FINAL REPORT

Methodology for Eurosif Market Studies on Sustainability-related Investments

Measuring progress of capital flows to support the sustainable transition of the real economy

The methodology was developed by Eurosif's SRI Study Group (SSG) in cooperation with the University of Hamburg, the Sustainable Finance Research Group, and Advanced Impact Research (AIR). In the course of 2023, both feedback from SSG members and from other practitioners was taken into account to make the methodology practicable, and we thank everyone involved for the constructive feedback.

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Hamburg/Brussels, February 2024

Executive Summary

The purpose of this paper is to present a new methodology for market studies on sustainability-related investments. The paper is based on an earlier white paper by the University of Hamburg and Eurosif (Busch et al. 2022). The updated methodology was developed by Eurosif's SRI Study Group (SSG) in cooperation with the University of Hamburg, the Sustainable Finance Research Group (SFRG) and Advanced Impact Research (AIR). Over the course of 2023, feedback from both SSG members and other practitioners was taken into account to make the methodology practicable.

Past market studies on sustainability-related investments typically gathered data on a range of different sustainability-related investment approaches and aggregated them to one of a number of "sustainable investments". However, these statistics did not differentiate between investments based on their investment strategy and/or objectives to actively support the transition towards a more sustainable economy.

The methodology presented in this paper aims to reflect current approaches to sustainability-related investment across Europe more accurately. It introduces four distinct categories of sustainability-related investments that reflect the investments' ambition level to actively contribute to the transition towards a more just and sustainable economy (see Table below). In this context, "ambition" level refers to the intention to achieve desired positive sustainability outcomes in the real economy.

Two core features of the proposed approach are that it applies to all asset classes and that investments only qualify as one of the four categories if they implement binding ESG- or impact related criteria in their investment process.

The methodology will serve as a basis for future market studies conducted by Eurosif in cooperation with its members. It will also be available to all Sustainable Investment Forums globally and other stakeholders to use. It is not intended to reflect the categorisations of sustainable products as established within regulatory frameworks but to be sympathetic with such systems and labels as they emerge.

Methodology for market studies on sustainability-related investments

		Basic ESG	Advanced ESG	Impact-Aligned	Impact-Generating
Investment objective		Integration of ESG factors	Systematic analysis & incorporation of ESG factors	Align with positive impacts on environment and/or society	Measurable contribution to positive real-world impacts
Investment process	**Investment approach**	Binding negative or positive screening	Binding negative & positive screening (≤80% of initial universe investable)	Binding negative & positive screening for assets with positive impact	Exclude non-transformable activities & use stewardship or provide new capital to assets to generate measurable positive impact
	Performance Measurement	-	Measurement of ESG performance	Measurement of company impact	Measurement of company impact & investor contribution
Ambition level		Low	Moderate	Medium	High
Investment focus		Double materiality			

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1 Introduction

There has been a tremendous increase in investments in the ESG (environmental, social and corporate governance) and sustainability context over the last decade—especially in Europe. The Global Sustainable Investment Alliance (GSIA) estimates that these investments have reached $30.3 trillion in 2022 globally (GSIA, 2023).[1] While such estimates are helpful to provide a broad picture of market trends for overall sustainability-related investments in terms of capital flows and total volumes, questions may arise as to what these studies consider "sustainable". Typically, a range of different investment approaches are included and aggregated into one number. These statistics do not differentiate investments based on their "ambition" or stated objective to actively support the transition towards a more just and sustainable economy. However, the shift towards actual impact is fundamental to "fully unlock the potential and the transformative power of capital markets and close the investment gap to achieve net-zero and the SDGs" (Eurosif, 2021, p. 6). The Paris Agreement also illustrates the need for this shift, stating that finance flows need to be "consistent with a pathway towards low greenhouse gas emissions and climate-resilient development" (UN Paris Agreement, 2015, Art. 2(c)). As such, the support of private finance is essential to effectively mitigate climate change.

Different regulatory approaches to promote sustainable investments have emerged in recent years, including, most prominently, the EU's agenda for sustainable finance. Its goals include fostering transparency and long-termism and reorienting capital flows towards a more sustainable economy (European Commission 2020a). Among others, the Sustainable Finance Disclosure regulation (SFDR) and the EU Taxonomy Regulation (European Commission 2019, 2020b, 2021) are key regulations that aim to increase the transparency of investments on sustainability matters and enable investors to make informed decisions as to how they may wish to reorient their capital. Their key concepts are also applied in other important regulations, such as the Markets in Financial Instruments Directive (MiFID II), to identify which types of sustainability products can be proposed to end investors depending on their sustainability preferences. Even though these regulations define "sustainable investments", neither of them sufficiently exploits the potential contribution of investments in a transition towards a more

[1] The Global Sustainable Investment Alliance's (GSIA) 2022 Review does not compare the change in global sustainable investing assets between 2020 and 2022 due to a "material change in the US methodology and the quantum of assets represented by this region" (GSIA, 2023, p. 10). They do, however, compare the numbers for the rest of the world (Europe, Canada, Australia & New Zealand and Japan), where they report a 20 percent increase in volumes.

sustainable economy. For example, the SFDR's definition of sustainable investments in Art. 2(17) does not distinguish between investor and company impact, one of the basic concepts in understanding how investors can achieve impact (Kölbel et al., 2020).

