In Focus

Impact and financial performance

Evidence from listed equities

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Impact investing has long been caught in the tension between purpose and profit. Many investors assume that generating meaningful social or environmental impact requires financial trade-offs. This perception has hindered the widespread adoption of impact investing. But is this assumption correct?

This paper, a collaboration between Schroders and Saïd Business School's Oxford Initiative for Rethinking Performance (ORP), challenges the conventional wisdom. It examines whether impact investing in listed equities can deliver competitive financial returns while achieving positive real-world outcomes. The findings offer compelling evidence that investors don't always have to choose between making a difference and making money.

Key findings

Our research suggests that impact investing, under the right conditions, can generate strong risk-adjusted returns. Analysing 257 impact companies, we assess whether they outperform traditional benchmarks[1] using asset pricing models and regression analysis. We control for key financial drivers–size, value, momentum, profitability, and investment factors–to determine if impact firms generate alpha, independent of their risk characteristics. By introducing impact materiality as a potential return driver and incorporating real-world case studies, this research provides a data-driven look at the financial viability of impact investing in listed equities.

Our analysis highlights three key findings:

1

Competitive risk-adjusted returns: The results suggest that impact portfolios can deliver strong raw and risk-adjusted returns, with annualized alphas of our back-tested portfolios exceeding 9% in some cases[2]. However, as our data does not allow us to consider point-in-time impact portfolios over our sample period 2010-2023, the magnitude of this result must be interpreted with caution

2

Lower volatility, greater resilience: These portfolios exhibit lower volatility, reduced drawdowns, and milder negative skewness compared to conventional indices, suggesting stronger downside protection. Impact portfolios showed stronger correlation with the market in expansions and weaker correlation in recessions, indicating asymmetric market exposure and stability

3

Impact materiality as a driver of returns: Companies with higher revenue alignment to measurable impact themes generate superior financial returns

These findings suggest that impact investing can deliver strong risk-adjusted financial returns, with impact itself acting as a driver of alpha in the right conditions. However, not all impact investments will outperform. Success depends on thorough selection and evaluation, ensuring that financial strength and impact reinforce–rather than compete with–each other.

[1]These impact firms have been identified and approved through Schroders proprietary Impact Framework, described in more detail in Section 2.
[2]The simulated result of the portfolio is based on historical data and does not represent the actual remuneration rate of the portfolio or a guarantee of future performance, simulation at different times can have different results.

Schroders

Looking ahead

While impact investing has historically been perceived as a niche strategy – we believe it is becoming a more mainstream approach to capital allocation. As regulatory landscapes evolve, consumer preferences shift, and environmental and social factors gain prominence in financial markets, impact should increasingly be seen as a legitimate driver of returns.

That said, successful impact investing requires rigor. Not all impact investments outperform, and careful financial analysis must go hand in hand with impact due diligence. This paper provides a framework to help investors assess opportunities where impact and financial performance reinforce – rather than compete with – each other.

As the market matures, ongoing research will refine our understanding of the drivers and scalability of impact investing. Future studies should explore the relationship between impact and financial returns in different asset classes, examine its long-term financial sustainability, and deepen insights into the causal relationship between impact and returns.

Ultimately, impact investing represents an evolution in how capital is deployed – one that integrates financial success with broader social and environmental goals. By adopting disciplined investment approaches, investors can position themselves at the forefront of this transition, capturing both financial returns and meaningful impact.

1 Introduction

The financial viability of impact investing: aligning purpose with profit?

The financial viability of impact investing – a strategy that seeks to deliver measurable social or environmental outcomes alongside financial returns – has long been a subject of debate. At the heart of this discussion lies a fundamental question: can purpose and profit truly coexist in investment strategies, or does prioritizing impact inherently require financial trade-offs? Foundational financial frameworks such as Modern Portfolio Theory (Fabozzi, Gupta, and Markowitz, 2002) often imply such a trade-off, reinforcing the misconception that impact investing is inherently concessionary. This perception remains a significant barrier to the growth of the impact investing industry.

Overcoming this challenge requires greater transparency and evidence on the risk-adjusted financial performance of impact investments. This paper explores whether impact investing can deliver competitive, risk-adjusted financial returns alongside positive social or environmental outcomes. Focusing on market-rate impact investments – seeking impact alongside competitive returns – in listed equities, we employ a mix of quantitative and qualitative analysis, including regression models and case studies, to assess the relationship between impact and financial performance.

This paper challenges the assumption that impact investing requires financial trade-offs by examining when and how it can deliver competitive, risk-adjusted returns. Rather than asserting that impact investing always delivers strong financial performance, we provide a framework for assessing the conditions under which competitive risk-adjusted returns can be generated. Through a combination of quantitative analysis and case studies, we identify key factors that contribute to financial performance in impact portfolios. While not all impact investments outperform, our findings suggest that, under certain conditions, impact strategies can deliver alpha. Although we cannot ascertain the magnitude of the risk-adjusted returns to a point-in-time impact portfolio given existing data constraints, the back-tested returns to a portfolio of impact firms as selected as of 2024 directly challenge the notion that impact investing must be inherently concessionary[3].

Theoretical constraints on impact-driven alpha

Theoretical frameworks provide useful context for understanding the perceived constraints on impact-driven returns. Modern Portfolio Theory (MPT) (Fabozzi, Gupta, and Markowitz, 2002) emphasizes broad diversification as key to optimizing risk-adjusted returns, leading to the assumption that narrowing the investment universe to companies that prioritize measurable social or environmental outcomes can increase risk and limit financial performance. However, impact investments can provide compensatory advantages, including performance and portfolio resilience benefits. Impact investments often have distinct sectoral, geographic, or structural characteristics that differentiate them from mainstream portfolios, potentially offering diversification benefits through lower correlations with traditional benchmarks, particularly in times of market stress.

Similarly, the Efficient Market Hypothesis (EMH) posits that asset prices reflect all publicly available information, including information relating to a company's sustainability or impact profile. From this perspective, the potential to outperform the market based solely on impact objectives is limited, even if it was value enhancing, as such information is, in theory, already priced in. However, impact-related data is often harder to acquire, assess, and standardise compared to traditional financial metrics, creating informational asymmetries that skilled investors may be able to exploit. Moreover, the market's slow adaptation to impact-related information and the perception that achieving impact is costly can contribute to persistent mispricing, allowing for sustained opportunities for excess returns.

Principal-agent dynamics and multitask contract theory

Beyond theoretical models, impact investing faces operational challenges rooted in principal-agent dynamics and multitask contract theory. Investors (principals) often delegate dual mandates – financial returns and measurable impact – to agents, such as company management teams. Multitask contract theory (Evans, 2013) highlights the tensions in aligning these objectives, with financial contracts often prioritizing profit at the expense of impact. Strategies such as aligning

[3]The simulated result of the portfolio is based on historical data and does not represent the actual remuneration rate of the portfolio or a guarantee of future performance, simulation at different times can have different results.

cost synergies, revising performance metrics to reward both financial and impact outcomes, and fostering trust-based relationships between investors and entrepreneurs offer potential solutions for those investors with dual objectives.

Viviani and Maurel (2019) expand on this by exploring the origins of value creation in impact investing, emphasizing that its success relies on hybrid organizations that integrate financial and social objectives. They argue that impact investing should deliver superior performance compared to separately investing in financial and non-financial enterprises, with value arising from synergies within multidimensional business models – noting challenges such as the risk of mission drift and difficulties of measuring non-financial impact. Beyond financial returns, impact may strengthen a company's social license to operate, fostering greater stakeholder trust, reducing regulatory risk, and enhancing customer and investor engagement, all of which can contribute to long-term value creation (Bice & Moffat, 2014).

Evolving market dynamics and fiduciary duty

Despite some of these theoretical constraints, the impact investing market has grown significantly, fuelled by rising demand from younger generations who prioritise investments that align with their values. According to GIIN, the impact investing market reached $1.571 trillion in 2024, representing 21% compound annual growth (CAGR) since 2019[4], driven by increasing institutional participation and intergenerational wealth transfers. For example, Millennials are far more likely than previous generations to integrate social and environmental goals into their investment decisions (Snider, 2024).

Certain markets have seen particularly strong momentum, with Japan experiencing a ninefold (9x) increase in impact investing between 2021 and 2023[5], as institutional investors adopt it as a portfolio diversifier, particularly across private and listed debt markets. In the UK, policymakers have intensified efforts to promote socially oriented investments, encouraging local institutional investors to channel capital into underserved regions and sectors as part of broader initiatives to address structural inequalities and support inclusive economic growth.

