

# ESG Strategy

## We're Not Saying That ESG Makes It Better – The Numbers Are

### A Deep-Dive Into the Brazilian ESG Funds Market

In this report we take a deep dive into the Brazilian ESG funds market and explore how this industry has grown and performed. In a nutshell, ESG funds' AuM has been growing faster and their performance has been better than for the consolidated fund industry. Will this momentum continue?

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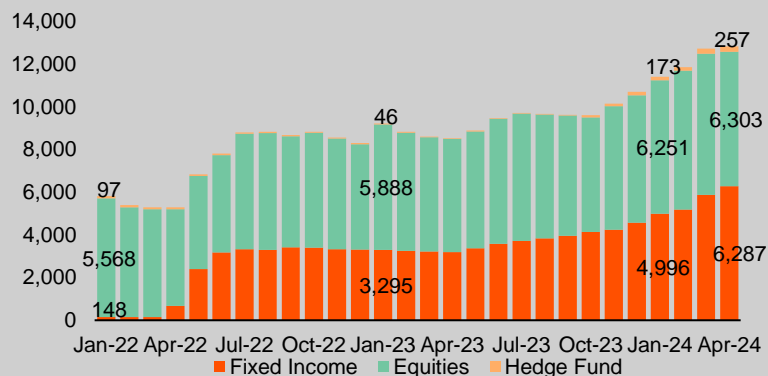
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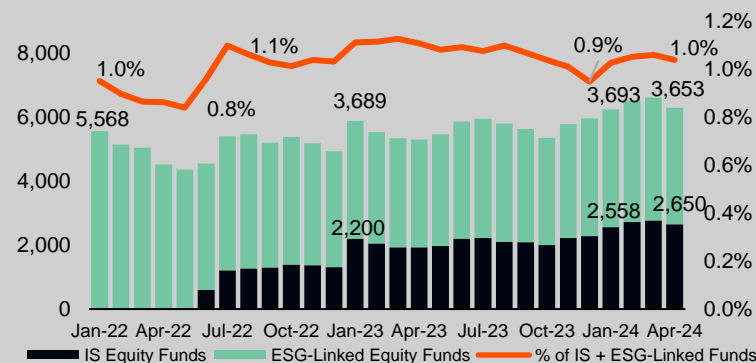
# Executive Summary

- Key message.** In this report we take a deep dive into the Brazilian ESG funds market and explore how this industry has grown and performed. Using ANBIMA's numbers, we evaluate funds' market evolution in terms of assets under management, net new money and number of funds incorporated, as well as the number of managers effectively running ESG funds. Lastly, we focus on ESG equity funds and assess their performance versus the total funds industry in Brazil. In our opinion, although the ESG fund industry is in its infancy, our findings make a good case for ESG resilience both in terms of returns and fundraising. We found that: i) there are 120 ESG funds in Brazil managed by 40 asset managers; ii) sustainable investment funds (fundos de investimento sustentável, or IS, in Portuguese), which have sustainable investment as their primary objective, have been gaining share over ESG-linked funds, which integrate ESG metrics into investment analysis, and the former already represent 69% of all ESG funds; iii) ESG funds' AuM currently amounts to BRL 12.8 billion – 49% of it allocated to equity funds and 49% allocated to fixed-income funds; iv) ESG funds have a lot of room to grow, as they represent only 0.15% of total industry AuM; v) net new money in the first four months of 2024 is already double the 2023 total; vi) IS equity funds outperformed the total equity fund averages in 2022, 2024, and the last 12 months; and vii) ESG-linked equity funds outperformed the total equity fund averages in 2023, 2024, and the last 12 months.
- New fund classifications.** In January 2022, ANBIMA (the Brazilian Financial and Capital Markets Association) established new rules for identifying IS funds and funds that integrate ESG into their management criteria (we refer to these as ESG-linked funds throughout this report). The new rules distinguish between funds with sustainability as their primary goal (IS funds) and funds that consider ESG risks and opportunities without that being their main objective.
- ESG fund industry size.** Totalling BRL 12.8 billion, the ESG fund industry has been growing faster than the total fund industry in Brazil in AuM terms. That said, ESG funds comprise only 0.15% of the total assets under management. Their growth has come primarily from IS funds, which grew by 77% in the last 12 months, much faster than the 15% rate for the total Brazilian fund market. Fixed-income funds have been growing faster than equities, and already make up 49% of the total ESG fund industry's AuM.
- ESG equity funds' performance.** We compared ESG equity funds' performance with total equity fund industry performance starting from April 2022 (the inception of the first IS fund). Since then, IS equity funds have returned 20.7%, vs. 15.3% for ESG-linked and 9.4% for the consolidated equity industry. Evidence of ESG outperformance is also seen in academia and the financial markets – MSCI Brazil ESG has outperformed MSCI Brazil by 29 pp since August 2013, and 59% of academic studies have concluded that incorporating ESG generates similar or better portfolio returns.

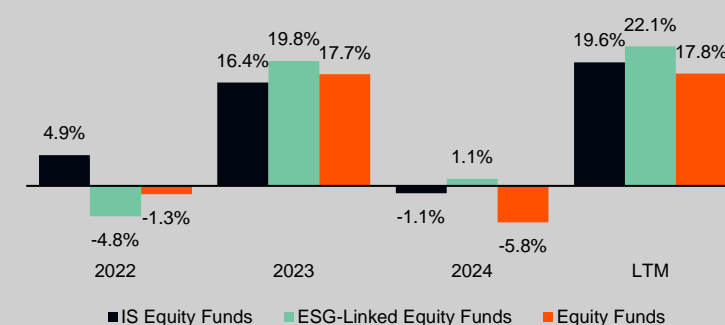
**Funds AuM – Breakdown by Asset Class (BRL in Millions)**



**Equity Funds AuM – Breakdown by Classification (BRL in Millions)**



**Equity Funds' Performance**



## ■ ESG Funds: How big is the market?

- **ANBIMA's New Fund Classifications.** Brazilian Financial and Capital Markets Association's differentiation of IS and ESG-linked funds (Slide 5)
- **There Are 120 ESG Funds in Brazil – They Have Grown 62% yearly.** A descriptive view of ESG managers and funds (Slide 6)
- **ESG Fund Market Has Reached BRL 12.8 billion and Has Grown at a 40% CAGR.** ESG fund market breakdown by asset class (Slide 7)
- **IS Funds Hold BRL 8.7 Billion – LTM AuM Growth of 77% vs. 15% for Brazil's Total Fund Market.** ESG fund market breakdown by ANBIMA's classifications (Slide 8)
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## ■ ESG Equity Funds: How Are They Performing?

- **Among the 120 ESG Funds, 83 Are Equity Funds.** The evolution of the number of ESG equity funds (Slide 11)
- **ESG Equity Funds' AuM Total BRL 6.3 Billion.** AuM and net new money figures (Slide 12)
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# ESG Funds:

How big is the market?