Company impact is defined as "change that a company's activities achieve in a social or environmental parameter" (Kölbel et al. 2020, p. 3). Investor impact refers to a change in company impacts within the portfolio actually caused by the investor's activities (Kölbel et al., 2020). In other words, company impact describes a real-world change, while investor impact is evident in cases when such a change is initiated / induced by the investor. In the following, we will use the term "investor contribution" for investor impact. We consider both terms to be equivalent.

As such, it remains unclear in the current sustainable investment frameworks whether an investment actually seeks to make any contribution to the transition. Therefore, future market studies on sustainability-related investments[2] need to use a methodology that (1) builds upon current regulatory developments and (2) provide additional terminology where necessary to provide transparency around an investment's ambition and stated objective to actively contribute to the sustainable transition.

Objective of this Paper

The purpose of this paper is to provide a new methodology for market studies on sustainability-related investments. The paper is based on an earlier white paper by the University of Hamburg and Eurosif (Busch et al. 2022). The updated methodology was developed by Eurosif's SRI Study Group (SSG) in cooperation with the University of Hamburg, the Sustainable Finance Research Group (SFRG), and Advanced Impact Research (AIR). Over the course of 2023, both feedback from SSG members and other practitioners was taken into account to make the methodology practicable. First, this report introduces clear dimensions to define investment categories, namely the main objective, the investment approach, and the sustainability - or impact performance measurement.[3] Second, the investment approach dimension of the methodology builds upon widely applied sustainability-related investment approaches, which were recently updated by the Global Sustainable Investment Alliance (GSIA), the CFA

[2] We use the terms "investments" or "financial products" as synonyms. We use these terms to refer to activities of asset owners or asset managers. We do not use these terms to describe the activities of investees (such as companies or sovereigns)

[3] Using all three of these dimensions to define the methodology for market studies is important to provide the necessary transparency and goes beyond the current definitions of Articles 8 and 9, which are "neutral in terms of product design, or investing styles" (Joint Committee of the European Supervisory Authorities, 2023, p. 26).

Institute, and the Principles for Responsible Investment (PRI) (GSIA et al., 2023). Based on this, the methodology proposes four distinct categories of sustainability-related investments that reflect on the investments' ambition level to actively contribute to the transition towards a more just and sustainable economy.

It is important to be transparent about the purpose of this methodology from the start. In the past, the rationale behind established SRI (Sustainable & Responsible Investment) market studies, e.g., those that were published by GSIA, Eurosif, or national Sustainable Investment Forums (SIFs), was to gather data and establish statistics about which sustainability-related investment approaches investors applied within a given market. The intention was not to generate any statement about the effectiveness of individual investments, i.e. how responsible or sustainable a given investment approach is. This is true across different approaches (e.g., ESG integration vs. best-in-class) as well as within one approach (e.g., whether two or five exclusion criteria are applied). The proposed methodology in this paper follows a similar logic. Its purpose is to gather data on different categories of sustainability-related investments and provide transparency about their main characteristics. This includes the transition-related ambition levels that investors pursue within a given market to achieve positive sustainability outcomes in the real economy (like decreasing CO2-emissions or increasing incomes of small farmers through microfinance). The intention is not to generate any statement about the impact of individual investments, i.e. to what extent investments effectively contribute to change (impact magnitude). Such claims go beyond the scope and possibilities of market studies since this would require gathering and reassuring a significant amount of additional data and information.

The paper is organised as follows: First, we introduce the dimensions and criteria that serve as the foundation for the methodology. Next, we present the resulting categories for sustainability-related investments and elaborate on their underlying logic. The third chapter concludes and provides an outlook for next steps. Appendix A provides a questionnaire developed by the SSG in cooperation with the University of Hamburg and Advanced Impact Research (AIR) that can be used to gather the data required for the new classification scheme. Appendix B provides an overview of important terms as a background to chapter 2. Appendix C provides a mapping of the categories defined in this methodology in light of several regulatory developments.

2 Methodology for sustainability-related investments

2.1 Dimensions defining the categories

From a methodological point of view, sustainability-related investments can be defined and distinguished based on three dimensions: (1) the investment objective, (2) the investment approach, and (3) the ESG- or impact performance measurement.

