozone Large-Cap Equity	93	-22.7	434	-24.5	65.6
EAA Fund EUR Corporate Bond	81	-6.3	336	-6.4	51.9

Source: Morningstar Research. Data as of 31/03/2020. Returns are annualised and expressed in the currency of the categories.

The overall outperformance of sustainable funds during the COVID-19 sell-off in the first quarter can be explained by a combination of factors, all of which have been discussed in recent Morningstar articles^{8, 9, 10, 11}. First, being underweight in less ESG-friendly sectors like oil and gas and overweight in technology and healthcare would have benefitted many ESG-aligned portfolios. Traditional factors such as quality and low volatility would also have played a role. Companies that score high on ESG tend to enjoy more conservative balance sheets and competitive advantages, and these are attributes that make companies more resilient during market downturns. Finally, companies that score high on ESG also tend to be well-run businesses that treat all their stakeholders fairly, address their environmental challenges, and have lower levels of controversies. Many such companies are better equipped to weather periods of uncertainty.

Conclusion

This study adds to the growing body of research on the performance of ESG funds. One should keep in mind that the European sustainable fund universe represents a wide range of ESG approaches. It also consists of a limited number of funds with long (more than 10 years) track records, which makes any analysis of long-term performance a challenge.

Based on our evaluation of the seven most popular Morningstar Categories for ESG investors, we can say that there has been no performance penalty associated with sustainable funds and that, in fact, sustainable funds have delivered superior returns on average relative to their traditional peers in the past 10 years. Investors who would have bought an ESG fund in the past 10 years would have had good odds of success. But this doesn't mean that all ESG funds have had equal odds of success and that outperformance will persist. As we have seen, success rates vary by category (that is, market exposure) and investment horizon. Fees also play an essential role. Through our analysis of performance in the

⁸ How Does Investing in ESG Companies Affect Returns?

⁹ How Did ESG Indexes Fare During the First Quarter Sell-off?

¹⁰ U.S. ESG Funds Outperformed Conventional Funds in 2019

¹¹ Sustainable Funds Weather the First Quarter Better Than Conventional Funds

lowest- and highest-cost quartiles, we have demonstrated that ESG investors can increase their odds of success by picking lower-cost options.

In future European studies, we will examine the topic of fees more closely. We will determine if the common belief that sustainable funds charge a premium is true. Somewhat related to this, we will also assess and compare the performance of active and passive sustainable funds. And finally, we will evaluate the extent to which known factors such as quality, low volatility, and size can explain some of the excess returns that we have documented here. ■■

Appendix - Methodology

Data Source

Morningstar's European open-end and exchange-traded funds database.

Universe

The eligible universe of sustainable funds includes all sustainable open-end mutual funds and ETFs (excluding feeder funds and funds of funds) in seven EEA Fund Morningstar Categories that existed as sustainable offerings at the beginning of the relevant periods (including funds that did not survive to the end of the period). To be included, the fund's inception date (or repurposed date for repurposed funds) must precede the start of the period and the obsolete date cannot predate the start of the period. Additionally, to be included, funds must have return figures.

We define sustainable funds as funds that, by prospectus, state that they use environmental, social, and governance criteria as a key part of their security selection and portfolio construction process, and/or indicate that they pursue a sustainability-related theme, and/or seek a measurable positive impact alongside financial return. The sustainable funds universe does not contain funds that employ only limited exclusionary screens without a broader emphasis on ESG, nor does it contain the growing number of funds that now formally integrate ESG factors in a nondeterminative way in their security selection¹².

The choice of categories included in the study is subject to the availability of sustainable funds with 10-year returns in each category. The seven EEA Fund Morningstar Categories considered also happen to be the largest in terms of both assets in and number of sustainable funds.

Survivorship

To calculate survivorship, we divide the number of distinct funds (based on unique Fund ID at the beginning of the period) that started and ended up the period in question by the total number of funds that existed at the onset of the period in question (the beginning of the trailing one-, three-, five- and 10-year period).

Repurposed Funds

Repurposed funds are traditional funds that changed investment objectives to make ESG their primary focus. We account for these funds during the surveyed periods from the date they repurposed, not from their inception date¹³.

Success Rate

The success rate indicates what percentage of sustainable funds that started the sample period went on to survive and generate a return in excess of the equal-weighted average traditional fund return over the

¹² For further reading on the European universe of sustainable funds: [European Sustainable Funds Landscape](#)

¹³ For further reading on repurposed funds: [Surge in Funds Rebranding as Sustainable](#)

period. We do not consider magnitude of outperformance in defining success - a fund that just barely beat the average traditional alternative counts as much as a fund that significantly outperformed.

We calculate the asset-weighted average of all the fund's share classes to come up with a single return figure for funds with multiple share classes. We then rank the funds by their composite returns, count the number that rank higher than the equal-weighted average return for the traditional funds in the category, and divide that number by the number of funds at the beginning of the period (using the same number from the denominator of the survivorship calculations).

Survivorship Rate

To calculate the survivorship rate, we divide the number of distinct funds (based on unique fund ID at the beginning of the period) that started and ended the period in question by the total number of funds that existed at the onset of the period in question (the beginning of the trailing 1-, 3-, 5-, and 10-year period).

Fees

We rank each fund by its KIID ongoing charge and group them into quartiles. We then apply the same steps described above to calculate the success rates for funds in each quartile. To be counted, each fund must have a KIID ongoing charge at the beginning of the sample period.

Excess Returns

We measure surviving sustainable funds' excess returns relative to the equal-weighted average traditional fund return in each category.

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