WELLS FARGO
Investment Institute

Sustainable Investing

Investing with a purpose

April **2020**

"Goodness is the only investment that never fails."

—Henry David Thoreau

What's inside

Aligning investments with values

Sustainable investing is gaining popularity as investors increasingly seek to align their investments with their personal values. One way to accomplish this goal is to use an investment approach that focuses on environmental, social, and governance (ESG) criteria. An ESG lens may consider issues such as climate change, pollution control, gender equality and diversity, human rights, or corporate board composition.

A common misconception is that sustainable investing—including ESG-driven strategies—imposes hurdles on performance. To the contrary, studies of longer-term historical performance suggest that ESG strategies have performed similarly to comparable traditional investments on an absolute basis and a risk-adjusted basis.[1] Yet, sustainable investment strategies do come with risks, like any investment.

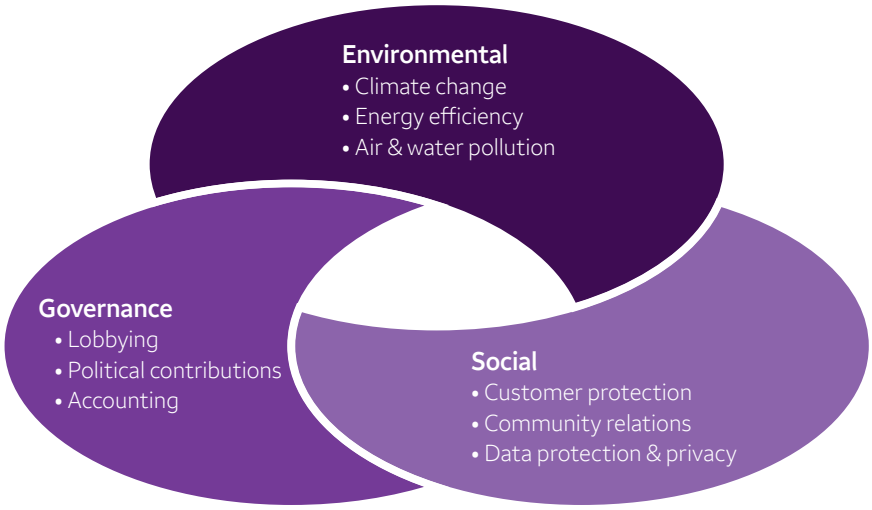
We expect that sustainable investment choices available for investors likely will continue to expand. In fact, some analysts predict that ESG factors could become a normal consideration of most investment strategies, particularly those intended for younger investors who tend to expect greater transparency from their investments.

Sustainable investing

- **ESG analysis**
  Seeks to manage risk by the ***integration*** of ESG factors that influence both financial performance and society at large.
- **Socially responsible investing**
  Seeks to avoid industries and companies that are not in ***alignment*** with an investor's values primarily through exclusions.
- **Impact investing**
  Intends to generate an identifiable and measurable ***impact***, in addition to a financial return.

The sustainable investing landscape

Environmental, social, and governance factors are often intertwined.



Key questions we answer in this report

Does sustainable investing forgo profit for principle?

What ESG factors appeal to today's investors?

How do investors implement a sustainable investing approach?

What challenges and trends do ESG-aware investors face?

1. Journal of Banking and Finance, 2005; Journal of Banking and Finance, 2011; and Journal of Investing, 2011

The evolution of sustainable investing

Today, sustainable investing accounts for about $1 out of every $4 under professional management in the U.S.[2]

Since the 1960s, sustainable investment strategies have shifted from an exclusionary approach to an inclusionary one. Over time, this shift has broadened the supply of investment offerings to meet demand.

A history of aligning assets with values

Investors have exhibited a long history of aligning investment assets with personal values. Philanthropic actions, like charitable giving or venture capital donations, historically have been used to support causes that match an individual's ethics, beliefs, or ideals. These actions typically come without expectation for return on investment. Traditional investing provides the potential for return but may not necessarily align with one's values. Sustainable investing strategies date back to the 1960s, offering investors the return potential of traditional investing and the opportunity to align investments with values.

Interest in sustainable investing began to accelerate in the 2000s. According to a recent study, assets in these types of investments grew by an estimated 38% from 2016 to 2018 in the U.S., rising from $8.7 trillion in 2016 to $12 trillion in 2018. Globally, sustainable investments total $23 trillion, which represents 26% of all professionally managed assets.[3] This has increased from 21.5% of professionally managed assets just four years ago. Investor demand has been a key driver for this, and we expect that growth to continue.

Sustainable investing strategies can provide the best of both worlds

Sustainable investing strategies can offer investors the return potential of traditional investing *and* the opportunity to align investments with values.

