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Insight

Sustainable Investing: From Disillusionment to Normalization

After a period of marked disillusionment, sustainable investing has shown signs of stabilization in recent months. This development points to the beginning of a normalization phase, characterized by a pragmatic approach with a renewed focus on financial materiality.

A look back at a journey marked by enthusiasm, a reversal, and normalization

Over the past 15 years, sustainable investing has emerged as a major trend in the financial markets. There are a number of reasons for this, including a paradigm shift: the transition from an exclusionary approach—based on investors' values—to one that integrates environmental, social, and governance (ESG) risks and opportunities throughout the investment process.

More recently, however, sustainable investing has attracted a number of criticisms[i]. These initially focused on doubts regarding relative financial performance, and later on the actual ability of sustainable investment funds to generate tangible benefits. They subsequently evolved into a more fundamental questioning, amplified by the current sociopolitical context. It was against this backdrop of disillusionment that 2025 began. Yet, despite pervasive pessimism, sustainable investing has shown signs of stabilization over the past few months.

In this regard, it is interesting to compare the evolution of sustainable investing with Gartner's Hype Cycle[1]. After initially experiencing a period of excessive enthusiasm, followed by a significant reversal, sustainable investing now appears to be entering a phase of normalization. This has resulted in a more disciplined, pragmatic approach grounded in financial materiality.

At iAGAM, we think that the fundamental principle of sustainable investing remains unchanged, even as it evolves. This principle implies that creating long-term value requires a comprehensive review of risks and opportunities facing issuers, regardless of whether they are labelled as ESG.

Thus, the normalization phase now underway appears consistent with our approach to sustainable investing.

PARALLEL BETWEEN THE EVOLUTION OF SUSTAINABLE INVESTING AND GARTNER'S HYPE CYCLE

Phase 1: From sustained growth to hype (2006–2021)

Formalized in the mid-2000s, notably with the adoption of the Principles for Responsible Investment (PRI) in 2006, the integration of ESG factors initially sought to better account for certain non-financial risks in investment decisions and to structure engagement activities with issuers. Over time, this approach gained increasing support from institutional investors. Despite a slight decline[ii] observed more recently, the number of PRI signatories continued to rise during the period, with more than 5,000 organizations now having publicly committed to these principles.

This momentum fostered rapid and widespread growth in sustainable investing. On the one hand, several frameworks emerged to strengthen its credibility and facilitate adoption.

1. Gartner's Hype Cycle is an analytical framework describing how the adoption and perception of an innovation evolve over time. It distinguishes five phases, ranging from initial enthusiasm to a phase of disillusionment, and then to a gradual maturity where applications become more realistic and value-creating. It allows us to assess an innovation in relation to its actual level of maturity and impact. Source: Gartner.com.

These frameworks have helped structure practices, improved information disclosure, and encourage the establishment of measurable objectives, particularly regarding climate change.

On the other hand, various approaches gained increasing popularity, ranging from ESG integration to shareholder engagement, including impact investing. The Responsible Investment Association's (RIA) annual reports on trends in Canada highlight how these approaches evolve[iii]. Meanwhile, new financial instruments emerged, with the rapid growth of the labelled bond[iv] market, while new expertise developed within the industry[v]. All of these factors contributed to sustained growth[vi] in assets under management (AUM) within so-called sustainable funds, driven by both significant net capital inflows and the positive performance of financial markets[vii]. In Canada, according to the RIA, sustainably managed assets accounted for 71% of the market at the end of 2024[viii].

In retrospect, however, this rapid expansion phase came with particularly high expectations regarding the simultaneous achievement of superior financial performance, risk management, values alignment, and measurable societal impact. This perception, fuelled by an escalating narrative[ix], helped create a kind of illusion that financial and non-financial objectives were perfectly aligned—a situation that paved the way for the subsequent phase of disillusionment.

Phase 2: Reversal and diverging realities (2022–2024)

Although AUM in so-called sustainable strategies have reached record highs, their growth has slowed significantly over the past three years. In fact, since the record inflows seen in 2021, capital flows into sustainable funds have declined sharply[x]. In 2024, in Canada, these funds recorded a net outflow of approximately $2.5B, marking the first annual outflow in six years[xi].

Several factors can explain this reversal. First, certain sustainable strategies underperformed relative to the market[xii], hurt in 2022 by widespread underweighting in fossil fuels and by the sharp correction in renewable energy stocks after the steep rise in interest rates[xiii].

Second, the lack of harmonization in regulatory and methodological frameworks at a global level raised doubts about the quality, comparability, and reliability of ESG data, heightening concerns about greenwashing and prompting greater caution around the development of new products[xiv].

In many respects, this first pullback in over a decade was interpreted by many investors as an expected pendulum swing following a phase of rapid expansion. It allowed for the recognition of certain limitations, the acknowledgment of criticism from stakeholders, and the implementation of necessary adjustments, both in investment approaches and in discourse[xv].

Phase 3: Politicization of the debate around sustainable investing (2024)

While sustainable investing remains a well-established practice globally, it is evolving within a significantly more polarized sociopolitical context. This dynamic is more pronounced in the United States but is now exerting a growing influence on the Canadian market.