The concept of fiduciary duty has also evolved in certain markets to recognize that incorporating social and environmental considerations into investment decision-making can complement, rather than conflict with, financial objectives. Legal and industry advancements increasingly demonstrate that addressing global challenges like climate change, resource scarcity, and inequality enhances long-term financial performance. For example, Pensions for Purpose has highlighted how UK pension funds successfully deliver competitive returns while achieving positive social and environmental impacts. These developments reflect a progressive understanding that aligning investments with these priorities is not only consistent with fiduciary responsibilities but essential for safeguarding sustainable, long-term value creation.

Impact vs. sustainability and the spectrum of capital

Impact investing is often conflated with sustainable or ESG investing, yet the two differ fundamentally in their roles within the spectrum of capital – a framework spanning traditional to philanthropic investing.

The spectrum of capital

Approach	Traditional	Responsible	Sustainable	Impact Investing	Philanthropy
				Finance first ⟷ Impact first	
Finance Goals	**Accept competitive risk-adjusted financial returns**			Accept lower risk-adjusted financial returns	Accept partial capital preservation / Accept full loss of capital
Impact Goals		**Avoid harm and mitigate ESG risks** Mitigate or reduce negative outcomes for people and the planet	**Benefit stakeholders** Generate positive outcomes for people or the planet	**Contribute to solutions** Generate positive change for otherwise underserved people or the planet	
Intentions	"I am aware of potential negative impact, but do not try to mitigate it."	"I want to behave responsibly." "I have regulatory requirements to meet."	"I want businesses to have positive effects on the world, and help sustain long-term financial performance."	"I want to help tackle climate change." "I want to help tackle the education gap."	

The 'impact economy'

Source: Bridges Fund Management and Impact Management Project.

[4]Sizing the Impact Investing Market 2024 – The GIIN.
[5]GSG Japan National Advisory Board.

Sustainable investment typically involves screening for responsible business conduct, mitigating risks, or identifying "best-in-class" companies within industries based on environmental, social, and governance (ESG) criteria.

Impact investing, by contrast, occupies a distinct position along the spectrum of capital; it is not a more concentrated version of "sustainable investment". It prioritises intentional, measurable contributions to specific social or environmental outcomes, targeting businesses that address critical global or local challenges such as climate change, resource scarcity, and equitable access to health and education. Three core principles – intention (clear impact objectives set out in a theory of change), contribution (the investment itself must actively contribute to achieving the intended social or environmental outcomes, typically through engagement within listed equities) and measurability (outcomes must be quantifiable) – set impact investing apart as a unique strategy.

Impact investing itself encompasses a range of investment approaches, from "impact-first" strategies that prioritise social or environmental outcomes over financial returns to "finance-first" approaches that seek market-rate returns alongside measurable impact (Agrawal & Hockerts, 2019). In recent years, impact investing has expanded beyond its traditional private market focus to play an increasingly significant role in listed debt and equities. While early research often framed impact investing as concessionary, GIIN's 2024 survey reveals that nearly 74% of impact investors now target market-rate returns, challenging the perception that financial trade-offs are inevitable.

Research gap and objectives of this paper

Most existing research on financial performance and environmental or social outcomes has focused on ESG or sustainable investing. For example, NYU Stern's meta-analysis (Whelan, Atz & Clark, 2021) finds that approximately 59% of studies report sustainability-oriented investments perform similarly to or better than conventional investments, while only 14% show negative results.[6]

Several studies provide deeper insights into these mixed results. Friede, Busch, and Bassen (2015), in a meta-analysis of over 2,200 studies, concluded that 90% found a non-negative relationship between ESG criteria and corporate financial performance (CFP), with many demonstrating positive correlations. Similarly, Clark, Feiner, and Viehs (2015) identified strong ESG performance as often associated with lower costs of capital, reduced risks, and enhanced operational efficiency. However, contrasting findings from Hong and Kacperczyk (2009) reveal that companies excluded from ESG-focused portfolios – often referred to as "sin stocks" – tend to outperform the market due to higher risk premiums and lower investor demand. More recently, Gibson, Krueger, and Schmidt (2021) argue that ESG performance's impact on financial returns is highly context-dependent, influenced by industry norms, regulatory environments, and investor sentiment.

Lo and Zhang (2024) propose a framework to quantify the financial value of impact investing that is based on induced order statistics. They rank securities based on 'impact factors' and treat financial returns as random variables to assess how performance varies across different levels of impact. Their findings suggest that returns depend on the chosen benchmark asset pricing model – in some cases, impact investing yields attractive returns, while in others, it comes at a cost. Notably, their impact factors focus primarily on sustainability and ESG indicators – such as carbon emissions, ESG, scores and R&D – rather than impact-focused metrics.

Despite the depth of this literature, much of it centres on ESG and sustainable investing, leaving a critical gap when it comes to impact investing, particularly non-concessionary models that seek competitive financial returns alongside positive impact.

This paper aims to bridge this gap by evaluating the financial performance of market-rate impact investing – seeking impact alongside competitive risk-adjusted financial returns – within listed equities. By leveraging both quantitative and qualitative methods, including regression analyses and case studies, this study evaluates whether and how impact aligns with risk-adjusted financial returns.

2 Methodology

2.1 Overview

This study employs a dual quantitative and qualitative approach to evaluate the financial performance of impact investments in listed equity markets. Using asset pricing models and regression analyses, we compare impact portfolios to traditional indices, controlling for investment factors such as size and momentum. This allows us to isolate alpha generation unexplained by certain asset pricing factors.

The impact portfolios are constructed using a subset of firms that have been approved into Schroders listed equity impact universe as of Q3 2024. We provide details on how impact firms have been identified in section 2.2. To abstract from portfolio selection and construction considerations and focus on impact characteristics, we randomly select 40 impact firms from this universe to form an equally weighted portfolio. We repeat this 10 times to obtain 10 randomly selected impact portfolios containing 40 equally weighted firms from the approved 257 impact firm universe and compare their performance to the MSCI ACWI IMI (Figure 3). To replicate the survivorship bias inherent in the impact portfolios for the benchmarks, we add comparisons to only survivors of the MSCI ACWI IMI.

We also assess the portfolio characteristics of an equal and value-weighted impact portfolio containing all impact stocks and further formally test their performance in asset pricing regressions controlling for common international risk factors (Table 1).

[6]The remainder had mixed results, largely because they look at multiple variables, time periods and samples within one study. Source: NYU-RAM_ESG-Paper_2021.pdf.

To complement these quantitative analyses, we incorporate three firm-specific case studies, providing qualitative insights into the operational dynamics and market conditions influencing impact-driven financial performance.

An important consideration in our analysis is distinguishing whether positive alpha in impact portfolios arises from their social and environmental objectives or from other intrinsic financial qualities, such as profitability and growth. While impact firms may exhibit strong financial metrics, such as return on equity (ROE) and sales growth, these outcomes may not necessarily stem from their impact mission. Clarifying this distinction is crucial for understanding the true drivers of financial performance in impact investments.

By controlling for traditional risk factors in asset pricing regressions, we assess whether alpha persists. Additionally, we explore firm-specific factors like sales growth and profitability as potential contributors to impact-driven financial performance. This comprehensive approach enables us to address the debate not only on whether impact investing can yield financial rewards but also provide initial, albeit suggestive, evidence on the mechanisms and conditions under which these rewards are realized. The combination of statistical trends and qualitative case studies provides a more comprehensive understanding of the factors driving financial returns within impact investments.

2.2 How we identify impact firms

This research examines the financial performance of a broad selection of impact firms drawn from Schroders' impact universe. This universe serves as the basis for inclusion in a range of dedicated listed equity impact funds managed by Schroders, with each firm undergoing rigorous impact due diligence via Schroders' proprietary Impact Toolkit. The toolkit evaluates companies across five core dimensions of impact, in line with the Impact Frontiers[7] framework:

1 What:
Assesses over 40 impact intents aligned with the 169 targets of the UN Sustainable Development Goals (SDGs) and external frameworks such as the Sustainable Development Investments Asset Owner Platform (SDI AOP).

2 How much:
Evaluates current and expected impact using a mix of core and asset-specific KPIs, categorized by stage (input, activity, output, or outcome) and focus (operations or products and services). Metrics are benchmarked against external standards like IRIS+ and include baseline, target, and historical data.

3 Who:
Assesses the level of need for the products and services being offered within a given country, using a series of macro indicators from international financial institutions, such as the World Bank and the SDG Index. We also assess the key customers and industries and the degree to which they are underserved.

4 Contribution:
Assesses investee contribution, including uniqueness of its products and services, as well as investor financial contribution (such as scale, speed, risk, terms, role or reputation) and non-financial contribution, including our degree of influence, as well as the type and depth of our engagement.

5 Risks:
Examines risks that could hinder impact realization, including evidence risk – the probability of insufficient high-quality data to measure impact – based on the nine impact risks identified by Impact Frontiers.

The toolkit assesses alignment with selected key impact themes – environmental solutions, social inclusion, health & wellness, responsible consumption, and sustainable infrastructure – and evaluates sustainability practices.

