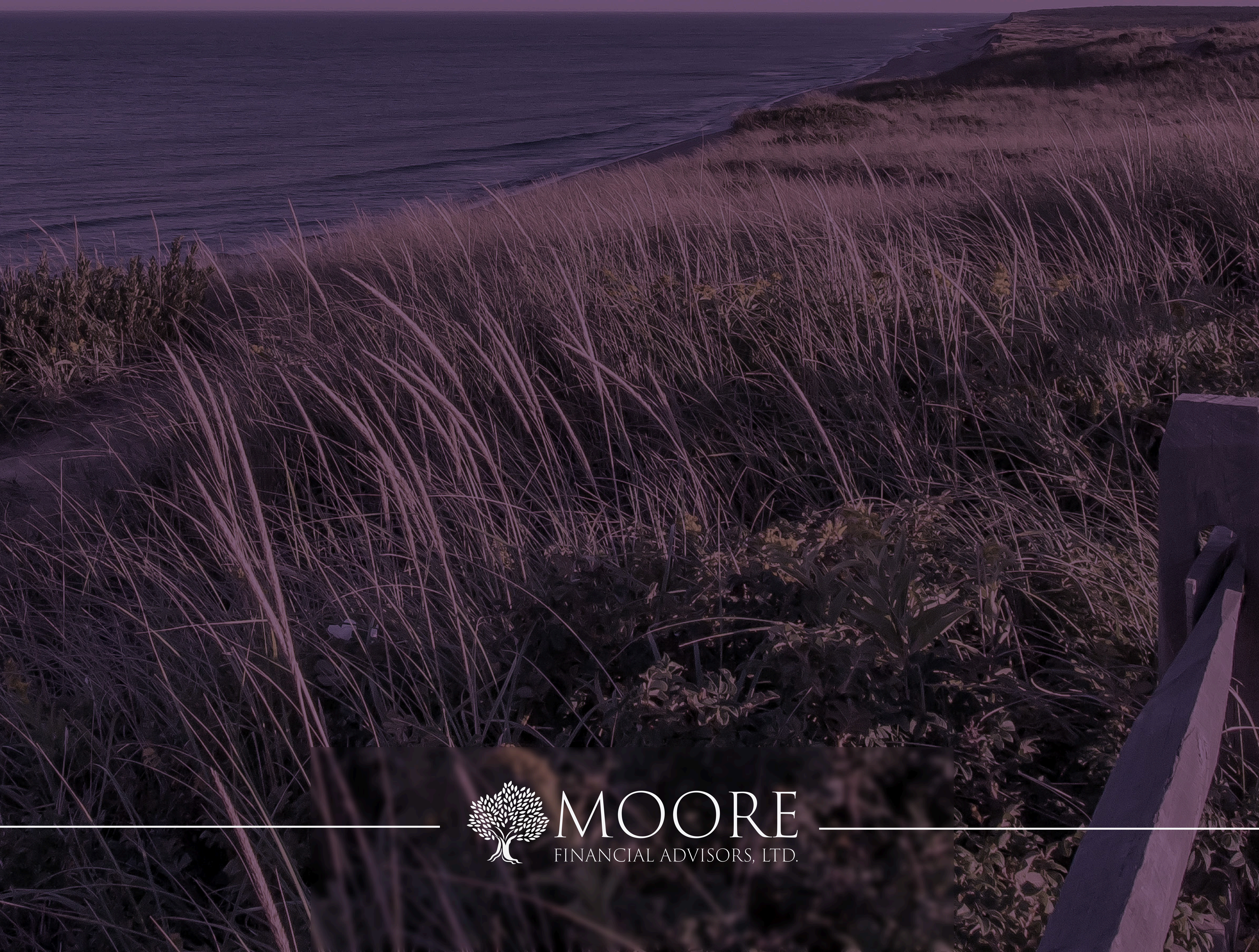
UNDERSTANDING SUSTAINABLE INVESTING



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INTRODUCTION

The battle against climate change is becoming near omnipresent. From electric cars to solar energy to even the increasing popularity of reusable water bottles, people are now more conscious than ever of the indirect costs of their actions. Sustainability extends beyond consumer products and clean energy. With increasing conscientiousness, sustainable investing enables investors to align their values with their financial goals. This paper serves to give background on sustainability in the investment space.