# ANBIMA's New Fund Classifications

- In January 2022, ANBIMA (the Brazilian Financial and Capital Markets Association) established new rules for identifying sustainable funds ("IS" funds) and funds that integrate ESG into their management criteria (we refer to these as ESG-linked funds throughout this report). The new rules distinguish between funds with sustainability as their primary goal (IS funds) and funds that consider ESG risks and opportunities without that being their main objective.
- ANBIMA's changes align with international trends, taking into account the maturity and specificities of Brazil, and aim to discourage greenwashing while ensuring the robust growth of sustainable investment alternatives in Brazil. Now, if a fund is not classified as "IS," it cannot use terms like "green," "ESG," "sustainable," or "impact," among others, in its name and description.
- ANBIMA's previous classification system was specific to equity funds and limited to setting standards for a subcategory known as "Sustainability/Governance." This subcategory was the only one that explicitly encompassed sustainable investments. It included funds that invested in companies demonstrating high levels of corporate governance or that were distinguished by their long-term social responsibility and corporate sustainability.
- In addition to further regulating funds, the changes also give fund managers the responsibility of incorporating ESG factors into their investment analyses and management processes. This includes documented policies, ongoing activities (such as governance and team qualifications) and transparency.
- The guidelines encourage the incorporation of ESG analysis and are not restrictive regarding the methods of achieving ESG goals, allowing for flexibility and innovation in fund-management strategies. Each manager must submit its fund methodology for analysis by ANBIMA.
- The framework is designed to evolve with international trends and market needs, ensuring that the Brazilian funds industry remains competitive and up-to-date with global standards. Additionally, it is important to note that the entity aims to encourage all managers to include ESG metrics in their analyses going forward – in other words, integrating ESG should not be considered a competitive advantage.

## ANBIMA's Rules for ESG Funds

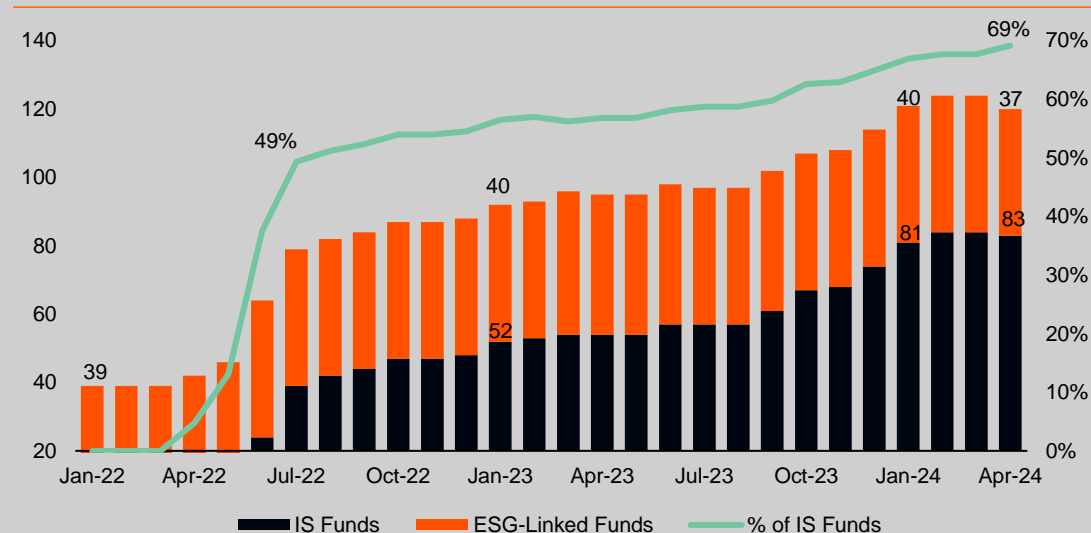
	Manager	"IS" Fund	Fund that takes into consideration ESG issues
Commitment to sustainability	Sustainability policy (approved document)	<b>The fund has sustainable investment as its objective</b>  Sustainable Investment objective summarized in the fund's bylaws and investment policies that seek portfolio alignment; "do no harm" (bylaws, policies, and declaration)	<b>Fund's investments consider ESG</b>  Investment policy or technical material includes ESG consideration (formal documentation)
Ongoing actions	Governance structure (approved report)	<ul style="list-style-type: none"> <li>Strategy (methodologies and data) other tools and engagement</li> <li>Limitations of methodologies, data, and tools</li> <li>Due diligence and monitoring measures (periodic statements/report)</li> </ul>	<ul style="list-style-type: none"> <li>Methodology and data; limitations</li> <li>Other tools and engagement (where applicable)</li> <li>Due diligence measures (periodic statements/report)</li> </ul>
Transparency	Disclosure of policy and governance (manager's website/materials)		
Important!	Refers to the management activity. Commitments accompanied by respective actions. Manager will not be classified	<ul style="list-style-type: none"> <li>Monitoring the goal with metrics and indicators, as well as a commitment to "do no harm"</li> <li>Specific risks and opportunities</li> </ul>	<ul style="list-style-type: none"> <li>Differentiation in advertising materials</li> <li>Monitoring of established parameters for ESG consideration</li> <li>Portfolios with different objectives</li> </ul>



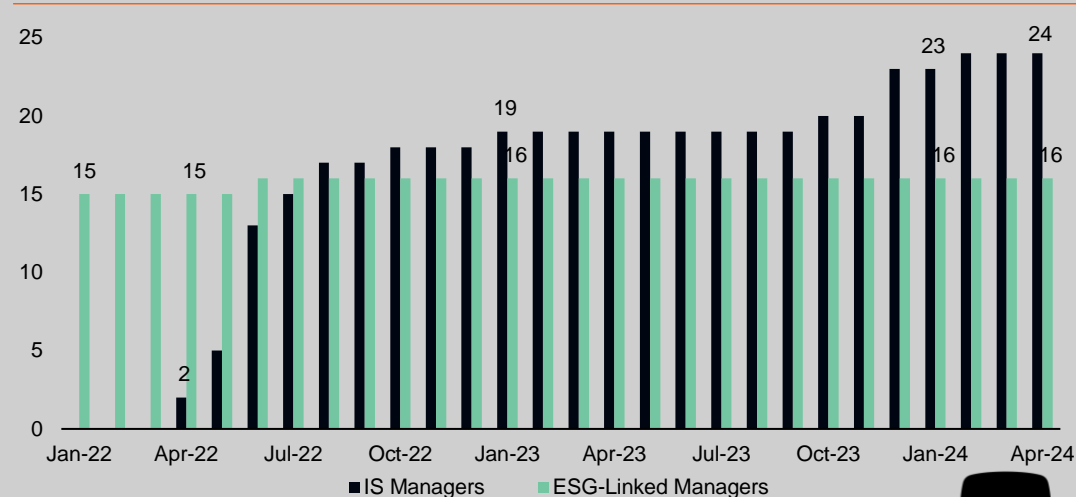
# There Are 120 ESG Funds in Brazil – They Have Grown by 62% Yearly