Investment objective

The investment objective[4] describes the explicit, sustainability-related goal of an investment. The investment objectives defined for this methodology describe how different categories of investments use the sustainability-related information reported by investees in their investment processes and product design. In July 2023 the European Commission published the European Sustainability Reporting Standards (ESRS), which prescribe what sustainability-related information large companies need to disclose, namely material sustainability-related risks, opportunities, and impacts (ESRS, 2023) (see also appendix B for an overview of important terms). Reflecting on this logic, our methodology differentiates between four types of sustainability-related investment objectives: (1) integration of ESG factors, (2) Systematic analysis & incorporation of ESG factors, (3) Alignment with positive impacts on environment and/or society, and (4) Having a measurable contribution to positive real-world impacts. The first two objectives focus on ESG risks and/or opportunities, while the latter two objectives focus on sustainability-related impacts (see section 2.2. for a category-specific description).

Sustainability-related investment approaches

In November 2023, the GSIA, the CFA Institute and the PRI published a set of definitions for sustainability-related investment approaches (GSIA et al., 2023). Their goal was not to provide criteria for product categorisation, but to increase understanding and consistency of terminology used in responsible investment. Recognising the need for convergence in the terminology of sustainability-related investments our methodology considers the investment approaches defined by GSIA and partners which are relevant to define the concrete sustainability-related investment categories proposed in this methodology. This section

[4] Many regard the intentionality of an investment to be an important defining criterion, especially for impact investments (Höchstädter & Scheck, 2015). Others criticise the concept of intentionality for not being observable and, hence, not directly measurable (Busch et al., 2021). We regard the investment objective to be the operationalisation of an investment's intention. We, therefore, use the term objective, since it describes concrete and measurable goals that reflect the intention of the investor / asset manager.

summarises the relevant GSIA definitions and explains their relevance for our methodology for future markets studies.

Screening. The GSIA defines screening as "Applying rules based on defined criteria that determine whether an investment is permissible" (GSIA et al., 2023, p. 3). They specify different types of screening that can be summarised as positive and negative screening. Positive screening determines whether an investment is permissible based on ESG criteria that are (1) desirable (positive screening per se), (2) desirable relative to peers (best-in-class screening), or (3) show compliance with ESG standards and norms (norms-based screening). Negative screening determines whether an investment is not permissible based on (1) (undesirable) ESG criteria (exclusionary screening), or on (2) non-compliance with ESG standards and norms (norms-based screening). In the methodology proposed in this paper, the desirability of ESG criteria or sustainability matters is determined by an investment's objective. It is important that screening is considered to be a binding element: "Screening rules categorically determine whether individual investments are permitted in a portfolio" (GSIA et al., 2023, p. 4). All types of screening can be used to implement the four investment objectives described above, but the screening approach differs depending on the objective (see section 2.2 for a specific description for each category of investment). While GSIA does not explicitly mention the best-in-universe or best-in-progress approaches, both can be understood as possible positive screenings. Best-in-universe entails selecting only leading or best-performing investees or assets within a universe. The best-in-progress or best-effort approaches selects investees based on their improvement regarding specific sustainability criteria or overall ESG/SDG ratings over time.

ESG Integration. GSIA defines ESG integration as "Ongoing consideration of ESG factors within an investment analysis and decision-making process with the aim to improve risk-adjusted return" (GSIA et al., 2023, p. 8). This definition implies that ESG factors are one aspect among others that are considered in investment processes. It does not mean that there are explicit ESG-related restrictions on the investment universe. Following this definition, ESG integration solely refers to considering ESG factors in the investment analysis and decision-making process – independently of what the actual effect of this consideration is. From this understanding, a company's impacts on the environment or society are not part of ESG integration since integration only focuses on financially material ESG factors. In contrast to screening approaches, ESG integration is not binding for investment decision-making: "ESG integration does not prescribe or preclude any investment opportunity" (GSIA et al., 2023, p.

10). In other words, ESG integration does not necessarily entail a binding sustainability-related selection or screening approach. For the proposed sustainability-related investment categories of this methodology, however, binding selection processes are a necessary condition. This is why the methodology does not count those volumes of sustainability-related investments that only use ESG integration. Instead, investments that use ESG integration can only be classified in our methodology if their ESG integration entails a binding sustainability-related selection or screening process (see chapter 2.2).

Thematic investing. Thematic investing is defined as "Selecting assets to access specified trends" (GSIA et al. 2023, p. 12). Trends can refer to economic, technological, demographic, social or environmental dynamics, among others. Key to thematic investing is the belief that such trends are closely connected to investment risk and return (GSIA et al., 2023). Importantly, thematic investing is not restricted to the optimisation of investment risk and return. It may also serve to increase exposure to sustainability trends: "investors may fund a sustainable agriculture project with the aim of supporting the trend toward greater use of these practices" (GSIA et al., 2023, p. 12). For the methodology described here, only sustainability-related thematic investing is relevant (i.e. investing focusing on trends that are connected to sustainability matters). Even though GSIA defines thematic investing as an investment approach in itself, we incorporate thematic investing as one specific form of positive screening. As a result, thematic investing is especially helpful as an investment approach to implement the second, third, and fourth investment objectives defined above.