Two critical concepts guide firm selection: materiality and enterprise contribution.

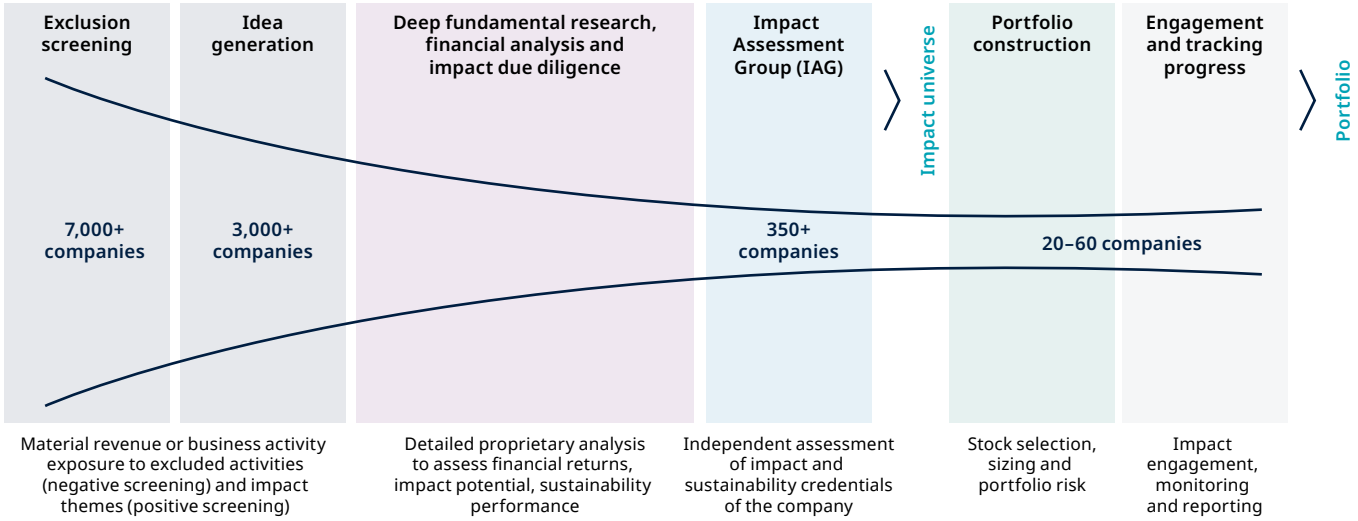
- **Materiality:** ensures that impact is core to a company's business model rather than incidental. This involves mapping impact at a granular level, down to specific products, segments, or verticals and respective associated revenues.

- **Enterprise contribution:** evaluates whether the company's efforts drive outcomes that would not otherwise occur. While real-world assessment is challenging due to the absence of counterfactuals, certain attributes can serve as indicators. These include innovation, differentiation, scale, quality, cost-effectiveness, or the uniqueness of the company's products, services, or delivery methods.

An essential component of this identification process is the Impact Assessment Group (IAG), an independent body responsible for reviewing and approving all firms within the impact universe. Before inclusion, each firm is vetted by the IAG to ensure compliance with Schroders' high standards for impact.

[7] Five Dimensions of Impact | Impact Frontiers.

Process for identifying impact firms



Source: Schroders, 2025. Figures are illustrative only based on a global universe.

Inclusion in the impact universe, while contingent on meeting high standards approved by the IAG, does not guarantee placement in an impact portfolio. Portfolio managers conduct traditional equity analyses alongside impact due diligence and may choose not to invest in firms within the impact universe if their financial returns or valuations are unattractive.

For this research, we focus on the broadest basket of impact firms – those within the impact universe, regardless of portfolio inclusion. This approach minimizes selection bias and mitigates the influence of non-impact factors identified by portfolio managers in the portfolio-inclusion process.

Focusing on this broader universe rather than portfolio holdings has introduced greater variability in the returns profile for the impact portfolios. This underscores a key point: impact analysis cannot be separated from traditional financial analysis when aiming to deliver strong, sustainable results.

3 Results

3.1 Descriptive results

The empirical analysis covers the 257 international impact firms that have been approved by the IAG as eligible investments in the impact universe (see above).

Figure 1 shows the distribution of impact firms by country, highlighting a relatively wide dispersion of firms across developed and emerging markets with a large fraction based in the United States, China and India followed by Australia, Taiwan, Brazil and South Korea. A small number of firms are based in Saudi Arabia, Puerto Rico, Poland, Norway, Belgium and Vietnam. The figure also shows the mean market capitalization and interquartile range by country. Market capitalization varies significantly both across and within countries. While developed markets generally have larger-cap firms, the U.S. stands out as an exception, with a higher concentration of smaller firms. Notably, some countries exhibit extreme variations in market capitalization, as seen in the large interquartile ranges for select markets. This suggests that while impact firms operate across a broad set of economies, their market size and financial scale remain highly diverse.

Figure 2 shows the distribution of the sample by sector (depicted by the bars) compared to the MSCI ACWI IMI (depicted by the diamonds). A quarter of the sample consists of healthcare companies followed by a fifth in the industrials sector and more than 15% in information technology. This compares to healthcare companies making up 12% of the MSCI ACWI IMI, industrials 11% and information technology almost 23% (as of Q3 2024). The sample of impact firms is also overweight firms in the materials sector and underweight consumer discretionary, consumer staples and communication services compared to the MSCI ACWI IMI.

This sector distribution in part reflects the focus areas of the investment desks contributing to the universe, rather than an effort to mirror market sector weights. Unlike traditional index construction, the impact universe is built based on specific impact criteria rather than market benchmarks, which naturally leads to deviations in sector representation. As a result, sector allocations emerge organically from the nature of impact opportunities rather than from a top-down allocation framework.

Figure 1: Distribution of impact firms across countries by frequency and market capitalization

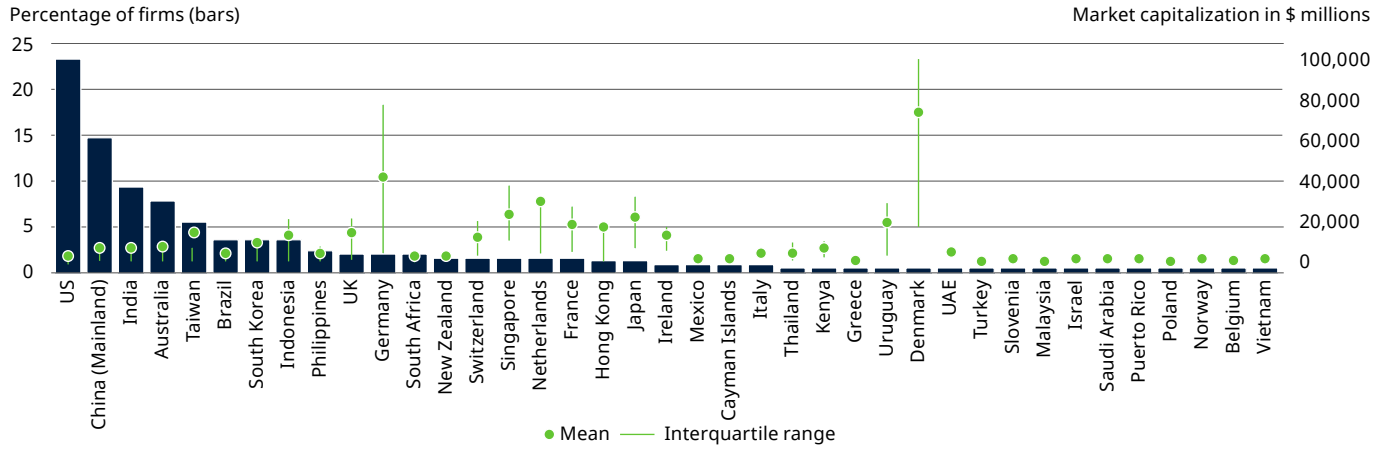
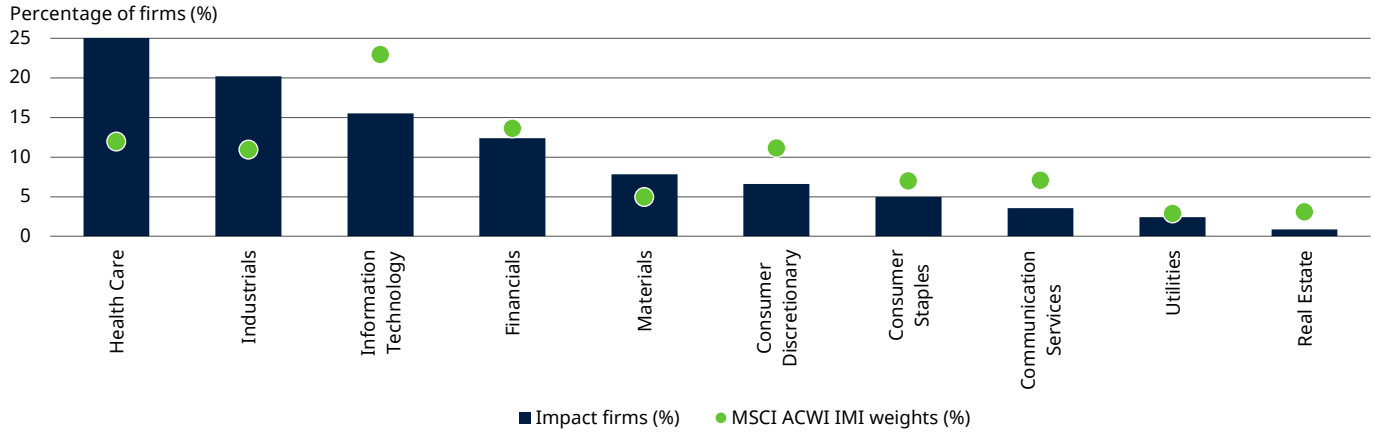