- Using ANBIMA's database and a lot of Python programming, we delved into more than 5 GB of data to chart the evolution of the ESG fund market in Brazil since the last change in fund categorization.
- As ANBIMA started the process of re-labeling funds at the beginning of 2022, we highlight that the figures for that year probably overstate the growth rate of the ESG market. This is mainly because it was not only actual new money that flowed into ESG during 2022; there was also a backlog of funds that used to carry ESG characteristics before the classification change and had requested to be recognized in the two new categories.
- Because of this, although we believe that our numbers paint an accurate picture, some adjustments were needed:
  - For IS funds, we were able to assess the precise time when the classification was awarded through the change of funds' names – we only count an IS fund after we see "IS" added to its name. Hence, the time series for those starts in April 2022.
  - For ESG-linked funds, there are no changes in the funds' names, so we consider the funds' incorporation date as the first date in which AuM is positive, as long as it happened after December 31, 2021.
- With all that said, the number of IS and ESG-linked funds has soared since the new classification was put in place: as of April 2024, the industry had reached 120 funds (excluding ETFs), up from 88 at the end of 2022 and 114 at the end of 2023. Considering that there were 39 funds in the beginning of 2022, this implies a CAGR of 62% since then.
- The number of IS funds has grown significantly faster than ESG-linked funds, and they currently represent 69% of the total ESG fund market.
- Regarding asset managers, there are currently 24 managers running IS funds and 16 managers running ESG-linked funds – a negligible figure when compared with the 986 managers registered at ANBIMA, suggesting that there is huge growth potential as ESG-investing awareness increases.

## Number of IS and ESG-Linked Funds



## Number of Managers Running IS and ESG-Linked Funds



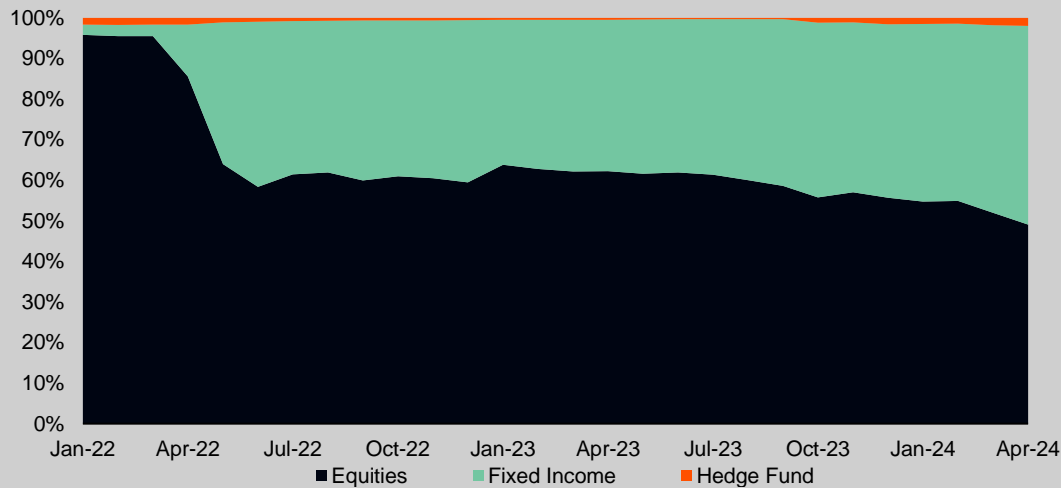
# ESG Fund Market Has Reached BRL 12.8 Billion and Has Grown at a 40% CAGR

- After disregarding double-counts due to master-feeder structures, the consolidated ESG fund market reached BRL 12.8 billion in April 2024, up from BRL 10.7 billion at the end of 2023 and BRL 8.3 billion at the end of 2022. Considering that the market was BRL 5.8 billion at the beginning of 2022, this implies a 40% CAGR.
- Regarding asset classes, equity and fixed-income funds each represent 49% of the total AuM, while hedge funds account for the remaining 2%. In absolute terms, equity and fixed-income funds hold BRL 6.3 billion each (hedge funds hold only BRL 257 million).
- Fixed income has been gaining share: at the end of 2022, the asset class accounted for 40% of total market, reaching 43% by the end of 2023 and 49% as of April 2024.

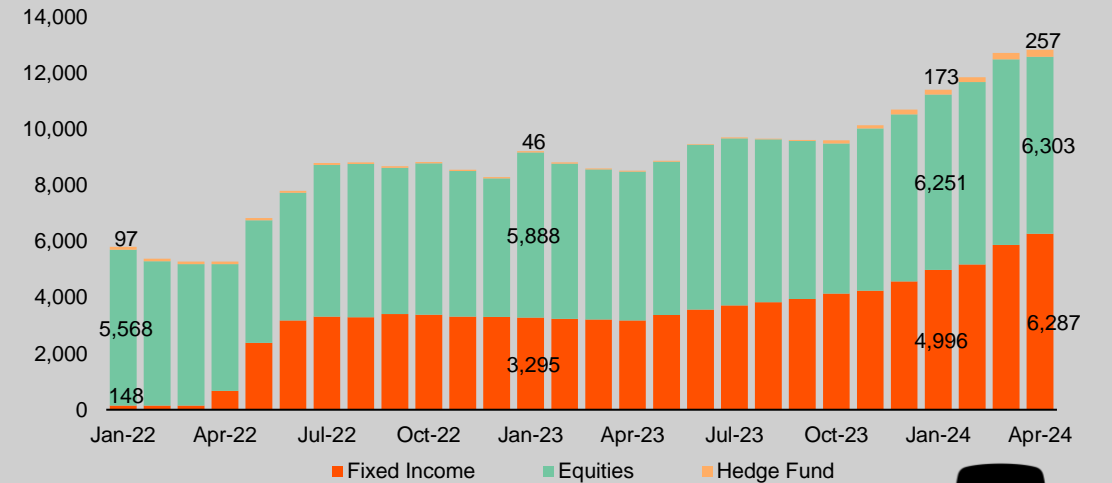
**Consolidated Funds AuM (IS + ESG-Linked, BRL in Millions)**