Sustainability, as defined by the United Nations Brundtland Commission in 1987, is the ability to "meet the needs of the present without compromising the ability of future generations to meet their own needs." [1] This definition highlights the fact that sustainability is not a sacrifice. A sustainable focus allows for the extended wellbeing of people while current generations still thrive. This concept of sustainability can also be used to describe political policies, economic targets, and even actions in interpersonal relationships.

Sustainable investing is an umbrella term – it takes the principles of sustainability, as detailed above, and applies them to the world of financial investment. Investing can be thought of as the allocation of one's resources (generally money) towards something (generally businesses in the form of equity and/or debt, though it can also be governments and tangible assets) with the expectation that the allocation of said resource will grow beyond its initial principal value and that growth can be realized as profit. Sustainable investing thus ensures that the initial allocation of one's resources is put towards something that does not jeopardize future generations' wellbeing while still garnering profit for the investor. Today, there are roughly three types of sustainable investment strategies ranging from profit driven to sustainably driven: Environmental, Social, and Governance (ESG) investing, Socially Responsible Investing (SRI), and Impact Investing.

[1] Sustainability. United Nations. https://www.un.org/en/academic-impact/sustainability

Traditional Investing & Philanthropy

Traditional investing and philanthropy oppose each other regarding the expectation of profits. Traditional investing solely aims to generate consistent and predictable returns for the investor over an extended time horizon. Conversely, individuals engaging in philanthropic endeavors do so without expectations of a monetary return. Rather, the investor is providing capital to projects dedicated to making concrete change. Return for a traditional investor is seen in the value of their portfolio whereas return for a philanthropist is the furthering of a selected cause. Notably, traditional investing and philanthropy are not mutually exclusive; one can engage in both forms of investing – as well as the three detailed below.

TRADITIONAL INVESTING	Maximize financial return
ESG	Financial focus with value guardrails
SRI	Balance financial returns & social outcomes
IMPACT INVESTING	Focus on social outcomes with financial returns second
PHILANTHROPHY	Maximize social outcomes

Environment, Social and Governance Investing

Environment, Social, and Governance investing, or ESG, has come to be one of the more popular strategies for institutional and retail investors alike. ESG uses a method of *positive screening* on companies and businesses to tell investors how sustainable said companies are concerning environmental (e.g. how much the company pollutes, amount/type of energy usage), social (e.g. business regulations, product integrity) and governance (e.g. executive pay, shareholder rights) issues.

Positive screening means all companies are given ESG scores, and those that prove to be most responsible in the three ESG domains receive higher scores. The goal of ESG investing is to align one's values with their investments without sacrificing returns.

Socially Responsible Investing

Socially Responsible Investing (SRI) is geared more towards the retail investor as the specific SRI strategy is unique to the investor. Differing from ESG investing, SRI uses negative screening – the investor creates a list of criteria of which they do not want to invest. For example, an SRI strategy could be used to construct a portfolio which completely excludes any company/fund that creates/distributes/invests in alcohol, tobacco, or arms. The goal of SRI is first to ensure an investor's money is not connected to unsustainable practices they have chosen with return on their investment as a secondary goal.

Impact Investing

Impact Investing, as opposed to ESG or SRI, is primarily concerned with creating a sustainable change (hence *impact*). While Impact Investing can be conducted in traditional financial markets, it can also be conducted through direct investment into tangible items or projects. For example, contributing money to one's city's green infrastructure project could be considered Impact Investing as more efficient infrastructure leads to higher productivity and thus profits. The goal of Impact Investing is to monetarily contribute to direct sustainable action/businesses while hoping for a profit.

HISTORY

While a relatively new investment strategy, it is difficult to pin down the gensis of sustainable investing. Perhaps the earliest semblance of modern sustainable investing can be traced back to the Methodist church, with John Wesley's *The Use of Money* (1744) [2] sermon encouraging his congregation "not to gain money at the expense of life, nor at the expense of health." [3] Concurrently, the Quakers avoided financing of tobacco and arms companies and refused to participate in the slave trade. While this is not an endorsement of a zero-carbon mutual fund (the concepts of both carbon and mutual funds were yet known to the world), it does outline the underlying principle of sustainable investing: align your money with your morals.