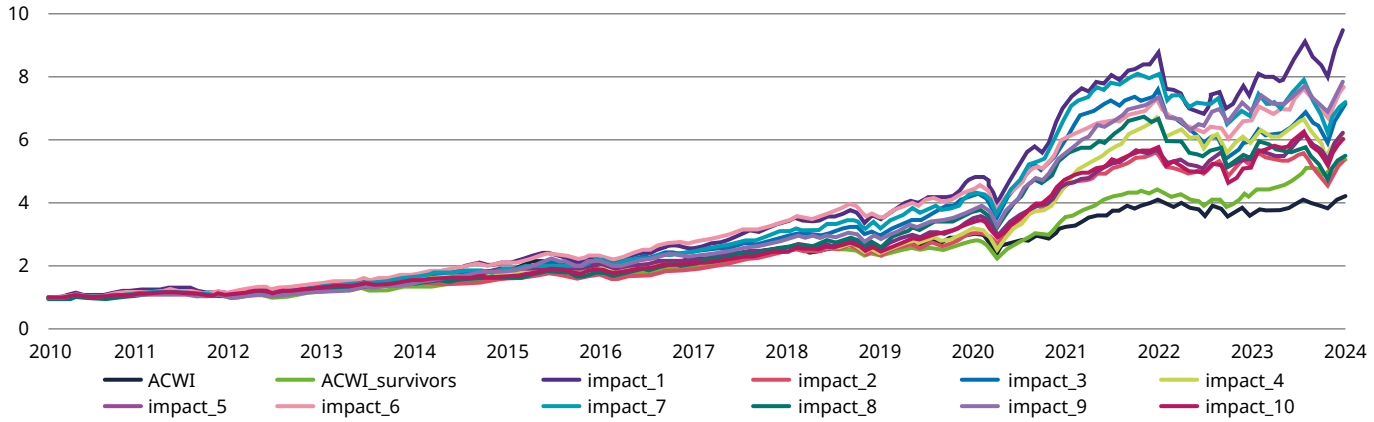
Figure 2: Distribution of impact firms across sectors versus the MSCI ACWI IMI



Next, we examine the raw total return performance of 10 randomly selected impact portfolios containing 40 equally weighted firms (with replacement, i.e. allowing the same firm to be picked across multiple portfolios), from the approved 257 impact firm universe and compare their performance to the MSCI ACWI IMI. As the impact portfolios suffer from survivorship bias (the portfolios are back tested based on firms available as of Q3 2024), we also include for more like-for-like comparisons the performance of the ACWI IMI surviving constituents (equally-weighted). It is important to note that most stocks were added to the impact universe between 2021-2024, meaning they were not classified as impact stocks at the start of the performance period. While this introduces the possibility that their historical performance may have contributed to their selection, past returns were not a criterion in the impact assessment process, and their inclusion was based solely on predefined impact qualifications.

Figure 3 shows the results. The figure shows that out of the 10 impact portfolios only two underperform the ACWI IMI survivors over the 2010-2023 period. Several of the impact portfolios outperform the ACWI survivors considerably.

Figure 3: Total return of impact portfolios 1 January 2010 – 31 December 2023



Further investigating the types of firms and sectors that contribute to the performance of the impact portfolios, we find firms in information technology, health care, materials and industrials to experience the highest returns, particularly in the period after the Covid market trough. Among the top performers are companies like Borosil Renewables (India's first and only solar glass manufacturer essential for photovoltaic modules, playing a critical role in India's renewable energy transition), Pro Medicus (an Australian leading provider of advanced medical imaging software solutions, enabling faster and more accurate diagnoses in radiology) and Bank Jago (a digital-first bank in Indonesia, focused on financial inclusion and accessibility)[8].

To assess whether this relative outperformance is associated with higher risk of impact firms, we compare the portfolio characteristics of equal and value-weighted impact portfolios to the benchmark indices next and in more robust regression analyses further below.

Table 1 shows the portfolio characteristics for an equally (EW) and market value weighted (MVW) impact portfolio containing all the 257 impact stocks. For comparison, the table also shows the characteristics of the ACWI IMI and an equal-weighted portfolio of the surviving firms of the ACWI IMI.

The table summarizes key return and risk measures, highlighting significant differences between the impact portfolios and the index benchmarks. Consistent with the results in the graph above, both the market-cap and equal weighted impact portfolios outperform the benchmarks in annualised raw returns. The market-cap weighted impact portfolio achieves annualized raw returns of 15.9% (MVW) and 15.1% (EW), compared to 10.7% for the ACWI IMI (12.9% for the surviving counterpart). Notably, the impact portfolios demonstrate higher abnormal returns (e.g., 3-Factor alpha of up to 9.4%) and risk-adjusted performance (Sharpe ratios of up to 1.31) than the benchmark portfolios, indicating superior returns relative to common risk factors using Fama-French international factor returns available on Ken French's website.

The impact portfolios show broadly similar volatility (annualized volatilities as low as 11.4%) compared to the index benchmarks despite containing a lower number of stocks. The betas to the ACWI IMI are also similar when comparing the equal-weighted impact portfolio with the equal-weighted ACWI IMI survivors. The relatively low volatility and beta of the impact portfolios reflect their diversification and reduced sensitivity to broader market movements.

Skewness further differentiates the portfolios. All portfolios, including benchmarks, display negative skewness, indicating a higher likelihood of extreme negative returns – a potential concern for stability-focused investors. However, the market cap weighted impact portfolio exhibits the mildest negative skewness, with –0.274.

Drawdowns are consistent with these results. Both impact portfolios exhibit lower maximum drawdowns (up to –17.5% for MVW and –17.6% for EW) compared to the benchmarks (e.g., -20.7% and –19.4% for the ACWI IMI and its survivors, respectively). This suggests that impact portfolios experienced smaller losses during market downturns, potentially reflecting their lower volatility and beta characteristics. Similarly, Value-at-Risk (VaR) metrics indicate somewhat reduced extreme loss potential for impact portfolios (0.042–0.048) compared to the benchmark portfolios (0.044–0.055).

These findings suggest the capacity of impact portfolios to deliver competitive financial returns and robust risk-adjusted performance, while achieving intentional social and environmental goals. This would put under question the notion

Table 1: Portfolio characteristics

	Impact MVW	Impact EW	ACWI IMI	ACWI IMI Survivors
Annualized Return	0.159	0.151	0.107	0.129
Alpha	0.091	0.083	0.000	0.048
3-Factor Alpha	0.094	0.091	0.038	0.069
5-Factor Alpha	0.102	0.102	0.037	0.070
Annualized Vol	0.114	0.117	0.127	0.111
Beta (to ACWI IMI)	0.685	0.714	1.000	0.711
Sharpe Ratio	1.309	1.211	0.776	1.081
Information ratio	1.411	1.244	0.000	0.731
Skewness	-0.274	-0.860	-0.556	-0.563
Max Drawdown	-0.175	-0.176	-0.207	-0.194
VaR (5%)	0.042	0.048	0.055	0.044

[8]Past Performance is not a guide to future performance and may not be repeated. The value of investments and the income from them may go down as well as up and investors may not get back the amounts originally invested. Exchange rate changes may cause the value of investments to fall as well as rise. Any reference to regions/countries/sectors/stocks/securities is for illustrative purposes only and is not a recommendation to buy or sell any financial instruments or adopt a specific investment strategy.

of inherent trade-offs between impact and financial performance. However, their performance may be influenced by systematic risk factor exposures, underscoring the need for further analysis. The regression analysis in the next section will explore whether this performance is driven by systematic factors or other portfolio characteristics, aiming to disentangle these effects.

3.2 Regression results

The descriptive findings above make a compelling case for their inclusion in impact investment strategies, offering competitive returns, with relatively lower exposure to extreme losses. However, these results might reflect the specific characteristics of the firms chosen in the impact portfolios – such as size, sector and other characteristics – highlighting the need for further empirical analysis.