**ESG Funds – AuM Breakdown by Asset Class**



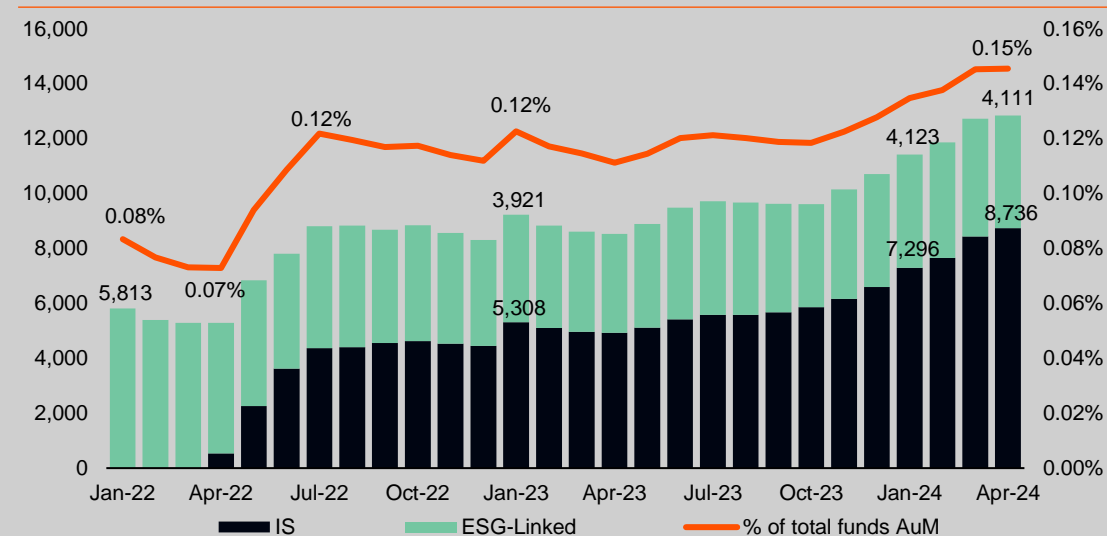
**ESG Funds – AuM Breakdown by Asset Class (BRL in Millions)**



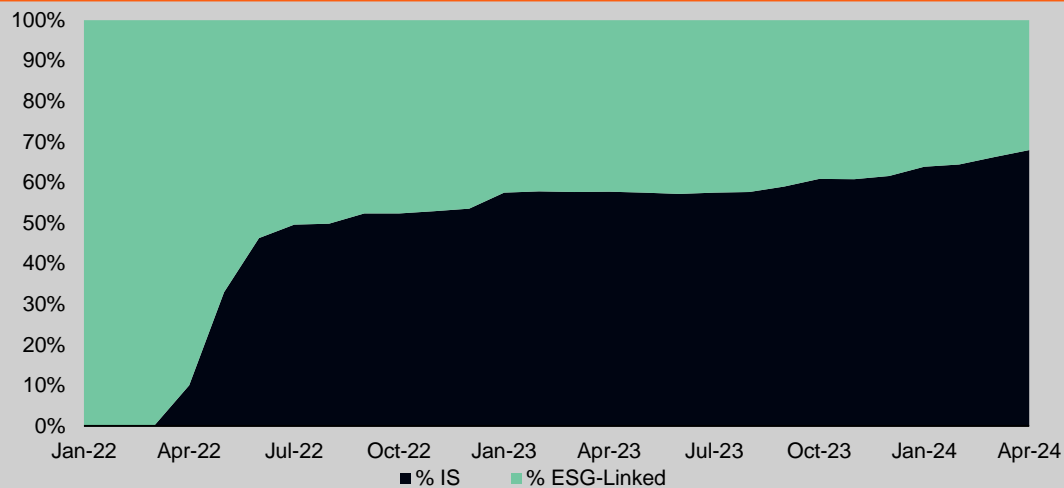
# IS Funds Hold BRL 8.7 billion – LTM AuM Growth Was 77%, vs. 15% for the Total Brazilian Fund Market

- IS funds reached BRL 8.7 billion in April 2024, while ESG-linked funds have reached BRL 4.1 billion; AuM has grown by BRL 3.8 billion in the last 12 months for IS funds (+77%). ESG-linked funds grew at a slower pace, as AuM increased by only BRL 335 million in the period.
- Compared with the total Brazilian fund market, IS funds' AuM grew at triple the rate. That said, the ESG market AuM is still small, amounting to only 0.15% of total funds.
- IS funds have been gaining share over ESG-linked funds and currently represent 68% of the ESG fund market, compared with 54% at the end of 2022 and 62% at the end of 2023.

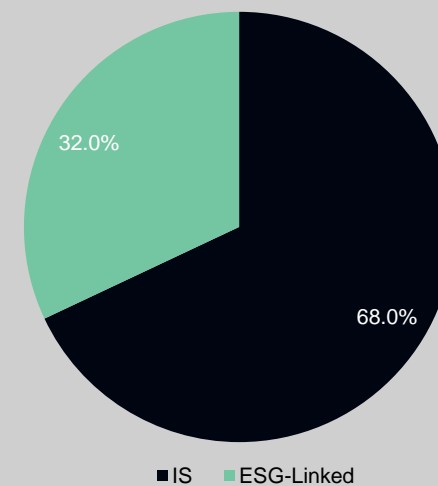
**ESG Funds AuM Breakdown by Classification (BRL in Millions)**