Stewardship. Stewardship is defined as "The use of investor rights and influence to protect and enhance overall long-term value for clients and beneficiaries, including the common economic, social, and environmental assets on which their interests depend" (GSIA et al., 2023, p. 14). Examples of using investor rights are serving as or nominating directors to a company's board, filing shareholder proposals, voting in shareholder meetings (voting) or directly engaging with (potential) investees (engagement) (GSIA et al., 2023)[5]. Protecting and enhancing long-term value includes both the market value of a portfolio, and the "common environmental, natural, intellectual, social, and institutional assets that underpin all economies" (GSIA et al., 2023, p. 14). In other words, stewardship is not only about protecting and enhancing the financial performance of portfolios, but also about protecting and enhancing the environment and society

[5] In many engagement processes, the direct dialogue plays a central role in trying to influence investees, while voting is often used as an escalation strategy in case direct dialogues do not lead to the expected results.

long-term, as a basis for economic activity. Consequently, stewardship can be used as a sustainability-related investment approach to implement all types of investment objectives (optimising risk and return from an ESG perspective or contributing positively to social or environmental impacts).

ESG and impact performance measurement

ESG or impact performance measurement is the last dimension used to define sustainability-related investment categories in the proposed methodology. ESG performance measurement refers to the measurement of performance in relation to specific sustainability risks and/or opportunities. This is often implemented by ESG ratings (for example on scales like AAA–CCC or numeric scores between 0–100). Impact performance measurement refers to the measurement of real-world changes. These impact measurements have to refer to company impact, defined as "change that a company's activities achieve in a social or environmental parameter" (Kölbel et al., 2020, p. 3). In cases where the investor intends to illustrate the impact that he/she generated, a reference should be made to the change in company impacts within the portfolio actually caused by the investor's activities.

In practice, the term "investor contribution" is more common than "investor impact" which is why we use investor contribution. We propose to define investor contribution as "The contribution that the investor makes to enable enterprises (or intermediary investment managers) to achieve impact" (IMP, 2023a). This definition of the Impact Management Platform (IMP) is shared by many important actors and stakeholders in the impact field.[6]

Impact measurements include the measurement of changes in environmental and/or social outcomes (either directly or via the assessment of reasonable proxies) and whether the company and/or investor contributed to that change. Several ESG research agencies provide SDG ratings that aim to measure the positive and negative impacts companies generate through services, products, and business practices and operations. The EU taxonomy provides another example for a framework that helps measuring the impact of concrete economic activities of assets or companies. It can also be used to plot an investee's trajectory towards meeting an environmental objective (e.g., using CapEx data) and allows for reporting on company impact.

[6] Partners of the IMP include, among others, the Organisation for Economic Co-operation and Development (OECD), the United Nations Environmental Programme Finance Initiative (UNEP-FI), the International Finance Corporation (IFC), the United Nations Development Program (UNDP), the Global Reporting Initiative (GRI), the Capitals Coalition, and the Global Impact Investing Network (GIIN).

It is not, however, a tool to measure investor contribution. This would require further information about the investor's activities.

Ambition level and investment focus

As a key feature, our methodological approach enables insights into the ambition level and investment focus of sustainability-related investments. In this context, ambition refers to an investor or asset manager's effort to actively support the transition towards a more sustainable economy. The ambition level describes how far the investment objective, investment approach, and ESG or impact performance measurement reflects the goal of contributing to the sustainable transition. Being explicit and clear about the ambition level of investments is a central element to create transparency about the actual characteristics of individual investments – i.e. if they effectively seek to contribute to the transition. The term ambition is also used in the regulatory context of the SFDR, without being clearly defined.[7]

It is important to note that the ambition level does not imply details about the impact of individual investments, i.e. to what extent investments effectively contribute to social or environmental change (impact magnitude). As mentioned in the introduction, such claims go beyond the scope and possibilities of this methodology for market studies. Table 1 shows the ambition levels of all four categories. Based on their respective investment objective, investment approach and ESG or impact performance measurement, the ambition level of the four categories increases from left to right (see chapter 2.2 for category-specific explanations).

The methodology provides insights into different sustainability-related investment focuses of investments. The investment focus describes the relevance of sustainability in an investment's objective, in the general investment approach, and within the ESG or impact performance measurement. The methodology starts from the left side of the table with a primary focus on sustainability matters that are financially material (ESG-related risks and/or opportunities as defined in the context of the ESRS, see appendix B). From left to right, the categories add an increasing focus on sustainability matters that are material from an impact perspective, which is why the focus on double materiality (financial and impact materiality combined) increases

[7] The questions and answers between the European Supervisory Authorities (ESAs) and the European Commission establish that Article 8 products have a lower sustainability-related ambition compared to article 9 products: "Article 8 of Regulation (EU) 2019/2088 lays down transparency rules for financial products that have a sustainability-related ambition lower than the ambition of financial products subject to Article 9" (Joint Committee of the European Supervisory Authorities, 2023, p. 29). It is, however, not further defined– i.e. more detailed –what ambition in this context actually means.

in Table 1. It is important to note that sustainability matters can be material from a financial or an impact perspective, or both. As a result, this implies, that financial and impact materiality are not always clearly distinguishable.[8]

[8] The ESRS describe the relationship between impact and financial materiality in the following way: "A sustainability impact may be financially material from inception or become financially material, when it could reasonably be expected to affect the undertaking's financial position, financial performance, cash flows, its access to finance or cost of capital over the short-, medium- or long-term. Impacts are captured by the impact materiality perspective irrespective of whether or not they are financially material." (ESRS, 2023, p. 9).