Potential for financial return				
Traditional investing	Potential for social/community benefit			
	ESG investing	Impact investing	Socially responsible investing	Philanthropy
• Strategies designed to maximize returns for a given level of risk	• Integration of environmental, social, or governance factors	• Aims to make a measurable impact while providing potential return • Can include green bonds	• Aims to avoid what doesn't align with values	Can include • Grants • Charitable donations • Donor-advised funds • Venture capital donations • Social enterprises

2. *The Impact of Sustainable and Responsible Investment, October 2018*
3. *McKinsey & Company, "From 'Why' to 'Why Not': Sustainable Investing as the New Normal," October 2017*

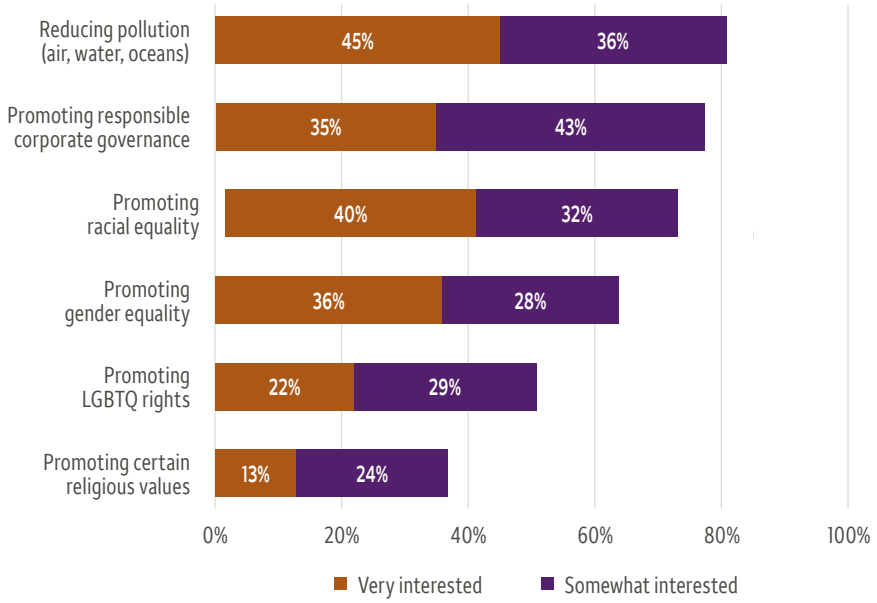
A closer look at sustainable investing

Proponents of sustainable investing tend to take a holistic view of both risk and return. For example, ESG-driven investors might believe that focusing on companies that place a high value on their employees will tend to result in fewer lawsuits and improved employee retention over long periods.

While environmental issues can, at times, dominate perceptions and discussions related to sustainable investing, there is far more to sustainable investing, and ESG, than the environmental factor. Even the word "sustainable" is often misconstrued as referring exclusively to the environment, when in its broader sense it can also refer to practices that help create and maintain a more equitable and inclusive society. When asked about which issues have the strongest impact on their investment decisions, it's true that many consumers highlighted environmental issues like reducing pollution and protecting the environment. However, social issues—such as humane working conditions or gender equality—and governance issues—including business practices and financial transparency—are viewed as equally important.[4]

Factors that interest investors

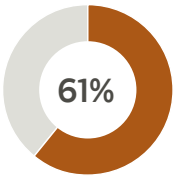
In a 2020 Wells Fargo/Gallup investor poll, investors expressed their level of interest in the following themes.



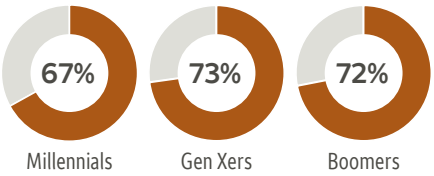
Source: *Wells Fargo/Gallup Investor and Retirement Survey, February 2020. Question format: How likely are you to invest in funds that are focused on each of the following issues or goals? very interested, somewhat interested, not too interested, or not interested at all*

4. *The Wells Fargo/Gallup Investor and Retirement Optimism Index poll was conducted online February 10–16 using the Gallup Panel, a probability-based longitudinal panel of U.S. adults. The results are based on 1,029 investors aged 18+ with $10,000 or more invested in stocks or bonds, either individually or as part of a retirement or mutual fund.*

Sustainable investing supply and demand



61% of Millennials indicate that they are interested in having some money in sustainable investments, and about half of Baby Boomers and Generation Xers expressed interest as well.[6]



73% of Generation Xers surveyed said that they are likely to invest in companies that align with their values, while 67% of Millennials and 72% of Baby Boomers feel the same.[7]

Retail demand crosses generations

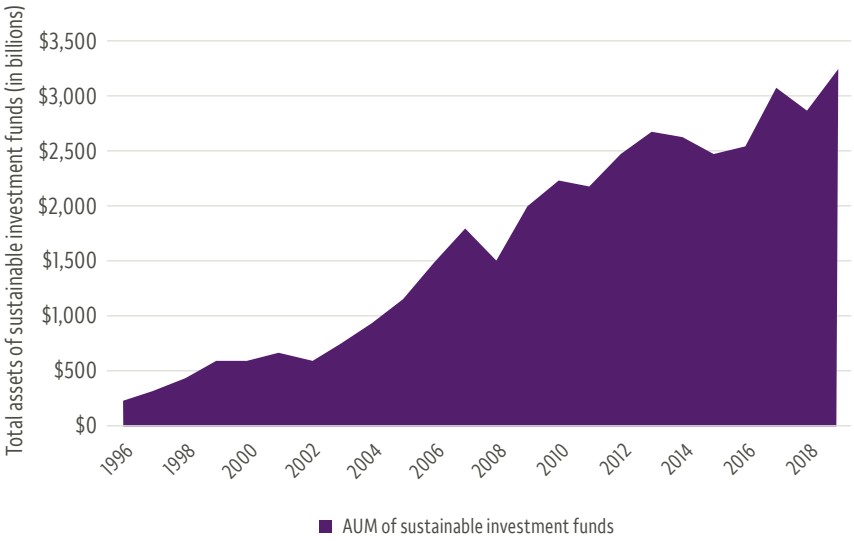
Investor demand has been a key growth driver for sustainable investment strategies, and managers have risen to the challenge. The number of sustainable funds approximately doubled from 2009 to 2019, although some of this growth can be attributed to existing funds that have added ESG factors to their list of investment considerations.