**ESG Funds AuM Breakdown by Classification**



**ESG Funds AuM Breakdown by Classification as of April 30, 2024**

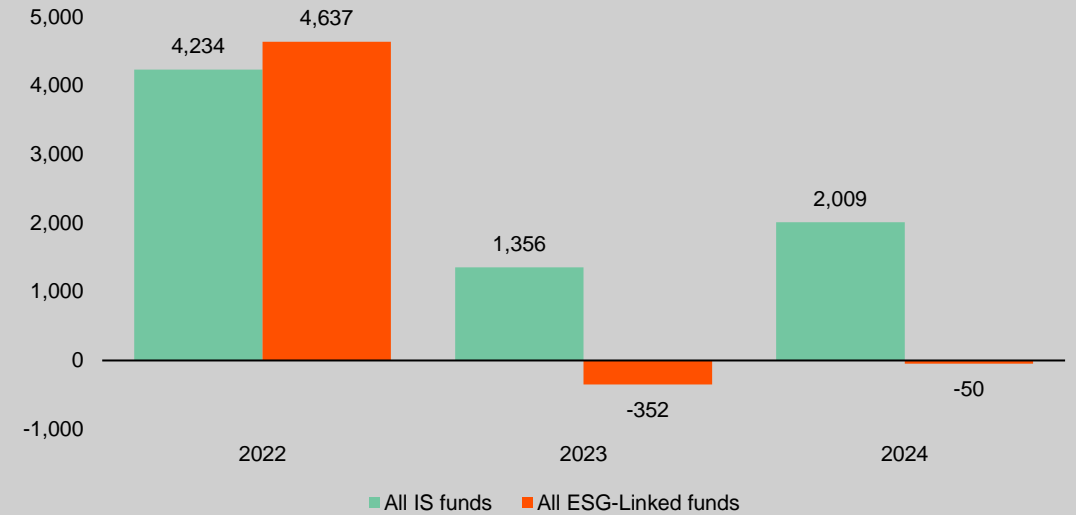




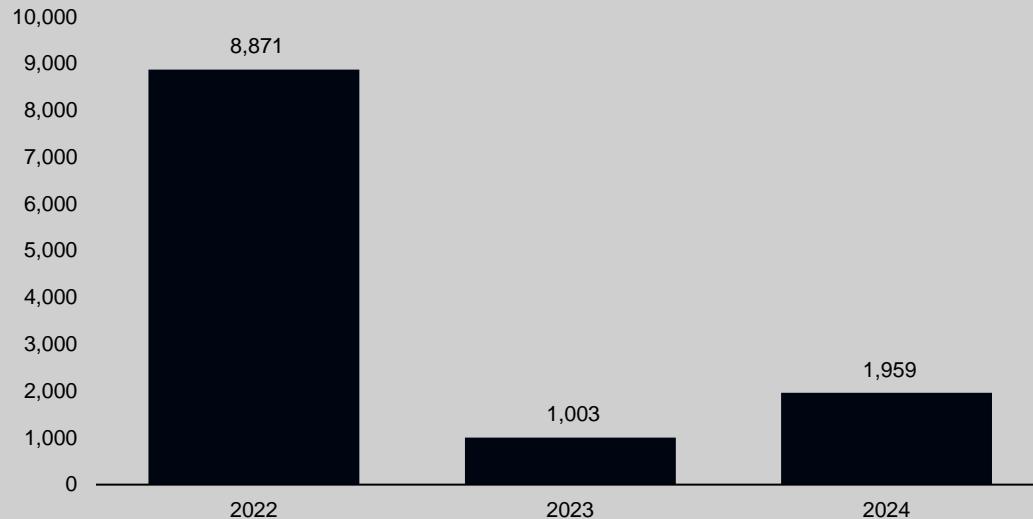
# Net New Money in 2024 Is Already Double the 2023 Total

- As stated above, net new money in 2022 probably overestimates the yearly figures, since a large chunk of what is considered “new” money is in fact only a reclassification of funds under ANBIMA’s new labeling standard. That said, 2023 and the first months of 2024 are probably much less affected by this factor, and they show inspiring trends: new money in the first third of 2024 already amounts to twice the net new money added in 2023 as a whole. The comparison is especially interesting given that the fund industry in Brazil registered net redemptions of BRL 108 billion in 2023.
- IS funds are clearly receiving more money than ESG-linked funds. Although it is not possible to be sure that this is the main factor behind it, we note that IS funds are clearly identifiable as “sustainable,” as ANBIMA allows them to make this statement in the fund name. Conversely, ESG-linked funds lack clear ESG appeal, as the only indications of their sustainable practices are found in the fund’s prospectuses.

### ESG Funds Net New Money Breakdown by Classification (BRL in Millions)



### ESG Funds Net New Money (BRL in Millions)



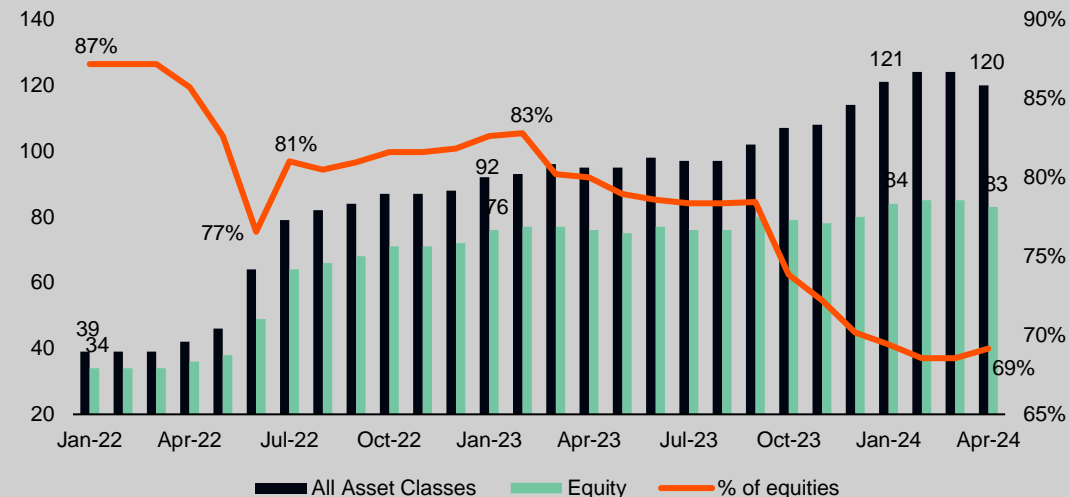
# ESG Equity Funds:

How are they performing?

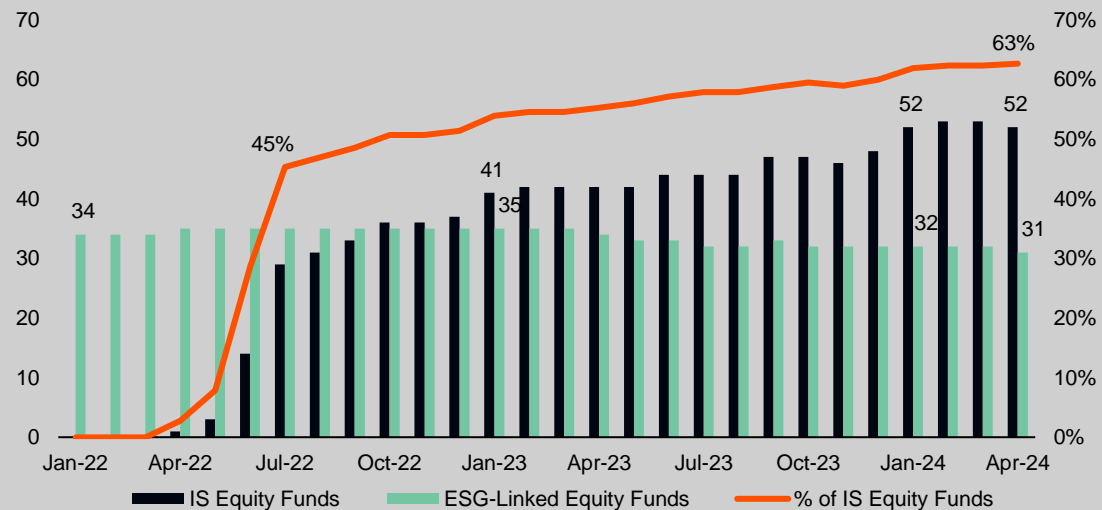
# Among the 120 ESG Funds, 83 Are Equity Funds

- Equity funds currently represent 69% of all ESG funds, but the share of equities has been declining since 2022 – a trend that is not being shown by AuM. There are 83 ESG equity funds today, up from 72 at the end of 2022. Eight funds were created in 2023, and three more were created in the first four months of 2024.
- Among the 83 ESG equity funds, 52 are IS funds and 31 are ESG-linked funds. The share of IS funds has been increasing steadily since July 2022 and represents 63% of the total ESG equities pie. On the other hand, the number of ESG-linked funds has remained virtually unchanged since the beginning of 2022.
- Although the number of ESG equity funds has grown by 144% since the new regulations were put in place, it represents only 2% of total equity funds registered in ANBIMA's database.