2.2 Four categories of sustainability-related investments

The proposed methodology introduces four sustainability-related investment categories: (1) Basic ESG investments, (2) Advanced ESG investments, (3) Impact-Aligned investments, and (4) Impact-Generating investments (Table 1). One overarching criterion that applies to all four categories is that they only use sustainability-related screening approaches that are binding. The four categories are also intended to be applicable across asset classes. One investment can fulfil the criteria for more than one category but should be classified into the highest category (e.g., if an investment fulfils the criteria for Advanced ESG and Impact-Aligned investments, it should be classified as an Impact-Aligned investment).

Table 1: **Methodology for market studies on sustainability-related investments**

		Basic ESG	**Advanced ESG**	**Impact-Aligned**	**Impact-Generating**
Investment objective		Integration of ESG factors	Systematic analysis & incorporation of ESG factors	Align with positive impacts on environment and/or society	Measurable contribution to positive real-world impacts
Investment process	**Investment approach**	Binding negative or positive screening	Binding negative & positive screening (≤80% of initial universe investable)	Binding negative & positive screening for assets with positive impact	Exclude non-transformable activities & use stewardship or provide new capital to assets to generate measurable positive impact
	Performance Measurement	-	Measurement of ESG performance	Measurement of company impact	Measurement of company impact & investor contribution
Ambition level		Low	Moderate	Medium	High
Investment focus		Double materiality			

Basic ESG investments

The main objective of Basic ESG investments is to integrate ESG factors with a focus on ESG risks or opportunities, including a possible focus on normative or ethical reasoning. As a result, Basic ESG investments provide an important category for the traditional focus of investors on long-term risk-adjusted returns or the focus on excluding companies from an ethical or sustainability perspective. To implement this goal, they use binding negative or positive screening, i.e. restrictions in the selection of companies or assets.

Negative screening of Basic ESG investments can for example be exclusionary screening or norms-based screening that enables the mitigation of ESG risks, such as excluding investments involved in the production of fossil fuels, human rights violations, or CO_2-intensive industries. In terms of positive screening, Basic ESG investments could use best-in-class screening or norms-based screening that focuses on investing in compliant companies or assets. Basic ESG can also use thematic investing to focus on ESG opportunities.

While Basic ESG investments assess risks or opportunities to implement their investment approach, they do not carry out explicit ESG performance measurements.

Basic ESG investments have a low ambition level since they do not include the contribution towards a sustainable transition in their investment objective or investment approach.

Advanced ESG investments

Advanced ESG investments systematically analyse and incorporate ESG factors with a focus on ESG risks and opportunities. With a clear additional focus on opportunities, they can go beyond the pure risk mitigation perspective that Basic ESG investments pursue. While the transition towards a more sustainable economy is not the explicit focus of such investments, Advanced ESG investments can still indirectly contribute to the transition, since ESG risks and opportunities often also include aspects that are relevant to support a sustainable transition (e.g. allocating capital to increase energy efficiency is reducing costs and supporting a sustainable transition).

To manage ESG risks or opportunities, Advanced ESG investments apply binding positive and negative screenings, such as excluding investments linked to the production of fossil fuels, human rights violations, or CO_2-intensive industries, to reduce exposure to material ESG risks. They can also use best-in-class, best-in-universe, best-in-progress or thematic investing as positive screening to focus on opportunities connected to specific ESG trends. One important

criterion that distinguishes Advanced from Basic ESG investments is that only 80 percent or less of the initial investment universe is still investable after screening. For thematic investing this threshold does not apply since respective investments should have an exclusive focus on one or more specific sustainability objectives. It is therefore assumed that a large portion of investable assets are automatically not investable.

While stewardship is not required for investments to qualify as Advanced ESG they might still use it as an additional part of their strategy, for example to differentiate themselves from other Advanced ESG investments. Stewardship alone, however, is not sufficient to be classified as Advanced ESG, since these investments need to implement binding positive and negative screening leading to a reduction of the initial investment universe (see above). In cases when Advanced ESG investments use stewardship in a way that fulfils the necessary criteria (see category Impact-Generating investments below), this can also lead to a higher classification in the proposed methodology.

In contrast to Basic ESG investments, Advanced ESG investments measure the ESG Performance of investees or assets they invest in. Examples include ESG-KPIs or ratings that measure financially material ESG factors, like the Principal Adverse Impact Indicators (PAIs) (e.g., GHG emissions or violations of the United Nations Global Compact (UNGC) principles), or ESG ratings that focus on the measurement of ESG risks and opportunities.