Table 2 further analyses the performance of the 257 impact firms in asset pricing models against systematic factors using the Fama-French 5 factor model plus the momentum factor. These models decompose returns into components that explain performance based on various factors like market risk, size (small vs. large companies), value (high vs. low book-to-market ratios), profitability, and investment patterns. This helps to determine whether the higher returns from impact portfolios are due to exposure to these well-understood risk factors or unique characteristics outside standard market explanations. International factor returns come from Ken French's website. It is important to note that historical factor returns are based on stocks listed at that time and thus survivorship corrected while the impact portfolios are not, which potentially overestimates monthly abnormal returns, particularly during downturns.

We use progressively stricter controls (country, sector, and time effects) in the regression models and explore how firm size, sector exclusions, and economic cycles influence results. The constant in the regressions captures the average monthly abnormal return unexplained by the risk factors and other

Table 2: Asset pricing regressions

	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)
	Full Sample	Full Sample	Full Sample	Full Sample	Ex USA	Ex IT	Ex IT & Health Care	Small Firms	Large Firms	Expansion	Recession
Mkt-RF	0.758***	0.760***	0.760***	0.789***	0.648***	0.735***	0.769***	0.746***	0.736***	0.886***	0.639***
	(17.21)	(17.21)	(17.21)	(9.20)	(8.04)	(7.95)	(6.72)	(5.12)	(8.34)	(7.43)	(6.97)
SMB	0.774***	0.766***	0.766***	0.676***	0.349**	0.575***	0.564***	1.139***	0.212	0.397**	0.960***
	(6.97)	(6.98)	(6.99)	(4.90)	(2.40)	(4.19)	(3.63)	(5.20)	(1.43)	(2.05)	(6.17)
HML	-0.242**	-0.269**	-0.268**	-0.222	-0.272*	-0.141	-0.047	-0.176	-0.184	-0.349	0.015
	(-2.05)	(-2.26)	(-2.26)	(-1.33)	(-1.87)	(-0.81)	(-0.23)	(-0.58)	(-1.07)	(-1.59)	(0.06)
RMW	-0.241*	-0.250*	-0.250*	-0.112	-0.130	-0.018	0.029	-0.289	-0.250	-0.506*	0.024
	(-1.82)	(-1.93)	(-1.92)	(-0.59)	(-0.68)	(-0.09)	(0.12)	(-0.93)	(-1.11)	(-1.92)	(0.10)
CMA	-0.179	-0.163	-0.163	0.158	0.234	0.093	0.121	0.020	0.122	0.242	-0.131
	(-1.36)	(-1.28)	(-1.28)	(0.90)	(1.42)	(0.53)	(0.61)	(0.07)	(0.66)	(1.21)	(-0.41)
WML	0.036	0.020	0.020	-0.021	0.016	-0.060	-0.082	-0.039	0.079	0.075	0.104
	(0.55)	(0.30)	(0.30)	(-0.20)	(0.15)	(-0.58)	(-0.73)	(-0.22)	(0.60)	(0.54)	(0.60)
Constant (Alpha)	0.012***	0.012***	0.012***	0.011***	0.012***	0.011***	0.010***	0.012***	0.011***	0.009***	0.015***
	(7.53)	(7.72)	(7.74)	(11.98)	(12.18)	(11.24)	(8.32)	(6.96)	(10.32)	(5.72)	(15.88)
Country Controls	no	yes	yes	yes	yes	yes	yes	yes	yes	yes	yes
Sector Controls	no	no	yes	yes	yes	yes	yes	yes	yes	yes	yes
Year-month Controls	no	no	no	yes	yes	yes	yes	yes	yes	yes	yes
Obs.	30,809	30,809	30,809	30,809	22,483	25,425	17,633	8,921	14,989	17,462	13,347
Adj. R-squared	0.123	0.124	0.123	0.145	0.121	0.133	0.135	0.132	0.192	0.147	0.147

Robust t-statistics in parenthesis. *** p<0.01, ** p<0.05, * p<0.1.

controls. Table 2 presents the results of these regressions, including the coefficients, which measure the strength and direction of each factor's influence on returns. To ensure the reliability of our findings, we calculated robust t-statistics using clustered standard errors by firm and year-month (shown in parentheses), which test whether the observed effects are statistically significant or could have occurred by chance.[9]

Key findings include:

- **Alpha:** The results further suggest that the impact portfolio earns excess returns unexplained by the traditional risk factors. On average, the monthly alpha is about 1% and highly statistically significant, yet caution is warranted interpreting the magnitude given the inherent survivorship bias in the impact portfolio as discussed above.

- **Market correlation:** The coefficient on the market factor Mkt-RF (Market minus risk-free) is consistently positive and significant across all specifications, indicating that impact firms' returns are correlated with overall market movements. However, the lower coefficient during recessions compared to expansions suggests that these firms capture more of the upside while giving back less on the downside. This pattern aligns with the low betas reported in the previous section, highlighting a more asymmetric market exposure.

- **Size effect:** The positive and significant SMB (small minus big) coefficient across most regressions suggests that the returns for the impact stocks are partly explained by exposure to the size factor, reflecting the portfolio's tilt toward smaller-cap companies. This aligns with the higher growth potential often associated with smaller firms in the impact investing universe.

- **Value effect:** The HML (high minus low book-to-market ratios) coefficient is negative in many specifications, albeit not always significant. This suggests a preference for growth-oriented firms (common in impact investing), which may prioritize innovative solutions over traditional value characteristics like low price-to-book ratios.

- **Profitability effect:** The RMW (robust minus weak profitability) factor is often negative or insignificant, indicating that the impact firms in the portfolio are not tilted towards more profitable firms. This may reflect the mix of firms in the portfolio combining firms in earlier growth stages, where profitability metrics are secondary to achieving scale and delivering impact, and more mature firms (see sample market cap distribution above). Additionally, early-stage firms investing heavily in R&D may exhibit lower current profitability but could be positioned for higher future profitability, a dynamic that may not be fully captured by the RMW factor in the short term.

- **Investment and momentum effects:** The CMA (conservative minus aggressive growth strategies) and momentum WML (winners minus loser) factors are generally insignificant, suggesting that the firms do not display a systematic preference for conservative or aggressive investment policies, nor are the returns driven by past winners or losers. The lack of strength in the momentum factor is particularly important, underscoring that past performance is not a primary driver of returns in this context.

Excluding the U.S. or sectors like Information Technology or Healthcare (columns 5-7) does not alter the results substantively, suggesting the outperformance is not solely driven by these geographies or sectors. Sub-sample analyses by firm size (columns 8-9) reveals that smaller firms (the two lowest size quintiles by market capitalisation) contribute more strongly to positive SMB loadings, while larger firms dilute this effect. Importantly, the alphas remain largely similar across these analyses.

Dividing the sample into expansion and regression periods (according to recessions in OECD countries as identified by the World Bank) shows that the impact portfolios perform better during recessions compared to expansions with a difference in monthly excess returns of about 60 basis points (or 0.6%). This pattern aligns with the observed betas, which indicate greater sensitivity to economic growth when it is positive than when it is negative. This asymmetric upside capture suggests that impact portfolios participate more in economic upswings while being relatively more resilient during downturns.

Overall, the regression results highlight that while the performance of the 257 impact firms is influenced by systematic market factors, with a strong tilt toward small-cap and growth-oriented characteristics, it remains robust to the various factors. The results are also robust to country, sector, and time controls, confirming that the outperformance is inherent to the impact firms rather than artifacts of geographic or sectoral biases or particular time periods.

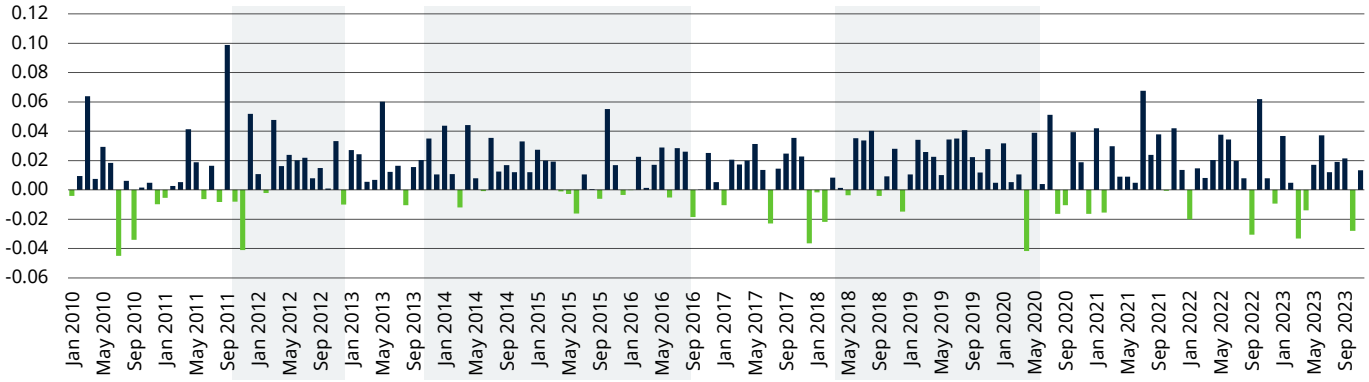
Smaller and growth-oriented impact firms appear to deliver the highest returns, while traditional value and momentum factors seem less relevant for these portfolios, reflecting some of the unique characteristics and priorities of impact investing. Additionally, robust performance across economic cycles suggests that impact portfolios may exhibit resilience and adaptability in challenging market conditions. Figure 5 further illustrates this resilience by showing average alpha by month over the sample period, with recession months in OECD countries shaded in grey.

