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RENAMING WITH PURPOSE: INVESTOR RESPONSE AND FUND MANAGER BEHAVIOUR AFTER FUND ESG RENAMING?

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EXECUTIVE SUMMARY

Over the previous decade, ESG investments exhibited remarkable growth, with record inflows into funds that invest according to environmental, social, and governance criteria. Accompanying this trend, a sizeable number of fund managers rebranded their mutual funds to signal ESG commitments, and they changed their funds' names accordingly. As an illustration, around 250 European funds changed their name and investment policies to include sustainability-related terms in 2020, rising to 536 in 2021 according to Morningstar classifications. In our own global sample, annual ESG renaming rises from just nine occurrences in 2016 to 243 in 2022.

Our interest in this topic at the time of research was motivated by concerns that mutual funds' stated integration of environmental, social and governance (ESG) criteria in investing was cosmetic – i.e., that funds were changing their names to include ESG-related terms merely to attract capital when ESG investing was "hot", without meaningfully changing what sat inside the portfolio. Those concerns had a basis in earlier evidence. Studies in the early 2000s already reported that U.S. mutual funds changed their names to portray investment styles that were hot in the market, without actually changing the styles of their portfolios subsequently.

KEY TAKEAWAYS FOR INVESTMENT PROFESSIONALS

- Fund managers on average do walk the talk: after ESG renaming, portfolios exhibit a higher overall ESG score, less exposure to controversial sectors, lower carbon intensity, and lower sustainability risk.
- Flow-driven incentives to rename are less widespread than previously thought, and are concentrated in Europe rather than the U.S.
- Improvements in portfolio ESG scores are larger for U.S. funds that rename than for European ones, most plausibly because European funds already exhibited a stronger ESG orientation to begin with.
- Fees are generally not materially higher (if not lower) after renaming, with only a subset of European retail funds raising the annual TER by a modest 4.5 basis points.

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More recently, studies of institutional investors that signed the Principles for Responsible Investing found that some enjoyed larger money flows without exhibiting stronger ESG tilts. Not surprisingly, regulators on both sides of the Atlantic were increasingly considering guidelines and policies to ensure that ESG-labelled investments were meaningfully distinctive. Against this backdrop, we set out to test whether ESG renaming was itself a cosmetic exercise, or whether funds that renamed did in fact walk the talk.

Using a global sample of 740 mutual funds that added an ESG-related term to their name between July 2016 and September 2022, we study fund flows, changes in ESG profiles, and expenses. Our results cast doubt on the idea that ESG renaming is merely a cosmetic event motivated by fund flows or fees. On average, fund managers do walk the talk: they follow through on the new label by improving portfolio-level ESG performance across multiple dimensions, while flow-driven incentives to rename appear less widespread than previously thought, and expenses are only marginally affected.

WHY THIS RESEARCH MATTERS NOW

Since we first researched and published this paper, sustainable finance has experienced something of a retreat. The decline in interest and participation in ESG investing has been conceptualised as "sustainable finance fatigue", driven partly by political backlash – most notably in the United States – and partly by legitimate concerns about greenwashing and impact washing. Some mutual funds have quietly walked back from their ESG labels, and inflows into funds that had powered the growth of the previous decade have slowed. In this environment, the question of whether an ESG label ever carried substantive meaning – and, by extension, whether the labels that remain do – has become more pressing, not less.

The evidence in this paper speaks directly to that question, using the period during which renaming activity was arguably at its peak. If ESG renaming had been purely cosmetic when the ESG label was most valuable, the case for treating current ESG labels as informative would be weak. What we find is different: renaming during the growth phase was on average accompanied by real improvements in portfolio ESG profile, and by only marginal fee changes. Investors and regulators facing today's more sceptical environment can therefore rely on a fund-level, evidence-based assessment of ESG labels, rather than either dismissing them as marketing or accepting them at face value.

RELEVANCE IN TODAY'S CONTEXT

- ESG labels are now assessed against a backdrop of sustainable finance fatigue and political backlash, so evidence on whether such labels have historically been substantive speaks directly to how they should be treated today.
- With some funds now removing ESG terms from their names, the same due-diligence question – do the portfolio actions mirror the label? – applies equally to "reverse" renaming events.
- Regional differences remain important, and there is no reason to expect the current backlash to be evenly distributed either.

RESEARCH QUESTION AND APPROACH

We ask two connected questions. First, do investors respond to first-time ESG renaming by mutual funds around the world? Second, do fund managers' subsequent investments align with the new name – do they rename with purpose?