Advanced ESG investments have a moderate ambition level. While they have a focus on financially material sustainability matters in their investment objective, investment approach, and performance measurement, they can aim to utilise ESG opportunities or trends. If these trends are material from both a financial and impact perspective (e.g., financing new renewable energy projects), Advanced ESG investments can also contribute to the sustainable transition of the economy, which justifies a moderate ambition level.

Impact-Aligned investments

Alongside their financial risk and return objective, Impact-Aligned investments have the objective and strategy of contributing to positive social or environmental real-world changes by aligning with positive impacts of investees or assets. They use binding positive and negative screening to implement this objective.

Negative screenings like exclusion or norms-based screening exclude investees with negative impacts, like companies producing fossil fuels or violating human rights. The positive

screening selects investees with positive impacts on environmental or social factors, for example, using the SDGs or the EU taxonomy as reference frameworks. Possible positive screenings include best-in-class[9] or thematic investing. As a consequence, the investment approaches used by Impact-Aligned investments seem quite similar to those used by Advanced ESG investments. The main difference is that Impact-Aligned investments are transparent about company impacts since they provide evidence through their impact performance measurement. This can be done, for instance, by highlighting the GHG emissions per invested Euro and comparing this to a benchmark. Advanced ESG investments, in contrast, primarily focus on ESG risks and/or opportunities and, accordingly, measure the ESG performance of investees or assets. This can be done, for instance, by aggregated ESG scores.

While not necessary, Impact-Aligned investments can also implement stewardship approaches, for example by distinguishing themselves from other Impact-Aligned investments. In cases when Impact-Aligned investments use stewardship in a way that fulfils the necessary criteria (see category Impact-Generating investments below), this can also lead to a higher classification in the proposed methodology.

Impact-Aligned investments measure company impact performance which captures the impacts of investees (company impact), providing the information necessary to select investees with positive impacts. These impacts need to refer to environmental or social objectives which are science-based or, in the case of social objectives, norms-based, e.g., referring to universally recognised sustainability frameworks like the SDGs, planetary boundaries, or human rights. There are many measurement approaches for company impact, both in public and private markets (Grieco et al., 2015; Klein & Rajagopalan, 2020; Corvo et al., 2021). The Impact Management Platform (IMP) provides an overview of how to approach impact measurement in practice (IMP, 2023b).

Impact-Aligned investments have a medium ambition level because they explicitly aim to align their portfolio with investees with positive impacts. This impact focus is systematically applied in their investment approach and impact performance measurement, increasing the likelihood of an actual contribution towards a sustainable transition through the allocation of capital to

[9] The best-in-class approach typically only determines the group of best performing investees within a sector. Without any further information investments would be classified as Basic or Advanced ESG. In cases when the underlying performance measurement of investees qualifies as impact measurement, best-in-class approaches can be applied by impact-aligned investments.

companies and assets with positive impacts.[10] Impact-Aligned investments, however, are not able to provide evidence that the investor or asset manager positively contributed to investees' positive impacts.

Impact-Generating investments

Impact-generating investments have an objective and a strategy of contributing to positive real-world impacts through their investment process alongside their financial risk and return objective. They use negative and either positive screening or stewardship to implement their investment objective.

Negative screening of Impact-Generating investments focuses on non-transformable activities,[11] excluding only those companies whose impacts cannot be changed positively. Beyond these non-transformable activities, Impact-Generating investments can invest in assets with negative impacts that can be improved in order to implement their objective of contributing to positive real-world impacts. If Impact-Generating investments aim to contribute by providing new capital, their positive screening focuses on investees with positive social or environmental impacts in need of new financing to grow or on investees with negative impacts who need capital to finance their transition towards improving their impacts.

Impact-Generating investments can also use stewardship (i.e. voting or engagement) as an investment approach to contribute to the improvement of investees' social or environmental impacts. In this case, they select companies or assets in particular due to their negative impacts (i.e. that are not yet sustainable) or engage with portfolio holdings found to have particular room for improvement. .[12] Importantly, engagement and voting needs to be a formalised process, with a clear policy, positive impact objectives and a monitoring system that tracks the achievement of the impact goals.

As a result, Impact-Generating investments differ from Impact-Aligned investments in that they aim to actively change investees' impacts in a more sustainable direction through investor actions (stewardship or new capital). To provide evidence for this strategy, Impact-Generating investments measure impact performance both at the investee or asset level (company impact)

[10] There is first evidence that screening of investments funds could have positive effects on reductions in carbon emissions (Rohleder et al., 2022), but the academic debate about these relationships is ongoing.
[11] For example, as defined by the EU's Platform on Sustainable Finance report on an extended environmental taxonomy (Platform on Sustainable Finance, 2022).
[12] Companies or assets selected will usually have both positive and negative impacts. Impact-Generating investments can aim to improve both negative and the positive impacts.

and the investor level (investor contribution), measuring both the expected and generated environmental and social impacts.