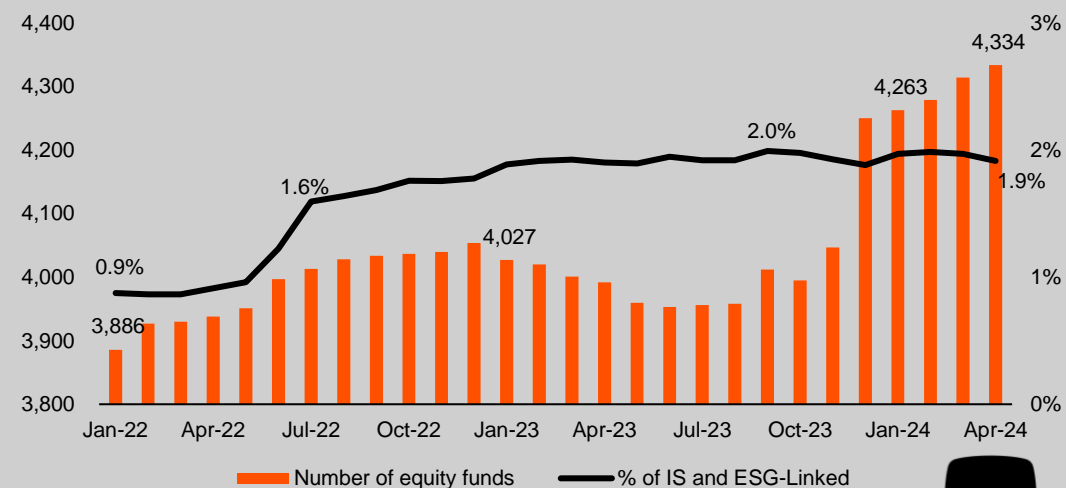
## Number of IS and ESG-Linked Equity Funds



## Number of ESG Equity Funds (BRL in Millions)



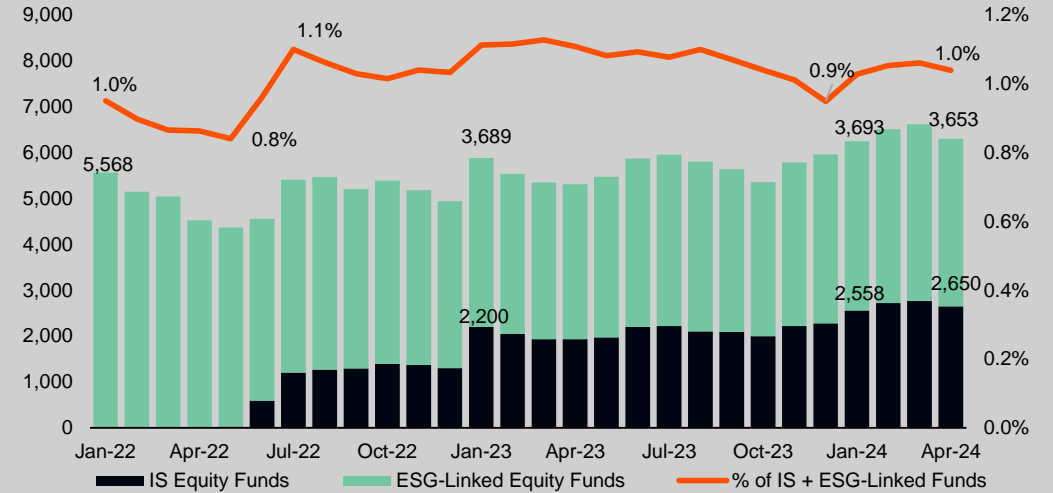
## Number of Equity Funds: Total Industry



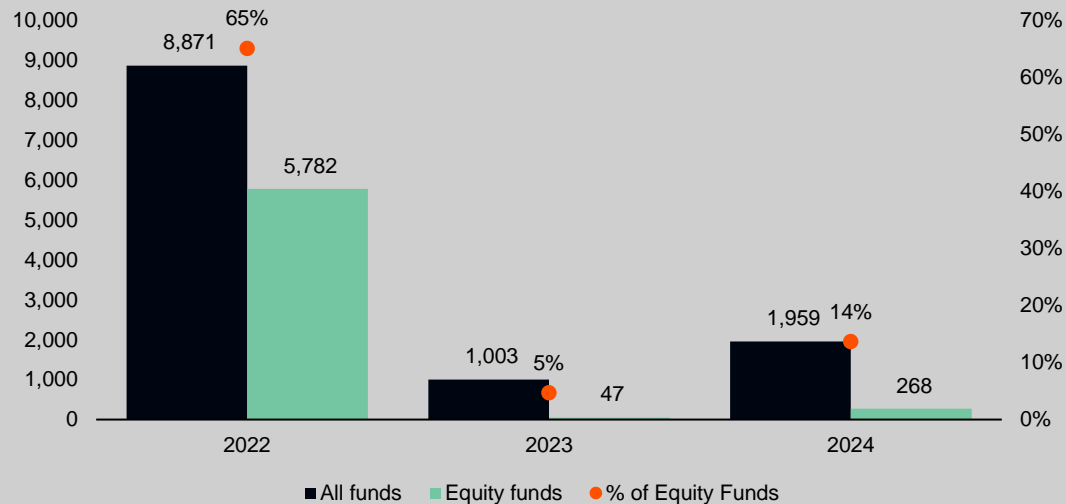
# ESG Equity Funds' AuM Totals BRL 6.3 Billion

- ESG equity funds' AuM has been growing steadily at a 5.5% annual rate since the beginning of 2022 and is currently BRL 6.3 billion. Additionally, IS equity funds' AuM has gained share over ESG-linked equity funds, and makes up 42% of total ESG equity AuM.
- Total ESG equity funds' AuM represents 1.0% of total investments in Brazilian equity funds.
- ESG equity funds' net new-money adds were weak in 2023 and 2024. Accounting for only BRL 47 million in 2023 and BRL 208 million in 2024, net new money has been dominated by IS funds, while ESG-linked equity funds posted net redemptions in both periods. That said, the Brazilian equity funds industry added only BRL 4 billion in 2023 and is currently posting net redemptions of BRL 1.6 billion in 2024.