Using a customised keyword search across an initial universe of over 220,000 share classes and a list of 172 ESG-related terms, we identify 740 open-ended equity funds that added an ESG term to their name for the first time between July 2016 and September 2022. We compare renamed funds with non-renamed peers, and analyse the ESG profiles of the underlying holdings along several dimensions: overall MSCI ESG score, Morningstar's portfolio sustainability risk score, exposure to controversial businesses, alignment with positive-impact investments, and portfolio decarbonisation. Expenses are analysed separately at the share-class level.

WHAT THIS RESEARCH DOES (AND DOES NOT) SHOW

- It shows that funds that rename meaningfully improve their portfolio ESG profile across multiple dimensions, with fees for a typical renamed fund essentially unchanged.
- It shows that flow effects are smaller and less widespread than earlier studies suggested, and are concentrated among European funds.
- It examines renaming during the growth phase of ESG investing; the current period of sustainable finance fatigue may have shifted the incentives faced by fund managers, and the evidence should be interpreted with this in mind.

APPLICATIONS FOR INVESTMENT PROFESSIONALS

The first application is fund due diligence. Our results support treating ESG renaming as a potentially informative event rather than automatically as a marketing signal. The portfolio dimensions we study translate naturally into a monitoring checklist: after renaming, has the fund's overall portfolio ESG score improved, has its sustainability risk score fallen, has controversial-sector exposure declined, has carbon intensity dropped? Where these dimensions move in the expected direction, renaming is consistent with substantive repositioning; where they do not, closer scrutiny is warranted. The same logic applies in reverse to the growing number of funds now removing ESG terms from their names: a change in label without a change in portfolio is arguably as informative in the current environment as it was in the growth phase.

A second application is regional differentiation. U.S. funds that rename exhibit larger post-renaming improvements in portfolio ESG scores than European ones, most plausibly because European fund managers already have a stronger ESG orientation to begin with. Although this result may seem intuitive considering that ESG investing has long been more developed in Europe, it contrasts with previous studies suggesting that especially U.S. funds have flow-driven motives to rename without walking the talk. For global allocators, this implies that rating frameworks which treat all funds that rename identically may under-reward U.S. funds that rename and deliver larger marginal improvements.

A third application concerns fees. In an environment where accusations of ESG-washing extend to pricing, our evidence provides limited support for the view that ESG renaming is primarily used to raise fees: only a subset of European retail funds exhibits on average a modest 4.5 basis-point higher annual TER, and the combined effect for a typical fund that renames and improves its ESG profile is close to zero.

PRACTICAL USE CASES

- Treat ESG renaming – and its reverse – as an informative event to be tested against the underlying portfolio, rather than at face value.
- Adjust regional expectations for post-renaming ESG improvement given the different baseline sustainability profiles of U.S. and European funds.
- Push back on blanket ESG-washing narratives with evidence-based, fund-level assessment of both portfolio change and fees.

CONCLUSIONS AND NEXT STEPS

In a nutshell, funds' ESG profiles improve after ESG renaming, which casts doubt on the idea that ESG renaming is merely a cosmetic event motivated by fund flows or fees. Taken together, our results are consistent with a signalling story, in which renaming conveys information about fund managers' commitment to equity allocations that improve the ESG profile of their portfolios, while the combined effect on fees for a typical renamed fund is close to zero and any fee increases are confined to a subset of European retail share classes.

Regardless of the current backlash, or perhaps because of it, this framework retains practical value. Rather than treating renaming – or de-renaming – as sincere by default or cosmetic by default, allocators and fund selectors can rely on a small set of observable portfolio dimensions to assess follow-through on a case-by-case basis. A natural next step is to revisit the analysis in the post-2022 period: do funds that renamed during the growth phase continue to walk the talk, and do funds that are now removing ESG terms from their names also unwind their portfolio ESG tilts, or is the reverse-renaming trend a labelling exercise disconnected from underlying holdings?

POINTS FOR PROFESSIONAL DISCUSSION

- Given the current sustainable finance fatigue, how much weight should investors place on the ESG label attached to a fund, and how does that answer differ across the U.S. and Europe?
- Should the same due-diligence framework we propose for ESG renaming be applied to the growing number of funds that are now removing ESG terms from their names?
- Are the portfolio dimensions we study the right set for monitoring whether funds continue to walk the talk under political and regulatory pressure?

About the Original Research

This summary is based on the following original research paper:

- **Title:** Renaming with Purpose: Investor response and fund manager behaviour after fund ESG renaming
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