Figure 4 shows that the impact firms, on average, have occasional months of underperformance, which do not seem to be clustered during recession months. While the recession indicator is not perfect – capturing recessions within OECD countries while our sample covers a broader geographic scope (as shown in Figure 1) – it remains a useful proxy. The most significant underperformance occurs in late 2010, 2011, and during the height of COVID-19.

Despite some negative monthly alphas during recessionary periods, many recession months outperform the benchmark, indicating that impact firms are relatively less sensitive to

[9]We used clustered standard errors by firm and year-month to account for patterns in the data, such as repeated observations of the same companies or time periods. This adjustment reduces the risk of overstating the precision of our results and ensures that the statistical tests are more robust to potential correlations within the data.

Figure 4: Alpha of impact firms versus MSCI ACWI IMI per month (grey shaded areas recession month in OECD countries)



economic downturns. However, alphas show greater variability during recessions; for example, in 2011, alphas range from -0.0408 to 0.099, reflecting heightened sensitivity to macroeconomic stress. Negative alphas are less frequent and smaller in magnitude during expansionary periods compared to recessions.

Overall, consistent with the cross-sectional results above, these findings suggest that impact portfolio provide a degree of downside protection during recessions while maintaining competitive performance during expansions. This resilience may stem from the structural characteristics of impact investments, such as their focus on certain sectors such as healthcare and industrials, which can remain relevant or even thrive during periods of economic uncertainty. Additionally, their emphasis on addressing global challenges could enhance their ability to weather economic cycles effectively.

While these interpretations are promising, they remain somewhat speculative and require further analysis to fully understand the mechanisms and drivers of the observed resilience and outperformance. They also have to be interpreted with caution in light of the survivorship bias discussed above. In the next section, we explore preliminary insights into these drivers, complementing the quantitative findings with qualitative case studies that offer anecdotal evidence of the factors contributing to impact returns.

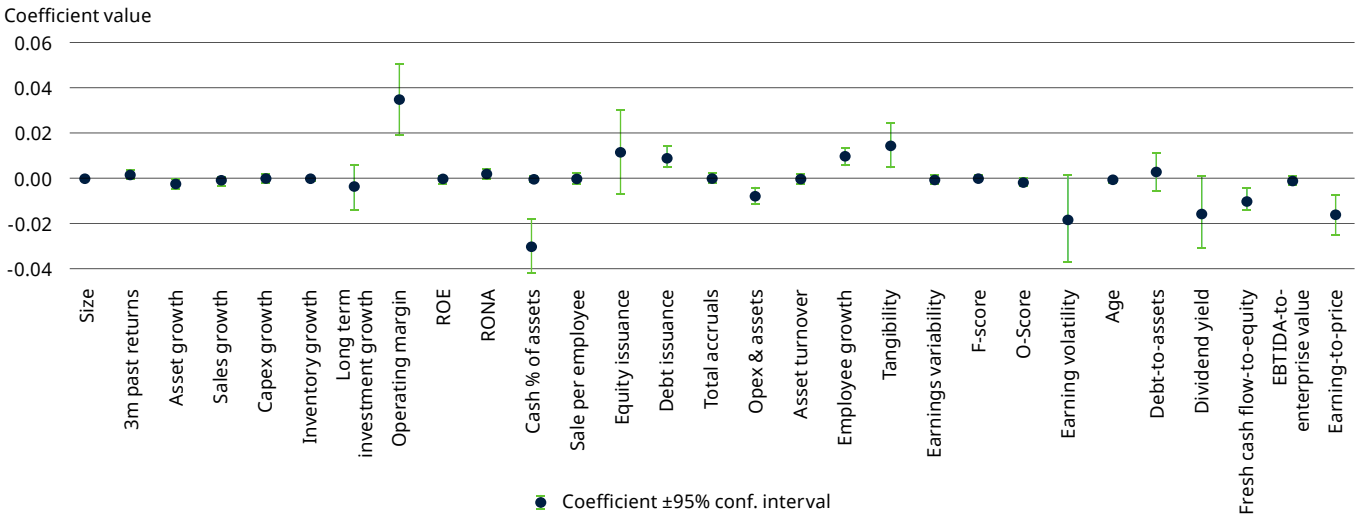
3.3 Drivers of financial returns

To explore differences between impact firms and the broader market, we compare their financial characteristics to a large sample of MSCI ACWI IMI constituents for which we are able to match financial variables. Using monthly logit regressions, we test whether being classified as an impact firm (indicator variable = 1) is associated with specific financial characteristics.[10]

Figure 5 summarises the results, showing the regression coefficients and 95% confidence band. The figure highlights several key financial characteristics that differentiate impact firms from the broader benchmark:

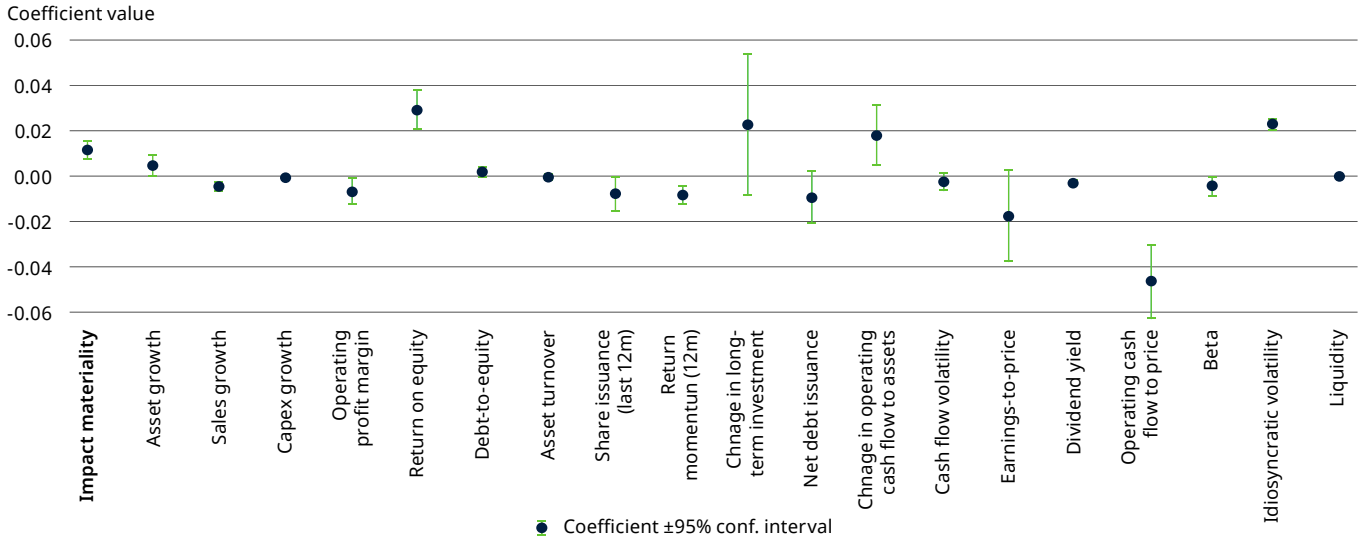
- **Operational efficiency and workforce expansion:** Impact firms exhibit significantly higher operating margins, suggesting they are more efficient at generating profit from their core business operations compared to the benchmark. Additionally, impact firms show higher employee growth, pointing to active expansion and investment in human capital.

Figure 5: Characteristics of Impact Firms versus MSCI ACWI IMI Constituents



[10]The data on firm characteristics comes from Jensen, Kelly, and Pedersen (2023) and Thomson Reuters Refinitiv. For definitions how these characteristics are calculated see https://jkpfactors.com/.

Figure 6: Drivers of Monthly Excess Returns of Impact Firms



- **Capital structure differences:** Impact firms tend to hold a lower percentage of cash to total assets, suggesting a more active capital deployment strategy. They are also more likely to issue debt and equity, indicating that they have been successful in recent fundraising efforts. This ability to access external capital supports the idea that these firms are in a growth phase, leveraging financing to expand operations.