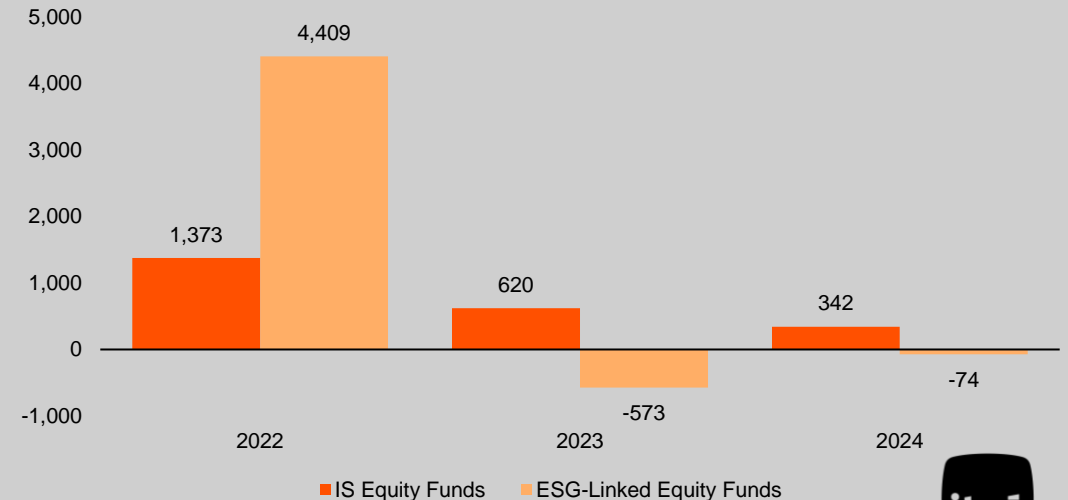
## IS Equity and ESG-Linked Equity Funds AuM



## IS Equity and ESG-Linked Equity Net New Money (BRL in Millions)



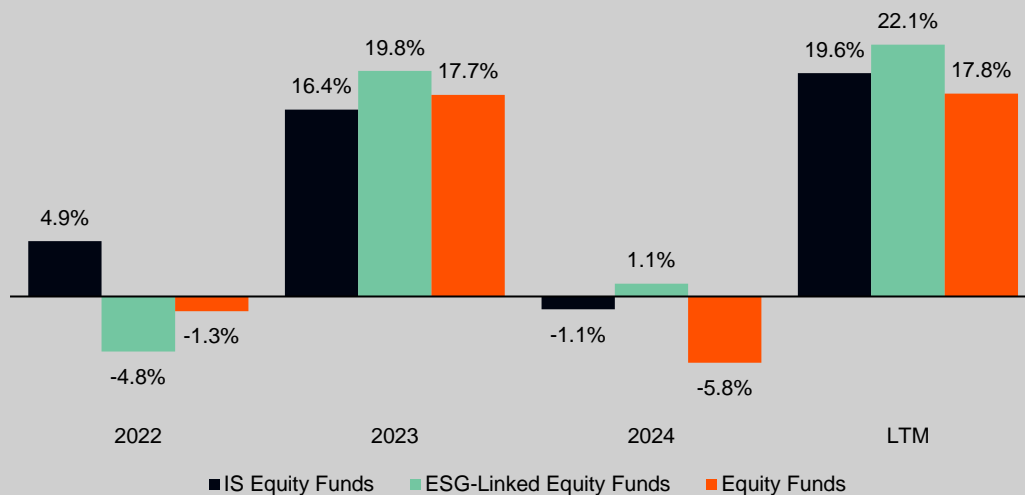
## IS Equity and ESG-Linked Equity Net New Money Breakdown by Classification (BRL in Millions)



# IS Equity and ESG-Linked Equity Funds Outperform the Equity Fund Industry

- We tried to evaluate ESG equity funds' performance and compare it with the total equity fund industry's performance. To do this, we took the average of ANBIMA's equity fund performance (published monthly) and compared it with the AuM-weighted average of ESG equity funds' performance. To provide a fair comparison, we chose April 2022 as the base date for our analysis, since it represents the inception of the first IS fund.
  - IS equity funds: +20.7% since the end of April 2022
  - ESG-linked equity funds: +15.3% since the end of April 2022
  - Equity fund industry: +9.4% since the end of April 2022
- In addition to longer-term outperformance, IS equity funds also outperformed the equity industry in 2023, 2024 and the last 12 months. Similarly, ESG-linked equity funds outperformed the equity industry in 2023, 2024 and the last 12 months.

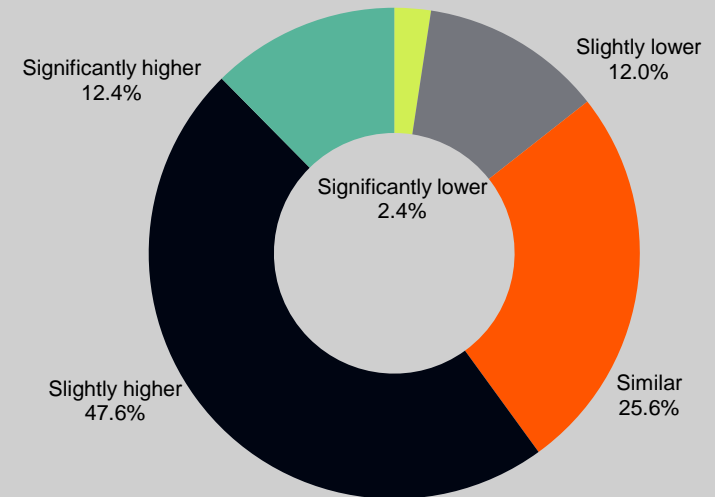
## Equity Funds Performance Comparison



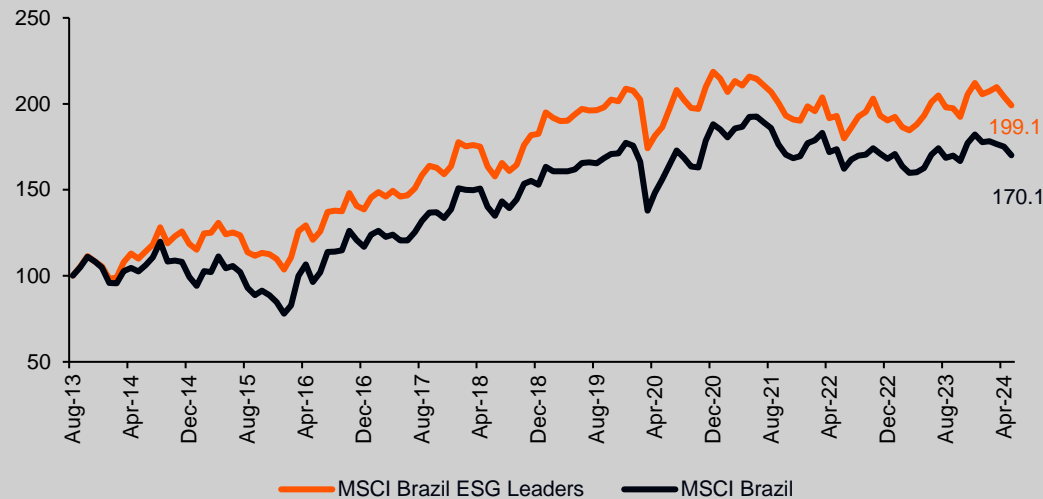
# ESG Outperformance Is Also Supported by Other Numbers

- ESG strategies in Brazil have yielded excess returns: The MSCI Brazil ESG index has delivered a 212% gain since 2013, compared with a 182% gain for the MSCI Brazil index.
- When PwC surveyed global institutional investors on ESG incorporation in 2022, more than 85% affirmed that financial products that account for ESG yield similar, slightly higher, or significantly higher returns than their non-ESG equivalents.