Consequently, Impact-Generating investments have a high ambition level; they systematically focus on creating impact as their investment objective and through the investment process. They use positive and negative screening as well as stewardship as investment approaches, going beyond the alignment of their portfolio with companies that have positive impacts. They also provide evidence of how they contribute to improving the social or environmental impacts of investees or assets.

3 Conclusion and outlook

This paper presents a methodology for market studies on sustainability-related investments developed by Eurosif's SRI Study Group (SSG) in cooperation with the University of Hamburg, the Sustainable Finance Research Group (SFRG), and Advanced Impact Research (AIR). It was developed based on an earlier White Paper by the University of Hamburg and Eurosif (Busch et al., 2022). The approach of the aforementioned paper underwent thorough testing by market practitioners.

The methodology reflects on the latest regulatory developments and provides additional terminology where necessary to provide transparency around investments' ambition levels to actively contribute to the sustainable transition. This is important since existing *de facto* categories in the SFDR (and as used in other regulations such as MiFID II) do not explicitly distinguish between investments where the investor actively contributes to the transition of the economy or not (European Commission, 2019 & 2021). The report also incorporates other market developments, including the definitions of sustainability-related investment approaches as recently defined by GSIA, the CFA Institute and UN PRI (GSIA et al., 2023), as well as extensive feedback from a practitioner review process that took place in autumn 2023.

Appendix A includes a set of questions developed to classify sustainability-related investments into one of the four categories of the methodology. An important next step is to develop a systematic data gathering approach and related infrastructure to ease use of the methodology for future market studies on the sustainable finance landscape.

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Appendix A: Questionnaire for classifying sustainability-related investment strategies

General remarks

1. All questions are asked at the fund-level, i.e. each question should be answered per fund.
2. Fund volumes will also be gathered at the fund-level (based on net asset value). The questions below need to be extended accordingly.
3. In case a family of funds uses the same sustainability-related investments approach, the questions can be answered once for the whole family of funds, without the need to answer them separately for each fund.
4. The questions below are the questions necessary to classify investments as one of the four types of investments. They can also serve as a basis to report data on different sustainability-related investment approaches as defined by the GSIA, the CFA Institute and UN PRI. Complete questionnaires will need to add questions about the organisations taking part in the survey, for example the type of organisation (asset manager or asset owner), its location, asset classes, or the net asset value of the funds for which the questions are being answered. These types of questions will need to be added when the methodology is used in market studies.

Questions

Sustainability-related investment approaches

Question 1: Which sustainability-related investment approaches do you apply? (please mark all that apply)

1. *Screening*
    1. *Negative/Exclusionary Screening*
    2. *Positive Screening*
    3. *Best-in-Class/Best-in-Universe/Best-in-Progress*
    4. *Norm-based Screening*
2. *ESG integration*
3. *Thematic Investing*
4. *Stewardship*
    1. *Engagement*
    2. *Voting*
5. *Impact-related investments*

Guideline for data analysis: Answers to these questions can be used to aggregate and report the volumes of individual sustainability-related investment approaches. As such, they serve as the data source to continue data gathering as in previous SRI market reports.

Sustainability-related selection process (e.g. Best-in-Class or other positive screening)

Question 2: What percentage of the initial investment universe is still investable after applying the sustainability-related investment approach?

1. *- greater than 80% investable*
2. *- between 61%-80% investable*
3. *- between 41%-60% investable*
4. *- between 21%-40% investable*
5. *- 20% or below investable*

Guideline for data analysis: The fulfilment of the 80 percent threshold indicates that an investment can be classified as Advanced ESG (i.e. if only 80 percent of the initial investment universe is still investable after the sustainability-related screening).

Engagement

Question 3.1: Do you have a formalised engagement policy applicable to this product?

- *Yes/No*

Question 3.2: Do you have clearly specified engagement objectives targeting significant social/environmental improvements and/or outcomes of the investees/assets for this product?

- *Yes/No*

Question 3.3: Do you have a monitoring system that tracks the impact of engagement activities and measures progress towards the achievement of the engagement objectives (e.g., achievement of milestones regarding social/environmental improvements and/or outcomes)?

- *Yes/No*

Voting

Question 4.1: Do you have a formalised voting policy applicable to this product?

- *Yes/No*

Question 4.2: Do you have clearly specified voting objectives targeting significant social/ environmental improvements and/or outcomes of the investees/assets for this product?

- *Yes/No*

Question 4.3: Do you have a monitoring system that tracks the impact of voting activities and measures progress towards the achievement of the voting objectives (e.g., achievement of milestones regarding social/environmental improvements and/or outcomes)?

- *Yes/No*

Guideline for data analysis (engagement and voting): A "Yes" to questions 3.1-3.3 or 4.1-4.3 provides an indication that an investment can be classified as Impact-Generating using stewardship approaches.