- **Higher asset tangibility:** Impact firms possess greater asset tangibility, meaning a larger share of their assets consists of physical, tangible items like property, equipment, and inventory, rather than intangible assets such as goodwill, patents, or brand value. This could mean they are in industries that require more physical capital (e.g., renewable energy, infrastructure, or manufacturing). It could also indicate that they have less goodwill on their balance sheet, as they tend to be smaller and earlier stage, so may have fewer acquisitions.

- **Higher valuation multiples:** The figure suggests that impact firms have lower free cash flow and earnings-to-price ratios, indicating that they may trade at higher valuations relative to earnings and cash flow, a common characteristic of growth-oriented firms.

There seem to be no difference in other financial characteristics between impact firms and the benchmark. Overall, these findings suggest that impact firms are distinguished by their strong operating margins, increased access to external financing, active workforce expansion, and capital deployment strategies. While traditional revenue growth metrics may not show a clear acceleration, the combination of higher equity and debt issuance, increased employee growth, and financial positioning indicates that these firms are actively building scale and investing in long-term expansion.

Next, we examine the drivers of financial returns for the impact firms. To do this, we regress monthly excess returns on various fundamental firm characteristics that have been found to be associated with stock returns in prior literature. We include as explanatory variable a measure of impact materiality that captures the percentage of a company's revenues aligned with the key impact intent of the company. Figure 6 summarizes the results. The regression includes country and time-varying sector controls.[11]

1. **The coefficient for impact materiality is positive at 0.012 and statistically significant at the 1% level. This suggests that firms with a higher percentage of revenues aligned with their impact themes generate higher excess returns controlling for a variety of firm characteristics associated with stock returns.**

The coefficient magnitudes suggest that companies with a 100% impact materiality generate monthly excess returns that are about 1.2% higher than those of firm with no impact alignment. The results on the control variables suggest that:

2. Impact firms with higher return on equity and lower cash flow volatility generate higher returns.

3. Impact firms with higher sales and capex growth and high dividend yield and operating cash flow to price ratios generate lower excess returns.

Overall, the results demonstrate that financial returns for impact firms are associated with their impact focus. **Specifically, impact materiality, the stronger alignment of revenues with impact, emerges as a driver of returns. This reinforces the idea that firms that generate revenues from measurable impact succeed in aligning impact and financial return objectives. However, these empirical tests do not allow for a causal interpretation, and it is still possible that impact materiality is correlated with some other financial or quality characteristic not controlled for in the regressions.**

To test the robustness of these findings, in un-tabulated robustness tests we repeat the regressions using the common risk factors as before as predictors of returns instead of firm characteristics and include the Quality minus Junk (QMJ) factor developed by Asness, Frazzini and Pedersen (2019) as an additional factor to control for a possible correlation of impact materiality with high-quality firms. We further include the same country, sector and year-month controls. We find a

[11]The data on firm characteristics comes from Jensen, Kelly, and Pedersen (2023) and Thomson Reuters Refinitiv.

similar and statistically significant coefficient of about 0.96% on impact materiality.

While the quantitative analyses establish an association between impact alignment and financial performance, they cannot fully capture the operational nuances or strategic decisions that drive this relationship. To complement these findings, we explore case studies of individual firms that exemplify how addressing global challenges can create measurable impact alongside competitive financial returns. These examples illustrate the mechanisms through which impact strategies align with robust financial outcomes, offering a more nuanced understanding of impact investing in practice.

4 Case studies

The fundamental hypothesis underpinning impact investment strategies is that enterprises addressing critical global issues identified by the SDGs are likely to experience tailwinds that enhance their financial performance relative to the broader market. These tailwinds include benefitting from supportive policy environments, appealing to changing consumer preferences, tapping into new end markets, and creating innovative solutions characterized by strong competitive moats.

This perspective is grounded in the premise that innovative, profitable companies operating in public equity markets are producing goods and services essential for the transition to a more sustainable, efficient, and health-oriented global economy. As Professor Michael E. Porter observed, "When a social need can be tackled with a profitable business model, the magic of capitalism is unleashed." This principle underscores the potential for such companies to deliver both societal benefits and competitive financial returns.

4.1 Schneider Electric: A business transformation for a new economy

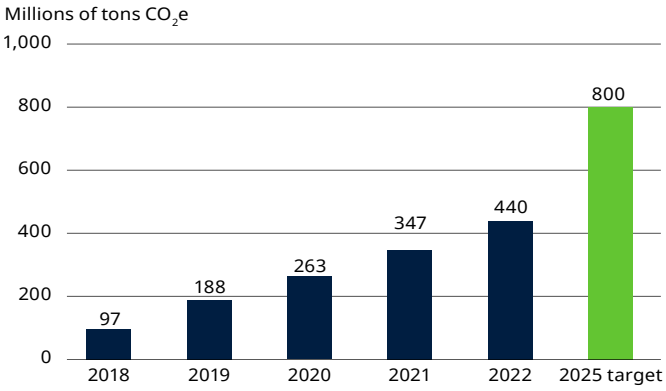
Schneider Electric demonstrates how a strategic transformation can align meaningful impact with financial outperformance. Over the past decade, Schneider Electric has evolved from a traditional electrical components provider into a global leader in digital energy solutions. This shift positions the company at the nexus of electrification and digitalisation, addressing global challenges whilst driving structural growth.

Schneider Electric's value proposition is rooted in three core elements: measurement, data processing, and control. By harnessing vast flows of data, Schneider Electric empowers customers to monitor and optimise the performance and energy utilisation of their operating assets – ranging from production lines in factories to batteries in off-grid solar power systems.

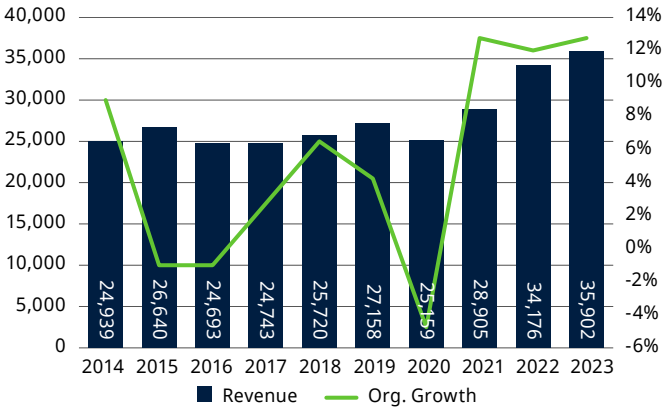
At the heart of this offering is Schneider Electric's flagship EcoStruxure platform, which integrates data from various operational components into a unified interface. This platform delivers actionable insights, enabling smarter decisions – such as detecting room occupancy in buildings to optimize lighting and energy use or monitoring critical electrical grid components to prevent outages. Schneider Electric's portfolio spans advanced digital solutions to essential infrastructure products, including circuit breakers, transformers, and variable speed drives. These offerings reduce costs, enhance operational efficiency, and lower emissions, making them indispensable to the global transition to a low-carbon economy. Without this foundational infrastructure, the speed and scale of electrification required to meet climate goals would be unattainable.

Between 2018 and 2022, Schneider Electric's solutions helped customers avoid 440 million tons of CO_2 emissions, with a target to reach 800 million tons by 2025. These achievements underline Schneider Electric's pivotal role in driving a sustainable energy transition.

Cumulative tons of CO_2e saved and avoided by customers thanks to Schneider Electric's products, since 2018



Schneider Electric revenue growth



Financial Performance: Impact as a growth engine

Schneider Electric's strategic transformation has not only established the company as a global leader in digital energy solutions but also driven exceptional financial performance. By capitalising on megatrends such as decarbonisation, industrial automation, and evolving energy policies, Schneider Electric has consistently outperformed its peers. In 2022, the company achieved 12.2% organic growth – well above industry

benchmarks – while adjusted EBITA margins reached 17.6%, with a long-term target exceeding 18%. Consensus estimates imply an organic compound annual growth rate (CAGR) of close to 8% for the company's topline between 2025-2027. The proportion of project expenditures dedicated to Schneider's solutions has grown from 3% to 6%, reflecting their rising importance in enabling efficient, decarbonized systems. The company's scale and cost leadership enhance its ability to deliver impactful solutions profitably, ensuring sustained financial growth while contributing to global impact goals.[12]

The company's technologies and products are increasingly indispensable, directly addressing customer needs to reduce costs, optimize energy usage, and lower emissions. This alignment with critical imperatives of the decarbonizing economy has driven a financial re-rating in equity markets, as investors recognize Schneider Electric's strategic positioning.