A common misconception is that this demand is mainly driven by younger investors. Yet, research suggests that investors across generations are interested in sustainable investing. Millennials are apt to discuss sustainable investing with their financial advisors, but the other generational cohorts also have an interest in the approach.

A 2020 Wells Fargo/Gallup survey found that 82% of surveyed investors showed interest in choosing investments based on the environment, human rights, diversity, and other social issues—if those investments provided returns similar to the market average. Additionally, 69% of investors would choose to use these types of investments in their retirement accounts if they were given the option to do so.[5] If the gap in perception between those interested in sustainable investing and those already invested in these funds starts to close, the demand could grow even faster than its current pace.

The rise of sustainable investing

Sustainable investment assets under management have doubled since 2007.



Sources: *Morningstar Direct and Wells Fargo Investment Institute, as of September 30, 2019. AUM = assets under management*

5. *Wells Fargo/Gallup Investor and Retirement Survey, February 2020*
6. *Ibid.*
7. *Ibid.*

More companies are incorporating ESG factors

Beyond the interest of individual and institutional investors in sustainable investing, corporations are finding added value when they incorporate this focus into their business practices. Moreover, incorporating ESG factors could potentially help reduce operational expenses and improve the bottom line.[8] Today, nearly 60% of U.S. institutional investors view ESG analysis as a fiduciary responsibility beyond meeting individual investors' interests.[9]

The advantages of considering ESG factors extend beyond the U.S. border. In Europe, regulations—largely from the European Commission's action plan on sustainable finance—encourage companies to become ESG compliant. Fund managers are required to inform the European Commission how their activities could affect the environment. In the U.K., the Department for Work and Pensions requires its members to disclose risks of their investments, including risk exposures related to ESG considerations.[10] Adhering to these requirements may increase transparency in ESG-related disclosures. Many CEOs in China and Hong Kong view ESG as a way to enhance corporate reputation and brand image while also improving financial performance and reducing costs through resource efficiency and improved long-term risk monitoring.[11]

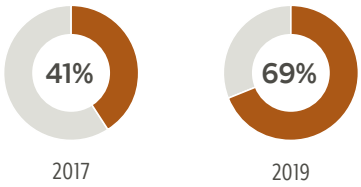
Benefits of sustainable investing

Sustainable investing offers several important benefits, including:

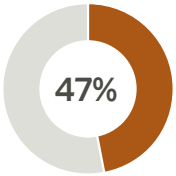
Contributing to positive change	Investors can help contribute to positive change by investing in companies whose business practices are more compatible with their values.
Complementing philanthropy	While contributions to a single nonprofit can be significant on a local level, investing in ways that align your philanthropic and investment interests can help generate a more global impact.
Involving family and fostering legacy decisions	Aligning investment decisions with values can add to important conversations and considerations related to a family's values, vision, and desired goals and legacy and can guide a family toward shared objectives.

Growth in ESG discussions

Percentage of financial advisors who report speaking to clients about ESG



Source: Ignites Research, 2019



47% of investors say that not knowing enough about sustainable investing funds is a major reason they don't currently invest in them. Fortunately, more advisors are starting to talk to clients about sustainable investing.

Source: Wells Fargo/Gallup Investor and Retirement Survey, February 2020

8. *McKinsey & Company, Five Ways That ESG Creates Value, November 2019*
9. *State Street Global Advisors, Into the Mainstream: ESG at the Tipping Point, November 2019*
10. *BNP Paribas, ESG Global Survey 2019, May 2019*
11. *State Street Global Advisors, Into the Mainstream: ESG at the Tipping Point, November 2019*

Doing well while doing good

Our research indicates that investors do not need to forgo return potential to align their portfolios with their values.

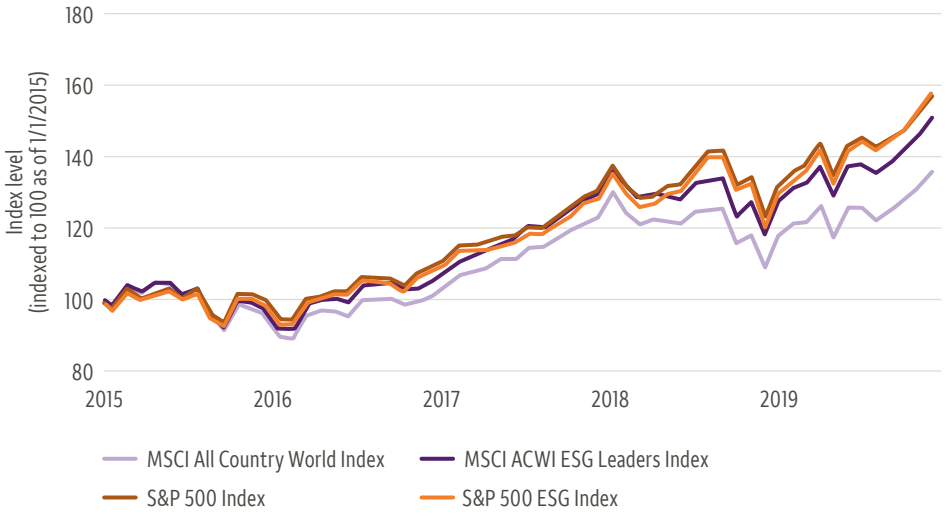
You don't have to trade profits for principles

One misconception is that investors must sacrifice performance to align portfolios with their values. A 2020 Wells Fargo/Gallup survey showed that only 11% of those surveyed already invest in sustainable investments, despite widespread interest.[12] This discrepancy may stem from the misconception that these strategies underperform the market. Only one-third of those surveyed believed that sustainable investments match or outperform the market, on average.