Fast forward nearly two and a half centuries, and the first modern form can be seen in the mid-1960s during the Vietnam War. Widespread dissent for the conflict led to the first sustainable fund in 1971: the World Pax Fund. This fund allowed investors to divest from the war, ensuring that their money was not going to companies that profited from the ongoing violence. In the following decade, corporations, schools, and states divested from the South African apartheid regime due to ethical concerns, continuing the new trend of active investment away from corporations/states acting unethically. [3]

As sustainable investing grew in popularity and practice, the US Sustainable Investment Forum (US SIF) aggregated all sustainable investments in 1995. At this point, sustainable investments made up $639 billion worth of market capitalization. Two years later, the Global Reporting Initiative was created to report on the sustainability of companies. This marked shift towards sustainable investing in the mid-90s indicated both institutional and individuals' drive to invest not only for profit, but for their own values.

At the turn of the twenty-first century, the United Nations held the Millennium Summit. Here, eight Millennium Development Goals, or MDGs, were articulated and set out to be achieved by 2015. These goals ranged from the eradication of extreme poverty and hunger to global partnership for development.

[2] Wesley, John. (1744). *The Use of Money.*

[3] Raden, Jake. (2025). A Brief History of Sustainable Investing. https://www.chase.com/personal/investments/learning-and-insights/article/a-brief-history-of-sustainable-investing

While not specifically tied to sustainable investing, MDGs laid the landscape for humanitarian issues to be combatted. Four years later, the 2004 report *Who Cares Wins* written by the Global Compact in conjunction with the Swiss Federal Department of Foreign Affairs and the United Nations consisted of “recommendations of the financial industry to better integrate environmental, social and governance issues in analysis, asset management and security brokerage.” [4] This report was the first piece of financial literature to enumerate the principles of ESG investing. Evidently, *Who Cares Wins* serves as a landmark development in modern sustainable investing.

Today, ESG remains one of the more popular sustainable investing strategies. This is how it works: independent rating entities, such as Morgan Stanley Capital International (MSCI), Sustainalytics (owned by Morningstar), and As You Sow rank companies based on their own proprietary rating methodologies. Though different among rating entities, they capture similar insights – how environmentally friendly companies are, how they interact with consumers and their product reliability, and how the companies are internally structured. ESG rating entities also screen for potential risks in companies. For example, companies heavily invested in stranded assets (assets that prematurely lose much of their economic value and/or become liabilities within their “useful” lifespan - e.g. coal) would score lower than companies with stable assets. Given these ratings, investors can individually pick companies based on their ESG rating, and/or can invest in ESG oriented mutual funds / exchange traded funds.

