Morningstar Sustainability Pillar Scores
Methodology

Executive Summary
In 2016, Morningstar released the Morningstar Sustainability Rating to help investors use environmental, social, and governance, or ESG, information to evaluate portfolios. The rating provides a reliable, objective way to evaluate how their portfolios are meeting ESG challenges.

In 2018, Sustainalytics launched a new company-level rating, the ESG Risk Rating, that measures the degree to which a company's economic value may be at risk driven by ESG issues. In late 2019, Morningstar will enhance the current Morningstar Sustainability Pillar Scores methodology by replacing Sustainalytics' company ESG scores with the ESG risk scores.

The changes to the methodology will be effective October 2019.

Introduction
The Morningstar Sustainability Pillar Scores are a measure of how well the holdings in a portfolio are performing on ESG issues relative to a portfolio’s peer group. The rating is a historical holdings-based calculation using company-level ESG analytics from Sustainalytics, a leading provider of ESG research. It is calculated for managed products and indexes globally using Morningstar’s portfolio holdings database.

The Morningstar Sustainability Pillar Scores are composed of three different pillar scores: Portfolio Environmental Score, Portfolio Social Score, and Portfolio Governance Score, referred to as Portfolio ESG Pillar Scores hereafter. The calculations for each score are detailed below.
Sustainalytics ESG Risk Scores

Sustainalytics calculates the ESG Risk scores as linear combinations of company-specific material ESG indicator (MEI) unmanaged risk scores, exposure scores, and management scores. The formula is listed below:

\[
E,S,G\ Risk = \sum_{i=1}^{n} w_i \times x_i \times UR_i
\]

Where:
- \(i\) is the MEI issue
- \(x\) is the MEI issue weight
- \(UR\) is the unmanaged risk score associated with the \(i\)th MEI issue

Note, Sustainalytics aggregates the unmanaged risk scores at the material issues level in a weighted manner by not only taking the respective issue weights into account, but also the weight of the ESG indicators within these different MEIs.

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Portfolio ESG Pillar Scores

The Portfolio ESG Scores are an asset-weighted average of company-level ESG scores. Sustainalytics’ company-level ESG risk scores can be disaggregated into three pillar scores: environmental, social, and governance. Morningstar calculates portfolio-level scores for each pillar. Scores are aggregated by using the peer group weighted contribution of the pillar, as follows:

\[
Portfolio\ Pillar = \sum_{x=1}^{n} Pillar\ Score \times Weight_{adj}
\]

To receive a Portfolio ESG Score, at least 67% of a portfolio’s assets under management must have a company ESG score. The percentage of the AUM of the covered securities is rescaled to 100% before calculating the Portfolio ESG Score.
Morningstar Global Category Rank, Category Percentage Rank, and Rank Description
The Portfolio ESG Score will be assigned absolute category ranks, percentage ranks, and normally
distributed ordinal scores and descriptive ranks within their Morningstar Global Category, as follows:

<table>
<thead>
<tr>
<th>Distribution</th>
<th>Score</th>
<th>Descriptive Rank</th>
</tr>
</thead>
<tbody>
<tr>
<td>Highest 10%</td>
<td>5</td>
<td>High</td>
</tr>
<tr>
<td>Next 22.5%</td>
<td>4</td>
<td>Above Average</td>
</tr>
<tr>
<td>Next 35%</td>
<td>3</td>
<td>Average</td>
</tr>
<tr>
<td>Next 22.5%</td>
<td>2</td>
<td>Below Average</td>
</tr>
<tr>
<td>Lowest 10%</td>
<td>1</td>
<td>Low</td>
</tr>
</tbody>
</table>

Source: Morningstar, Inc.

Frequency of Calculations
The Morningstar Sustainability Pillar Scores are on a monthly basis with a one-month and six-business-
day lag. The scores will be issued using the most recent company data from Sustainalytics, which is
reported to us on a monthly basis. If a portfolio has not yet been received for the rating date, the most
recent portfolio available will be used for score and ranking, provided the portfolio is fewer than 276
days old. 

References

https://www.morningstar.com/content/dam/marketing/shared/research/methodology/860250-GlobalCategoryClassifications.pdf


https://www.morningstar.com/content/dam/marketing/shared/Company/Trends/Sustainability/Detail/Documents/SustainabilityRatingMethodology.pdf?

https://www.sustainalytics.com/controversies-research/#1482352879777-ebfb8fdd-0440

https://www.sustainalytics.com/esg-ratings/
About Morningstar Sustainability Research
Morningstar Sustainability Research is dedicated to helping investors evaluate the values and impact of their investments.

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