Schneider Electric's transformation – from a traditional hardware provider to a global leader in integrated digital energy solutions – demonstrates how businesses can align impact with financial performance. By addressing urgent global challenges through innovation, digitalization, and scale, Schneider Electric has created sustainable competitive advantages. The result is measurable environmental impact, significant growth opportunities, and robust financial returns, reinforcing the finding that impact investing does not need to come with concessional returns.

4.2 A model of inclusive growth: expanding market reach as a growth engine

Gentera is a regional microfinance institution operating in Mexico and Peru, focused on providing financial services to underserved populations. Its offerings include group and individual loans, insurance products, and financial education programs, with a particular emphasis on women and small-scale entrepreneurs.

Gentera's business model centres on empowering underserved populations through microfinance solutions tailored to their needs. Its loan portfolio is split evenly between group and individual loans, with an emphasis on supporting women and micro-entrepreneurs. The company's offerings range from working capital loans to insurance products, providing customers with essential financial tools to improve their livelihoods. For example, Gentera's insurance products help mitigate risks such health issues, strengthening customer resilience.

To expand its reach, Gentera combines a human-centric approach with operational efficiency. Its hybrid digital-physical model facilitates faster loan processing and paperless applications while maintaining the personal relationships essential for trust. By 2023, Gentera had reached almost 4 million active borrowers and has over 51 million active insurance policies.

Customer protection is central to Gentera's operations. The company adopts robust measures to safeguard clients from over-indebtedness, offering financial education and setting realistic repayment schedules. In addition, Gentera prioritizes fair treatment of clients facing repayment challenges, avoiding aggressive collection methods and ensuring transparent communication.

A critical driver of Gentera's growth stems from its focus on expanding the markets it serves. In Mexico, the company has shifted its attention to individual lending – a segment with significant growth potential among small-scale entrepreneurs. These loans are tailored to support working capital needs, targeting underserved entrepreneurs who lack access to traditional bank credit. Meanwhile, in Peru, Gentera has extended its operations into previously unbanked regions, creating opportunities for economic development and deepening its market penetration.

Financial performance: growth with purpose

Gentera's strategic focus on market expansion has yielded significant financial returns. Between 2021 and 2024, the company increased return on equity (ROE) to over 20%, while sustaining double-digit loan growth. Its deliberate efforts to penetrate new regions and serve underserved customer segments have unlocked structural growth opportunities.[10]

Gentera's disciplined execution and scalable business model ensure its capacity to maintain financial strength while broadening its impact. By reaching deeper into underserved regions and targeting new customer segments, Gentera has demonstrated how expanding addressable markets can align social impact with financial success. Its ability to adapt to market conditions – evident in proactive adjustments to credit policies and geographic expansion – positions it to sustain strong growth going forward. With a strong capital base, adaptability, and innovative approach, Gentera provides a compelling case for investing in businesses that prioritize financial inclusion while achieving both social and financial returns.

These case studies underscore how strategic alignment with impact objectives can drive financial performance, demonstrating the interplay between innovation, operational efficiency, and societal outcomes. However, they also highlight the diversity of approaches and contexts within impact investing, emphasizing the importance of sector, geography, and company-specific dynamics. Combined with the quantitative findings, these qualitative insights reinforce the need for further research to understand the broader applicability of impact investing strategies and their long-term implications for both investors and society.

[12]Past Performance is not a guide to future performance and may not be repeated. The value of investments and the income from them may go down as well as up and investors may not get back the amounts originally invested. Exchange rate changes may cause the value of investments to fall as well as rise. Any reference to regions/countries/sectors/stocks/securities is for illustrative purposes only and is not a recommendation to buy or sell any financial instruments or adopt a specific investment strategy.

5
Limitations and potential extensions

While this study provides valuable insights into the financial performance of impact investments in listed equities, several limitations warrant consideration:

1 Sample representativeness:
The impact portfolio analysed in this study is not fully representative of the broader market. Firms included in the sample are drawn from a curated universe approved through Schroders' proprietary impact toolkit, potentially biasing results toward higher quality, rigorously assessed impact investments. Expanding the sample to include a wider range of impact firms could provide a more comprehensive view.

2 Survivorship bias:
The impact portfolios analysed are based on companies that are part of Schroders' impact universe today. This means the analysis does not account for firms that may have exhibited strong impact credentials in 2010 but have since ceased to exist or been excluded from the universe due to financial underperformance, acquisition, or other reasons. As a result, the findings may overstate the financial performance of impact investments by focusing on companies that have demonstrated resilience and sustained operations over time. Schroders launched the first listed equity impact portfolio in 2021, meaning that it was not possible to construct a historical impact universe that includes firms from earlier periods. To partially address survivorship bias, we incorporated ACWI IMI survivors within the analysis in Section 3.1, comparing impact firms to other companies that have also remained in the index over time. Addressing this limitation further in future research would require identifying historical impact firms from earlier periods, even if they no longer exist today. This could provide a more accurate and comprehensive view of the relationship between impact and financial performance over time.

3 Sectoral and geographical skews:
The distribution of impact firms across sectors and geographies shows concentrations in healthcare, industrials, and technology, with significant geographic concentration in a few key markets. This uneven distribution may influence results, particularly regarding sectoral and regional performance dynamics. This pattern may, in part, reflect the focus of Schroders' impact portfolios rather than the broader distribution of impact stocks in the market. For example, the sectoral and geographical composition is shaped by Schroders' five core impact themes, which underpin the construction of the impact universe and inherently influence the types of companies included in the analysis.

4 Causality and mechanisms:
While the study identifies correlations between impact and financial performance, establishing causality remains challenging. It is unclear whether impact drives financial performance or if other intrinsic qualities (e.g., innovation, management quality) contribute to both. Several plausible mechanisms could theoretically explain a causal link but remain difficult to verify empirically. Impact firms may benefit from competitive moats that arise from addressing long-term structural challenges, such as climate change or social inequality, positioning them ahead of regulatory or consumer shifts. Many are also highly innovative, developing new technologies, business models, or solutions that create differentiation and drive financial returns. Additionally, their strong alignment with real-world challenges allows them to tap into growing demand for solutions in underserved markets or emerging industries. By expanding into new geographies, customer segments, or industries, these firms may broaden their addressable markets, creating additional revenue opportunities beyond traditional market constraints.

Further research should aim to isolate these mechanisms, perhaps by examining firm-level fundamentals over time or conducting experimental studies to better understand the drivers of impact-related financial performance.

5 Data availability and measurement challenges:
Assessing impact relies on high-quality data, which varies significantly across firms and regions. Limitations in data availability, standardisation, and reporting may affect the robustness of impact measurements. Future studies could explore how advancements in impact reporting standards influence these analyses.

Extensions to this research

Building on this research, several avenues for future exploration include:

- Expanding the analysis to new asset classes, including within private markets, where impact investing is also prominent
- Delve deeper into the drivers of financial returns to impact companies and use more robust empirical designs to examine causal relationships
- Future research could explore whether impact is associated with higher revenue or earnings growth rates, future profitability levels, or improved capital efficiency, rather than focusing solely on stock market total returns. Expanding the scope of financial performance metrics may provide a more comprehensive understanding of how impact aligns with long-term value creation

6
Conclusion

This study provides compelling evidence that impact investing in listed equities can deliver competitive financial returns while achieving meaningful social and environmental outcomes. By leveraging a combination of rigorous quantitative analyses and qualitative case studies, we challenge the notion that impact investing inherently requires financial trade-offs. Our findings provide initial evidence that impact and profitability can align, and that impact investing is not inherently concessionary.

Key takeaways include:

1
Competitive returns:
The study found that impact portfolios delivered strong absolute and risk-adjusted returns, exhibiting statistically significant alpha that is unexplained by traditional risk factors.

2
Lower volatility, greater resilience:
Impact portfolios exhibited lower volatility, smaller drawdowns, and reduced downside risk compared to the benchmark, indicating greater stability. Impact portfolios showed strong performance during recessions, with defensive characteristics in sectors like healthcare and industrials. Their sensitivity to market risk is lower in recessions than in expansions, meaning they experience smaller declines in downturns while benefiting more from strong marketsfindings provide initial evidence that impact and profitability can align, and that impact investing is not inherently concessionary.

3
Impact materiality as a source of alpha:
Companies with higher revenue alignment to impact generated superior financial returns, suggesting that impact itself can be a driver of financial performances

While the findings are promising, this research is not without limitations. Survivorship bias, sectoral concentration, and the challenge of establishing causality highlight areas for further investigation. Future research should expand the scope to include a broader dataset, explore private markets, and examine causal links between impact alignment and financial performance.

In conclusion, this research reinforces the viability of impact investing as a dual-purpose strategy, capable of delivering both competitive financial performance and measurable contributions to addressing global challenges. As investor demand for purpose-driven portfolios continues to grow, impact investing is poised to play a critical role in shaping portfolio allocations where the pursuit of financial returns is aligned with generating positive outcomes.

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