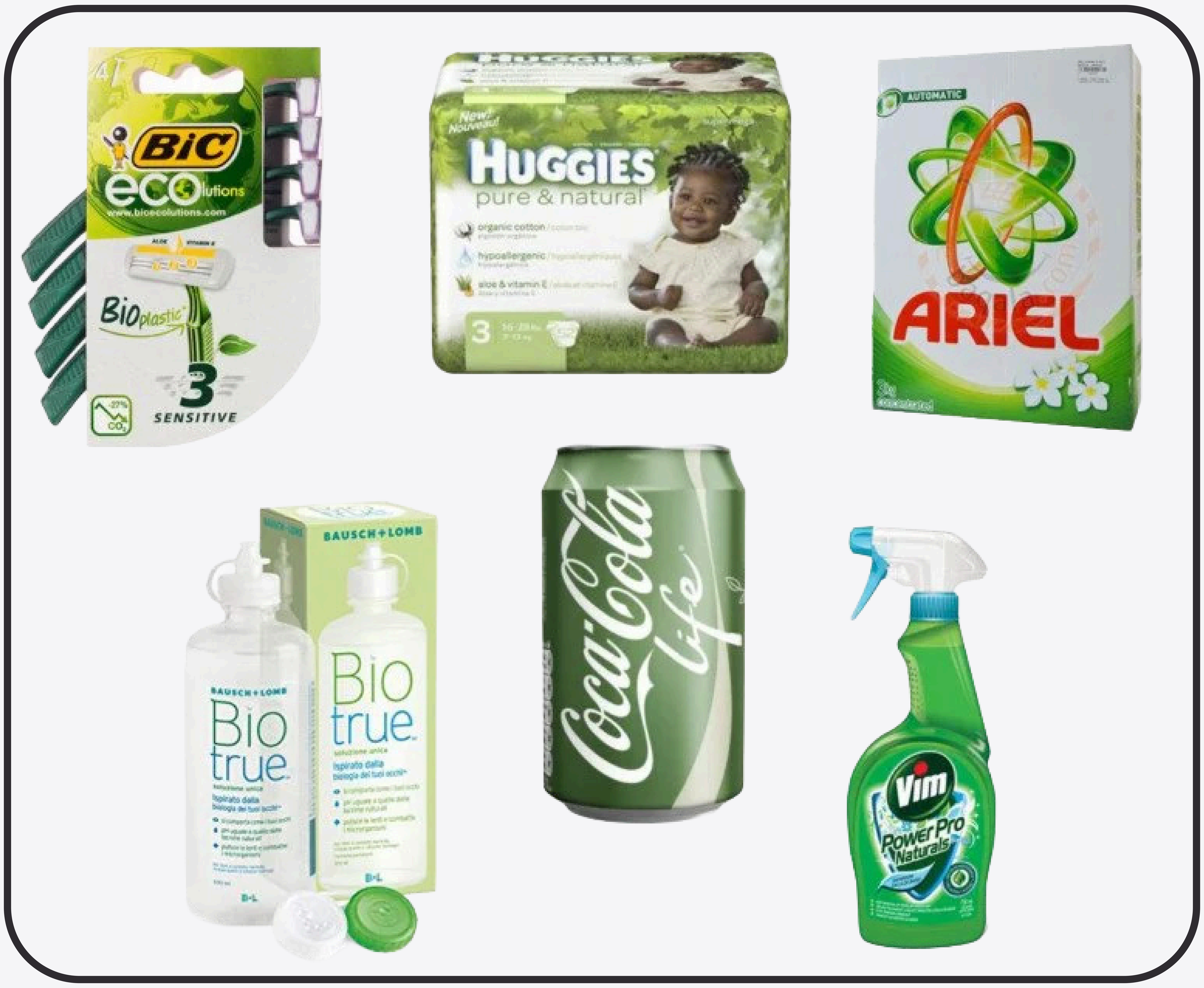
Greenwashing

Sustainable investing’s draw to socially conscious investors has also created an opportunity for companies, fund managers, and even governments to label investments as “green” as a form of marketing rather than a genuine effort towards sustainability. A hypothetical example of this could be a company offering a “sustainable” version of their product while the vast majority of their sales are through unsustainable means (e.g. a coffee company who offers a line of free-trade beans but continues to sell and profit most from unethically harvested products).

[4] Who Cares Wins. (2004). The Global Compact.

An even simpler and everyday example are plastic water bottle companies whose packaging depicts lush wilderness and crystal-clear lakes. Faux environmentalism plays better with consumers than a polluted waterway full of single-use plastic, even though the product itself contributes more to the latter than the former.

Greenwashing can be best understood as a marketing strategy: it’s far easier for a company to simply say they are green than implement green processes across the board. Luckily for investors, information on companies and their practices is more easily accessible than ever. Third parties like non-governmental organizations (NGOs) and even governments themselves can help hold private organizations accountable for mis-marketing and elucidating unsustainable practices that would have otherwise gone unchecked. If having an ESG focus is part of your investment strategy, then looking for potential greenwashing should be considered as part of your financial due diligence.



Examples of "greenwashed" products

WHAT IT MEANS FOR YOU

Put simply: ESG allows one to invest i*n accordance with their principles without sacrificing financial returns*. With this said, it is still essential that the chosen positions in one's portfolio are intentional and calculated. Below an example of an ESG rating methodology is presented, including ESG funds with their respective scores, followed by a discussion and comparison of returns of sample ESG and traditional funds.