Our research indicates that investors do not need to forgo return potential to align their portfolios with their values. To the contrary, a growing body of evidence suggests that financial performance of companies using ESG strategies is commensurate with those that do not.[13] Moreover, as shown in the graphic below, adjusting for certain fundamental differences such as style and sector, U.S. ESG stocks showed comparable returns to those of other U.S. stocks.

ESG-related stocks have tended to keep pace

Our research has shown that ESG-related stocks have shown comparable returns to non-ESG-related stocks over time, adjusting for fundamental differences such as style and sector.



Sources: Bloomberg and Wells Fargo Investment Institute, as of December 31, 2019. ***Past performance is no guarantee of future results.*** *An index is unmanaged and not available for direct investment.*

Please see the end of this report for the definitions of indices and descriptions of asset-class risks.

12. Wells Fargo/Gallup Investor and Retirement Survey, February 2020

13. In fact, more than 90% of the 2,200 individual studies reviewed by the Journal of Sustainable Finance & Investment have shown a nonnegative relationship between ESG and corporate financial performance, with a majority of findings showing positive results

Company data—quality and quantity

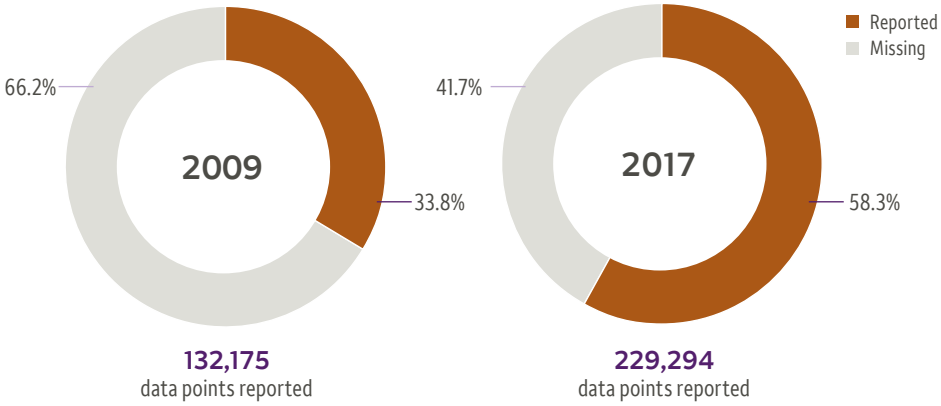
ESG-related reporting has helped increase transparency and sophistication in research and security selection. It is now possible for dedicated managers to fully integrate ESG factors into each step of the security selection, investment, and portfolio construction process.

Yet, despite an increase in available data, the underlying quality of and lack of consistency in the data can be problematic—there is no designated regulatory body to set these reporting standards. This lack of oversight for ESG-focused funds can pose challenges for investors. Recently, the Sustainability Accounting Standards Board published a set of industry-specific accounting standards. These standards allow companies and investors to consider codified, market-based criteria to measure, manage, and report sustainability standards. But there is still work to be done in standardizing oversight.

Until more regulation is in place that sets clear standards in this investment space, we believe that it is important for investors to understand the various levels of ESG factor implementation and engagement before making their investment choices. (See our classification system on the next page.)

Reported ESG data points continue to grow

In a sign of companies' growing willingness to provide ESG-related data, the percentage of data points that companies reported grew significantly between 2009 and 2017.



Sources: *BlackRock Sustainable Investing and BlackRock Investment Institute, with data from MSCI, December 2018. ESG data points include 150 key metrics used by MSCI in its ESG corporate ratings system. A company reporting a given key metric at least once in a given year is considered one data point. The total number of potential data points are calculated by multiplying the number of companies in the MSCI ACWI (2,607 in 2009 and 2,622 in 2018) by 150. The darkest portion of each ring shows the share of those data points that were actually reported by companies.*

Our approach to ESG transparency

We employ a top-down and forward-looking approach to identify the intentionality of a manager to incorporate financially material ESG analysis.

For more information see Wells Fargo Investment Institute's new ESG transparency categories report.