Other investor contribution mechanisms

Question 5: Which of the following investor contribution mechanisms apply to your product? (please mark all that apply)

1. *Provide new capital (debt/equity) to help investees/assets improve environmental/social performance.*
2. *Provide capacity building to investees/assets to help improve environmental/social performance.*
3. *Other, please explain.*
4. *None*

Guideline for data analysis: A positive answer to questions one or two provides an indication for the necessary condition to be classified as an Impact-Generating investment.

Question 6: Do you measure your investor contribution? (i.e. whether your actions as an investor (provision of new capital, capacity building, engagement, voting) have initiated/caused social/environmental improvements of investees/assets?

- *Yes/No*

Guideline for data analysis: A "Yes" indicates that an investment measures an investor contribution, as required for Impact-Generating investments.

Social and environmental performance measurement

Question 7: How do you measure the environmental and/or social performance of investees/assets? (please mark all that apply)

1. *Not at all*
2. *We use ESG ratings.*
3. *We measure/use investees'/assets' exposure to ESG-related risks and opportunities based on concrete social/environmental indicators (e.g., exposure to physical climate-related risks or exposure to growth opportunities via the provision of sustainable products or services).*
4. *We measure/use changes in concrete social/environmental indicators (e.g., CO_2 footprint / water consumption / Board diversity / human rights controversies).*
5. *We measure/use specific social/environmental impacts and/or outcomes.*
6. *We measure/use specific SDG contributions (e.g., revenue percentage contributing to SDGs).*

Guideline for data analysis: A positive answer to two or three indicates that an investment measures its ESG performance (required for Advanced ESG investments). A positive answer to four, five, or six indicates that an investment measures or estimates company impact (required for Impact-Aligned and -Generating investments).

Question 8: How do you compare the social/environmental performance of investees/assets? (please mark all that apply)

1. *We do not compare the social/environmental performance of assets/investees to any of these standards of comparison.*
2. *We measure/use social/environmental indicators or ratings relative to industry peers (e.g., using an index or a benchmark).*
3. *We measure/use social/environmental indicators or ratings relative to historic performance (e.g., based on GHG emissions, or ESG/SDG ratings, etc.).*
4. *We measure/use social/environmental indicators relative to absolute thresholds (e.g., Paris-alignment metrics like those provided by SBTi, or metrics based on other planetary boundaries).*
5. *Other, please explain.*

Guideline for data analysis: A positive answer to two, three or four indicates that an investment compares the measured performance to a benchmark. This distinction is required in order to distinguish Advanced ESG investments from Impact-Aligned or Impact-Generating investments.

Appendix B: Glossary of terms

Term	Definition	Source
ESG factors	Environmental, social and governance issues that are identified or assessed in responsible investment processes. - Environmental factors are issues relating to the quality and functioning of the natural environment and natural systems. - Social factors are issues relating to the rights, well-being, and interests of people and communities. - Governance factors are issues relating to the governance of companies and other investee entities.	PRI, 2022[13]
Sustainability factors	Environmental, social and employee matters, respect for human rights, anti-corruption and anti-bribery matters.	Article 2(24) SFDR, 2019[14]
Sustainability matters	Environmental, social and human rights, and governance factors, including sustainability factors defined in Article 2, point (24), of Regulation (EU) 2019/2088 of the European Parliament and of the Council38.	ESRS 2023, p. 280[15]
Opportunities (in a sust. context)	Sustainability-related opportunities with positive financial effects.	ESRS 2023, p. 273
Risks (in a sust. context)	Sustainability-related risks with negative financial effects arising from environmental, social or governance matters that may negatively affect the undertaking's financial position, financial performance, cash flows, access to finance or cost of capital in the short, medium or long term.	ESRS 2023, p. 276
Financial materiality	A sustainability matter is material from a financial perspective if it generates risks or opportunities that affect (or could reasonably be expected to affect) the undertaking's financial position, financial performance, cash flows, access to finance or cost of capital over the short, medium or long term.	ESRS 2023 p. 267
Impact materiality	A sustainability matter is material from an impact perspective when it pertains to the undertaking's material actual or potential, positive or negative impacts on people or the environment over the short-, medium- and long-term. A material sustainability matter from an impact perspective includes impacts connected with the undertaking's own operations and upstream and downstream value chain, including through its products and services, as well as through its business relationships.	ESRS 2023, p. 270

[13] https://www.unpri.org/reporting-and-assessment/reporting-framework-glossary/6937.article
[14] https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:02019R2088-20200712
[15] https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=OJ:L_202302772

Appendix C: Methodology compared to different regulatory approaches

Categories	Basic ESG	Advanced ESG	Impact-Aligned	Impact-Generating
SFDR (Article 8)[16]	✓	✓	✓	✓
SFDR (Article 9)[17]			✓	✓
FCA[18]			Sustainability Focus Sustainability Improvers	Sustainability Impact

[16] https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A02019R2088-20200712
[17] https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A02019R2088-20200712
[18] https://www.fca.org.uk/publication/policy/ps23-16.pdf