SCORING METHODOLOGY: AS YOU SOW	DOMESTIC		INTERNATIONAL	
	ESG	NON ESG	ESG	NON ESG
	PARNASSUS VALUE EQUITY FUND	VANGUARD VALUE INDEX FUND	IMPAX INTERNATIONAL SUSTAINABLE	VANGUARD TOTAL INTERNATIONAL
FOSSIL FUELS	B	F	C	F
DEFORESTATION	B	C	C	D
GENDER EQUALITY	A	B	A	C
CIVILIAN FIREARMS	B	D	A	C
PRISON INDUSTRIAL COMPLEX	D	F	B	F
MILITARY WEAPONS	A	F	D	F
TOBACCO	B	F	B	D

Scoring Agencies' Methodologies

As You Sow offers ESG-oriented individuals a comprehensive and accessible rating system. Utilizing public information, the organization grades A – F on seven categories: fossil fuels, deforestation, gender equality, civilian firearms, prison industrial complex, military weapons, and tobacco. While not necessarily oriented towards advisor research, As You Sow enables individuals to become actively aware of the ESG leanings of their holdings. The table above compares traditional funds to their sustainable counterparts using *As You Sow* metrics.

Given the inherent diversified architecture of funds themselves, it is unlikely that a singular fund will scores "As" across the board. However, the two ESG-oriented funds above show that financial products are available which capture similar market capitalization and investment styles, and offer a greener alternative to their traditional counterparts.

ESG vs Traditional Funds: A Comparison

When discussing returns of traditional versus ESG funds, it would be unwise to blanketly posit that one outperforms the other. Factors such as time horizon, what one considers “green” in the first place, and the sage wisdom that “past performance does not predict future returns” all come into play.

DOMESTIC U.S. LARGE CAP	ESG PARNASSUS CORE EQUITY	NON ESG VANGUARD TOTAL STOCK	DIFFERENCE PARNASSUS - VANGUARD
YEAR TO DATE	7.24%	5.56%	1.68%
1 YEAR	13.58%	15.08%	-1.50%
5 YEARS	15.54%	15.87%	-0.33%
10 YEARS	13.16%	12.90%	0.26%
EXPENSE RATIO	0.61%	0.03%	0.58%

INTERNATIONAL NON-U.S. LARGE CAP	ESG IMPAX INTERNATIONAL SUSTAINABLE EQUITY	NON ESG VANGUARD TOTAL INTERNATIONAL STOCK	NON ESG DIFFERENCE IMPAX - VANGUARD
YEAR TO DATE	19.86%	18.45%	1.41%
1 YEAR	17.28%	18.24%	-0.96%
5 YEARS	10.57%	10.41%	0.16%
10 YEARS	6.47%	6.31%	0.16%
EXPENSE RATIO	0.45%	0.05%	0.40%

Sourced from Morningstar Direct, as of June 30, 2025.
10 yr starts 1/1/2015, 5 yr starts 1/1/2020, 1 yr starts 1/1/2024, all end 6/30/2024

The tables to the left compile trailing returns (annualized historical returns for periods longer than one year) for four widely held funds: two ESG focused and two traditional. As seen, performance varies more widely over shorter periods, such as the 6-month and one-year periods displayed. But over the longer term, it is reasonable to expect comparable performance between ESG and traditional funds. In our example, ESG demonstrates slightly better long-term performance: 0.26 percentage points annually over the 10-year period for the Domestic U.S. Large Cap fund, and 0.16 percentage points annually for the International Large Cap fund.

It is worth noting that the actively managed ESG mutual funds in this example have higher costs, as demonstrated by the expense ratio. For the Domestic U.S. fund, the expense ratio is 0.58 percentage points higher, and for the International fund it is 0.40 percentage points higher. This annual “cost drag” is included in the performance statistics referenced above (performance is “net of fees”).

RETURNS: GLOBAL ESG EQUITY VS. GLOBAL NON-ESG EQUITY INDEX

RETURN PERIOD	ESG EQUITY MSCI ACWI ESG LEADERS INDEX	NON ESG EQUITY MSCI ACWI INDEX	DIFFERENCE ESG - NON ESG
1 YEAR	16.85%	17.49%	-0.64%
5 YEAR	10.03%	10.06%	-0.03%
10 YEARS	9.29%	9.23%	0.06%

Source: Morningstar Direct, January 2015 to December 2024
Time Periods: 10 year 1/1/15 - 12/31/24, 5 year 1/1/2020 - 12/31/2024, 1 Year 1/1/2024 - 12/31/2024