A five-category analysis of ESG managers

To respond to demands for increasing clarity around ESG-related considerations and implications of the investment decisions and products, we have created a proprietary ESG Analysis Assessment Framework. The Framework builds ESG considerations into our standard due diligence process. The criteria begins with a qualitative assessment of the investment management firm but ultimately focuses on the implementation approach used by specific investment/portfolio managers and products.[14]

1

Immaterial or not applicable

- No or minimal consideration of ESG factors
- ESG analysis may not be applicable to the investment process

2

Aware

- Some consideration of ESG factors (all three)
- The manager can speak to broad ESG themes and how they relate to the portfolio
- ESG analysis is primarily a risk mitigation tool and not a driver of idea generation

3

Integrated

- ESG analysis is a key part of the investment process
- The manager can speak to granular ESG themes and focuses on materiality
- ESG analysis is a risk mitigation tool and one component of idea generation

4

Key driver

- ESG analysis is a key element of the investment process, including idea generation
- Likely there is an individual or team dedicated to ESG analysis
- There is a fully incorporated proprietary ESG scoring methodology

5

Impact leader

- Leader in positive impact and pioneer in ESG analysis and application
- "Impact" could include, but should not be limited to, selective investment, encouraged divestment, proxy voting, direct company engagement, and collaborative sustainability efforts
- Actively work to improve the ESG profile of companies held in the portfolio

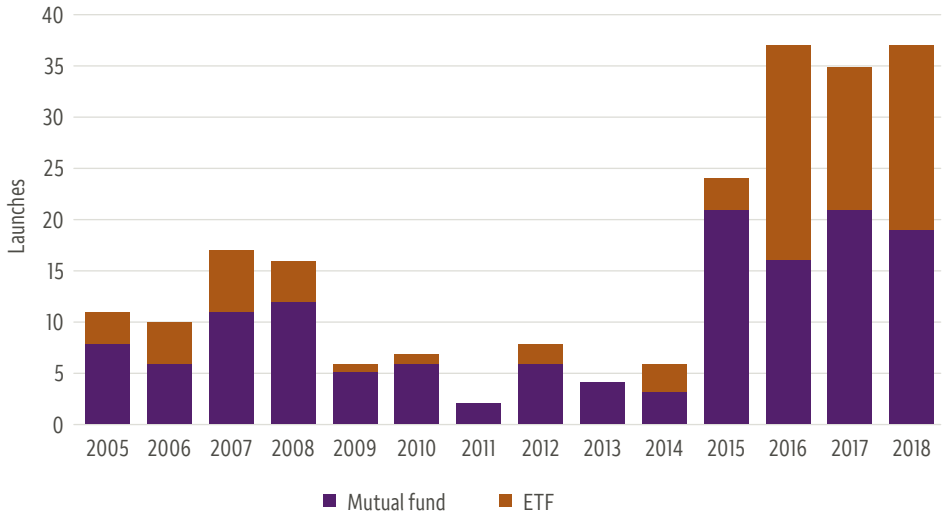
14. Wells Fargo Investment Institute, "How Much ESG is Really in Your Portfolio?" April 13, 2020

Aligning your investments with your values—investor implications

Sustainable investment strategies and vehicles—for example, exchange-traded funds (ETFs) and mutual funds—historically have been associated with a more active investing approach, but broadly diversified passive approaches that systematically tilt portfolios away from certain industries/companies and toward others can also be incorporated into overall solutions. We believe that combining our approach to ESG analysis with traditional portfolio management concepts such as diversification, relative expenses, tax considerations, and risk-adjusted returns can help generate sustainable performance for investors.

ESG fund launches by year

Once largely the province of actively managed mutual funds, the ESG space now includes passively managed portfolios among both funds and ETFs. Sustainable investing can accommodate a wider range of investor preferences.



Sources: *Morningstar Direct and Wells Fargo Investment Institute, as of December 31, 2018*

ESG-focused investment opportunities

- **Green bonds** enable capital raising and investment for new and existing projects with environmental benefits. With total estimated issues above $300 billion in 2019—and projected to rise to $400 billion in 2020[15] —green bonds are a growing niche in the fixed-income market.
- **Social impact bonds,** first launched in 2010, are contracts between a special purpose vehicle and the government, in which the government continues to support improved social outcomes.
- **Impact investing in private equity vehicles** offers diverse opportunities for qualified investors to potentially earn competitive returns and achieve measurable social benefits. These funds are typically driven by mission-focused entrepreneurs who launch initiatives to tackle global challenges. We favor three impact investment themes: health and wellness, education and workforce development, and sustainability.[16]

15. Moody's Investors Service, Sustainable Finance – Global Sector In-Depth, February 3, 2020
16. "Investing for Social and Environmental Impact," WFII, November 4, 2019

The future of sustainable investing—challenges and trends

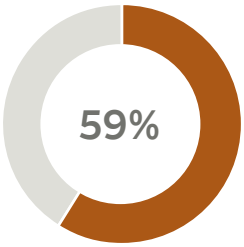
Notable challenges

Despite the recent growth in demand for sustainable investments, there are still a number of challenges and barriers to widespread adoption, including a lack of standardized terminology, uniformity in data collection, and oversight and accountability. A joint survey by the United Nations (UN) and CFA Institute showed that 43% of U.S. investors cited a lack of historical ESG performance data and 41% cited limited understanding of ESG issues as the top barriers to adoption.[17]

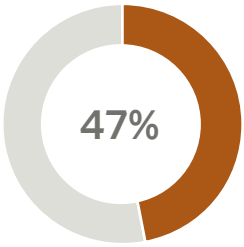
Lack of standardized terminology: Definitions of sustainable, responsible, or impact investing can vary widely from firm to firm. For instance, the acronym "SRI" could mean socially responsible investing or it could mean sustainable, responsible, and impact investing.

A 2017 CFA Institute survey indicates that investor confusion is a key reason for fund managers not to consider ESG-related issues in their analysis. Yet, 73% of respondents in this same survey take ESG issues into account in their analysis and decision-making. Investors' interest in sustainable investing may have grown since 2017, but these types of investments remain perplexing because of the terminology used and a lack of uniformity in security selection standards.