## Reported Yields of ESG Incorporation According to Asset Managers, 2022



## Factoring In ESG: MSCI Brazil vs. MSCI Brazil ESG (BRL)

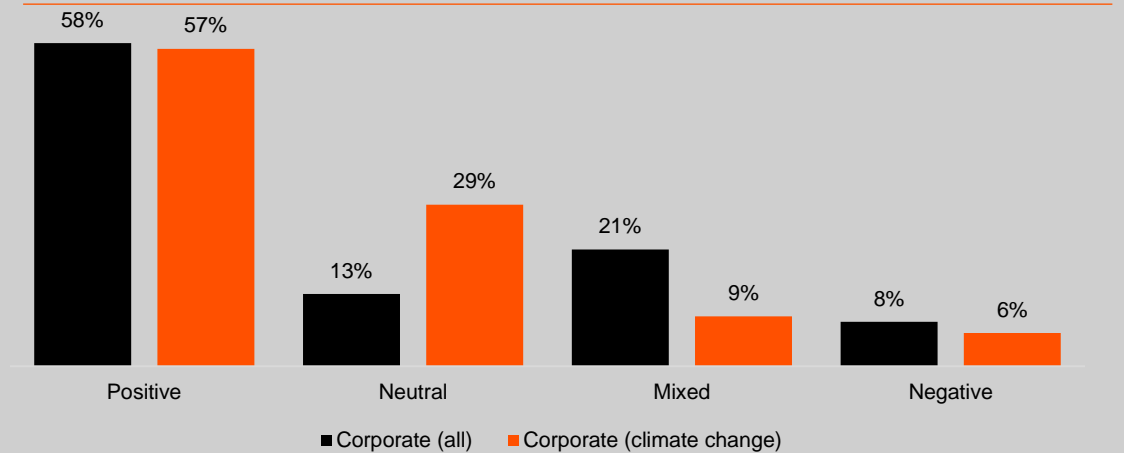




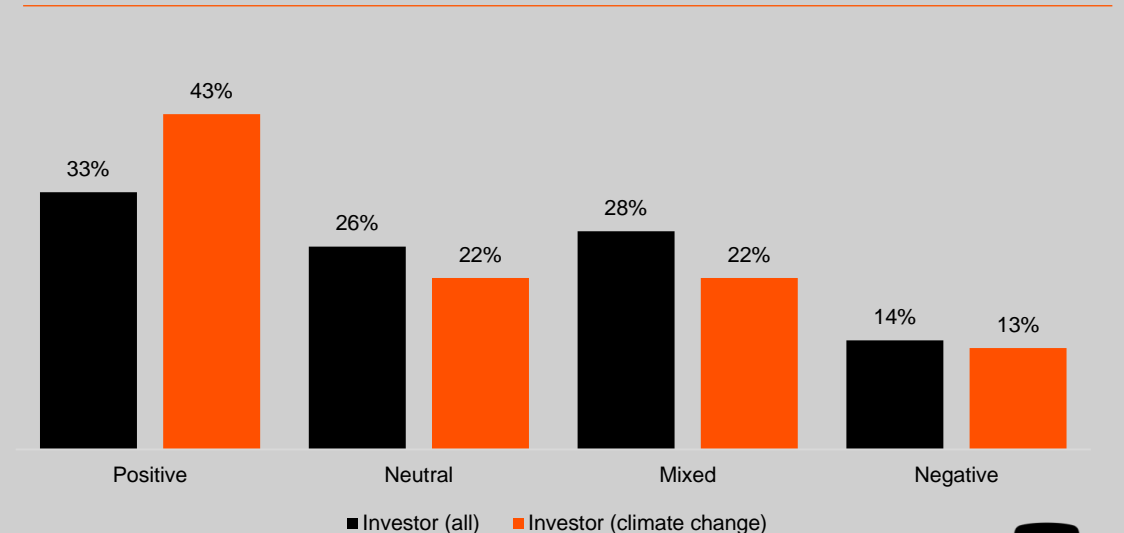
# 59% of Academic Studies Conclude That ESG Generates Similar or Better Portfolio Returns

- Academia's takes on ESG returns.** A plethora of studies on this subject have been produced in the last couple of decades. Depending on the parameters used, the results have been hard to reconcile. More than one meta-study has attempted to address the apparent inconsistency by compiling studies into a broader analysis of the issue.
- A 2021 NYU meta-study analyzed over 1,000 research papers from 2015 to 2020 to evaluate the relationship between ESG metrics and financial performance. By examining a wide range of research frameworks, metrics and definitions, the study provides a comprehensive overview of the subject. Here are its key takeaways:
  - Time horizon:** The positive impact of ESG on financial performance becomes more apparent over longer time frames. This finding suggests that a long-term investment approach can enhance the benefits of ESG-focused strategies.
  - Investment strategies:** ESG integration strategies yield better results than negative screening strategies.
  - Downside protection:** ESG investing provides downside protection during economic or social crises. This could indicate that ESG-conscious companies have lower risk profiles, which is particularly valuable in volatile market conditions.
  - Corporate sustainability:** Companies engaging in sustainability initiatives often see improved financial performance. This improvement is attributed to better risk management and innovation.
  - Low-carbon future:** Companies actively managing for a low-carbon future tend to experience better financial outcomes. This finding aligns with the global shift toward sustainability and the increasing importance of environmental stewardship in corporate strategy.
  - ESG disclosure:** Merely disclosing ESG information without strategic implementation does not lead to enhanced financial performance.
- In a nutshell, the NYU study found that factoring ESG into traditional financial analysis resulted in non-negative financial performance in 92% of the corporate studies in the meta-analysis, as measured by operational metrics such as ROE and ROA. For investment studies, which typically focus on risk-adjusted attributes such as alpha or the Sharpe ratio in a portfolio of stocks, ESG yielded a non-negative contribution in 86% of the studies analyzed.

## Correlation Between ESG and Financial Performance – Company Perspective



## Correlation Between ESG and Financial Performance – Portfolio Perspective



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Analysts	Disclosure Items				CNPI*
	1	2	3	4	
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