Fragmentation in public debate and deepening ideological divides have helped turn sustainable investing into a highly politicized issue. In this context, certain ESG practices have been perceived by some stakeholders as an attempt to impose social and environmental values on financial markets, rather than as a pragmatic investment strategy based on the analysis of risks and economic opportunities[xvi].

This perception has fuelled the rise of an "anti-ESG" sentiment. Several U.S. states have taken steps to restrict the integration of ESG criteria into investment decisions[xvii].

This shift in the debate—from the financial to the ideological arena—has exacerbated the disillusionment observed in recent years.

It has also prompted many investors and companies to adopt a more cautious stance in their communications, without, however, actually calling into question the integration of material issues into their decision-making processes.

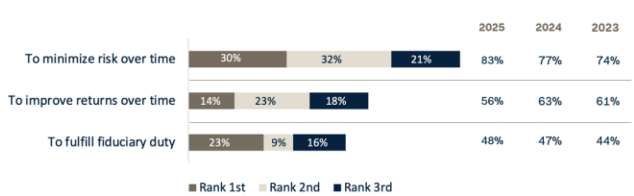
2025: A return to financial materiality

Recent developments have naturally raised concerns about the future of sustainable investing, and 2025 in fact began amid considerable disillusionment; expectations were modest, if not negative. However, the year turned out to be generally more positive than anticipated. According to Morningstar data for 2025[xviii], the first three quarters were positive for sustainable funds in Canada, while the fourth ended with net outflows[xix].

Furthermore, several surveys suggest that, overall, investors remain committed to sustainable investing, including institutional investors, retail investors, and investment advisors[xx]. The RIA's latest survey also notes that the majority of investors expect growth in the coming years.

One striking observation is the cautious approach currently being advocated: more low-key and less visible in terms of communication, but essentially unchanged with regard to the underlying strategy—a stance befitting the current climate of uncertainty affecting many aspects of the economy. In addition, the latest RIA survey shows that risk minimization is a growing priority as investors adapt to geopolitical uncertainty and the recent reversal in sustainable investing. Climate-related risks, in particular, remain a key consideration.

TOP THREE REASONS TO CONSIDER ESG FACTORS



Sources: RIA, 2025 Canadian Responsible Investment Trends Report.

This trend should come as no surprise, as long-term value creation is a universal goal. While opinions have become polarized, the risks and opportunities associated with ESG criteria remain. And the reality is more nuanced than extreme views would suggest.

For example, although recent changes bring uncertainty and potential delays to the energy transition, climate risk remains a persistent and significant factor in investment decision-making. In fact, recent trends suggest that investment firms are already adapting their portfolios in response to climate risks, while global investments are increasingly diversifying between low-carbon energy solutions and fossil fuels[xxi].

The shift toward greater pragmatism is also reflected in the Canadian government's recent policies[xxii]. Decisions over the last few months demonstrate a more explicit commitment to linking sustainability ambitions to concrete economic imperatives, such as industrial competitiveness, energy security, attracting capital, and long-term productivity. The approach favoured emphasizes tangible economic levers, thereby helping to reposition sustainability as a driver of economic resilience.

Ultimately, increased caution and a streamlined narrative do not signal weaker momentum in sustainable investing, but rather its entry into a phase of maturity.

As highlighted by a recent survey[xxiii] of institutional investors, sustainable investing is not fading; it is evolving, becoming more deeply rooted in financial analysis, economic materiality, and rigorous risk management.

Combining financial returns and sustainability

At iAGAM, we believe that incorporating ESG factors into the investment process enables better risk management and helps identify opportunities across various asset classes. This contributes to enhancing a portfolio's long-term return potential.

This conviction is based on four pillars that define both the "what" and the "how" of our approach. We focus on material risks and opportunities with a real financial impact, integrating them rigorously into the core of the investment process. Our approach prioritizes research, analysis, and the empowerment of investment teams, rather than the creation of parallel ESG structures.

THE PILLARS OF IAGAM'S SUSTAINABLE INVESTING APPROACH

- Exhaustive risk management is embedded in our investment culture
- Sustainable growth comes with opportunities of long-term value creation
- Sustainable investment builds on evidence and analysis
- Empowering investment teams to drive sustainability engagement and ownership

This disciplined and pragmatic approach aligns with the expected normalization phase in sustainable investing. It allows us to provide our clients and partners with tailored investment solutions that balance financial performance with sustainability objectives, in line with their needs and preferences.

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A magnet for top investment talent, iA Global Asset Management is one of Canada's largest asset managers, with over $100 billion under management across institutional and retail mandates. We help investors achieve their long-term wealth creation goals through innovative investment solutions designed for today's complex markets. We are building upon our historic success, supporting the growth of our core strengths, and exploring innovative ways to meet investor needs. We are rooted in history and innovating for the future. Our experienced portfolio managers use a proprietary investment methodology, rooted in iAGAM's unifying commitment to strong risk management, analytical rigor and a disciplined, process-driven approach to asset allocation and security selection.

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