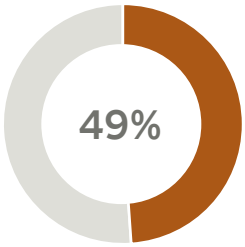
The knowledge gap for sustainable investing is wide today



59% of respondents do not know an ESG approach to saving and investment is even possible



47% would welcome greater support and advice on ESG from their advisors



49% would like their advisors to provide more information on ESG topics

Source: *Vontobel, Drive Positive Change With ESG, September 2019*

17. "ESG Integration in the Americas: Markets, Practices, and Data," CFA Institute and Principles for Responsible Investment (PRI), 2018

Lack of standardization of data: According to *The Wall Street Journal*, "there is often little overlap" in how ESG ratings agencies rate a company. There is more uniformity, however, when ratings agencies such as Moody's Investors Service (Moody's) and Standard & Poor's (S&P) grade the same companies for their creditworthiness.[18]

In fact, MIT researchers recently found that the correlation between five top providers of ESG ratings is 0.61, significantly lower than the correlation between Moody's and S&P for credit ratings of 0.99.[19]

Lack of oversight and accountability: Due to the relatively new advent of most responsible investing strategies, regulatory oversight generally has been lacking. The UN has developed 17 Sustainable Development goals, but adoption is voluntary in most countries. The UN also supports Principles for Responsible Investment, but its six main tenets are self-described as "voluntary and aspirational." Furthermore, a 2018 study by Bain & Co., a consultancy, found that just 2% of companies beat or even achieved their self-stated sustainability goals.

Although sustainable investing faces certain challenges, we believe that these are improving as the industry continues to coalesce. We expect that an eventual convergence of terminology, improved data reporting, and more clear-cut regulatory oversight likely will support demand growth for sustainable investment strategies.

Common sustainable investing terms

Greenwashing is an attempt to capitalize on the growing demand for environmentally sound products. Greenwashing can convey a false impression that an investment manager or fund is environmentally sound. We are attempting to solve this problem with our proprietary methodology.

Transitioning brown companies to green companies is a common phrase for corporations that have policies in place to reduce their carbon footprint and transition to a low-carbon economy.

Certified B Corporations are businesses and social enterprises that balance purpose with profit. They are verified by B Lab[20] and are legally obligated to consider the impact of their decisions on employees, clients, suppliers, the local community, and the environment. The first B Corporations were certified in 2007. Today there are more than 2,400 Certified B Corporations in more than 130 industries and 50 countries.

A donor-advised fund allows donors to make charitable contributions, receive tax benefits, and assist in grant-making. These funds allow donors to make grants anonymously and may establish a legacy of gift giving for the donor. Many donor-advised funds are used to address environmental and social issues.

18. "Why It's so Hard to Be an 'Ethical' Investor," The Wall Street Journal, September 1, 2018
19. Berg, Koelbel, and Rigobon, "Aggregate Confusion: The Divergence of ESG Ratings," August 2019, MIT Sloan Research Paper No. 5822-19
20. https://bcorporation.net

Green accounting

This is an accounting method that attempts to factor environmental costs into the financial results of operations. The aim is to help businesses understand and manage the potential balance between economic and environmental goals.

For ESG investors interested in green accounting, we favor investing in companies that have made commitments to achieving sustainability goals and reducing carbon emissions.

Trends to keep an eye on: Energy, data protection, animal rights

Energy

For the past several decades, the assumption has been that fossil fuels will continue to be the main source of energy, with increases in carbon-intensive assets making it difficult to attain climate goals set by the Paris Agreement. We believe that the trend will be changing to a more clean energy source. Emerging technology, integrated with new policies that limit the use of carbon, likely will take shape over the next several decades.[21] We believe that lower production costs and the opportunity to scale in emerging markets via disruptive technologies will be the main levers to enable a transition to renewable energy sources.

For investors interested in renewable energy, we favor investing in companies that focus on disruptive technologies, such as long-duration batteries, electric vehicles, and wind and solar technology.

Data protection

According to International Data Corporation (IDC), the Internet of Things (IoT) and increased connectivity to the IoT will generate 79.4 zettabytes (10^{21} bytes) of data by 2025.[22] Increased usage of cloud technology and data centers has introduced a new role within firms' C-suites: the Chief Data/Information Officer. A survey of approximately 60 Fortune 1000 firms, conducted by NewVantage Partners, reported that 67.9% have appointed a Chief Data/Information Officer.[23] This indicates a trend of viewing data as an asset, giving rise to the importance of data protection and privacy.

For investors interested in data privacy, we favor investing in companies that have strong data regulation and governance policies in place within the subsectors of data science and analytics.