RISK: GLOBAL ESG EQUITY VS. GLOBAL NON-ESG EQUITY INDEX

STD. DEV PERIOD	ESG EQUITY MSCI ACWI ESG LEADERS INDEX	NON ESG EQUITY MSCI ACWI INDEX	DIFFERENCE ESG - NON ESG
1 YEAR	9.72%	9.17%	0.55%
5 YEAR	17.42	17.48%	-0.06%
10 YEARS	14.68%	14.84%	-0.16%

Source: Morningstar Direct, January 2015 to December 2024
Time Periods: 10 year 1/1/15 - 12/31/24, 5 year 1/1/2020 - 12/31/2024, 1 Year 1/1/2024 - 12/31/2024

The two US and two International funds were chosen as they serve to represent both the domestic and international markets as a whole and both have longer tenors. Many ESG funds have less than a decade of performance history, whereas it’s possible to find traditional funds that have been on the market for twenty years or more.

The next set of tables tells a similar story with respect to returns, along with corresponding risk data. The tables utilize data from indexes, which are groups of securities compiled for benchmarking purposes.

In the tables above, we see that returns were lower, and risk was higher, for the ESG index in the 1-year period.

Over the longer term, though, the ESG Equity Index produced a slight performance advantage: 0.06 percentage points when compared to the Non-ESG Index over the 10-year period. And, the ESG Equity index delivered these long-term results with less risk. The standard deviation of returns for the ESG Equity Index was 0.16 percentage points lower than the Non-ESG Index. Standard deviation measures the variation of return around the average – or volatility – and volatility is one way to think about risk. With an index or investment that has lower volatility, one would expect more consistent returns (smaller return "swings") over time.

This data leads us to conclude that individuals utilizing a sustainable investing approach employing ESG-focused funds need not sacrifice returns over the long term. Also, ESG-oriented investors might reasonably expect that portfolios using a sustainable investing approach may deliver long-term returns with a similar level of risk (or perhaps even less risk) when compared to portfolios with similar exposures that rely on traditional investment strategies.

Recent Trends

Interest in sustainable investing is not impervious to the broader geopolitical climate. With the current administration's commitment to roll back environmental regulations and push for traditional sources of energy, [5] little should be expected of government-directed sustainably oriented energy and infrastructure projects in the near term. Further, as the "hype" surrounding ESG investing has died down, investors have raised serious questions about the prolonged efficacy of both exceeding (if not matching) traditional investment strategy returns as well as the measurable impact of green investing. In the United States, the first three months of 2025 marked the 10th consecutive quarter of sustainable investing outflows from the market. [6]

All this said, it is not fair to say that sustainable investing is a "fad" or "trend." Rather, this drawback can likely be attributed to both the volatile global political climate and the realization by investors that ESG is not a catchall solution to externality problems but must be accounted for and deployed intentionally. A recent survey by BNP Paribas indicated that 87% of institutional investors "say their ESG and sustainability objectives remain unchanged, while 84% believe the pace of progress of sustainability is either going to continue or accelerate between now and 2030." [7] The picture we are trying to paint is that ESG is not a magical investment tool, but it can bring peace of mind in terms of aligning your money with your values without sacrificing financial return.

[5] Trump, D. (2025, April). Protecting American Energy from State Overreach. The White House. https://www.whitehouse.gov/presidential-actions/2025/04/protecting-american-energy-from-state-overreach/

[6] Morningstar Inc. (2025, May). Investors Turn Away from ESG Funds in Record Numbers in Q1 2025. https://global.morningstar.com/en-gb/sustainable-investing/investors-turn-away-esg-funds-record-numbers-q1-2025

[7] BNP Paribas. (2025, May). Institutional Investors Remian Committed to Sustainable Investing. https://securities.cib.bnpparibas/bnp-paribas-esg-survey-2025-press-release/

FINAL THOUGHTS

Sustainable investing allows investors to align their values with their financial goals. The challenges that sustainable investing aims to account for are not only pressing and pertinent, but will persist unless an intentional, global strategy is implemented to combat them. Incorporating ESG strategies thus allows you to ensure that your money is working responsibly. Put simply: sustainability efforts are not fads insofar as climate change, corporate governance responsibility, and equity and equality are not fads. Sustainable investing allows one to square their money with their morals.

IMPORTANT INFORMATION