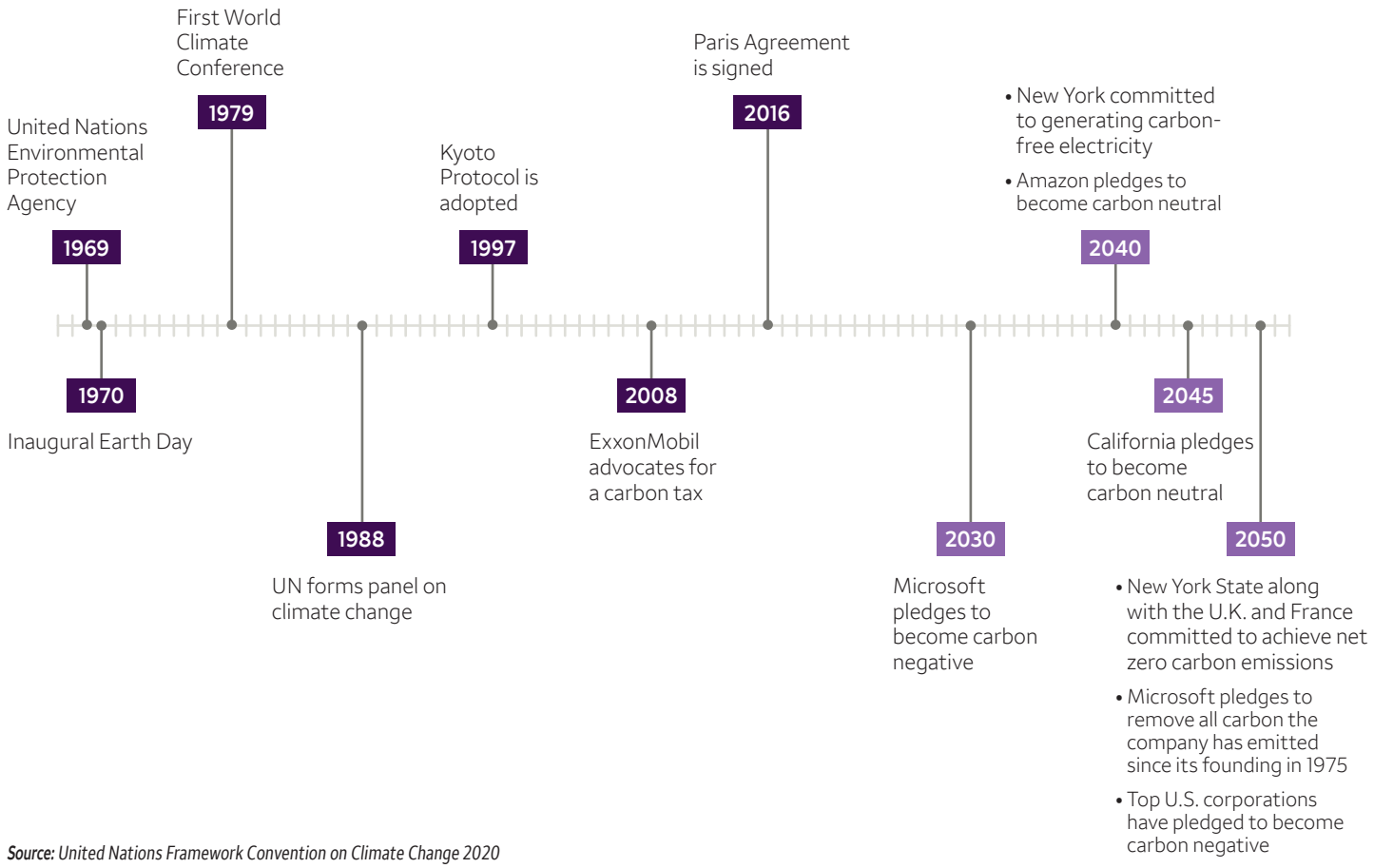
Animal rights

Cruelty-free investing excludes investments in corporations that exploit and abuse animal rights. This methodology avoids corporations that manufacture food, beverage, or clothing containing animal products; use animals for experimentation and testing; and are involved in killing or harming animals.[24]

For investors interested in cruelty-free investing, we favor companies that are advocates for animal rights and create products, such as plant-based proteins, without exploiting or abusing animals.

21. "The Speed of the Energy Transition: Gradual or Rapid Change?" World Economic Forum
22. "The Growth in Connected IoT Devices Is Expected to Generate 79.4ZB of Data in 2025, According to a New IDC Forecast," IDC, August 18, 2019
23. "Big Data and AI Executive Survey 2019," NewVantage Partners, January 2, 2019
24. Crueltyfreeinvesting.org, February 12, 2020

A look back and a look ahead



Source: *United Nations Framework Convention on Climate Change 2020*

Significant milestones

The Kyoto Protocol put into action the United Nations Framework Convention on Climate Change, with participants committing resources to reducing and limiting greenhouse gas emissions. It set binding emission reduction targets for 36 industrialized countries and the European Union.

The Paris Agreement is a global climate effort aimed at combating climate change for a sustainable low carbon future. The intent is to strengthen the global response to the threats of climate change by containing the rise in temperatures well below 2 degrees Celsius (3.6 degrees Fahrenheit).

Growing a sustainable investment strategy

Define goals

Identify issues

- Environmental
- Social
- Governance

Determine objectives

- Satisfy values preference
- Generate financial benefit
- Effect meaningful change

Target sustainable or responsible investing options

Areas of potential focus that help guide the selection of varied sustainable investing options:

- Investors who want to own companies judged to be best in class based on (ESG) practices
- Investors concerned about climate change and environmental pollution
- Investors who want portfolios free of nuclear energy and fossil fuel holdings
- Investors who are concerned about protecting endangered species or wildlife
- Investors who are concerned about social issues like poverty and homelessness
- Investors who seek to align faith-based or religious beliefs with their assets
- Investors who want to avoid companies that conflict with their beliefs
- Investors who are concerned about data privacy and security

Reassess periodically

Are the portfolio holdings still aligned with investors' values?

Sustainability plans for small business owners

If you're a small business owner, the best sustainable investment may begin at home—small businesses can develop these strategies, too. Adopting sustainable small business practices may help boost the bottom line while also protecting the environment. Use these tips to get started:

1. Assess your starting point:

During the beginning stages of planning, assess your company's compliance. Make sure you are aligned with local and federal regulations pertaining to sustainability.

2. Educate yourself and your team:

It's important to educate yourself and your team members on what it means to be a sustainable business.

3. Identify room for improvement:

Identify the opportunities for your business to become more sustainable. Look for actionable practices for your business to implement. Plan how your team can improve and set measurable goals to stay on track.

4. Implement your plan and make real changes:

Communicate the company's sustainability goals with your team, change policies that no longer align, and then measure your progress moving forward.

5. Stay consistent and transparent:

Once you have created a sustainability plan, you can communicate your new sustainable practices to your customers. But be ready to substantiate your claims.

Take the next step

We expect that the popularity of sustainable investing will continue to grow—and that the number of investment choices to meet this demand also will increase. Many investors are taking a broader view of performance, assessing sustainability performance along with risk and return measures. They are learning that they can pursue financial goals while helping improve the broader world.[25] For such investors, the question isn't "Why would I invest this way?" but rather "Why wouldn't I?" We encourage speaking with an investment professional about potential risks and opportunities of these investment strategies that are appropriate for designated investment objectives. Wells Fargo is committed to helping investors meet their interest in sustainable investments.

25. See reports "Can ESG-Focused Investments Benefit Portfolios?" Wells Fargo Investment Institute, December 2019, and "The Alpha, Beta, and Sigma of ESG: Better Beta, Additional Alpha?" Jacobsen, Lee, and Ma, Journal of Portfolio Management, September 2019

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Definitions

The **MSCI All Country World Index (ACWI)** captures large- and mid-cap representation across 23 developed market and 26 emerging market countries.

The **MSCI ACWI ESG Leaders Index** is a capitalization-weighted index that provides exposure to companies with high environmental, social, and governance (ESG) performance relative to their sector peers. The MSCI ACWI ESG Leaders Index consists of large- and mid-cap companies across 23 developed market and 26 emerging market countries.

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The **S&P 500 Index** consists of 500 stocks chosen for market size, liquidity, and industry group representation. It is a market-value-weighted index with each stock's weight in the index proportionate to its market value.

The **S&P 500 ESG Index** is a broad-based, market-cap-weighted index that is designed to measure the performance of securities meeting sustainability criteria while maintaining similar overall industry group weights as the S&P 500 Index.

An index is unmanaged and not available for direct investment.

Risk considerations

All investing involve risks, including the possible loss of principal. There can be no assurance that any investment strategy will be successful. Investments fluctuate with changes in market and economic conditions and in different environments due to numerous factors, some of which may be unpredictable. Each asset class has its own risk and return characteristics. The level of risk associated with a particular investment or asset class generally correlates with the level of return the investment or asset class might achieve.

Sustainable investing focuses on companies that demonstrate adherence to environmental, social, and corporate governance principles, among other values. There is no assurance that social impact investing can be an effective strategy under all market conditions. Different investment styles tend to shift in and out of favor.

The risks associated with the representative index asset classes discussed in this report include: **Stock markets,** especially foreign markets, are volatile. Stock values may fluctuate in response to general economic and market conditions, the prospects of individual companies, and industry sectors. **Foreign investing** has additional risks including those associated with currency fluctuation, political and economic instability, and different accounting standards. These risks are heightened in emerging markets. **Bonds** are subject to market, interest rate, price, credit/default, liquidity, inflation, and other risks. Prices tend to be inversely affected by changes in interest rates.

Alternative investments, such as private equity, are speculative and involve a high degree of risk that is suitable only for those investors who have the financial sophistication and expertise to evaluate the merits and risks of an investment in a fund and for which the fund does not represent a complete investment program. They entail significant risks that can include losses due to leveraging or other speculative investment practices, lack of liquidity, volatility of returns, restrictions on transferring interests in a fund, potential lack of diversification, absence and/or delay of information regarding valuations and pricing, complex tax structures and delays in tax reporting, less regulation, and higher fees than mutual funds. Hedge fund and private capital investing involves other material risks including capital loss and the loss of the entire amount invested. A fund's offering documents should be carefully reviewed prior to investing.

Exchange-traded funds (ETFs) seek investment results that, before expenses, generally correspond to the price and yield of a particular index. There is no assurance that the price and yield performance of the index can be fully matched.

ETFs and mutual funds are subject to substantially the same risks as individual ownership of these securities would entail. Investment returns may fluctuate and are subject to market volatility, so that an investor's shares, when redeemed or sold, may be worth more or less than their original cost.

Donor-advised donors do not receive investment returns. The amount ultimately available for donor-directed grants may be more or less than donor contributions to the donor-advised fund. While annual giving is encouraged, the donor-advised fund should be viewed as a long-term philanthropic program.

Investment expertise and advice to help you succeed financially

Wells Fargo Investment Institute is home to more than 120 investment professionals focused on investment strategy, asset allocation, portfolio management, manager reviews, and alternative investments. Its mission is to deliver timely, actionable advice that can help investors achieve their financial goals.

For assistance with your investment planning or to discuss the points in this report, please talk to your investment professional.

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